UK Finance

UK Finance response to His Majesty's Treasury's consultation on the UK's Anti-Money Laundering (AML)/Counter Terrorist Financing (CTF) Supervisory Regime

30 September 2023

Executive Summary

1. UK Finance is the collective voice for the banking and finance industry. Representing more than 300 firms across the industry, we act to enhance competitiveness, support customers and facilitate innovation.

2. We welcome this consultation as a means of addressing some of our longstanding concerns regarding the entry, management and mitigation of risk within the system. While recognising the need for the UK to prepare for the next Financial Action Task Force (FATF) Mutual Evaluation, we do not think that this should distract or delay attention from the urgent need for a more effective UK system.

3. It is crucial that we move towards a system that is more effective at managing risk; ensuring the financial sector is not expected to act as de facto regulator of other less-robustly supervised sectors, and that we maintain a strong, collective regulatory perimeter. As part of this the discussion must recognise effective supervision as being far broader than legal compliance, incorporating risk management, prevention and disruption.

4. The consensus view across our membership is that the preferred option for reform within this consultation would be Model 3, the Single Professional Services Supervisor (SPSS). It is our view the system will see the most benefits if this single supervisor is a public body.

5. However, we do have some different views to those set out in the consultation which we believe will further strengthen the proposal. Instead of moving some sectors from His Majesty's Revenue and Customs (HMRC) to the new SPSS, we believe known risk sectors such as High Value Dealers (HVDs) or higher risk Trust or Company Service Providers (TCSP's) would benefit from moving to the Financial Conduct Authority (FCA) for supervision.

6. Model 1, the option to expand the Office of Professional Body Anti-Money Laundering Supervision (OPBAS), in our view lacks the ambition and therefore the ability to encourage the transformative improvements our system needs.

7. Equally, we strongly oppose Model 4, the Single AML supervisor, where we believe the proposal contradicts the key objectives of improved system coordination and feasibility that this consultation seeks to achieve.

8. We would like to see inclusion of new entrants, such as media and fintech sectors, within this consultation. Inclusion of these sectors during these initial discussions would help to ensure their inclusion in future should a phased approach be required.

9. It is our view that ambitious outcomes from this consultation are vital to ensure we are putting the UK on a stronger footing as and when the regulatory perimeter expands, in an effort to continue to protect our economic crime ecosystem.

Chapter 2: Objectives

10. Whilst we agree with the stated objectives of increased supervisory effectiveness, improved system coordination and feasibility, we believe the concept of feasibility needs to be balanced with the appropriate level of ambition.

11. Costs are an important consideration but there are options for support that have not been explored here. Vehicles such as the AML levy and the potential unlocking of suspended funds are set to provide the government with a substantial sum which has been agreed should be invested back into the UK's economic crime priorities. It is our view that this is an obvious and appropriate project for these funds to be put towards.

Chapter 3: OPBAS+

12. We understand the rationale behind the need to boost the powers being granted to OPBAS, but it is the clear view of industry that the proposals being put forward under the OPBAS+ model would not reflect the level of ambition that we are trying to achieve in bringing about a more effective AML/CTF supervisory regime.

13. It is our view that this model would not address some of the fundamental issues with consistency, and as a result, not help to strengthen the management and mitigation of risk across the ecosystem. However, we have responded to some of the specific questions contained within the consultation below:

    a) Across the economic crime ecosystem, there is a need to ensure that all supervisory bodies are working together to ensure a consistent approach in relation to the rules. This could be achieved through a structure of committees and working groups.

    b) With regards to rulemaking powers, OPBAS may require an increase in resources to monitor Professional Body Supervisor (PBS) compliance with the OPBAS rules. OPBAS could implement rules similar to the FCA's Senior Management regime which will drive improved PBS accountability.

    c) At present, it is legal for PBSs to set their own guidance; the MLRs and HMT practice allow PBSs to set varied guidance for the sub-sectors which they supervise. This could continue to drive inconsistencies which an OPBAS+ may not address.

    d) Granting OPBAS fining powers would allow them to hold individuals accountable i.e. fining and, depending on the nature of the fail, identified consideration that those individual(s) are banned from working as a PBS.

    e) We would welcome further consideration of HMT or FCA (as the OPBAS Handbook is housed within the FCA) having desk-based reviews with OPBAS to ensure compliance with the supervisory regime. Currently, OPBAS only provides HMT with reports.

f) We agree with the creation of a "default" sector supervisor to identify and address those unsupervised firms in the legal sector carrying out activity in scope of the MLRs without supervision. For example, this could look like the issuance of warning injunctions against unsupervised firms with any costs associated sent back to the unsupervised firm. If PBSs continue to operate as they do, then they could be designated as default supervisor for the legal sector.

14. The OPBAS+ model does not change the supervision structure and would therefore have a limited impact on supervisory effectiveness due to continued inconsistency of risk-based approaches across PBSs, and limited powers to enforce compliance such as fines and individual accountability.

15. The OPBAS+ model would also require the appropriate skill set to ensure effective oversight of the PBSs, who are currently more skilled on the details of the sector they work within.

16. The current OPBAS+ structure is too fragmented to allow for system coordination to be effective. The 2018 FATF Mutual Evaluation Report (MER) highlights this inconsistency between supervisors, noting that the quality of supervision varies among the 25 AML/CFT supervisors with significant weaknesses in supervision by the 22 legal and accountancy sector supervisors under OPBAS.

17. Feasibility constraints may need to be managed where OPBAS+ enhance the knowledge of their current staff to cover implementation of enhanced powers. There will be an increase in Subject Matter Expert (SME) resources required to fulfil the enhancement in OPBAS powers.

18. However, as above, it is our view that these proposals will not go far enough in addressing issues with consistency and therefore not bring about the ambition of system coordination improvement that we are all hoping to effect.

Chapter 4: Professional Body Supervisor Consolidation

19. It is worth noting that our comments regarding the following options are focused on our view of the AML supervision of professions, not their other conduct regulations nor the way professional associations organise themselves.

20. The PBS consolidation model would ensure consistency across the accountancy & legal sector, allowing SMEs within the current 22 PBSs to be brought together as one, with both the accountancy & legal sector working together to ensure a more consistent approach. At a minimum this would require support by sector specific guidance or similar to ensure the intricacies across and between sectors were still being reflected. With that said, it does not appear feasible for one of the existing supervisors to be able to take on these additional responsibilities.

21. Conceptually, the idea of consolidating the PBSs in an effort to encourage a more consistent approach across supervisors, and introduce consistent accountability for participants within the system, is welcome. However, it is our view that due to existing capacity and capabilities

within PBS's, there would be better improvements to overall effectiveness if we explored the SPSS model.

22. We have responded to some of the specific questions set out in the consultation below:

    a) Effective oversight is required whilst the new model is embedded to ensure continuity of business. With OPBAS housed within the FCA, it is reasonable for them to provide the oversight for consistency, with all supervisory bodies accountable to HMT.

    b) We believe that supervision of Accountancy Service Providers (ASPs) and TSCPs should be covered by a more consistent risk-based approach, with ASPs and TCSPs supervised by the consolidated PBSs to ensure consistency of approach and supervision. As noted below, our preferred approach is for the majority of routine risk ASPs and TCSPs to be supervised by a consolidated supervisor and higher-risk TCSPs to be supervised by the FCA's more robust capabilities. The fragmented model, which was the result of having too many supervisors, led to inconsistencies in risk-based approaches which is one of the key weaknesses identified by the 2018 FATF MER.

    c) The UK-wide consolidation approach should mitigate unsupervised firms conducting business within the sector, strengthening the UK's framework with the PBSs being able to close down firms and/or issuing legal proceedings against them to do so. Any new powers afforded to PBSs should also be included in the Money Laundering Regulations (MLRs) for transparency.

    d) The PBS consolidated model would see PBSs following a consistent approach as defined by OPBAS, which should lead to less inconsistencies. However, this model could potentially lead to a stronger focus on larger firms, leading to smaller firms receiving less scrutiny. The fundamental requirement is for PBSs to be resourced with the skillset and capabilities required to adequately oversight the difference in specialism and firm size within the sector. As noted below, our preferred option is for PBS supervision in a single body to pool the necessary capabilities and resources for effective supervision.

    e) HMT would need to ensure that PBSs have effective powers similar to the FCA's to allow for the driving of consistent compliance. Where compliance has failed, there is a need to ensure that the consequence will be aligned across all sectors.

23. Whilst we support the principle of consolidation of the many legal and accountancy supervisors, we do not envisage one of the existing supervisors as being resourced and able to support this. It is difficult to envision how improvements to system coordination from an effectively resourced supervisor would be developed within this model. As a result, we believe the option of a single professional services supervisor under a new public body, as below, is the preferable option.

Chapter 5: Single Professional Services Supervisor

24. It is our view that this model most accurately reflects the level of ambition we should be striving for within UK supervisory reform. This model combines the improvements to consistency of supervision set out in Model 2 with a more feasible structure of a new public body to adequately resource and support this process. A new public body would help to support overall system effectiveness and better support delivery of cross-cutting government objectives.

25. There is consensus view that a public body would be best placed as the single supervisor. Whilst we acknowledge there will be initial set up costs here, we believe there will be savings long term from having fewer operational bodies and believe there are many benefits from bringing together the regulated population in this way. It is our view that costing considerations must utilise existing and upcoming spend mechanisms such as the AML levy and potential unlocking of suspended funds.

26. However, rather than take sectors from HMRC and move them to the new SPSS, the preference would be for these to be moved to the FCA. Our view is that the FCA is far better placed to pick up the supervision of those sectors, at pace, compared to a new body. It will also be more prepared for the specifics of many of these sectors, especially those deemed to include higher risk categories.

27. The FCA is recognised as an effective regulator in terms of monitoring and enforcing compliance with the Money Laundering Regulations, comprehensive supervisory visits and providing balanced industry guidance. It is further recognised that they continue to strengthen their risk-based approach to AML/CTF supervision. The FCA have been forthright in its warnings to money launderers, with several keynote speeches warning firms of the severe consequences where they fail to enact purposeful AML measures.

28. It is our view that we should take advantage of the FCA's experience and skill in AML/CTF supervision and support the movement of those sectors deemed to fall into higher risk categories e.g. MSBs, and higher risk TCSPs.

29. Some members also support a further extension to the SPSS proposition where the single supervisor would sit within the FCA. This would help to provide consistency and upskilling of the new supervisor to the standards of the FCA but would need to be balanced with capacity constraints.

30. It is our view that this strengthened model, of a SPSS with extended FCA supervision, helps to address the fundamental concerns with consistency of supervision across the regulated sector and best supports improvements in our existing systemic weaknesses. There would be considerable benefit to leveraging the capabilities and skillsets across existing PBS's into one professional sector focused supervisor.

31. We believe that this model could strengthen it's understanding of the intricacies of the professional bodies by developing supporting guidance similar to JMLSG. It is crucial that,

mirroring the JMLSG model, this sector specific guidance is fed into by the respective sectors to ensure accuracy and tailoring to practical requirements.

Chapter 6: Single AML Supervisor

32. We do not believe the Single AML Supervisor is a feasible option for consideration. It is difficult to envision a single entity that could adequately supervise the breath and scope of the current regulated sector. Whilst this approach could tackle the concerns regarding consistency of approach across supervisors, it would be at the cost of knowledge, resource and capabilities for effective supervision.

33. There are a number of significant differences between financial services and non-financial professional services that we believe require separate treatment by dedicated supervisors. These include differences in scope of regulated activity, with nearly all financial services but only a subset of professional services falling under the MLRs and AML supervision. There are similarly significant differences in the volume and structure of regulated transactions as well as the relationship between AML regulations and sector-specific conduct regulations.

34. As a result it is our view that this model would significantly and radically weaken the economic crime supervisory regime, resulting in an ecosystem more vulnerable to abuse by bad actors, where risks are more easily let in and more difficult to identify and manage.

Chapter 7: Sanctions

Given the change in the sanctions context in the UK since Russia's invasion of Ukraine, have supervisors changed their approach to oversight of sanctions systems and controls amongst regulated populations? If so, what activity has this entailed?

35. There is greater scrutiny of firms' sanctions systems and controls. The FCA is conducting sanctions screening testing in firms whereby synthetic data from the OFSI consolidated list is plugged into firms' systems and the number of alerts is reviewed by the FCA.

36. Additionally, there has been greater engagement from OFSI with firms. This is evidenced by several briefings and Q&A sessions to clarify certain sanctions measures that the UK government have introduced such as the oil price cap and legal advisory services restrictions.

37. Early in 2022, the FCA request copies of all OFSI notifications (potential breaches and frozen funds) to also be submitted to the FCA regardless of whether there had been an underlying control failure or weakness. It appears that this was not consistently applied across all UK FIs.

38. This change in approach resulted in duplicative reporting of matters and in a number of cases duplicative requests for information (RFIs); there has been a significant increase in RFIs from the FCA in 2022/2023.

Do supervisors need additional powers to monitor sanctions systems and controls effectively, or can this be done under existing powers? What would any new powers need to consist of?

39. From an OFSI and FCA perspective, we do not believe that supervisors require additional powers as the current powers provide sufficient legislative grounds / mechanisms to oversee sanctions compliance within the financial services sector.

40. There is a need for greater co-operation between the sanctions and export control setting authorities (FCDO & Department for Business and Trade ("DBT") and the supervisory and enforcement authorities; FCA & OFSI) so there is a clearer link between the sanctions/export controls requirements and potential enforcement risk.

41. While we understand the different roles undertaken by setting and enforcement authorities, we would encourage greater coordination between the two on listings to ensure clarity on reasons and intent.

42. In the context of the Russia sanctions some listings by the FCDO contained wording around designated persons having control over other entities which resulted in considerable confusion and uncertainty over the treatment of such entities – with OFSI appearing unable to explain or clarify the position.

43. Given the nature of the more recent trade sanctions (activity based), other authorities outside of the FCA and OFSI also have an increasingly important role to play e.g. DBT (ECJU) in providing proper guidance across all relevant industry sectors, so the measures are properly administered and are effective.

44. While sanctions and export controls apply to all UK persons, the current regime is very focused on compliance within the financial services sector, rather than the actual UK persons undertaking the activity.

45. For example, the current requirement for FIs to obtain separate financial services licences, for export activity that has already been authorised by the ECJU for the UK exporter. This duplicative licensing requirement appears to provide no additional value for the authorities but instead diverts FI compliance resources and time away from more critical sanctions and export controls compliance activities.

Aside from legislative powers, do you foresee any other barriers to supervisors effectively monitoring sanctions systems and controls?

46. Yes, while all UK firms (and non-UK firms in the UK) must comply with all sanctions imposed by the UK government, each firm will have an approach tailored to their specific sanctions risks based on their activity (e.g. financial services, import and export of goods, legal and professional services, etc.). Therefore, it is imperative for supervisors to issue guidance on what is expected from different firms, across all industries, regarding their systems and controls to comply with the different types of sanctions and ensure that the required standards are met across the board. Firms of different sizes and in different industries do not all have the same capacity to invest in their sanctions systems and controls. The sanctions framework of manufacturing firms would be geared more towards trade sanctions, while financial

institutions gear their sanctions systems towards financial sanctions; bigger firms generating more revenue will have a greater capacity to implement a more holistic sanctions framework.

47. Another barrier is the lack of financial services expertise from the relevant supervisors. We often see a misunderstanding of the financial activity or products in the types of questions being asked by the supervisors. Prior to issuing sanctions, supervisors should undergo extensive consultation with financial services firms to fully understand the type of activities and products that will be affected by sanctions and other regulations to ensure that unintended consequences are eliminated.

48. The need to upskill supervisory staff, not just on regulatory requirements, but operational processes and controls within FIs, including screening technology is paramount to an effective UK sanctions regime.

49. Among other benefits, this would give a better understanding of the challenges FIs face in quickly operationalising complex new sanctions measures (new debt, equity, export & import, new investment banks and correspondent banking restrictions) plus restrictions on the provision of associated financial services. OFSI and the FCA have increased their engagement and dialogue with industry since the new Russia sanctions have been imposed, and we underline that this is a positive step that should continue and be built upon. A better understanding of FIs' processes would also help address the lack of acceptance of a risk-based approach for the design and application of sanctions controls e.g. when compared to AML. For example: a belief that sanctions screening lists can be updated "immediately" without appreciation that list updates take time to ingest (including impact assessment on payment systems) and alerts take time to be adjudicated.

50. Lack of oversight in other non-FI sectors, that are also subject to sanctions laws and regulations e.g. manufacturers & exporters of sensitive technologies, insurance companies, other service providers. At times there is a seemingly disproportionate focus on the larger FIs which tend to have well-resourced and established sanctions compliance frameworks.

51. Inconsistencies in the application of sanctions prohibitions between the UK, US and EU, including a lack of alignment on timing, targets, and ownership and control definitions.

52. There is a current move within a number of EU countries requiring FIs to screen domestic transactions which detracts compliance funding and resource away from greater sanctions risk processes. We would strongly caution against any such requirements as they are inefficient and ineffective.

53. Given the mandatory reporting regime and lack of statute of limitation in the context of sanctions breaches / reporting can result in compliance resources as well as supervisory resource being diverted to activity that for the most part adds little to no value in managing sanctions risk:

    a. Investigation of historic breaches – in some cases going back to the start of a sanctions programme appears to offer little benefit and simply ties up resource that could be better utilised (Libya 2011) (note: US has a five-year limit);

b. The requirement to report non-material low value breaches (note: US is a voluntary reporting regime).

Should any new potential supervisory powers relating to sanctions broadly cover all types of UK sanctions?

54. No, sanctions covers the whole of the UK economy and as mentioned above, firms belonging to certain industries will interact with different types of sanctions more than others e.g. banks deal mostly with financial sanctions and exporters with trade sanctions, although we recognise that there is often overlap.

55. Any new potential supervisory powers should be given to multiple supervisors with a clearly defined remit. This proposal follows the current model whereby the ECJU broadly covers trade sanctions and would lead enforcement action regarding trade sanctions breaches. Similarly, OFSI broadly covers financial sanctions and would lead any enforcement action to do with financial sanctions. Having a separate supervisory authority for each type of sanction would likely mean that the authority will have an in-depth understanding of the sanctions in place and the practical implications for the firms that have to implement them. Having one supervisor covering all types of sanctions may lead to a more generalist approach to sanctions supervision, and the specialist knowledge of the sanctions and the industry sectors impacted by the measures will be lost.

56. Increased collaboration across the various regulators and implementers with industry would be more beneficial and allow the specialists to concentrate on their areas of specialism, while ensuring there are no gaps.

Chapter 8: Options Comparison

57. Our view is that the option leading to most improved supervisory effectiveness and improved system coordination will be the consolidation of all professional body supervisors under one new public supervisor, the SPSS. To further encourage improvements across the system, we believe the sectors being removed from HMRC supervision should instead be moved to the FCA as a more experienced and better resourced existing supervisor.

Please contact secretariateconomiccrime@ukfinance.org.uk to discuss the content of this consultation further.