HOUSE OF LORDS

European Union Committee

19th Report of Session 2008–09

Money laundering and the financing of terrorism

Volume I: Report

Ordered to be printed 14 July 2009 and published 22 July 2009

Published by the Authority of the House of Lords

London : The Stationery Office Limited
£price

HL Paper 132–I

The European Union Committee

The European Union Committee of the House of Lords considers EU documents and other matters relating to the EU in advance of decisions being taken on them in Brussels. It does this in order to influence the Government's position in negotiations, and to hold them to account for their actions at EU level.

The Government are required to deposit EU documents in Parliament, and to produce within two weeks an Explanatory Memorandum setting out the implications for the UK. The Committee examines these documents, and 'holds under scrutiny' any about which it has concerns, entering into correspondence with the relevant Minister until satisfied. Letters must be answered within two weeks. Under the 'scrutiny reserve resolution', the Government may not agree in the EU Council of Ministers to any proposal still held under scrutiny; reasons must be given for any breach.

The Committee also conducts inquiries and makes reports. The Government are required to respond in writing to a report's recommendations within two months of publication. If the report is for debate, then there is a debate in the House of Lords, which a Minister attends and responds to.

The Committee has seven Sub-Committees which are:
Economic and Financial Affairs and International Trade (Sub-Committee A)
Internal Market (Sub-Committee B)
Foreign Affairs, Defence and Development Policy (Sub-Committee C)
Environment and Agriculture (Sub-Committee D)
Law and Institutions (Sub-Committee E)
Home Affairs (Sub-Committee F)
Social Policy and Consumer Affairs (Sub-Committee G)

Our Membership

The Members of the European Union Committee are:

Baroness Cohen of Pimlico
Lord Dykes
Lord Freeman
Lord Hannay of Chiswick
Baroness Howarth of Breckland
Lord Jopling
Lord Kerr of Kinlochard
Lord Maclennan of Rogart
Lord Mance
Lord Paul
Lord Plumb
Lord Powell of Bayswater
Lord Richard
Lord Roper (Chairman)
Lord Sewel
Baroness Symons of Vernham Dean
Lord Teverson
Lord Trimble
Lord Wade of Chorlton

The Members of the Sub-Committee which conducted this inquiry are listed in Appendix 1.

Information about the Committee

The reports and evidence of the Committee are published by and available from The Stationery Office. For information freely available on the web, our homepage is:
http://www.parliament.uk/hleu
There you will find many of our publications, along with press notices, details of membership and forthcoming meetings, and other information about the ongoing work of the Committee and its Sub-Committees, each of which has its own homepage.

General Information

General information about the House of Lords and its Committees, including guidance to witnesses, details of current inquiries and forthcoming meetings is on the internet at:
http://www.parliament.uk/about_lords/about_lords.cfm

Contacts for the European Union Committee

Contact details for individual Sub-Committees are given on the website.
General correspondence should be addressed to the Clerk of the European Union Committee, Committee Office, House of Lords, London, SW1A 0PW
The telephone number for general enquiries is 020 7219 5791. The Committee's email address is:
euclords@parliament.uk

CONTENTS

Note: References in the text of the Report are as follows:
(Q) refers to a question in oral evidence
(p) refers to a page of written evidence

The Report of the Committee is published in Volume I, HL Paper 132-I.
The Evidence of the Committee is published in Volume II, HL Paper 132-II

SUMMARY

In the United Kingdom alone the turnover of the most serious forms of organised crime is perhaps £15 billion a year, two thirds of which is laundered through banks and other bodies. Much of this constitutes the proceeds of drug trafficking. The problem is global, and so must be the response. More than 180 countries are involved as members of or by being associated with the Financial Action Task Force (FATF), which recommends the action they should take to counter money laundering and the financing of terrorism, and promotes the monitoring of their compliance with those standards.

The European Commission has been a member of the FATF from the outset, and the Community has been in the forefront of the fight. For the Member States, the FATF policy is implemented by a Directive which sets out in detail what is expected of them. The first requirement is that they should implement the Directive, and not all have yet done so. The United Kingdom has done so very effectively, but in other respects the Government have been slow. Astonishingly, they have not even signed, much less ratified, the Warsaw Convention on Money Laundering and Terrorist Financing, which would extend to all Council of Europe States arrangements through which to access financial information on money laundering and terrorist financing, and information on assets held by criminal organisations, including terrorist groups.

The Warsaw Convention, if in force, would also help with recovery of the proceeds of crime, especially through civil proceedings. This is vital for the prevention and deterrence of drug trafficking and other serious crimes. Freezing the assets of suspected terrorists is another essential weapon, but it must not be abused; those whose assets are frozen have a right to know why, to make representations, and to have them considered. The European Court has led the way to progress in the EU; the United Nations still has some way to go.

Information is the key. Whenever a transaction or other activity appears suspicious, it has to be reported. The burden falls mainly on banks, but also on other financial institutions, lawyers, accountants, insurers and others. In the United Kingdom, in the last full year the banks alone submitted 145,000 suspicious activity reports to the Serious Organised Crime Agency. The cost of doing so is considerable: one bank spent £36 million in that year to carry out this and related duties. We have considered whether the benefit is commensurate; the feedback is insufficient, and there is practically no way of knowing whether in any specific case the provision of information was fruitful. Access to the database of suspicious activity reports is too wide, and the data are retained unnecessarily long. We have made recommendations on how these matters might be improved.

Today, any study of terrorist financing has to take account of the proceeds of piracy. The Government say that they have not found a link between the two. We believe that they would find one if they looked for it, making the same effort as they have, with other States, in naval operations.

Money laundering and the financing of terrorism

CHAPTER 1: INTRODUCTION

The scale of the problem

1. Acquisition of the wealth and property of others is the ultimate objective of every serious criminal; those assets are also the lubricant of criminal activity, and so the motivation for further crime. In the case of the terrorist, finance is acquired not as an end in itself, but to achieve political ends by violent means. In either case, the tracing of the finance may be a way of identifying the criminal, recovering the proceeds, and preventing further criminal acts. The laundering of money, disguising its source and giving it an aura of respectability, thus plays an essential part in serious and organised crime; from which it follows that the combating of money laundering plays an equally important part in the fight against organised crime, and in countering the financing of terrorism.

2. The scale of this can scarcely be exaggerated. Estimates have to be treated with caution, but the International Monetary Fund estimated over ten years ago that the aggregate size of money-laundering was anywhere between 2% and 5% of the world's gross domestic product.[1] For the United Kingdom, an estimate by HM Treasury in 2007 was that the most serious forms of organised crime alone generated an illicit turnover of some £15 billion a year, leading to money laundering through the regulated sector—banks, insurers, accountants, lawyers and the like—of £10 billion a year; and also generated criminal "capital formation"—that is, assets invested in a possible seizable form—of about £5 billion, £3 billion of which was exported overseas.[2] This estimate is now 2½ years old; but organised crime is one global industry which we doubt to have suffered from the current economic downturn.

What is money laundering?

3. Money laundering is the process by which the source and ownership of criminally derived wealth and property is changed to confer on it a perception of legitimacy. From the point of view of the criminal, there seem to be three basic requirements:

   - the need to conceal the true ownership and origin of the proceeds;
   - the need to maintain control of the proceeds; and
   - the need to change the form of the proceeds.

---

1 Michel Camdessus, Managing Director of the IMF, "Money Laundering: the Importance of International Countermeasures", an address to the Plenary Meeting of the Financial Action Task Force on Money Laundering in Paris, 10 February 1998.

2 HM Treasury, The financial challenge to crime and terrorism, February 2007.

4. We set out in Box 1 a summary of the acts which constitute money laundering offences under current international standards.

BOX 1

Money laundering offences

- the conversion or transfer of property for the purpose of concealing or disguising its illicit origin or of assisting any person to evade the legal consequences of his actions
- the concealment or disguise of the true nature, source, location, disposition, movement, rights with respect to, or ownership of criminally derived property
- the acquisition, possession or use of criminally derived property.

For the purposes of United Kingdom law section 340(11) of the Proceeds of Crime Act 2002 contains a detailed and extensive definition of money laundering offences by reference to other provisions of Part 7 of the Act.

The processes and techniques

5. Money laundering involves the following stages, which may overlap:

- Placement stage: where cash derived directly from criminal activity (for example, from sales of drugs) is either placed in a financial institution or used to purchase an asset;
- Layering stage: the stage at which there is the first attempt at concealment or disguise of the source of the ownership of the funds;
- Integration stage: the stage at which the money is integrated into the legitimate economic and financial system and is assimilated with all other assets in the system.

6. Techniques of laundering, known as typologies, are numerous and vary from the basic to the highly sophisticated. The following typologies are currently those of most concern to United Kingdom law enforcement, based on intelligence and investigative experience:[3]

- cash/value couriering;
- abuse of "gatekeepers" (e.g. accountants and lawyers);
- abuse of money laundering transmission agents (including Hawala and other alternative remittance systems[4]);
- cash rich businesses and front companies;
- high value assets and property; and
- abuse of bank accounts and other over-the-counter financial sector products.

7. In its 2008/09 threat assessment of serious organised crime, the Serious Organised Crime Agency identified the following specific risk areas where the legitimate and criminal economies intersect: laundering money through

---

3 Financial Action Task Force (FATF), Third Mutual Evaluation Report of the United Kingdom, June 2007, para. 17. The typologies are not ranked in any particular order.

4 We explain the working of Hawala in Chapter 5, paragraph 147.

businesses; financial and legal professionals; money service businesses (including bureaux de change and money transmission agents); informal value transfer systems (including the Hawala system). It also highlighted the movement of illicit cash and the purchase of assets: "Serious organised criminals invest in property, shares, trusts, and pensions as well as accumulating high value goods, such as jewellery, vehicles, art and other collectable items. These assets may be held in the names of friends or family to conceal the true ownership. Investment in private and commercial property, including overseas, is especially attractive because it appreciates in value over time."[5] To that list of assets we can now add football clubs.[6]

Terrorist financing

8. The mounting of terrorist operations is notoriously inexpensive. The 9/11 plotters were estimated to have spent no more than $500,000 to plan and conduct their attack.[7] In the case of the 7/7 London bombings the initial report stated: "Current indications are that the group was self-financed. There is no evidence of external sources of income. Our best estimate is that the overall cost is less than £8,000, the overseas trips, bomb-making equipment, rent, car hire and UK travel being the main cost elements."[8]

9. But a terrorist group, like any other criminal organisation, needs to build up and maintain a financial infrastructure. For this it must develop sources of funding, a means of laundering those funds and a way to ensure that the funds can be used to obtain material and other logistical items needed to commit terrorist acts. The CIA estimates that it cost Al-Qaida[9] about $30 million a year to sustain its activities before 9/11.[10]

Our inquiry

10. The subject of our inquiry is international cooperation to counter money laundering and the financing of terrorism.[11] This too is on a global scale, involving cooperation between governments in the United Nations, the Council of Europe, other multilateral and bilateral fora, and—the direct focus of our inquiry—the EU. Our inquiry has therefore concentrated on a number of questions:

- How effective is EU and international cooperation in countering money laundering and the financing of terrorism?
- Is enough effort being invested in confiscation of the proceeds of crime, especially by civil recovery?
- What part is played by the United Kingdom Government, and what could be done to enhance it?

---

5 The United Kingdom Threat Assessment of Serious Organised Crime 2008/9, paragraphs 103–110.

6 FATF report Money laundering through the Football Sector, July 2009.

7 Final report of the National Commission on Terrorist Attacks upon the United States, chapter 5.4.

8 Report of the Official Account of the Bombings in London on 7th July 2005, HC 1087, 11 May 2006, paragraph 63.

9 This is the spelling commonly used in documents relating to money laundering; see further paragraph 50, footnote.

10 Final report of the National Commission on Terrorist Attacks upon the United States, chapter 5.4.

11 The common abbreviation for anti-money laundering is AML, and for countering the financing of terrorism is CFT.

- Is the effort and cost required of the private regulated sector proportionate and effective for compliance with EU and United Kingdom legislation on money laundering?
- Is that legislation compatible with fundamental human rights, in particular the right to property, and the right to privacy of persons and businesses?

Lastly we have looked at a number of matters which have lately assumed particular importance, including the relationship between money laundering and piracy.

Conduct of the inquiry

11. This inquiry has been conducted by Sub-Committee F (Home Affairs), a list of whose members is printed in Appendix 1. They issued a call for written evidence in December 2008; this is reproduced in Appendix 2. In reply they received evidence from 30 persons and bodies. Between March and May 2009 they received oral evidence from 28 witnesses, and a considerable volume of supplementary evidence. They visited Brussels to take evidence from the Commission, the Council Secretariat and the EU Counter-terrorism Coordinator. The volume of the evidence is such that it is printed in a separate volume. A full list of the witnesses is at Appendix 3. To all of them we are most grateful.

12. Throughout the course of this inquiry Professor Bill Gilmore, Professor of International Criminal Law at Edinburgh University, has acted as our specialist adviser. His unrivalled knowledge of the subject and wise guidance have been invaluable. We express our gratitude to him.

Structure of this report

13. We start in the next chapter with a detailed examination of the various fora of international cooperation. Chapter 3 considers confiscation of the proceeds of crime, which assumes ever greater importance, and Chapter 4 the contribution of the private regulated sector. We then consider four specific issues: Hawala and other alternative remittance systems; the effect of the global economic downturn; piracy; and data protection. Lastly in Chapter 6 we summarise our conclusions and recommendations.

14. **We recommend this report to the House for debate.**

CHAPTER 2: THE FORA FOR INTERNATIONAL COOPERATION

The international strategy

15. Money laundering and the financing of terrorism more often than not take place in an international context. The EU Council of Ministers accepts that "measures adopted solely at national or even Community level, without taking account of international coordination and cooperation, would have very limited effects".[12] Over the last twenty years the emphasis has therefore been on the development of a common international strategy. Box 2 summarises its major features.

BOX 2

International strategy

- the criminalisation of money laundering;
- adopting legislative and other measures to identify, trace, freeze, seize and confiscate the proceeds of crime;
- engaging the private sector in playing a major role in the prevention of money laundering by imposing mandatory customer due diligence and record keeping requirements;
- requiring relevant institutions, professions and other entities to cooperate with national authorities, including through the reporting of suspicious transactions (known in the United Kingdom as Suspicious Activity Reports or SARs);
- requiring institutions to establish internal controls and staff training; and
- promoting comprehensive and effective international cooperation in the investigation and prosecution of money laundering and in securing the confiscation of the proceeds and instrumentalities of criminal conduct.

16. In the 1980s money laundering was used by criminals largely for laundering the proceeds of drug trafficking. The first important international responses were the United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, adopted on 19 December 1988 in Vienna (the Vienna Convention) and, more generally in relation to all criminal activities, the Council of Europe Convention on laundering, tracing, seizure and confiscation of proceeds of crime, opened for signature on 8 November 1990. A still more important development took place in 1989 when the G7 States[13] decided to set up a Financial Action Task Force—the FATF—to combat the growing threat of money laundering.

The Financial Action Task Force (FATF)

17. Most international bodies in which a number of States participate have a formal structure and constitution contained in a treaty, convention or other

[12] Directive 2005/60/EC of the European Parliament and of the Council of 26 October 2005 on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing (the third money laundering Directive), OJ L309 of 25 November 2005, recital 5.

[13] Canada, France, Germany, Italy, Japan, United Kingdom and United States.

agreement. The FATF is not one of them.[14] It can be seen as a partnership between governments, accountable to the Ministers of its member Governments, who give it its mandate. The current mandate lasts from 2004 to 2012, but was revised in April 2008.

18. When the FATF was set up the European Commission and a number of other states[15] were invited to join the Task Force in order to enlarge its expertise and to reflect the views of other countries particularly concerned by or having experience in the fight against money laundering. The membership has since further widened, and there are now 34 members.[16] The organisation is based in Paris. It has a rotating Presidency, which the United Kingdom last held in 2007–08.

Money laundering

19. The FATF is widely recognised as the international standard setting body in the field of anti-money laundering (AML). It is best known for its Forty Recommendations. These were originally drawn up in 1990 as an initiative to combat the misuse of financial systems by persons laundering drug money. They recommend to countries how their legal systems and financial institutions could best operate to combat money laundering, what institutional measures they should take, and the international cooperation they should undertake. The Recommendations were revised for the first time in 1996, and again in 2003, to reflect evolving money laundering typologies. Together they constitute a comprehensive regime which has been endorsed and adopted by more than 180 countries, and in addition by a number of international bodies including the United Nations, the International Monetary Fund (IMF) and the World Bank; they are the international anti-money laundering standard. We publish a summary of them in Appendix 4.[17]

20. Setting standards would be of little use if there was no mechanism for seeing whether they were adhered to. The FATF assesses formal compliance with those standards, and their effective implementation, through a process of mutual evaluation. This involves for each country an assessment by experts from other countries of whether they are fully compliant with each recommendation, or if not, where they fall short.[18] A report is presented to the FATF plenary session, and two years later the country must report what it has done to remedy those areas where the report found weaknesses. To date there have been two rounds of evaluations, and a third is in progress. The United Kingdom's third evaluation took place in June 2006. The report, presented in June 2007, found the United Kingdom to be fully compliant with 19 of the 40 recommendations, and largely or partially compliant with all but 3 of the others. The Treasury describe this as the highest number of such ratings achieved at the time.[19]

---

14 We consider in paragraphs 25 et seq whether a more formal structure would be desirable.

15 Australia, Austria, Belgium, Luxembourg, the Netherlands, Spain, Sweden and Switzerland.

16 The 34 members of the FATF are: Argentina; Australia; Austria; Belgium; Brazil; Canada; China; Denmark; the European Commission; Finland; France; Germany; Greece; the Gulf Co-operation Council; Hong Kong; Iceland; Ireland; Italy; Japan; Luxembourg; Mexico; the Kingdom of the Netherlands; New Zealand; Norway; Portugal; Russia; Singapore; South Africa; Spain; Sweden; Switzerland; Turkey; the United Kingdom; and the United States.

17 This summary is based on one kindly sent to us by the British Bankers' Association.

18 The ratings are Compliant, Largely compliant, Partially compliant, and Non-compliant.

19 Note by HM Treasury on Financial Restrictions Amendments to the Counter-Terrorism Bill, 6 November 2008.

Terrorist Financing

21. Prior to the 9/11 terrorist attacks relatively little attention was paid by the international community to the financing of terrorism. A UN Convention on the topic had been concluded in 1999,[20] but by September 2001 it had been ratified by only four States (including the United Kingdom), and had not entered into force. However in October 2001 the issue of countering the financing of terrorism (CFT) was specifically added to the FATF mandate, and the FATF formulated eight Special Recommendations on the subject (and added a ninth in 2004).

BOX 3

FATF Special Recommendations on Terrorist Financing

- ratification and implementation of the 1999 United Nations Convention for the Suppression of the Financing of Terrorism and relevant UN Security Council Resolutions;
- criminalising the financing of terrorism, terrorist acts and terrorist organisations;
- freezing and confiscating terrorist assets;
- reporting suspicious transactions related to terrorism;
- providing the widest possible assistance to other countries' law enforcement and regulatory authorities for terrorist financing investigations;
- imposing anti-money laundering requirements on alternative remittance systems;
- strengthening customer identification measures in international and domestic wire transfers;
- ensuring that entities, in particular non-profit organisations, cannot be misused to finance terrorism; and
- putting in place measures to detect physical cash movements.

FATF-style regional bodies

22. The extension of the influence of the FATF, with a membership of 32 States and two international bodies, to the great majority of the world's nations, including all the developed economies, is achieved by a system of FATF-style Regional Bodies (FSRBs) which take forward the global anti-money laundering message and mutual evaluation beyond the FATF membership.[21] Fifteen Member States of the EU—the pre-2004 members—are members of the FATF, but the remainder are members of MONEYVAL, a body set up

---

[20] International Convention for the Suppression of the Financing of Terrorism, opened for signature on 10 January 2000.

[21] The full list of FSRBs is: Asia/Pacific Group on Money Laundering (APG), the Caribbean Financial Action Task Force (CFATF), the Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG), the Eurasian Group on Money Laundering (EAG), the *Grupo de Acción Financiera de Sudamérica* (GAFISUD), the Intergovernmental Task Force against Money Laundering in Africa (GIABA), the Middle Eastern and North African FATF (MENAFATF) and the Council of Europe Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism (MONEYVAL).

by the Council of Europe in September 1997 to conduct self and mutual assessments of the anti-money laundering measures in place in those Council of Europe countries which are not members of the FATF.[22]

23. In 2005 the FATF offered the status of Associate Member of the FATF to FSRBs which met particular criteria. In 2006 MONEYVAL became an Associate Member in the first set of FSRB accessions to Associate Member status. Associate Membership allows more active participation in the work of FATF and input into FATF policy making.

24. While the separation of EU Member State participation between the FATF and MONEYVAL is not ideal, we are satisfied that it has not given rise to major problems in practice to date. One reason for this is the close working relationship which has been developed between the two bodies. As Sir James Sassoon, who was President of the FATF during the United Kingdom Presidency from July 2007 to June 2008, noted, "there is a high degree of mutual respect and co-operation; they are working to absolutely the same standards in terms of their evaluations …" (Q 411) Furthermore, the European Commission facilitates, through the Committee for the Prevention of Money Laundering and Terrorist Financing, discussion among all 27 Member States in advance of each FATF plenary meeting. (Q 273)

Transparency

25. As we have said, the FATF has no formal constitution, and Professor Peter Alldridge, Head of the School of Law at Queen Mary, University of London, suggested to us that it needed one. The FATF had operated on an *ad hoc* and temporary basis for the last twenty years; if it was to be a standing body it should, in his view, be properly constituted and established by an international convention. (Q 326) But Sir James Sassoon told us that the organisation as described by Professor Alldridge did not bear much resemblance to anything that he recognised. When he first came to the FATF it struck him as "a rather extraordinary entity in its way", but he thought its interesting constitutional set-up had served it reasonably well over the last 20 years. (QQ 391, 395)

26. We agree that the constitutional set-up of the FATF is unusual—extraordinary is perhaps not too strong a word—but we feel it is none the worse for that. In particular, we believe that the fact that it is not set up by a convention between the States is greatly to its advantage. Such conventions take a long time to be agreed and even longer to ratify, as is clear from some of those we consider below. They create a rigid structure so that amendment of the mandate of the FATF, or enlargement of its membership, might have been impossible without an amending protocol.

27. Professor Alldridge told us that the decision-making and policy-making structures of the FATF were "insufficiently transparent to warrant their own uncritical acceptance". (p 150, QQ 326–327) We agree with him that these are processes which, in any powerful legislative body, would be transparent; but the FATF, though undoubtedly powerful, is not a legislative body. Its recommendations and assessments are addressed to governments. If and when they affect natural and legal persons, as they undoubtedly do, that is

[22] Russia is a member of both the FATF and MONEYVAL. Two FATF States are also nominated by the FATF President to be full members of MONEYVAL for 2 year periods without being evaluated by MONEYVAL (currently France and the Netherlands).

because those governments have implemented them in their domestic laws. That is the stage at which openness and transparency are required.

28. In any event, Sir James Sassoon thought that the work of the FATF was sufficiently transparent. On the particular issue of the criteria for membership, which Professor Aldridge thought were unclear (Q 326), Sir James's view was that they were laid out with great clarity,[23] though he conceded that since membership, like everything else, had to be dealt with on a consensus basis, an outsider might justifiably question what the future membership approach of the FATF might be. (QQ 392–393) Satisfying the criteria for membership is only a preliminary step towards becoming a member.

Accountability

29. Sir James Sassoon gave us a description of the FATF meeting at ministerial level in Washington DC in the spring of 2008 under the United Kingdom Presidency, which was attended not only by ministers from the States which are members of the FATF but also by the regional FSRBs and some 20 other organisations including the IMF, the World Bank, the relevant agency of the United Nations and other groupings of international regulators. His conclusion was that "in terms of the accountability, there is a high degree of it". (Q 391) Ian Pearson MP, the Economic Secretary to the Treasury, took the same view: "All FATF decisions are taken in plenary which is chaired by the president or in working groups which are chaired by members of country delegations". (Q 476) James Robertson, the head of the Financial Crime Team at HM Treasury, told us that one of the objectives of the United Kingdom Presidency was more ministerial oversight for the FATF. (Q 108) In our view the FATF is adequately accountable to the governments of the States which are members.

30. Whether the FATF is adequately accountable to the parliaments of those States is another matter. Mr Pearson pointed out that "FATF is accountable to ministers and therefore indirectly accountable to Parliament"(Q 476). We believe direct accountability to parliaments would be preferable. The FATF and its policies played a central part in our inquiry, and we invited Rick McDonell, the Executive Secretary, to give us oral evidence. While he sent us useful written evidence (p 243), he was unable to obtain permission to give us oral evidence. Mr Pearson explained that the role of the secretariat was to serve the president and the plenary. He did not think it would be right for the secretariat to give opinions on policy matters on behalf of the FATF. He told us that, for the same reasons, the secretariat had also declined to give evidence to a US Congressional inquiry.

31. We appreciate that the policy of the FATF is a matter for the ministers of the constituent States, but **we regret that a senior official from its secretariat was not permitted to give us oral evidence on the organisation and current activities of the FATF**. Issues such as the harmonisation of counter-measures and the involvement of FATF in measures on Somali piracy were not ones on which Sir James Sassoon could comment, and we would have benefited from evidence on these and other matters from the Executive Secretary. MONEYVAL provided us with full written evidence and its Executive Secretary, John Ringguth, was able to

[23] http://www.fatf-gafi.org/dataoecd/25/48/41112798.pdf

supplement it with very useful oral evidence. We much regret that Mr McDonell was not allowed to do likewise.

32. **Since the Government accept that they are accountable to Parliament for United Kingdom membership of the FATF, they should find a more systematic way to report to Parliament on FATF developments. Written statements after each plenary session would be a start.**

Cooperation at EU level

33. The first Community measure, the 1991 money laundering Directive,[24] was adopted at a time when drug trafficking offences were at the base of most money laundering. However the Directive acknowledges in its recitals that "any measures adopted by the Community in this field should be consistent with other action undertaken in other international fora; in this respect any Community action should take particular account of the recommendations adopted by the financial action task force on money laundering, set up in July 1989 by the Paris summit of the seven most developed countries". Thus from the outset the Community's involvement has been based on cooperation with the FATF and other international bodies.

34. The Community adopted a second money laundering Directive in 2001 making major amendments to the first Directive.[25] Both Directives were repealed and replaced in 2005 by the third money laundering Directive, which is the EU measure currently in force. The third Directive, unlike the first two, specifically deals with terrorist financing. It was adopted on 26 October 2005 under the United Kingdom Presidency. Article 45(1) required Member States to transpose it into their national laws by 15 December 2007. The United Kingdom did so by the Money Laundering Regulations 2007, which came into force on that day.[26] However some Member States have been slow to do so. In October 2008 the Commission referred Belgium, Ireland, Spain and Sweden to the European Court of Justice for their failure to do so, and in December 2008 it referred France and Poland. But, as the Commission points out, the remedial procedures have long lead times and lack teeth; pecuniary sanctions can be imposed only on a second reference to the Court for failure to comply with the first decision.[27] (p 130)

35. While the money laundering Directive has as its focus the implementation in Community law of the preventative aspects of the FATF's 40 Recommendations, other legislative initiatives have been required to give effect

---

24 Council Directive 91/308/EEC of 10 June 1991 on prevention of the use of the financial system for the purpose of money laundering, OJ L166 of 28 June 1991.

25 Directive 2001/97/EC of the European Parliament and of the Council of 4 December 2001 amending Council Directive 91/308/EEC on prevention of the use of the financial system for the purpose of money laundering, OJ L344 of 28 December 2001.

26 SI 2007 No 2157.

27 In the case of Sweden, the Commission first wrote to the Government about its failure to implement the Directive on 28 January 2008, delivered a reasoned opinion under Article 226 of the EC Treaty on 6 June 2008, and instituted proceedings before the Court on 9 December 2008 (Case C-546/08). On 11 June 2009, i.e. 18 months after Sweden should have transposed the Directive, the Court ruled that its failure to do so put it in breach of its obligations under Article 45(1) of the Directive; but the only available sanction was to order Sweden to pay the costs.

to certain of the Special Recommendations on the financing of terrorism.[28] Philippe Pellé from the Internal Market Directorate General of the Commission (DG MARKT) explained that the EU had encountered "tremendous difficulties" within the FATF as to the manner in which transposition of two of the Special Recommendations had taken place in order to ensure appropriate sensitivity to the economic integration process of the EU, but we were pleased to learn that these problems had been satisfactorily resolved. (Q 276)

36. There are other relevant EU measures. On 16 October 2001 the Member States signed a Protocol to the Convention on Mutual Assistance in Criminal Matters which they had concluded the previous year. The Protocol deals with such matters as requests for information on the identity of holders of bank accounts, requests for details of those accounts and of banking transactions, and requests for the monitoring of banking transactions. Banking secrecy is not a ground for refusing the request, and nor is the fact that it relates to a fiscal offence. The Protocol is therefore central to EU action on money laundering. It entered into force for some Member States on 5 October 2005. The United Kingdom deposited its instrument of ratification on 15 March 2006, and the Protocol entered into force for the United Kingdom on 13 June 2006. But **nearly eight years after its signature it is not yet in force for five member States,[29] so that there is still no full cross-border cooperation even on obtaining details of bank accounts. This is a situation which Professor Gilles de Kerchove, the EU Counter-terrorism Coordinator described as "shocking". (Q 268) We think this is not too strong a word.**

37. The Crown Prosecution Service (CPS) indicated that these innovative forms of mutual legal assistance relating to banking evidence are currently applicable to 25 Member States, and that this will be extended to Bulgaria, Romania and certain EFTA countries later this year. However, it also noted that "anecdotal information … suggests that cooperation in customer information and account monitoring remains relatively rare to date as between the UK and other EU Member States". (p 77) Jeremy Rawlins, the head of the Proceeds of Crime Delivery Unit of the CPS, elaborated on the reasons for this. One important factor mentioned was the lack of timeliness with which cooperation of this kind could be secured. (Q 165) **The Government should satisfy themselves that the United Kingdom is in a position to provide these forms of cooperation in a timely and effective manner, and should press other Member States to do likewise.**

EU Agreement with the United States

38. The EU and the United States concluded an Agreement on mutual legal assistance on 25 June 2003.[30] This Agreement, like the others to which we

---

28 Examples are Regulation (EC) 1889/2005 of 26 October 2005 on controls of cash entering or leaving the Community (OJ L 309 of 25 November 2005) which implements FATF Special Recommendation IX; Regulation (EC) 1781/2006 of 15 November 2006 on information on the payer accompanying transfers of funds (OJ L 345 of 8 December 2006) which addresses the substance of Special Recommendation VII on wire transfers; and Directive 2007/64/EC of 13 November 2007 on payment services in the internal market (OJ L 319 of 5 December 2007) which covers the requirements of Special Recommendation VI on alternative remittance systems.

29 Estonia, Greece, Italy, Ireland and Luxembourg. For further details on ratifications and entry into force see Supplementary memorandum (6) by the Home Office, p 191 .

30 OJ L181 of 19 July 2003, p 34. Sub-Committee E (Law and Institutions) of this Committee conducted a full inquiry into this agreement at the time of its negotiation and conclusion: *EU/US Agreements on*

refer, contains important provisions on access to bank account information and banking data. However, at the request of the United States the EU-US Agreement requires that all Member States need to exchange "written instruments" with the United States in order to acknowledge the way in which the provisions of the Agreement are to be implemented at the bilateral level (Article 3). The negotiation of 27 such bilateral instruments is plainly a time-consuming process, but some States have approached the matter with an astonishing lack of urgency.

39. The EU Counter-terrorism Coordinator told us that negotiations for the EU-US Agreement were launched "the day after 9/11", and he was highly critical of the delay in bringing it into force. (Q 268) The United Kingdom and United States signed the necessary bilateral instrument on 16 December 2004, but it remains unratified. The Home Office have told us that the United Kingdom bilateral instrument will be ratified "shortly"; all the necessary legislation needed to be updated before that could be done, but that was completed in August 2008.[31] Greece is the last Member State to have concluded a bilateral agreement, on 24 June 2009. On completion of all outstanding national constitutional procedures a Council Decision will be required to authorise the entry into force of the EU-US Agreement. The Council Secretariat have informed us that this is planned for early 2010.

40. **It is deplorable that negotiations for an agreement on mutual legal assistance, begun nearly eight years ago and concluded over six years ago, should still not have resulted in an agreement which is in force between the EU and the United States. We hope the Government will press ahead urgently with the ratification of the United Kingdom's bilateral agreement, and encourage other Member States to do likewise.**

The Council of Europe

41. The Council of Europe has for many years afforded a high priority to seeking to facilitate criminal justice cooperation among its members, which include all 27 Member States of the EU. There are two Council of Europe measures in this area which are of particular relevance to our inquiry. The first (in order of time) is the Second Additional Protocol to the 1959 European Convention on Mutual Legal Assistance in Criminal Matters. The Protocol was signed on behalf of the United Kingdom when it was opened for signature on 8 November 2001, but the United Kingdom has yet to ratify it; it is in force for some States, but not for the United Kingdom. This failure, as Lorna Harris told us, "will exclude possibilities for cooperation with Council of Europe Member States, and is a further barrier to effective and broad ranging cooperation." (p 267)

42. Stephen Webb from the Home Office said that he expected the United Kingdom to ratify the Protocol "by the autumn." He added: "We are very far from being unique; only 18 of the 47 countries have actually ratified and so France, Germany, the Netherlands and Ireland, for example, are in the same position as we are."(Q 102) It does not seem to us that a failure by other important countries to ratify the Protocol is any justification for a failure by

---

Extradition and Mutual Legal Assistance, 38th Report, Session 2002–03, HL Paper 153, http://www.publications.parliament.uk/pa/ld200203/ldselect/ldeucom/153/153.pdf

31 Supplementary memorandum (6) by the Home Office, May 2009, p 193.

this country to do so. **The Government must hasten the procedure for United Kingdom ratification of the Second Additional Protocol to the 1959 Mutual Legal Assistance Convention.**

The Warsaw Convention on Money Laundering and Terrorist Financing

43. The second Council of Europe measure is the Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime and on the Financing of Terrorism—the Warsaw Convention. It is the first comprehensive international treaty covering both the prevention and control of money laundering and the financing of terrorism. It addresses the fact that quick access to financial information, or information on assets held by criminal organisations, including terrorist groups, is the key to successful anti-money laundering systems. The Convention incorporates cooperation principles on bank account information and access to banking data.

44. The Warsaw Convention was opened for signature on 16 May 2005—over four years ago. The Government say that "The United Kingdom generally supports and welcomes the Convention."[32] One may therefore justifiably ask why the United Kingdom has yet to sign it, let alone ratify it. Lorna Harris, who between 2003 and 2005 chaired, on behalf of the United Kingdom, the working group which led to the finalisation of the Convention, points out that the Convention extends to Council of Europe States some provisions which would otherwise be available only to EU Member States. She believes that the failure by the United Kingdom to sign or ratify the Convention is a major disincentive to effective international cooperation in the area. We share this view.

45. Stephen Webb told us that the Government expected to sign the Convention "very soon" and to ratify it "within about 18 months". (Q 99)[33] He told us that there had been "quite a knotty policy issue" over Article 47, which allows the postponement of transactions at the request of a foreign financial intelligence unit. We are familiar with this question from the scrutiny by our Sub-Committee on Law and Institutions of the proposal for a Council Decision concerning the signing of the Convention on behalf of the European Community. We share the Government's doubts about Community competence in this matter.[34]

46. In the case of mixed agreements, to which both the Community and the Member States as such are party, there are advantages in coordinated signature and ratification. But since this problem related only to Community competence, and hence to signature of the Convention on behalf of the Community, it did not prevent the United Kingdom signing the Convention before the Community, as some other Member States did. In any event the problem has now been resolved, and the Convention was signed by the Community on 2 April 2009.

---

[32] Explanatory Memorandum of 17 December 2008 on the proposal for a Council Decision concerning the signing of the Convention on behalf of the European Community, signed by Alan Campbell MP, Parliamentary Under-Secretary of State at the Home office.

[33] i.e. 18 months from 11 March 2009, the date on which he gave evidence to us. A further three months would then elapse before entry into force: Article 49(4).

[34] For correspondence on this issue between the Chairman of the Select Committee and Home Office ministers, see http://www.parliament.uk/documents/upload/CwMSubEDec08-Apr09.pdf The Commons European Scrutiny Committee reported on this in their 5th Report of Session 2008–09, Paper HC 19-iv, page 93.

47. **We doubt whether there was ever any good reason for the delay in signature of the Warsaw Convention by the United Kingdom; certainly there is now no reason for any further delay. Still less do we see why a further 18 months should be needed before ratification.**

48. **The failure to sign and ratify the Warsaw Convention sends out a negative message about current United Kingdom commitment to the prevention and control of money laundering and the financing of terrorism. If the United Kingdom is to preserve, let alone enhance, its reputation in this sphere, Ministers must demonstrate the priority they attach to this by setting a clear timetable for signature and ratification.**

United Nations Cooperation

49. The United Nations Convention against Transnational Organized Crime, adopted by General Assembly Resolution 55/25 of 15 November 2000, is the main international instrument in the fight against transnational organised crime. It was opened for signature in Palermo on 12 December 2000 and entered into force on 29 September 2003. It has now been ratified by the great majority of UN Members, and requires them to criminalise the laundering of the proceeds of crime, to institute measures to counteract money laundering, and to adopt measures for the confiscation of the proceeds of crime. The International Convention for the Suppression of the Financing of Terrorism was also negotiated under UN auspices.

50. The UN also is responsible for what is perhaps the most effective means of freezing the assets of terrorists. Resolution 1267 (1999) set up a Sanctions Committee of the Security Council to freeze funds owned by or used for the benefit of the Taliban, and the EU Council adopted a common position on the implementation of such sanctions.[35] Security Council Resolution 1333 (2000) strengthened the sanctions of the earlier Resolution, providing that States are to freeze funds and other financial assets of Usama bin Laden and individuals and entities associated with him as designated by the Sanctions Committee, including those of Al-Qaida. The Security Council instructed the Sanctions Committee to maintain a list of the individuals and entities designated as associated with Usama bin Laden, including Al-Qaida.[36] The EU Council adopted a Regulation to implement decisions of the Sanctions Committee.[37]

Sanctions and human rights: the UN and EU dimensions

51. The listing of a person or body by the Sanctions Committee is done at the request of a UN Member State which has evidence that the person or body is associated with Usama bin Laden, Al-Qaida or the Taliban. At that stage the only remedy of that person or body is to submit a petition for de-listing. The question whether this procedure is consistent with human rights was

---

[35] Common Position 1999/727/CFSP of 15 November 1999 concerning restrictive measures against the Taliban (OJ L294 of 16 November 1999).

[36] A variety of spellings of these names are common. The ones we adopt—Al-Qaida, Taliban, Usama bin Laden—are those used by the UN Sanctions Committee, and hence in EC legislation relating to those sanctions and in United Kingdom statutory instruments implementing those sanctions.

[37] Council Regulation (EC) No 467/2001 of 6 March 2001 prohibiting the export of certain goods and services to Afghanistan, strengthening the flight ban and extending the freeze of funds and other financial resources in respect of the Taliban of Afghanistan, and repealing Regulation No 337/2000 (OJ L 67 of 9 March 2001). This Regulation was subsequently repealed and replaced: see paragraph 51, footnote.

considered by the European Court of Justice in the case of *Kadi.*[38] The Court set aside the judgments of the Court of First Instance and decided that it had jurisdiction to review Community measures giving effect to resolutions of the Security Council. It ruled that the Regulation imposing sanctions on Kadi and the Al Barakaat International Foundation[39] infringed their fundamental rights under Community law. It did so primarily on the basis that in order to observe the rights of the defence, in particular the right to be heard and the right to judicial review, the grounds on which the decision to freeze funds and other economic resources had been taken had to be communicated to the individual or entity concerned. Thereafter this information was supplied to Kadi and to the Al Barakaat Foundation and they were given an opportunity to comment, which they both did. The Commission, after considering their comments, concluded that the freezing action was justified, and both were relisted.[40] Since that time the Commission has come forward with a proposal for a revised procedure to deal with this and other enhancements to the process.[41]

52. In evidence to us it was stressed that the United Kingdom had supported and helped to achieve due process improvements to the UN sanctions regime in the Security Council. Resolution 1822, adopted in June 2008, provides that the cases of all individuals and entities on the UN list should be reviewed by June 2010, and narrative summaries of the reasons for listing provided to the persons named. This was characterised by both the Treasury and the FCO as "an important step forward".[42] Whilst these improvements are welcome, the process in New York remains problematic. As Lord Justice Wilson was to note in the Court of Appeal in October 2008: "The [Sanctions] Committee's procedures for determining a request that a person be de-listed are almost as opaque; and, notwithstanding the Council's recent attempts, by resolutions No 1730 (2006) and, since the hearing before us, No 1822 (2008), to improve such procedures … there is no evidence which establishes that, at UN level, the listed person's fundamental rights to fair consideration of his request for de-listing are observed."[43]

53. The Community position post-*Kadi* is an improvement. We believe however that more needs to be done at the UN, and that Resolution 1822 does not go

---

38 Joined Cases C-402/05 P and C-415/05 P, Yassin Abdullah Kadi and Al Barakaat International Foundation v Council and Commission, 3 September 2008. This judgment was followed by the Court of First Instance in Omar Mohammed Othman v Council and Commission, Case T-318/01, 11 June 2009. Omar Mohammed Othman is also known as Abu Qatada.

39 Council Regulation (EC) No 881/2002 of 27 May 2002 imposing certain specific restrictive measures directed against certain persons and entities associated with Usama bin Laden, the Al-Qaeda network and the Taliban, and repealing Council Regulation (EC) No 467/2001 (OJ L139 of 29 May 2002).

40 Commission Regulation (EC) No 1190/2008 of 28 November 2008 (OJ L322 of 2 December 2008).

41 Proposal for a Council Regulation amending Regulation (EC) No 881/2002 imposing certain specific restrictive measures directed against certain persons and entities associated with Usama bin Laden, the Al-Qaida network and the Taliban of 23 April 2009, COM (2009)187 final, document 9042/09. The proposal would allow the Commission to decide immediately on provisional measures, but to reach a final decision only after communicating to the persons involved the grounds on which the decision was reached, and giving those persons an opportunity to comment.

42 Memorandum by HM Treasury, Annex A, p 44. FCO Explanatory memorandum submitted on 3 June 2009 on the Proposal for a Council Regulation amending Regulation (EC) No 881/2002 imposing certain specific restrictive measures directed against certain persons and entities associated with Usama bin Laden, the Al-Qaida network and the Taliban of 23 April 2009 (document 9042/09), paragraph 18.

43 Per Lord Justice Wilson in *G v HM Treasury* [2008] EWCA 1187, para 152. Leave to appeal to the House of Lords was given on 3 March 2009.

far enough. There is no suggestion that a person on the UN list, once provided with the reasons for his being on that list, will find it any easier to get fair consideration of a request for de-listing, nor that a person will be provided with such reasons before being placed on a UN list.

54. **We believe these cases demonstrate the need for human rights enhancements at UN Security Council level when the Sanctions Committee is considering whether to impose sanctions on persons or bodies or is responding to requests for de-listing. The Government should press for United Nations practice to evolve in a manner consistent with the jurisprudence of the European Court of Justice.**

Financial Intelligence Units and FIU.NET

55. Recommendation 26 of the FATF Forty Recommendations reads: "Countries should establish a FIU [Financial Intelligence Unit] that serves as a national centre for the receiving (and, as permitted, requesting), analysis and dissemination of STR [Suspicious Transaction Reports] and other information regarding potential money laundering or terrorist financing." In the United Kingdom the designated FIU is the Serious Organised Crime Agency (SOCA). Their figures show that SOCA is cooperating proactively, and making spontaneous disclosures to other FIUs.[44]

56. International cooperation between FIUs is plainly of crucial importance. The Egmont Group is the coordinating body for the international group of FIUs, formed in 1995 to promote and enhance international cooperation in AML and more recently in CFT. The FIUs of nine new States joined the Group at the Plenary Session in Doha in May 2009, bringing the total to 116. All EU FIUs are members of the Egmont Group, though not all use the Egmont Secure Web for the encrypted exchange of information over the internet. In 2000 a Council Decision was adopted to enhance further the cooperation between the FIUs of Member States (the FIU Decision).[45] In 2006 the Commission set up the EU FIU Platform, an informal body to discuss the implementation aspects of the Third Directive of direct relevance to FIUs.

57. FIUs across the world are structured and formatted in different ways. David Thomas, the Director of UKFIU at SOCA, explained that FIUs are "split between what is described as administrative, which may be based within a central bank, for example, or within law enforcement, or within a prosecutor's office, a judicial FIU, or be a hybrid of all of those things. Within the EU it is reasonably well split between administrative and law enforcement based. I think there are 11 administrative, 11 law enforcement, one judicial and two hybrids". (Q 195)

58. On 21 December 2007 the Commission produced a report[46] on the working of the FIU Decision which concluded that, although Member States largely complied with the legal requirements of the Decision, there was scope for operational improvement. A particular criticism was of the implementation of Article 4(2) of the Decision, where the Commission said that "many administrative FIUs cannot exchange police information or can provide such

---

44 The Suspicious Activity Reports Regime Annual Report for 2008.

45 Council Decision 2000/642/JHA of 17 October 2000 concerning arrangements for cooperation between financial intelligence units of the Member States in respect of exchanging information (OJ L271 of 24 October 2000).

46 Document 5153/08, COM(2007)827 final.

information only after a long delay. Some law enforcement FIUs might not be able to provide certain crucial information from their databases to administrative entities. Many difficulties arise because there is no common understanding of what information is accessible to FIUs and what 'relevant information' is to be exchanged. This lack of clarity can lead to miscommunication and misunderstandings."

59. Mr Thomas thought that the system for obtaining information was effective for the UK, inasmuch as information which could not be obtained by one means could be obtained by another. In his view the FIU Decision did not need changing: "For the UK it works, as much as it can". (QQ 194–196) Our impression is that, even if the system works operationally for the United Kingdom, the same cannot be said of all other Member States. **We agree with the Commission that it is essential to strengthen operational cooperation among EU FIUs, and to eliminate the problems which administrative FIUs have with the exchange of information. We urge the Government to work towards this end.**

FIU.NET

60. Jakub Boratynski from DG JLS told us that the Commission anticipates recasting the FIU Decision only "in the longer term". (Q 297) At present it is working on "a two-pronged approach which foresees firstly in the short term operational guidelines which would aim at a better and more coherent implementation of the existing Council Decision". One way of doing this, suggested by the Commission in its report, was through "a well-defined FIU.NET project providing for operationally efficient cooperation".

61. The existing FIU.NET is a system for the automated transmission of financial intelligence information between FIUs. It was born from an initiative of the Dutch Ministry of Justice in 1998, and after the adoption of the FIU Decision in 2000 a network was built connecting the FIUs of France, Italy, Luxembourg, the Netherlands and the United Kingdom. It became operational in 2002.[47] The Commission has provided financial assistance, and it is anticipated that the FIUs of 22 Member States will be connected to FIU.NET by the end of 2009. (Q 301) But the Counter-terrorism Coordinator has explained the problems with getting all the Member States connected; Estonia has from the start shown no interest, and Latvia and Lithuania have had to be disconnected "due to financial reasons".[48]

62. The question remains whether, even if and when all 27 FIUs are connected to it, FIU.NET will achieve the Commission's ambition of "providing for operationally efficient cooperation". The United Kingdom supports it, and is on its bureau, but David Thomas described it as "still a rudimentary tool … It does not meet the UK's requirements. It is not sufficiently sophisticated to match the operations and intelligence operations that we run." But, he added, "we are committed to making it work." (Q 201)

63. The Commission told us that there was an expectation that the practical possibilities for operational co-operation in FIUs would be extended and that

---

47 Fuller information on the background, structure and plans of FIU.NET can be found in their Memorandum at p 254.

48 Implementation report of the revised Strategy on Terrorist Financing, Document 8864/09, 21 April 2009.

FIU.NET would become "more attractive as a platform of choice for FIUs exchanging information." The Commission was granting new funding, and was expecting to focus increasingly on co-operation between FIU.NET and third countries. This was related to the goal of ensuring compatibility with the international Egmont Secure Web system. "For us it is obviously a priority project." (Q 301)

64. We agree that FIU.NET should be a priority project, but we are far from convinced that this is yet the case. First, **since all Member States are bound by the FIU Decision to have FIUs exchanging information in a secure manner, all should participate in FIU.NET.**

65. Secondly, **if the United Kingdom is indeed "committed to making it work", the Government must take active steps to give it the necessary "sophistication".**

66. And lastly, **if FIU.NET is to continue to be financed from the EU budget, the Commission needs to manage it more proactively and to ensure that it provides value for money to the Member States which participate in it.**

CHAPTER 3: CONFISCATION OF THE PROCEEDS OF CRIME

67. We began by saying that acquisition of the wealth and property of others is the ultimate objective of every serious criminal. For that reason, locating, identifying and confiscating the proceeds is one of the best ways of combating serious crime.

68. All prosecutions for money laundering by the Serious Fraud Office (SFO), and a significant proportion of those by the CPS and the Revenue and Customs Prosecution Office (RCPO), involve assets that are located abroad. These assets are often in the form of real property or bank accounts. There are no available statistics to show the exact proportions, but a study of CPS confiscation orders made in the first quarter of 2008 in respect of all crimes estimated that 36% by value included foreign or hidden assets. The Asset Forfeiture Division of the RCPO estimated in September 2008 that 86% of the value of unenforced confiscation orders was in respect of assets held overseas or hidden overseas.[49]

69. We put to the CPS questions designed to elicit, among other things, the number of cases in which they (and, in Scotland, the Crown Office and Procurator Fiscal Service) had made requests for enforcement by foreign States of United Kingdom confiscation orders; the number of cases in which English and Scottish courts had given effect to foreign confiscation orders; the value of the assets involved; and similarly for the freezing of assets. The reply is printed at pp 100–106. In a number of cases the information is not available; but the figures we have been given show that the value of the assets frozen or seized is very small compared to the Treasury estimate that serious crime involves every year perhaps £5 billion of assets in a possible seizable form.[50]

70. FATF Recommendation 38 requires countries to take "expeditious action in response to requests by foreign countries to identify, freeze, seize and confiscate property laundered, proceeds from money laundering or predicate offences,[51] instrumentalities used in or intended for use in the commission of these offences, or property of corresponding value." John Ringguth, the Executive Secretary of MONEYVAL, told us: "On the confiscation agenda it is submitted that still more needs to be done by many countries: in the proactive investigation of the financial aspects of major proceeds-generating cases … in the detection of assets / proceeds hidden by criminals in countries other than the one where the predicate offence was committed … in achieving restraint and other provisional measures in respect of proceeds held in countries other than the one where the predicate offence was committed …. in the negotiation and implementation of asset sharing agreements …"[52]

71. Some of our witnesses thought there was a gap between estimates of formal compliance with this recommendation, and what happened in practice. For the Treasury, James Robertson told us that the United Kingdom was leading a project on confiscation within the FATF, and was "trying to put a much

---

49 Written evidence from the Crown Prosecution Service, p 76. Oral evidence QQ 122, 131, 132.

50 HM Treasury, The financial challenge to crime and terrorism, February 2007.

51 Predicate offences are those through which a person can receive criminal property, in order then to launder it. See further paragraphs 101 et seq.

52 Supplementary evidence, p 216.

stronger focus on the effectiveness of the regimes that are in place rather than the strict, simple compliance with the standards". (Q 109) Mr Ringguth took the same view: "… the practice in FATF and the FSRBs is that if the essential criteria for the Recommendation are formally observed in all their particulars, but the evaluators are not satisfied that the country has demonstrated effective implementation, this leads to one downgrading [from Compliant to Largely Compliant] … MONEYVAL will press for a reconsideration of the effectiveness issues under Recommendation 38 and a re-think about the way we evaluate Recommendation 38 and other international cooperation recommendations."[53]

72. An evaluation of the FATF Recommendations is in progress, and Sir James Sassoon hoped that they would be looked at carefully one by one. (Q 408) **The review of the FATF Recommendations is a good opportunity to re-examine, not just the text of Recommendation 38, but the manner in which it is implemented, and the way in which compliance is measured.**

73. Within the EU there has been a focus, since the Tampere European Council in October 1999, on progressively placing cooperation between Member States in this area on a mutual recognition footing. Several Framework Decisions have been adopted, most recently on the application of the principle of mutual recognition to confiscation orders.[54] We were disappointed to learn that the Commission has identified significant problems with the drafting of some of these instruments, and with the manner and pace of the transposition process in others, and as a consequence has suggested that consideration be given to a recasting of the EU legal framework.[55] A somewhat negative assessment was also provided by Dr Valsamis Mitsilegas of Queen Mary, University of London. (Q 373) Equally disturbing is the conclusion in a recent Commission study that "at present the overall number of confiscation cases in the EU is relatively limited and the amounts recovered from organised crime are modest, especially if compared to the estimated revenues of organised criminal groups".[56]

74. **We commend the Commission for its efforts to increase cooperation among Member States over confiscation of the proceeds of crime. We urge the Government to take a lead in driving this agenda forward with renewed vigour.**

Asset sharing agreements

75. Where a country enforces a confiscation order made by the courts of another country, the normal default position is that assets remain in the country that enforces the order, not in the one that initiated the request. An asset sharing agreement enables part of the proceeds to be returned to the initiating country, forming an added incentive for cooperation in enforcing confiscation orders. There is no legal precondition in the United Kingdom

---

53 Ibid.

54 Council Framework Decision 2006/783/JHA of 6 October 2006 on the application of the principle of mutual recognition to confiscation orders (OJ L 328 of 24 November 2006).

55 Memorandum by the European Commission, p 129.

56 Commission Communication *Proceeds of Organised Crime: Ensuring that 'crime does not pay'*, November 2008 (Document 16123/08; COM(2008)766 final).

for a formal asset sharing agreement to be in place with a third country before this can happen, thus permitting *ad hoc* arrangements to be entered into on an opportunistic basis. However, we received no evidence to suggest that this option is resorted to in practice.

76. The major exception in international practice to the default position, mandated by the UN Corruption Convention,[57] relates to the proceeds of certain forms of corruption such as the embezzlement of state funds. As the 2007 FATF mutual evaluation of the United Kingdom notes:[58] "Where funds recovered represent the proceeds of grand larceny or corruption by a kleptocrat and an entire state is the victim, it is UK policy to repay 100% of recovered funds, minus costs".

77. At present there are very few asset sharing agreements. We were told by Stephen Webb of the Home Office that the United Kingdom has between six and eight such agreements "with countries such as the US, Canada, Jamaica, the Channel Islands and a few other countries of that description. We have been having discussion with some of our bigger European partners as well." (Q 458) Mr Webb also told us of the importance attached to asset-sharing agreements; he thought there might be an opportunity of "driving forward on bilateral agreements, piggy-backing where possible with partners like the US".(QQ 143, 146) Be that as it may, the present position represents a very modest level of achievement given that the default position on confiscated assets was first established in the 1988 Vienna Convention, and that the FATF has been encouraging asset sharing agreements since 1990.

78. **The Government should give higher priority to the negotiation of bilateral asset sharing agreements with non-EU countries not already involved.**

79. The reason we place emphasis on the conclusion of agreements with non-EU Member States is that within the EU the issue of asset sharing is addressed in Article 16 of the Framework Decision on the mutual recognition of confiscation orders referred to in paragraph 73. The basic position it establishes is that if the amount of money confiscated is below €10,000 it accrues to the Member State where the order is executed; if above that sum 50% of it is transferred by the executing State to the State which issued the order.

80. This Framework Decision was due to be transposed into national law by all Member States by 24 November 2008. A number of Member States have yet to do so; regrettably, the United Kingdom is among them. We are told that the Government are looking for a suitable legislative vehicle. This is an inadequate explanation more that 2½ years after its adoption. **The Government must take immediate steps to remedy this. Given the importance of the Framework Decision, the Commission must adopt a robust stance in monitoring its effective implementation by all Member States, and react swiftly should delays or problems arise.**

Civil recovery

81. Recommendation 3 of the FATF Recommendations reads in part: "Countries may consider adopting measures that allow [proceeds of crime]

---

[57] United Nations Convention against Corruption, opened for signature at Merida (Mexico), 9 December 2003.

[58] Paragraph 1293.

to be confiscated without requiring a criminal conviction, or which require an offender to demonstrate the lawful origin of the property alleged to be liable to confiscation, to the extent that such a requirement is consistent with the principles of their domestic law."

82. This hesitant language demonstrates at once the importance of civil recovery and some of the obstacles to it. In many countries civil recovery is not consistent with domestic law; in some it is unconstitutional, since it involves an adjustment to the burden of proof. A confiscation order made in criminal proceedings of course follows a conviction made on proof beyond reasonable doubt. Civil recovery may arise when there is only a suspicion that assets are the proceeds of serious crime, based on their being disproportionate to the declared income of their owner. The suspicion may be reinforced by other facts, such as contacts between the owner and known criminals. A case may be brought before a civil court based on an assumption, on the balance of probabilities, that the assets may be proceeds of crime. In some countries the burden of proof may then be reversed, and it is for the owner of the assets to prove that their origin is legitimate.

83. Civil forfeiture has for long been available in the United States and an analogous system was introduced in Ireland in the 1990s. It was first introduced in the United Kingdom by Part 5 of the Proceeds of Crime Act 2002 (POCA). This scheme permits the recovery by way of civil proceedings of property that is or represents the proceeds of unlawful conduct, whether or not criminal proceedings have been brought. Alan Campbell MP, Parliamentary Under Secretary of State at the Home Office, informed us that "it has been tested and has passed the test of it being ECHR compliant". (Q 442)

84. We referred in paragraph 73 to the Commission Communication entitled *Proceeds of Organised Crime: Ensuring that 'crime does not pay'*. Its main conclusion is: "To fight crime effectively means to hit criminals where it hurts them most. The confiscation and recovery of the proceeds of crime targets their resources and is an essential part of the wider EU financial crime strategy." Civil recovery is one route the Commission tentatively suggest exploring, though they acknowledge that "a balanced approach is necessary and appropriate safeguards need to be provided for", given that fundamental rights are involved, such as the right to property and the right to an adequate means of recourse. At present most relevant EU legislation, as with the Framework Decision on the mutual recognition of confiscation orders, anticipates that the cooperation envisaged will arise within the framework of criminal proceedings.

85. For the Home Office, Stephen Webb thought that the Commission working paper had a number of recommendations about civil recovery that were very important to the United Kingdom. He told us that "One of the big priorities is to improve the mutual recognition in civil recovery and we are putting a lot of effort into it … a lot of other countries are still trying to get their heads around this as a concept and how they would cooperate with it in practice." (Q 143) We welcome this positive approach.

86. Similar difficulties are present at the wider international level. As the CPS explained, "the criminal conventions and treaties deal only with criminal confiscation and the Hague Convention is only concerned with private commercial civil actions. The difficulties manifest themselves at each stage of the civil recovery process …". (p 78)

87. Article 23(5) of the Warsaw Convention[59] is a very significant provision on civil recovery.

BOX 4

Warsaw Convention, Article 23(5)

> The Parties shall co-operate to the widest extent possible under their domestic law with those Parties which request the execution of measures equivalent to confiscation leading to the deprivation of property, which are not criminal sanctions, in so far as such measures are ordered by a judicial authority of the requesting Party in relation to a criminal offence, provided that it has been established that the property constitutes proceeds or other property in the meaning of Article 5 of this Convention.

88. This is a mandatory provision to which no reservation is allowed. It is a broad provision, given the wide definition of "property" in Article 5 of the Convention; and cooperation has to be provided "to the widest extent possible". Mr Ringguth pointed out that if more countries actually ratified the Warsaw Convention the possibilities for the United Kingdom to enforce civil confiscation orders would be considerably increased. He thought this was "also relevant to a number of MONEYVAL States as well because, although a lot of our countries are of Roman law origin, one of the interesting features over ten years of MONEYVAL evaluations is actually seeing how there has been some convergence towards some of what are more popularly known as common law notions." He gave Bulgaria and Georgia as examples. (Q 492)

89. We have already given a number of reasons why the Warsaw Convention should be ratified.[60] **This mandatory provision on civil recovery is yet another reason, if one were needed, why the United Kingdom should ratify the Warsaw Convention without delay.**

90. In Mr Ringguth's view there was for practical purposes no global impetus to enforce civil confiscation under the FATF standards. This was an issue that MONEYVAL would push in the review of the FATF Recommendations on international cooperation. He added: "So far as our own organisation is concerned, I have discussed this issue with the President of the Committee in the light of your questions and we have decided that we will actually open up a much larger discussion within the MONEYVAL membership on the whole issue of enforcement of civil orders outside of the general discussions that we have on mutual evaluation reports." (Q 493) We are glad to see that our inquiry has already triggered this initiative.

91. We agree with Mr Ringguth that international cooperation on confiscation of the proceeds of crime is an issue of growing importance, and one where most progress could be made if Governments showed the necessary determination. **The Government should give the highest priority to international cooperation on the confiscation of the proceeds of crime, whether by post-conviction criminal confiscation or by civil recovery.**

92. **We welcome the suggestion of the Executive Secretary of MONEYVAL that the Council of Europe may press the merits of civil**

---

59 We discuss the Warsaw Convention in paragraphs 43 to 48.

60 Ibid.

recovery in the review of the FATF Recommendations. We trust that the Government will support such a move.

93. **Cooperation in relation to civil recovery must be given much greater prominence in the current FATF review of its standards and the associated methodology for assessment of its members, so that failure to provide this would have a significant negative impact on compliance ratings for the countries concerned.**

94. Given the lack of support for civil recovery in existing multilateral arrangements, we were disappointed to learn that the United Kingdom has not yet concluded a single bilateral agreement in this sphere (Q 443), though discussions with the United Arab Emirates and the Cayman Islands "are almost finished." (Q 453) Mike Kennedy, Chief Operating Officer of the CPS, pointed out some of the real opportunities in this area. (Q 145) Mr Campbell assured us that this was a priority for the Government and that sufficient resources were in place to give effect to it. (Q 442)

95. **The Government must devise an overall strategy for the conclusion of bilateral agreements with third countries, including asset sharing provisions, and press for their early negotiation and for their timely and effective entry into force.**

CHAPTER 4: THE PRIVATE REGULATED SECTOR

Introduction

96. The fight against money laundering and terrorist financing depends on close cooperation with the authorities by those who may, however unwittingly, handle on behalf of criminals large sums of money or other valuable property. They include, among many others, banks and other financial and credit institutions; lawyers, auditors, insurers and estate agents; dealers in precious metals and precious stones; and casinos. These constitute the private regulated sector. We took oral evidence from the Law Society, the Institute of Chartered Accountants in England and Wales (ICAEW), the British Bankers' Association (BBA),[61] and Lloyd's.[62]

Customer due diligence (CDD)

97. FATF Recommendations 5 to 12 deal with customer due diligence (CDD): the measures which institutions in the regulated sector are required under normal circumstances to take in respect of their customers and their transactions. Chapter II of the Third Directive sets out what is required from such institutions when establishing a business relationship; when carrying out large occasional transactions as one transaction or part of a series; where there are suspicions of money laundering or terrorist financing; or where there are doubts about data previously obtained.

BOX 5

Customer due diligence measures: a summary

- identifying the customer and verifying his identity on the basis of reliable independent data;
- identifying the beneficial owner and verifying his identity, and being satisfied of the ownership and control structure of the customer;
- obtaining information on the purpose and intended nature of the business relationship;
- ongoing monitoring of the business relationship including scrutiny of transactions to ensure that they are conducted in a manner consistent with the institution's knowledge of the customer, the business and risk profile including, where necessary, the source of funds.

98. In 2003 the FATF introduced a significant risk-based approach into its Recommendations for the first time: "The principle is that resources should be directed in accordance with priorities so that the greatest risks received the highest attention".[63] CDD is one of the areas where this approach is manifest. Examples of higher risk situations, requiring enhanced CDD, include dealings with politically exposed persons[64] and correspondent

61 Evidence session on 4 March 2009, QQ 1–53.

62 Evidence session on 13 May 2009, QQ 506–541.

63 "Guidance on the Risk-Based Approach to Combating Money Laundering and Terrorist Financing: High Level Principles and Procedures", FATF, June 2007, p.2.

64 The Glossary to the FATF Forty Recommendations contains the following definition: " 'Politically Exposed Persons' (PEPs) are individuals who are or have been entrusted with prominent public functions

banking relationships. In lower risk situations, such as dealing with listed public companies, financial institutions may reduce or simplify (but not completely avoid) CDD measures.

99. This risk-based approach, with its promise of facilitating the more efficient allocation of resources, has been incorporated into the Third Directive. In the CDD context this approach has been elaborated in considerable detail by a Commission Directive.[65] The approach is supported by the United Kingdom Government[66] and has been broadly welcomed by the regulated private sector. Some, such as ICAEW, suggested its further extension. (Q 37)

Suspicious Activity Reports (SARs)

100. FATF Recommendations 13 to 16, and Chapter III of the Third Directive, impose on the regulated sector the duty to report to the FIU—in the case of the United Kingdom, to SOCA—any transaction or activity which seems to involve funds which are the proceeds of criminal activity, and related aspects of the reporting regime. As Ms Sally Scutt, the Deputy Chief Executive of the BBA, told us, "it is a suspicion based regime … the law requires that if you suspect, you must report". She agreed with the statement: "You smell a rat and you report it". (QQ 40–43) And the figures show that the BBA smell a great many rats: in 2007–08 their members submitted no fewer than 145,000 SARs to SOCA, and 838 SARs specifically on terrorist financing. (p 1)[67]

The "all crimes" approach

101. The breadth of the obligation depends on the criminal activities involved. What is described as the predicate offence[68] is the underlying criminal offence that gave rise to criminal proceeds which are the subject of a money laundering charge. Plainly a requirement to report a transaction which may involve even a relatively minor predicate offence will be more onerous than one limited to serious criminal offences. The approach to adopt is left to individual States.

BOX 6

FATF Recommendation 1 (extract)

Predicate offences may be described by reference to all offences, or to a threshold linked either to a category of serious offences or to the penalty of imprisonment applicable to the predicate offence (threshold approach), or to a list of predicate offences, or a combination of these approaches.

in a foreign country, for example Heads of State or of government, senior politicians, senior government, judicial or military officials, senior executives of state owned corporations, important political party officials. Business relationships with family members or close associates of PEPs involve reputational risks similar to those with PEPs themselves. The definition is not intended to cover middle ranking or more junior individuals in the foregoing categories." FATF Recommendation 6 sets out some of the enhanced CDD measures appropriate where the customer is a PEP.

65 Commission Directive 2006/70/EC of 1 August 2006 laying down implementing measures for Directive 2005/60/EC of the European Parliament and of the Council as regards the definition of politically exposed person and the technical criteria for simplified customer due diligence procedures and for exemption on grounds of a financial activity conducted on an occasional or very limited basis (OJ L214 of 1 August 2006).

66 Memorandum by HM Treasury, paragraph 16, p 42.

67 The corresponding figures for the Law Society were 6,460 (Q 7), .for the ICAEW 7,300 (Q 7), and for Lloyd's 70 (Q 508).

68 A term of US origin now widely used in the FATF and elsewhere.

102. The approach adopted by the United Kingdom is the "all crimes" approach. No matter how trivial the criminal activity, if there is a suspicion that it might involve property which might be laundered, there is an obligation to report it. From the standpoint of the authorities, the advantages are plain. If every criminal offence is potentially a predicate offence, laundering of the proceeds of any such offence constitutes the criminal offence of money laundering. The prosecutor thus has a choice of prosecuting for the predicate offence, or for the money laundering offence to which it gives rise, or both. And, as John Ringguth pointed out, it facilitates prosecution if all that needs to be shown is that the money laundering defendant knew that the proceeds came from some crime, without necessarily knowing which. (Q 490)

103. We put to our witnesses from the regulated sector the question whether the "all crimes" approach was right for them. For the BBA, Ms Scutt believed it was. She thought it important to remember that the reputation of the United Kingdom and the City as an international centre rested upon doing what is necessary. The fact that other European countries did not do so should not influence this. Ms Felicity Banks of the ICAEW entirely agreed. (Q 45)

104. The Law Society's view was different. The Chief Executive, Desmond Hudson, agreed on the importance of reputation for a well regulated market, but was not certain that this was enhanced by the current system. He pointed out that the all-embracing definition of property, and hence of criminal property,[69] resulted in the inclusion of criminal property deriving from a wide number of regulatory offences which could not have been intended to be within the focus of the Government's AML/CFT strategy. Examples were a failure to register as a processor of personal data with the Information Commissioner; failure to obtain a waste disposal licence; or failure to obtain a fire and asbestos report for the sale of commercial premises. There was also a need continually to report old offences.[70]

105. It can be argued that in practice prosecutions would never be brought for a failure to report such matters; but we agree with the Law Society that this is not an adequate answer. If the regulated sector is to be certain that prosecutions will not follow in such cases, this must be because the law does not require them to be reported. It is not enough to say that a law which requires them to be reported can be broken with impunity because a solicitor can be certain—or so he hopes—that a prosecution will not follow.

106. If the "all crimes" approach is to be modified, the most radical of the two alternatives postulated by the FATF is to have a list of serious crimes which would constitute the predicate offences. In the Glossary to their 40 Recommendations the FATF set out a long list of designated categories of offences which should be included as a minimum. There are examples of similar lists in EU legislation, as for example the list of offences for which the European Arrest Warrant disapplies the normal requirement of double criminality.[71] The Third Directive itself has a definition of "serious crimes" which relates to definitions in other instruments, but has in Article 3(5)(f) a wrap-up provision reading: "all offences which are punishable by deprivation of liberty or a detention order for a maximum of more than one year or, as

---

69 Proceeds of Crime Act 2002, section 340.

70 Q 45, and Supplementary memorandum by the Law Society, March 2009, paragraphs 2.5 to 2.10, pp 35–36.

71 Council Framework Decision 2002/584/JHA of 13 June 2002 on the European arrest warrant and the surrender procedures between Member States, Article 2 (OJ L190 of 18 July 2002).

regards those States which have a minimum threshold for offences in their legal system, all offences punishable by deprivation of liberty or a detention order for a minimum of more than six months".

107. Our witnesses differed as to the best course to follow. Professor Alldridge favoured "a more thought-out list" of crimes. (Q 346) Jonathan Leslie, a partner in the solicitors firm Travers Smith, suggested qualifying the definition in the Proceeds of Crime Act by excluding offences listed by the Secretary of State in a statutory instrument. (p 273) Although this would achieve the result they seek, we believe the list would be inordinately long and need constant updating, which would not benefit users.

108. The approach we prefer is that suggested by John Ringguth. He told us, on behalf of the Council of Europe, that he subscribed to the "all crimes" approach, but thought it appropriate to look at the possibility of a *de minimis* provision. (Q 490) He did not suggest how this might be drafted, and nor do we.

109. **Failure to report a suspicious transaction based on a minor criminal offence should not be prosecuted; and this should be achieved, not by a decision that in a particular case prosecution would not be of public benefit, but by amending the law so that such a transaction would not need to be reported.**

110. **Consideration should therefore be given to amending the Proceeds of Crime Act 2002 to include a *de minimis* exclusion.**

Consultation with the private sector

111. Given the degree of involvement of the private regulated sector, ongoing consultation with it is no more than common sense. At the level of the FATF it seems that significant progress was made during the British Presidency.[72] The Secretariat told us that the FATF undertook a series of consultation meetings with private sector representatives, including a meeting in London in December 2007 which focused on the exchange of information on money laundering and terrorist financing techniques. They told us that this reflected "an enhanced commitment by the FATF to engage with the private sector. The response by the private sector has been overwhelmingly constructive and productive." (p 249) In support of this view, Ms Scutt told us that the BBA and the International Banking Federation had a great deal of interaction with the FATF and that their experience was "very positive indeed". (Q 48)

112. Within the United Kingdom, the Government "views continued cooperation and engagement with the private sector as critical to the success of the anti-money laundering and counter terrorist financing regime."[73] The Government consulted extensively prior to the implementation of the Third Directive and have established various fora through which they seek to maintain an ongoing dialogue. Several of the private sector representatives from whom we heard participate in the work of these bodies. While there was a generally positive attitude towards these efforts at securing better interaction it was felt in some quarters that there remained room for improvement. (QQ 1–6)

---

72 Sir James Sassoon, Q 396.

73 Memorandum by HM Treasury, paragraph 23, p 43.

113. In the Revised Strategy on Terrorist Financing which he issued on 17 July 2008[74] the EU Counter-terrorism Coordinator recommended that the Commission and Member States should consider steps to increase the effectiveness of public-private cooperation on countering terrorist financing. **We agree with this recommendation, and urge the Government and the Commission to take it forward. We believe this applies equally to AML.**

Feedback

114. FATF Recommendation 25 requires FIUs to "establish guidelines, and provide feedback which will assist financial institutions and designated non-financial businesses and professions in applying national measures to combat money laundering and terrorist financing, and in particular, in detecting and reporting suspicious transactions." Article 35 of the Third Directive is to the same effect. Paragraph 2 requires that institutions governed by the Directive must have access to up-to-date information on the typologies adopted by launderers and terrorist financiers to facilitate the identification of suspicious transactions, while paragraph 3 provides: "Member States shall ensure that, wherever practicable, timely feedback on the effectiveness of and follow-up to reports of suspected money laundering or terrorist financing is provided."

115. The Treasury told us that there was extensive bilateral engagement with the private sector across the SARs regime. A number of improvements to private sector cooperation and communications had been taken forward. These included structured feedback by the UKFIU to a vetted group of private sector representatives of SARs reporters. Additionally there was direct feedback to firms from security and law enforcement agencies, and ad-hoc bulletins were produced by the UKFIU for reporting entities, describing current terrorist financing techniques drawn from current counter-terrorist investigations.

116. One of the 24 recommendations in Sir Stephen Lander's review of the SARs regime[75] was that SOCA's discharge of its responsibilities should be supervised by a Committee of SOCA's Board which would also include representatives of the reporting sectors and the end users. The SARs Regime Committee was set up in October 2006; it oversees the performance of regime participants and the discharge of their responsibilities. The Committee has produced two annual reports, for 2007 and 2008.[76] They provide a useful overview of the overall working of the regime, with valuable statistics.

117. Notwithstanding these improvements in private sector cooperation since the creation of SOCA, we received evidence that there remains room for improvement in both the guidance and the case-specific feedback addressed in Article 35 of the Third Directive. An important criticism by the BBA was that the information contained in guidance issued by SOCA was often of too general a character to be of much practical utility to private sector participants. (Q 46)

---

74 Document 11778/1/08.

75 Review of the Suspicious Activity Reports Regime (the SARs Review), SOCA, March 2006.

76 The Suspicious Activity Reports Regime Annual Report 2007 and The Suspicious Activity Reports Regime Annual Report 2008, published by SOCA.

118. We agree with Sir James Sassoon (Q 396): "It also comes back to what is happening to suspicious activity reports. There is only a certain length of time when we can expect the private sector across the world to be generating this vast volume of data without giving them more general feedback and an opportunity to discuss the methodology." **We urge SOCA to intensify its dialogue with the private sector in order to improve the practical utility of its guidance, and so to ensure better focus on matters of real importance.**

Case-specific feedback

119. SOCA at present provides only a limited degree of case-specific feedback to those who have filed SARs. (Q 175) Ms Banks for the ICAEW concluded: "… we think SOCA are already working hard with us in that area and so it is not something that necessarily needs political or parliamentary attention at this time". She did say that many accountants would like more feedback on a case by case basis, but she conceded that this was problematic. (Q 24)

120. The Law Society believes there are more significant shortcomings in feedback within the United Kingdom.[77] "In relation to individual SARs, the private sector will only receive feedback on the usefulness of their SAR and what action law enforcement is taking if they have sought consent, or if law enforcement requires further information from the reporter during an investigation. However, the level of feedback will be very limited or non-existent in most cases. Many of the Society's members still report a perception that their SARs are simply going into a black hole and they are not sure that they are actually making any difference in the fight against crime generally or money laundering more specifically." The Society gives only qualified support to the SARs Regime Annual Reports, and would like to see the Government look at how they can provide a more comprehensive review of the effectiveness of the anti-money laundering and asset recovery regimes within the United Kingdom on a regular basis.

121. Sean McGovern, the General Counsel of Lloyd's, also emphasised the need for improvement in this area. As he noted, "feedback would be quite helpful because it would justify the effort that has gone into it, but also may help in preventing further cases in future". (Q 512)

122. We appreciate the problems of providing case-specific feedback; they include the fact that SARs feed into different law enforcement processes, that many SARs can contribute to a single criminal investigation and that some SARs are used more for civil proceedings than criminal proceedings—reports of tax evasion being a particular example.[78] Nevertheless we believe that **it is only by being provided with increased levels of case by case feedback that the regulated sector will be persuaded of the value of the efforts it puts into the SARs regime.**

123. **Where it is clear that particular SARs have contributed to the success of an AML or CFT operation, and that feedback on this can be given to the originator of the SARs without compromising operations, SOCA should make it the practice to do so in selected cases where**

---

77 Memorandum by the Law Society, paragraphs 3.2.9 to 3.2.16, pp 10–11.

78 Ms Felicity Banks, Q 24.

they believe that this will demonstrate the importance of providing such reports.

Cost/benefit analysis

124. From the evidence we have received it seems that no cost/benefit analysis is carried out by any body at any level: not by the FATF, not by the EU,[79] and not by any department or agency within the United Kingdom. Yet individual institutions are dedicating very large sums of money to fulfilling their statutory obligations—as much as £36 million a year from one bank. (Q 29)

125. Ms Banks told us that the accounting profession believes that the SARs regime is cost-effective as it stands. "The benefits must be measured not only in terms of prosecutions for money laundering but in prosecutions for the underlying criminal offences; they must be measured not only in terms of the recoveries made but also in terms of more cost-effective criminal investigation generally, in the reputation of this country in terms of clean business practices, and in economic benefits in that business can be carried out much more fairly if people are competing on a level playing field, in that economic crime is picked up and dealt with." (Q 26)

126. Only the Law Society attempted to provided us with a cost/benefit analysis.[80]

BOX 7

Law Society estimate of cost/benefit of SARs

In the United Kingdom there are approximately 150,000 private sector entities regulated for anti-money laundering. In 2007/08 they made 210,000 SARs. In that period, the Government recovered approximately £135.7 million in criminal property. Even if all of the criminal property recovered was as a result of the AML regime and the receipt of SARs, which it is not, the highest average return per SAR would be approximately £646. The Government may point to the prevention value of the anti-money laundering regime. It is difficult to calculate the monetary value of crime that is disrupted and prevented but there has been no change to the estimated economic and social cost of serious organised crime of around £20 billion, according to the threat assessments in both 2006/07 and 2008/09.

The Law Society was unable to put a figure on the cost to solicitors' firms of compliance with the Money Laundering Regulations, since a survey carried out in 2008 showed that 77% of firms do not record such costs separately; but the costs to firms ranged from thousands of pounds to millions of pounds.

127. The Law Society would be the first to admit that this can only be the roughest of estimates, yet in our view it shows that the return per SAR, though low, is high enough to demonstrate the value of the regime.

128. However, we also think that the system will work better if reporters believe the benefit to AML/CFT is worth the effort and cost to them. **It is vital that SOCA should make a serious attempt to calculate the cost/benefit of the reporting of suspicious activities by the United Kingdom private**

79 But see paragraph 129 for details of a Commission study of the cost of compliance.

80 Memorandum by the Law Society, paragraph 7.3.4, p 15, and Annex B, p 18.

regulated sector. The Government must similarly press international bodies to provide a rigorous cost/benefit analysis.

129. On 10 June 2009 the Commission released a review of the cost of compliance with financial services regulation.[81] The study considers the cost of compliance with five Directives forming part of the Financial Service Action Plan (FSAP), together with the Third Money Laundering Directive which (unlike the Second Directive) was not part of the FSAP. **We commend the Commission for commissioning this study, recognising the importance of attempting to estimate the burden of compliance. We hope they will take this work forward, in particular to see whether the benefits of compliance justify the burden.**

Is the burden on the private sector disproportionate?

130. We have already referred in paragraphs 103–104 to differences of opinion between our witnesses from the regulated sector on the burden imposed on them by the SARs regime. The Law Society also believes that the implementation of the Third Directive in the United Kingdom, which is much more rigorous than in many other Member States, puts the regulated sector at a competitive disadvantage, though again the BBA and the ICAEW differ. (Q 45)

131. Jonathan Fisher QC, a barrister practising in London and advising firms in the regulated sector, agreed that they complained "on occasions bitterly" about the cost and burden of compliance, but thought they took the view that these were outweighed by the advantages of continuing to operate in London. He pointed out that there had not been an exodus of financial institutions from London as a result of the new AML and CFT regime being implemented. On the contrary, he believed that the imposition of robust AML and CFT procedures, far from damaging a country's financial interests, arguably served to enhance a financial centre's reputation and made it a more attractive venue for financial services. (p 253)

132. Later this year the Treasury will be beginning a review of the burden on the private sector. (Q 464) We welcome this. **One matter to which we expect them to pay particular attention is whether this burden does, as has been claimed, put the regulated sector at a competitive disadvantage compared to other countries.**

Third country equivalence and simplified customer due diligence

133. FATF Recommendation 9 authorises countries to permit financial institutions or intermediaries or other third parties to perform certain elements of the CDD process or to introduce business subject to certain conditions. The Recommendation further stipulates that "it is left to each country to determine in which countries the third party that meets the conditions can be based, having regard to information available on countries that do not or do not adequately apply the FATF Recommendations." This is the system of third country equivalence. The purpose is to help the private sector by allowing simplified due diligence—a lifting of the more rigorous customer due diligence—in relation to transactions with persons in named third countries.

---

[81] Study on the Cost of Compliance with Selected FSAP Measures: Final Report by Europe Economics, 5 January 2009.