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Money laundering and the financing of terrorism

Volume II: Evidence

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Minutes of Evidence

WEDNESDAY 4 MARCH 2009

Present	Avebury, L	Hodgson of Astley Abbots, L
	Dear, L	Jopling, L (Chairman)
	Faulkner of Worcester, L	Marlesford, L
	Garden of Frogmal, B	Mawson, L
	Hannay of Chiswick, L	Richard, L

Memorandum by the British Bankers' Association (BBA)

The British Bankers' Association (BBA) is grateful for the opportunity to submit evidence as part of the Sub-Committee's inquiry into EU and international cooperation to counter money laundering and the financing of terrorism.

The focus of the Sub-Committee's inquiry is into the nature and extent of Member States' cooperation in the global response to money laundering and terrorist financing and not the legal obligations imposed on Member States, credit and financial institutions and related professions by the anti-money laundering framework.

COOPERATION WITH AND BETWEEN FINANCIAL INTELLIGENCE UNITS (FIUs)

How effective is cooperation among FIUs, and between FIUs and other authorities? What are the practical results of this cooperation?

Unable to comment. The BBA and its members are not involved in the cooperation arrangements among FIUs and between FIUs and other authorities.

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

BBA members, as part of the reporting sector under the Proceeds of Crime Act, disclose information to the UK FIU by filing suspicious transactions reports and other reports provided for by relevant legislation. BBA members also provide information in response to further requests from the FIU's. The Serious Organised Crime Agency (SOCA) reports that in 2007–08 the BBA's members submitted over 145,000 Suspicious Activity Reports (SARs) to the UK FIU, sought consent on 5,238 occasions and submitted 838 SARs specifically on terrorist finance.

Requirements on FIUs to provide feedback are established by the Financial Action Task Force (FATF) standards and the third Anti—Money Laundering Directive. FATF Recommendation 25 deals with feedback. The FATF has produced a document entitled "Best Practice Guidance on Providing Feedback to reporting Financial Institutions and Other Persons". According to this guidance, the FIU should publicly release reports that include statistics, typologies, and trends as well as information regarding its activities. Competent authorities should establish guidelines that will assist financial institutions and designated non-financial businesses or professions ("DNFBPs") to implement and comply with their respective AML/CFT requirements. At a minimum, the guidelines should give assistance on issues covered under the relevant FATF recommendations, including (i) a description of money laundering (ML) and terrorist financing (TF) techniques and methods, (ii) any additional measures that these institutions and DNFBPs could take to ensure that their AML measures are effective.

It is important to note that under Article 35 of the third AML/CFT Directive "Member States shall ensure that wherever practicable timely feedback on the effectiveness and follow-up of suspicious reports on money laundering and terrorist financing is provided". Moreover, "Member States shall ensure that the institutions and persons covered by this Directive have access to up-to-date information on the practices of money launderers and terrorist financiers and on indications leading to the recognition of suspicious transactions".

Therefore, the following types of feedback have to be provided, according to the Directive:

- Feedback on suspicious transactions reports, to inform the reporting entities about their follow-up; this case-by-case feedback should be provided “wherever practicable”.
- Feedback on money laundering and terrorist financing practices (trends and typologies).

BBA members recognise the necessity to provide feedback on specific cases does not imply the need of a systematic case-by-case feedback, ie on each and every disclosure filed by reporting entities. Indeed, according to the Directive, information on the outcome of particular reports has to be fed back “wherever practicable”. However, the volume of cases receiving direct feedback from the UK FIU is currently extremely low in comparison to the number of SARs submitted by BBA members. Feedback can be received in writing, along with indirect feedback by way of a Court Order (although there need not be a direct correlation between the SAR and the Order). Direct feedback is very occasionally received also in the form of telephone calls or letters of thanks from individual officers, although again volumes are very low. It has been known that at the conclusion of a major investigation that involved SARs being a submitted a de-briefing session is held for interested parties.

The UK FIU does produce a range of information and alert products that seek to provide general feedback to the reporting sector on money laundering/terrorist financing typologies. While helpful such information products tend to confirm prior or existing knowledge of money laundering and terrorist financing typologies. The BBA has called upon the UK FIU to involve the reporting sector more regularly in the development and drafting of information products to ensure these add value to recipients.

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

Unable to comment. The BBA and its members are not aware of any feedback and terrorist financing issues from the intelligence and security services.

What are the respective roles of Europol and Eurojust in countering money laundering and terrorist financing?

The BBA understands that Europol fulfils a role in the system of exchange of information between EU authorities on SARs in countering money laundering and terrorist financing. Eurojust’s role is to improve cooperation and coordination between the competent judicial authorities of the member States when investigating and prosecuting transnational organised crime.

MONITORING IMPLEMENTATION

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

Other than the European Union’s general infraction proceedings, the BBA is unaware of any formal mechanisms for monitoring implementation of the relevant legislative measures. Under the umbrella of the European Banking Federation, national trade associations including the BBA do share information on the status of implementation of relevant legislative measures in each Member State represented.

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

The BBA is unaware of any such consideration but would welcome such an exercise.

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

The BBA is not aware of any such plans but would welcome such a development.

Richard Cook
Director, Financial Crime

3 February 2009

Memorandum by the Institute of Chartered Accountants in England and Wales (ICAEW)

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

INTRODUCTION

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

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

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

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

MAIN POINTS

Differences in Implementation—Predicate Offences and Definitions of Money Laundering

1. There are significant differences in the implementation of the money laundering directives in the UK, as compared to other EU member states.

2. The ICAEW believes that the UK has been exemplary in its speed and thoroughness of implementation. The directives have also been implemented in the UK in a way which has led to a very large number of money laundering suspicious activity reports (SARs) having been made to SOCA, with an expensive and sophisticated system for their recording and use. For example, through our work with the European Federation of Accountants (FEE—www.fee.be) we understand that although practising accountants in the UK submit over 8,000 SARs a year, the accountancy professions in other member state have submitted no more than 100 in any year, and some much less.

3. Some other member states have been slow and reluctant to implement the money laundering directives. However, the ICAEW does not believe that inadequate implementation represents the most significant differences in the operation of the systems in the UK and other member states. Rather, the differences lie in the rigour and enthusiasm with which the implemented directives are interpreted and enforced, in the ways in which options in the directive are implemented and the underlying criminal offences are framed. The greatest differences seems to lie in two particular characteristics of the UK legislation, which are often not reflected elsewhere. These are:

— All crimes reporting.

Under the directives, the definition of "criminal activity" is limited to involvement in the commission of a serious crime, with the effect that the laundering of the proceeds of less serious crimes can be left out of the SARs reporting regime. That is not the case in the UK.

— Proceeds of own crime.

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

Cost Effectiveness, and its Measurement

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

RESPONSES TO SPECIFIC QUESTIONS

Cooperation with and between Financial Intelligence Units (FIUs)

How effective is cooperation among FIUs, and between FIUs and other authorities? What are the practical results of this cooperation?

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

10. The ICAEW can provide little evidence on the effectiveness of cooperation between FIUs, though we are aware of the existence of the Egmont Group of FIUs and we believe it to be operating satisfactorily. For example, we have received assurances from SOCA that sensitive reports of suspicions provided by ICAEW members will only be released to overseas jurisdictions through a member of the Egmont Group, with the result that ICAEW members need not fear irresponsible disclosure or misuse of their confidential information.
11. Cooperation between the UK FIU and other authorities appears to be extensive, and the evidence of our own relationship with SOCA supports this conclusion. Feedback operates in both directions, increasing trust between the various parties involved, and hence the efficiency and effectiveness of the system.
12. The private sector feeds into this cooperation through:
 - the Money Laundering Advisory Committee, led by HM Treasury and the Home Office, which includes representatives of key elements of the regulated sector, law enforcement and Government Departments;

- the Anti-Money Laundering Supervisors and Regulators Fora, where AML supervisors (including both public bodies and private professional bodies) discuss matters of consistency and concern with each other and with SOCA and Government Departments; and
- the inclusion of trusted individuals from the private sector in SOCA consultative bodies headed by the Suspicious Activity Reporting Regime Committee but also encompassing the “Vetted Group” which works with SOCA to share sensitive intelligence with the reporting community, and special focus groups such as those set up to provide private sector input into the development of information management systems within SOCA.

13. In addition, SOCA run their own training events for members of the private sector, and provide speakers for privately run training events. These events promote two way communication, with questions from the floor allowing concerns and comments on effectiveness to be expressed.

14. An example of the effectiveness of feedback and cooperation is in the area of the confidentiality of SARs. In the early years after the implementation of the Money Laundering Regulations 2003, we received fairly frequent reports of the disclosure to the clients of our members that their accountant had made a SAR, revealing a suspicion that the client had acted illegally. This most frequently occurred through administrative carelessness, or to assist the effectiveness of questioning (by indicating the seriousness of evidence of wrongdoing to a suspect). The effect on the client/accountant relationship could be catastrophic, and led to marked reluctance in other accountants to report their suspicions when these instances were revealed in the press. However, since feedback was given of the serious effects that these lapses could have on cooperation by the accounting profession, and (we believe) a more effective relationship between SOCA and the Law Enforcement Agencies, the reports of breach of confidentiality have radically reduced and are now very rare.

15. Both EU Directives and the FATF “Recommendations” require feedback to the private sector, but are not specific about how or what feedback should be given. Members of the accountancy profession would prefer more feedback, at a number of levels, both to help firms and the accounting professional bodies to manage risk and to provide feedback on the usefulness of reports. The ICAEW is aware that SOCA is working on increasing the amount and usefulness of the feedback that can be given.

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

16. The ICAEW understands that SOCA has good links with the intelligence and security services, and that terrorist and financing issues form a sizeable section of the their work.

17. Feedback given to the ICAEW by SOCA (for dissemination to selected members) includes information on areas of growing illegal activity which could be associated with terrorism, and where it is believed that higher awareness of these by our members could improve the intelligence available to Law Enforcement Authorities, by the making of more and better relevant SARs.

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

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

EU INTERNAL ARCHITECTURE

19. The ICAEW has no views on this matter.

INTERNATIONAL COOPERATION

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

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

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

21. The ICAEW has no views on this matter.

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

22. The ICAEW's knowledge of the use of the AML system to enforce compliance with tax obligations is mainly limited to the UK, where SARs are submitted in relation to suspected tax evasion, and are used by HMRC.

23. Not all jurisdictions consider tax evasion to be a predicate offence for money laundering purposes.

EU-UN COOPERATION

24. The ICAEW has no views on this matter.

MONITORING IMPLEMENTATION

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

What are the implications of those results for cooperation within the EU, and more broadly?

25. Besides the formal EU mechanisms for monitoring compliance with the money laundering directives, the professions and some trade groups have pan-European associations which also monitor implementation, particularly as it affects their members or stakeholder groups. An example of this is the ICAEW's work with FEE.

26. Global professional associations also work to monitor compliance in various jurisdictions on a global basis and advise their members on expectations, when acting overseas or in a cross border context. A good example of this is the useful site that the International Bar Association has set up at <http://www.anti-moneylaundering.org>, which gives a comprehensive guide to anti-money laundering legislation and compliance, throughout the world.

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

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

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

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

COMPLIANCE AND EQUIVALENCE

What are the powers and procedures with respect to those third countries which fail properly to implement international standards in these areas? Are these adequate?

Does the 2005 Directive adequately encourage non-EU States which have introduced equivalent systems to counter money laundering and the financing of terrorism?

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

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

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

How does the system for determining equivalence operate in practice?

32. Whatever the underlying jurisdiction with which financial institutions or professionals carry out commercial or advisory business, it is important for them to ensure that they understand the identity of the person with whom they are transacting, and the likely risks of the relationship. This is so whether or not the jurisdiction from which the contractual partner is operating has equivalent anti-money laundering systems and requirements. Though overall risks will be higher in non-compliant jurisdictions, there will nevertheless be higher risk clients in lower risk jurisdictions and vice versa.

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

ABOUT THE ICAEW

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

Felicity Banks
Head of Business Law

Nick Maxwell
Public Policy Manager

Memorandum by the Law Society of England and Wales (The Law Society)

1. SUMMARY

1.1 The Law Society (“The Society”) is the professional body for solicitors in England and Wales representing over 115,000 solicitors. The Society represents the interests of the profession to decision makers within Parliament, Government and the wider stakeholder community, and has an established public interest role in law reform.

1.2 The Society is committed to ensuring that anti-money laundering measures are clear, proportionate, effective and workable in practice. Through lobbying, the Society is campaigning for the achievement of a level playing-field across the EU and the rest of the world, in order to ensure that UK legal practitioners and businesses are not at a disadvantage in relation to non UK legal practitioners and businesses.

1.3 The Society welcomes the opportunity to provide evidence to the Sub-Committee on UK's anti-money laundering regime, and in particular, the opportunity to address the interplay with the anti-money laundering regimes across European and the rest of the world.

1.4 The European anti-money laundering Directives impose quite burdensome obligations on certain parts of the private sector. The strict implementation of the Directives by the UK Government and its decision to impose criminal sanctions for all breaches of the Directive is negatively affecting the competitiveness of UK solicitors, particularly in comparison to other legal practitioners in the EU and around the world.

1.5 The Society encourages the UK Government, the European Commission and the Financial Action Taskforce (FATF) to comprehensively examine whether the benefits of the anti-money laundering and asset recovery regimes they have each instigated actually outweigh the burdens imposed. The Society would like them to consider practical ways to help reduce the burdens placed upon the private sector and to provide more detailed information of methodology to help the private sector be more effective in their compliance.

2. BACKGROUND

2.1 International action to tackle money laundering began with the UN treaties on trafficking of illicit substances in 1988 and confiscating the proceeds of crime in 1990.

2.2 Following the G7 summit in Paris in 1989, FATF was formed to develop international policies to combat money laundering. FATF published the 40 Recommendations on Money Laundering in 1990 (the FATF recommendations).

2.3 The European Commission incorporated the FATF recommendations into its First Money Laundering Directive in 1991. That Directive was implemented into UK law via the Criminal Justice Act 1993 and the Money Laundering Regulations 1993. The Regulations applied to financial institutions and to those engaged in investment business under the Financial Services Act 1986 eg solicitors undertaking private client and corporate work.

2.4 In 2001, the European Commission responded to amendments to the FATF recommendations, by passing the Second Money Laundering Directive (the Second Directive). The Second Directive extended anti-money laundering obligations to a number of "service" professionals, such as accountants, auditors, tax advisors, estate agents and independent legal professionals. The individuals and entities covered by these obligations are referred to as "the regulated sector" throughout this evidence. The Second Directive was incorporated into UK law via the Proceeds of Crime Act 2002 and the Money Laundering Regulations 2003.

2.5 In 2005, the European Commission decided to adopt a Third Money Laundering Directive (the Third Directive). Key changes within the Third Directive were the extension of client due diligence checks to beneficial owners, the recognition of the need for checks to be applied on a risk-based approach, and the requirement for enhanced client due diligence to be undertaken in certain circumstances.

2.6 The Third Directive was implemented in the UK via the Money Laundering Regulations 2007, and further amendments to the Proceeds of Crime Act 2002. Implementation was completed on 15 December 2007.

2.7 The Society has had many years experience of the UK's legislation and the Money Laundering Regulations and has been actively involved in lobbying on the Directives and the Regulations, both in Europe and in the UK. The majority of the Society's members undertake work which is within the regulated sector and are therefore familiar with the primary legislation as well as having to comply with the regulations.

RESPONSE TO QUESTIONS

3. COOPERATION WITH AND BETWEEN FINANCIAL INTELLIGENCE UNITS (FIUs)

3.1 *How effective is cooperation among FIUs, and between FIUs and other authorities? What are the practical results of this cooperation?*

3.1.1 The Society's representative arm is not generally involved in making suspicious activity reports (SARs) to the Serious Organised Crime Agency (SOCA), the UK's FIU. As such, the Society does not have direct experience of the effectiveness of cooperation between FIUs.

3.1.2 However, a number of the Society's members have been required to submit SARs in relation to suspected cross-jurisdictional money laundering activities. They advise us that SOCA generally takes the lead in sharing the SARs with other FIUs through the EGMONT Group (an international group of FIUs) and keeps the Society's members informed of the progress of the SAR and the granting of consent in different jurisdictions. Solicitors advise the Society that on this practical level, there appears to be a good level of cooperation between FIUs at an international level.

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

Private sector's involvement

3.2.1 Through the submission of SARs, in accordance with the requirements under the Proceeds of Crime Act 2002, the private sector provides the FIUs with raw intelligence on money laundering and other crimes. Where those SARs contain information on cross-jurisdictional criminal activity, they may form the basis for intelligence reports to be disseminated by SOCA to other FIUs.

International standards on feedback

3.2.2 The provision of feedback to the private sector from FIUs is required by a number of international standards, issued both by FATF and the European Commission.

3.2.3 FATF recommendation 25 provides: *The competent authorities should 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.*

3.2.4 FATF recommendation 32 provides: *Countries should ensure that their competent authorities can review the effectiveness of their systems to combat money laundering and terrorist financing systems by maintaining comprehensive statistics on matters relevant to the effectiveness and efficiency of such systems. This should include statistics on the STRs (suspicious transaction reports) received and disseminated; on money laundering and terrorist financing investigations; prosecutions and convictions, on property frozen, seized and confiscated; and on mutual legal assistance or other international requests for cooperation.*

3.2.5 The Third Directive contains the following articles:

Article 33

- (i) Member States shall ensure that they are able to review the effectiveness of their systems to combat money laundering or terrorist financing by maintaining comprehensive statistics on matters relevant to the effectiveness of such systems.
- (ii) Such statistics shall as a minimum cover the number of suspicious transaction reports made to the FIU, the follow-up given to these reports and indicate on an annual basis the number of persons prosecuted, the number of persons convicted for money laundering or terrorist financing offences and how much property has been frozen, seized or confiscated.
- (iii) Member States shall ensure that a consolidated review of these statistical reports is published.

Article 35 (sub parts 2 and 3)

- (ii) Member States shall ensure that the institutions and persons covered by this Directive have access to up-to-date information on the practices of money launderers and terrorist financiers and on indications leading to the recognition of suspicious transactions.
- (iii) 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.

Feedback from FATF

3.2.6 FATF provides a number of detailed typology reports on their website each year. In 2008 these reports began to focus in greater detail on terrorist financing methodologies and to cover how these methodologies apply in non-financial sectors also covered by the FATF Recommendations. These reports are of interest in identifying global money laundering and terrorist financing trends and methodologies, but can be of less relevance for smaller firms wanting to understand the money laundering risks they face in their local communities.

3.2.7 While mutual evaluations are undertaken in relation to different FATF jurisdictions each year, there is no consolidated report produced by FATF which outlines the size of the criminal economy in each jurisdiction and how effective the anti-money laundering regimes have been in disrupting and preventing the criminal activity and the laundering of the proceeds of that criminal activity. At present there is no agreed methodology for making such assessments, and academic research questions the capacity of agencies to undertake such assessments on the basis of existing information.

Feedback from the European Commission

3.2.8 The European Commission does not provide any information on methodologies or an annual report on the effectiveness of the money laundering regimes within each of its jurisdictions.

Feedback within the UK

3.2.9 SOCA issues an annual threat assessment which outlines the estimated size of the criminal economy and provides a general overview of the criminal activities prevalent across the UK, as well as an indication of where certain criminal activities are concentrated.

3.2.10 SOCA has recently started producing a range of “alert products” which highlight detailed methodologies being utilised within the UK to launder funds. Some information is also provided as to where in the UK these particular methodologies are being employed. Currently these alert products are provided to law enforcement bodies and anti-money laundering regulators and supervisors. Due to the nature of the protective marking and confidentiality disclaimers on these products, permission needs to be obtained from SOCA on a case by case basis when disseminating this information publicly to one’s members.

3.2.11 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.

3.2.12 SOCA is now producing an annual SARs report. This provides an overview of:

- the number of SARs received;
- who is making those SARs; and
- where they are able to obtain information from other law enforcement agencies: information on the amount of money seized or recovered, arrests made, and convictions obtained.

3.2.13 This report goes some way to helping demonstrate to those covered by the UK’s anti-money laundering regime that their SARs are actually being used. However, the report does not make clear how many of the SARs made by the non-financial sector provide information which adds value to that provided by the financial sector. Nor does the report provide a comprehensive review of the whole UK criminal asset recovery regime. Responsibility for asset recovery sits across 43 police forces; a number of government departments, including HM Revenue and Customs and the Department of Work and Pensions; as well as the CPS. The information held by all of these separate agencies on asset recovery is not collated into a single report.

3.2.14 The Society welcomes the efforts by SOCA to provide greater levels of feedback to the private sector and greater transparency in its processes. The Society also welcomes the consistent support from FATF to the regulated sector through the public dissemination of emerging methodologies.

3.2.15 The Society would encourage the UK government to look at how they can provide a more comprehensive review of the effectiveness of the anti-money laundering and asset recovery regimes within the UK on a regular basis. The Society would be interested in seeing both the European Commission and FATF produce a regular review on the effectiveness of the activities being undertaken across their member jurisdictions to prevent and disrupt money laundering. The Society appreciates that at this time, there is no

internationally agreed methodology for collecting and assessing this information. The creation of such a methodology should be the first step in this process.

3.2.16 The Society would also be interested in more information being provided about methodologies which will assist those regulated persons in the non-financial sector to identify warning signs of money laundering within their sector and particularly to help identify suspected terrorist financing.

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

3.3.1 The Society appreciates that the provision of information about terrorist methodologies can be particularly sensitive and has the potential to jeopardise existing investigations or provide inspiration for new terrorists cells in their planning. However, there is a legal obligation on solicitors to be alert to warning signs of terrorist financing and to report cases of known or suspected terrorist financing. Failure to discharge those legal obligations effectively may lead to a jail term.

3.3.2 For this reason the Society is concerned about the lack of information, particularly for those in the non-financial sector, in relation to warning signs of terrorist financing. The Society appreciate the work being done by FATF to incorporate more terrorist financing methodologies within their typology reports, and encourages both the UK Government and the European Commission to look at ways to develop greater information on terrorist financing methodologies for those outside of the financial sector.

3.3.3 The Society would be happy to work with governments and law enforcement agencies on ways to disseminate this information to its members for the purpose of terrorist financing prevention, without it being disseminated more widely to the public.

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

3.4.1 The Society has no comment to make on this question.

4. EU INTERNAL ARCHITECTURE

4.1 *To what extent is the EU internal architecture adequate to counter current and future challenges?*

4.1.1 The European Union's internal architecture in this field is a complex structure of inter-governmental cooperation under the third pillar in relation to policy and judicial cooperation mechanisms and first pillar Community law. Because the anti-money laundering obligations originate from FATF, an international body, there is no obligation on the Commission to undertake any impact assessment to consider whether the obligations imposed are proportionate to the perceived ill within Europe or that they are fit for purpose.

4.1.2 The competence relating to anti-money laundering matters is split between the Directorate General for Internal Market and the Directorate General for Freedom, Security and Justice.

4.1.3 This results in a myriad of decision-making procedures, including:

- co-decision;
- consultation;
- implementation measures adopted under the comitology procedure; and
- adoption by parliament in the form of a directive.

4.1.4 Implementation into national law is left to Member States, who may face internal pressures during implementation processes that are different to those taken into account during negotiations for the passing of the Directive through Commission processes. This may mean that Member States significantly delay implementation, only partially implement or implement on a basis that is different to its represented intentions during the negotiations in relation to a Directive.

4.1.5 While the Commission has the power to commence infringement proceedings against those Member States which fail to implement a Directive, this procedure is costly and time consuming. The Commission cannot act to remove either gold-plating or under-implementation in national law which acts as a competition barrier.

4.1.6 The Society has found that the current approach has not provided the best model for coherence and clarity. The Society appreciates that in the area of money laundering there is a delicate balancing act in developing legislation that will give sufficient powers to law enforcement, but not overburden private sector participants, all within the confines of the FATF recommendations.

4.1.7 During the drafting of the Third Directive, the Society proposed a number of amendments which were tabled by a Member of the European Parliament. These amendments were proposed on the basis of the Society's detailed understanding of how various legal entities are formed and conduct their business, and how different transactions proceed to completion. The Society recommended amendments which were designed to reduce unnecessary burdens on the regulated sector while ensuring that the right information about ownership and transactions were obtained at the time where it was most likely to uncover money laundering. The Society also made a number of recommendations which were designed to ensure a more level playing field across the European Union.

4.1.8 During the committee stages many of the Society's proposed amendments were adopted and formed part of the draft plenary session report. However most of these amendments were withdrawn seemingly as part of the wide political negotiations with the Council of Ministers and the rush to secure agreement on the text. Many of the issues on which the Society sought amendments are the same issues which are still causing the solicitors profession much difficulty and great expense.

4.1.9 In terms of national implementation, many of the other Member States have not extended their anti-money laundering regime to legal professionals and seven Member States have failed to implement the Third Directive a year after the deadline for implementation.

4.1.10 The UK, on the other hand, has strictly implemented the directive. The Society found the implementation of the concept of beneficial owners in relation to trusts particularly challenging. During negotiations in Europe, the Society were advised that steps would be taken during implementation into national law to make sure the definition actually worked for common law jurisdictions. Unfortunately when it came to drafting the regulations, HM Treasury advised that they were unable to make amendments because they were bound by the wording of the Third Directive.

4.1.11 The Society did not accept this as the correct position on UK implementation and received support from the Commission for its view. This meant that the Society had to undertake extensive lobbying work and obtain legal opinion which demonstrated that the proposed drafting was so lacking in meaning in English law that it was unconstitutional and unlawful. Compromise drafting was eventually agreed upon, although the application of the civil concept of beneficial ownership to common law trust is still an area which causes difficulty to many solicitors and others within the regulated sector. The repeated need to re-lobby on particular issues uses up valuable resources of professional and supervisory bodies, limiting the time available to be devoted to preparing guidance and advice for their members to help them comply with their obligations.

4.2 What are the respective roles of Europol and Eurojust in countering money laundering and terrorist financing?

4.2.1 Europol is the organisation that aims to improve the effectiveness and co-operation of competent authorities in the Member States in preventing and combating terrorism, unlawful drug trafficking and other serious forms of international organised crime. Under this remit, they have competence to deal with anti-money laundering and examine activity in relation to terrorist financing. However, the Society understands that Europol has little direct impact in the UK and that investigations will instead be led by UK agencies, such as SOCA.

4.2.2 Eurojust is a permanent network of judges and prosecutors, with a remit to enhance the effectiveness of the competent authorities within Member States when they are dealing with the investigation and prosecution of serious cross-border and organised crime. In the Council Decision establishing Eurojust, the competence to act in relation to the laundering of the proceeds of crime is clearly set out. The Society understands that co-ordination meetings between national authorities have taken place in relation to money laundering offences, but that the cases considered at these meetings have not had terrorist financing as their core issue. Eurojust has a coordinating function rather than a prosecutorial or investigative role as such. The Treaty of Lisbon would provide Eurojust with a mandate to initiate criminal investigations which it does not have under the current legal basis.

5. INTERNATIONAL COOPERATION

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

5.1.1 Full details of the mutual evaluations can be found on the FATF website. A short summary of the key international cooperation indicators for the mutual evaluations published in 2007 and 2008 is attached at Annex A of this paper [*not printed*].

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

5.2.1 The mutual evaluation reports appear to suggest that criminal justice cooperation in the area of anti-money laundering and counter terrorist financing works well at times but could be improved.

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

5.3.1 While the Society is aware that information on suspected breaches of taxation obligations, both nationally and internationally, forms the basis for SARs made in the UK, the Society is not aware of the extent to which this information is being shared with other FIUs.

6. EU–UN COOPERATION

6.1 *What is the extent of EU–UN cooperation on financing of terrorism? What are the longer-term implications of the Kadi judgment?*

Background to Kadi's case

6.1.1 The United Nations Sanctions Committee designated Mr Kadi and the Al Barakaat International Foundation as associated with Usama bin Laden, Al-Qaeda or the Taleban. In accordance with resolutions of the Security Council, UN Member States must freeze the funds and other financial resources of such persons or entities. To give effect to the resolutions, the Council amended Regulation 881/2002, ordering the freezing of funds and economic resources of the persons and entities listed, in order to include the claimants. The Court of First Instance (CFI) rejected Mr Kadi's and Al Barakaat's action for annulment of the Regulation. It ruled that in principle the Community courts have no jurisdiction, except concerning *jus cogens*, to review the validity of the Regulation as Member States are bound to comply with Security Council resolutions according to the Charter of the United Nations, an international treaty which prevails over Community law.

Judgment

6.1.2 While the ECJ confirmed that the Council was competent to adopt the Regulation, it set aside the CFI judgment. It found that Community courts must ensure the review of the lawfulness of all Community acts in the light of the fundamental rights which form an integral part of the general principles of Community law. This includes the review of Community measures which are designed to give effect to resolutions adopted by the Security Council. It annulled the Regulation in so far as it froze Mr Kadi's and Al Barakaat's funds as their rights of defence, including the right to be heard, and the right to an effective legal remedy had not been respected. Indeed, the Regulation had no procedure for communicating the evidence justifying the inclusion of the names of the persons concerned in the list. Moreover, the lack of guarantee, enabling the case to be put in the circumstances, constituted an unjustified restriction on the right to property. The Court maintained the effects of the Regulation for a period of three months in order to allow the Council to remedy the infringements.

Implications from the judgement

6.1.3 The Society appreciates and accepts that there is a public interest in the protection of society as a whole from terrorism and terrorist financing, and accept that at times law enforcement and international bodies will have to act quickly on preventative measures. However the Society firmly believe that due regard must be had for the individual's human rights at all times. These rights must particularly be respected once the initial threat of the financing has been curtailed through the imposition of sanctions and freezing orders.

6.1.4 In terms of the relationship with the UN/EU for future counter terrorist financing cooperation, the Society believes that this judgement will promote a greater transparency and accountability in the relationship. This will allow the European Union, through its legislative body to act as a responsible check and balance on the UN's use of what is an extremely draconian power.

6.1.5 The Society hopes that the Kadi judgement will produce a greater awareness within all international and legislative bodies of the need to balance carefully the public interest with the fundamental human rights of individuals when exercising powers.

7. MONITORING IMPLEMENTATION

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

7.1.1 The Directorate General for Internal Market publishes a log of the transposition measures for the Financial Services Action Plan Directives. As of 8 January 2008 this includes the Third Directive.¹ This table identifies where Member States have completed that notification process on the implementation of the Third Directive—or not.

7.1.2 At present there are seven Member States who have not communicated this information and infringement proceedings have been commenced.

7.1.3 Where a Member State notifies the Commission of their implementation measures the file is closed. To date no examination of the substance of the provisions contained in the Member State's legislation has been undertaken to determine infringement of specific articles. As such there is extensive variation in the level of implementation between Member States.

7.1.4 While the infringement procedure may be helpful in the long term as regards effective compliance with the EU Directive this is a lengthy and time consuming process.

7.1.5 As regards third pillar measures, the Council instigates a system of peer review. The European Commission publishes implementation reports. While these have the persuasive "name and shame" capability, there are no infringement powers under the third pillar.

7.1.6 The FATF mutual evaluations have a similar persuasive "name and shame" capability. However the fact that these reviews are conducted as a peer review and adoption of the final report is subject to a vote by the FATF membership. The Society is concerned that there may be pressure to soften criticism of fellow jurisdictions for political reasons rather than a strict application of the evaluation methodology. This may in turn reduce the effect of such mutual evaluation reports in shaping governmental action by the individual Member States.

7.1.7 FATF also has the power to list a jurisdiction as being non-compliant. The review of 47 jurisdictions commenced in 1998, with 23 jurisdictions listed as non-compliant in 2000 and 2001. FATF can not prohibit individuals or entities undertaking business with other individuals or entities within the non-compliant jurisdictions. However, it can issue warnings about those jurisdictions and recommend that Member States imposed high levels of due diligence for transactions and business relationships with individuals and entities from those jurisdictions. In 2006 the last two jurisdictions were removed from the non-compliant list. It should be noted that removal from the FATF non-compliant list does not mean that a jurisdiction has an anti-money laundering or counter terrorist financing regime which is fully compliant with the FATF recommendations or equivalent to the Third Directive.

7.2 What are the implications of those results for cooperation within the EU, and more broadly?

7.2.1 Where there are differing levels of implementation across different jurisdictions there is the risk of businesses within more regulated jurisdictions suffering a competitive disadvantage to those in less regulated jurisdictions.

7.2.2 The Society is aware that in certain jurisdictions where legal professionals are not covered by the Third Directive, their complete exemption from reporting suspicious activities is being used as a selling point. Even where direct competition is not affected, the costs of the extra burden of compliance with stringent anti-money laundering obligations decreases the ability of those firms to price their services competitively.

¹ http://ec.europa.eu/internal_market/finances/docs/actionplan/index/transposition_en.pdf

7.2.3 There is a risk that regulated businesses within strictly compliant jurisdictions will be subsidising law enforcement and crime reduction in other jurisdictions, where their greater compliance and higher levels of quality reporting result in relevant intelligence being disseminated abroad. This is of greater significance if the other jurisdictions are failing to provide timely and relevant intelligence to the FIUs in the strictly compliant jurisdictions.

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

7.3.1 The mutual evaluations conducted by FATF do not consider the costs actually borne by the private sector in meeting their compliance obligations. The mutual evaluations also do not quantify the scale of the criminal economy in the relevant jurisdiction or the actual overall results in disturbing or preventing criminal activity achieved through the anti-money laundering regime in that jurisdiction.

7.3.2 The European Commission did not undertake an impact assessment of the FATF obligations before passing any of the European Directives on anti-money laundering. The Second Directive contained a requirement to conduct a review of the extension of anti-money laundering obligations to legal professionals. This review did not occur until after the adoption of the Third Directive. Due to the number of Member States which had either not extended their anti-money laundering regime to cover legal professionals at all or who had significantly delayed in doing so, the report was unable to draw any significant conclusions as to the appropriateness of their inclusion.

7.3.3 The Society is of the view that it would be appropriate for both FATF and the European Commission to consider in detail whether the overall benefits from anti-money laundering regimes justify the burden placed on the private sector. As stated earlier in this evidence, a starting point for such a review would be the difficult task of formulating an agreed methodology by which to collect information and assess the extent of the criminal economy and the effectiveness of the anti-money laundering regime.

7.3.4 In the UK the Society understands that 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 UK government actually recovered approximately £135.7 million in criminal property. Even if all of the criminal property recovered in the UK was as a result of the anti-money laundering regime and the receipt of SARs, which it is not, the highest average return per SAR would be approximately £646. While government may point to the prevention value of the anti-money laundering regime, it is very difficult to calculate the monetary value of crime that is disrupted and prevented. However, it is interesting to note that there has been no change to estimated economic and social cost of serious organised crime in the UK of around £20 billion, according to the UK threat assessments in both 2006–07 and 2008–09.

7.3.5 Estimating the cost of compliance with anti-money laundering obligations for the regulated sector is also not an easy task. Firms may be able to quantify:

- the number of staff employed to undertake client due diligence checks and make SARs;
- the cost of subscriptions for e-verification services;
- the cost of new case management systems to record due diligence and ongoing monitoring; and
- fees incurred for training programmes or the cost of providing internal training.

7.3.6 Many firms will not however be able to quantify the amount of time spent by individual staff members across the firm:

- assessing the risks of clients;
- chasing up due diligence material;
- monitoring clients and transactions for warning signs; and
- discussing suspicions and internal reports with MLROs and deciding whether or not a SAR is required to be made.

7.3.7 These hidden costs are felt more keenly by those parts of the regulated sector where transactions are not mere numbers and ongoing monitoring is not susceptible to automated processes. What is clear is that the private sector is investing more in the UK's anti-money laundering regime than the UK government is recovering because of it.

7.3.8 The Society conducted a survey in late 2008 to assess how solicitors were implementing the Money Laundering Regulations 2007. While the responses in relation to costs of compliance were very small in number, by comparison to the profession as a whole, they do provide illustrative examples of what some firms

are spending on compliance. The results suggest that even small firms are spending thousands of pounds a year in compliance, while large international firms are spending millions.

7.3.9 The results of the survey are at Annex B of this response (*printed only in part*).

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

7.4.1 The Society is aware that the European Commission is set to review certain aspects of the implementation of the Third Directive during 2009 and 2010. The Society is already in discussion with the Commission about the issues which the review may legitimately cover.

7.4.2 From December 2007, FATF engaged in more open dialogue with the non-financial parts of the private sector which are covered by the FATF Recommendations. The Society was pleased to be involved, in conjunction with the CCBE and the IBA, in these productive discussions with FATF. These discussions lead to the development of useful guidance on applying the risk based approach to the legal sector.

7.4.3 The Society welcomes increased dialogue with legislators and policy setters in the area of anti-money laundering and counter terrorist financing. The Society is particularly keen to enhance understanding of legislators as to how non-financial sections of the regulated sector operate, so that greater proportionality can be built into anti-money laundering obligations.

8. COMPLIANCE AND EQUIVALENCE

8.1 *What are the powers and procedures with respect to those third countries which fail properly to implement international standards in these areas? Are these adequate?*

8.1.1 As outlined in section 7.1 above, FATF undertakes mutual evaluations and regular reviews of their non-compliant list. Where a jurisdiction is listed as non-compliant, FATF can recommend that Member States impose higher due diligence and require extra precautions be taken when dealing with individuals and entities from those third jurisdictions. FATF cannot take any direct action against the non-compliant jurisdictions.

8.1.2 The Commission's infringement powers do not extend to non-EU jurisdictions.

8.1.3 Individuals and firms in strictly regulated Member States which undertake business with those from under-regulated third jurisdictions face a higher risk of being involved in money laundering. This risk may act as a deterrent for some in conducting business within those third jurisdictions, but it is not clear that this restriction on business is sufficient to bring about changes in the anti-money laundering regimes of third jurisdictions. Instead, the higher the sanctions for those in the strictly regulated Member States, the greater the risk to undertake business in these third jurisdictions and the greater restriction is placed on their competitiveness and ability to operate freely across jurisdictions.

8.2 *Does the 2005 Directive adequately encourage non-EU States which have introduced equivalent systems to counter money laundering and the financing of terrorism?*

8.2.1 The Third Directive allows for client due diligence burdens to be reduced in certain cases where a regulated individual or entity is undertaking business with an individual or entity in a jurisdiction with equivalent anti-money laundering obligations. The Third Directive also requires that enhanced due diligence is undertaken in circumstances where there is a higher risk of money laundering; although what amounts to enhanced due diligence in such cases is undefined.

8.2.2 There are two key areas where equivalence can reduce burdens, these are through reliance and simplified due diligence.

8.2.3 In the Society's recent survey (at Annex B), only 40% of respondents had relied on regulated persons outside the UK and this was generally only other legal professionals. 64% of respondents advised that they chose not to use the reliance provisions because they remained criminally liable for any failures by the person relied upon, while 48% were not happy with the due diligence undertaken by others, even where the standards were supposed to be equivalent.

8.2.4 In relation to simplified due diligence, 71% found these provisions useful when they could use them; but for the majority of respondents, these provisions applied to less than 50% of their clients. Also, 43% found it difficult to obtain information which would allow them to decide that simplified due diligence actually could be applied.

8.2.5 Respondents reported a very small amount of work being lost due to enhanced due diligence, although some had received negative comments from clients about the extra requirements.

8.2.6 As such the barriers to non-equivalent jurisdictions are not insurmountable and the reductions in burdens for those which are equivalent are minimal.

8.2.7 The greatest incentive for other non-EU jurisdictions to develop equivalent systems to counter money laundering and terrorist financing would be clear evidence that the benefits to their economy and society as a whole outweigh the burdens imposed on the private sector. Unfortunately, to date this analysis has not been undertaken, nor this evidence provided.

8.3 *How does the system for determining equivalence operate in practice?*

8.3.1 There is currently no transparent system which provides an individual or entity in the regulated sector in the UK with any certainty that they are dealing with an equivalent jurisdiction or regulated market.

8.3.2 Regulated individuals or entities are required to make the assessment of equivalence themselves. Under the Money Laundering Regulations 2007 there is no single definition of an equivalent non-EU jurisdiction.

8.3.3 For reliance provisions to apply in relation to persons within a non-EU jurisdiction, the person must be:

- a credit or financial institution (or equivalent institution), auditor, insolvency practitioner, external accountant, tax adviser or independent legal professional;
- subject to mandatory professional registration recognised by law;
- subject to requirements equivalent to those laid down in the money laundering directive; and
- supervised for compliance with those requirements in a manner equivalent to section 2 of Chapter V of the money laundering directive.

8.3.4 Simplified due diligence will apply where the client is a company whose securities are listed on a regulated market subject to specified disclosure obligations. These are disclosure obligations which are consistent with:

- Article 6(1) to (4) of Directive 2003/6/EC of the European Parliament and the Council of 28 January 2003 on insider dealing and market manipulation;
- Articles 3, 5, 7, 8 10, 14 and 16 of Directive 2003/71/EC of the European Parliament and of the Council of 4 November 2003 on the prospectuses to be published when securities are offered to the public or admitted to trading;
- Articles 4 to 6, 14, 16 to 19 and 30 of the Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 relating to the harmonisation of transparency requirements in relation to information about insurers whose securities are admitted to trading on a regulated market; or
- Community legislation made under the provisions mentioned above.

8.3.5 Neither the Third Directive nor the Money Laundering Regulations 2007 specify whether it is sufficient that the other jurisdiction simply has legislation in place or whether practical compliance and enforcement is actually required. It is also not clear whether it is sufficient that the majority of the requirements set out are met or if all must be met.

8.3.6 Simply obtaining information, in one's own language, on the legislative frameworks existing in other countries, let alone information on their practical application is very difficult, time consuming and costly for those within the private sector.

8.3.7 HM Treasury has agreed a list of countries outside of the EU which are considered to have equivalent money laundering legislation. However this list is voluntary, non-binding and does not have the force of law.

8.3.8 The countries included on that list are:

- Argentina;
- Australia;
- Brazil;
- Canada;
- Hong Kong;
- Japan;
- Mexico;
- New Zealand;

- Russian Federation;
- Singapore;
- Switzerland;
- South Africa; and
- United States.

8.3.9 However, in the case of Argentina, Australia, Brazil, Canada, Mexico, and the United States, the anti-money laundering legislation does not apply to legal professionals, which is a requirement under the Third Directive. Other countries on the list have been reviewed by FATF which has deemed aspects of their compliance only partial or in some cases there are aspects which are non-compliant. As such, it is not clear that reliance on the list issued by HM Treasury would satisfy the requirements set out in the Money Laundering Regulations 2007 for assessing equivalence.

8.3.10 The Society and its members appreciate the flexibility that the current regulations provide in allowing firms to take a risk based approach in assessing equivalence in emerging markets. However the Society is of the view there needs to be greater transparency in the law, not just guidance or government statements, to make it easier and more cost effective for regulated individuals and entities to actually assess equivalence, particularly in well established jurisdictions and markets.

Annex B

THE LAW SOCIETY

ANTI-MONEY LAUNDERING COMPLIANCE BY THE LEGAL PROFESSION IN ENGLAND AND WALES

A REVIEW OF COMPLIANCE BY A NUMBER OF FIRMS ONE YEAR AFTER IMPLEMENTATION OF THE THIRD MONEY LAUNDERING DIRECTIVE IN THE UK

BACKGROUND

In August 2008, 115 solicitor's firms in England and Wales volunteered to take part in a detailed survey considering the processes adopted by solicitors to comply with the Money Laundering Regulations 2007 and the associated costs.

The survey was conducted in September 2008, with print copies of the surveys sent to participants. We received 55 responses, some of which were only partially completed.

HEADLINE RESULTS

- AML compliance pervades the whole firm. Half of the respondents were training 88% or more of their staff, with 36% of respondents training all of their staff.
- The 2007 regulations have required significant changes in existing systems; although that does not mean that there is the same level of sophistication in firms' systems. There was a general trend towards an increase in the complexity of the system and the amount of data it can capture. There was also an indication of increased staffing.
- The UK is exporting AML compliance for lawyers world-wide, with 62% of respondents with international offices advising that they are applying the UK standard to all of their offices.
- Documentation and audit of compliance activities remains an area for development:
 - 76% of firms had conducted a risk assessment on their firm as a whole, but only 72% had formally documented these risks.
 - 54% of respondents rely on fee earners' normal file notes to provide evidence of ongoing monitoring, only 23% have set deadlines for these notes to be made to ensure they are done.
 - 65% are auditing compliance through file checks undertaken internally. This suggests auditing of compliance on individual matters, rather than the auditing or review of the compliance system as a whole. While this is understandable given that the regulations have only been in place for 12 months, it is an area for future development.

- Greatest reported challenges include:
 - Time constraints are the greatest challenge in implementing the risk based approach.
 - The lack of publicly available data is the greatest challenge in identifying and verifying beneficial owners.
- The reliance provisions, which were meant to reduce the compliance burden, are not widely used.
 - In the UK, only:
 - 57% of respondents have relied on other solicitors.
 - 41% have relied on a financial institution.
 - 27% have relied on an external accountant.
 - Respondents are less willing to rely on other regulated professionals.
 - Outside of the UK, the level of reliance drops even further.
 - 64% of respondents said that the criminal sanctions attaching to them, if the other person made an error, were the greatest deterrent in not using the reliance provisions.
 - 64% of respondents had been asked by others if they could be relied upon, but only 48% agreed to the request. The risk of civil action against them if they made an error was a key reason for not agreeing to be relied upon.
- 33% of respondents had turned down a retainer from a politically exposed person, due to the perceived risks of that client.
- While there was a general perception that costs have increased since the 2007 regulations, 77% of respondents do not record specifically the costs of complying with anti-money laundering obligations.
- From the very small sample who provided costs information:
 - Costs of compliance range from thousands of pounds to millions of pounds.
 - Most of this is spent on undertaking due diligence and training.
 - 50% of firms which responded on the issue of costs indicated an increase in gross expenditure since the new regulations of 10% or more.
 - 90% of firms which responded on costs do not pass on the full cost of compliance to their clients.
- 67% of respondents felt that the Society had been supportive or very supportive of them in meeting their AML obligations.

January 2009

Examination of Witnesses

Witnesses: MR DESMOND HUDSON, Chief Executive, Law Society, MS FELICITY BANKS, Head of Business Law, Institute of Chartered Accountants in England and Wales, MS SALLY SCUTT, Deputy Chief Executive, British Bankers' Association, and MR RICHARD COOK, Director of Financial Crime, British Bankers' Association, examined.

Q1 Chairman: First of all can I say to all four of our witnesses thank you very much indeed for coming. Sally Scutt is hotfoot from Washington, she arrived this morning, and we particularly appreciate your being here. We appreciate very much the helpful information you have already sent us. This is the first witness session we have had—which will run on into the summer. Let me begin. The Government say that they seek to maintain an ongoing dialogue with the private sector on the nature and scope of the anti-money laundering and terrorist finance regime. Could each of you from the three organisations summarise the manner in which your organisations are involved in such consultation and the extent to which you believe they have proved to be valuable. Maybe I can start with the accountants, taking it from left to right.

Ms Banks: I am Felicity Banks and I have represented the Institute of Chartered Accountants in England and Wales in this area for about 15 years. I have sat on the Treasury's Money Laundering Advisory Committee since it was first set up where I represent the main accountancy bodies and I also chair the Anti-Money Laundering Supervisors Forum Accountants Affinity Group. These are all fora through which we communicate with Government, with other regulatory bodies and with law enforcement. I think they are all working really quite well. At the time that the Proceeds of Crime Act was passed in 2002 we had serious concerns with the regime. We thought it was far too rigorous and would undermine the relationship of professional accountants with their clients but since then several reforms have been made which have improved the regime, made it more cost-effective and to some

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extent less burdensome. We now feel that it is a cost-effective system that requires further improvement but we are content that our comments are taken into account.

Q2 Chairman: What sort of improvements?

Ms Banks: The change in the definition of the reporting regime so, for example, our members no longer have to report suspicions where the identity of the suspect and the whereabouts of the proceeds are not known. Before that our members felt we were obliged to report shoplifting, for example where our members advised small retail shops. Such reports took as much time as an anti-money laundering report of more substance to make but were virtually useless in the hands of law enforcement.

Q3 Chairman: Can we turn to the Law Society?

Mr Hudson: Yes, My Lord Chairman, my name is Desmond Hudson, I am Chief Executive of the Law Society. I would largely echo the comments of my colleague Ms Banks in relation to the first part of her answer. For the Law Society we find that our engagement with things like the Anti-Money Laundering Supervisors Forum, the Regulators Forum, the other committees is very good; we find that SOCA has made a noticeable difference in terms of the responsiveness to the comments and submissions from the wide professions and we also of course have contact with the Government, particularly through the Treasury, as well as through the European Union which clearly has a significant role here. However, we would depart somewhat from the latter part of the ICAEW's comments in the sense that we continue to have concerns as to the effectiveness of the scheme, the regulatory burden that it imposes on UK Plc and certainly on the practice of law in the UK and that there are a number of important questions that we believe need to be addressed.

Q4 Chairman: The bankers, which one of you would like to answer?

Ms Scutt: I am Sally Scutt, I am Deputy Chief Executive of the British Bankers' Association and also Managing Director of the International Banking Federation which represents the banks in the US, Canada, Europe, Japan, Australia, China, India and South Africa. In the BBA, and less so internationally with the others, we have worked closely over the years with the authorities in terms of trying to ensure that we have a regime that is effective and does its work in terms of barring criminals from the financial services industry. We have worked closely always with the Bank of England originally but now as an independent group on the joint money laundering steering group, and I am currently chair of the

editorial panel, and we produce guidance notes for the industry in order that they can achieve a suitable standard in ensuring that they comply with all the obligations that are put upon them. We also deal extensively with SOCA and have a role on their SARs transformation project which is about improving the effectiveness of their handling of the intelligence that they get from the industry and we too, like Felicity, are represented on the Money Laundering Advisory Committee. We have always held the view that no one part is alone and the system can only work if the industry, the authorities—and by that I would say the Treasury and the Financial Services Authority—and law enforcement have a balanced relationship in terms of obligation and effort. Our criticism would be that law enforcement are the ones who are rarely at the table for the policy debate but actually their problem is that they are simply completely under-resourced and that they do not have a target to tackle financial crime. That means that the burden on the industry is therefore greater, but that alone, the industry by taking its responsibilities, cannot ensure that the system is thoroughly effective.

Chairman: Thank you. Lord Hodgson.

Q5 Lord Hodgson of Astley Abbots: I wonder if we could go to the Law Society for a discussion about feedback. Your evidence—extremely impressive evidence if I may say so—is very helpful and you talk about the need for improvement in the regime by the UK Financial Intelligence Unit of case specific feedback on SARs. Certainly my discussion with City firms indicates that there is very little of this and therefore your members are operating slightly in a vacuum. What practical and legal difficulties do you think there would be for your members when the feedback is not provided—it is important to get that on the record—and also what priority would you afford to getting improvements in these areas?

Mr Hudson: I suppose the first part of the question is that in direct terms the absence of that feedback does not create an immediate problem for the practitioner; it is more the sense of the potential imposition of a higher burden of obligation or activity on behalf of the practitioner and the sense that they are not able to direct that in the way that they perhaps could if they were aware of what are the signs, what are the aspects, what are the issues. In saying that I recognise that there is clearly a very sensitive balance to be struck here between the provision of particularly specific case feedback, which one would not want to see in the wrong hands, so I understand that there needs to be some degree of confidentiality, but there is, as I say, a practical problem and what we would like to look at is to see whether there are better ways of making that case-specific feedback available. If I may say so I would specifically endorse the points

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made on behalf of BBA that the role of law enforcement is particularly important in those activities. As to what priorities I would give that, we think that is important but you might gather that we believe there are perhaps some wider-ranging issues that the UK Government should be reconsidering in relation to our AML regime.

Q6 Lord Hannay of Chiswick: I wonder if I could pursue that a little bit further. All of you have said that you are broadly satisfied with your dealings with the authorities on this; and that there is a real dialogue. But could you perhaps explain how that dialogue occurs. Do you sit and wait for the Government to come to you and talk about these matters or do you have a regular basis on which you can talk to them? If you want to propose changes do you generate those yourself or do you wait for them to come forward with them? It would be good to get some feel for how this dialogue works; is it purely a formalistic one or does it really leave scope for adjustment, flexibility and so on?

Mr Hudson: That is a very interesting series of questions. There is no regular dialogue so far as the Law Society is concerned with Government. We are in a position to initiate that dialogue and for the Law Society, for example, we have published some objectives, possibly some lobbying objectives, that we have set ourselves. For example, we believe it would be highly beneficial if there were to be a thorough study undertaken of the cost-benefit analysis because we have some concerns about the absence of clear empirical evidence here. The relationship, the dialogue that exists in terms of some of the taskforces we have spoken about, that is much more effective and there is more regularity to it. SOCA, for example, has introduced a whole series of improvements in that and information and views are passing two-ways in a much better way there and we are beginning to see practitioner-driven improvements and changes. As I say, it is in the wider systemic issue that I believe there is no regular dialogue, speaking of the Law Society, with Government and there needs to be such. We certainly feel ourselves free and the Government departments are receptive, they will obviously give one an audience to listen to proposals, and as I say we have set ourselves some public targets. The most obvious perhaps, in terms of our discussion this morning, is the importance we attach to providing this study of where the cost and benefit lie because it is our view, as you will have gathered from our evidence, that the strict application that we have here in the UK carries some issues with the wider debate and appreciation as to the appropriateness and the benefits that arise from them.

Q7 Lord Marlesford: It is in a sense a follow-up to what has been said, but the whole burden of the evidence from all three of our witnesses is to do with the burden and the cost and, as you put it, the cost benefit, all very important points. To give us some feel for the scale of the thing I found it very helpful that the bankers have told us that they have approximately 145,000 suspicious activity reports a year; could the other two groups give us some comparable figure for the number of suspicious activity reports which their members file a year?

Mr Hudson: On behalf of the Law Society I can give you that information. In the last year solicitors in England and Wales filed 6,460 SARs, quite markedly down from our previous estimate that would have been about 10,000 or so. One of the factors that I am sure is important, certainly speaking on behalf of solicitors, is that the provision of a report is a very important step in managing the potential criminal liability, the criminal sanctions, that solicitors face.

Ms Banks: Accountants in practice submitted something over 7,000 reports, I think of the order of about 7,300. Of course, chartered accountants working in financial services will have contributed to a lot more made by the regulated financial services.

Q8 Chairman: Would the bankers like to make a response to Lord Marlesford?

Ms Scutt: As we said in our figures last year we made something like 145,000 reports. That number could be significantly higher: one of the issues we have had with the system is the working of the consent regime which puts a very particular burden on the banks and, currently, the banks have to operate—we have a sort of agreement with SOCA on how to proceed. If the banks actually reported, as they were required to, according to the law under the consent regime SOCA would be completely swamped and that number would be very significantly higher and the whole system would grind to a halt. We were deeply disappointed with the review of the consent regime by the Home Office recently and they have decided not to change it; however, that does not change the situation with regard to the risk of sanction upon money laundering reporting officers in banks being found to not perform properly, so we are seeking a memorandum of understanding with SOCA and with the Home Office in order that they should be adequately protected.

Ms Banks: We would agree with the banking industry that it was extremely disappointing that the Home Office were not able to complete their proposed reform on the consent regime; however it is a very difficult area in that the necessities for professional firms in this area are very different from the needs of retail banks and so the problem was that it could not be changed in a single way which would make it easy

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to be operated by retail banks without making it more difficult to be operated by professional firms, so the decision was taken to run it on in the informal pragmatic way that necessarily worries the banks.

Q9 Lord Marlesford: Could the bankers submit to us as a paper, please, a copy of the way in which they wanted the consent regime changed, the submission they made, and if indeed the other two bodies also made submissions it would be very helpful if we could have a copy of those.

Mr Hudson: Certainly.

Ms Scutt: Yes, we can do that.

Chairman: That would be very helpful, if you could all do that. Lord Mawson.

Lord Mawson: I have been very interested in reading all these papers and getting a feel for all the macro relationships but I am a simple soul really and I wonder how it works for individual people like the lady who arrived in my office this week with very large folders about a problems which show that her family may have lost three houses through money laundering, with linkages into Pakistan and Oman—a very complicated picture really—but she is finding it impossible for anyone out there to take seriously her probably, even when she goes to the local police station. I am just wondering, firstly, how does a person like that actually get into the system to share her problem with someone who will take it seriously and drill into the detail of the problem and, secondly, how many people like her are out there, finding it impossible to engage with all this infrastructure that is meant to be in place to deal with these realities?

Q10 Chairman: Shall we have the Law Society's response to that?

Mr Hudson: My Lord Chairman, I would be very happy to have a go at that. Clearly the facts are rather complicated and one would need to know those, so my comments are perforce generalised. It seems to me that there are probably two issues that you are alluding to here: first of all that there could well have been criminal activity, criminal activity if I may say so beyond the predicate offence of, say, money laundering, and that must be an issue that the police ought to be considering. I would have thought that they have to be the first port of call in relation to an allegation of criminal activity. It might also be the case that the petitioner who spoke to you also has suffered some form of loss in relation to the transfer of title to property through identity impersonation, and you may be aware, my Lords, that this is not an unknown situation so far as the land registration is concerned, certainly in England and Wales. There one would have thought that again they could perhaps get in touch with the Land Registry if that is a factor, that that would be a place to start. As to the

questions of how many I have to say I find that very difficult to answer. I am certainly aware that there is a problem, for example, in terms of the potential for identity impersonation leading to property being mortgaged or sold away underneath an owner as it were, but the number of cases of that I think are relatively small; in relation to the specific context of AML I really just could not estimate but my guess would be that it is relatively small scale. I would suspect that this is a very intractable problem and, pursuing this through a retained and remunerated accountant or solicitor I submit would be very expensive.

Q11 Lord Avebury: We have moved a very long way from Lord Hodgson's original question which was about the feedback rather than individual SARs and in referring to this matter in 3.2.11 you outline the factors which determine whether or not there is feedback; that is to say whether the law enforcement requires further information from the reporter and even in those cases you say the feedback is very limited. What I would like to ask is whether you think this limitation on individual feedback is satisfactory or whether you would want to broaden the circumstances in which there is individual feedback on particular SARs.

Mr Hudson: From the Law Society's perspective we would see some benefit in providing more feedback on SARs, I think it could be helpful. I understand, as I alluded to in my earlier answer to the noble lord, that we need to balance that issue for reasons of confidentiality but, in a sense, if I may put it so without being disrespectful, this is something of a palliative. Our concern is that there is a systemic issue here and if I may, very briefly, I will give you an example. Let us say I am a solicitor in London and I am dealing with the sale of a hotel for £5 million and it turns out that the owners of that hotel have failed to obtain an appropriate licence—let us say they did not have their required waste disposal licence. They might have saved themselves £30 or £40 in not paying that waste disposal licence; that is probably a criminal offence and therefore the entirety of the sale proceeds of that hotel become tainted money and the full force of AML would bear on that circumstance. When I allude, my Lord Chairman, to the importance that we see in the progress, for example, that SOCA have made—particularly compared to NCIS—we welcome that and we support that and we applaud them for doing that, but there are more wide-ranging issues that concern the Law Society, such as that example I quote of a solicitor dealing with that problem, a £30 to £40 licence not obtained, therefore the entirety of the sale proceeds under our strict application of AML are tainted. That would not be the case if the lawyer dealing with that sale was based

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in Amsterdam or Paris or Frankfurt. It is important, therefore, that we do look at this issue of interchange of ideas as the system is here, Parliament has put this law in place and we need to make it work, but there are some wider issues that I would urge my noble lords to be considering and cost benefit and that sort of issue—the criminal application of sanctions and the applicability to all criminal offences, even something as I suggested there—I put to you is problematic.

Chairman: We have strayed an awful long way from Lord Hodgson's question and I am watching the clock because we are going to have to move on. Lord Dear, do you want to follow up Lord Hodgson or do you want to move on to SOCA?

Q12 Lord Dear: We will move on. Mr Hudson, thank you; I was going to ask something which has largely been covered anyway and that was to do with, on the one hand, this enormous volume of reports into an organisation which, by and large, may or may not be able to deal with the volume—you have covered that and are going to cover it in response to Lord Marlesford who asked for a further paper from you. Could I just focus on the question of the relationship between the Law Society and SOCA (the Serious Organised Crime Agency); to what extent is there co-operation and consultation? I recognise that you have links, but what are they like on the more general feedback of typologies of money laundering and terrorist financing as well, and what steps if any do you think could be taken to increase the effectiveness of that sort of guidance? You have brushed up against that already so it is coming right into volume on the one hand and accurate drilling down or response on the other.

Mr Hudson: Certainly from the Law Society's perspective we believe that SOCA has made a number of very useful improvements, that they are working seriously and effectively and there is this issue of co-ordination and sharing of information within sensible bounds. For example, we have seen them react very positively and sensibly to issues in relation to the SARs regime and in particular the consents regime. The performance we see from SOCA, for example, despite the clear resourcing problems that arise here, are much, much better than those that went before them. Also, as I have said before—forgive me for repeating this but it is important—we do recognise the need for a sensible balancing of openness and sharing of awareness with the need for confidentiality of some of those issues, so within the constraints that we are currently working with in the system I think we have seen sensible progress in the right direction. It has been very helpful and we would be very supportive of SOCA's intents in that regard.

Q13 Lord Dear: Could I follow that up? I am very concerned about volume as against the bottleneck effect that the volume would cause and it occurs to me as we sit here that one way that you could help to sieve out the wheat from the chaff is a signal on the SARs report that this really does look as if it is something serious or, frankly, this is the example you gave of the £5 million hotel and the waste disposal licence—"Frankly, we are letting you have this because we have to but we would not look any further". Does that sort of approach go on unofficially, because it would be a huge advantage to SOCA to have a professional indicating the wheat from the chaff so to speak?

Mr Hudson: There are already limited value reports so that point that you very sensibly suggest, can we have some way of identifying the very big matter and the rather small matter, there is already a structure for that to work and that is very sensible.

Q14 Lord Dear: Does that work?

Mr Hudson: It works within the constraints of the system because we come back to the point that we have this very strict application. My example was a little dramatic but it is not fanciful because of the very strict application of the way we would regard tainted money and, therefore, potential proceeds of crime; it is all-enveloping and that is different in many respects from the approach adopted by other European Union partners. My colleague from the BBA also made the point about pragmatic steps being taken, practical choices having been made, if you like, on a common sense basis, simply to make the volume of transactions work. It is not as acute for the legal profession as it is probably for bankers by a long, long way, but our members are having to take some of those pragmatic steps. Of course, for a lawyer and for a law firm there is inherent risk there because if I volunteer more information, trying to be helpful, what if my information is incorrect; what liability do I bring on myself or my firm in terms of trying to make the system work. If I may say so without appearing to be obstructive it is for the enforcement authorities and for the Government to design a system that is workable rather than for the practitioners, with all the best will in the world, to try and make the best of it.

Lord Dear: Could we ask for a similar view from the other agencies because it would be very helpful?

Q15 Chairman: If you wish to, but briefly if you could.

Ms Scutt: Of course we have a suspicion-based regime so the moment a bank suspects that there is something wrong with a transaction then they must submit reports. I would say in the early days of the regime, with the deep concerns about regulatory

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sanction from the FSA, there would have been many, many defensive reports in terms of just making sure that they were not going to miss something. Now we get feedback from SOCA, that helps a little, but we have to consider that even in these times the banking industry is passing through 550 transactions a second; without very much feedback—there is some but it is limited—it is very difficult to be able to prioritise, without intelligence of any kind, finding the sorts of things that are going through. The big step that we could take, particularly in the realms of counter-terrorist financing and now proliferation financing, is if we could find a way of communicating intelligence straight back to those required to report I think we would end up with a reporting regime that was much more accurate, that was better informed, and more intelligence which would be of use to SOCA and others would then be available.

Q16 Chairman: I am anxious to move on; can we hear very quickly from the chartered accountants?

Ms Banks: There is a box at the end of the SARs reporting form called “The reasons for suspicion” which enables reporters to identify what it is about the report that makes it worth making. Also, for extremely urgent cases, I understand from my members that you can ring up the duty desk at SOCA and this helps both with obtaining consent in very urgent cases and also drawing attention to live intelligence issues that need to be actioned very quickly.

Chairman: I am going to move on, I am very sorry, because we are getting very behind the clock. Lord Richard.

Q17 Lord Richard: Thank you, my Lord Chairman. I am quite interested in this concept of third-state equivalence and as I understand it—and can I just say my understanding is not yet very great—if you can establish third-state equivalence that does two things: one, it makes business transactions a bit easier and, secondly, it removes some of the potential risk that there is from the person in this country who is conducting the business. If one looks at the Law Society’s evidence—which I agree with Lord Hodgson is indeed comprehensive and terribly useful—at paragraph 8.3.7 you say that the Treasury has agreed a list of countries outside of the EU considered to have equivalent money laundering legislation. You then say: “However, the list is voluntary, non-binding and does not have the force of law.” I can understand the not have the force of law but what about the voluntary and non-binding clause, what is the use of something that is just voluntary?

Mr Hudson: I suppose that the argument behind the voluntary is to encourage participation and involvement and that might be seen as an initial step to, as it were, get the thing launched, but certainly for the legal practitioners there is a clear problem if it is voluntary and non-binding, it leaves you in a grey area, so if I were advising you as your solicitor would I say, “Look, we can take a risk on blah-blah-bah, it looks okay” or do we say “Well, this is a very high-profile transaction, public notoriety, we had better repeat all of the due diligence activities that we need.” It is in a sense, therefore, this grey area that we have a problem with. You will of course remember that there is this voluntariness on the part of the government of the relevant country to take part and these are difficult beasts to drag into line as it were.

Q18 Lord Richard: Could I just follow this up with one or two questions. You have a list of countries there which includes Argentina, Australia, Brazil, Canada, Mexico and the United States; as I understand it the anti-money laundering legislation does not apply to legal professionals in any of those countries, so if you are a solicitor in this country dealing with an attorney in America, the relationship there would not be one which was covered by third-state equivalence, is that right?

Mr Hudson: Yes.

Q19 Lord Richard: Good heavens.

Mr Hudson: It is very limited in its efficacy, it is very limited indeed.

Q20 Lord Richard: Finally, what amendments to the regulations would you like to see in order to cover it?

Mr Hudson: What we would ideally like to see—I stress the word ideally—is that there would be effective third-state equivalence that you could rely upon, but that is very problematic because of the point you make: if there is a different regime applying to a legal professional in the United States of America just how much equivalence can we get even if the government of the United States would want to agree? For example, there are significant differences between the positions of bars and law societies in continental Europe and here in the United Kingdom about the obligation to make any reporting. If I was speaking to colleagues at the French Bar or the Belgian Bar it would be a breach of my obligation as an avocat to make any disclosure, whereas in our country we take the view that solicitors for example as officers of the court have a wider obligation, and we generally, if I can put it this way, take the view that helping to deal with the financing of terrorism is an important obligation on a solicitor as an officer of the court, but that difference of approach makes the whole thing with third-state equivalence very, very

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problematical lawyer to lawyer and transaction to transaction.

Q21 Lord Faulkner of Worcester: Staying with the same thing, Mr Hudson, you make the point in your written evidence that there are common standards adopted within the European Union and you say in 3.2.8 that “The European Commission does not provide any information on methodology or an annual report on the effectiveness of money laundering regimes”. Are you saying that because that does not exist you think the problems are particularly severe in certain Member States?

Mr Hudson: No, the Law Society is not expressing an opinion on whether there are particular problems in Member State X or Member State Y; what rather we are saying is that because of those problems the comparability of processing, if you like the regulatory burden, differs across the EU, that certain activities for a law firm based in London would be more problematic, more expensive and carry a greater risk to the partners of that firm than if that activity was being done in Amsterdam or Paris or a different Member State.

Q22 Lord Faulkner of Worcester: How would you improve that?

Mr Hudson: I think that we here in the UK need to review the very strict application that we have brought in with the use of criminal sanction and liability for a lawyer or a chartered accountant to look at this all-enveloping definition of tainted money and, you know, if it is a criminal offence then it is money laundering. That is part of the problem.

Q23 Lord Faulkner of Worcester: A further part of the problem is that we in Britain enforce these directives and regulations to the letter while others do not; are you saying that as well?

Mr Hudson: There have not so far been many prosecutions that I am aware of involving solicitors but certainly our assumption is that the strict application we have adopted will follow all the way through to the courts.

Chairman: I am sorry, I know I have a number of people who want to come in but we are going to go on halfway through the afternoon at this rate. I had proposed that at the end of each of the three sections to ask the two who were not concerned in those sections if they wish to add anything, but I would say to the bankers and the chartered accountants if you have any further comments you would like to make with regard to what Mr Hudson has been saying, perhaps you would let us have that in a paper. I want now to move across to the chartered accountants. Lady Garden.

Q24 Baroness Garden of Frognal: Thank you, my Lord Chairman. I wonder if I could ask you about your relationship with SOCA. You are actively involved in various activities with SOCA but could you elaborate on the nature and the value of that engagement and perhaps particularly say how you think SOCA might further improve the effectiveness of the discussions, the processes and the product and touch on the feedback that you may or may not be getting in adequate quantity from SOCA?

Ms Banks: My response actually would be very similar to my colleague Mr Hudson’s response for the Law Society. Our relationship is close and we are getting increasing feedback in the form of typologies. Many accountants would like more feedback on a case by case basis, but that is particularly problematic for a number of reasons including the fact that SARs feed into different processes, different law enforcement engagements. Many SARs can contribute to a single criminal investigation and some SARs are used more for civil proceedings than criminal proceedings—reports of tax evasion being a particular example of that. While we want to see continuous improvement, therefore, 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.

Q25 Baroness Garden of Frognal: Do you have regular meetings with SOCA? Are they on a set basis or just as when?

Ms Banks: We have regular meetings through the Anti-Money Laundering Regulatory Forum and numerous informal meetings. We have representation on the SARs Review Committee which also meets regularly.

Lord Hannay of Chiswick: Could I just follow up a little bit on this from the earlier discussion; if I understand it rightly all three of you would like to see better information and feedback from SOCA on the various criminal issues which might be crossing your desks, and that divides into two sections—one which is specific to each individual case and the other is as it were generic. Presumably that means better information about the sort of things that people who are dealing with nuclear proliferation materials need to look out for and so on. How would you evaluate those two things in real value to you? Is what you really need more generic training, or are you looking for feedback specific to each case, which seems to be pretty sensitive?

Chairman: Before you answer that the question which Lord Hannay has put is one which Lord Avebury very largely was going to put in a few moments, so before you answer that I would like to ask Lord Avebury if he would like to add to what

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Lord Hannay has asked so that we get a complete answer.

Q26 Lord Avebury: Could I refer to the answer you gave earlier that there were 6,460 SARs in a particular year 2007. Could you tell us how many of those cases did result in criminal prosecutions and whether you felt that in the cases where they did not there was sufficient individual feedback to enable those who submitted them to evaluate the merits of the process? Do you think that in cases where there are no criminal prosecutions there should be more general feedback on the principles behind the submission of the SARs?

Ms Banks: I cannot answer on how many of the SARs made by our members resulted in criminal prosecutions partly because of the lack of the one-to-one relationship between SARs and criminal prosecutions. For example, we have been told by SOCA that in one particular really serious criminal investigation a contribution was made by the information contained in 5,000 SARs. It would be very difficult to give feedback to every one of the originators of those SARs. Also, as I said, a lot of the information goes through into civil investigations and into the disruption of future crime. It is probably better if you get evidence from SOCA in this area but certainly in the accounting profession we believe 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.

Q27 Lord Avebury: If I could ask a quick supplementary, looking at it the other way round if you took the prosecutions for money laundering or for terrorist offences and you said in each case were there any SARs that contributed to this prosecution, then you would have some measure of the effectiveness of the SARs process, would you not, so that in the year where these 6,000 SARs were submitted have you looked at the number of prosecutions for, if you like, SARs-related offences in money laundering and terrorism to see in what proportion of those cases where the prosecutions occurred there was a contribution from the SARs process?

Ms Banks: I would very much like to see that information, yes. It is not something that we can tell you because it is extremely important to our members that their SARs are kept confidential. We do not know which of our members made the 7,000 SARs and we would not expect to get that information because as I have said confidentiality is so important for the makers of SARs.

Q28 Lord Avebury: It would not actually breach confidentiality if the responses by SOCA or whoever it was were in a generalised form and did not particularise the individual SAR that contributed to those prosecutions.

Ms Banks: I agree that would be very valuable; I would like to see that.

Q29 Lord Hannay of Chiswick: Could I possibly have an answer to my question now because it was not in fact the question that Lord Avebury asked?

Ms Scutt: I am happy to answer that. There is a role for both types of feedback; we get very little and the banking industry does not know how many of their reports lead to prosecutions. The SOCA annual report does say how many from the consent regime may lead to prosecutions but we do not. I believe there is a role for both types of feedback for different purposes to make the system overall more effective. For instance, we believe that a bank recently has submitted a SAR on proliferation finance and we are led to believe that it was absolutely spot-on; the intelligence that was provided and the way in which it was provided was a perfect example. However, for the rest of the industry we can have no knowledge of what it was that was spotted, how it was spotted and whether or not information on that could actually help other banks find these very important transactions. In that sense, therefore, taking specific information and enabling it to be applied more generally is very important. For individual institutions when they are dedicating £36 million a year from one bank in order to try and fulfil their obligations in this regard it is very helpful to get specific feedback on their own, so it is a question of feedback to improve the system but also to raise the standard throughout the industry in terms of understanding what it is they are looking for and how to go about it, so I think you need both.

Q30 Lord Mawson: I am not an expert in banking and I am very naïve about banking but my reading of the recent credit crunch thing is that lots of these different parts of the system have ticked lots of boxes and when you look at it all the processes have been followed very fairly but all the sheep have run off the cliff together and landed us in difficulty. I wonder with regard to this whole area of money laundering

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and these various aspects of this complex jigsaw who is the person and what is their name and address who is actually worrying up here about all of these pieces and how they actually interrelate together. Is there such a person and do they have a name and address and what is it?

Ms Scutt: Within an individual bank there is a person who is nominated and they will be the chief money laundering reporting officer and it is their responsibility and they are responsible to the regulators and they must worry about it.

Q31 Lord Mawson: The bank is one piece of the jigsaw but what we are hearing is that there are these other pieces. I am just wondering out there who is the person who is watching the interrelationship between these pieces of the jigsaw and how it is worked into the big picture and worrying about it in a coordinated and continuous way. Who is worrying about that? Is there such a person?

Ms Scutt: I believe that responsibility is vested between the Treasury and the Home Office.

Q32 Lord Mawson: Is there a person? I am always interested who the person is?

Ms Scutt: It is the Treasury Minister who is responsible.

Q33 Lord Mawson: Who is the Treasury Minister?

Ms Scutt: I think it is Stephen Timms. Sorry, it is Home Office and Treasury together.

Chairman: We have those witnesses next week so we can pursue that.

Q34 Lord Marlesford: Can I just ask are your three bodies given a guidance book by SOCA as to how you are expected to comply? If you are, I do not know whether you all get the same book or whether you each get a different book but it would be helpful if we could have a copy of the book or the books and also see the forms that you are meant to fill in.

Mr Cook: If I could answer that, that is actually available on SOCA's website, detail about how to fill in a SAR and the SAR forms are available; so it is publicly available information.

Ms Banks: We have also separately, each of us, written authoritative guidance for our members on how to comply, which is better than having one because it is modified for the characteristics of our professions or trade.

Q35 Lord Marlesford: Can we have a copy of that?

Ms Banks: Yes.

Chairman: Lord Mawson, do you want to come back with this?

Q36 Lord Mawson: Yes. What has been the experience of the ICAEW in the Money Laundering Advisory Committee led by HM Treasury and the Home Office? To what extent has it proved to be an effective forum for the discussion of private sector concerns in the AML/CFT sphere?

Ms Banks: It is really quite effective, though on many occasions there seems to be relatively little talked about it. Nevertheless, the fact that it meets regularly means that if there are matters of concern they can be raised. Not only that, but it means that you meet and know the most important people, the most important stakeholders in this field who are law enforcement and government departments as well as your colleagues in the regulatory sector, which makes it far easier to raise things informally. I have a current example actually which may reflect on equivalence in that one of the firms we regulate for money laundering purposes has a client that was introduced from Switzerland, which has been known as an equivalent jurisdiction, but they are having trouble in being given the underlying identity of the client. We have raised this and it is going to be put on the agenda for the Money Laundering Advisory Committee—a very swift response to something that could be a difficult problem.

Chairman: I am going to have to apologise to our witnesses in that I have to go to a memorial service now and forgive me if I do that. Lord Richard has most kindly said that he will stand in as the Chairman of this meeting, so if we could have a very brief pause whilst I move out and he moves in. Thank you again for coming; we appreciate it.

**In the absence of the Chairman,
Lord Richard took the Chair**

Q37 Lord Hodgson of Astley Abbots: You will have gathered from the line we have been following that we are very interested in finding ways of reducing regulatory burden and I think you welcome the idea of the introduction of some risk based approach to compliance and regulation. Could you tell us how that is working, could you tell us something about where you hope it could take us to; is there a glorious sunny tomorrow we can arrive at? If so, how will we achieve it?

Ms Banks: The risk based approach is difficult in its application but it is worth working hard on because it enables the regime to be more cost effective. It is the application of the risk based approach which means that accountants taking on new clients are required to get good evidence of identity, say from South African or South American general traders, while they have less trouble in taking on as a client an old lady with neither a passport nor a driving licence. So I think it is absolutely essential to make the regime work well and in an acceptable way. We see it as having

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produced fewer burdens on low risk clients while probably increasing them in higher risk clients.

Q38 Lord Hodgson of Astley Abbots: For all three witnesses. When I have asked people out there about how can we do something to reduce the regulatory burden and to reduce the risk they say a carve out in the definitions of the Proceeds of Serious Crime Act sections 327 to 329 to get rid of things like health and safety requirements. Is this a practical proposition and, if so, could we achieve it?

Ms Banks: Our preference would be to keep an all criminal offences reporting regime. When I talk to money laundering reporting officers they tell me that it is actually easier just to report everything where a crime is there than to try and make a judgment as to whether or not the crime is serious or not.

Q39 Lord Hodgson of Astley Abbots: There needs to be a crime then?

Ms Banks: There has to be a crime. So a lot of things which initially people feared they might have to report are not now reported because, for example, a parking offence is a civil offence not a criminal offence.

Mr Hudson: It will be no surprise to say that we differ from the ICAEW and the example I quoted earlier on I think goes to the heart of it. It is the fact that we take all criminal activity as the initiator of a predicate offence, therefore for money laundering purposes and so on, and it seems to me that that is central to what we perceive to be part of the UK problem here.

Ms Scutt: I would agree that the risk based approach does not sit comfortably with the all-crimes approach of SOCA. However, we would argue as the banks that the risk based approach brings great efficiency in the system, as it were, in that it enables banks to dedicate their resources to those things which are of higher risk and, as Felicity suggested, those customers of lower risk cannot be burdened with undue due diligence and such like. So there is benefit. There is a risk to the risk based approach itself in that it does mean that banks have to make judgments, people have to take responsibility and in the sort of environment in which we are now, if we take US sanctions, actually many banks would like to see a more prescriptive rules based approach with sanctions because of the extra territorial reach of US law and for which they are forced to make a judgment between do they comply with US law or do they comply with EU law, and that is a very uncomfortable decision to have to make and we have made those points on a number of occasions but unfortunately it is not easily resolved.

Q40 Lord Dear: This may be a terribly naïve question and you are at perfect liberty to tell me if I am naïve, if that is indeed the case. We are talking

about reporting very large volumes of instances where there has been some sort of criminal offence. It seems to me that if I were laundering money I would do my best not to commit the offence at all and to get on to the tick box, but that if I raised a doubt of there is some more to this than meets the eye sort of approach, in one of your three organisations, then that is exactly the sort of thing that ought to be reported. That is a very loose way of putting it, and I as I understand that; but my fear is not dissimilar to Lord Mawson's in that if all the boxes are ticked *de facto* we are all right, yet we are not all right because something has gone badly wrong. Is there a mechanism or maybe should there be a mechanism whereby you can report, notwithstanding the fact that there has not been the tripwire of an offence?

Ms Scutt: No. I believe it is a suspicion-based regime, and Sir Stephen Lander in his discussions with us says there is a benefit of having that regime—you rely on the instincts; you have the framework of the law; you have the framework of the banks' own methodology for assessing risks, whether it is the type of customer or the product they are taking, or the country in which they are situated, and that it is the suspicion, it is the experience of the person concerned that triggers that.

Q41 Lord Dear: I understand that; we are at one on that. Are you telling me that you can report on that gut feeling, that suspicion?

Ms Scutt: Absolutely; you are required to, that is what the law requires.

Q42 Lord Dear: You can do that?

Mr Hudson: We have to.

Ms Scutt: We have to. The law requires that if you suspect you must report.

Ms Banks: Many of the reports of our members anyway will be based on the fact that clients are acting in a way which is inconsistent with usual business practice under the expectation of making a profit.

Q43 Lord Dear: You smell a rat and you report it?

Ms Banks: Yes.

Q44 Lord Faulkner of Worcester: My question has very been substantially answered but I will just ask a second part to it. Are you able to say how often the risk based approach has gone wrong in the banking sector, where you perhaps have allowed something to slip through and you have found that it has been a disastrous mistake?

Ms Scutt: I do not think you can know that. That is one of the concerns about the framework itself with the regulators. We are fortunate in that I believe we have farsighted regulators and authorities in respect

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of the approach to this regime, but you cannot know; it is only with the application of hindsight can you actually see, possibly, that a wrong judgment was made. It is very difficult to stand there and know that at the point that something is happening that actually there is something going wrong here. But the regime allows for the authorities to come in and do inspections and for banks constantly to reassess whether or not their risk based approach is correct and whether they should perhaps not take customers from a particular place; or, for instance, stop doing business in Iran because they must balance the risk to their business and their reputation overall as well as their relationship with their customer.

Q45 Lord Marlesford: It seems to me that what you have described is a British system which is very heavily gold plated compared to many of those in other EU countries, and we are concerned of course with the EU picture overall. Also, it seems to me, you have highlighted a pretty basic contradiction between making the use of the professional expertise of your members in thinking that something is worth reporting and the obligation to report things which are perfectly clearly not worth reporting, and if you are going to make your own efforts more cost effective and indeed swamping SOCA with rubbish it needs a pretty major change in attitude of the British Government as to how they interpret the EU directive. Would you agree?

Ms Scutt: I am not sure I would agree with that actually. Yes, we have implemented the Directives and you are correct that there are countries in Europe who simply have not implemented the second, let alone the third Directive. I think that we have to remember that the reputation of the UK and the City—we have a very substantial City, even today—and the reputation as an international centre rest upon us getting this framework right and doing what is necessary. The fact that other countries in Europe do not do it—two wrongs do not make a right and we have to get the balance right but actually we are doing much more, I think, in terms of maintaining our reputation and seeking out those crimes.

Ms Banks: I could not agree more with my colleague. SOCA is not swamped. Initially it was but it has made huge reforms to its systems and I would not be able to say that any of the reports made by our members are wasted. It is very difficult to divide out those reports that seem to be small in monetary amounts and where you do not know what the particular offence is; it is very difficult to say whether those actually provide a trigger for an extremely important investigation from those which are not.

Mr Hudson: My Lord, I find myself more in agreement with your point than my two very learned colleagues. I say so because I think we have disparity

of application across the Union. I entirely endorse the point that the BBA makes that having a well regulated market, well regulated City is very important for us. Where I depart from that point is that I am not sure how our reputation as a well regulated market is enhanced by a system where, I believe, we have many problems because the regulations bite at the wrong point. If it is biting at the wrong point it is not going to help our reputation. If I may, I will give you an example. I could be in my office today and Mr Smith, a senior employee of Acme Inc., can come and instruct me. I could do some personal work for Mr Smith. A month later the work is finished and I send him my bill; he pays that bill and he sends it to my cash office. My cashier cashes the cheque. The cash office does not notice that he has drawn that cheque on the company. The company then contacts me and say, “Mr Smith should not have done this; this is potentially fraud, potentially a criminal offence; can I have my money back?” I would not, as a solicitor, be able to give them their money back until I got a Consent Order from SOCA. I know you might say that that is a rather trivial example compared to the very weighty points of view that BBA have just been speaking of so eloquently, but I think it gives an example of our all encompassing approach, the problems that we have, that we are not enabling our people to do the right thing and exercise judgment—we all agree about the benefits of the risk based thing and we all agree about bankers, accountants, solicitor exercising responsibilities as professionals. But there are some systemic problems, the Law Society believes, with the system we have here, which is why, as I say, I find myself more in agreement with the noble Lord’s points than my colleagues.

Q46 Lord Avebury: Can I turn to the passage in the BBA evidence where it says that recognising the necessity to provide feedback on specific cases does not imply the need of a systematic case-by-case feedback, but you think that the volume of cases that do receive direct feedback is currently extremely low. I take it by that you mean disproportionately low, and that would be some merit in increasing the number of cases where there is feedback in individual cases. But the only suggestion you make there is that there is a debriefing session held for interested parties on the conclusion of some major investigations, and that is a process that might possibly be expanded. Could you tell us on how many occasions there have been these de-briefing sessions and whether you think that is one way in which people who are suggesting SARs would get a better indication of the value of their submissions? Then on the general feedback you say that the BBA has called on the FIU to involve the reporting sector more regularly in the development

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and drafting of information products. Have you made such a recommendation formally to the FIU and what sort of response have you had from them?
Ms Scutt: We have regular dialogue. We have a stakeholder manager, someone who looks after us and listens to our concerns and with whom we work quite closely; so we have formal quarterly meetings. We do also have meetings with some of the law enforcement, so the Met and the City of London Police and specifically the Terrorist Financing Units, so that they can talk generally about some of that feedback. We have given SOCA specific feedback on their typologies, on some of their written alerts which, to be honest, we have not found very helpful in that they are too general; they say that charities might be a source of financial crime and, yes, we know that already. But we have a conversation to try and improve those so that we can ensure that better information goes back and better information comes out to the industry. That is an ongoing structured conversation which we have.

Mr Cook: If I could just add, I think the feedback that we get from SOCA tends to confirm what the industry already knows; it does not tell us anything we do not know, which I think the industry is looking forward to have a better dialogue with SOCA. So tell us what we do not know and where we should be looking and do not tell us what we already know. I think it is a learning process that we are going through SOCA; we are educating them about how the banks work and how they submit sales and the processes they go through. We are also trying to understand how SOCA operates so that we can add value to their operations as well.

Q47 Lord Avebury: Have you had specific meetings with FIU to discuss the way in which they develop and draft the information on products to ensure, as you say, that these add value?

Mr Cook: Yes. SOCA operates a group called the Small Vetted Group, which are a number of representatives from the reporting sector who are vetted and meet with SOCA and other law enforcement officials to discuss how the regime is operating. Beyond that we use our own panels at the BBA and invite SOCA in to discuss specific concerns we have around particular alerts, issues or typology issues so that we can work through some of those issues and say, “What did you mean here? Where are you going with that? What would you like us to do? We cannot give you that information because it would expose us to legal risk.” So we have that dialogue quite regularly with them. What we are encouraging them to do is to come to us early in the process so that we can add value to their alert products or their information products so that they are actually of benefit to the end user rather than just

a very bland statement, as my colleague said, that charities are used for terrorist financing—we knew that.

Q48 Lord Mawson: Has the BBA been directly or indirectly involved in the private sector consultations engaged in by the FATF? If so, how would you characterise that experience? How does your experience of interaction with the FATF in this sphere compare with that enjoyed with the European Commission?

Ms Scutt: The BBA and also the International Banking Federation had a great deal of interaction with FATF. I personally spend a lot of my time dealing with all the international standard setters because I believe they have a very important role. FATF was one of the first to actually take up the challenge by the private sector to talk about things that both sides could learn about the global framework in individual country implementation of this. I specifically chaired one of their first meetings on the risk based approach and with the help of Philip Robinson of the Financial Services Authority I think we achieved a very dramatic change in terms of many of those countries attending and their attitude towards a rule based regime or the risk based approach. So I think that the experience we have with FATF is very positive indeed. I am about to host a further meeting with them around the area of equivalence in terms of how we do more about that and it works very well because it gets the message across not only to those within our industry from various countries around the world, but it also puts the message across to other finance ministries or regulators who happen to be at the table who do not necessarily have the same approach. The importance of these supranational bodies is that we manage to raise the standards overall because banking is a global industry, even today, and we need to ensure that all points within the system have an approach and a framework that actually gets at the weak points and FATF, I think, provides a very valuable role in the sense of bringing people to the table and putting them through that experience and understanding ways of improving and going about it.

Q49 Lord Hannay of Chiswick: Could I go off the script a bit and ask whether any of your three organisations have had to grapple with—and, if so, how you grapple with—the hawala system?

Ms Scutt: We are often asked and of course that is one of the things that we talk about in terms of if you get the balance wrong in the system all that you will do is drive money to these other informal money exchanging systems. So I cannot speak for hawala systems because clearly money perhaps would move out of the banking system and into these and I would

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reiterate my point about getting the balance right. These informal systems work, exist and they work for some people, but we do not need to have a system which drives more from the mainstream into these informal systems where it is much more difficult to gain intelligence and to understand what is going through.

Mr Hudson: We would share very much many of the comments from the lawyers' perspective. It is the linkage of the transaction with the passing over of the finances and if the money was passing in that sort of way the disconnect would clearly be a problem and the solicitor would have I think a rather complex process to resolve and I would find that it would probably be the case that they would be in grave difficulty if the money were not passing through a more formal, transparent system. I cannot help you, my Lord, as to the incidence of those sorts of problems—I suspect it is low so far.

Ms Banks: Some of our members undoubtedly advise Asian grocery shops and will both be able to advise such shops if they do provide informal banking services on the need to register with HMRC as a money service business. They also have their own responsibilities if they see what they suspect is money laundering going through their clients of making their own report.

Q50 Lord Hannay of Chiswick: Am I right in thinking that the answers from the bankers and the lawyers is a bit different to the answer of the accountants because hawala transactions do not escape the accounting system.

Ms Banks: Many of them will escape the accounting system, of course, because since the audit exemption limit was raised so high most commercial organisations in the United Kingdom are not required to have an auditor and therefore are not required to have a relationship with an accountant, and of course the unincorporated businesses have never been required to have a professional accountant.

Q51 Lord Mawson: A very experienced politician once said to me that government understands the shape of the forest but it has no idea what is going on under the trees and it seems to me that one of the difficulties in the present situation, as government gets more and more involved in banks and all of this stuff, is that bureaucracies talk to bureaucracies and this whole little world begins to emerge. But a lot of this stuff has to do with what is going on down here in lots of little places—certainly where I come from, the East End of London actually—and I just wonder how we make sure that as all this stuff is going on this detail is properly engaged with and understood

because in a modern enterprise culture this is where it is really happening and not here. There is a gap.

Ms Scutt: I think from the banking industry point of view in terms for the banks themselves the industry writes guidance in order that they can understand how they should approach these things on a day to day level and how they work. I think guidance is very important in terms of how your average bank employee understands their responsibilities and can act accordingly, so I think industry guidance is a very important part of that. I think also banks are using not only individuals looking at transactions but they are using things like electronic monitoring and such like and I think that is the effective way of looking at those billions of transactions that go through in the course of a year. So I think that attention to detail is very important and it is doing that combined with the risk based approach and actually providing training, and training is a very important thing to make sure that those involved in the system actually understand the risks that are involved and what they are looking for, and I think that is the important thing so that people like me talk to the Treasury and the Home Office about the strategic approach; and organisations like ours work with the regulators in order to talk about how they should go about regulation and enforcement, but it is what the industry and bodies like ours do in terms of training and guidance and such like, which actually establishes the standard and makes sure that all that detail that is going on is properly dealt with.

Q52 Lord Avebury: Britain is now the largest centre of Islamic banking in the world. Are the Islamic banks based here members of the BBA and are they fully engaged in the discussions on these processes?

Ms Scutt: Yes. Yes, they are members of the BBA and also they participate in all the information we provide and the guidance we provide in this respect.

Q53 Lord Richard: Thank you very much indeed. Could I say how grateful we are to see you again this morning? With the combination of the accountants, solicitors and the bankers we are bound to be better informed and more able to deal with the problem we have. Having given you the compliment, may I say one other thing, which is that I think it certainly struck me—and it may have struck one or two others—that your comments on the regulation service are in general fairly clear in the sense that you do not like bits of it, but we are not absolutely certain what bits of it you do not like. So what would be very helpful is if your three organisations could perhaps submit another evidence paper—it need not be a very long one—just specifying specifically what it is that

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you want to see changed and how you want to see it changed. I think that might be helpful.

Ms Banks: My Lord Chairman, I think I have been remiss in that I should have declared another interest in that I am a Trustee Director of the Fraud Advisory

Panel, which also submitted written evidence to you. I had very little involvement in the preparation of their evidence but I did read through it before it was submitted.

Lord Richard: Thank you very much indeed; and thank you very much indeed for coming.

**Supplementary memorandum by The Institute of Chartered Accountants
in England and Wales (ICAEW)**

Guidance available to the Accountancy Sector

1. Comprehensive, formal, guidance was published for the accountancy sector in December 2007, prior to the coming into force of the Money Laundering Regulations 2007. This was reissued in August 2008 with minor changes, having been granted Treasury approval. Under the Money Laundering Regulations 2007 and the Proceeds of Crime Act 2002, this gives the Guidance formal legal recognition which will result in it being taken into account by the Courts in determining whether our members and other accountancy service providers have complied with certain of their obligations under the law. We attach a copy of our formal Guidance to this evidence.
2. The formal Guidance is also available from our web site at www.icaew.com/moneylaundering, together with other less formal guidance, the background to the legislation, and ICAEW representations in relation to the requirements.
3. Sections 6 and 7 of the formal Guidance covers the suspicion reporting requirements. We have not included copies of standard suspicion reporting forms with the Guidance, since these are designed and issued by SOCA in a form which makes them compatible with their recording system. The forms are available from SOCA's web site, together with guidance on completing them, at <https://www.ukciu.gov.uk/g0yssc45v4icbe55m10janej/saronline.aspx>. We have a Money Laundering Helpline available to our members, should they wish for assistance in filling out the forms.

The Consent Regime

4. The Home Office carried out an extensive consultation on the consent regime, in December 2007. We attach a copy of our response to this consultation [*not printed*]. Further copies are available from our web site at http://www.icaew.com/index.cfm/route/164127/icaew_ga/Technical_and_Business_Topics/Topics/Law_and_regulation/Obligations_to_report_money_laundering_The_constent_regime_Law_and_Regulation_ICAEW/pdf
5. We sympathise with the problems that many banks have with complying with the current consent regime, especially in combination with the prohibition on "tipping off" which means that they are unable to explain to their customers the reason for the delay in carrying out instructions. An amendment to the legislation to allow Pre-Event Notification ("PEN") of a transaction which might otherwise be within the definition of money laundering could assist them in carrying out their normal business without breaking, or undermining, the anti-money laundering legislation. However, it is important that any changes do not either undermine the usefulness to Law Enforcement of the consent regime, nor prejudice the position of either:
 - those who wish to seek consent as a legitimate means of obtaining a defence to accusations of money laundering; and
 - those engaged in legitimate commercial transactions where the conduct of another party has introduced the need to consider seeking consent, eg in a corporate finance transaction where the target and/or its owners are suspected of having benefitted from criminal behaviour and the related proceeds. Without the certainty of consent, parties may be extremely reluctant to continue to invest their own resources and those of their professional advisers in a transaction whose final consummation may be influenced by other than normal commercial considerations. The PEN system must necessarily be accompanied by the possibility that implied permission to transact may

subsequently be withdrawn, for law enforcement purposes. This is likely to adversely impact the reputation and utility of the City of London as a corporate finance centre of excellence.

6. SOCA have considerably improved the speed with which consent to carry out a transaction can be provided and their flexibility in providing consent to carry out a series of related transactions (which can be necessary, for example, in carrying on business in a company which includes in its funds some which are tainted with criminality). On the whole, we believe that accountants working in practice find the current regime broadly and usually workable in practice, and justified in the public interest in effective law enforcement. It is important to avoid any reform which risks upsetting this balance, and improves the operation of the consent regime in some sectors, while worsening it in others.

Beneficial Ownership

7. We consider it an important element of the current AML regime in the UK that entities within the regulated sector (including both lawyers and accountants) should know the identity of the beneficial owners of their clients when carrying out any business within the scope of the Money Laundering Regulations. Further, this is an irreducible requirement of the international Anti-Money Laundering obligations issued by the Financial Action Task Force and hence a treaty obligation of the UK. Without this information, entities' staff and Money Laundering Reporting Officers would be seriously handicapped in forming money laundering suspicions, and would not be able to provide comprehensive and useful suspicions reports to SOCA backed by the necessary identification information. Further, compliance officers in professional firms are likely to need this information anyway, in order to consider reputational issues, avoid conflicts of interest and, in the case of auditors, to ensure no breach of strict independence requirements and to audit the disclosure of related party transactions.

8. We understand the difficulties that some firms have in resolving the concerns of clients over the security of their personal information, but believe that these concerns can almost always be resolved by careful examination of the issues involved and any legitimate concerns eg in relation to vulnerable parties, including minor children, by restricting the number of people who know the identities of the beneficial owners. Where there are exceptional needs for privacy, it may be possible to very severely restrict information to only senior compliance and risk personnel within a firm rather than, as would be normal, allowing the information to be held by client serving staff as well as compliance and risk. Clearly, nothing in any such arrangement can override the need and duty to disclose to SOCA and other authorised agencies in response to exercise of legal powers.

9. We do not think that it would be appropriate for the beneficial ownership of companies or trusts to be required to be filed on a register open to inspection by the whole of the regulated sector. We support the right to privacy in that it should not be compulsory to disclose sensitive information widely, whilst fully supporting the absolute need for such information to be made available to regulated persons when their services are required. We believe that the current system supplies an appropriate balance between the rights of the client and the needs of law enforcement where a suspicion report is made, providing as it does a measure of due diligence by the service provider when a client is first taken on, and thereafter on a continuing basis as necessary.

The Current Regime and its Cost Effectiveness

10. We would welcome consideration of any improvements in the current regime that reduced compliance costs without undermining its effectiveness. Any such improvements would be likely to be incremental, and should be introduced with care to avoid unanticipated damage to the value of the current regime to law enforcement, and hence to the reputation of the UK and the safety of its citizens. We are not convinced that any changes apart from minor ones would be useful to the regulated sector, and radical changes could effectively seriously damage the value of the current regime to law enforcement.

11. The costs of the regulated sector are increased every time there is a significant change to the regime, due to the cost of training to ensure that relevant staff have achieved an appropriate level of understanding—this is significantly more than is needed on a routine basis as a periodic reminder of continuing requirements. We would prefer a period of stability of the Anti-Money Laundering Regime, with improvements focussing on better use of suspicion reports and better feedback to the regulated sector. We believe that this would be greatly preferable to significant changes to the requirements on the regulated sector, even where these purport to decrease the requirements but which may further complicate the regime.

12. In particular, our members in practice tell us that they would find it more laborious in practice to have to make a judgement on the nature of the predicate offence which led to suspected money laundering (in order to judge whether or not it is serious) than it is to report all suspicions. Further, we understand that some very important criminal investigations have been triggered by suspicion reports of activities which at first sight appear relatively minor if not trivial. SOCA is in a better position to judge the usefulness of suspicion reports than members of the regulated sector.

13. We welcome any well conducted research into the costs and benefits of the regime. In evaluating research, however, it is important that the cost/benefit ratio takes into account not just the benefits in terms of criminal proceeds recovered, but also the cost savings in terms of more efficient criminal investigations, the improved reputation of the UK as a safe place to do business and the saving of the potential costs of crime which is averted as a result of better criminal intelligence. I attach a copy of the results of the academic research that we sponsored in conjunction with the City of London and which was published in June 2005 [*not printed*]. The conclusion of this research at the time was that the requirements in the UK are set at a broadly appropriate level—and significant improvements have been introduced since that time, both reducing the costs borne by the regulated sector and improving the use that is made of suspicion reports. Further copies of the research report are available from our web site at http://www.icaew.com/index.cfm/route/112460/icaew_ga/en/Technical_and_Business_Topics/Thought_leadership/Anti_money_laundering_requirements_costs_benefits_and_perceptions.

Supplementary memorandum by the Law Society of England and Wales

1. Summary

1.1. The Law Society (“The Society”) is the professional body for solicitors in England and Wales representing over 115,000 solicitors. The Society represents the interests of the profession to decision makers within Parliament, Government and the wider stakeholder community, and has an established public interest role in law reform.

1.2. The Society is committed to ensuring that anti-money laundering measures are clear, proportionate, effective and workable in practice. Through lobbying, the Society is campaigning for the achievement of a level playing-field across the EU and the rest of the world, in order to ensure that UK legal practitioners and businesses are not at a disadvantage in relation to non UK legal practitioners and businesses.

1.3. The Society thanks the committee for the opportunity to give oral evidence on 4 March 2009, and welcomes the opportunity to provide supplementary evidence relating to the UK’s anti-money laundering and counter terrorist financing regime.

1.4. The committee specifically requested access to:

- The Society’s advice to the profession on complying with its anti money laundering and counter terrorist financing obligations; and
- The Society’s submission to the Home Office on the consent regime.

1.5. The Law Society’s practice note is available at: <http://www.lawsociety.org.uk/productsandservices/practicenotes/aml.page>

1.6. The Law Society’s submission to the Home Office is available at: http://www.lawsociety.org.uk/documents/downloads/dynamic/lsresp_consentregime.pdf

1.7. The committee also asked for the Society’s views on how the anti-money laundering and counter terrorist financing regime could be improved to address the concerns we had raised in our initial written evidence and our oral evidence.

1.8. We see that there are two key areas of improvements which could be made, namely:

- Targeting the AML regime more effectively so that the regulated sector can focus their preventative activities on the criminal conduct which is the focus of the Government’s anti-money laundering and counter terrorist financing strategy; and
- Reducing the cost of client due diligence compliance on the regulated sector.

1.9. The Society has outlined in more detail below the specific changes to legislation and actions by government which we think would achieve these improvements.

1.10. The Society has also noticed with concern a number of suggestions in evidence before the committee that the problems with the legislation could be resolved through memorandums of understanding with law enforcement, prosecutorial discretion, Executive Government agreements, professional guidance and the like. We urge the committee to take care with respect to such suggestions. The rule of law provides that the Executive Government cannot contract out of the normal and legal consequences of the legislation which Parliament has enacted. Where there is a problem with the legislation, it is only legislative intervention which will rectify the situation.

TARGETING THE AML REGIME

2. *Review the focus of the definition of criminal property*

2.1. The Society appreciates that this is a complex and difficult area of law, where unintended consequences can easily arise. This is particularly evident in the difficulties faced by the Home Office in achieving consensus on the way forward with respect to the consent regime.

2.2. As the Society advised in our oral evidence there are a number of issues with respect to the definition of criminal property as it applies in the UK. This is partially due to a departure from the FATF recommendations and the EU directives and partially due to the nature of our domestic law.

2.3. The FATF 40 recommendations provide a number of options for countries to define criminal property, through the way they define a predicate offence.²

2.4. FATF encourages countries to apply their anti money laundering laws to all serious predicate offences. It defines serious predicate offences as:

- (a) all crimes; or
- (b) a list of crimes with a penalty of at least one year's imprisonment; or
- (c) or a list of crimes which at least covers the following:
 - participation in an organised criminal group and racketeering;
 - terrorism, including terrorist financing;
 - trafficking in human beings and migrant smuggling;
 - sexual exploitation, including sexual exploitation of children;
 - illicit trafficking in narcotic drugs and psychotropic substances;
 - illicit arms trafficking;
 - illicit trafficking in stolen and other goods;
 - corruption and bribery;
 - fraud;
 - counterfeiting currency;
 - counterfeiting and piracy of products;
 - environmental crime;
 - murder, grievous bodily injury;
 - kidnapping, illegal restraint and hostage-taking;
 - robbery or theft;
 - smuggling;
 - extortion;
 - forgery;
 - piracy; and
 - insider trading and market manipulation.

2.5. The UK has adopted the all crimes approach. As we advised in our oral evidence, this can create a stricter application of the law in the UK because of the very wide range of offences in the UK which are treated as criminal. In many parts of Europe many such offences are dealt with by way of administrative action and have administrative sanctions. This could mean that even in other European countries which adopt an all crimes approach, certain activities which are caught within the UK will not be caught in those countries.

² A predicate offence is the first criminal offence (ie theft) through which a person can receive criminal property, in order to then launder the criminal property.

2.6. Once one understands the definition of criminal conduct, the legislation goes on to define criminal property as: “*Property which is, or represents, a person’s benefit from criminal conduct, where the alleged offender knows or suspects that it is such*”.

2.7. Property is defined as: “*All property whether situated in the UK or abroad, including money, real and personal property, things in action, intangible property and an interest in land or a right in relation to any other property*”.

2.8. These definitions raise a number of other problems, which we outlined in our oral evidence, including issues of money laundering on the basis of monies saved, the need for repeated reports about old offences despite attempts to rectify past criminality and the need to obtain consent even where there is absolutely no intent to launder.

2.9. Consequently in practice you may have criminal property from a wide number of regulatory offences which, we do not believe, are intended to be within the key focus of the Government’s anti-money laundering and counter terrorist financing strategy, such as:

- 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.

2.10. There may also be anomalous results such as:

- The need to continually report old offences, such as the previous failure to pay the minimum wage, with respect to a business entity, despite efforts to rectify the criminal activity, because the assets of the business entity remain tainted by the criminal conduct of a previous owner; or
- The potential need to seek consent to return criminal property to the victim of the crime.

2.11. The Society notes the Crown Prosecution Service’s evidence before the committee that it would exercise its discretion not to prosecute in relation to such minor regulatory matters or in cases where the law is clearly producing such anomalies. While the Law Society is in favour of prosecutorial discretion generally, the rule of law requires that law, particularly criminal law, is made as clear and as certain as it can be. It is not desirable that solicitors, who are Officers of the Court, are encouraged to knowingly break the law on the basis that the Executive did not really intend the law to operate as it does and avoid prosecution because of the discretion of the prosecutor.

2.12. The Society would like to work with the Home Office to review ways of re-focusing the definition of money laundering and the money laundering offences to ensure that they target the anti-money laundering and counter terrorist financing regime so that it is more effective in disrupting serious and organised crime which is at the heart of the Government’s strategy in this area. We appreciate that this will be a detailed process which will require the involvement of a number of stakeholders.

3. *Expanding the adequate consideration defence*

3.1. Under section 329 of the Proceeds of Crime Act 2002, it is a defence for someone to acquire or possess criminal property if they provided adequate consideration for the property, unless they know or suspect that the goods or services they provided may help another to carry out criminal conduct.

3.2. This defence applies where professional advisors receive money for or on account of costs. The fees charged must be reasonable and the value of work must equate with the fees received.

3.3. Unfortunately this defence does not apply to sections 327 and 328 of the Proceeds of Crime Act 2002. Where a solicitor enters into a retainer and is receiving funds for costs which they suspect may be tainted, they will be:

- assisting a person to transfer criminal property in contravention of section 327 and
- Entering into an arrangement which enables a person to use their criminal property in contravention of section 328.

3.4. To ensure that the legislative intention of the defence of adequate consideration is fully implemented, the Society would like to see the defence also applied to sections 327 and 328. This defence does not provide an open gate for criminals to siphon off criminal funds to their professional advisors. Instead it helps to guarantee the fundamental human right of access to justice and a fair and just legal system for people suspected, accused or even convicted of criminal activities.

4. *Removal of criminal sanctions from the Regulations*

4.1. The Money Laundering Regulations 2007 (the Regulations) do not cover the offences of being involved with money laundering. They cover:

- obtaining correct identity information;
- turning away business if you cannot obtain correct identity information;
- setting up systems to enable you to comply with your obligations; and
- Training your staff.

4.2 Within the supervisory regime for compliance with the Regulations, there is the power to discipline, fine, and remove from practice or remove licences of, those who fail to comply with the Regulations. This is consistent with the approach in many other European countries.

4.3 We believe that by going further to criminalise a breach of the Regulations; the UK is undermining the proper application of the risk based approach. Instead of the regulated sector in the UK looking first at their client and the transaction to assess the risk of money laundering, they tend instead to look at the risk of going to jail if they get the process wrong. This has tended to result in over-compliance with the Regulations in practice.

4.4 Rather than being of benefit to the fight against money laundering, this over-compliance means that a considerable amount of time and resources are spent on the process eg obtaining detailed client identification material in situations which pose little or no risk of money laundering rather than focusing resources on the real risks. With finite resources able to be spent on compliance, particularly in increasingly difficult economic times, this misapplication of resources because of fear so that the risk-based approach is not properly applied is detrimental to the overall fight against money laundering.

4.5 The law enforcement agencies may take the view that these criminal sanctions exist only for the most serious of cases. However it is hard to imagine that a person in the regulated sector whose failings with respect to the regulations were so bad as to warrant criminal action would not also be able to be charged with a failure to report offence or even a principal money laundering offence. This added level of criminal sanction is neither warranted nor proportionate and is not beneficial to the effective operation of the Government's anti money laundering and counter-terrorist financing strategy.

5. *Reducing the cost of compliance with the regulations*

5.1. During oral evidence before the committee, it became apparent that small firms in the regulated sector are spending thousands of pounds a year to comply with client due diligence, training and monitoring obligations. Larger firms are spending millions of pounds, while some of the banks are spending tens of millions of pounds in compliance.

5.2. Some of our firms have advised us that opening a new international corporate client matter can cost in the vicinity of £5,000 due to the lost time of fee earners or compliance staff in undertaking all of the checks required and the direct costs associated with obtaining documents or e-information to verify the information they have received. These costs are not directly passed on to the client and present a challenge to such firms as to whether they take on clients who may cost more to verify than the value of the retainer. Smaller firms are also concerned about the costs of client take-on.

5.3. The Society is concerned that much of the client due diligence information required under the Regulations is difficult, if not impossible, to obtain, costly and the requirements to obtain such information are not necessarily targeted at the right point or person to help detect possible money laundering.

5.4. The Society would like to see the UK government and other governments around the world, work together to increase the availability of client due diligence information to the regulated sector in an affordable way.

6. *Obtaining beneficial ownership information*

6.1. Obtaining information on beneficial owners, particularly in complex structures can be extremely difficult. There are a number of jurisdictions where secrecy of beneficial ownership is protected by law or where the only information you will get is directly from your client.

6.2. The Regulations also require that beneficial owners are identified wherever they exist, and the risk based approach only applies to whether you verify them. This means that even in low risk transactions, you are still required to go through quite detailed beneficial ownership searches. Where the only information available is

from the client, you are in effect verifying the information as best as possible, simply by obtaining it. Therefore the risk based approach, as it currently stands, provides limited benefit in reducing the compliance burden.

6.3. The Society would like to see the Regulations amended so that beneficial owners only have to be identified on a risk based approach. This was one of our recommended amendments to the Third European Directive on Money Laundering, which was accepted during the committee stages but was abandoned during the Council of Ministers negotiations.

6.4. Also, the Society would ideally like to see all FATF countries prevent entities with obscure beneficial ownership structures from being established in their jurisdiction. However, as an interim measure, we think it would be of assistance if all FATF countries require entities formed within their jurisdiction to register beneficial ownership information on a register. We would like to see that information made available to the regulated sector either free of charge or at a minimal cost.

6.5. The Society would like to see the UK government take a lead in negotiations with other jurisdictions to facilitate the creation of such a register.

7. *Equivalence*

7.1. The Society outlined in paragraphs 8.2 and 8.3 of its initial written evidence to this committee how equivalence is meant to reduce the burdens of compliance and how in practice this is not working.

7.2. The Society is of the view that the equivalence provisions would be more effective if:

- (a) There were an agreed list of equivalent jurisdictions and regulated markets at an EU or FATF level.
- (b) The Money Laundering Regulations 2007 were amended so that reliance on the government issued list was deemed to be compliance with the Regulations for the purposes of the legal question of equivalence.
- (c) The Money Laundering Regulations 2007 were amended to remove the extra requirements with respect to assessing equivalent markets.

8. *Politically Exposed Persons and Sanctions*

8.1. Firms are spending large sums of money on commercial providers to help them assess whether a client is:

- (a) a politically exposed person (PEP), on whom they have to do enhanced client due diligence; or
- (b) On a sanctions lists, therefore requiring them not to do business with that client.

8.2. The definition of a PEP is very wide. It includes all persons who within the last year held one of the following positions with a Community Institution, International Body or a state (other than the UK):

- (a) heads of state, heads of government, ministers and deputy or assistant ministers;
- (b) members of parliament;
- (c) members of supreme courts, or constitutional courts or of other high level judicial bodies whose decisions are not generally subject to further appeal;
- (d) members of courts of auditors or of the boards of central banks;
- (e) ambassadors, charges d'affairs and high-ranking officers in the armed forces; and
- (f) members of the administrative, management or supervisory bodies of state-owned enterprises.

8.3. The definition also includes immediate family members of a PEP and their known close associates. For known close associates, it is sufficient that a regulated person only have regard to information in their possession or which is publicly known.

8.4. Where a solicitor is acting for a PEP, it is a criminal offence not to:

- (a) have senior management approval to commence the business relationship,
- (b) take adequate measures to establish source of wealth and source of funds, and
- (c) Conduct enhanced ongoing monitoring of the transaction.

8.5. In terms of the sanctions list, it is a criminal offence to deal with financial resources of a person on the sanctions list. There are currently approximately 7,000 persons on HM Treasury's consolidated sanctions list. The list is available in HTML or PDF and runs to some 135 pages the way in which it is formatted means that it is not possible to search it electronically. The numbers of clients that firms take on daily makes it time consuming to search the list manually.

8.6. With so many people covered by the above definitions and the risks to a firm for dealing with either a PEP or a person on a sanctions lists being so high, it is understandable that many are seeking the assistance of commercial providers to create and search lists for them. However the costs for these services are high.

8.7. Within the solicitor's profession, approximately 87% of our member firms are small, with four partners or less. They do not have a person who can dedicate their full time to anti-money laundering compliance. Nor can they afford the £1,000 a year fee that is a general starting rate for access to these types of commercial providers. However, the Society is receiving increasing information that PEPs are starting to target smaller legal firms in the hope that they will go undetected.

8.8. The Society has long argued that governments are best placed to know who their own PEPs are and it is unfair to impose a requirement on the private sector to conduct enhanced due diligence on those people without providing a public list of who they are.

8.9. The Society would like to see:

- (a) EU and FATF country governments provide free and easily searchable lists of their own PEPs for use by the regulated sector.
- (b) The UK government make its sanctions list more easily searchable.

9. *Conclusion*

9.1. The Society is happy to provide any further information to the committee as required.

9.2. We look forward to continuing to work with the UK government and other relevant bodies to ensure that the UK has an anti-money laundering and counter terrorist financing regime which is clear, effective, workable and proportionate and addresses the real risks.

The Law Society of England and Wales

March 2009

WEDNESDAY 11 MARCH 2009

Present	Avebury, L Dear, L Garden of Frogal, B Hannay of Chiswick, L Harrison, L Henig, B	Hodgson of Astley Abbots Jopling, L (Chairman) Marlesford, L Mawson, L Richard, L
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Memorandum by HM Treasury

1. This memorandum sets out the UK's involvement in Anti-Money Laundering/Counter Terrorist Financing (AML/CTF) activities internationally including through the EU and globally through the Financial Action Task Force (FATF) and our responses to the Committee's questions.

2. The UK Government's over-riding goal in this area, as set out in the 2007 paper "*The Financial Challenge to Crime and Terrorism*"¹ is to protect its citizens and reduce the harm caused by crime and terrorism. Whilst finance is the lifeblood of criminal and terrorist networks, it is also one of their greatest vulnerabilities. The Government's objectives in using financial measures are to:
 - deter crime and terrorism in the first place—by increasing the risk and lowering the reward faced by perpetrators;
 - detect and investigate criminal or terrorist abuse of the financial system; and
 - disrupt criminal and terrorist activity—to save lives and hold the guilty to account.

3. In order to deliver these objectives successfully, action in this area must be underpinned by the three key organising principles that were first set out in the 2004 Anti-Money Laundering Strategy:
 - effectiveness—making maximum impact on the criminal and terrorist threat;
 - proportionality—so that the benefits of intervention are justified and that they outweigh the costs; and
 - engagement—so that all stakeholders in government and the private sector, at home and abroad, work collaboratively in partnership.

4. The UK has a robust regime for countering money-laundering and terrorist financing. This includes solid legal foundations that outlaw the financing of terrorism and money laundering; financial safeguards applied by industry—backed-up by law; supervision and guidance to ensure compliance of firms with the legal and regulatory requirements; measures to maximise the investigative and intelligence value of the financial information generated by criminals and terrorists as they move through the financial system; a range of instruments to disrupt the flow of criminal or terrorist assets and hold those responsible to account. A wide range of organisations are involved in this work, including regulators and supervisors; law enforcement agencies including police forces, HM Revenue & Customs (HMRC) and the Serious Organised Crime Agency (SOCA); and the security and intelligence agencies.

5. The threat from money laundering and terrorist financing is international and the UK places a high value on international cooperation in this area. Much of our effort is focussed on the establishment and enforcement of internationally agreed standards to ensure adequate safeguards against money-laundering and terrorist financing in all countries, with assistance to enable low-capacity countries to achieve these standards. The Financial Action Taskforce (FATF) is the main international body responsible for anti money laundering and countering terrorist finance. In 2006 the FATF conducted a Mutual Evaluation of the UK regime. The UK achieved a rating of Fully Compliant in 24 out of the FATF's 40 + 9 recommendations, and was judged Largely Compliant in a further 12 ratings. This places the UK as one of the highest-graded countries assessed to date.

¹ http://www.hm-treasury.gov.uk/d/financialchallenge_crime_280207.pdf

COOPERATION WITH AND BETWEEN FINANCIAL INTELLIGENCE UNITS (FIUS)

6. The principal mechanism for dealing with flows of financial intelligence is the Egmont Group, the international coordinating body of 106 FIUs, in accordance with the Egmont Statement of Principles of Information Exchange Best Practice and using the Egmont Secure Web.

7. In 2008 the UK initiated 501 requests to Egmont members and received 898 requests to the UK (within these figures 192 requests were sent to and 457 received from EU Member States). The resulting information flows have produced good results in assisting prosecutions and identifying assets for confiscation. For example in 2008 a restraint order for nearly \$50 million was achieved following the receipt of a Suspicious Activity Report (SAR) in the UK and liaison with two overseas FIUs. Work is in hand within the Egmont Group to review the utility and practical outcomes of these exchanges. The UK engages bilaterally with non-Egmont member countries, subject to risk assessment and assurance that the information will be used appropriately and in line with the Egmont principles.

8. SOCA has a network of SOCA Liaison Officers (SLOs), including five Financial Liaison Officers, who engage with host countries' FIU and law enforcement agencies (LEAs) to extract and develop financial intelligence. As representatives of the UKFIU they are able to engage both with the hosts' FIU and their operational money laundering LEA teams and to draw upon a wide range of operational and intelligence material on criminal finance that is harming to the UK. HMRC also deploy a network of Fiscal Crime Liaison Officers (FCLOs) overseas. They are trained in financial matters and engage with partner agencies and FIUs in-line with HMRC responsibilities. They also work closely with SOCA colleagues and sometimes benefit from MOUs between SOCA FIUs and third country FIUs.

9. Within the EU, FIUnet, an IT system linking most Member States' FIUs facilitates cooperation by allowing them to make enquiries and exchange certain information. The UK is also a key contributor to the EU FIU Platform, a forum of Heads of FIUs initiated by the European Commission, which identifies and promulgates learning and best practice amongst EU FIUs.

10. Europol collates money laundering intelligence that EU Member States contribute and adds value to this. It undertakes this through a series of projects, referred to as Analytical Workfiles (AWFs). At present the UKFIU is contributing to a project known as "Sustrans", set up to analyse data submitted in the EU in Suspicious Activity Reports and Suspicious Transaction Reports relating to cross-border money laundering activity. In addition through the Metropolitan Police Service counter-terrorist liaison officer, based within the UK Liaison Bureau at Europol, UK agencies responsible for counter-terrorism matters engage with the Europol AWFs relating to terrorism. The exchange of intelligence with Europol also includes intelligence on terrorist financing. HMRC second an officer to the SOCA office within Europol to lead on HMRC-related activity and exploit intelligence within the AWFs. HMRC have also seconded an expert to help set up the AWF created to tackle EU-wide MTIC fraud (AWF MTIC), which regularly identifies intelligence cross-matches with AWF Sustrans.

11. The high performance of the UKFIU was recognised in the mutual evaluation by the Financial Action Task Force (FATF) in 2006 which reported that the UKFIU substantially met the criteria of FATF Recommendation 26 and appeared to be a generally effective FIU; it noted the private sector reported improved relations and co-operation since the transfer of the FIU responsibilities to SOCA in March 2006. With regard to compliance with FATF regulations on international co-operation (including Egmont), the UKFIU received the highest possible rating—"fully compliant".

EU INTERNAL ARCHITECTURE

12. The EU has an important role in both the UK's AML/CFT regime and in meeting our international objectives. Many key regulations in this area are established at EU-level, including through the Third Money Laundering Directive, which is the basis for the UK's 2007 Money-Laundering Regulations. In addition to its regulatory role, the EU acts to facilitate cooperative approaches by member states in several related areas.

13. In practice, there are a number of different bodies in the EU which have responsibilities for issues related to money-laundering and terrorist financing. The principal forum for policy and technical discussion is the *Committee on the Prevention of Money Laundering and Terrorist Financing*. This committee, chaired by the European Commission and based within the Directorate-General for the Internal Market, is the central coordinating regulatory and policy mechanism for EU Member States concerning AML/CTF. It has been in existence since 2006, and was formed to assist with transposition and implementation of the Third Money Laundering Directive, including monitoring the domestic implementation of the directive. Since then its role has developed to stimulate debate among industry bodies and member states on financial crime themes; to share information and best practice, and where possible to promote a common approach; to coordinate an

EU position on FATF issues which it will represent at FATF meetings (the European Commission is an independent member of FATF); and to review for consistency other relevant EU legislation such as the Wire Transfer Regulations, Payment Services Directive; E-Money Directive.

14. There are a number of coordination and expert groups focused on regulatory issues on which the FSA represents the UK. The principal group in this area being the *EU Regulators' Anti-Money Laundering Task Force*. The aim of this Task Force is to provide a supervisory contribution to anti-money laundering and terrorist financing issues, in particular to foster the convergence of supervisory practices and to facilitate the exchange of information and good practice relating to the implementation of the Third EU Money Laundering Directive.

15. Terrorist Finance and Asset Freezing is also coordinated within the Council of Ministers through several Council formations and working parties, including

- *Financial Attachés* concerning the implementation of FATF Recommendations into EU-legislation;
- the *Council on External Relations* (RELEX) concerning the implementation of UN Security Council Resolutions and autonomous EU financial sanctions;
- *Working Party on Terrorism* for internal EU aspects;
- *Committee on Terrorism* (COTER) for external aspects (and EU TF Strategy);
- the *CP 931 Working Party* for the designation of organisations and individuals involved in terrorist acts; and the
- *Multidisciplinary Group on Organised Crime*, for law enforcement aspects of AML/CFT.

16. The EU's mechanisms for coordinating action against money-laundering and terrorist financing have produced important elements of regulation and made a valuable contribution to improving wider cooperation among member-states on AML/CFT issues. The Third Money Laundering Directive, agreed during the UK's 2005 Presidency of the EU, adapted and implemented the FATF's revised AML/CTF standards across the EU. The directive considerably boosted the consistency and standard of legislation across the EU, while at the same time allowing for minimum harmonisation and the existence of national variations. It also incorporated a risk-based approach to AML rules, which was strongly supported by the UK, significantly broadening the influence of this approach in the EU. The Third Money-Laundering Directive met the UK's objective of establishing a robust system without imposing unnecessary compliance costs and has allowed the UK to construct a very well respected AML regime. The EU cash control Regulation supplements the Third Money Laundering Directive by providing for a harmonised control system for cash entering or leaving the Community.

17. The EU continues to work to ensure that community legislation takes ML/TF risks into account, and covers emerging trends. Two current areas are the Payment Services Directive which will extend the regulation of money laundering to new business sectors, such as bill payment providers and mobile phone payments systems, to reflect their emerging importance as money transmission systems and guard against potential criminal exploitation; and the E-Money Directive where the EU is looking to review the AML provisions to ensure that they are not too prescriptive and will not inhibit growth in the industry.

INTERNATIONAL COOPERATION

18. 22 of the 27 EU member states have been assessed by the FATF, IMF or MONEYVAL (the evaluation and review mechanism for AML/CTF in Council of Europe member States which are not members of the FATF) against the current FATF standards. Overall, the reports show a high level of compliance with those Recommendations addressing international cooperation, with only 9% of the ratings across the range of requirements falling below what is judged to be an acceptable level, and only three countries falling short on more than one of the six key issues.

19. Following a recent fact-finding visit to the UK, an Executive Director of the UN Counter Terrorism Committee (UNCTED) acknowledged that the UK "has developed a comprehensive and coherent all-of-government counter-terrorism strategy" and that they had noted "many areas which we will be able to use as an example of best practice when advising other governments on how to improve their CT strategies and organization".

20. The UK is working with international partners to address due process concerns raised by the courts in the *Kadi* case and others, see Annex A for further details, and to work with the EU and UN to enhance implementation of international sanctions mechanisms and explore the implications of the case.

21. While the FATF Recommendations do not include tax offences as a predicate crime for money laundering as some jurisdictions are opposed to this approach, the UK has an “all crimes” approach and so is able to provide assistance in respect of money laundering offences based on predicate tax offences. HMRC may receive potentially tax-related information from anti-money laundering and other authorities either domestically or internationally. By virtue of the Commissioners for Revenue and Customs Act 2005, any information acquired by HMRC in connection with one of its functions may be used in connection with any other function. The extent to which such information is used for enforcing compliance with tax obligations is judged on a case-by-case basis having regard to a range of criteria including an assessment of the potential risk to the Exchequer.

MONITORING IMPLEMENTATION

22. The EU *Committee on the Prevention of Money Laundering and Terrorist Financing* has responsibility for monitoring member states’ transposition of the Third Money Laundering Directive into national regulations, using informal mechanisms and if necessary, formal infraction proceedings. The UK was one of the first Member States to fully transpose the Third Money-Laundering Directive, and did so within EU deadlines. However several member states have not yet fully transposed the Directive, and are now the subject of infraction proceedings. The success of these proceedings in ensuring the successful transposition of the Directive in the remaining member-states will be an important test for the effectiveness of the EU’s enforcement mechanisms, which has yet to be demonstrated in this area.

23. The UK views continued cooperation and engagement with the private sector as critical to the success of the anti-money laundering and counter terrorist financing regime. HM Treasury consulted extensively prior to the implementation of the third Money Laundering Directive through the Money Laundering Regulations 2007. It also set up a *Supervisors’ Forum* to bring together all organisations with responsibility for ensuring compliance with domestic and international AML/CTF standards, to ensure they perform at the level of the best.

24. In addition to considering the overall burden placed on the private sector by the AML/CFT regime, the Government maintains an ongoing dialogue with the private sector aimed at further improving the effectiveness, and reducing the burden, of the regime, including with private sector forums such as: The *Money Laundering Advisory Committee* (MLAC) which brings together representatives from Government, law enforcement, trade bodies and industry, regulators, and consumers to ensure that the UK’s anti-money laundering regime is fair, efficient and effective, proportionate to the risks involved, and provides a forum for discussing the views of all relevant stakeholders; and the *Joint Money Laundering Steering Group* (JMLSG), which is an example of an sector wide body which issues detailed and practical guidance on interpreting and implementing the money laundering regulations and terrorist financing requirements. The EU also holds regular consultations with the private sector through dedicated organisations such as *Anti-Money Laundering Europe*.

25. On Terrorist Finance issues, the *Terrorist Finance Working Group* (TFWG) was established to look at the system for countering terrorist financing and make recommendations to ministers on how it might be improved. The FSA’s *Financial Crime Intelligence Group* looks to facilitate sharing knowledge and intelligence between public and private sectors on financial crime matters including terrorist finance.

26. There is extensive bilateral engagement with the private sector across the SARs regime. Following Sir Stephen Lander’s review and the creation of SOCA in April 2006, a number of improvements to private sector cooperation and communications have been taken forward. These include: structured feedback to SARs reporters by the UKFIU to a vetted group of private sector representatives, including discussion of sensitive casework and reporting issues, and development of intelligence products for industry; the UKFIU working with the *Regulators Forum* to ensure that regulated firms have access to the information that they need to protect themselves from inadvertent involvement in money laundering and terrorist financing; the creation of the *SARs Regime Committee* to oversee the performance of regime participants and the discharge of their responsibilities. The work of these groups is supplemented by direct feedback to firms from security and law enforcement agencies, and by ad-hoc bulletins produced by the UKFIU for reporting entities, describing current terrorist financing techniques drawn from current counter-terrorist investigations.

27. During the UK’s recent presidency of the FATF (June 2007—June 2008) considerable progress was made on among other things advancing the organisation’s engagement with the private sector. A private sector consultative forum is now in operation within the FATF, which provides a formal structure within which the private sector can both be informed about the work of the FATF and contribute to the FATF work programme. This gives the private sector the opportunity to raise concerns about the cost of implementing AML measures.

COMPLIANCE AND EQUIVALENCE

28. The *Counter Terrorism Act 2008* has conferred on the Treasury new powers to act against jurisdictions of concern. These powers allow the UK, in respect to either a specific entity, a specific class of entity, or all entities in a jurisdiction, to:

- Require credit or financial institutions to undertake enhanced due diligence (to ensure knowledge of the source and ownership of funds) on transactions with specific jurisdictions;
- Require credit or financial institutions to undertake enhanced and ongoing monitoring of transactions with specific jurisdictions;
- Require credit or financial institutions to systematically report on all transactions with a specific jurisdiction;
- Require credit or financial institutions to limit or cease business with entities in specific jurisdictions.

The new powers mean the UK is now able to comply fully with FATF Recommendation 21 concerning the requirement to impose counter-measures against jurisdictions of concern.

29. Equivalence is a concept designed to inform risk assessments and indicate when Simplified Due Diligence and Reliance are appropriate as an aid to businesses. Equivalent status allows financial institutions to apply simplified due diligence to customers in that country, making business transactions quicker and potentially cheaper. Businesses may rely on another firm's customer identity checks from within that jurisdiction, rather than having to perform their own (although they remain liable for their customer checks). It does not exempt the firm from carrying out ongoing monitoring of the business relationship with the customer, nor from the need for such other procedures (such as monitoring) as may be necessary to enable a firm to fulfil its responsibilities in the UK under the *Proceeds of Crime Act 2002*.

30. Member states agreed to a list of equivalent countries in the *EU Committee on the Prevention of Money Laundering and Terrorist Financing* in May 2008. The equivalence list recognises all EU and EEA Member States as equivalent (because of their obligations to implement the EU's Third Money Laundering Directive). It also includes FATF member countries with a sufficiently good mutual evaluation assessment. Gibraltar is equivalent because it is obliged to implement the Third Money Laundering Directive by virtue of being considered a territory within the EU for the purposes of implementing Pillar 1 (Internal Markets) Directives. The equivalence list is not exhaustive, and nor is it binding on member-states. JMLSG guidance advises firms to carry out their own assessment of particular countries. The list will be reviewed periodically.

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Annex A

THE KADI CASE AND ECJ JUDGMENT

Mr Kadi and Al Barakaat challenged the legality of EU implementation of the UN assets freeze imposed upon them under UN Security Council Resolution 1267(1999) in the Community Courts. They were initially unsuccessful in the Court of First Instance but in its judgment dated 3 September 2008, in Joined Cases C-402/05 P and C-415/05 P *Kadi & Al Barakaat International Foundation v Council and Commission*, the ECJ found that the EC Regulation breached the fundamental rights of Kadi and Al Barakaat, in particular by failing to provide them with the reasons for their listing or giving them a chance to make their views known. The Court did not review the Security Council resolution but did review the implementing EC Regulation. The Court suspended its judgment for three months which allowed the Council and the Commission time to take action to correct the due process failings identified by the Court. The EU addressed these defects, by providing to Mr Kadi and Al Barakaat narrative summaries of reasons for their listing, giving them an opportunity for comment, and considering the basis for their listing. Following this process, a new EC Regulation was published on 2 December 2008, re-listing Mr Kadi and Al Barakaat. The assets freeze against Mr Kadi and Al Barakaat therefore remains in place at EU level.

The UK is working with international partners to address due process concerns raised by the courts in this case and others.

The UK has supported on an ongoing basis due process improvements to the existing UN Al Qaida and Taliban sanctions regime, inter alia, through Security Council resolution 1822, adopted in June 2008. UNSCR 1822 provides that the cases of all individuals and entities on the UN list should be reviewed by June 2010 and that narrative summaries of the reasons for listing should be provided for all persons named. The UN Sanctions Committee is working to provide listed individuals with summaries of reasons for listing as soon as

possible. UNSCR 1822 is an important step forward. The UK recognises the need to strengthen procedures to enhance the efficiency and transparency of the regime. We are continuing to work with EU and international partners to enhance implementation of international sanctions mechanisms and explore the implications of the case.

Examination of Witnesses

Witnesses: MR JAMES ROBERTSON, Head of Financial Crime Team, HM Treasury, MR STEPHEN WEBB, Acting Director of Policing Policy and Operations, Home Office, Ms GAYNOR ITHELL, Head of Proscription and Terrorist Financing, Office of Security and Counter Terrorism, Home Office, and MR CHRISTOPHER YVON, Deputy Head, International Organisations Department, Foreign and Commonwealth Office, examined.

Chairman: Good morning. We have a plethora of Whitehall talent before us this morning from three departments. Welcome. We are most grateful to you for coming and giving evidence. As you know, we are carrying out an inquiry on money laundering. I am going to ask you to introduce yourselves to begin with, but before that I think Lord Marlesford has some specific questions he would like to ask you in terms of your particular responsibilities.

Q54 Lord Marlesford: Thank you, Lord Chairman. I just think it would be helpful to us if each of you, in introducing yourselves, said briefly what you are there to do, how long your units have been in operation, the costs if you have them and what the total staff of those units is and, in the case of HM Treasury, the linkage with HMRC in particular.

Mr Robertson: I am James Robertson. I am the Head of the Financial Crime Team in the Treasury which is comprised of ten staff. I could not tell you the overall costs of that but it could be worked out and I can certainly submit that afterwards if it was required, but it is essentially the cost of basic staff salaries and associated expenses with that. The role of the team is across financial crime as a whole so that incorporates not only money laundering and terrorist financing but also issues relating to fraud, to corruption and to proliferation financing. In relation to money laundering and terrorist financing, the Treasury has, particularly for money laundering, responsibility for the oversight of the regime as a whole in terms of the money laundering regulations, for instance in terms of coordinating the various supervisory and regulatory bodies. Obviously there is a link to the Home Office and for most of the major groups and committees we will co-chair those with the Home Office, for instance the Money Laundering Advisory Committee. We are responsible in particular for the financial regulations and standards whether that is domestic or international; for the monitoring and oversight, ensuring consistent activity amongst the regulators, the supervisors and so on; similarly monitoring within the EU and internationally by the Financial Action Task Force and I am head of the UK delegation to the FATF. We are also responsible for corrective action on capacity building, to identify and fill in any gaps in the regime, and also then for the financial systems and infrastructure, so safeguarding

the integrity of the payment systems and financial infrastructure more broadly. In terms with links with HMRC, HMRC is a regulator and it has certain responsibilities under the money laundering regulations and so our relationship with them is pretty much as any other regulator in that extent. The fact that HMRC report to Treasury ministers does not make a material difference necessarily because they regulate their sector which, in relation to money laundering, is primarily money services businesses whereas the Financial Services Authority, for instance, regulates the bulk of the financial sector.

Ms Ithell: I am Gaynor Ithell. I lead the Terrorist Financing and Proscription Team. We have four people covering both areas. The Home Office have the overall lead for the UK counter terrorism strategy CONTEST and as such has a coordinating role bringing together departments to deliver part of the terrorist finance strategy. We work very closely with the Treasury with their lead with the financial sector. That is basically what we do. In terms of cost, I am afraid I do not have the costs of the team but we could always pass the details to you later on.

Mr Webb: I am Stephen Webb. I am the Acting Director of Policing Policy and Operations in the Home Office. It is a very disparate directorate and I will just focus on the bits that are of interest to you, one of the units within the directorate is the Organised and Financial Crime unit and within that there is a team that is responsible for the process of crime acts, so the criminal law, money laundering and asset recovery. That is a team of five so I guess that would be around £300,000 to £350,000. The Organised and Financial Crime unit is also the sponsor unit within the Home Office for the Serious Organised Crime Agency. Again there would be a couple of people working on that. The other area I am responsible for is the UK Central Authority within the judicial cooperation unit which will process mutual legal assistance requests including those in the financial area. The total size of the FIU is now 35 staff so the budget would be somewhat under £2 million. As I say, that is really all the requests for evidence of which the financial will only be a fairly small proportion. As James said, we work with the overall money laundering policy in the Treasury, the criminal law and the suspicious activity report regulation; the criminal sanctions for that

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resting in the Home Office it is very much a joint effort and we jointly share groups like MLAC. I hope that is helpful.

Mr Yvon: My name is Christopher Yvon. I am the Deputy Head of the International Organisations Department within the Foreign and Commonwealth Office. My department is 33 people strong. The direct relevance to this particular Committee's interest I think is where the department carries out sanctions work which is essentially maintaining sanctions regimes including one that is about asset freezing against terrorists. That is probably the direct interest for this Committee and there are five people in that team of people who work on sanctions and the unit has been in existence since 1998. We do UN sanctions as well as EU sanctions and the broader department does multilateral institutions.

Q55 Chairman: Thank you. There is a bit of scope for supplementary evidence, particularly on costs. Let me now begin with the first question. In June of last year the UK, Brazil and the Netherlands proposed a review of the standards of the Financial Action Task Force and of the mutual evaluation process. To what extent has the global financial crisis made the need for such a review more pressing? What is the current status of this initiative?

Mr Robertson: I think the financial crisis has certainly added a degree of impetus. The G20 in its report in November set out certain action points; some of those were directed towards the FATF in particular. Indeed we have recently had an FATF plenary meeting at the end of February in Paris and the financial crisis was one of the issues that was strongly debated in this context. Where that feeds into the proposal that the three presidencies made to review the standards, the idea behind that was to look at the FATF standards and review them with a view to being in a position to improve those standards where relevant before the commencement of a fourth round of mutual evaluations (the mechanism by which the FATF monitors compliance is to undertake mutual evaluations of countries). At the meeting in February in Paris ten initial issues were identified for further consideration. I would say that list of issues almost completely matched up with those that were highlighted in the initial Three Presidencies Paper. I would say that some of those issues in particular—for instance on international cooperation—have been given extra impetus by the financial crisis. Separately and in addition to that the Dutch, who are about to take over the presidency of the FATF from July, have proposed a specific piece of work to look at how the financial crisis has had an impact in relation to money laundering and terrorist financing: what we should take from that, what it might mean with the nature of the global financial system and what that should

mean for money laundering and terrorist financing controls.

Q56 Lord Hannay of Chiswick: If I could just raise one specific issue arising from your reply, there is one area which has seen very rapid growth in recent times of criminal activity and presumably of money laundering and that is the proceeds of piracy off the Horn of Africa, in particular off Somalia. Judging from press reporting very large sums of money have been transferred from, among others, insurers in the City and elsewhere to criminals in Somalia in order to obtain the release of crews and of ships. The FATF covers piracy as I understand it; it is part of its original remit. To what extent is work going on to ensure that these very large sums of money are traced and indeed pursued? Is there any consideration being given to forbidding the payment of such sums for the purposes of rewarding criminal activity?

Mr Robertson: I would say in broad terms that the FATF is a standard setting body so its role is to set the standards in relation to money laundering and to terrorist financing. In terms of the implementation of those and pursuit of individual cases, that would be for individual jurisdictions to take forward. The FATF itself would not engage in that sort of activity. What it would do, for instance, would be to consider whether there were particular ways in which pirates could launder their money or particular things that jurisdictions should look for in trying to spot money laundering that was related to piracy. At the present time there is nothing that I am aware of that is underway within the FATF on that particular issue. They are not in a position to drive forward any enforcement action.

Q57 Lord Hannay of Chiswick: I understand that, but, should there not be some consideration given to the specifics of this activity which seems to have grown pretty large so that all the jurisdictions are given guidelines on how best to deal with it? Is the normative activity of the FATF not relative here?

Mr Robertson: I think in relation to issues like an examination of the methods used and so on, that would certainly be an appropriate thing for FATF to do and if this is a growth sector, if you like, in relation to criminal proceeds and money laundering then it would be entirely appropriate for FATF to undertake that sort of work.

Mr Webb: There is quite a difference in treatment across jurisdictions internationally about the payment of ransoms. In some areas it is illegal and in other countries it is not. It is not currently an offence in the UK. Clearly once the money has got to the pirate that is extortion and the proceeds of crime and we would expect to see it traced if we can. There has been a lot of work. As you say, there has been an

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upsurge in the problem although that seems to have damped down since the heavy naval deployments in the area, but nonetheless it is clearly a problem. It is a very complex area, particularly as so many of the transactions happen outside the jurisdiction. I cannot say an awful lot more yet, but there is work going on to look at it.

Q58 Lord Mawson: In an area of work that I work in, which is not this, I watched government spend £450 million on processes and systems that have not actually built anything, and yet small enterprise projects have built many things at a tenth of the cost. I am just wondering what success looks like from these processes and systems—how effective they are—and whether there is any entrepreneurial input into the way you are approaching some of this because it seems to me that people who are involved in money laundering are thinking not in a processing system way but a very different sort of way and I wonder how much of that logic is involved in your thinking, particularly if you are going to review some of these things.

Mr Webb: That would be the wider issue of money laundering and the processes and systems that the financial sector has put in. The Serious Organised Crime Agency has put a lot of work into understanding the methodology with money laundering and obviously using its various covert sources to understand what motivates them and how the techniques change in response to the law enforcement activity we put in. As you said, it is a rapidly changing area and of course we have to keep track of that. I think there is a lot of that kind of work going on. On the wider issue of what success looks like, I think the easiest thing to measure is obviously the proceeds of crime that come in as a result partly of the suspicious activity reports being made and financial investigations. We are hoping this year to achieve a sum basically six times more than we were achieving seven years ago. The pipelines are quite long and there is even better stuff in the pipeline; we would expect performance to continue to increase over future years. I think dramatically better use has been made of the intelligence provided by the regulator sector. The Serious Organised Crime Agency does an annual report on the workings of the SARs system that looks at it in some detail and gives case studied of specifically how reports have made a difference.

Q59 Lord Marlesford: Under the EU money laundering directives does HMG require financial institutions in the UK to report to HMG any payments of ransoms made. If not, why not? Do you have the power to require this information? If you do not have them, do you think you should have them?

Mr Webb: This is quite a complex legal issue. I will give an answer now and hope I get it right. My understanding of this is that a ransom payment in itself is not illegal. The way the Proceeds of Crime Act regime works is that you are required to notify SOCA in the case of making a payment that is an act of money laundering and therefore something illegal. The initial payment would not necessarily be illegal and therefore not necessarily need to be reported. Much will depend on circumstances and once it gets to the criminal then it becomes criminal property because it is proceeds of extortion. It is quite a fine legal point and different people take a slightly different view on individual transactions.

Q60 Lord Marlesford: Perhaps we could have a supplementary on this in writing.

Mr Webb: Of course.

Q61 Lord Hannay of Chiswick: It does seem a pretty odd situation we are in in that the money is transformed at the moment it gets into the hands of the criminals into something that is proper for you to pursue but does not seem to fall within your bailiwick up to the moment it reaches the hand of the criminal. Perhaps you could clarify that.

Mr Webb: It bears on when the actual activity becomes illegal which bears on the overall regime of paying ransoms which, as I say, is quite complex and some countries treat it differently. I know in Italy, for example, the payment of ransoms has been illegal for a long time. There are different views on the effectiveness and the impact of that and how likely people are to report it. I think it would be well worth a proper written explanation.

Lord Avebury: Could the supplementary memorandum cover the point that was raised by Mr Robertson that any study of the methodologies used by the pirates to dispose of the criminally acquired money would be a matter for the FATF. We need to know whether the FATF has actually looked at the problem and whether they are developing a methodology for looking at the monies that are paid over to the pirates once they reach the banking system.

Chairman: We look forward to hearing from you on that. Lord Hannay?

Q62 Lord Hannay of Chiswick: In the United States it seems that consideration is now being given, in the context of the need to increase fraud enforcement in the wake of the economy downturn (I suppose it is only fortuitous that Mr Madoff's plea is coming in today), to amending the federal money laundering statute to apply to tax evasion. Is it your assessment that there is going to be a growing willingness within the FATF to reassess its traditional stance on the tax

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evasion issue? If not, is there any alternative international forum in which timely progress in this direction might be better secured?

Mr Robertson: I spoke earlier about the review that is being undertaken of the FATF standards and working practices and so on. In the discussions that have just taken place one of the topics that will be subject to that review is the very question of tax crimes as a predicate offence. To some extent the FATF has already demonstrated a willingness to debate that issue again, however I cannot determine the outcome. There are 34 members of the FATF and some of them have varying views on the question of taxation. My sense would be that the very fact that there is a re-opening of what is a contentious issue really does demonstrate an appetite. Some of the interventions that were made during that meeting suggest that certainly some Member States may be shifting their position on this issue. As you have highlighted, in the US, for instance, there is a fresh debate on the question of tax crimes as a predicate offence. I think it is clearly the case that the debate is going to happen and it has been re-opened.

Q63 Lord Hannay of Chiswick: Could you say something about whether the British Government's attitude to that issue has shifted in a more positive direction?

Mr Robertson: Tax crimes and tax fraud are a predicate offence in the UK. I do not know whether it is in a more positive direction but we very strongly believe that tax fraud should be considered a predicate offence and we do so under our regime. We are certainly very supportive of the debate and we will try to progress that in a positive manner within FATF. Your question also asked about other fora in which the debate will take place. This is a matter that is under consideration by the G20 as well. The obvious place where these debates would take place would be within the context of the OECD where things like the harmful tax practices initiative or the work that is done in working party 8 in the tax area which looks at tax and money laundering are obvious places where you would expect that agenda to be progressed in parallel.

Q64 Lord Dear: Could I turn the focus onto the G20 summit that was held in Washington DC at the end of last year which concerned itself with financial markets and the world economy. The emphasis there was placed on "protecting against illicit finance risks arising from non-cooperative jurisdictions". Three points occur to us from that. Has the issue been discussed within the FATF? If it has, what was the effect of it and, logically, what further developments do you foresee for the immediate future?

Mr Robertson: One of the things I should say is that I would interpret the G20 action plan statement as actually quite positive in its language towards work that the FATF has undertaken on this issue in the past. The FATF has historically had processes which are designed specifically to address jurisdictions that do not meet the required standards. The current process is called the international cooperation review group which serves to examine those jurisdictions which are not cooperating sufficiently with the international community. There are a number of countries there which are currently listed and against which members of FATF and members of the FATF style regional bodies and other jurisdictions are then encouraged to take steps in terms of protecting our financial sector. There is already an FATF process. As it happens, the FATF has decided to review that process and there is a review already underway with a view to seeing what improvements could be made. The call from the G20 and the broader issue of the financial crisis brings certain aspects of that into focus. Also, just more generally, when I talk to the fora about the review that is underway about the fourth round of mutual evaluations, how those should be conducted and whether the standards need to be changed, one of the topics that has been suggested for that review is a set of recommendations that relate to international cooperation specifically. There are a series of recommendations that relate to mutual legal assistance, to extradition, to cooperation between financial intelligence units and so on. Whilst the feeling is that those standards themselves are correct, there is scope for a further look at how they are implemented and how the performance against them is evaluated. I would say that in a number of ways the financial crisis and the sorts of issues that the G20 has highlighted have very much come into focus and are actively under discussion in the FATF in that regard.

Q65 Lord Dear: There may be no answer to this, but I get the picture that you identify non-cooperative jurisdictions measured against an international standard. Having identified them, then what? It is one thing to identify them—you have them in some sort of metaphorical pen wishing that they were not in there but they are—but you want them to cooperate; what can you then do to bring them on side?

Mr Robertson: The current process is something called the International Cooperation Review Group process (the ICRG process) and what happens there is that once a jurisdiction has been put into that process and has been nominated, it is then communicated with by the FATF in terms of where it is thought to have failings and there will then be a process of engagement with the FATF in terms of identifying the sorts of improvements that are

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required. Whilst that is on-going FATF members in other jurisdictions are then encouraged to take steps to protect their financial systems from engagement with that jurisdiction. Ultimately, if that proves not to be fruitful and if the jurisdiction does not make the necessary progress, the FATF can then recommend that countries impose a series of what are called counter-measures which are essentially steps designed to protect more formally their financial systems from engagement with that jurisdiction. That could be, for instance, requiring extra levels of diligence in financial transactions. To give you a concrete example, at the moment the countries that are under consideration in that process are Iran, Uzbekistan, Pakistan, Sao Tome and Principe and Turkmenistan. There has been a varying degree of cooperation from those jurisdictions so in some cases they are actively making progress and they have engaged with FATF, and it is a question of time to make sure that the necessary changes are made. In other instances there has been a lack of progress. In relation to Iran and Uzbekistan there was very little positive engagement and at the October discussion in the FATF those two jurisdictions were highlighted in particular and the strongest language, if you like, in the FATF communiqué was applied to those. Subsequent to that Uzbekistan then engaged very positively, made a number of commitments and undertook to reform its regime in a six month period. So the process at that point has really taken off. However, in relation to Iran the feeling in FATF was that sufficient progress had not been made. At the February meeting it was agreed that Member States should now enact counter measures against Iran. FATF has not specified what the counter measures are but there are examples in the FATF methodology of the counter measures that countries can implement. It is now for individual jurisdictions to decide what counter measures they feel are appropriate vis-à-vis Iran and that would depend on the strength of their relationship between their banking system and Iran and the exposure they have. In June we would expect a discussion and a report back by the FATF members on what action each one has taken vis-à-vis counter measures on Iran. That is a concrete example of how the process currently works but, as I say, that process is under review.

Q66 Lord Richard: What sorts of things are covered with that general phrase of counter measures? Is it done within the umbrella of the FATF or is it down to each country to decide what it wants to do? Is there a list of approved FATF counter measures? If there is, what are they? Could you go outside that if you wanted to put more pressure on a particular country? It is not exactly a concerted attack on the non-compliant countries.

Mr Robertson: The methodology sets out four examples of counter measures but they are only examples. Those are that a jurisdiction could require its businesses to undertake enhanced due diligence of any transactions, so basically to subject those transactions to greater scrutiny. They can also apply the same approach to on-going business relationships that they already have with the businesses in that jurisdiction that they might otherwise have considered to be meeting the necessary standards. Another example is what is called systematic reporting which is that a jurisdiction can decide to impose on, say the financial sector, systematic reporting of all transactions within a jurisdiction so that the information would come in centrally and would be analysed. Then the fourth example is ceasing or limiting business with a jurisdiction, so at its most extreme that would be cutting off all financial sector business.

Q67 Lord Richard: These have all been done, have they?

Mr Robertson: They have been done in varying degrees with different jurisdictions at different times by different FATF members. Part of the nub of your question was the extent to which these things are harmonised and concerted and the answer is that they are not. If you were to take, say, the relations between the UK and Pakistan there would be a different relationship and a different volume of transactions from the UK and Turkmenistan. Perhaps Canada has very little business with Iran. To some extent there is an issue about what is appropriate in the context of the economic relationship between the two jurisdictions but, as I say, I think one of the things that will be under scrutiny in the review of the process that is about to take place will be that question of the extent to which those sorts of counter measures need, in some way, to be harmonised, whether that be in terms of a clearer statement of groups of counter measures that might be taken in relation to a particular jurisdiction. At the moment it is quite a flexible process.

Q68 Lord Richard: Does the FATF actually have to sanction the counter measures in advance of them being imposed?

Mr Robertson: Ultimately it is for individual countries to decide what actions they take. It is sort of more the other way round I think in that the FATF, having called for counter measures, you could then expect quite a serious debate potentially if members then failed to take any action in relation to jurisdiction. Under the current system it is not for the FATF to specify what the counter measure is and it cannot force anyone to take it, but then as a standard setting body you would then expect a debate if counter

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measures had been agreed in plenary by all the members and then subsequently actions are not taken. There is a process whereby people report what measures they have taken in relation to each of the countries and jurisdictions under review at each plenary.

Q69 Chairman: What measures has the UK taken with regard to all of this over Iran?

Mr Robertson: Our normal process in relation to a jurisdiction that is named by FATF as one that is required to make improvements is to issue an advisory to the regulatory sector alerting them to this fact and consistent with the risk based approach tell them that is something they need to factor into their scrutiny and their diligence in terms of their transactions with that country. Now there has been a specific call for counter measures against Iran we are internally reviewing what we think the most appropriate action would be for the UK, so at this point in time we have not made any decision but there will be a press notice that is likely to be issued either today or tomorrow which will set out in broad terms the fact that, in relation to the named jurisdictions, what actions we expect the relevant sector to take. That will also refer to the fact that we are now reflecting on what the appropriate counter measures would be for the UK to take against Iran.

Q70 Chairman: The press notice that you are going to issue in the immediate future will not cover the eventual decision that you take.

Mr Robertson: No, it will merely highlight—

Q71 Chairman: Give a guess when you might come to the final decision.

Mr Robertson: That is very hard for me to say because, depending on the nature of the measure, it would not necessarily just be a decision I think for the Treasury; the sort of range of measures we talk about are quite great. There will be a need to identify what is the appropriate measure in relation to the UK and some of the possible actions that relate to counter measures are contained in the Counter Terrorism Act which was enacted at the end of last year. One of the major points for debate in both the Lords and the Commons in relation to that act was the need for any action to be taken to be proportionate. I think there is a fair amount of due diligence on the part of government to ensure that in assessing the options we have that those are proportionate to the risks. I think there is quite a lot of internal work to be done within government before we can settle on specific counter measures. I am not sure I can give you a commitment but the next plenary meeting is in June so we would be expected to report in June on actions that we have taken.

Q72 Chairman: Could we have an assurance that as decisions are taken you will acquaint this Committee with those decisions?

Mr Robertson: Yes, of course.

Q73 Lord Hannay of Chiswick: I am not sure I have properly understood this process. Is this process purely technically driven? It relates to doubts that the FATF has about the transparency and nature of the Iranian financial system and banking system and so on, and it is in no sense a set of sanctions in the UN or EU sense related to Iran's nuclear programme? Am I right in understanding it that way? So if things went on an improved trend in the negotiations over Iran's nuclear programme that would have no automatic effect on what you are doing under FATF, or would it?

Mr Robertson: The FATF's remit in terms of the standards it sets and enforces relates to money laundering and terrorist financing only. The counter measures that exist are primarily designed to protect the relevant financial sector from engagement with a financial sector in another jurisdiction which is not properly regulated. There is no direct relationship between what FATF undertakes and the question of proliferation. That said, the FATF has been asked to undertake work by the UN in terms of identifying proliferation financing techniques and how that works and helping, if you like the educational process and also in terms of assisting countries in knowing how to look for and how to implement policies relating proliferation finance, but it has no responsibilities at all in terms of the standards.

Q74 Baroness Garden of Frognal: We note from your written evidence that Member States agreed in May 2008 to a list of equivalent countries for the purposes the Third Anti-Money Laundering Directive. What criteria were utilised in determining which non-EU/EEA countries to include on it? Could you also say whether the Foreign Office was involved in these discussions?

Mr Robertson: The FATF standards are what are referred to as the 40 + 9—there are 40 money laundering standards and there are nine that relate to terrorist financing—and those were the core criteria that were used in the equivalence process. The Anti-Money Laundering and Terrorist Financing Committee in the EU also took account of information in terms of feedback from the financial intelligence unit over the degree of cooperation received, for instance, between the relevant jurisdictions. They analysed the 12 core recommendations in the FATF methodology against which jurisdictions would often be looked at. A lot of those refer to things like customer due diligence, so are there processes in place to make sure that when

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someone comes along and wishes to open an account or make a deposit that you know who they are, that you know who the beneficial owner is and so on, as well as issues like whether money laundering and terrorist financing is criminalised in that jurisdiction, about whether there is a suspicious activity reporting regime in place and so on. Those are the core criteria that were used for the assessments of the equivalents list. As to the extent to which Foreign Office was involved, I am afraid I could not say but I would be happy to check and provide that in writing. I was not actually in this field at the time in which the list was drawn up.

Q75 Baroness Garden of Frognal: Is there an agreed process by which third countries and territories may seek inclusion on the list? If there is a procedure for that perhaps you could tell us what it is. Have any countries or territories been added to or deleted from the list so far?

Mr Robertson: There is supposed to be a six monthly discussion in the committee of the list and any Member State or the Commission can put on the agenda a nomination for a country or a territory to be added to the list. I think what would happen in practice is that a third country would have to request via the Commission or Member State that its candidature, if you like, could be discussed. As yet there have been no nominations for additions or deletions from the list, but the list is relatively new, having only been agreed in May 2008.

Q76 Baroness Garden of Frognal: How public is the information that is submitted? There must be some security related information that is involved with it, so presumably not all the information that goes into making these decisions can be made public.

Mr Robertson: No, indeed. In the decision that was made within the committee there was no consensus to publish the specific criteria and the discussions so in the end there is no publication of the material or the reasoning behind the decision.

Q77 Chairman: Mr Yvon, I am sure you do not come from a Trappist order; would you like to comment on the question from Lady Garden about the Foreign Office?

Mr Yvon: I am afraid it is not an area of direct responsibility of mine in the Foreign Office so I actually cannot respond as to the extent of the Foreign Office involvement in that particular case.

Q78 Baroness Garden of Frognal: There must be diplomatic implications in the decisions you are taking.

Mr Robertson: We liaise very closely with the Foreign Office and obviously it being a committee in the EU the UK representation to the EU would, as a matter of course, be copied into discussions about these things. I would be very surprised if the Foreign Office were not involved but I was not there at the time so I cannot say for sure.

Q79 Lord Richard: Have there been any additions?

Mr Robertson: As yet no; there have been no additions or deletions at this point. It should be said that not all of the FATF core membership were successful in gaining addition to the list because it was felt that in some cases they had not met the required standards that were set. Both China and Turkey, although they are members of the FATF, did not make it onto the EU equivalence list. The process was quite thorough I think in terms of assessing the jurisdictions against the criteria.

Q80 Lord Marlesford: I understand there are negotiations taking place on the possibility of additional countries signing up to the EU money laundering directives. I wonder which countries these are and what progress is being made.

Mr Robertson: The money laundering directive applies to all members of the EU; it does not then apply to anyone else. There are certain Member States who have yet to implement—

Q81 Lord Marlesford: I m talking about outside the EU.

Mr Robertson: In terms of seeking equivalence, on the list? The directive, as it stands, it would be up for any territory or jurisdiction outside the EU if it wished to apply the legislative approach that is in the directive, that can be entirely applicable for them to do so, but clearly if they are not a member of the European Union then the directive cannot apply to them per se. They could obviously then seek inclusion on the equivalence list but the equivalence list works on the basis of a number of core criteria rather than in relation to the actual legislative provisions of money laundering.

Mr Webb: Countries thinking of wanting to put in an application to become members would have to comply with all the Acquis Communautaire and they would have to do it in advance of actual membership. I have not heard specifically of countries wanting to join.

Q82 Lord Marlesford: My recollection is that I have seen press reports months ago about negotiations which have already started between the Commission and further countries outside the EU for compliance with the EU money laundering directives.

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Mr Robertson: That is not something I am aware of. Unless they were candidate countries for membership—

Q83 Lord Marlesford: No.

Mr Robertson: The directive applies to the EEA as well.

Q84 Lord Richard: Can I come back to equivalence? I think there was a statement last year in May where the Treasury indicated the UK Crown dependencies—Jersey, Guernsey and the Isle of Man—might be considered as equivalent if Member States wanted to consider them as equivalent. Is it open to an individual Member State to declare equivalence for its dependent territories or is it something that the FATF have to agree to before they can get onto a list to be treated as equivalent? Secondly, have any members of the EU actually exercised this option to date? Finally, what is the position of the overseas territories?

Mr Robertson: The equivalence list is something that is part of the EU process rather than the FATF process; there is no direct FATF issue at hand. In terms of equivalence, ultimately equivalence is a matter for Member States, its national competence. The decision was taken to try to coordinate this at community level in order to be of assistance and provide a degree of consistency, but ultimately it is national competence in terms of who is put on the list. In relation to the Crown dependencies nine Member States have so far put the Crown dependencies on their lists as being equivalent, those being Cyprus, Ireland, Latvia, Lithuania, Luxembourg, Malta, the Netherlands, Romania and the UK. Those countries have decided to include the Crown dependencies on their equivalence list. There are then some ten jurisdictions who have published an equivalence list and have not included the Crown dependencies. Then there are a further eight Member States who have yet to publish any kind of equivalence list at all. So the picture is a mixed one. With regards to the overseas territories, at the moment there is no mention in the text. As I have explained, there is the option for new territories to be added to the list and within the UK we have embarked on a process of engagement with the overseas territories to try to ensure that they reach a standard that we would be satisfied with, where we could consider them equivalent for our purposes. Once we reach that stage I would expect that we would then push for them, after discussion within the relevant committees, to be considered equivalent by other jurisdictions that would wish to do so.

Q85 Lord Avebury: What can you tell us about the implications of the fact that certain Member States are still not fully transposed to the Anti-Money

Laundering Directive? Can you tell us anything about the infraction proceeding that have been initiated?

Mr Robertson: Clearly non-transposition is far from ideal but I think one of the things to note is that to a certain degree there are fundamentals in place. This is the third money laundering directive; there are two already. All of the countries against which infringement proceedings are under way are members of the FATF so in general they will have a relatively high standard of a money laundering regime. It is not necessarily the case that the impact in terms of cooperation and so on is highly material but it is unhelpful. We would not expect, for instance, there to be a significant impact on things like cooperation between financial intelligence units or cooperation on asset recovery and so on. That said, it is far from ideal and there is a potential cost to business because it may well be that some of the regimes will not match up entirely and that may cause difficulties to business. On the latest statement on the Commission website the list is now down to six countries who have not fully transposed or notified. The three who have not fully transposed or had not at the time of the updated list on 20 February were Finland, France and Belgium but I happen to know that the French have enacted their legislation and are now in the process of issuing a series of decrees to provide greater guidance to each of the regulated sectors of their industry. Spain, Ireland and Sweden have not notified. It may be that they have actually enacted the directive and simply not notified; that is not necessarily that unusual. So it is not a clear picture, I am afraid, in terms of the state of implementation in each of the six Member States who have not fully implemented the directive. However, because of the nature of those states and, as I say, the baseline in terms of the anti-money laundering and terrorist financing regimes they already have in place it is in likelihood not as problematic as it might appear on the face of it.

Q86 Lord Avebury: It certainly looks problematic. You say in your paragraph 18 that three of the countries are falling short on more than one of the six key issues. Is that still the case?

Mr Robertson: If you look some of the deficiencies, it may be something specific like in relation to reporting on casino transactions; it could be something quite specific where they have failed. One of the things that the money laundering directive does is extend the regime into new areas previously not regulated. That is clearly far from ideal and it seems likely that that will impose costs for the businesses that are engaged in cross-border transactions with those jurisdictions and there will not be the kind of level playing field that one would hope for. That is precisely why infringement proceedings are under way and we

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would very much hope that the relevant Member States would act quickly to ensure that they reach the standards required and that they implement the directive. The point I was trying to make was that while it is not ideal and there are problems and those problems may be more acute in certain aspects scope of the money laundering and terrorist financing regulations, the likelihood is that the underlying regime as a whole may be functioning well; a lot of fundamentals will be in place but the chances are that there will be specific sectors of the economy that are not in compliance with the directive and that is clearly something that needs to be rectified.

Q87 Lord Avebury: If there are specific sectors that you are anxious about, is it not incongruous to think that states concerned meet the equivalence tests?

Mr Robertson: One of the problems about the equivalence test is that the equivalence test only applies to certain types of transactions. It does not apply across the board to every type of transaction. I watched the evidence session from last week and I have read the submissions that have been made to the Committee, and the Law Society makes some points about equivalence. However, equivalence in general only applies to one particular aspect of the legal profession which is something called pooled accounts which relates to where solicitors hold money on behalf of a number of clients and do so in one single account. Other than that specific area the equivalence list does not apply to the legal profession. So it is not necessarily the case. The interaction is quite complex between the equivalence list and the broader transposition of the directive.

Chairman: Before Lord Avebury continues, I wonder if Lord Marlesford wishes to make a point on the Hawala point.

Q88 Lord Marlesford: I want to raise this question of informal transfer of money. In the culture of certain countries there is a very long standing tradition that money can be transferred between countries on an informal basis, commonly known as the Hawala basis. As I understand it, it involves somebody in country A who wishes to transfer money to somebody in country B going to an agent in country A and giving the funds to that agent; that agent then arranges for an agent in country B to provide the funds to the person to whom the original transferor wants to transfer to the funds. Obviously there is nothing intrinsically wrong with this, but one can see that this could raise considerable difficulties if it is used by criminals. I wondered how you are tackling what is probably already a problem and indeed in the case of piracy—to which we have already referred—the press reports do indicate that Hawala is one of the methods used for laundering the proceeds of piracy.

Mr Robertson: Hawala is treated as a form of money service business and HMRC regulates Hawala operations alongside other money service businesses. I think one has to be cautious about the use of the word informal because actually they are required to be registered under the money laundering regulations. Anyone who is operating a Hawala business is required to register. Their directors have to be subject to a fit and proper persons test and they need to provide training and procedures in order to comply with the regulations. HMRC carries out risk based supervision in relation to Hawala. Whilst there is an issue, we aim not to discriminate against different forms of transmission of funds. What we do try to do is make sure that those people who are carrying out whatever form of money transmission it is are subject to the regulations, are regulated, have in place the necessary procedures and are subject to the necessary standards.

Q89 Lord Marlesford: Monitoring must be very difficult where it is being used by criminals who would not wish the transactions to be monitored or detected.

Mr Robertson: The suspicious reporting activity applies to Hawala as much as to anything else. If you are operating a Hawala business and somebody came in and you had reason to suspect that this was a transaction that related to money laundering or terrorist financing you would be required to report it. I am not sure I can say the extent to which that is a preferred method. Different groups, whether it is serious organised crime or different terrorist groups, have different preferences for the type of regime they will tend to operate in terms of transmission of money and of money laundering. Certainly the key is to ensure that all the relevant forms of money transmission are properly regulated and that the people undertaking those are subject to the relevant tests and that they are part of the suspicious activity reporting regime.

Mr Webb: There is an obligation on Hawala to report suspicious activity but also they will have a link into the banking sector because physically there will be cash payments made at one point or another to balance between agents in one country and another, so that activity can be picked up on there and noticed if it has not been properly registered. There has been a lot of work to raise the visibility of the regulatory regime, a lot of work with HMRC in going through the country sector by sector to talk to people and raise awareness of the requirements that have been imposed on them and a certain amount of law enforcement activity as well. It is an area we are looking at very carefully.

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Q90 Lord Avebury: We note from annex to the Treasury memorandum that you are supporting, on an on-going basis, due process improvements to the existing UN al-Qaeda and Taliban sanctions regimes, referring in particular to UN Security Council resolution 1822 which I think was in June 2008. Could you tell us what further enhancement to the regime you would like to see and whether there are any signs of this matter being brought before the Security Council again considering that it is now nine months since June 2008?

Mr Yvon: I think firstly I would say something about the context which may be helpful for the Committee to hear. Sanctions are very much an evolving tool. They are a relatively recent phenomenon in foreign policy tool kit terms and so we are deepening our understanding all the time about how they operate and how we can make improvements. On the issue of due process—or humanitarian concerns as it is sometimes called—I think there have been quite a lot of improvements that the UK has supported. In 2002 we played a part in negotiating a Security Council resolution which would improve humanitarian access to funds where that was necessary for people who were actually on the UN watch list so that they could get basic food and provisions. That is quite an important advancement and it is something we see across the range of sanctions regimes not just the ones concerned with terrorist asset freezing. In 2005 the World Summit took place in New York and members of the United Nations came together and reiterated that there should be fair and clear procedures for adding people onto lists and for removing them and for the operation of humanitarian exemptions as well. In 2006 we supported efforts to create a focal point which is a part of the United Nations secretariat which can receive petitions from individuals who believe that they should not be on the list and previously an individual would have to go to their Member State of residence or nationality and ask for that Member State to petition the UN, but now they can do so directly. This is a huge welcome advancement and the resolution to which you referred, 1822, makes a big advancement as well in that the Security Council has committed itself to reviewing everyone on the list by June 2010. That is an important stock take of UN procedures. In terms of the question about what further advancements we would like to see, that is difficult for me to answer at the moment because we are still actually conducting our review and analysis of all the options. We have not ruled any option in; we have not ruled any option out at the moment. We are not quite at the stage of discussing with other international partners. So it is difficult for me to say that we have settled on a particular model for further improvements, but we are aiming towards a further Security Council

resolution in December of this year when we will take that process of evolving the sanctions regime further.

Q91 Lord Avebury: In the resolution 1822 the Security Council directs the committee to make accessible on the committee's website a summary of the reasons for an entry in the list. Is that what you mean by the review, that everybody will know why they are included in the list and will have an opportunity to challenge the inclusion of their name?

Mr Yvon: Yes. The review is two-fold. It is the Security Council having a stock take of all the names and deciding whether or not those people should remain on the list, but it is also drawing up a statement of reasons so that individuals are absolutely clear about why they are on the list. They have, at present, the ability to challenge their listing.

Lord Avebury: I declare an interest because I wrote to the Foreign Office about the inclusion of Mrs Charles Taylor on the list and she was in fact subsequently removed after a great deal of hard labour.

Q92 Lord Hannay of Chiswick: In the UN High-level Panel report to which I contributed a number of recommendations were made in 2004 about this of which only rather few saw their way into the summit proceedings which you have referred to. One of the areas we focussed on was the fact that the UN Secretariat's expertise in this matter was pretty weak and that they did not have the resources that enabled them to inform the Member States, the Security Council and others about how best to make these systems operate. Has there been any improvement at all on that? Are we supporting a strengthening of the UN Secretariat's capacity in this area?

Mr Yvon: There have been some developments. The Canadians are funding a project at the moment which is helping to enhance the ability of the Secretariat to keep proper records and to ensure that it has proper databases set up within the Department of Political Affairs which is where the sanctions branch is located. I think they do a very good job as you will recall from your time there. There are some longstanding and dedicated UN staff working on the sanctions. We should not be complacent; we should always look for where improvements can be made, but I hoping that this latest Canadian project will indeed deliver some improvement.

Q93 Chairman: I wonder if you would like to comment on a judgment by Lord Justice Wilson last October in the Court of Appeal. I will read what he said: "Notwithstanding the Council's recent attempts, by resolutions No. 1730 (2006) and, since the hearing before us, No. 1822 (2008)" (which Lord Avebury referred to), "to improve such procedures, for example by allowing the listed person in his own

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capacity to lodge at the ‘focal point’ a request for de-listing instead of making such a request through the state of which he is a citizen or in which he is a resident, 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.”

Mr Yvon: I think it throws up something very interesting in terms of the effectiveness of sanctions and an individual’s human rights. I have read quite a bit around this subject and often the issue is portrayed in that you have sanctions effectiveness, you have human rights on the other side and these two are somehow in conflict with each other. I actually think that if you probe a bit further what you actually reveal is a question of human rights on one side and human rights on the other. As much as the individuals on the list have human rights that properly should be respected and promoted by Member States, the people on the bus in Tavistock Square on 7/7 had human rights and the people on the tube that day had human rights as well. I think when we are looking at the effectiveness of sanctions we have to remember what their purpose is and in many cases the sanctions regimes are in place to support human rights. I think that is an important bit of context in terms of how the balance is struck. That does not mean that due process should go away for any of the individuals on the list. I think it is fundamentally important for the credibility of the sanctions regime that it should be transparent and it should be fair. The “focal point” I think is a good advancement of that. There are many other ideas out there about how you would review the people on the list. At the moment the Council is doing that through 1822. I think there are a lot of achievements that have been made that actually do move us closer towards what people would call due process.

Q94 Lord Mawson: Is the UK satisfied, in the light of the *Kadi* judgment of the European Court of Justice and the response to it in Brussels, that the EU legislation is now ECHR compliant?

Mr Yvon: I will take that question as well as it is related to sanctions. The judgment itself said two quite important things. One was that individuals should be informed if they are on a list and the other that they be provided with an opportunity to respond and give comments. That clearly came out in the judgment. Once the judgment was out in fact that the EU did very much that. The European Commission wrote to the individual and organisation that the judgment is concerned with, set out the reasons for the listing and gave them an opportunity to respond. I think I am satisfied that appropriate action has been taken consistent with the court judgment.

Q95 Lord Harrison: In its June 2007 mutual evaluation report the FATF expressed concern about the ability of the UK authorities (excluding Scotland) to handle mutual legal assistance requests in a timely and effective manner. Do you think that was a fair concern and, if you do, to what extent and in what manner have these concerns been tackled?

Mr Webb: I will take that as I am responsible for UK Central Authority. I think on balance it probably was a fair assessment and we have been conscious of the problems. The staff in that area have been working very hard but for very positive reasons there has been a huge increase in the amount of mutual legal assistance requests going around and they have not been able to cope. What I have done, as director of this area, is put a considerable expansion of the UK Central Authority in place, a 30 per cent increase in the number of staff and also quite a substantial restructuring has addressed a number of the other points that the FATF evaluation came up with. Some senior lawyers have come in to advise the case workers in complex cases to make sure they were properly allocated which should hopefully also increase the productivity and speed things up; it will reduce the number of times we need to go back and get letters going backwards and forwards to clarify things. We have also introduced best performance management system, brought a new database in which I am happy to tell you is working. Basically we have at the moment an active case load and this is across all mutual legal assistance, not just in the money laundering areas. There are around 12,000 cases which we are projecting having cleared by around October or autumn next year.

Q96 Lord Harrison: Is that a 30 per cent increase in manpower?

Mr Webb: Yes.

Q97 Lord Harrison: Also a re-jigging and re-focussing. How are you going to judge that? How soon will you be in a position to be able to make an assessment?

Mr Webb: Almost as we speak the staff are being trained up. They have been brought in and they are pretty much a full complement now but they need to be trained. Then the performance manager will be keeping a very close eye on the speed in which incoming requests are dealt with and the speed at which the actual case work is being dealt with. What we also did at the time of this expansion was to write round to all colleagues in UK central authorities in other countries to tell them what we were doing, to ask them to bear with us because the results are not going to happen overnight, but nonetheless to demonstrate that we take very seriously speeding up the process of our handling this partly for our

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reputational reasons and partly because in practical terms you want to ensure that you have good relations with other people's central authority and they will continue to deal with our requests in a speedy way.

Q98 Lord Harrison: It is very useful that you have talked to colleagues. Does that mean you report back to FATF that you have done these things and put them in place?

Mr Robertson: The UK is due for a follow-up to its mutual evaluation in June and we are actually in the process of providing answers back to the secretariat now about the changes we have made to our regime. That would be one of the aspects.

Mr Webb: I think we shall be able to satisfy them in respect of the UKCA that we have addressed all concerns raised.

Q99 Lord Hodgson of Astley Abbots: Can you tell the Committee why the UK has not yet ratified the Council of Europe Convention on laundering, search, seizure and confiscation of the proceeds from crime and on the financing of terrorism which dates back to 2005? Given that all this negotiation was chaired by the UK originally and that ratification by the European Community was agreed by the Council on 26 February 2009, is the time right to reassess this position?

Mr Webb: The short answer to this is that we expect to sign the convention very soon and ratify within about 18 months. There has been quite a knotty policy issue that we need to resolve around particular aspects of this convention which is around article 47 which itself is to do with postponement of certain transactions on the request of a FIU. The difficulty with this is that it does not fit at all well with our domestic regime and the way we should cooperate on the consensus. If we were to have one regime for cases of money laundering domestically and a different one for cases which have been referred to us from a foreign FIU, we thought that would be quite problematic for the regulator sector. We then had a discussion about the competence issues and what we were busy negotiating with the EU for an acknowledgement which they did in the recital that article 47 is a matter that falls to Member State competence so we can decide how to adapt this or make a reservation if necessary. Happily that was agreed and we got a clearance with the Scrutiny Committee for the position we were planning to take also at the end of February. We are now on track to finally ratify that.

Q100 Lord Dear: Before I ask a further question about ratification, I wonder if I might go back to what Mr Robertson was talking about earlier in the

discussion about Iran. That is an on-going example but I was wondering if you could give us a written submission on something which is already wrapped up. Iran is on-going; do you have an example—or preferably two—of something where you can see something in totality.

Mr Robertson: Under the current process there is only one example of a territory that has come out the other side of the process and that is the Northern Part of Cyprus.

Q101 Lord Dear: Could you send us the details in writing?

Mr Robertson: Yes.

Q102 Lord Dear: Could I then chase the same ratification point and ask you to look at the Second Additional Protocol to the European Convention on Mutual Assistance in Criminal Matters, a 2001 protocol, which I understand the UK has signed but not ratified. That of course leads to the supposition that you might want to dispute that that damages our reputation as a leader in the area of international cooperation. It has been hanging around for eight years and has not been ratified. Is there a reason for that?

Mr Webb: We would expect to ratify this one by the autumn. 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. Again there are one or two policy issues to be dealt with which, as you can imagine from your own career, are to do with complex issues around mutual recognition in areas like control, delivery, covert surveillance, joint intelligence teams. There are some quite tricky issues that we need to work our way through, but we would hope to be in a position to ratify by the autumn.

Q103 Lord Dear: They are the impediments that stopped an earlier ratification.

Mr Webb: We have been considering them. It has been dealt with by the same partner, UK Central Authority, and was dealt with by individuals who also had a heavy case working load and we split case working policy to free people up to ensure that we can tackle these things in a more timely way in the future.

Q104 Lord Dear: Eight years is rather a long time.

Mr Webb: Yes, we recognise that and, as I say, we are far from unique in this.

Q105 Lord Dear: I pursue my point, if we are holding ourselves up as leaders and trying to set an example by that, delay in ratification of seven or eight years seems excessive.

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Mr Webb: I agree and I think what we have done with the UK Central Authority, as I say, expanding the case working function and creating dedicated policy function will enable these sorts of things to be dealt with in a more timely way in the future.

Q106 Chairman: I want to go back, if I may, to Lord Hodgson's question about the non-ratification of the Council of Europe Convention. I understand that in April there will be the first meeting of the conference of the parties of the Money Laundering Convention. Do the United Kingdom expect to have a seat at the table and to participate in that meeting?

Mr Webb: Sorry, would it be possible to repeat the question? Which meeting is this?

Q107 Chairman: I understand that there is to be a first meeting of the conference of the parties of the Money Laundering Convention taking place in April but we have not yet ratified the convention. Will the United Kingdom be present at that meeting?

Mr Webb: I do not have specific knowledge of that meeting; I would need to get further briefing from my team. I can get back to you and confirm.

Chairman: It seems that the Committee is one jump ahead of you. Would you let us know as soon as possible what the UK's position will be? Lady Henig?

Q108 Baroness Henig: In the 2007 paper *The Financial Challenge to Crime and Terrorism*, one of the strategic priorities set for the following five years was "engaging international partners". Given everything that we have heard this morning, I think I would have thought that this is clearly of major importance to success. I wondered therefore what have been the major accomplishments to date and what you hope to accomplish in the next three years under this heading.

Mr Robertson: I think it is fair to say that we have achieved a wide ranging set of objectives in the last two years. If I could look at the FATF first, we held the presidency for a year and during that time we achieved a number of objectives, one of which was more ministerial oversight for the FATF, we held a ministerial meeting in spring 2008 which endorsed the revised FATF mandate; we have also commenced work on a review of the FATF standards in terms of how the FATF prepares for its fourth round of mutual evaluations and that is underway. We promoted a greater consideration of the surveillance of systemic threats; the plenary of the FATF endorsed a three level strategic surveillance function which involves guidance for national threat assessments, a surveillance dialogue within the FATF to look at current threats and then a global threat assessment project which the UK is co-chairing. We also focussed quite hard on trying to improve private

sector engagement with the FATF. In October 2007 we established a consultative forum in order to structure engagement between the FATF and the private sector. That allows the private sector to raise issues for further discussion within FATF and drive work forward. There are a number of international bodies that sit on that. We also held a number of joint meetings and projects during our time as president of the FATF looking at money laundering and terrorist financing methods, a project on reliance on third parties for customer due diligence which is still underway. We got input from private sector on a typologies exercise to look at money laundering and terrorist financing in the security sector. We also drafted risk based approach guidance for the insurance sector and money service businesses which is being completed. Another of our objectives was low capacity countries where we wanted to develop tools to assist low capacity countries to meet and implement the FATF standards. We co-chaired a project on that with the Netherlands and with significant input from the World Bank. In October 2007 the FATF approved a guidance paper for the assessors (the people who carry out the mutual evaluations), for national authorities and for FATF style regional bodies to maximise the value of mutual evaluations in low capacity countries so they could really take that forward. Within the EU we have obviously implemented the third money laundering directive and the EU has agreed a new terrorist financing strategy which adopts the UK based evidence approach. Bilaterally we have undertaken a range of work with a number of countries on money laundering and terrorist financing controls, in particular for instance on improving their financial intelligence units. That is quite a broad span and there may be things that Home Office colleagues could add to that.

Mr Webb: To give a concrete example, a particular interest of mine is recovery of the proceeds of crime and we have done a lot of work with law enforcement and prosecutor colleagues to highlight the countries bilaterally who are likely to be of most assistance in this and target them when they are outside the EU framework for bilateral agreements. We had a successful memorandum of understanding agreed with the United Arab Emirates which included an asset sharing agreement, so potentially not just mutual recognition of our confiscation orders but then arrangements for sharing the assets once they are seized. That is the sort of activity we are very keen on pursuing because there are partners who are outside frameworks like the EU who nonetheless have very close links to the UK.

Q109 Baroness Henig: You did touch on private sector engagement. From your perspective, you seem to be happy with the way things are going. I am not

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entirely certain that the private sector might share that. If I can press you a bit, I got the sense from the evidence last week that there were a lot of things that they felt could be done to facilitate relationships. In the next three years are there other things you think might be able to be done in that area?

Mr Robertson: We are in the process of more generally setting out targets for the medium term future at the moment. I am not sure I can give a precise answer to the specific objectives but certainly where, in relation for instance to terrorist financing, we are looking to focus our practical actions on high risk jurisdictions and identifying key vulnerabilities in those jurisdictions (whether that would be around cash couriers or lack of financial investigative capacity). Within the FATF we are leading a project on confiscation; confiscation is an important issue to improve cooperation. As I have explained, there are number of issues which are up for review in terms of how the FATF conducts its evaluations. We are really trying to put a much stronger focus on the effectiveness of the regimes that are in place rather than the strict, simple compliance with the standards, and also around a stronger focus on the threats and vulnerabilities in the relevant countries. Similarly we are putting a strong emphasis on improving the relationships between the FATF and the regional bodies and the contribution the regional bodies can make and methods to drive up the standards outside of the core FATF membership. On the question of private sector engagement, having watched the evidence session and read the contributions, my sense is that in general the witnesses were quite positive about the degree of private sector engagement in the UK. It is something that I would say we take very seriously indeed. I am not going to say that the system is perfect; there is always room for improvement and it is a high priority of ours to drive that forward, but through things like the money laundering advisory committee and the supervisors forum and the various bodies that try to make sure that we have that degree of structured engagement with a range of private sector actors. On the international stage, opinions on this vary. There are other countries in the world who perhaps have not got the same perspective we do on private sector engagement and that was one of the reasons why, for our presidency of the FATF, we made that a bit of a cornerstone, if you like. We feel we made significant progress in driving forward private sector engagement with the FATF on an international basis. I would not say for a minute that we have cracked it; there is a lot more still to do. However, the show is on the road. We are starting to make progress on that front and we are increasing the dialogue. I would say that the FATF does have observers in its plenary sessions of various private sector groups so there is a

degree of private sector engagement, but I would certainly agree with the sentiment you are expressing, that there is more still to do and it is a priority.

Mr Webb: I have been dealing in this area for five to six years now and really the relationship with the private sector over that period has improved quite dramatically. I think some of the submissions and hearings you have had will testify to that level of improvement that there has been. I think it was something that quite struck the FATF evaluators, the level of engagement there was. We are always trying to improve the level of feedback that goes to the private sector but in that give them the opportunity to engage in the UK's policy formation process. I think we are pretty advanced in that respect but there is always more that can be done.

Q110 Lord Hodgson of Astley Abbots: Could I press you a little further on these matters because you say in your evidence to us about the key organising principles being effectiveness, proportionality and engagement. While I hear a lot of honeyed words about how things are much better and it is all jolly good stuff, when you actually get down to hard evidence of how it is working the evidence it is rather thinner. For example, when you talk about proportionality, that the benefits of intervention are justified and they outweigh the costs, we have recovered, according to SOCA, £26 million as a result from SARs in 2007-08 or £110 million that has been confiscated. An average city law firm is spending over a million pounds a year on its compliance requirements and I am not sure that there is any evidence of proportionality at all.

Mr Webb: There is an awful lot to unpack in that. The investment that the private sector has undoubtedly made is going to serve a lot of purposes: due diligence for its own customers, a certain amount of self-protection as well as the actual financial reporting process. I think the accountants' (ICAEW) submission picked that up a little. There is an issue about the cost and to what extent some of those costs would have been incurred anyway. Then there is the issue about the level of benefits that we manage to secure. SARs will play a role in a very wide range of financial investigations. Some of them will lead directly to identifying capacities; others will contribute. We are hoping this year to recover in total about £150 million but what we are recovering now is really a reflection of what we were doing two, three, sometimes even four years ago. There is a pipeline and this is heading steadily upwards. As I said, we are hoping to secure a performance this year six times better than it was seven years ago. If we can keep that level of performance up you begin to reach levels of monies being taken off criminals which are really quite substantial. You also have to bear in mind that

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when you are talking about recovering criminal assets that is a sort of sub-set of the total amount we are recovering. That is money coming back to the Exchequer. There is also money that we are identifying that has been handed back to victims, compensation orders that are not included in those figures that are typically ten to 15 per cent of the total on top. Then there are other SARs that lead to other activity within the HMRC, for example, in respect of tax credit fraud, some of which will not be included in these numbers. We are very, very conscious that we need constantly to improve the system. We made various legislative changes in the past to try to identify areas that were particularly irksome to the regulator sector and tackle them. SOCA has also put a lot of investment in the IT and ensuring the processing and improving the actual use of the intelligence that is then generated. Then there is the whole communications effort, to get that regulator sector to understand the enormous value that these reports generate.

Q111 Lord Hodgson of Astley Abbots: Have you given thought to suggesting a revision of the definitions in the Proceeds of Organised Crime Act to try to carve out the by-product of health and safety legislation which seems to cause enormous aggravation and may actually the result in the regulator, SOCA, being blinded by the wood for the trees?

Mr Webb: Different Member States and different countries around the world apply the regime differently. We use a risk based “all crimes” approach; other people will use serious crimes only; other people use mandatory reporting of all transactions over a certain amount or transactions crossing national frontiers and they all have different burdens on the regulated sector. The problem with trying to strip down the number of crimes you are dealing with in many cases, particularly for the banking sector who deliver the vast majority of suspicious activity reports, may have no idea what the underlying predicate offence would be. They then have to make an additional judgment whether they think this is likely to be related to crimes within a particular schedule or not, whereas at the moment they merely need to make a decision as to whether it is suspicious, is it likely to be criminal of some sort or another. Some regulated sectors know exactly what it is and they find that more frustrating when they are required to report on things that they would see as fairly trivial. It would be very difficult to have a different reporting requirement for different members of the regulated sector as a whole. We do discuss this regularly with the regulated sector. I think our approach is the most proportionate and the results are bearing fruit.

Q112 Lord Marlesford: It is clear to me that you have a great deal of extremely important work to do on preventing money laundering connected with terrorism at any level and serious organised crime. On the other hand the very preliminary impressions I have, as of now, is that there is much too much pursuing of trivial matters and one would have hoped that you could in some way or other either put down some form of *de minimis* or allow more judgment to the banks and others or, at the very least, to allow a recommendation by the person making a suspicious activity report to say, “We are making this because it may come within, but frankly we think there is nothing in it so file it”. Otherwise it is fairly obvious that the volume of SARs which SOCA has received is wildly unmanageable and you really are going to lose the wood for the trees, as Lord Hodgson said.

Mr Webb: SOCA can answer the point specifically about the volumes. I think there is some evidence that it is now stabilising and I would question whether it is unmanageable because SOCA has invested a lot into some quite impressive IT solutions which enable them to mine these and particularly to spot linkages between different reports rather than treating every one as an individual one that needs to be investigated; you can spot linkages which might not otherwise have been obvious. This is already bearing some quite impressive results. *De minimis* is not I believe possible. A cash limit would be extremely difficult because obviously a cash limit that we would see as significant maybe for serious crime could be very different from terrorism where potentially quite small sums could do an enormous amount of damage in the wrong hands. The “all crimes” approach has its own difficulties because for many members of the regulated sector they would have no idea necessarily what the related crime was. We do continue to discuss with the regulated sector all these issues and we are beginning to be able to demonstrate that we can make a really powerful impact with these reports and therefore that the cost benefit equation is looking increasingly favourable, added to which the work that SOCA has put in place to make the process a lot easier and to make the process as painless as possible for the regulated sector, particularly in those cases where they think the reports are unlikely to be of great value.

Q113 Lord Hodgson of Astley Abbots: When you do your assessment, do you ever ask the private sector what the costs are? Have you done an assessment of what this whole regime is costing across the private sector?

Mr Webb: We have had a number of reviews of the suspicious activity report system. There was a review very early on; there was another significant review which we will be talking about at the next session I

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think. That involved very extensive consultation with the private sector. As I say, because so much of the investment for private sector is of dual or triple use potentially it is hard to strip down exactly what is solely required for this purpose as opposed to customer due diligence. It is interesting that there is a different perspective between the accountancy profession and the legal profession on that where the accountancy profession thought that the balance was in favour of the existing system.

Q114 Lord Avebury: Going back to the original answer given by Mr Robertson on the three years look ahead and in particular to what was said about the examination of powers to confiscate terrorist assets, I want to relate this to earlier comments on the *Kadi* judgment because we only covered one aspect of it and that was due process. There was another conclusion that the court reached which was that the freezing of funds belonging to Mr Kadi and Al Barakaat constituted an unjustified restriction of their rights to property. Is the FATF going to have a look at this with a view to reaching recommendations on how states should treat assets which are assumed to be the result of terrorist activities in the light of the *Kadi* judgment? Although the control of the assets might be suspended—as it was the case of Mr Kadi—there needs to be a general solution, does there not, to compliance with the ECHR in the cases where terrorist funds are either frozen or confiscated.

Mr Yvon: I can take part of that; I will not be able to say what FATF are doing in that particular area. I think this raises a very valid point and it does play into due process and the interference with individuals' funds. Of course that is very much the whole purpose of the regime, to deprive people who are associated with al-Qaeda or Taliban from having funds, so there is actually a point in the restraint there. I think something was mentioned earlier about a Security Council resolution 1452 which is dated 2002 was actually a very big advancement because that did mean that anyone who had their funds frozen could apply to the United Nations, to the Security Council to have a certain amount of funds released whether for food or housing, even legal fees as has happened in some cases; individuals on the list who actually asked the UN to give them money so they could actually bring a legal challenge. So the operation is quite broad in scope and I think that does go a long way towards addressing the idea that actually we are seizing people's funds because that is not the case. In fact they are frozen and it may be that they will be returned to the individual when they are removed from a list. I think that 1452 goes quite a long way towards tackling that sort of issue that you have raised.

Q115 Lord Avebury: Does FATF in particular need to have a look at this with a view to ensuring that states act in compliance with the European law in either freezing or confiscating terrorist assets?

Mr Robertson: There is a question about the extent of FATF's remit and, to some extent, compliance with the EU law is for the Commission and for the EU to consider. What I should say is that there is a discussion under way in the FATF about whether it would be helpful to find a mechanism for more discussion between countries in terms of the asset freezing process, how that works and to allow the units that are involved in asset freezing to compare notes to discuss issues like the judgments and to have a more joined-up consideration of the issues. There is already some debate within the FATF about this.

Q116 Lord Mawson: I worry a bit that these systems and processes seem quite cumbersome and quite dated given the scale of what we are dealing with here. We are dealing with a very enterprising culture really that is becoming more and more enterprising. Is there any investment into rather smarter ways of dealing with some of this, are you actually bringing on your side of the fence some rather more entrepreneurial behaviour and mindset about how you deal with problems of this scale. I have a little case running at the moment with the Law Society where one family has lost three homes through some of this stuff to just try to see what happens in one micro-circumstance when it tries to engage with these macro-systems. I just wonder whether you have done or whether you ought to do some small scale tests of real examples of this so that you see the relationship between the micro-problem and the macro-systems and processes you are creating and developing and how effective they are. I do wonder whether we need some smarter behaviour with this problem.

Mr Webb: You will be hearing next week from the FIU and SOCA and it is really within the Serious Organised Crime Agency that there are both the skills of the analysts and the considerable investment in IT which enable them to do a lot cleverer things with these reports than they have done in the past. They will give you a lot of reassurance in that area when they see you next week.

Mr Robertson: I might add more generally that for the way the system works the UK has adopted a risk based approach and to some extent that is relatively innovative; it is not necessarily the norm across the globe. That does allow the sector that deals with these issues on a day to day basis to be the ones that make the judgment on how to apply the systems rather than a straightforward tick box approach. The other thing in relation to individual cases which, as you say, really sharply bring into focus the system and how it works, it is precisely for that sort of reason that we have

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things like the money laundering advisory committee and other consultative groups so that we can engage directly with the practitioners and have a mechanism if you like to zoom in and zoom out of the broad picture and be able to focus on the specifics. I am sure there is more we could do to help inform the broader level decision making.

Q117 Lord Mawson: Are you satisfied that the FATF standards on international cooperation, especially Recommendations 36 to 40, are fully fit for purpose? Does the current methodology for assessing compliance with this important part of the FATF standards deliver the most useful product in terms of helping the jurisdiction in question, and the international community understand whether the processes of cooperation are being appropriately utilised in practice?

Mr Robertson: I think as I mentioned previously these very standards will form part of the review that is underway within the FATF. I think, as I have stressed before, our view is that it is not necessarily the case that the standards themselves are in need of radical overhaul—they are largely correct—but I think the second part of your question gets more to the heart of the issue which is how is it that the standards are applied, what does practice look like on the ground? It is evaluation of that performance that we feel needs greater scrutiny. It is all very well for a country to have laws about extradition or asset recovery or cooperation between FIUs or mutual legal assistance, but the statistics demonstrate that that is not happening in practice. If you do not have the live examples on the ground of that happening then that is the more fundamental problem. I think this also comes back to what we are pushing for within the FATF which is more of a focus on threats, vulnerabilities, risks; a real sense of looking at a particular jurisdiction in the round and assessing their regime and their performance against the nature of their economy and the nature of their criminal sector and where they fit into the bigger picture. I think in terms of a reflection of our desire to progress just this sort of issue, the fact that we pushed hard for this project on confiscation and to really examine what the barriers are to the international cooperation on confiscation of assets, that really is a good example that shows our desire to address the heart of these sorts of issues.

Mr Webb: It is a time consuming process but it is one on the whole I think, having gone through it, we could probably benefit from in other parts of the international cooperation not just in the financial sphere. I know the European Commission is quite interested in it as a methodology because you get to the stage where we know that people have complied

with all the various directives but what have they actually done with them.

Q118 Chairman: Thank you. I think that almost brings our session to an end, but maybe not quite. The way we organised this session is that we have asked you a series of formal questions and one or other of you have taken the lead in answering it. I think it would be inconceivable that if we had invited each of you to respond to each question we would have been sitting for much, much longer than this. It is inconceivable too, I think, that each one of you might well have added something to the answer which was given to us by the lead responder. Therefore I feel sure that each of you will have comments you would wish to add to what has been told to us. I said at the beginning that if there were supplementary points you wanted to raise—I shall be quite surprised if each of you do not have some supplementary points to send to us—but just before we end I wonder if any of you would like to add anything to the lead answer which was given to any one of our formal questions. I would like to give you that opportunity now because, as I say, I cannot believe that each of you did not have something in mind you would quite like to have said but did not.

Mr Robertson: The question has been raised about the cost effectiveness of the regime and the costs that it imposes. I agree with what has been said but I think it is really important to stress on this issue that a lot of this is about prevention of money laundering, it is about prevention of terrorist financing and the value you associate with that is very hard to judge; it is simply not an easy thing. I note in paragraph nine of the evidence submitted by the Institute of Chartered Accountants of England and Wales they said that ultimately the benefit of averting even a single serious terrorist outrage is extremely high. This is a difficult issue and we do have these principles of engagement, of proportionality and effectiveness but those are hard to judge and hard to deal with in this context. I would just say that I think it is really important that we keep sight of the fact that some of the regulatory burden that is imposed on the sector has a multiple effect. There may be things that are being undertaken which sectors would want to undertake anyway for their own reasons, and some of it responds to various different regulatory regimes. Ultimately the focus here is on a risk based approach. We work very hard with the sector. Generally they draft the guidance and then we approve it in terms of how they should operate. We work very hard with them; the focus is on risk. I think it is very important not to underestimate the importance of the deterrent effect in this area. That is not to say that we should not be looking to try to find ways of minimising the burden, but I think we

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need to bear in mind the point that deterrents are really very important in relation to this regime.

Mr Webb: I did generally intervene with other people's answers so I have probably said all I need. I have noted that we have some homework to do.

Q119 Chairman: Are there any other points any of you would wish to make?

Chairman: Thank you for coming. I think you have helped us a great deal in our inquiry; it has been extremely instructive to us and we are very grateful.

Supplementary memorandum (1) by HM Treasury

EVIDENCE SESSION 11 MARCH—REQUESTS FOR ADDITIONAL EVIDENCE

COST OF UNITS

In response to Lord Marlesford's request for the costs and staff numbers of the units of each of the witnesses, I am able to provide the Committee with the following information:

HM Treasury

The staff costs of the Financial Crime Team who are involved in money laundering or terrorist finance are £358,832. However, it should be noted that many of these staff also work on fraud, corruption and proliferation financing issues. They are based on (average cost of each grade in 2008-09):

- 1 x Range F (Grade 5) = £93,000
- 3 x Range E (Grade 7) = £150,666
- 3 x Range D (HEO/SEO) = £95,721
- 1 x Business Support = £19,445

HOME OFFICE

(i) The staff costs of the Anti-Money Laundering Team are £127,740. They are based (using Home Office average total pay costs including superannuation and National Insurance Contributions) on:

- 0.5 x Grade 6 = £41,709
- 1.0 x Senior Executive Officer = £47,990 (2 x 0.5 staff)
- 1.0 x Higher Executive Officer = £38,041

(ii) The staff costs of the Terrorist Finance Team. They are £136,718, based on:

- 0.5 x Grade 6 = £41,709
- 0.5 x Grade 7 = £33,013
- 0.5 x Senior Executive Officer = £23,955
- 1 x Higher Executive Officer = £38,041

Foreign and Commonwealth Office

Based on the full economic costs which represent average administration costs calculated for recharging purposes, and reflecting 2007-08 average salaries for London, the cost of the Foreign and Commonwealth Office Sanctions Team is £461,813.

Piracy

In response to the questions by Lord Marlesford and Lord Hannay on the legal status of ransom payments paid and the point at which they become proceeds of crime, a note by the Home Office² and a circular by the Home Office on the consent regime are attached.

Lord Averbury also requested evidence on what consideration FATF has given to the problem of piracy.

² Not printed here. Printed in a revised form with the supplementary evidence of May 2009 at p.69.

An international debate is currently underway, including through the UN, on appropriate responses to the growing threat of piracy, which is likely to consider the role of ransom payments to pirates. Piracy is a complex criminal issue. It involves not only issues of maritime security, but also has humanitarian, international jurisprudence and financial consequences.

The interface between the mandate of the FATF and the issue of piracy is similarly complex. A key part of the FATF's role is to examine the methods and typologies used in money laundering and terrorist financing. As it currently stands, piracy is considered by the FATF standards as a predicate offence for money laundering, which means that the proceeds of an act of piracy are considered illicit funds. As set out at Annex A, money which is assembled in the UK in preparation for the payment of a ransom to pirates is not at that stage criminal property. It becomes criminal property when in the hands of the recipient.

The appropriate role for the FATF would therefore be to examine the methods and trends used by pirates to launder the proceeds of their crime. However, given the low capacity in the Horn of Africa region to participate in such an exercise, this would be a difficult task for the FATF to undertake. As a result, no stand-alone project is currently planned on piracy. However, the FATF's Strategic Surveillance Initiative, which includes a Global Threat Assessment, may consider the typologies of Money Laundering in relation to the proceeds of piracy.

Furthermore, the UK is keen that the FATF continue to prioritise the work on assisting low capacity countries, including through their FATF style regional bodies, to develop effective frameworks for anti-money laundering and combating terrorist financing, to assist them in tackling piracy and the numerous other threats they face. The UK Government will also continue to provide support to the FATF style regional bodies both in the Middle East and North Africa region (MENA FATF) in East Africa (ESAAMLG).

IRAN

The Treasury will undertake to inform the Committee of any decision on counter measures taken against Iran, as and when that decision is taken, as requested by Lord Jopling.

No decision has yet been taken, but the Committee can be assured they will be informed of any developments in this area. Attached for information is our most recent advisory notice issued following the FATF Plenary in February.

EQUIVALENCE

Baroness Garden asked whether the Foreign Office was involved in the discussions on the equivalence list.

The FCO and UKREP were involved in the development of the UK policy position on the equivalence criteria to be adopted in the EU, and the relevant negotiations on the EU common position (on who was to be included on the list). The formal discussions took place in the EU AML/CTF Committee where the UK was represented by HMT, supported by UKREP.

IMPLEMENTATION OF THE THIRD MONEY LAUNDERING DIRECTIVE

We were asked about the situation with countries outside the EU implementing the Third Money Laundering Directive.

MONEYVAL, a FATF Style Regional Body under the auspices of the Council of Europe, evaluates all its members, whether or not they are members of the EU, against a number of standards, including aspects of the Third Money Laundering Directive.

ICRG PROCESS

Lord Dear requested written evidence on a jurisdiction that has been through the International Cooperation Review Group (ICRG) process.

Note: As the northern part of Cyprus, is not recognised as a sovereign jurisdiction by the UK, it is standard practice to place all references to the authorities of the jurisdiction of the northern part of Cyprus and their actions in inverted commas. This convention is adhered to below.

The northern part of Cyprus was put under the surveillance of the International Cooperation Review Group of the FATF (ICRG) in February 2007, when the plenary recommended that the ICRG examine the risk emanating from the jurisdiction due to its lack of money laundering and terrorist financing controls and consider what remedial action could be taken. With the European Commission acting as an honest broker, the

“authorities” in the jurisdiction were able to provide specific commitments regarding the introduction of new “legislation” covering anti-money laundering, casino regulation, and off-shore banking. The first of these “laws”, concerning anti-money laundering, was adopted in early 2008, demonstrating early engagement with the ICRG process.

Despite the progress made, FATF agreed it was necessary to inform the financial sector of their concerns relating to the northern part of Cyprus through the FATF public statement of February 2008. Reference to the risks posed by the jurisdiction was also made in the FATF statements of June and October 2008. However, the ICRG regularly commended the progress being made in the northern part of Cyprus in its reports to the plenary. Notable achievements included: the implementation of customer identification, verification and enhanced due diligence requirements; the establishment of suspicious transaction reporting requirements; supervision for offshore banks; provision of training for prosecutors, law enforcement agencies and judges.

The European Commission confirmed in June 2008 that an administrative unit with five full-time staff had been established to coordinate reporting, assessment, and action concerning suspicious financial activities. Various awareness-raising activities have been organised with the banking and bar associations and training activities with compliance officers. Progress towards implementation of the revised action plan culminated in the passing of “law” regulating casinos in January 2009. Having implemented the action plan in full, the ICRG agreed in February 2009 that the northern part of Cyprus should be removed from the FATF statements, and that the EC should continue to give periodic reports on their progress in developing a robust AML/CFT regime.

COUNCIL OF EUROPE CONVENTION NO 198 ON LAUNDERING, SEARCH, SEIZURE AND CONFISCATION OF THE PROCEEDS FROM CRIME AND ON THE FINANCING OF TERRORISM

Lord Jopling asked whether the UK would attend the first Conference of the Parties to the Money Laundering Convention.

The first Conference of the Parties to the Convention will be held on 22–23 April 2009 in Strasbourg. We understand that there have been no objections from State Parties to the CETS 198 to the Chair’s proposal that all Council of Europe Member States and the Observers to the Committee of Ministers that are not yet Parties to this Convention should be invited to the First Conference of the Parties. We have just this week received an invitation and the UK will attend as an Observer

HM Treasury

6 April 2009

Annex

FATF ADVISORY NOTICE

11 March 2009

HM TREASURY WARNS BUSINESSES OF SERIOUS THREATS POSED TO THE INTERNATIONAL FINANCIAL SYSTEM

Important

This notice constitutes advice issued by HM Treasury about serious threats posed to the integrity of the international financial system. The Money Laundering Regulations 2007 require firms to put in place policies, procedures or systems in order to prevent money laundering or terrorist financing. Regulated businesses are also required to apply enhanced customer due diligence and enhanced ongoing monitoring on a risk-sensitive basis in certain defined situations and in “any other situation which by its nature can present a higher risk of money laundering or terrorist financing”.

On 25 February 2009 the Financial Action Task Force (FATF) issued a statement drawing attention to deficiencies in several jurisdictions of concern. The UK fully supports the work of the FATF on these matters and HM Treasury agrees with the FATF’s assessments.

The UK additionally draws attention to, and supports, the public statement of MONEYVAL (a FATF style regional body under the auspices of the Council of Europe) of 12 December 2008 in respect of Azerbaijan.

Iran

The FATF announced that it remains concerned by Iran's failure to meaningfully address the deficiencies in its anti-money laundering and combating terrorist financing (AML/CTF) regime, particularly in respect of terrorist financing and suspicious activity reporting.

The FATF has called on its members to consider effective countermeasures to protect their financial sectors from risks emanating from Iran, and to protect against the use of correspondent banking relationships to bypass or evade counter-measures and risk mitigation practices.

All UK businesses regulated under the Money Laundering Regulations 2007, whether financial institutions or other regulated persons should treat transactions associated with Iran as situations that by their nature can present a higher risk of money laundering or terrorist financing, and which therefore require increased scrutiny, enhanced due diligence, and ongoing monitoring, including in the case of correspondent relationships.

All other persons authorised by the Financial Services Authority should also take this advice into account in respect of their systems and controls to counter financial crime, and take appropriate actions to minimise the associated risks.

In the light of the call for countermeasures the UK is, in addition, considering what further action is required.

Uzbekistan

The FATF has also drawn attention to the continuing AML/CTF deficiencies in Uzbekistan.

The attention of UK financial institutions and other persons regulated for money-laundering purposes is therefore drawn to the FATF statement in respect of this jurisdiction, and the risk that it continues to present. They should take this advice into account in respect of their systems and controls to counter financial crime, and take appropriate actions to minimise the associated risks.

Turkmenistan, Pakistan, and Sao Tome and Principe

The FATF has also drawn attention to the continuing AML/CTF deficiencies in Turkmenistan, Pakistan, and Sao Tome and Principe,

The attention of UK financial institutions regulated for money laundering purposes is therefore drawn to the FATF statements in respect of those jurisdictions, and the risks that they continue to present. They should take this advice into account in respect of their systems and controls to counter financial crime, and take appropriate actions to minimise the associated risks.

The northern part of Cyprus

The northern part of Cyprus is no longer highlighted as a jurisdiction of concern, following improvements made to its AML/CTF regime.

Azerbaijan

MONEYVAL drew attention to deficiencies in the AML/CTF regime in Azerbaijan in December 2008.

The attention of UK financial institutions regulated for money laundering purposes is therefore drawn to the MONEYVAL statement in respect of this jurisdiction, and the risks that it continues to present.

This advice is effective immediately.

HM TREASURY CONTRIBUTION TO Q166–Q169

Lord Hodgson in Questions 166 to 169 raised the issue of reliance on third parties to carry out customer due diligence and possible sanctions, and relevant guidance.

As was explained in the hearing, the legal provisions relating to reliance are contained in Regulations 17 and 19 of the Money Laundering Regulations 2007. These provisions are intended to provide a basis for reducing the incidence of duplicative or repetitive checks, while ensuring there is continuing clarity that the relevant person remains responsible for any failure to apply the necessary measures.

The regulations set out the circumstances in which a relevant person can rely upon another, and the nature of the persons who can be relied upon, nationally and internationally.

It is difficult to comment on the hypothetical possibility of a civil penalty or prosecution where there has been reliance. In a case where a person who has relied on another has acted with appropriate care and in good faith that would be a relevant factor.

In addition, where a person has acted in accordance with approved guidance that should be taken into account under Regulations 42(3) and 45(2). (Regulations 42(3) and 45(2) require the relevant authority or court respectively to take compliance with approved guidance into account.)

The Joint Money Laundering Steering Group (JMLSG) has, for example, produced detailed guidance on reliance which can be found in section 5.6 of Part 1 of their December 2007 guidance for the UK financial sector. The JMLSG guidance is available at their website:

<http://www.jmlsg.org.uk/bba/jsp/polopoly.jsp?jsessionid=af7paEXXEUDd?d=749>

In addition to the JMLSG guidance, HM Treasury has approved several other sets of guidance, for Notaries, accountancy bodies and firms supervised by HM Revenue and Customs, and is considering several other sets including one for the legal profession.

Supplementary memorandum (2) by HM Treasury

Points of clarification on Q471 (languages of notices issued by HMRC to MSBs and their customers on their obligations under MLR 2007)

In his evidence on 18 March 2009, David Thomas notes that Hawala dealers and other small money service businesses present unique awareness and language problems for regulators: they often operate within ethnic communities, where English is not the first language with limited contact to the wider community. The businesses themselves are less likely to be members of trade associations and may be unaware of their obligations to register with the supervisor and have AML systems.

HMRC publish two public guidance notices in English and Welsh to help businesses comply with the Money Laundering Regulations:

- “MLR8: Preventing money laundering and terrorist financing”.
- “MLR9: Registration Notice”.

They also publish an abbreviated version of MLR8, aimed at small businesses, “MLR8 at a glance—a quick guide to the prevention of money laundering and terrorist financing”.

HMRC provide guidance to businesses on compliance with their obligations under the MLR 2007 in English and Welsh. HMRC’s general approach is to provide information directed at businesses in English on the basis that a command of the language is necessary in order to operate any business in the United Kingdom.

In his evidence on 29 April 2009, Ian Pearson drew attention to the languages in which assistance is available to customers of money transmitters from minority ethnic communities. This is the form of a notice explaining to customers why they may be required to produce evidence to their identity when undertaking a transaction. Money service businesses can download from HMRC’s website a notice “MLR4—Protecting society against crime and terrorism” and give it to their customers. This is available in various languages and further translations can be requested.

8 May 2009

Supplementary memorandum (3) by HM Treasury and the Home Office

This memorandum deals with questions relating to ransom payments to Somali pirates, and the supplementary Questions from Lord Marlesford about removing Suspicious Activity Reports from the Serious Organised Crime Agency’s database.

CURRENT INTERNATIONAL WORK UNDERWAY TO ADDRESS THE PROBLEM

The Government is seized by the issue of piracy; we are taking action on a number of fronts to address the problem and exploring the most effective way of addressing the concerns of the private sector on this issue. The current legal position around the consent regime and ransom payments would mean that any guidance produced by HMG would have to reiterate that while we do not condone the payment of ransoms we have no legal instrument to prevent companies from doing so or for requiring them to report their activities, unless a link is established between piracy and terrorism. Regulated firms are well aware of their obligation in terms of receiving money that is the proceeds of piracy and there is a high level of public awareness of the nefarious

activities in the region. Maritime insurers factor the price of ransoms into their shipping insurance costs, and therefore are in a better position to price the risk of pirate attacks than the government or the FATF.

As the Chair of an International Working Group on Somali piracy (a working group on international cooperation and coordination, one of four sub-groups set up under the auspices of a UNSCR) the UK promotes full co-operation and co-ordination within the international community's response to piracy. We are engaged in identifying regional capacity building initiatives to help address the problem. In addition;

- The Royal Navy is actively participating in counter piracy activities off the Horn of Africa, as well as coming to the aid of those under attack.
- We are at the forefront of the European Union mission—Operation ATALANTA—established to escort World Food Programme vessels bringing aid to Somalia, protect vulnerable shipping, and to undertake counter piracy operations in the region. We are providing the Operation Commander and the Operation HQ at Northwood.
- The Royal Navy provides frigates to the Combined Maritime Force conducting maritime security operations in the region. As part of this, HMS PORTLAND is conducting counter piracy missions.

The EU AML committee considers tackling piracy to be a matter of security and intelligence, and the legality or otherwise of ransom payments is a national competence. As such, it is not currently considered by the Commission to be an appropriate issue for discussion in that forum. The EU supplies development assistance to Somalia through RELEX, and will continue to combat instability in Somalia through this.

FATF guidance already stipulates the circumstances under which regulated firms need to submit suspicious activity reports, including which crimes they suspect might be the predicate to the ML offence. Under FATF recommendation 1, piracy is covered as a predicate offence to money laundering, so all firms must report if they suspect that their client is a pirate or has been involved in piracy, and is laundering the proceeds of this crime. The remit of the FATF does not extend to the legality or otherwise of the payment of ransoms. The FATF recommendation for countries to impose reporting requirements on financial institutions and other businesses in the form of SARs is drafted in a way that ensures that the existing proceeds of crime are captured by the requirement.³ The recommendation does not extend to situations such as the payment of ransoms, where the proceeds involved are only criminal once they are in the hands of the individual demanding the ransom—unless they are related to terrorism. The FATF cannot therefore give guidance on the provisions countries attach to the payment of ransoms that are not related to terrorist financing.

The FATF does issue public statements on high-risk jurisdictions, which are supplemented by national advisories after each plenary. We are in consultation with international partners on the appropriateness of such a statement in this instance. Considering that such statements are generally designed to secure the engagement of governments in rectifying the deficiencies in the money laundering and terrorist financing systems, which is clearly not a plausible goal for Somalia at the moment, and that the private sector is well aware of the risks of doing business in the region already, the practical benefits of such a statement are not entirely clear.

However, some reference to the problem in the public statements of the FATF may give us leverage to require business operating in the neighbouring region to be vigilant to the issue and this is something we will continue to pursue until we are satisfied that we have fully explored the options.

SPECIFIC WORK ON SOMALI PIRACY BEING PURSUED THROUGH THE FATF

The FATF is a policy making and standard setting body for money laundering and terrorist financing. That is the extent of its remit. It is not an operational body, and does not undertake intelligence work or enforce its own recommendations. Countries participation in FATF activities always takes place through their own volition, even those in the ICRG process are not forced to initiate cooperative action in response to FATF concerns.

The FATF undertakes typologies work in order to examine different methods of laundering, rather than the kind of criminal offence that predicates the money laundering. This work is designed to identify particular vulnerabilities in the financial and other sectors to criminal abuse—which allows the FATF to ensure that its standard is sufficiently comprehensive and its members to factor in such risks in the operation of their systems. The FATF does not look at the methods used by particular groups of criminals or terrorists to launder funds—such activity is intelligence led, and would not be an appropriate subject for an open-source typologies exercise.

³ Recommendation 13: If a financial institution suspects or has reasonable grounds to suspect that funds are the proceeds of a criminal activity, or are related to terrorist financing, it should be required, directly by law or regulation, to report promptly its suspicions to the financial intelligence unit (FIU).

The FATF can only function according to its mandate and remit. Piracy is certainly on the radar of the FATF, and will be looked at within the strategic surveillance initiative, the Global Threat Assessment and the work on low capacity countries. These exercises will allow the FATF to determine the reach of the problem among its membership, and what its distinguishing features are. This preliminary information will allow the organisation to determine what further actions, if any, are appropriate.

In addition, the low capacity of the Somali government and the minimal banking system in the country would make it almost impossible to collect useful information on the movement of these funds to assist in any typologies work. Within Somalia there are vast ungoverned spaces, long coastlines with a tradition of coastal trading in small boats, multiple landing points, a few large ports and limited means to police territorial waters. Most pirates are former fishermen who have been unable to sustain their livelihood due to over-fishing in their territorial waters by boats from neighbouring countries. Gathering information on the methods by which the proceeds of piracy in Somalia are laundered is extremely difficult. Somalia is not a member of an FSRB, and has had no evaluation of its anti-money laundering or counter terrorist financing regime. The formal banking system is minimal and the state has no capacity to enforce the FATF recommendations. It is critical that the UK continues to work with the international community to tackle piracy at its root—instability in Somalia—through the provision of humanitarian and development assistance.

We have therefore suggested that FATF continues its work on promoting money laundering and terrorist financing controls in low capacity countries (LCCs) as the best means of addressing this issue through the FATF. LCC work in neighbouring countries will also help to address the problem if indeed the proceeds of piracy are indeed being laundered outside of Somalia. The Strategic Surveillance Initiative and Global Threat Assessment will enable the FATF to remain informed of the scale and impact of the problem. A further potential course of action through the FATF that we are currently exploring would be some kind of FATF statement about the problem, and we are in discussion with international partners about the utility of this.

CONSENT UNDER THE PROCEEDS OF CRIME ACT 2002 AND TERRORISM ACT 2000

The Home Office earlier note to the Committee on the law in the UK has been updated and now includes a new section on terrorist finance offences under the Terrorism Act 2000. This is attached at Annex A.

The Government did not contemplate ransom payments when section 328 of the Proceeds of Crime Act 2002 was drafted.

On the question of advising maritime insurers and others, SOCA reaches out in a number of ways on how to submit suspicious activity reports, for example through conferences and seminars, and a range of written material. In terms of understanding specific requirements to report under the Proceeds of Crime Act, reporters are assisted by industry guidance such as that produced by the Joint Money Laundering Steering Group guidance for the financial sector. SOCA also engages closely with interested parties in respect of Consent cases. As well as consulting with any interested law enforcement agencies to obtain relevant information and reach a decision, SOCA will also consult with reporters to obtain further information as required.

However, SOCA does not give guidance in interpreting legislation in respect of specific predicate [underlying criminal] activity. Its role is restricted to operating the regime set up by the legislation, and ensuring that it is functioning effectively. Nor is it Home Office policy to interpret the law; this is a matter for the courts.

On the question of prosecution for failing to obtain consent, there may have been a “reasonable excuse” for the failure to obtain consent. This is provided for by the statute. It is not general policy to try and set out scenarios that might constitute a reasonable excuse—that is entirely for the courts in each case.

There is also the matter of prosecutorial discretion and the prosecutors’ public interest test in deciding whether to prosecute—that is for the Crown Prosecution Service to decide. It is possible that the CPS might reach such an assessment even where no specific “reasonable excuse” issue has been raised.

One of the key purposes of consent is to create an opportunity for UK law enforcement to intervene prior to the transaction. Consent can only be refused to allow temporary “freezing” of the monies whilst law enforcement action is taken, namely arrests or the obtaining of restraint orders from UK courts in order to further criminal investigations. In the case of a ransom payment to Somali pirates, there are not opportunities for UK criminal investigations (nor for any overseas law enforcement agencies due to the ungoverned state of Somalia) to take action, and so any refusal of consent (ie a delay of up to 30 days of ransom payments) would be ineffective and counter-productive if it led to increased threats to life of crew members.

It has also been suggested that financial institutions should be generally required to report when they are involved in gathering money for a ransom payment to pirates. This reporting regime would be different from seeking consent to make the payment, and the value of such reports would primarily be to form an intelligence

picture of the financial flows related to piracy in order to fill existing gaps. This would of course only relate to ransoms paid with the assistance of UK financial institutions.

Such an option would require consideration of the implications not only for piracy related ransom demands but also for the generality of kidnap and ransom demands both domestically and internationally. In addition primary legislation would be needed. The current assessment is that legislation in this area is not viable. The institutions concerned would not necessarily know for what end the money was intended and, currently, we assess that that there would be little opportunity for putting the information or intelligence gathered to use in Somalia to counter piracy. We currently assess that it is more practical to address this problem through the international channels detailed above than by legislating to introduce a new reporting scheme that is likely to be of limited value.

FOLLOW—UP QUESTIONS FROM LORD MARLESFORD ABOUT REMOVING SUSPICIOUS ACTIVITY REPORTS FROM THE SOCA DATABASE

Upon receipt of a SAR, including in the event of an investigation that makes use of a SAR, steps are not taken to confirm whether the suspicion is founded or not, and it would not be practicable or useful to do so.

The Proceeds of Crime Act 2002 requires the reporting of activity that makes the person suspicious. As future circumstances unfold, including if the SAR is not used for a period of time or if an investigation is carried out which fails to produce a law enforcement result, the fact that the reporter was suspicious is unaltered. Therefore the SAR remains on the database and is available for use by the full range of end users.

SOCA is not able, or empowered, to make decisions as to whether a SAR is of value or the suspicion is founded. The legislation is framed around the suspicion of the reporter. It would not be appropriate to second guess this.

Each SAR in the database is assigned a deletion date of ten years after receipt. The deletion process happens daily—automatically deleting those SARs when the ten year date has been reached unless there have been any amendments or updates made to the SAR, in which case the deletion date is then reset to six years following that event.

Additionally, there is a process in place that allows the FIU (SOCA), based on advice received from law enforcement users of SARs, to mark individual SARs as “completed” or “closed” (ie all necessary activity relating to that SAR has been undertaken). A “marker” is then placed on the SAR for it to be automatically deleted after six years unless there have been any amendments or updates made to the SAR, in which case the deletion date is then reset to six years following that event.

SOCA estimates that 20,880 SARs have been permanently deleted from the database.

There are no changes planned to the ELMER database concerning the removal of SARs. It remains a suspicion-based regime and reporters are legally obliged to report activity they deem to be suspicious.

Finally, SOCA is not subject to the Freedom of Information Act 2000. If an individual contacted SOCA with an FOI request to establish whether they were on the SARs database, their request would be treated as a Subject Access Request under section 7 of the Data Protection Act 1998.

May 2009

Annex A

THE LAW IN THE UK ON RANSOM PAYMENTS

1. In UK law the payment of a ransom is not an offence as such, although HMG itself will not make or facilitate a ransom payment, and will always counsel others against any such substantive concessions to hostage takers. Acts of piracy, and other forms of extortion, may include a threat to life of any persons taken, and potential damage to property. The person or group of whom the demand is being made may also be instructed not to contact the authorities. Although the payment of ransom *per se* is not illegal, depending on who the money is paid to and in what circumstances, there is a possibility of a money laundering or terrorist financing offence being committed.

2. In kidnap situations there are invariably extremely testing judgements to be made between paying a ransom and not making a payment which could endanger the hostage(s) and any property held. If ransom payment was an offence it would risk criminalising families and employers who were already in the position of having to make these difficult decisions regarding the fate of the hostages. A change in the law could also discourage those of whom the demand is made from contacting the law enforcement authorities for their assistance.

PROCEEDS OF CRIME AND RANSOM PAYMENTS

3. Section 328(1) of the Proceeds of Crime Act 2002 makes it an offence for a person to enter into or become concerned in an arrangement which he knows or suspects facilitates (by whatever means) the acquisition, retention, use or control of criminal property by or on behalf of another person.
4. Criminal property is defined in section 340 as property that constitutes a person's benefit from criminal conduct or represents such a benefit (in whole or in part and whether directly or indirectly), and the alleged offender knows or suspects that it constitutes or represents such a benefit.
5. There are defences to the offence in section 328(2) if a person makes a report to and obtains prior consent from the Serious Organised Crime Agency (SOCA) (who operate the suspicious activity reporting system in the UK); intends to make such a report but have a reasonable excuse for not doing so; or the person is carrying out a function relating to the enforcement of any provision of the Act or any other enactment relating to criminal conduct or benefit from criminal conduct.
6. Money which is assembled in the UK in preparation for the payment of a ransom to pirates is not at that stage criminal property. It becomes criminal property when in the hands of the recipient. Therefore, consent may be required when assembling money in order to provide a defence to the money laundering offence under section 328(1) of the Proceeds of Crime Act. Determining whether consent is required under POCA occurs on a case-by-case basis. Where such a request for consent is made SOCA considers it in the light of Home Office guidance (Circular 029/2008) (attached at Annex B). Their decision is made on the facts of each case and the effect of their decision will be to confer, or not, a defence to a prosecution for a money laundering offence; it is not to judge the propriety of the planned ransom payment. In the event that a person did not seek consent, and the money was in all respects legal until it reached the hands of the pirates, it is unlikely that a prosecution for money laundering, solely because consent was not obtained, would be regarded as being in the public interest.

TERRORIST FINANCING AND RANSOM PAYMENTS

Terrorist finance offences

7. Section 15 (3) of the Terrorism Act 2000 makes it an offence for a person to provide money or other property if he knows or has reasonable cause to suspect that it will or may be used for the purposes of terrorism. Section 17 of that Act makes it an offence for a person to enter into or become concerned in an arrangement as a result of which money or other property is made available or is to be made available to another, and the person knows or has reasonable cause to suspect that it will or may be used for the purposes of terrorism. There is extra-territorial jurisdiction over these offences, meaning that a person could still be found guilty in a UK court if the action took place overseas (s.63).
8. The definition of terrorism for the purposes of these offences is set out in s. 1 of the 2000 Act (as amended by the Counter-Terrorism Act 2008) as being the use or threat of action which is designed to influence the government or an international governmental organisation or to intimidate the public or a section of the public, and is made for the purpose of advancing a political, religious, racial or ideological cause. The types of action that fall within the definition of terrorism are set out in s.1(2) and (3). The definition of terrorism includes action taken for the benefit of a proscribed organisation (s.1(5)).

Failure to disclose offences

9. Section 19 of the Terrorism Act 2000 stipulates a general duty to report suspicions of terrorist finance offences to the police or SOCA, failure to do so being an offence. Section 21A makes separate provision for those individuals working in the regulated sector; it is an offence not to report suspicions of terrorist finance offences to the police or SOCA. There are certain defences to these offences, including that the person had a reasonable excuse for non disclosure, and that the person is a professional legal adviser who received the information in privileged circumstances.

Defences to terrorist finance offences

10. Under s. 21, a person does not commit one of the terrorist finance offences (s.15–18) if he is acting with the express consent of a constable. Under s. 21ZA a person does not commit one of the terrorist finance offences if he has made a SAR to SOCA about the transaction or financial arrangement in question before becoming involved and has received consent from SOCA to becoming involved in the transaction or arrangement.

11. Section 21ZB provides that an offence is not committed if a person who is involved with a transaction or arrangement had a reasonable excuse for not making a SAR beforehand, and made one as soon as practicable (and on their own initiative) afterwards. Section 21ZC provides a defence for those who have a reasonable excuse for failure to make a disclosure of the kind mentioned in section 21ZA and 21ZB.

Could payment of a ransom constitute a terrorist finance offence?

12. In broad terms therefore, the payment of ransoms to individuals who are acting purely for personal gain would not constitute a terrorist finance offence. As such the issues of consent under the Terrorism Act do not arise.

13. In the case of Somalia, the existence of terrorist groups in the area is well-known. However it is not thought at the present time that Somali pirates are connected in any systematic way to those terrorist organisations. If in the future it were to become known that such a connection existed, then it might become the case that the knowledge or suspicion limb of the offence would be satisfied, ie that a person had “reasonable cause to suspect that [the money or property involved in a ransom] ... may be used for the purposes of terrorism”, and therefore an offence under ss15–18 of the Terrorism Act 2000 would be committed by the provision of a ransom payment to Somali pirates. Were this to be the case, a person would need to provide a SAR if they had a suspicion that such an offence was taking place, and seek consent from SOCA to proceed with any transaction they were involved in.

14. There is no current Home Office guidance on ransom payments and terrorist finance offences, and it is not Home Office policy to offer legal advice in specific situations. Anyone involved in the provision of a ransom payment must satisfy themselves that there is no reasonable cause to suspect that the money or other property will or may be used for the purposes of terrorism.

May 2009

Annex B

HOME OFFICE CIRCULAR 029/2008

Proceeds of Crime Act 2002: Obligations to Report Money Laundering—The Consent Regime

1. This circular contains guidance on the operation of the “consent” regime in the Proceeds of Crime Act 2002 (POCA). It has been drawn up in consultation with the Serious Organised Crime Agency (SOCA), Association of Chief Police Officers (ACPO), Association of Chief Police Officers (Scotland), the Crown Prosecution Service, HM Revenue and Customs, Revenue and Customs Prosecutions Office and others. It is being issued to ensure consistency of practice on the part of law enforcement in considering requests for consent under Part 7 of POCA. This is in response to concerns from the financial services industry and other sectors and professions that decisions are taken in an effective and proportionate way, with due engagement with all participants.

BACKGROUND

2. The Proceeds of Crime Act 2002 (POCA) created a single set of money laundering offences applicable throughout the UK to the proceeds of all crimes; these are known as the principal money laundering offences. There are separate offences of failure to disclose money laundering. These are set out in more detail in Home Office Circular 53/2005. A disclosure of money laundering or that another person is engaged in money laundering is commonly known as a Suspicious Activity Report (SAR). SARs can also be made under the Terrorism Act 2000. SARs submitted by firms in the regulated sector (defined by the legislation) reporting that another person is engaged in money laundering must be made to SOCA.

3. Under POCA individual persons and businesses in the regulated sector are required not only to report before the event suspicious transactions or activity that they become aware of, but to desist from completing these transactions until a specific consent is received. This is the “consent regime” in section 335 of POCA. A person does not commit one of the principal money laundering offences in sections 327–329 of POCA if he makes a disclosure before the “prohibited act” takes place and obtains the appropriate consent. (Under certain conditions, as set out in section 338(3), a defence can be obtained by reporting after the event). Such disclosures, or “consent SARs”, can be made to any constable or officer of Revenue and Customs. However,

current practice is for them to be made to SOCA. Where they are made to a constable or officer of Revenue and Customs they must be forwarded to SOCA as soon as practicable.

4. The “consent” provisions in sections 327–329 and section 335 of POCA have two purposes: they offer law enforcement agencies an opportunity to gather intelligence or intervene in advance of potentially suspicious activity taking place; and they allow individuals and institutions who make reports seeking to consent to proceed with a “prohibited act” the opportunity to avoid liability in relation to the principal money laundering offences in the Act.

CONSENT—THE DECISION MAKING PROCESS

5. Decisions on requests for consent to proceed with a transaction or activity (“a prohibited act”) are taken by SOCA in consultation with the relevant law enforcement agency. There is a great need to ensure that the practices of all law enforcement agencies are consistent in this area. A policy has been formulated, in agreement with key partner agencies, which sets out the high-level principles by which the law enforcement agencies should make decisions on consent, and how these principles should be applied. In broad terms it is important that law enforcement agencies recognise the potential significant impact that each report and decision can have, for example on whether or not:

- the proceeds of crime are recovered;
- crime is prevented;
- honest individuals and businesses are exposed to financial loss or litigation; and
- the smooth running of commercial business is disrupted.

6. The detailed policy is attached. It is very important that a consistent approach to dealing with requests for consent is adopted by all law enforcement agencies in order that the regime achieves its intended objectives. Against this background, chief officers of police and other relevant stakeholders should adopt and apply this policy in their organisations.

SOCA CIRCULAR ON CONSENT POLICY

This document sets out the high-level principles by which decisions to grant or refuse consent under s.335 of the Proceeds of Crime Act 2002 should be taken.

BACKGROUND

1. One of the defences to the money laundering offences in sections 327–329 of the Proceeds of Crime Act 2002 (POCA) is the making of an authorised disclosure and the obtaining of appropriate consent.
2. Further detail is available on the SOCA website, including on:
 - what constitutes an authorised disclosure for these purposes;
 - what constitutes appropriate consent;
 - the time limits within which SOCA must respond; and
 - the moratorium period before which the reporters cannot act in the event of a refusal of consent.

THE ROLE OF SOCA AND OTHER LAW ENFORCEMENT AGENCIES

3. In practice SOCA operates as the national centre for all authorised disclosures and also for the issue of decisions concerning the granting or refusal of consent. However, the majority of consent requests are of interest to other law enforcement agencies (LEAs) beyond SOCA.⁴ In such cases, the decision-making process will consist of a collaborative effort between SOCA and the other LEA, with the latter providing a recommendation to SOCA. While the final decision will be taken by SOCA, in most cases it is likely to be based largely on the recommendation provided by the interested LEA.

⁴ 54.5% of requests for consent were referred to LEAs in the year October 2007 to end-September 2008.

CONSENT—THE BALANCING EXERCISE

4. Policy on the operation of the consent regime, including on the basis for making decisions on whether to grant or refuse consent, has been developed in line with the Government's anti-money laundering and counter-terrorist financing strategy. This determines three organising principles which must guide anti-money laundering activity:

- effectiveness—making maximum impact on the criminal threat;
- proportionality—ensuring that the approach is balanced as far as possible in respect of the costs and benefits; and
- engagement—collaborative working amongst regime participants to ensure success.

5. The manner in which these three principles should be applied to the consent regime is set out below.

Effectiveness: Decision making in relation to whether to grant or refuse, including the formation of recommendations by LEAs, should be informed by the need to ensure the regime delivers law enforcement objectives in accordance with the Proceeds of Crime Act 2002. These objectives are to:

- enable suspected money laundering and other underlying criminal activity to be detected;
- prevent money laundering, and lead to the possible prosecution of offenders and recovery of the proceeds of crime which would otherwise be used to fund further crime or a criminal lifestyle or both; and
- prevent the movement of suspected criminal property for a limited period to allow such measures to be taken.

Proportionality: However, decisions on whether to grant or refuse consent, including the formation of recommendations by LEAs, are also informed by the need to balance the public interest of the impact on crime with other interests. This includes the private rights of those involved in the activity which is subject to the consent request, and those of the reporter. All parties may have contractual and/or property rights which may be affected by a refusal of consent. Officers should also bear in mind the practical implications for these parties. If the case does not prove to involve money laundering a decision to refuse consent will cause a legitimate transaction to be frustrated. The results of this might include:

- significant financial loss,
- a legitimate business might cease trading; or
- severe financial or personal consequences to an individual (for example if concerns the purchase of residential property).

The result of such a balancing of interests is that, in the majority of cases, consent should only be refused when a criminal investigation with a view to bringing restraint proceedings is likely to follow or is already under way. However consent may be refused for other reasons (for example, to permit an application for a property freezing order) subject to the outcome of the same balancing exercise.

Engagement: as well as consultation with interested LEAs to obtain relevant information and reach a decision, SOCA will also consult with reporters to obtain further information as required. In addition, when a decision has been taken to refuse consent, SOCA is responsible for actively monitoring the situation throughout the moratorium period. This is to ensure that, in cases where consent continues to be withheld, this is justified. SOCA Officers therefore engage with interested LEAs to conduct periodic reviews accordingly. In addition, SOCA will consider any reasonable request for a review by persons affected by the decision (such as the reporter).

RECORDING THE DECISION

6. Any decision or recommendation to SOCA, particularly if a refusal of consent, should be properly documented, in order to demonstrate compliance with this guidance, and to reduce the likelihood of legal dispute.

THE NEED FOR REVIEW

7. Where a decision has been taken to refuse consent, it should be kept under review during the moratorium period. SOCA officers are responsible for actively monitoring the situation throughout the moratorium period to ensure that, in cases where consent continues to be withheld, this is justified. It is equally the responsibility of the appropriate LEA to monitor any change in circumstances and to inform SOCA. SOCA will conduct

regular periodic reviews in collaboration with any interested LEAs. The potential of a refusal to have a serious impact on any party and the speed at which circumstances are changing will determine the frequency of these reviews.

WIDER APPLICATION OF THE POLICY

8. LEAs are invited to make their own recommendations by reference to these criteria. It is in the interests of fairness to all those affected, and in the interests of good public administration, that any recommendations are provided consistently with this policy and the strategic principles of the Government's anti-money laundering strategy.

Supplementary memorandum (4) by the Home Office, on SARs

1. *Which other EU Member States maintain a database of SARs?*

All EU Member States' Financial Intelligence Units (FIUs) maintain a financial intelligence database of suspicious activity or suspicious transaction reports (STRs).

2. *What exchange of information is available to law enforcement or other agencies in other EU countries?*

FIUs in the EU and elsewhere can only request a check with another FIU [FIU to FIU] if they meet strict criteria eg the check is for a financial investigation, such as money laundering or terrorist financing, and the country in question is believed to feature in the investigation. Overseas FIUs do not have direct access to the UKFIU database, ELMER.

All exchange with other FIUs is made on the basis of the Egmont statement of principles of information exchange. Conditions of use are placed on information exchange, for example, no onward transmission without the originators' approval. Information supplied by the UKFIU is also subject to a risk assessment on the content of any reply before its release, which may limit the information provided.

June 2009

WEDNESDAY 18 MARCH 2009

Present	Avebury, L	Hodgson of Astley Abbots, L
	Dear, L	Jopling, L (Chairman)
	Garden of Frognal, B	Marlesford, L
	Hannay of Chiswick, L	Richard, L
	Henig, B	

Memorandum by the Crown Prosecution Service (CPS)

1. Thank you for the invitation to respond to the call for evidence to the inquiry into EU and international cooperation to counter money laundering and the financing of terrorism. The Crown Prosecution Service (CPS) contributed to the HM Treasury submission made on behalf of the Government dated 30 January 2009 on this topic and so this document sets out the role of the prosecutor and only addresses issues on which prosecutors have particular knowledge and experience. At the request of the Attorney General's Office, the CPS has sought the views of prosecutors from the Serious Fraud Office (SFO) and the Revenue and Customs Prosecutions Office (RCPO) and their views are also included below.
2. Prosecutors contribute to the UK Government's strategy as outlined in the 2007 paper "The Financial Challenge to Crime and Terrorism" by robustly prosecuting in appropriate cases, so as to ensure that the guilty are held to account and that those found guilty are deprived of the proceeds of their crimes. This acts to disrupt criminal and terrorist activity and to ensure that crime and terrorism are deterred.
3. Since the Serious Crime Act 2007, prosecutors may apply to the High Court for civil recovery orders and appear in the magistrates' courts on behalf of law enforcement on civil cash seizure/forfeiture hearings. Prosecutors also contribute to the UK Anti-Money Laundering and Counter Financing of Terrorism (AML/CFT) strategy by:
 - Providing high quality practitioner input into draft legislation and regulations.
 - Capacity building work both in England and Wales and with partner countries abroad.
 - Supporting the work of MONEYVAL and other organisations by providing expert staff to take part as examiners for mutual evaluation processes.
 - Seconding staff to Eurojust, MONEYVAL and to other government departments and to non-government organisations.
4. The FATF Methodology states that an effective AML/CFT system requires an adequate legal and institutional framework, which should include: (i) laws that create money laundering (ML) and terrorist financing (FT) offences and provide for the freezing, seizing and confiscation of the proceeds of crime and terrorist funding; (ii) laws, regulations or in certain circumstances other enforceable means that impose the required obligations on financial institutions and designated non-financial businesses and professions; (iii) an appropriate institutional or administrative framework, and laws that provide competent authorities with the necessary duties, powers and sanctions; and (iv) laws and other measures that give a country the ability to provide the widest range of international co-operation. The Methodology also stresses that it is essential that the competent authorities ensure that the whole system is effectively implemented.
5. The 2007 FATF review of the UK found the UK fully compliant in respect of Recommendations 1, 2 and 3 and Special Recommendations I, II, and III that require a compliant legislative framework that is effectively implemented as demonstrated by effective prosecutions and prosecutors.
6. The CPS is responsible for prosecuting terrorist offences and extradition and has a specialist Counter-Terrorism Division and a specialist Extradition Unit to undertake this work. All three prosecution departments, the CPS, RCPO and SFO, are responsible for prosecuting money laundering offences.
7. Since the Proceeds of Crime Act 2002 (POCA 2002), there has been a substantial increase in the number of money laundering prosecutions.¹ The increase has mainly been the result of domestic CPS money laundering prosecutions under sections 327, 328 and 329 of POCA 2002.² These cases generally arise from domestic predicate offences, although the SFO and the Organised Crime Division of the CPS are taking forward a small

¹ Extracts from Home Office figures are set out at Annex A

² The dramatic increase in the number of section 329 POCA 2002 prosecutions was considered in the case of *CPS Notts v Rose & R v Whitwam* [2008] EWCA Crim 239 when the Court of Appeal approved the CPS approach not to routinely charge section 329 POCA 2002 in place of section 22 Theft Act 1968.

number of money laundering cases based on foreign corruption offences investigated by the SFO, SOCA or the Metropolitan Police. There have been no prosecutions in respect of terrorist financing.

8. All SFO and a significant proportion of RCPO and CPS money laundering prosecutions will involve assets that are located abroad.³ These assets are often in the form of real property or bank accounts. The CPS will generally encourage the defendant to consent to the realisation of the foreign property, or alternatively make use of repatriation orders or mutual legal assistance. A further possibility, is the use of receivers, however, this presents a financial risk to prosecutors, who must bear the costs of the receivers, if insufficient money is realised to satisfy the receivers' costs.

COOPERATION WITH AND BETWEEN FINANCIAL INTELLIGENCE UNITS

9. Generally, prosecutors only have direct contact with foreign FIUs, during the course of mutual evaluations⁴ and when assisting in capacity building work and training in the UK and abroad.⁵ Contact with foreign FIUs in respect of ongoing investigations and cases is undertaken by the UK FIU within SOCA and we are unable to comment on effectiveness.

10. The UK FIU will generally deal with investigators rather than prosecutors in respect of ongoing investigations and cases, however, prosecutions arising from SOCA's criminal investigations are prosecuted by the CPS and the RCPO.

11. The CPS Proceeds of Crime Delivery Unit has had contact with representatives of the UK FIU to discuss the concerns of the private sector in relation to the obligations imposed upon them by the Proceeds of Crime Act 2002 and the Money Laundering Regulations 2007. These concerns have also been discussed at the Money Laundering Advisory Committee (MLAC), which comprises of representatives from the government and private sectors and includes the CPS Proceeds of Crime Delivery Unit and the UK FIU. Cooperation has been effective and has, for example, resulted in SOCA guidance to the private sector regarding the use of suspicious activity reports (SARs) as evidence in criminal trials and steps that would be taken for the safety of the makers of SARs in the event that it became necessary for their identity to be revealed.

12. There is recognition by both FATF and the UK that cooperation from the private sector must be encouraged and that every effort must be made to ensure that the concerns of the private sector are addressed when possible. FATF Recommendation 31 requires that countries should ensure that policy makers, the FIU, law enforcement and supervisors have effective mechanisms in place which enable them to co-operate, and where appropriate coordinate domestically with each other concerning the development and implementation of policies and activities to combat money laundering and terrorist financing. In dealing with this Recommendation, the FATF Methodology requires examiners to ensure that countries have mechanisms in place for consultation between competent authorities, the financial sector and other sectors (including DNFBP) that are subject to AML/CFT laws, regulations, guidelines or other measures. This is an "additional element" and as such, although it forms a part of the overall assessment, it is not taken into account for compliance purposes.

EU INTERNAL ARCHITECTURE

13. Eurojust was set up by the Council Decision of 28 February 2002 to improve the coordination of investigations and prosecutions of the member states of the EU; to promote cooperation between judicial authorities regarding transnational and serious crime; and to otherwise support the competent authorities of the EU Member States to render investigations and prosecutions more effective. Each of the 27 EU Member States is represented within Eurojust by a National Member, who may be a judge, a prosecutor, or a police officer of similar competence. A CPS prosecutor was formerly the President of Eurojust and a second CPS prosecutor is currently seconded to Eurojust as the UK National Member.

14. Eurojust plays an important role in the facilitation of criminal prosecution casework in transnational cases and money laundering and crimes likely to be committed in the course of terrorist activities are specifically included in the list of Eurojust's competencies⁶. An ongoing CPS money laundering case is being taken forward through the auspices of Eurojust as a part of a Joint Investigation Team (JIT) with Denmark and

³ There are no available statistics to show the exact proportions, however, a study of CPS confiscation orders made in the first quarter of 2008 in respect of all crimes revealed that 4.5% of the 1,076 orders included foreign or hidden assets, estimated at 36% of the total value ordered. The Asset Forfeiture Division of RCPO estimated in September 2008 that 86% of the value of its unenforced confiscation orders is in respect of overseas and hidden assets. It is likely that many of the hidden assets are located abroad.

⁴ The CPS has taken part in evaluations on behalf of the OECD; MONEYVAL and the UN.

⁵ Capacity building and training has been arranged by CPS in conjunction with the FCO; the NPJA and also with international organisations, eg UNODC, UNDP, Commonwealth Secretariat, and the IMF.

⁶ Article 4.1 (b) and (a) respectively.

Holland and is benefiting from the cross-border team approach. Membership of a JIT allows prosecutors and investigators to agree which country may best take forward different aspects of a joint investigation and to decide in which countries prosecutions should take place and at what time, so as not to hamper ongoing investigations. A further advantage to prosecutors is that there is no need for letters of request for evidence to be sent to those countries taking part in the JIT. The CPS is currently considering taking part in further JITs with a number of EU countries.

15. Other prosecuting agencies have also referred cases to Eurojust for assistance. In one RCPO case concerning large scale VAT fraud and money laundering, the purpose of the referral was to spread awareness about the use of a particular bank by EU based suspects and to discuss issues of jurisdiction and prosecution venue with EU partners.

16. Prosecutors have found the involvement of Eurojust in investigations and prosecutions to be very helpful.

INTERNATIONAL COOPERATION

17. Criminal justice co-operation and the Mutual Legal Assistance (MLA) process rests on mutual obligations in bi-lateral and multi-lateral agreements as well as domestic law. The existence of this process ensures that relevant evidence can be formally requested and obtained by the competent authorities in one jurisdiction from those in another jurisdiction. The MLA process is essential in relation to cases concerning money laundering, when moving money across borders is often used as a device to not only to disguise its provenance, but also to make the job of obtaining evidence more difficult for law enforcement.

18. Prosecutors have an important role to play in seeking mutual legal assistance from foreign jurisdictions in respect of evidence for criminal prosecutions, but also in respect of restraining, seizing and confiscating criminal assets. The 2007 FATF report scored the UK fully compliant in respect of four of the five international cooperation recommendations (Recommendations 35, 37, 38, 39 and 40). Recommendation 36 was given a largely compliant rating due to concerns about the ability of the UK authorities (excluding Scotland) to handle mutual legal assistance requests in a timely and effective manner. The Home Office is addressing these concerns by restructuring the UK Central Authority (UKCA).

19. The current framework for obtaining evidence to support money laundering prosecutions is generally adequate both within and outside the EU, however, timeliness and effectiveness is also a major issue amongst some of the EU Member States in respect of UK outgoing requests and the process works more smoothly when prosecutors are directly in contact with the persons who are to provide the assistance requested. Some statistics on outgoing requests provided by the UKCA are set out in Annex B.

20. Mutual provision of banking evidence is a common form of assistance provided for by all the principal international instruments such as the Council of Europe Convention on Mutual Assistance in Criminal Matters of 1959, the United Nations Conventions against Narcotic Drugs and Psychotropic Substances (1988); Suppression of the Financing of Terrorism (1999); Transnational Organised Crime (2000); and Corruption (2005).

21. Innovative mutual assistance developments relating to banking evidence appear in the 2001 Protocol to the EU Convention on Mutual Assistance of 2000 (which itself is intended to supplement the 1959 Council of Europe Convention). The EU 2001 Protocol requires signatory Member States to provide, upon request, information on customers and information on bank accounts. The UK has ratified the EU Convention of 2000 and Protocol and the relevant provisions of the Crime (International Co-operation) Act 2003 were commenced in the UK on 11 November 2006. These provisions apply to designated and EU Member States; currently applicable to 25 EU member States but Bulgaria, Romania, Switzerland, Norway and Iceland are to be designated later in 2009 so the ability to co-operate in this way will be further extended to those countries. Anecdotal information from UK colleagues responsible for transmitting MLA requests suggests that co-operation in customer information and account monitoring remains relatively rare to date as between the UK and other EU Member States (as currently designated).

22. The EU/USA Agreement on Mutual legal Assistance is not yet in force, but it allows for the provision of customer information. Information on specific banking transactions and account monitoring are also provided for in the Council of Europe Convention on Laundering, Search, Seizure, Confiscation and Financing of Terrorism of 2005, which came into force in May 2008, but has not yet been ratified by the UK. The Home Office is leading on the development of an order in council pursuant to section 445 of POCA 2002, which will allow the use of the Part 8 investigative powers for an incoming MLA request to support a confiscation investigation and will include orders for customer information and account monitoring.

23. A significant portion of co-operation through MLA in money laundering is conducted with jurisdictions beyond the EU and is done on the basis of either the UN conventions, the Harare Scheme with Commonwealth countries, or bi-lateral arrangements, for example, the treaty with the United Arab Emirates which came into force in early 2008. These bi-lateral arrangements generally provide for access to banking documentation, but do not usually provide for customer information and account monitoring. Bi-lateral arrangements are not in place with all countries and assistance was recently obtained from a country in Central America in the absence of a bi-lateral agreement in circumstances when the number of persons involved in committing the offence meant that assistance could not be provided under the Palermo Convention.

24. The need to recast some of the current legal framework was highlighted in a Communication from the Commission to the European Parliament and the Council dated 20 November 2008 concerning the proceeds of organised crime, which advocates a change to the EU framework to ensure mutual recognition of freezing and confiscation orders, including orders based on extended benefit criminal confiscation and non-conviction based forfeiture. Generally, MLA is problematic in respect of domestic civil recovery actions. This was an issue for the Assets Recovery Agency and is now an issue for SOCA and is likely to become an issue for prosecutors in the future, as prosecutors undertake more civil recovery work. Difficulties arise from the fact that most countries do not have a civil recovery regime and some constitutions specifically preclude non-conviction based forfeiture. Further, 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, namely obtaining evidence; recognition of freezing orders and of court appointed receivers; and when enforcing against assets located abroad.

25. The CPS is contributing to a Home Office led FATF Working Group on Terrorist Financing and Money Laundering (WGTM) study on confiscation issues commissioned at the meeting at Rio de Janeiro (Brazil) on 14 October 2008, following a proposal by the United Kingdom. A Project Team has been established, chaired by the United Kingdom and the Netherlands and it currently consists of a number of FATF Members and Observers. The objectives of the project are to:

- Examine the enforcement of foreign restraint and confiscation orders and problems encountered in this area.
- Identify best practice for the management of confiscated/seized or frozen assets and effective international cooperation in asset sharing.
- Increase awareness of confiscation techniques.
- Identify issues for further consideration to enhance international cooperation in this field.

EU-UN COOPERATION—THE LONGER-TERM IMPLICATIONS OF THE KADI JUDGMENT

26. Mr Kadi's claim was that his fundamental rights had been breached by the EU, namely his right to be heard; the right to respect for property and the right to effective judicial review. He was unsuccessful in the Registry of the Court of First Instance and he appealed to the European Court of Justice (ECJ).

27. The ECJ considered three points:

- The competence of the EU Council to adopt the relevant regulations.
- The compatibility of those regulations with Article 249 of the EC Treaty.
- The compliance of the particular regulation with certain fundamental rights.

28. The ECJ found that the obligations imposed by an international agreement could not have the effect of prejudicing the constitutional principles of the EC Treaty, which included the principle that all Community acts should respect fundamental rights. The Court noted that the UN Charter leaves Member States a free choice as to the way in which they will transpose resolutions into domestic law and that this could provide the opportunity for judicial review of the legislation.

29. The ECJ set aside the first instance decision and annulled the EU regulation, but allowed the regulation to remain in effect for three months to allow time to address the defects identified in the judgment. Mr. Kadi and Al Barakaat were subsequently provided with summaries of the reasons for their listings and were given the opportunity to comment. A new EC regulation was published on 2 December 2008, which re-listed Mr. Kadi and Al Barakaat and their assets continue to be frozen within the EU.

30. The *Kadi* judgment is a clear warning that sanctions must respect fundamental rights and that if EU regulations are to be effective, then there must be mechanisms in place to protect those rights and to allow persons listed to challenge effectively their inclusion on the lists.

31. Similar fundamental rights issues were raised domestically in the Court of Appeal in England in the case of *G v HM Treasury; A and others v Same* [2008] EWCA Civ 1187, which considered whether the *Terrorism (United Nations Measures) Order 2006* and the *Al-Qaida and Taliban (United Nations Measures) Order 2006* were valid. The Court of Appeal held that the former was valid if certain words were deleted from article 4(2) so that there would have to be reasonable grounds for suspicion that the person designated was involved in committing or facilitating terrorism and not merely might be such a person and the latter was only valid and lawful as long as the designated individual was entitled to a merits based review of the case. The Court of Appeal confirmed that the High Court had power to hear an application for judicial review by a person to whom the Al-Qaida Order applied and considered that there was potentially a role for the appointment of a specialist advocate in a particular case to protect the rights of the individual, but if those rights could not be protected adequately, then the direction in respect of that individual would have to be set aside.

Jeremy Rawlins

Head of Proceeds of Crime Delivery Unit

10 February 2009

Mike Kennedy

Chief Operating Officer

11 February 2009

Annex A

MONEY LAUNDERING PROSECUTIONS BY ALL AGENCIES

	<i>Year</i>	<i>Proceeded against</i>	<i>Found guilty</i>	<i>Sentenced</i>
Total for all offences	2003	300	123	119
	2004	552	207	205
	2005	1,327	595	575
	2006	2,379	1,273	1,244
	2007	2,318	1,348	1,322
S 327 POCA	2003	29	4	3
	2004	140	39	37
	2005	392	154	150
	2006	574	300	290
	2007	502	286	281
S 328 POCA	2003	33	4	4
	2004	79	23	22
	2005	229	69	69
	2006	311	156	151
	2007	360	194	191
S 329 POCA	2003	25	7	5
	2004	186	61	62
	2005	674	343	326
	2006	1,460	801	788
	2007	1,419	850	832

UKCA STATISTICS OF ALL AGENCY OUTGOING MLA REQUESTS⁷**THROUGHPUT QUARTERLY OUT*

<i>QUARTER</i>	<i>Asset Restraint/ Confiscation</i>	<i>Coercive Evidence</i>	<i>Non-Coercive Evidence, other</i>	<i>Non-Coercive, Service of Process</i>	<i>Other</i>	<i>Total</i>
2006-1	3	2	305	39	33	382
2006-2	1	1	260	29	40	331
2006-3	0	0	328	63	22	413
2006-4	4	2	241	49	26	322
2007-1	7	1	221	87	20	336
2007-2	10	0	176	33	7	226
2007-3	3	0	229	107	22	361
2007-4	9	0	155	64	4	232
2008-1	7	1	197	112	6	323
2008-2	9	2	190	114	28	343
2008-3	8	1	184	151	92	436
2008-4	24	1	192	122	25	364

Examination of Witnesses

Witnesses: MR STEPHEN WEBB, Acting Director of Policing and Policy Operations, Home Office, MR MIKE KENNEDY, Chief Operating Officer, MR JEREMY RAWLINS, Head of Proceeds of Crime Delivery Unit, Crown Prosecution Service and MR DAVID THOMAS, Director, UKFIU, Serious Organised Crime Agency, examined.

Q120 Chairman: Good morning to our four witnesses. We very much welcome your presence with us this morning, representing the bodies some with which we have already had discussions and some we have not. At the beginning it would be helpful for the record if you could very briefly introduce yourselves so that we have it on the record.

Mr Webb: I am Stephen Webb; I am Acting Director of Policing Policy and Operations in the Home Office.

Mr Thomas: My name is David Thomas; I am Head of the UKFIU, the Financial Intelligence Unit that sits within the Serious Organised Crime Agency.

Q121 Chairman: That is SOCA?

Mr Thomas: SOCA.

Mr Rawlins: My name is Jeremy Rawlins; I head the Proceeds of Crime Delivery Unit at the CPS.

Mr Kennedy: I am Mike Kennedy; I am the Chief Operating Officer for the Crown Prosecution Service.

Chairman: Thank you. Lord Richard, would you like to start?

Lord Richard: The CPS delivered its written evidence for which we are extremely grateful—it was very helpful. But in the course of that evidence you did note that a significant proportion of domestic money laundering prosecutions involved assets which were located abroad. What major legal and practical constraints have been encountered in securing

foreign mutual legal assistance in relation to those assets? What can you do to try and increase the effectiveness of those prosecutions in cases which flow from criminal prosecutions and convictions here in the UK?

Q122 Chairman: Just before you begin, the format I think we should pursue is that the earlier questions we are going to ask you refer to the Crown Prosecution Service and the later ones are more directed to SOCA. I do not want any of you to be inhibited because the question may not directly refer to your particular responsibilities. If any of you feel having heard the lead answer that you want to come in then please signify that you do and please do not be inhibited. So perhaps Mr Kennedy would like to proceed?

Mr Kennedy: Thank you; that is very helpful. It is difficult to be precise about the proportion of assets that are held abroad relating to the restraint orders held in this country. We estimate—and it is an estimate—that of the 1760 orders we held last year about 4.5 per cent had some assets that were held abroad, but 4.5 per cent of the 1760 is relatively small. However, the value of those assets we estimate at around 36 per cent. Our colleagues—a different prosecution service but the Revenue and Customs Prosecution Office—estimate that in September 2008 86 per cent of the value of unenforced confiscated

⁷ UKCA has indicated that the above figures do not include direct transmission requests; non-legal staff are responsible for the classifying requests; and there are concerns about the reliability of the database. Many requests for MLA to support confiscation are included with requests for evidence.

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assets was held abroad, overseas. There is a range of difficulties and problems that exist, mainly to do with, on the one side, legislative issues and on the other side practical issues. There needs to be, of course, complementary legislation that will allow our investigators and prosecutors to make appropriate orders and to realise confiscation orders made in this country abroad. If there is not appropriate complementary legislation in other jurisdictions it is very difficult, if not impossible for us to make any headway. The way that we in this country now approach the problem, particularly through civil recovery, is something that is not necessarily mirrored in other jurisdictions that are not familiar with this relatively new concept. There are a range of international agreements, particularly through the EU but through other organisations as well, that have developed a framework within which this can happen. However, particularly for civil recovery the concept itself is sometimes contrary to the constitution of the country involved. So not only is it right at the very highest level very difficult to do this, even when there is an agreement or a convention or an international treaty in place, the practical application of that can be difficult because it is against the culture of the country concerned.

Q123 Lord Richard: Can you give an example of what countries you are talking about?

Mr Kennedy: A number of countries in the European Union have constitutional issues and problems; a number in South America; Bangladesh.

Q124 Lord Richard: So which ones in the EU?

Mr Kennedy: There were difficulties in France and I understand in Germany too. But that is at the legal level, the legal framework. If the legal framework does not exist then there are real problems. But even where the legal framework exists there are still the practical barriers—obviously the linguistic difficulties not just in translating requests but in actually dealing with the nuts and bolts and the practicalities of the different legal systems that exist across the European Union.

Q125 Lord Richard: So what would you want to do to try and put it right?

Mr Kennedy: We are doing a number of things, both at prosecutorial level and at the level of the police and SOCA investigators. In terms of prosecution we have focused within the Crown Prosecution Service and appointed a number of liaison prosecutors, or liaison magistrates as they are sometimes known, so that these people who are experts in our own system are appointed to work in other countries. We have appointed one to work in Madrid; we have appointed one to work in France; we have appointed one to

work in Italy; additionally we also have one in the United States and we have recently appointed one in Pakistan. This is to help facilitate our requests and to provide somebody on the ground who can deal with the legal issues and explain to the relevant and often very independent judges and prosecutors in those countries what the issues are for us, how we would like to take them forward and how they might help us to take it forward. That is one way that we are dealing with it and I know that my colleague from SOCA would like to say a little bit about the number of fiscal and other liaison officers that have been appointed to work from embassies around the world as well. We focus these particular liaison prosecutors in areas where there have been historically difficulties or lots of business, lots of request for mutual legal assistance, whether it relates to money laundering, terrorist financing or indeed other practical criminal investigations and prosecutions.

Q126 Lord Richard: Where are these prosecutors, in which countries?

Mr Kennedy: The prosecutors that I have mentioned are in Spain, France, Italy, the United States and Pakistan. These are prosecutors appointed by the Crown Prosecution Service but actually representing the United Kingdom and doing work for the Scottish legal system and not just for the Crown Prosecution Service—also for the Serious Fraud Office and the Revenue and Customs Prosecution Office in this country.

Q127 Lord Marlesford: In your interesting table in Annex A, Money Laundering Prosecutions by All Agencies, you say that the figures for 2008 are not yet available but I hope you can make them available so that we can incorporate them into the inquiry.

Mr Rawlins: These figures in fact are provided to us by the Home Office.

Q128 Lord Marlesford: The point that I really want to ask is that you have put a breakdown of the figures, the great majority out of the 6876 prosecutions you split into three categories which cover 6413. Unfortunately my ignorance is such that I am a little unclear as to what these three categories are. They presumably refer to sections of the Proceeds of Crime Act; what are the three classifications in ordinary language that you have chosen to split them into?

Mr Rawlins: Section 327 is the main act of money laundering provision, which deals with concealing or transferring money out of the country or changing the format of criminal property, whereas section 328 is the section which deals with the professionals and others who are said to enter into agreements to assist others to commit money laundering offences. Section

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329 is the offence which deals with possession and use of criminal property.

Q129 Lord Marlesford: So the biggest by far is the possession and use?

Mr Rawlins: Absolutely because if we then find someone in possession of criminal property that is the offence that covers it, unless they have done deliberate money laundering acts in terms of concealing or changing the format or taking it out of the country.

Q130 Lord Marlesford: Just following up Lord Richard's point. Are the difficulties equally in respect of all three categories or is one of those three categories more difficult than the others?

Mr Rawlins: I suppose they would be equal. In terms of section 329 that is usually on the basis of what we can show someone has in their possession, so that would be less of a problem; but definitely in terms of 327 and 328 it would not be easy to make a distinction.

Q131 Lord Avebury: You mentioned the figure of 86 per cent in relation to 2008, of assets held abroad. Is it possible that the differences are increasing because that compares with 36 per cent of assets held abroad in the previous year? I think I took the figures down correctly.

Mr Kennedy: Perhaps I was not clear enough. The Crown Prosecution Service figures for 2008 were the 36 per cent. We have been in contact with our colleagues at the Revenue and the Customs Prosecution Office who tell us that in September 2008 their estimate was that 86 per cent of the value of unenforced confiscation orders was assets held overseas or hidden overseas.

Mr Webb: So it is not comparing like with like and RCPO frauds tend to be much more sophisticated; they are often to do with these complex VAT frauds, so there is more likely to be an overseas involvement in areas abroad rather than CPS—

Q132 Lord Avebury: Maybe if you are looking at the figures in relation to one year it might be at the end of the road when you try to reclaim these assets and the 86 per cent related to cases that have been undertaken during the year and not completed by September.

Mr Rawlins: No, the 86 per cent covers all of their unenforced orders.

Q133 Lord Avebury: Throughout the time.

Mr Webb: Some of which could be very old by now.

Q134 Lord Avebury: In that case it is rather alarming.

Mr Rawlins: Whereas the CPS figure was a study over the first quarter of 2008 so any orders made within that period.

Q135 Lord Avebury: What value are we talking about? When you say 86 per cent, of what total value are the unenforced orders?

Mr Webb: The total of all unenforced orders from all the prosecutors I believe is around £600 million.

Q136 Lord Avebury: Could you let us have a note on that?

Mr Webb: Certainly, yes.

Q137 Chairman: Could we have a note on that, please?

Mr Webb: Certainly, yes.

Q138 Lord Hodgson of Astley Abbotts: Just on that last issue of Lord Avebury's question. When we get the breakdown can it differentiate terrorism from, say, VAT fraud because we are interested in the impact of money laundering as far as terrorism concerned. I am not denigrating VAT fraud but it is a completely different issue and not the subject of our main inquiry. My question is when you look at the different sections of the Proceeds of Crime Act, if I have failed to carry out a health and safety survey about asbestos regulations do I have to make a report under section 329?

Mr Rawlins: No, the reports are under section 331.

Q139 Chairman: Could you speak up?

Mr Rawlins: I apologise. The offence would be a non-reporting one.

Q140 Lord Hodgson of Astley Abbotts: No, I am reporting. I am saying to you that I am I selling my company; I have failed to make a survey under the asbestos disposal regulations; I have therefore committed a criminal offence. The value of my company is therefore £600 higher than it should be and I am therefore benefiting from the proceeds of organised crime and I have to make a report. Under what section am I making that report?

Mr Rawlins: It is section 332 and 331 that really deal with the reporting offences and the consent regime which requires reporting and these—

Q141 Lord Hodgson of Astley Abbotts: But I am possessing and using criminal property.

Mr Rawlins: If you are saying that you are possessing and using potentially there is an offence then under section 329 but that does not mean that you will be prosecuted under section 329. Clearly the CPS has a

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discretion whether or not to prosecute and you will be aware that it is a two-stage test: firstly on evidential sufficiency, but secondly whether it is in the public interest and clearly in the circumstances you have outlined it would not be in the public interest.¹

Q142 Baroness Henig: I think part of this has already been touched on possibly by Mr Kennedy, but can you elaborate on the reasons which prompted the United Kingdom to propose that the FATF undertake a study of confiscation and related issues, including cooperation? What timeframe has been established for the completion of this study and what do you hope will come out of it?

Mr Webb: In the Home Office and with Treasury and other colleagues we have done quite a lot of work attempting to analyse the criminal cash flows and such like and what that has really brought home, as you would expect, is the sheer degree to which the organised criminals in this country are intertwined with colleagues overseas. So many of the frauds, many of the trafficking offences would involve assets both here and overseas. The other thing that came to our mind particularly was the extent to which on a more mundane level it is much more likely now how even quite ordinary UK citizens will have assets abroad than they used to, with hundreds of thousands of property in Spain and France and such like. The tighter we have made the regime on the proceeds of crime and recovering criminal proceeds in the UK the more important it is to ensure that international cooperation rises in pace because otherwise there is obviously going to be a major incentive to shift assets overseas. We committed to do some work in the 2007 Asset Recovery Action Plan that the Home Office put forward and FATF seemed like an obvious helpful forum for doing this and we secured agreement in October 2008 in a meeting in Rio de Janeiro—unfortunately I could not attend! So we have a commitment for a 12-month project, which we are chairing jointly with the Dutch, who are very close partners in this area and will be taking over the FATF Presidency in April or May. We have already had a preliminary report in February and there is another one due in June. The purpose of the report is to examine practice at the moment, identify potential problems, identify best practice, raise awareness and then identify some potential areas for future action, whether in FATF or in other international forums. We see it as quite a constructive process, really just auditing the quite complex process that Mike talked about for recovering assets from one jurisdiction to another. Certainly we discussed a bit last week the overall performance on asset recovery and the

proportion we are getting back from overseas is still relatively small and that is something we would look to drive up.

Q143 Baroness Henig: We have already heard that the range of potential problems in this is very considerable. I therefore wonder what would be the UK priorities.

Mr Webb: I think the priorities we will come to later but one of the big priorities is to improve the mutual recognition in civil recovery because that is an area in which we are very interested and we are putting a lot of effort into it and yet a number of the Anglo-Saxon countries have schemes—some other countries do but 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. We also have a priority in agreeing asset sharing agreements, particularly with the countries where most UK criminal assets would be based. There are lots of complexities but equally it is in the interests of everyone not to have criminal assets in their country and if we can share the evidence and they can use their local powers to enforce it then we can come to an amicable agreement potentially about sharing the assets; or, frankly, even if we do not get a share of the assets that it is taken off the criminals is actually the most important thing.

Q144 Lord Dear: I would like to turn the light, if I can, on to civil recovery. We noted in the written evidence from the CPS of the difficulties faced by the UK in getting cooperation from the EU partners in a civil recovery context. We wondered whether you can help us as to whether the UK is affording full support to the Commission's desire to take forward discussions on this topic and whether there are any prospects for securing enhanced cooperation within the EU in this area?

Mr Webb: We are delighted by the Commission's interest in this area and we like to feel that we had quite an important role in attracting their interest. We sent a lot of experts over there to various groups to explain our system and how it works. I had a useful meeting a few months ago with Irish colleagues because obviously the Irish actually pioneered this area and we want to do as much as we can together. Mike has already discussed some of the constitutional issues that some of the countries have. For some of them it may be insuperable and others may feel it is a problem where it is not necessarily. The sort of work we have done, we have been working in EU working groups and the multi-disciplinary group on organised crime; we have also been working with Italy and the US through the G8 in their group that

¹ Jeremy Rawlins subsequently expanded on his reply to QQ 140 and 141: see p 106.

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looks at the Palermo Convention, and obviously this working paper of the Commission on proceeds of organised crime, *Ensuring that crime does not pay*, has a number of recommendations about civil recovery that are very important to us. A minor victory we secured a couple of years ago, in 2007, when we had a Council direction on the asset recovery offices, which are sort of single points of contact, we secured the agreement that their remit should cover civil recovery and not just prosecution. So that gives people the power to use this network to pass round requests in the civil recovery area. It is going to be a slow process, but there are already well understood processes for mutual legal assistance in the confiscation cases that can be made to work better. But civil recovery will be very much the next thing on which we look for more progress and it is going to be a process of awareness raising and negotiation in international forums. I think probably the way we will look to do it is first an enabling provision to assure people that there is an international framework to allow this sort of thing to happen. It is going to take a long time, I think, before we get consensus among the EU to make it compulsory to recognise these because some countries do have some concerns which will take a while to deal with.

Q145 Lord Dear: That is quite disappointing in a way because colleagues will join me I think in recognising that we often hear that sort of answer when we are dealing with the relationships between this country and Europe; and one understands that you cannot build Rome in a day but at the same time what you have said is admirable, that we are working very hard to do it. Is there anything that you can draw to our attention which would enable us to make reference within the report that would help, recognising that not everyone is travelling at the same speed? Is there anything that we could do to help?

Mr Kennedy: I think that the success of the system, both in Ireland and in this country—and indeed the United States have adopted not quite the same but a similar system, as I understand it, and the United States have negotiated a series of bilateral agreements with countries around the world to encourage them to have the same system in place in those countries so that the US can use civil recovery—I think there is an opportunity in the United Kingdom to, as it were, piggy-back to some extent and pursue the same line as the United States has pursued. The United States is often in quite a strong negotiating position and is able to secure agreements that perhaps the UK might not be able to do so easily; but there is an opportunity there to do that. There is also an opportunity to talk about the sharing of assets recovered. An incentive is

something that is always very encouraging, particularly when we are talking about such large amounts of money.

Q146 Lord Dear: So the two countries concerned would take a proportion each of the monies received, rather than it all going back to the initiating country? *Mr Kennedy:* Or not coming back at all.

Mr Webb: The default position is that it all remains in the country that enforces it, not the one that initiated the request; so an asset sharing agreement then enables something to come back to the initiating country. We have some of those with a number of key partners—the US, Canada, some jurisdictions like that—and, as I mentioned, last week we secured an agreement with the UAE. So driving forward on bilateral agreements, piggy-backing where possible with partners like the US—and that was one of the things we were discussing with Irish colleagues—would be helpful. Then getting enabling provisions through in Europe and actively working with the European Parliament and with the Commission to follow up this communication that is mentioned in your question five. We are in the best place on civil recovery we have ever been since we brought it in in this country and I think it is in the Commission's interests and that is quite promising. But it is a slow process and we are very aware of that.

Q147 Chairman: Can I follow that up? Mr Webb, do you see any chance of the Commission making new proposals during the remainder of this year?

Mr Webb: This year would probably be a little quick. I do not know if my CPS colleagues have a view on that. Not formal proposals in terms of starting a directive.

Q148 Chairman: That is what I mean. Do you see it next year?

Mr Kennedy: Can I help possibly? I had an informal lunch with Commissioner Jacques Barrot, who is the Commissioner for Justice, Freedom and Security, as I am sure you know. He was quite interested to talk about what might be possible during the remainder of his period as Commissioner, and one of the things I mentioned to him was in fact the opportunities that were being missed for asset restraint and confiscation throughout the European Union, and whilst the structures were in place there might be some things he could do, particularly at a practical level, and he is looking quite closely at setting some fairly firm objectives for Eurojust, an organisation for which I used to work, to encourage them to actually set up networks of people and packages to help develop the cooperation in this sort of area because it is something that Eurojust has not really focused on heavily during its early years of existence.

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Q149 Chairman: The Commissioner's term ends at the end of this year, does it not?

Mr Kennedy: I believe it does, yes, and that is why I think he was anxious to get something rolling before we left. Of course it is possible that he could be renewed.

Q150 Lord Avebury: What I would be interested to get hold of is some impression of the proportion of the £600 million you talked about earlier, whatever that figure is, that is attributable to constitutional or statutory difficulties in the countries concerned of the EU. First of all, is the £600 million to be broken down into EU and other? Secondly, if you are looking at the EU total of that £600 million how much of it can we effectively say is irrecoverable intrinsically because of the constitutional or statutory difficulties in the compass to which it relates; and would require this kind of blanket or universal amendment to the laws throughout the whole of the European Union.

Mr Webb: The £600 million is actually criminal confiscation orders that do not cover the civil, so there would not be constitutional bars in any of the countries. What we have already broken the £600 million or so figure down to is where there are assets that we know of in the UK that we are proceeding against; assets that we know that exist overseas; and then a category that we call hidden assets because sometimes in a criminal confiscation the level of the criminal benefit order that was secured from the court would be higher than the level of assets that we know exist. For example, if we know that a trafficker has generated an income of a certain amount and we do not know where some of it has gone we will try to secure an order to the full level of the criminal benefit that they have secured, so that if later the assets turn up we can go back and reclaim it. So quite a significant proportion of that £600 million we simply do not know where the assets are. That does fit in rather well with the point that my Lord Chairman made where what we are quite clear about at the moment is the extent to which we have international cooperation—whether it is something that needs more legislation or whether actually we have the tools already—and there is a problem in cooperation with our colleagues and that is really one of the prime reasons, as in your last question, that we wanted to do this FATF study; we wanted to look on a case by case basis and look at a sample of areas and at what are the real blockages to coordination because certainly in the criminal confiscation order field we feel that we ought to in principle have the powers already. So there should not necessarily need more legislation for us as it could be the kind of process of peer review that we have with FATF on our money laundering system that could usefully work in this area too to drive up performance. But it is something we are

quite open minded about whether we need more powers or whether we just need to make the existing system work better.

Q151 Lord Hannay of Chiswick: I want to follow up on Lord Dear's question. Surely the answer to his question as to whether there is anything that we can usefully do in this report to strengthen the move towards better civil recovery, since our report goes to the Commission as well as to the British Government, is that we should be urging the Commission, whichever Commission it is—either this one or the next one—to be more active in this area and, where necessary, to make the necessarily proposals. That is broadly speaking the answer, is it not?

Mr Webb: That would be extremely helpful, yes.

Q152 Lord Dear: Could I carry on looking at blockages in the system. The confidentiality laws that govern overseas institution financial and secrecy laws I guess would act as a significant barrier in terms of cooperation in money laundering, and you have already alluded to that, I think—both money laundering itself and terrorist financing. You have already talked about the EU; could you take us outside of it into the EEA and EFTA as well in the context of those two areas?

Mr Kennedy: I do not think there is quite the problem that perhaps there was in the past in relation to criminal offences and secrecy. Of course it is the definition of the country concerned as to what might be criminal or what might not be. Tax fraud, for example, is regarded in Switzerland as criminal so there would not be a problem in getting through the bank secrecy laws that existed there because they have a complex appellate structure which causes problems too. In terms though of tax evasion, that is not regarded as criminal within the Swiss system, as I understand it, and that is at least until the G20 last week and the meeting of finance ministers. That would have caused problems in terms of secrecy and I do not know the detail of what has been agreed, but I think we may possibly be quite encouraged by what was said there but we would need to look at the detail and see it in that context.

Q153 Lord Dear: You have mentioned in effect the definition of terms and this sub-Committee has met this problem before where different people work off different understanding of dictionaries. Would it be useful if we were to suggest that countries try very hard to have a common definition?

Mr Kennedy: Yes.

Q154 Lord Dear: It would put you all on the same playing field—a mix of metaphors—would it not?

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Mr Kennedy: I am sure there would still be problems but at least if we had the same baseline it would make life a lot easier.

Q155 Lord Dear: It should not be too difficult, surely, for countries to come to some sort of contract with 90 per cent of the definitions and have those in common use.

Mr Kennedy: One would hope so but there have been problems, as you probably know, in defining terrorism itself.

Lord Dear: We have met the problem before.

Q156 Lord Marlesford: A supplementary to your answer to Lord Dear. You made a distinction between tax fraud and tax evasion. I do not understand that; what is the distinction? Can you define the two?

Mr Kennedy: I could not promise to give a definition of the Swiss law—

Q157 Lord Marlesford: No, in Britain.

Mr Kennedy: As I understand it a fraudulent tax crime involves some sort of mental intention to defraud, to deceive the authorities. Evasion is effectively not declaring or not providing the information.

Q158 Lord Marlesford: This is the British definition, is it?

Mr Kennedy: No. I think that is my understanding; it is a British man trying to give a definition of what I understand the Swiss law to be.

Q159 Lord Marlesford: What would it be in Britain—the distinction between the two?

Mr Kennedy: Again, I am not an expert on revenue law but I understand that if one does not make a complete declaration when one completes a tax return that that is itself a criminal offence.

Q160 Lord Marlesford: That is fraud not evasion, is it not?

Mr Kennedy: It is crime. The difference I think is that evasion in Switzerland is not crime.

Mr Webb: Can I just give you an example where this has been a problem for us in terms of national cooperation where, again, in the VAT fraud, the antique fraud, it is actually straightforward theft—you are getting money back, spurious rebates from the tax people when there has never been intent to trade honestly. Sometimes we have had difficulties with jurisdictions that have seen that as is that just not another sort of tax evasion when we would argue it is straightforward theft from the Exchequer. That is something we have never had trouble with in Switzerland because they would recognise that as

theft. But this is quite a complex area for us and our colleagues from CPS. I am not an expert on tax law.

Q161 Baroness Garden of Frognal: Could I follow that on a little further, this talk of definition of terms and the slight confusion about that. Could you say what part language difficulties play within this confusion, the languages amongst the different countries? I take it that English is the language that is used predominantly; would that be the case?

Mr Kennedy: Certainly it is the baseline language across Europe that most people tend to speak if it is not their mother tongue—most people tend to speak English as their first second language or, indeed if it was not English, it would be their third language. So in my work in Europe English certainly and French to some extent—but English certainly—was the language that was used. But it is often quite difficult to describe something in English that has an exact equivalent in the legal system of another country and this is often where the confusion can arise, particularly when in mutual legal assistance or cooperation situations there is a requirement that is in the law of another country in their language—in German, French, Italian or Slovenian, whatever it might be—to actually find that equivalent in the English language definition. But that does cause a problem, particularly when we are dealing with concepts that might be completely alien to some of the systems that we are talking about across cross-country constitution. There is also a range of other difficulties to do with the accuracy of translation, for example, when requests are made, which are very practical but often are a significant torpedo to some of the requests for assistance that we receive in this country and indeed the letter that we send out. There are also very different responsibilities. A judge in this country has quite a different responsibility from a judge in France or in Germany, and a prosecutor too, and indeed police officers, particularly when we are getting into the area of money laundering and fraud and customs and tax offences, and the responsibilities can be a completely different part and not a natural equivalent part of the legal system.

Chairman: I think Lord Dear wants to come in on that issue.

Q162 Lord Dear: This may be a thoroughly naïve question and you are perfect liberty to state that in public if it is. But it occurs to me suddenly, listening to your reply to the last question, that the same sort of problem had to have been addressed in extradition proceedings, getting compatibility between the rules of one country and the rules of another. I wonder whether in looking for a solution to this we could not work off the same base, ie that if you have a definition which satisfies extradition surely the money

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laundering legislation could fall into the same set of criteria.

Mr Kennedy: I would think so but my colleague can perhaps help you.

Mr Rawlins: On money laundering we are very fortunate that there are a number of international agreements on this—and there are also of course the three money laundering directives—so in deciding what is money laundering and what an offence should include at a very minimum is quite clear. I think the issues that we were discussing earlier, the ones of taxation and the different approach taken by countries such as Switzerland to taxation, I think that on money laundering itself we are very clear what is involved and we are very clear what the minimum standard is and in the UK we have gone beyond that minimum and we would hope to encourage international partners to go further.

Q163 Baroness Garden of Frognal: If I may come on to the next question, to which Mr Webb has already referred to the document *Proceeds of Organised Crime: Ensuring that Crime Does Not Pay*. In that the Commission makes a range of further proposals for the recasting and extension of the relevant EU legal framework, which you have touched on. But I wonder which of these recommendations, if any, would be of the greatest potential benefit to the UK in the view of the CPS?

Mr Webb: I think definitely the ones about mutual recognition of the civil recovery regime. There are a number of other proposals that we would support, as Jeremy said, but in fact we have already done them progressively, some of the changed definitions in money laundering; but we have a very broad definition in our legislation already so we think that we can tick off most of the things on the list already within our existing regime. If we could get the Commission's weight behind a civil recovery regime and encourage the need for recognition and support of it that would be a fantastic benefit to the UK, Ireland and those other partners around who use these sorts of tools.

Q164 Baroness Garden of Frognal: Would there be additional resources required to make that effective?

Mr Webb: I do not think so; I think it is very much about mutual recognition of the systems. We are already doing these investigations and targeting assets in this country and we would like to be able to extend and target them to assets overseas and get them realised. Actually if you recovered more assets from that process from the same investigation it could even make savings.

Q165 Lord Hodgson of Astley Abbotts: In the CPS evidence, paragraph 21, suggests the emergence of innovative mutual legal assistance developments on banking evidence, but indicates that actual cooperation is pretty rare as regards customer information and that kind of monitoring. Could you explain why you think this is the case and would you attribute it to the fact that several of the multilateral instruments which envisage these forms of cooperation are either not in force or not widely ratified?

Mr Rawlins: I have made some further inquiries on this to find out from investigators why it is that it is not used too often, and the answer is that apparently often this kind of information can be obtained informally so that the request that is then made will be for a production order because the investigators have already discovered then where the accounts are held. Definitely, so far as the current monitoring orders are concerned, delay can be an issue. If assistance is not obtained quickly it is likely to be too late then to be looking at a particular account over a given period of time. That particular order is often used where, for example, investigators are waiting for money to go into an account to then take out a restraint order and clearly speed is then of the essence, so that may well put people off when making use of it. There are issues around whether we can get that assistance in all cases because some of the agreements are not yet fully in force, but, of course, even where they are in force within the EU there may be issues such as, like ourselves, we do not have a central database of all bank accounts which would then make it difficult to obtain that information quickly.

Q166 Lord Hodgson of Astley Abbotts: Could I follow that up at a slightly lower level? One of the anecdotal sort of evidence one gets is that firms wishing to try and operate effectively across Europe and thereby operating and talking to a reputable firm of solicitors or accountants in another European jurisdiction in order to short-circuit some of the elaborate mechanics that are envisaged, are told, informally or formally, "That is fine, go to it, but do not think that that in any way releases you from any of your responsibilities under UK law", and that therefore any attempt to try and get to a level playing field is negated because our regulators, our enforcement officers, are not interested in hearing, "I went and talked to this firm in a jurisdiction which has signed all the papers", because that is not a defence in any way.

Mr Webb: The defence to the charge of non-reporting, do you mean?

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Q167 Lord Hodgson of Astley Abbotts: What I am endeavouring to discover is, if I make reasonable endeavours as a firm of solicitors about a customer of mine and I go to a reputable firm and I am told that this potential client of mine has been checked by them and is fine, at that point I am therefore able to take them on, but they are subsequently found to have been involved in an offence. I am told anecdotally that the fact that I took reasonable precautions does not stop my firm being vulnerable to an attack for prosecution. If we are seeking a level playing field with minimum interference with our commercial activities, should that not be a defence?

Mr Webb: This is in the “Know your customer” provisions. It is due diligence under the Money Laundering Regulations.

Mr Rawlins: There is, in fact, for those within the regulated sector provision to have not made a report if objectively they should have been aware of circumstances that meant that they should have made a report (ie, providing the regulated sector is properly trained, and, of course, it is an offence to employ it if they have not been trained) and they have not made such a report, so, providing there has been training there, it ought to be possible to recognise those signs and to make a report, and if in fact those signs objectively were not there then there was no need to make a report and therefore there is no risk to the firm.

Mr Webb: If you are talking about the Money Laundering Regulations themselves, which are a Treasury and FSA responsibility, I know a lot of work has been done on the underlying guidance and firms are encouraged to do a risk-based approach, so it strikes me that if you have made all reasonable endeavours to identify the customer you would be in very little danger of any prosecution. As I say, I am afraid that is a part of the regime that the Treasury leads on rather than the Home Office.

Chairman: I take it that Lord Hodgson is quoting a hypothetical situation. If you would like to ponder over this and send us supplementary evidence I think it would be most welcome, but if Lord Hodgson wants to come back again, please do.

Q168 Lord Hodgson of Astley Abbotts: In paragraph 11 you talk about the SOCA guidance to the private sector. Does the guidance in any way refer to the reliance that can or cannot be placed upon reputable firms in other EU jurisdictions?

Mr Thomas: I will speak on behalf of SOCA. SOCA’s guidance does not include that but that guidance is out there in the shape of the Joint Money Laundering Steering Group guidance and other guidance from professional bodies. It is not provided by SOCA guidance. I think that assistance is available to firms.

Q169 Lord Hodgson of Astley Abbotts: Could we have a copy, please?

Mr Thomas: Yes.

Mr Rawlins: The Law Society has guidance of its own on this issue. As I understand it, it is updating that guidance and further guidance I am sure will be issued.

Q170 Lord Dear: Article 33 of the Third Anti-Money Laundering Directive and also Recommendation 32 from FATF both acknowledge the importance of statistical information for the analysis of the effectiveness of AML and CFT systems, and they impose obligations on parties to retain the information. As we understand it, FATF mutual evaluation of the UK has noted some deficiencies in this regard here in this country and it would help us to know, firstly, what were those concerns, and, secondly, whether they have been addressed.

Mr Thomas: I shall take that question. I was certainly interviewed during the FATF process and represented the UK at the FATF plenary. The point made by FATF in Regulation 32 was that there was in their judgment insufficient statistical information released to the public in relation to Suspicious Activity Reports.

Q171 Lord Dear: That is the feedback from SOCA back to the initiator of the SAR?

Mr Thomas: It incorporates that as well as part of the feedback and there are other statistical standards set in relation to money laundering prosecutions and convictions. Since the FATF evaluation SOCA, on behalf of the cross-agency, cross-department community within the SARs review have produced a public Annual Report. The Committee has asked for a copy of that report and we have just this morning given you last year’s report ending September 2008. It is the second such Annual Report produced by SOCA on behalf of the SARs regime as a whole. It is produced by what is known as a SARs Regime Committee which consists of SOCA personnel, representatives from the BBA, the Law Society, the ICAEW, the FSA, and law enforcement and other government departments, so it truly is a representation of all those with an interest in making the system work. The SARs Regime Committee, with its, if you like, independent cross-section overview, recommends this report to SOCA which adopts it, SOCA presents it to ministers who adopt it and then it is made a public report. Within the report, as you can see, are statistics in relation to the number of SARs received month by month, sector by sector, how many of those relate to consent, which is a particular type of SAR, those that relate to terrorism financing and have been referred to the terrorist unit

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in the Metropolitan Police, and a whole range of statistics relating to efficiency gains and various measurables about how quickly requests are dealt with, et cetera. There is also, importantly, a list of all the agencies which use SARs. That is not required under the standards but the SARs Regime Committee felt it was useful to show the extent to which SARs are now embedded in all law enforcement and other activity across the UK, and there are qualitative measures of the effectiveness of the regime in terms of quotations from key stakeholders and the like and some analytical examples. We feel that that does meet the required standards and is certainly a significant improvement on the situation prior to the FATF evaluation.

Q172 Lord Dear: Does FATF believe it meets those requirements as well?

Mr Thomas: I believe it will. We are waiting for their re-evaluation and this will be a key part of that. I am confident that they acknowledge that improvement.

Q173 Lord Richard: Do the SARs figures include Scotland?

Mr Thomas: Yes.

Q174 Lord Richard: So that is the whole of the UK?

Mr Thomas: Yes.

Q175 Lord Dear: Feedback, in essence, was a lot of what FATF was concerned with, and certainly the anecdotal evidence we get from people who labour under the SARs procedure, is that they never hear back or they hear back very infrequently about what individually is referred to the system. Are you picking up on that point? I have not read the report and I guess that this is good in generality to some extent, but would you go back specifically to the initiator itself and tell them the result of what came in from that?

Mr Thomas: In part. This is an area of work where SOCA puts in, quite rightly, much energy and resource. It recognises the importance of referring specifically back to the regulated sector within the framework of a much better collaborative environment. We have certainly made it our strategic objective from day one to improve the relationship with the regulated sector and in fact improve the relationships across all of those parties within the regime, including law enforcement, which complete that virtuous circle, if you like, of using SARs and feeding back. Having created that collaborative relationship, and I think you have heard evidence from the regulated sector about the improvement in relation to transparency, collaboration and openness, within that framework we have been able to have very grown-up discussions about what precisely will

be most useful for firms to know about, so focusing on the effects of what we give them rather than the process of giving that information. The results of that discussion are that there are two requirements behind feedback which are agreed between ourselves and the regulated sector. The first is to assure those that report that there is some utility in what they do. This goes from the micro level of an individual reporter to a whole sector. It is the same concern. You want to be assured that what they provide is of use. The second requirement is that they report in the appropriate way, describing what they are seeing in a way that is most helpful, so they want feedback in order to drive up the quality of the reports they give us. We have been running for a couple of years now a programme of activity to address those two requirements that do not necessarily require individual, one-by-one, tailored feedback. The discussions that we are having with the Law Society, which has made comments to this Committee, I know, and the BBA and the ICAEW and a whole host of others is that the programme of informing regulated sectors how the system works is helping to meet those requirements. Our measure of success, if you like, is that we want to get to the stage (and we are seeing it) that reporters are sufficiently confident now that they know how the system works, whether they hear directly or not, that the SAR has been used. It is a very healthy position to get to. I was very pleased to hear the oral evidence of the ICAEW that that sector recognises that, whether or not individual members hear. We are also sending that message about the key things to make a perfect SAR, what we would expect to see in it, the six questions of who, where, when, how, why, et cetera. I think that programme is working. All of our debates, which are not quite daily but certainly weekly, with a whole range of the regulated sector are telling us that that is exactly the right way to go about this. It certainly is positive. Having said all of that about the strategic approach which is dealing with the individuals concerned, we do also provide a degree of tailored, one-by-one feedback. You have heard about consents. You have heard evidence to say that every consent receives a reply. Contact is made by SOCA or law enforcement to the reporter. If you take the Law Society as an example of how this works, 67 per cent of all SARs submitted by the legal sector, which includes Scotland; it is not just the Law Society of England and Wales, relate to consent, receive one-to-one feedback in addition to other feedback that comes from investigators, et cetera, so it does exist. Our primary concern is to satisfy the requirements behind the feedback that reporters are confident of the SARs they use, and we are seeing that because they are used more and more, and that they understand about what sort of information is the most helpful, and I am confident about that as well.

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Q176 Lord Hannay of Chiswick: Is there now a sufficient evidence base upon which to assess the extent to which the mechanisms of international co-operation in the AML/CFT spheres are in fact being utilised (on both an incoming and an outgoing basis), and to what effect? If so, has any such detailed assessment been undertaken?

Mr Thomas: I can take that one in relation to exchange of international information on an FIU-to-FIU financial intelligence basis, so it does not cover the whole range of anti-money laundering international co-operation, but I can tell you that there are regular FIU-to-FIU exchanges of suspicious transaction information. There are 108 FIUs around the world that are members of the Egmont Group. Egmont is an international group of like-minded FIUs, although no FIU is the same, but we all have similar standards about receiving Suspicious Activity Reports from the private sector and sharing that information and making use of it. The Egmont Group has a secure mechanism for sharing and it has agreements behind that about appropriate use. I think we have provided you with some statistics on this. In 2008 the incoming requests from a variety of FIUs around the world to the UK numbered some 1,500, which was double the previous year, and similarly we have outgoing requests, which in 2008 were slightly down on 2007, and I make no comment about the relevance of that but I can say that the channels are being used. It is difficult to judge whether there is a right level and therefore the effectiveness of that. I am encouraged that it is an open channel and it is being used. What lies behind that is that each investigator within the UK and overseas makes the appropriate decision whether to seek the information and will always apply the test of necessity and proportionality, so just because the information may lie elsewhere does not necessarily mean there should be a request and does not necessarily mean it will be requested. The summary of that is that the channels are open, they are being used and are they being encouraged to be used. We do set certain criteria about the questions that the UK asks. We avoid the term “fishing expedition”. There must be a basis for making that request. We vet all of the inquiries coming in so that they satisfy the UK criteria about relevance and proportionality. We believe all valid questions that are received deserve as full an answer as possible, which we deliver. We do not have a complex or elaborate structure about tracing thereafter the effect of that exchange of information. We satisfy ourselves that it was a valid reason and that we have a duty to reply.

Q177 Lord Hannay of Chiswick: And is that Egmont network increasing in size?

Mr Thomas: Yes. Not so long ago, maybe six or seven years ago, the number was in the 20s or 30s. Now it is 108 and there is a considerable in-tray of applications to join. We estimate that there are about a further hundred FIUs in jurisdictions that are not yet members of Egmont. These FIUs operate a wide range of standards. Egmont wants to encourage the growth, wants to encourage the standardisation and wants to encourage, and is encouraging, that exchange of information.

Q178 Lord Hannay of Chiswick: Could I now go on to a specific issue which we tried to grapple with without huge success last week, which is the very large increase in illegal money transferred in the international system as a result of piracy operations off the Horn of Africa? We asked some questions of your Treasury colleagues last week about why FATF had not focused on this. For example, the FATF press release of 11 March contained a large number of items which referred to countries as disparate as Turkmenistan and São Tomé and Príncipe, but had nothing about this problem which has been, as far as we can tell, growing in scale and size for the last year or so at least, if not longer. What I would like to ask you is whether all these systems you talk about are being properly utilised in the context of the laundering of the proceeds of these crimes committed off the Horn of Africa.

Mr Thomas: The macro picture of all of the processes and the international standards does apply and will catch that which enters it. There are some cases (and some may be appropriate to the Somali pirates case) whereby the money taken by the pirates, which is then deemed to be criminal,—I think that was part of the discussions last week, that it becomes criminal once it is in the hands of the pirates, the criminals—may or may not enter the financial sector, particularly if you take into consideration the jurisdiction in which they are based. There are no formal structures, no government. It is unlikely to enter the formal financial sector. If it were to enter then it is as vulnerable as any other criminally associated money. The answer to that particular current problem is being addressed by the authorities at a global level but it may not be best addressed by using the financial sector and its controls.

Q179 Lord Hannay of Chiswick: I see. You would not perhaps explain that last remark, which struck me as a little Delphic?

Mr Thomas: I would be happy to expand on that perhaps in a submission.

Mr Webb: I suppose the point is that if the money is in cash and goes to a jurisdiction where there is really no financial centre, and there is an issue in some of the jurisdictions about taking criminal action, the

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Egmont Group will only really kick in if someone is doing a criminal action against the pirates and is looking for co-operation from other jurisdictions. We are in the position at the moment where taking criminal action against pirates is extremely difficult and where they may not be using the financial system at all once they have got the money, so it may be less productive. At the moment there has been some success, obviously, with a large deployment of naval forces in the area but in the long run we would want to get a criminal justice outcome.

Q180 Lord Hannay of Chiswick: Is there no obligation at all on somebody who, under British law legitimately pays an insurance claim which then enables the criminals to get the money; and they then as a counterpart release the ship and the crew, to notify you that this money is knowingly going to a criminal purpose even though they are themselves not committing a crime?

Mr Webb: We do owe you a formal submission on that which we are working on. My understanding is that a lot will depend on the precise circumstances of who you are dealing with and how the money is being freed.

Q181 Lord Hannay of Chiswick: I had not realised that.

Mr Webb: We promised it at the last session and we are working on that. It is quite a complex legal conundrum.

Q182 Lord Marlesford: May I follow that up, because frankly I very much agree with Lord Hannay? The letters “SAR”, as I understand it, stand for “Suspicious Activity Report”, and therefore apparently the most trivial matters are required to be reported by the regulated sector. It is to me frankly incredible that a company which is within the regulated sector can even receive a request to make payments to pirates without, under the law, having to make a report to SOCA of that fact. Am I right in thinking that that is the situation?

Mr Webb: As I say, we will try and clarify the precise legal position as much as we can. I do share people’s surprise at this. In a suspicious activity the suspicion is a suspicion of money laundering, so it all bears on whether this money is criminal property in any way. The issue is whether it belongs to a shipping company or an insurance company and at what stage it then becomes criminal property. As I say, it can vary quite a lot, depending on the precise circumstances of the case. We have very much taken on board the Committee’s surprise at this and we will try and clarify the position for you.

Q183 Lord Hannay of Chiswick: And you will cover the point that Lord Marlesford has made?

Mr Webb: Indeed.

Q184 Lord Hannay of Chiswick: Whether or not it is quite legal, is it nevertheless not bizarre that British companies do not have to notify under this system that they know this is going to an illegal purpose, even if what they do is not illegal?

Mr Webb: It is a fair point and we will try to cover that.

Q185 Lord Avebury: When you say that the money may not enter the financial sector does that mean that people use the dollar bills that they get from piracy transactions as a medium of exchange, say, within Somalia or within East Africa without it entering the banking system at all?

Mr Webb: Yes.

Q186 Lord Avebury: I must say I find that extremely surprising because you would imagine that everybody in East Africa is aware that money is obtained by pirates through criminal means and they would be rather cautious about accepting dollar bills that they think are not going to be capable of being lodged in the banking system. I am surprised that you think this money would remain being circulated in East Africa without anybody being too bothered about accepting it as a medium of exchange.

Mr Webb: Our understanding is that it is a very largely cash driven economy because there will be very considerable lack of trust in whatever financial institutions there are in that country and pirates themselves are obviously violent and armed criminals and are capable of looking after the cash themselves and they probably would not feel the need to put it in banks. At some stage, once it has gone through a number of hands, it may reach somebody who does put it in the financial system, but certainly in the initial use they could get full value for the money and they would never ever need to put it in the financial system.

Q187 Lord Avebury: Are the numbers of the bills recorded?

Mr Webb: That would be an operational matter. If law enforcement heard about it at all that would be an operational decision for them.

Lord Avebury: Do you mean that the insurance company that hands over the money is not obliged to make a record of the numbers of the bills?

Lord Richard: Not if they used one-dollar ones. A million used one-dollar bills? That is a fairly hefty transaction.

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Q188 Lord Avebury: So, even if they were not obliged to make a note of the numbers of the bills, if they did come back into the banking system no-one would pay attention to them?

Mr Webb: You would not necessarily know. That would be the position.

Q189 Chairman: I am going to move on, but before I call Lord Hodgson I want to go back to a question which occurred to me and it follows what Lord Hannay asked. If you look outside the context of the Financial Intelligence Unit, and I am thinking in particular here of the Home Office and the CPS, do you and other similar bodies keep comprehensive statistics with respect to, for instance, mutual assistance and asset forfeiture? I think it is important to know whether this is just confined to the FIU. Could you please tell us that?

Mr Kennedy: We do not keep comprehensive statistics in relation to mutual legal assistance requests that we make as an organisation. We do not have that data. They grew in the mid nineties, when the figure was in the region of 300 or so, to several thousand, if not more, at the moment, and we do not have any comprehensive data on any requests that the Crown Prosecution Service makes on behalf of investigators. In relation to statistics on financing terrorism, we do not have any data on convictions. We are setting up a database within our Counter-Terrorism Division, which is responsible for the prosecution of terrorist offences, including terrorist financing, to enable that sort of information to be more readily available.

Q190 Chairman: And asset forfeiture?

Mr Kennedy: We have data within the Crown Prosecution Service on the numbers of restraint orders and confiscation orders that are made, so in that sense it is covered.

Mr Webb: We have a joint asset recovery database that has quite a lot of data on individual orders, including, in some cases, where we think the assets may be. The UK central authority, the new database that I mentioned at last week's session, will certainly give us better data on requests incoming and outgoing and with better categorisation of the sorts of purposes for which the requests were made. In terms of "comprehensive", it is obviously going to slightly depend on your definition of "comprehensive" but we will certainly have better data in place within the next six months to a year.

Mr Kennedy: I think we have supplied some data already to the Committee about the Crown Prosecution Service's confiscation orders. The Crown Prosecution Service, as I am sure you know, is divided into 42 areas around the country. Part of my responsibility with the Director of Public

Prosecutions is to hold to account each of the Chief Crown Prosecutors for their performance, and part of their performance is a target in terms of restraint orders in relation to value and in relation to confiscation. This has proved to be quite an incentive, as I say, to ensure that performance is driven up and it has in fact increased in the past four or five years since we have been recording this data and more recently since we have had targets in this area.

Q191 Lord Hodgson of Astley Abbotts: When you come to reply to Lord Hannay and Lord Marlesford on this question about piracy could you draw to our attention any differences that occur in the case of kidnap and ransom, which is also quite a substantial activity though not so well publicised at present but nevertheless has the same sort of implications? My question is for Mr Thomas. It has partially been covered already because we have talked about a feedback and you have given us some evidence about that, and it refers, obviously, to paragraph 26 of the Treasury's notes, which talk about the improvements that have taken place. We continue to get evidence about difficulties in this area and it would be helpful if you could say a bit more about what the legal and practical constraints are for the UKFIU and how you think you could improve them. There are three areas which we have not covered before which are perhaps worthwhile looking at. First, I am told the authorities became very excited with a firm who asked for a Spanish bullfighter buying property in this country because bullfighting is illegal here and he was therefore committing a crime; secondly, under the new regime the position of politically exposed persons who are extremely hard to track down because usually you are dealing with people who are overseas—how you identify them and how you provide guidance to firms about for example, a Nigerian chief, who might or might not have a particular involvement in an unattractive aspect of Nigerian life; thirdly, UK trust law, which does not exist on the continent, where the ultimate beneficiaries to the trust are almost impossible to identify and where anecdotal evidence suggests that you are taking an unreasonably stringent approach.

Mr Thomas: Could I reverse that order and start with PEPs? The requirement to report to SOCA suspicions relating to financial activity in relation to PEPs is in place. Firms have a wealth of material, I would say, to draw upon to inform them who those people might be. There is open source material from specialist internet-based companies that provide that information. The relationship between SOCA and reporters on the subject of PEPs is healthy and good, I think, and within the last 12 months a substantial number, tens of millions of pounds, has been identified by firms that are subsequently under

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restraint by law enforcement with the intention of returning tens of millions back to the country from where it was stolen. I think the system is working well. I do appreciate it is difficult to identify all the public servants that may be in every country of the world at every level who may be involved in crooked activities, but I am confident that the financial institutions have sophisticated systems to be able to identify this; they have proved that they do so and they have proved to be providing us with the right information and action has been taken and fed back to them, so I am comfortable about where we are jointly with PEPs. What I am hearing from the regulated sector partners is that they too are pleased with that situation, so it is gratifying to know that stolen funds from an impoverished country are being sent back, and that is the UK policy. I am not sure how to answer the UK trust point. I do not recognise any point that says that SOCA or the authorities are giving anybody in the regulated sector a hard time. Just generically I do not recognise that position. We have a partnership approach. We share information that we think might be helpful to reporters and they report back what they think is appropriate. I do not recognise a particular problem so I cannot elaborate on that. The Spanish bullfighting anecdote I remember from many years ago and I thought it had gone away. I am told it has.

Q192 Chairman: Wait a minute. I have never heard of that case. Take the case of a Formula One racing driver who takes part in a road race somewhere abroad where it is legal. It is illegal in this country, with the exception years ago where there was a special law passed. If it were to apply to a bullfighter because bullfighting is illegal here, would it not also apply to a racing driver who performed on a track which he would not be able to do here because it would be illegal?

Mr Webb: It would have done in the past but we have changed the legislation so that it needs to be illegal in both countries except for serious crimes, so there would no longer be any reporting requirement on that. I was looking for the precise reference. I believe it was in the Serious Organised Crime and Police Act 2005. We recognised the sector's concern and fixed it.

Lord Hodgson of Astley Abbotts: I think there is a miscommunication about trust law that I think firms are concerned about. It is impossible to trace back a trust which is in an overseas jurisdiction in order to find out the ultimate beneficiaries but I do not think they are confident at the moment that reasonable endeavours inquiries will be accepted by you as a defence.

Chairman: Lord Marlesford, I think you wanted to come in on this.

Q193 Lord Marlesford: Indeed; thank you, my Lord Chairman. The SOCA report will be extremely helpful and I am sure we will look forward to looking at it in detail. The total number of Suspicious Activity Reports is shown as being at the present time, taking the two most recent years, something over 200,000, and therefore presumably there must have been since this system was set up at least a million in total. My concern is to get some feel from you as to how many of these turn out to be trivial matters that require no follow-up of any sort, because we have had evidence of those from some of the professional bodies and it may well be that the system is being revised so that the more trivial reports are no longer made in the way they were. We were given one example in evidence. What would help us, I think, would be if you could give us, for perhaps the most recent year for which you have got it available, what you do broken down with these 200,000-odd reports into who they get forwarded to, percentage-wise or whatever, whether they go to the police or to the Inland Revenue or to HMRC, or terrorist branches, and then how many of them are, as it were, and I am sure nothing is ever destroyed, merely filed away as being irrelevant. I suppose behind this is one's feeling that there must be the possibility of developing a system so that either some form of *de facto*, *de minimis* acceptance emerges so that people do not produce unnecessary ones, or indeed that the general rules of proportionality, which is something the EU is increasingly covering in policy matters, could apply.

Mr Thomas: I will explain how the system operates and how full value is extracted from the SARs that come in. You quite rightly said that there have been about 200,000 in the last year and that accrues into a database of some 1.5 million now, I think. The position many years ago, pre-SOCA certainly, was that SARs came in from a wide variety of reporters, and there are many of them out there with a wide range of business size and business nature reporting a wide range of different activities. These were read by analysts and decisions were made, having made checks with other databases about the potential for action, and then sent out to the appropriate law enforcement agency—a police force, as you say, HMRC, DWP or whoever it may be, and many FIUs around the world operate on that basis and that is largely enabled by numbers where it is possible for humans to deal with an in-tray and read each report. The UK has not operated like that for several years and I think as a result of that is much more efficient and effective. All of the SARs which populate the database each day are subject to immediate checks, not just those that come but again all of those in the database because new information may change the nature of an old one; that often happens. Every day during the day and overnight we have a horizontal

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washing through the database of various checks which relate to subjects, persons, companies, locations, account numbers, those things that are of particular interest to us because there is active investigation or an intelligence interest. We extract those immediately using key word searches, for example, anything relating to terrorism, anything to do with Somali pirates or whatever we happen to be looking at. They are extracted and dealt with appropriately. We also run continuously an extraction of other words that we find helpful, such as “one million”, anything with a high value. At the same time that entire database is made available to over 75 different UK agencies. When I say “made available”, it is now desk-top accessed to investigators from every police force in England and Wales, Scotland, Northern Ireland, all of the national agencies that have prosecution powers—HMRC, DWP, the Serious Fraud Office, together with other agencies such as trading standards, and some county councils. That means that whilst the FIU and SOCA are busy extracting maximum value on the more strategic serious related issues, every day there are over 1,500 trained and authorised users across the country who as their core business are examining SARs that relate to their own public duty. For example, Avon and Somerset Police will look primarily at all of those SARs in the database that relate to Avon and Somerset postcodes or persons of interest to them, and this is happening with every agency, so there is a proliferation of activity, which we have clearly encouraged, and we are pushing that out still further. We therefore are coming rapidly to the conclusion that there are few SARs with no value because of the diversity of interest. You will see in the back of that report² a range of agencies that use the database. It includes, for example, the Department for Business, Enterprise & Regulatory Reform, so when we hear of some SARs that on the face of it may seem trivial to reporters in terms of good business governance, I believe there is a value in that information and that value is drawn from it at strategic level to inform policy, that value is drawn from it to direct resources, particularly amongst law enforcement, it reveals hotspots of activity geographically, and it enables continuous use. We have found that a single SAR, and I hope you find this helpful, is often used several times by several different users for different purposes because the information within it informs HMRC about taxation, it may inform local police about fraud or theft, it may inform a government department about another issue or a weakness in a financial product or whatever it might be. SARs have multiple uses and they very rarely become time redundant. We are seeing usage of SARs become relevant many years

after the date they were lodged, and I am very encouraged by that. There is no concept of an in-tray, “Is this actionable or is it not?”, “How many are in the non-actionable box?”. It does not work like that, I am pleased to say. Statistically, measuring all of that activity is almost by design difficult. It is the price to pay for such proliferation of use and I would not necessarily be keen on introducing new processes to track all of that activity because it may serve as a disincentive to action. We are in a good place. We cannot answer all the questions but we are getting closer to understanding the value of the regime.

Mr Webb: If I could just take an analogy from another area I am responsible for, the more these reports become mainstream the more difficult it is to say precisely what results come from any individual report because it would be one of a whole range of investigative tools used. CCTV is another thing I am responsible for and it is used in so many police investigations now that I would not like to answer how many convictions have been achieved as a result of CCTV; it is very difficult to say. CCTV will be looked at in hundreds of thousands of investigations and will play a varying role, sometimes peripheral, sometimes absolutely crucial, and there will be a huge burden on the police to ask in every case, “What was the key bit of evidence in this case?”. It is important but the more mainstream it gets the harder it will be to give you good answers on that sort of subject.

Q194 Lord Hannay of Chiswick: Regulation EC 1889/2005 on controls of cash entering or leaving the Community envisages that relevant information will be made available to national FIUs and may in appropriate instances be shared with similar bodies in other Member States and third countries. How has this worked in practice to date and has it been of value to the UK’s FIU? Perhaps I could ask you to take into account a continuing theme of our inquiry, which is: is the playing field level? Are all Member States operating these controls in a reasonably harmonised and serious way? Secondly, if the answer to that is no, does that put the UK at a disadvantage in being reasonably rigorous itself or, as some of our witnesses have suggested, does it, because of the very great importance to the UK of its own financial sector, mean that we need to be rigorous however good or bad the level of co-operation elsewhere in the EU is? If you could cover those questions it would be very helpful.

Mr Thomas: In terms of the decision relating to cash declarations collected at the border and being provided to national FIUs, HMRC do provide cash declaration data to the UKFIU and we value that. I will expand on that shortly. I just want to add that the context of that is that we do more than compare cash declarations with the FIU material. We have a very

² The SARs Annual Report 2008

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good relationship with the UK Border Agency and HMRC and examine closely all cash cross-border movements. All cash seizures we debrief and get intelligence from those. SOCA and HMRC issue intelligence assessments to our partners nationally and internationally, so we do share our findings and our judgments at strategic and tactical level with international partners. Turning to the data around the cash declarations, we have received during the period June 2007 to March 2008 2,076 declarations from 1,904 travellers. This was the first tranche of data from HMRC. We compared that with the full SARs database and found that we had 812 accurate matches on travellers, so those that have made cash declarations have also been the subject of SARs. In fact, 971 travellers have been the subject of SARs and 23 per cent of those appear in more than one SAR, which is the cumulative intelligence value. What does that mean? It is still subject to much analysis but I can say that so far 13 individuals have been referred to the Metropolitan Police in relation to suspected terrorist financing, so that alone I think is significant value. Five travellers who made declarations we now know are subject to law enforcement activity in relation to drugs, corruption, fraud and other matters, and there have been several international ones, including those relating to suspected corrupt politically exposed persons, and we are sharing that information with our EU and non-EU partners. That is now an embedded process whereby HMRC, the UK Border Agency and SOCA share and circulate that intelligence. Is that happening equally and at equal pace throughout the EU? I do not know accurately but I feel confident enough to say I do not think so. It is much like other parts of cross-EU controls: things move at different paces.

Mr Webb: But we are not imposing any more burdens on the actual travellers at the frontiers than anyone else is doing. It is just that we may be doing more with it when we get the declarations in.

Q195 Lord Richard: In its report of December 2007 on the implementation of the Council Decision on co-operation between the FIUs the Commission identified some difficulties in the implementation of Article 4(2). They said that “many administrative FIUs cannot exchange police information or can provide such information only after a long delay”. What has been the experience on that? What steps have we taken to try and address the issue? Thirdly, is there a need for the Council Decision to be amended and, if there is, how would we amend it?

Mr Thomas: I recognise that description. Just looking wider than the EU for the moment, I talked about 108 FIUs across the world. They are all structured and formatted in different ways, 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. The UK’s experience is that we understand the limitations of administrative FIUs in obtaining and sharing law enforcement information. The UK is fortunate in that the UKFIU is within SOCA, our law enforcement agency, and therefore we have very close links with all law enforcement agencies across the world, particularly in Europe. We are the Europol UK office. We have European law enforcement officers in London and we have officers throughout the EU, so the practical implication of this difficulty is that we obtain the information we need through another means with some minor inconvenience but it is effective for the UK.

Q196 Lord Richard: It is a European solution?

Mr Thomas: Yes. The service that the UK provides to administrative FIUs is that we share with them all our enforcement information, so they get an enhanced service. In the light of that would I or SOCA think that there is a requirement to change the Council Decision, which would require substantial legislative and structural changes? I think not. For the UK it works, as much as it can.

Q197 Lord Hodgson of Astley Abbots: Paragraph 8 of the Treasury notes talk about the establishment of SOCA’s liaison officers which includes five liaison officers who engage with host country FIUs to develop financial intelligence. Could you give us some background to this? Are they of any value, where are they, are we going to add more, and what is the cost of them?

Mr Thomas: The development of financial SOCA liaison officers is reasonably recent, within the last 12-18 months, and it augments an extensive SOCA liaison network around the world. The purpose and role of these financial liaison officers is quite broad relating to criminal finances. It is to improve intelligence flows. They are there to improve operational activity between those countries and countries in the region that they also cover, and SOCA and UK law enforcement. They also operate on policy matters such as sharing agreements and a whole range of things to improve the UK’s reach into criminal finances overseas. They operate in North America, South America, Europe and the Middle East. How effective are they? They are effective in a whole range of things. One measure, although it is not a description of their total effectiveness, is that between April 2008 and January 2009, ten months, they were responsible for denying to criminals

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overseas £79 million worth of assets. These are assets held overseas in the possession or control of overseas criminal groups who have active links with UK crime. This is not money that is counted in the UK statistics about assets recovered but is impact in taking money out of crime groups that facilitates crimes in the UK. We are very content with that activity so far and the other activity in terms of relationship building and intelligence gathering, and we are certainly going to expand our reach in this field. This may be an expansion of specialist financial liaison officers; we are reviewing that, or it may be expanding the role of the existing network of liaison officers to include this work, but certainly we are increasing our efforts. The cost I do not have to hand. Officers overseas are expensive. I hope I have outlined some of the value they bring back. We see it as very cost effective. I can provide that.

Q198 Chairman: You referred to criminals and criminal groups. How do you define those?

Mr Thomas: Criminal groups are those criminals who are known by us and the host country where they are operating to be engaged in serious crime such as significant drug trafficking, human trafficking and the like, that impact directly on the UK.

Q199 Chairman: When you say “known”, do you really mean “suspect”?

Mr Thomas: I mean “suspect”, occasionally proved in prosecutions overseas.

Q200 Chairman: So those people you are pleased to describe as criminals or criminal groups are just suspected of being involved in crime?

Mr Thomas: Thank you. That is my terminology. “Suspected criminals”.

Q201 Lord Hannay of Chiswick: In what manner and to what extent does the FIU.NET system, hosted within the Ministry of Justice in The Netherlands, reinforce operational co-operation within the EU? What further developments in your view at UKFIU are required for FIU.NET to achieve its full potential?

Mr Thomas: FIU.NET is an IT network to allow EU FIUs to exchange information. There is a parallel network in the Egmont Secure Web that links all FIUs, including the EU, so FIU.NET is, as you know, an EU initiative to link EU-only FIUs. I have to say that my assessment of that is that it is still a rudimentary tool. I know that some EU FIUs use it to a great extent and are very happy with the service it provides. It does not meet the UK’s requirements. It is not sufficiently sophisticated to match the operations and intelligence operations that we run. We are committed to making it work and the UKFIU

sits as a member on the board of partners, the strategic group, to ensure that FIU.NET moves forward in a helpful way. From the UK’s perspective we are not extensive users, I have to say. We do not feel ourselves disadvantaged by that because there are other networks open to us to exchange information but we are engaged strategically and in terms of finance in making that work.

Q202 Lord Hannay of Chiswick: Thank you very much. Does this imply that you do not think that there is a straightforward duplication of effort in having FIU.NET and the Egmont net working, as it were, side by side? You do not think that is a complete waste of time? You think that FIU.NET amongst EU members only has a real, useful purpose; the only problem is that at the moment it is not fully effective? *Mr Thomas:* That is absolutely it. I do see a real and discrete purpose within the EU.

Q203 Lord Hannay of Chiswick: Could you perhaps explain why that should be when Egmont already exists?

Mr Thomas: Egmont is a system that has evolved over many years and is many things. It is an exchange of information which satisfies at basic standards. It also serves as a posting site, an email exchange. It can be over-cluttered. It is a multi-purpose tool. FIU.NET seeks to deliver, and I think there is a requirement for it to deliver, a sophisticated solely intelligence-sharing network across the EU and for that to lead to direct action. Egmont Secure Web assists that but does not address it.

Q204 Lord Avebury: Is it possible for us to have a note on what the changes would be to FIU.NET to make it fully effective as far as the UK is concerned?

Mr Thomas: Yes.

Q205 Chairman: And at the same time could you tell us whether it is a disadvantage that not all European Union members participate in FIU.NET initiatives?

Mr Thomas: It will be a disadvantage once it is a fully functioning effective tool. I think some Members are holding back to see how FIU.NET develops before they commit to it, but once it continues on the path of development it would be clearly advantageous for all EU Members to be connected to it and use it.

Q206 Chairman: How many do not participate now?

Mr Thomas: I am not sure exactly. I believe it is around six or seven. I would need to verify that in a submission.

Q207 Chairman: You can perhaps let us know at the same time as you reply to Lord Avebury’s questions.

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Mr Thomas: Yes.

Q208 Lord Dear: Mr Thomas, I am sorry; there is no respite because the next question is for you too. You probably do not know but this Committee as a Sub-Committee recently looked in depth at Europol and that makes us even more interested to know how you think Europol performs in this area.

Mr Thomas: SOCA has a particular position in Europol, being the UK office, of course, in everything that Europol brings to the world of law enforcement, its very structure, its IT capacity and connectivity between countries. Its experts are drawn from different Member States. It also brings that expertise to the world of anti-money laundering and to a lesser extent terrorist financing, but it is valuable in terrorist financing, so there is certainly a role for it to play. The UK contributes to the intelligence submission to Europol's overall picture. We draw from it. We contribute to the thinking about continuous improvement, as we do to many things, particularly around Europol's approach to wider intelligence gathering as well as co-ordinating and driving operational activity, which it does very well. SOCA would like to see an expansion of its organised crime threat assessments work towards perhaps an EU control strategy expansion and publication of an EU intelligence requirement.

Q209 Lord Dear: Would that be a redefinition of terms or an injection of extra resources?

Mr Thomas: I think it fits within the existing terms. We are not proposing that that would require extra resources. It is very similar to what the UK has done in shifting impetus in order to understand crime more and then make judgments about how best to act as a result of that.

Q210 Lord Dear: Has SOCA already made that sort of suggestion to Europol and not been successful?

Mr Thomas: It is not that we have not been successful. It is part of our dialogue with Europol.

Q211 Lord Dear: But you intend to do it again in the coming year?

Mr Thomas: Oh, absolutely, yes.

Q212 Lord Avebury: Can I ask you about the Hawala system which, as you know, we have touched on with other witnesses, and what particular problems this poses for us in relation to AML/CFT strategy? Could I point you in certain directions? Is not the fact that there is a lack of visibility with transactions an incentive to people who are engaged in criminal activities to use Hawala as opposed to conventional systems? Is it a fact that we receive no SARs in relation to Hawala and other

unconventional systems of money transfer, and, if that is so, would that not be a hint to the law enforcement agencies to take a closer look at these systems?

Mr Webb: Shall I give you a general view of the regime and then maybe pass on to SOCA for some specifics? Hawalas are regulated by HMRC because HMRC would regard these all as informal money transmission and they fall to be regulated in the same way as other money service bureaux. They do have to be registered, therefore, and the directors would have to be subject to passing a fit and proper test and have training procedures in place to comply with the Money Laundering Regulations. There has been quite a lot of activity between SOCA and HMRC on raising awareness among areas where Hawalas and other informal systems are being used a lot, and not just awareness raising. There has been a fair bit of enforcement. There was a major operation that you may have seen in Bradford last year that targeted this area, first raising awareness and then doing some enforcing operations on compliance. I think it is fair to say that there are some problems with the sector, often because they are very embedded in certain ethnic communities, which means getting awareness among them is that much more of a challenge. There can sometimes be language issues with them. Finally, the process that often happens of netting off money between the agent in the UK and the agent abroad means that actual transactions are that much harder to trace through the system. There may not be a particular flow that you can see coming in the door of the UK and out the door on the other side. Finally, the fact that their agents overseas are often unregulated, unknown to the authorities and in some cases potentially questionably legal in some countries again makes that other end of the network that much harder to do. One of the emphases in relation to enforcement operations has been to impress on people the importance of making Suspicious Activity Reports when they have due suspicion. There have been some successes in this area but it is clearly still an area we need to keep a very close eye on. As I say, there are some very obvious vulnerabilities in it.

Mr Thomas: This is not an area that is off the radar of law enforcement and our knowledge of how the system operates and who operates it within the UK is quite well developed. There are SARs received from that sector.

Q213 Lord Avebury: Could you give us an indication of how many?

Mr Thomas: Yes. In the SARs that are submitted the submitter describes himself or herself. Very few come in saying, "I am a Hawala trader". We have SARs from money service businesses, money transmission agents, those that operate in greengrocers, butchers,

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newsagents that provide that service. These are caught by the provisions. They do submit some SARs. I do not readily make a differentiation between what might be Hawala and what is a money transmission agent. It is the same service. They do provide SARs, we do find them helpful. The difficulty that we have, as Stephen has mentioned, is finding a representative body that will enable us to push out the messages we want to push out. Our real concern here is that these are business people who are themselves vulnerable to abuse by criminals. Our focus is on suspected criminals abusing them, not so much on the businessmen that provide the service, so our concern is that they are vulnerable and we do find them hard to reach. That is principally because there is not a BBA, there is not a Law Society. There are some associations. The Money Transmitters' Association is a very close partner of ours. Their members are the larger firms and not the individuals that operate in retail premises, so we have a programme that I entitled "The Hard to Reach Sector", which includes these people. That demonstrates to you our determination to give them information that will help them protect themselves. We run road shows and conferences in city centres and we invite small and medium sized businesses to them. We recognise that gap and we are reaching out to fill it.

Q214 Lord Avebury: Can I ask you whether you reach out in other languages, and particularly in Urdu, and whether it is your impression that there are hundreds, if not thousands, of these small greengrocers and similar businesses which are operating informal money transfer arrangements without having the faintest idea that they are required to report suspicious activities?

Mr Thomas: We do not yet provide other language information.

Q215 Lord Avebury: Do you not think you ought to?

Mr Thomas: We certainly should be thinking about that, yes, as part of our outreach. How many are there? Certainly hundreds but we really do not know. However, we are determined to reach them because we are determined to help them and inform them, and we are trying a number of channels. The language may be an inhibitor.

Q216 Lord Hannay of Chiswick: Do you have any evidence that terrorists or people you suspect of being terrorists perceive this as being a weakness in the system and are trying to capitalise on it, or have you have no evidence of that at all?

Mr Thomas: The information that we have in relation to terrorist financing across the board shows that suspected terrorists and those associated with them

use a broad range of services, including by-passing the services and taking cash overseas. There is nothing to indicate a general gravitational pull towards these providers but they are vulnerable.

Q217 Chairman: To wind this session up I have two more questions. The first one harks back to Lord Dear's question about Europol because I cannot resist the temptation, having a former President of Eurojust here. We did refer to Eurojust and its relationship with Europol in our report. I wonder if you feel, now we have got you here, that there is potential for greater contribution by Eurojust in this whole sphere that we have been talking about.

Mr Kennedy: I do. I think there is a huge opportunity. In terms of the types of cases referred to Eurojust in the first five years, each year has always included a majority of fraud and fraud-related cases. The focus seemed to be, perhaps for obvious reasons, on dealing with and encouraging referrals of cases and consequently focusing on helping in terrorist cases, helping in drug trafficking cases and helping in people trafficking cases, but I think there are some real opportunities that need to be seized, not just by Eurojust but by Europol as well. The two should be working much more closely together. During the time I was there the Director of Europol and I and colleagues in both organisations were trying to develop a much closer practical arrangement so that the information that was being sent to Europol and analysed there, as David has said, which needed quite sophisticated analysis to capture it almost, was actually bearing fruit and was being shared, not just with those who were contributing to Europol but also with the prosecutorial side and the judicial side, using the European understanding of the *expressio*!. I think there is a great deal of potential for using both organisations to bring together practitioners dealing with these cases to design good practice, not just to build networks of individuals who know each other but to talk about the problems and identify the problems that exist in practice, because no matter how wide and how detailed the agreements are that are reached internationally between governments, the practical implementation of those agreements often leaves a lot to be desired, for a whole variety of reasons, and the more we can get police superintendents working with instructing judges, forgetting the professional barriers that exist, the better that is for effective investigations and ultimately prosecutions.

Q218 Chairman: I am most obliged. Could you tell us about what data protection safeguards apply to the information which you process further to the Suspicious Activity Reports and what is the retention period for those things in SOCA?

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Mr Thomas: Let me deal with the safeguards first. It was a key concern of the regulated sector about the appropriate use of the SARs that they submitted to us confidentially. The SARs review produced by Sir Stephen Lander at the outset of SOCA undertook to address the data protection and safeguarding that material. We have a number of safeguards in place which I am very happy to run through. The outcome of those safeguards in place is that the regulated sector members of the SARs Regime Committee, the key stakeholders, have said in the Annual Report that any previous concerns of vulnerability in terms of the appropriate use of their data have now diminished. They are satisfied with the measures that SOCA and our partners have in place. That relates to securing the data on a secure database with only authorised password user access, et cetera. There is a Home Office circular that dictates the use of this data and protects the confidentiality of it and the identity of those that make it. The effectiveness of that circular, as well as making clear the data handling provisions, is that it is a disciplinary offence to mishandle such data, so all of the users in law enforcement and other agencies take this very seriously and have their own internal mechanisms to protect and safeguard the data and the reporting sectors are content with that. With regard to the retention period, there is a ten-year review period. We have deleted SARs from the accruing database. In practice what that means now is that we link new incoming SARs to any existing SAR. It might be linked to the person and address and account number, it might be any linkage to an earlier SAR, and the most recent SAR becomes the relevant data for review because there is clearly value in that existing material. We have also looked at the criteria which include where there has been a recent law enforcement inquiry or added intelligence from law enforcement that links to a previous SAR. The nucleus of information becomes the relevant data. In summary, despite the prolific use across the country by all these agencies, the material is safe and proven

to be safe. Just as a check on that, SOCA has opened up a confidentiality hotline to check on ourselves. It is a public line that is available to any reporter to ring in to an external agency to report any inappropriate use, any breach of confidentiality, real or perceived. SOCA undertakes to investigate that and report it publicly in the interests of transparency, and where there are any systematic failings in any agency we undertake to put that right together with Her Majesty's Inspectorate of Constabulary. So far, in the first year of operation, there have been six reported breaches. Last year there were two reported breaches, leading to the added confidence of reporters. I hope that is helpful.

Q219 Lord Avebury: If we connect this with what you were saying earlier about the increasing rights of access to the SARs database by organisations such as local authorities, do you obtain the approval of the Information Commissioner every time there is a new class of persons granted access?

Mr Thomas: The class remains the same. It is those that have prosecution powers under the Proceeds of Crime Act. There are some peculiarities within some councils which have prosecution powers. If we were to broaden the classes then yes, most certainly, but it is still within the same classification.

Q220 Lord Marlesford: Do you have a linkage between your database and the Criminal Record Bureau?

Mr Thomas: There is no automated linkage but there are cross-checks being made, so we are in conversation with them and we hope we are doing the right thing but there is no automated linkage.

Chairman: Thank you. I think that brings the session to a close. I want to express the Committee's warmest thanks. You have been extremely interesting and extremely patient with us, if I may say so, and we hugely appreciate the information you have shared with us. With those thanks I close this meeting of the Committee.

Supplementary memorandum (5) by the Home Office

Further to the Home Office evidence of 18 March in response to Q136 and Q137, this memorandum provides further details of unenforced confiscation orders.

Broadly these can be split by agency and by where the assets are held. This is set out in the table below based on data collected mainly in October 2008.

<i>Agency</i>	<i>Outstanding orders (£m)</i>	<i>Assets hidden (£m)</i>	<i>Assets held overseas (£m)</i>	<i>Identifiable and UK based assets (£m)</i>
Crown Prosecution Service (Organised Crime Division)	131	51	34	46
CPS (Areas)	42	7*	2*	33*
Serious Fraud Office	58	16	41	1
Revenue and Customs Prosecution Service	240	157	50	33
Her Majesty's Courts Service	64	23	2	39
Total	535	254	129	152

*Estimates

Outstanding assets fall broadly into three categories and some outstanding orders might consist of all of them.

First, there are those assets that are readily identifiable and UK based. Recovery of these assets can be carried out using the full range of enforcement powers.

Secondly assets can be held overseas. There are two ways in which we can attempt to recover such assets. The first is to seek Mutual Legal Assistance from the country where the assets are located to enforce our order. In such a case, unless an asset sharing agreement is in force or an *ad hoc* asset sharing arrangement is entered into, the enforcing state will retain what is enforced. The second method is for an enforcement receiver, appointed by the English Court, to secure the recognition of his appointment in the foreign state and then to exercise his powers there. Whilst the advantage of this method is that the receiver will pay what he realises into the enforcing magistrates' court here, the receivers' fees can be substantial and they are met from the sums that are realised.

The final group is hidden assets. It is likely that a significant proportion of hidden assets are located overseas. Where the offender has hidden his assets and refuses to co-operate in realising them for the purposes of satisfying the confiscation order, the only remedy available is the default sentence of imprisonment. Its length is fixed when the confiscation order is made and it is activated by the enforcing magistrates' court on a finding that the order has not been paid and that other methods of enforcement will not prove effective.

In terms of the age of the orders, there is no data readily to hand. However a confiscation order once made is an order of the court and can never be written off as bad debt, although that there are European Court decisions to the effect that an order that is not enforced within a reasonable amount of time may be unenforceable.

The age of an outstanding order may not in itself be particularly helpful in understanding the effectiveness of enforcement in large order cases. Enforcement can be delayed for a long time as a result of, for example, appeals, third party property claims and matrimonial claims.

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Supplementary memorandum (1) by the Crown Prosecution Service (CPS)

The Sub-Committee has made 16 requests for further information and has asked that if in relation to any of the matters requested, statistical data is not held, that an indication of the frequency of use (with illustrations where appropriate) should be given and an explanation of when/if the defect in record keeping will be addressed.

The matters of interest to the Committee are as follows:

(1) *The total number of money laundering prosecutions and convictions*

Please refer to Annex A below, which sets out data provided by the Home Office for calendar years 2003 to 2007. Data for 2008 will become available by the end of this year.

The following data has been received from the Crown Office and Procurator Fiscal Service (COPFS):

<i>YEAR</i>	<i>PROSECUTIONS</i>	<i>CONVICTIONS</i>
2006	7	12
2007	7	8
2008	2	2

There are currently a further four cases indicted and with trials pending for a total of 16 accused and one case not completed where two of four accused have pled guilty in the last month to money laundering charges and are awaiting sentence.

There were two further prosecutions in 2007 where the accused were not found guilty of money laundering, but were convicted of drugs and fraud offences.

(2) The total number of terrorist finance prosecutions and convictions

The CPS is developing a central database to store this information and the database is expected to be operational shortly.

In 2007, the CPS prosecuted three defendants, who pleaded to offences contrary to section 17 of the Terrorism Act 2000. A further defendant pleaded to murder and conspiracy to defraud, which was terrorism related.

In 2008, the CPS successfully prosecuted four defendants, who were convicted of inviting funds for terrorist financing contrary to section 15 of the Terrorism Act 2000.

(3) The number of money laundering convictions secured where the proceeds had been generated by offences committed abroad

Current IT systems do not record this information and there is no available collated data either at a national or agency level showing the number of money laundering convictions secured in respect of predicate offences committed abroad. Prosecuting agencies are reviewing what data is collated for case management and management information purposes and will consider what further information may be collected.

It is not uncommon to prosecute money laundering offences in respect of proceeds generated by foreign offences. The CPS is concerned in a number of ongoing investigations and prosecutions in respect of foreign Politically Exposed Persons (PEPs) arising from predicate offences of corruption committed abroad.

The CPS has an ongoing case in which a defendant has been convicted in the UK of laundering the proceeds of a drug importation into France committed by the defendant's spouse.

Operation Upsurge in 2006–07 concerned a defaulting (VAT) trader fraud in Denmark where the proceeds of the fraud, amounting to approximately one million pounds, were laundered (via bank accounts in Hong Kong) to the account of the UK defendant company's bank account in the UK. The RCPO restrained the account in the UK and the monies were eventually repatriated to Denmark following civil proceedings. In Denmark the defendants were convicted of the VAT fraud and in the UK the defendant company and co-defendants were convicted of money laundering contrary to the Proceeds of Crime Act 2002.

The COPFS report that they know of none.

(4) Any known instances in which foreign money laundering convictions had been secured in instances in which the proceeds generating activity took place in the UK

There is no available collated data either at a national or agency level showing the number of foreign money laundering convictions secured in respect of predicate offences committed in the UK. Prosecuting agencies are reviewing what data is collated for management information purposes and will consider what further information may be collected.

The UK will generally not be aware of foreign money laundering prosecutions based on UK predicate offences unless Mutual Legal Assistance (MLA) has been provided and even then the UK will not generally be aware as to whether such a prosecution was successful, unless there is a further request for MLA to confiscate assets that remain within the jurisdiction.

The CPS and SFO are co-operating in a number of ongoing foreign money laundering investigations and prosecutions in respect of PEPs, for which the predicate corruption offences were committed in the foreign states and the money laundering took place in the UK.

Co-operation has also been provided to the Dutch authorities by HMRC/RCPO in relation to ongoing regulatory and money laundering proceedings in the Netherlands arising from UK VAT fraud activity. Proceeds are believed to have been laundered in the Netherlands Antilles. Eurojust facilitated discussions on jurisdiction and prosecution and it was agreed that the Dutch authorities were in the best position to take the case forward.

The COPFS report that they know of none.

(5) The number of instances in which the English (and if possible Scottish) courts have given effect to foreign confiscation orders, and their value

The Joint Asset Recovery Database (JARD) contains the details of domestic restraint and confiscation orders. Unfortunately, it is not currently able to record payments made to the High Court in respect of the enforcement of foreign confiscation orders and so has not been used to record foreign restraint or confiscation orders. This issue has been raised and it is hoped that it will be addressed either as a change to the current JARD or in a new version of JARD that is currently being developed. JARD II is unlikely to be available for the next two years, however, it should then be possible to produce management reports showing the requested information.

Management information held by prosecutors does not distinguish between assistance provided by UK prosecutors for confiscation and restraint, as a case opened on behalf of a foreign jurisdiction for restraint will generally be followed at a later date by a request for the enforcement of a confiscation order.

For example, the CPS obtained a restraint order in 1997 in respect of a confiscation order made in the US District Court in 1995 in the sum of US\$7.8 million. The confiscation order was registered in the UK in the sum of £5.7 million in June 2002 and the registration was appealed by the defendant's spouse. The House of Lords dismissed the appeal in July 2004 and a receiver was subsequently appointed in 2008.

In January 2009, the CPS was dealing with 72 ongoing foreign requests for restraint and/or confiscation. In January 2008, the figure was 52 and in January 2007 there were 50 ongoing foreign request cases.

The COPFS have not been requested to enforce a foreign confiscation order to date.

(6) The number of restraint orders secured in England (and if possible Scotland) as the result of foreign requests, and their value

Please see the answer to (5) above.

The COPFS report that they have obtained two restraint orders as a result of a foreign request in the sums of £6.2 million and £170,000 respectively.

(7) The number of UK requests for the enforcement of our confiscation orders by foreign states, the results of such requests and the total value confiscated as a consequence

The UK Central Authority (UKCA) has provided a table set out at Annex B showing statistics for all outgoing MLA requests. The figures provided do not include direct transmission requests and there are concerns about the reliability of the database and the accuracy of the information it contains.

The JARD cannot currently provide this information and prosecutors are unable to provide this information from other IT sources. JARD II should address this issue.

The CPS does not hold collated data on the number of MLA requests made by its prosecutors nationally. The CPS Central Confiscation Unit of the Organised Crime Division has issued 24 letters of request seeking MLA for restraint and confiscation in the financial year 2008–09. In 2007–08, 23 requests; in 2006–07, 21 requests; and in 2005–06, 15 requests were made.

The RCPO is able to provide combined figures for restraint and confiscation requests transmitted for the last two years. In the period April 2007 to March 2008, 33 MLA requests for restraint and/or confiscation were transmitted. In the period April 2008/February 2009, 29 MLA requests for restraint and/or confiscation were transmitted.

The SFO has provided a table of its use of MLA, which is set out at Annex C.

The COPFS report that three have been granted and that in total approximately £284,000 was confiscated.

(8) The number of UK requests for the freezing and seizure of assets abroad and the outcome of such requests

Please refer to the answer to (7) above.

The COPFS report that five requests for enforcement of a Scottish restraint order abroad have been made since the beginning of 2006 in respect of which assets remain restrained abroad. They are not aware of any such request having been made and refused. A few additional ones may have been made and subsequently recalled during the relevant period.

(9) The total of confiscated assets shared by or with the UK

In 2004, the CPS enforced a US confiscation order to the value of £4.2 million and this sum was shared equally between the US and the UK. UK authorities also assisted the US concerning a drug money laundering operation resulting in an order for US\$20 million to be paid to the US authorities, of which US\$10 million was shared with the UK in 2004.

(10) Total numbers of requests for mutual legal assistance in money laundering and terrorist finance cases made to the UK, and whether any such requests were refused

Data collected by the UKCA does not include a breakdown of the offences concerned in each case and so cannot provide statistics solely in relation to money laundering or terrorist financing. Please refer to Annex B(2) for UKCA statistics of incoming MLA requests in respect of all offences.

The COPFS report that over 600 MLA requests have been sent to Scotland during the relevant period, some regarding money laundering investigations (exact statistics are not easily collated) and they are not aware of any which have been refused.

(11) The total number of requests made by the UK to foreign states and territories for mutual assistance in money laundering and terrorist finance cases, and the outcome of such requests

Please refer to the answer to (10) above.

Over 400 MLA requests have been issued by Scotland during the relevant period, many of them in relation to money laundering cases (exact statistics are not easily collated). Only one has been made regarding a terrorist case. COPFS are not aware of any which have been refused.

(12) The number of cases in which extradition (or surrender under the European Arrest Warrant) has been sought from the UK for money laundering or terrorist financing, and the outcome of such requests

The number of extradition requests received in the last three calendar years under Part 2 of the Extradition Act 2003 from non-EU countries, which resulted in an arrest are set out in the table below:

<i>Year</i>	<i>Part 2 EA 2003 Requests</i>	<i>Money Laundering</i>	<i>Terrorist Financing</i>
2006	29	2	0
2007	22	2	0
2008	20	1	0

Data held by the Serious Organised Crime Agency in respect of European Arrest Warrants under parts 1 and 3 of the Extradition Act 2003 does not include a breakdown of the offences concerned in each case. It is therefore not possible to provide statistics solely in relation to money laundering or terrorist financing.

(13) The number of cases in which the UK has requested extradition or surrender for money laundering or terrorist financing, and the outcome of such requests

The UK has made one request for extradition in respect of money laundering offences in the period 2006–08.

The Serious Organised Crime Agency is unable to provide data in respect of the number of requests for surrender for money laundering or terrorist financing for the reason set out in answer 12 above.

(14) *The number of spontaneous disclosures made by UK FIU to foreign FIUs*

The number of spontaneous disclosures made by the UK FIU to foreign FIUs is set out in the table below:

<i>Year</i>	<i>Number</i>
2006	43
2007	87
2008	81

These figures include data from the Crown Dependencies and Gibraltar.

(15) *The number of spontaneous disclosures received by UK FIU from overseas FIUs*

The number of spontaneous disclosures received by the UK FIU from overseas FIUs is set out in the table below:

<i>Year</i>	<i>Number</i>
2006	34
2007	58
2008	511

These figures include data from the Crown Dependencies and Gibraltar.

(16) *The total of terrorist assets frozen or confiscated in the UK*

As of January 2009, approximately £632,000 of suspected terrorist funds has been frozen under the Al-Qaida and Taliban Order and Terrorism Order.

There are currently no terrorist assets restrained under the Terrorism Acts, although a restraint order was obtained in 2006, which has subsequently been discharged. Although there have been confiscation orders made following convictions under the Terrorism Acts, the confiscation orders were made under the Criminal Justice Act 1988 and the Proceeds of Crime Act 2002 rather than by way of forfeiture orders made under the Terrorism Acts. Information as to the total value of the confiscation orders made in these cases is not available.

The Crown Prosecution Service

May 2009

Annex A**MONEY LAUNDERING PROSECUTIONS BY ALL AGENCIES**

	<i>Year</i>	<i>Proceeded against</i>	<i>Found guilty</i>	<i>Sentenced</i>
Total for all offences	2003	300	123	119
	2004	552	207	205
	2005	1,327	595	575
	2006	2,379	1,273	1,244
	2007	2,318	1,348	1,322
S 327 POCA	2003	29	4	3
	2004	140	39	37
	2005	392	154	150
	2006	574	300	290
	2007	502	286	281
S 328 POCA	2003	33	4	4
	2004	79	23	22
	2005	229	69	69
	2006	311	156	151

	<i>Year</i>	<i>Proceeded against</i>	<i>Found guilty</i>	<i>Sentenced</i>
S 329 POCA	2007	360	194	191
	2003	25	7	5
	2004	186	61	62
	2005	674	343	326
	2006	1460	801	788
	2007	1,419	850	832

Annex BUKCA STATISTICS OF ALL AGENCY OUTGOING MLA REQUESTS⁸

*THROUGHPUT QUARTERLY OUT

<i>QUARTER</i>	<i>Asset Restraint/ Confiscation</i>	<i>Coercive Evidence</i>	<i>Non-Coercive Evidence, other</i>	<i>Non-Coercive, Service of Process</i>	<i>Other</i>	<i>Total</i>
2006-1	3	2	305	39	33	382
2006-2	1	1	260	29	40	331
2006-3	0	0	328	63	22	413
2006-4	4	2	241	49	26	322
2007-1	7	1	221	87	20	336
2007-2	10	0	176	33	7	226
2007-3	3	0	229	107	22	361
2007-4	9	0	155	64	4	232
2008-1	7	1	197	112	6	323
2008-2	9	2	190	114	28	343
2008-3	8	1	184	151	92	436
2008-4	24	1	192	122	25	364

Annex B (2)

UKCA STATISTICS OF INCOMING MLA REQUESTS IN RESPECT OF ALL OFFENCES

<i>QUARTER</i>	<i>Asset Restraint/ Confiscation</i>	<i>Coercive Evidence</i>	<i>Non-Coercive Evidence, other</i>	<i>Non-Coercive, Service of Process</i>	<i>Other</i>	<i>Total</i>
2006-1	3	23	449	388	24	887
2006-2	3	19	578	252	20	872
2006-3	1	6	637	209	12	865
2006-4	0	9	523	300	6	838
2007-1	6	27	730	278	3	1044
2007-2	3	15	603	407	7	1035
2007-3	1	5	587	341	4	938
2007-4	2	8	572	361	2	945
2008-1	1	7	549	516	2	1075
2008-2	2	8	560	447	8	1025
2008-3	2	13	521	310	3	849
2008-4	1	10	291	211	2	515

1. This does not include supplementary letters of requests of which UKCA receives a considerable number (no official figures).
2. Casework staff are not legally trained so may make mistakes in classification of cases.
3. Not all rejected cases will appear in the figures as they will not have been registered.

⁸ UKCA has indicated that the above figures do not include direct transmission requests; non-legal staff are responsible for the classifying requests; and there are concerns about the reliability of the database. Many requests for MLA to support confiscation are included with requests for evidence.

4. The database is not reliable—a new database has been procured and is currently live but is experiencing some teething difficulties. The Home Office is working with its suppliers to resolve these issues as quickly as possible.
5. This does not necessarily reflect all cases received, only those that were registered on the database during these months (a simple point I know but important to be aware).
6. Does not include all cases received that were then forwarded on to HMRC or Crown Office (as the correct central authority for that case).

Annex C**SFO MLA REQUESTS**

	03/04	04/05	05/06	06/07	07/08	08/09Jan (28th)
New requests referred	30	35	41	53	45	42
Requests accepted	30	30	40	53	45	27*
Under consideration (at end of year)	2	4	1	0	0	2
Supplementary requests	33	41	40	50	33	20
No. of countries assisted**	30	31	23	24	30	37
Requests active at year end	44	51	57	71	68	65
Section 2 Notices issued for MLA	261	206	274	345	281	233
Search warrants executed	10	8	0	7	7	6

*includes 2 request for sect 3(5) disclosure

** includes all open case assistance: Germany, Finland, Turkey, Belgium, France, The Netherlands, Bulgaria, Czech Republic, Portugal, Spain, Italy, Russia, Sweden, Switzerland, Luxembourg, Denmark, Hungary, Poland, Jersey, Austria, Greece, Ukraine;

USA, Canada,

Israel, Iran, Bahrain, Kazakhstan

Tanzania, South Africa, Zambia, Kenya, Namibia;

Costa Rica, Argentina;

India, Pakistan

Supplementary memorandum (2) by the Crown Prosecution Service (CPS)

Additional to the evidence of Jeremy Rawlins in reply to QQ 140 and 141

Q 140: Sections 330 to 332 POCA 2002 deal with the reporting regime for those working in the regulated sector and for money laundering reporting officers in and outside of the regulated sector. These sections create offences for failing to report suspicious activity. In contrast, there is no compulsion to make an authorised disclosure to SOCA under section 338 POCA 2002, but it may avoid the commission of money laundering offences contrary to sections 327 to 329 POCA 2002.

The reply to Q 141 concerns a potential CPS prosecution for a money laundering offence contrary to section 329 POCA 2002 based on the lack of a relevant licence in the absence of aggravating features and when a defendant has voluntarily approached the authorities with the intention of regularising his position. Aggravating features would include the deliberate flouting of the licensing regime and safety procedures in order to maximise profits illegally. The answer does not address a range of other potential offences, eg under Health and Safety regulations, which would not generally be prosecuted by the CPS. The advice given to prosecutors in the CPS Legal Guidance is that it will usually be appropriate to proceed with the underlying offence, however, each case must be decided on its own facts.”

Supplementary memorandum by the Serious Organised Crime Agency (SOCA)

This note sets out requested follow up material on FIU.NET, SOCA’s network of Financial Liaison Officers, categories in the SARs Annual Report, guidance to reporters and retention of SARs.

FIU.NET

What changes, from the UK's perspective, need to be made to FIU.NET to make it fully effective?

The UK is a supporter of a new model that is currently being developed to improve the effectiveness of FIU.NET. The model will allow FIU.NET to have better connectivity with the Egmont secure web and will enable users to reduce costs on technology requirements.

The new model will also allow users to create, build and share “case files” with selected Financial Intelligence Units (FIUs). This will improve the content of information exchange and lead to a more coordinated response to SAR intelligence. The user will be able to see data held by other Member States and build up analysis around it. This new model is due to be in place by the end of 2009.

Additionally, the UK would like to see a fuller membership of FIU.NET and believes that the above changes will make the system a more attractive one for those EU Member States that are not members (see below).

The UK is also supporting a proposal to house FIU.NET within Europol, as its current home, the Dutch Ministry of Justice, will no longer be an option. Some Member States are pushing for FIU.NET to be housed as an independent entity, but the UK's view is that the Europol option would allow for a more effective exchange of data on money laundering and terrorist financing.

Which EU Member States are not participating in FIU.NET at the moment?

The following EU Member States are not currently participating in FIU.NET: Austria, Ireland, Lithuania, Latvia and Estonia.

Together with a core group of other FIUs, the UK created a Board of Partners (in partnership with the Dutch Ministry of Justice and with EU Commission funding), to develop FIU.NET into a more effective tool. The FIU.NET Board of Partners consists of the Dutch Ministry of Justice and FIUs in the Netherlands, UK, Greece, Germany, Italy, France, Romania, Belgium, and Finland.

FINANCIAL LIAISON OFFICERS

What is the cost of the five Financial Liaison Officers?

The cost of Financial Liaison Officers varies from country to country, but the officers are UK based staff, the majority of whom are employed on a pay range of £32,469 to £41,274.

EXPLANATION OF CATEGORIES IN THE ANNEXES OF THE SARs ANNUAL REPORT 2008

Do you have a fuller explanation of what some of the names mean in the list of sectors in Annexes B and C of the report? How for example does “Education” or “Charity” or “Leisure” (since it does not include Gaming) fit into the SARs regime?

Before reporters could submit a SAR via the internet, new reporters were assigned to a category by UKFIU staff based on the content of their SAR or if they provided a Source Registration document stating their business type. With the current system, reporters that register on SAR Online (which are the vast majority) choose a category that they believe best describes their activity.

Reporters that come under the category of “Education” are schools, colleges and universities that have had reason to submit information about suspicious financial activity to the UKFIU. For instance, a private school may submit a SAR if it was concerned about the origin of a payment of its fees.

Those that fall under the category of “Charity” are charitable organisations, including trusts, foundations and religious bodies, which have identified suspicious financial activity in the course of business, for example in respect of funding or donations.

The category “Leisure” refers to hotels, leisure groups, holiday resorts, sporting clubs and entertainment groups. Suspicion may be aroused for example because of large payments made in cash. Some casinos may appear under this category as they may have categorised themselves under “Leisure” instead of “Gaming”.

Other sectors that might not obviously fit into the SARs regime are IT and Manufacturing. These are companies in the information technology and manufacturing sectors that wish to report a suspicious transaction; such transactions may relate to anomalies around contracts for goods such as a change in payment method or suspicion around the destination of funds.

GUIDANCE TO REPORTERS

Is there any guidance issued to those expected to make SARs reports—for example different guidance for different sectors?

The UKFIU provides a range of guidance to the reporting sector on submitting SARs. For example, it produces and distributes the following flyers:

- “*Introduction to Suspicious Activity Reports (SARs)*”—explains what a SAR is and why SARs have to be submitted;
- “*Reporting via SAR Online*”—gives details on how reporters can submit a SAR using SAR Online and how to receive further support;
- “*United Kingdom Financial Intelligence Unit*”—provides details of the activity of the different departments of the UKFIU.

SOCA supplements this with a range of targeted communication products, including:

- SOCA Alerts—which often originate from the UKFIU alerting industry to specific issues;
- magazine articles—often sector specific;
- training material;
- booklets—for example on terrorist financing (to be issued shortly);
- by running seminars and conferences (originally sector specific seminars but now targeting the hard-to-reach sectors);
- specific sectoral feedback reports including to the Law Society Northern Ireland and the Law Society Scotland;
- case studies; and
- the SARs Annual Reports.

Additionally, staff in the UKFIU provide input at seminars, hold meetings with specific reporters, and attend the Vetted Group and the Regulators Forum.

SOCA’s website (www.soca.gov.uk) also provides guidance on completing and submitting a disclosure and directs reporters to SAR Online.

More specific sector guidance is produced by industry and the regulators themselves. The Joint Money Laundering Steering Group (JMLSG) produces detailed guidance on reporting for the UK financial sector which is approved by HM Treasury (see www.jmlsg.org.uk—Guidance for the UK Financial Sector Part I and Part II). As part of the approval process the guidance is put to the Money Laundering Advisory Committee (MLAC) of which SOCA is a member. In its response to follow-up requests in Q166–Q169, HM Treasury provided details of other industry guidance that has been approved in this way.

RETENTION OF SARs

What happens when a SAR is made and the suspicion is proved to be unfounded? If for example a reporter is concerned about a transaction which at first sight appears suspicious, so that a report is made, what happens if on investigation the suspicion proves to be unfounded? Is the data about the transaction retained? And if so, for how long? And who can access it in that time?

For the reasons outlined in SOCA’s evidence on Q193, in respect of the diversity of end users, ranges of use, and the long time periods after which SARs can be utilised, SOCA is of the view that there are few SARs with no value. Upon receipt of a SAR, including in the event of an investigation that utilises it, steps are not taken to confirm whether the suspicion is founded or not, and it would not be practicable or useful to do so.

In addition, the Proceeds of Crime Act 2002 requires the reporting of activity that makes the person suspicious. As future circumstances unfold, including if the SAR is not used for a period of time or if an investigation is carried out which fails to produce a law enforcement result, the fact that the reporter was suspicious is unaltered. Therefore the SAR remains on the database and is available for use by the full range of end users.

17 April 2009

WEDNESDAY 25 MARCH 2009

Present Garden of Frognal, B. Jopling, L. (Chairman)
 Hannay of Chiswick, L.
 Henig, B.

Memorandum by the General Secretariat of the Council

The General Secretariat of the Council would like to thank the Honourable Members of the Select Committee on the European Union, Sub-Committee F (Home Affairs, of the House of Lords) for their interest in the EU's actions in the field of money laundering and financing of terrorism.

Disclaimer: It should be noted that all information provided in this document is **not** evidence "from the Council" but only from the General Secretariat of the Council. Only the Presidency would have the right to speak on behalf of the Council.

EU STRATEGY ON TERRORIST FINANCING

In July 2008, the Council endorsed a revised Strategy on Terrorist Financing. The revised Strategy was necessary as most of the actions included in the original strategy of December 2004 have been carried out. Those actions not yet implemented or in the process of implementation have been taken up in the revised strategy. All three EU pillars are actively involved in implementation.

The revised strategy calls for enhanced implementation of existing actions, effective implementation of legislation adopted, in particular, the implementation of the nine FATF Special Recommendations and relevant JHA-legislation (mutual legal assistance, confiscation, cooperation between Financial Intelligence Units (FIU) and the exchange of information and cooperation concerning terrorist offences). Particular attention is paid to the internal and international exchange of information between all bodies involved in the fight against terrorist financing, including the private sector. Furthermore, the strategy calls for better targeting of action to counter terrorist financing, based on an intelligence led approach, and improving the effectiveness of mechanisms for asset freezing, as well as working closely with the UN and other international bodies in order to strengthen the international dimension.

According to their respective legal instrument both Europol and Eurojust are competent in the field of money laundering and financing of terrorism. Condition is that two or more Member States are affected in such a way as to require a common approach by the member states owing to the scale, significance and consequences of the offences. Both bodies fulfil a support and coordination role in order to facilitate investigations and analysing information. The requests for support are constantly increasing.

In this regard it is useful to mention Council Decision of 20 September 2005 on the exchange of information and cooperation concerning terrorist offences (2005/671/JHA). To enhance cross-border cooperation by national police forces and judicial authorities in the fight against terrorism, a more frequent and earlier use of the services of Europol and Eurojust in this regard would be helpful and will also contribute to the efficient implementation of this Council Decision.

FINANCIAL INTELLIGENCE UNITS COOPERATION

As regards FIU cooperation, the European Commission has evaluated the implementation of Council Decision 2000/642/JHA of 17 October 2000 concerning arrangements for cooperation between financial intelligence units (FIUs). A report has been transmitted to the Council in January 2008 and concluded that Member States can be largely considered as legally compliant with most of the key requirements of the Decision. However, more is needed in terms of operational cooperation, which includes ensuring wide exchange of all necessary financial and law enforcement information and additional questions in this regard have been transmitted to member states. An important (support) tool to reinforce operational cooperation is the FIU.NET and the informal FIU Platform, established by the Commission to support the operational implementation of the third AML/CFT Directive (Directive 2005/60/EC on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing. The Council is awaiting further proposals from the Commission on how to improve the operational cooperation.

INTERNATIONAL COOPERATION

The Financial Action Task Force (FATF) is an inter-governmental body whose purpose is the development and promotion of national and international policies to combat money laundering and terrorist financing. The FATF is therefore a “standard-setting body” that works to generate the necessary political will to bring about legislative and regulatory reforms in these areas. The FATF has published 40 + 9 Recommendations in order to meet this objective. Associated to the FATF are the so-called FATF Regional-style bodies (FSRBs). MONEYVAL is such a FSRB.

The FATF and MONEYVAL monitor members’ progress in implementing necessary measures, reviews money laundering and terrorist financing techniques and counter-measures, and promote the adoption and implementation of appropriate measures globally.

FATF and MONEYVAL member countries are strongly committed to the discipline of multilateral monitoring and peer review. The self-assessment exercise and the mutual evaluation procedure are the primary instruments by which the FATF and MONEYVAL monitor progress made by member governments in implementing the FATF Recommendations.

In the self-assessment exercise, every member country provides information on the status of its implementation of the 40 Recommendations and Nine Special Recommendations by responding each year to a standard questionnaire. This information is then compiled and analysed, and provides the basis for assessing the extent to which the Recommendations have been implemented by both individual countries and the group as a whole.

The second element for monitoring the implementation of the 40 Recommendations is the mutual evaluation process. Each member country is examined in turn by the FATF and MONEYVAL on the basis of an on-site visit conducted by a team of selected experts in the legal, financial and law enforcement fields from other member governments. The purpose of the visit is to draw up a report assessing the extent to which the evaluated country has moved forward in implementing an effective system to counter money laundering and to highlight areas in which further progress may still be required.

The mutual evaluation process is enhanced by the FATF’s policy for dealing with members not in compliance with the 40 Recommendations. The measures contained in this policy represent a graduated approach aimed at reinforcing peer pressure on member governments to take action to tighten their anti-money laundering systems. The policy starts by requiring the country to deliver a progress report at plenary meetings. Further steps include a letter from by the FATF President or sending a high-level mission to the non-complying member country. The FATF can also apply Recommendation 21, which results in issuing a statement calling on financial institutions to give special attention to business relations and transactions with persons, companies and financial institutions domiciled in the non-complying country. Then, as a final measure, the FATF membership of the country in question can be suspended. Within MONEYVAL an equivalent procedure has been developed.

An important part of EU policy on terrorist financing is derived from the work of the FATF, in particular from its nine Special Recommendations on terrorist financing and their transposition into community law. The work undertaken by the FATF has also been taken into account in the revised EU Strategy on Terrorist Financing.

EU member states whether, members of the FATF or MONEYVAL, have to comply with the FATF Recommendations and are assessed on their own merits by both bodies on their compliance with the criteria of the FATF Recommendations and Special Recommendations. Monitoring the implementation of EC/EU legal instruments, transposing these FATF Recommendations into community and EU law, is not the task of the FATF and MONEYVAL. According to the EU Treaty, it is the role of the Commission to follow the implementation of EC-legislation in the EU member states, and to take appropriate action in case a Member State has infringed upon its obligations according to EC legislation.

The third round of mutual evaluations (FATF and MONEYVAL) of EU member states to date shows that most EU member states are compliant or largely compliant with the Recommendations on international cooperation. Having implemented the formal framework for criminal justice might be beneficial to those results.

On 3 September the European Court of Justice delivered judgement in Joined Cases C-402/05 P and C-415/05 P *Kadi and Al Barakaat International Foundation v Council and Commission*. The appellants were designated by the UN in 2002 under UNSCR 1267 (Al Qaeda and Taliban list). The Court annulled the EU Regulation aimed at transposing the UN obligation in so far as it concerns the two appellants, on the ground that the appellants’ procedural and fundamental rights had not been sufficiently respected. However, accepting that the freezing might in fact be justified, the Court maintained the effects of the freezing orders concerning the

appellants until 3 December 2008. The Community has since complied with the requirements of the judgment by communicating the reasons for listing to the parties concerned and providing them with an opportunity to comment. Having considered the comments received, the Commission adopted Regulation (EC) No 1190/2008 listing Mr Kadi and the Al Barakaat International Foundation, which entered into force on 3 December 2008. The Commission has also invited those parties listed since the date of the judgment to contact it in order to receive the reasons for their listing.

MONITORING IMPLEMENTATION

All the legal instruments adopted by the Council provide EU member states the framework for taking action and to facilitate the cooperation between them. The General Secretariat of the Council would remind the Committee that the Council is not a law enforcement body. Efficient and effective implementation is the main task of the EU member states and the European Commission's role is to monitor implementation and, if necessary start infringement procedures.

Not all EU member states have ratified the Protocol to the 2000 Convention on mutual legal assistance and the EU Counter-Terrorism Coordinator (EU CTC) has called upon those EU member states that have not done so, to ratify as quickly as possible.

As already stated above, according to the EU Treaty, it is the role of the Commission to follow the implementation of EC-legislation in the EU member states, and to take appropriate action in case a member state has infringed upon its obligations according to EC legislation.

At this stage the General Secretariat of the Council is not in a position to answer the questions on the consequences, if any, to Regulation (EC) No 1781/2006 of 15 November 2006 on information on the payer accompanying transfers of funds and the other legislative instruments mentioned in the call for evidence. As the same questions will be answered by the Commission, the Council Secretariat General refers the Honourable Members of the Select Committee on the European Union, Sub-Committee F (Home Affairs) to the content of the answers given by the European Commission.

2 March 2009

Examination of Witnesses

Witnesses: Ms MIENEKE DE RUITER, General Secretariat of the Council, PROFESSOR GILLES DE KERCHOVE, EU Counter-Terrorism Co-ordinator, and MR HANS G NILSSON, Head of JHA Counsellors, Permanent Representation of Sweden to the European Union, formerly Head of Division, General Secretariat of the Council, examined.

Q221 Chairman: Thank you so much for coming; we appreciate that. I understand that your colleague, Professor de Kerchove, is not coming and I understand that Mr Nilsson may come. It will be good to see him if he is able to do that. Perhaps I can begin by asking you what, in the view of the Council Secretariat, are the major challenges presently facing European efforts with regard to money laundering and counter-terrorism?

Ms de Ruiter: This is a very broad question. You can look at the economic crisis, you can look at every other thing, but in my opinion the main challenge to the European effort is not the EU effort but the efforts of the individual Member States because framework decisions, directives and all kinds of other things are decided upon at the political level. However, as you know, the EU is not a law enforcement agency so implementation of rules agreed upon between 27 Member States of the European Union depends on a fairly uniform implementation of the provisions mentioned in these regulations, framework decisions and so on. I think that is one of the major challenges of the EU because if you read the provisions of certain framework decisions and directives they are

written in a very policy-making way and are usually, in my opinion as I come from a Member State of the European Union, difficult for practitioners to implement in a uniform way. A challenge for the European Union therefore could be for regulations, directives or framework decisions, as we still have them, to be accompanied by rules for Member States on how to implement them. One example I would like to mention is the Financial Intelligence Unit. It is mentioned in all directives and regulations in the whole of EU legislation but we do not have in the EU a uniform definition of an FIU. Every Member State is entitled to implement it in its own way, be it law enforcement, be it administrative, be it judicial, and there you see a lot of difficulties in exchanging information. If you are a law enforcement FIU you have easy access to police information. If you are an administrative one you do not. The same goes for the financial sector and so on. There would be major challenges in my personal opinion, therefore, in implementing the rules accompanying legislation which is adopted or agreed upon by Member States and finally adopted by the various counsellors at the European Union.

25 March 2009

Ms Mieneke de Ruiter, Professor Gilles de Kerchove and
Mr Hans G Nilsson

Q222 Lord Hannay of Chiswick: One specific challenge which we have stumbled across in the course of this inquiry and which is relatively new is the rather large sums of money which are being paid to Somali pirates who hijack ships on the high seas and take them into Somali waters and then hold them until they are paid often very substantial sums of money. It seems fairly evident that while this money may be paid in a perfectly legal way by insurance companies or the owners of the ships, it is certainly being paid to someone who has committed a crime, an international crime moreover, and there does not seem to be much sign that any of the organisations—FATF, the EU, our national regulators—have got a sharp focus on this. I therefore wondered whether you had given any thought to the problems posed by these transfers of money and the laundering of the money, which presumably takes place once it is in the hands of the criminals, because one assumes that they do not just spend the money going down to the grocer's store in Mogadishu but on a whole lot of other things, some of which, of course, could be related to terrorism too. I am not alleging that; I have no evidence to do so, but it certainly could be. I wonder whether you have given any thought to that at all, either as an entity, the EU, or as part of FATF.

Ms de Ruiter: For the EU I cannot recall at the moment whether any Justice and Home Affairs Council has raised this topic. I am not sure. I cannot answer the question because I have not read the conclusions of the last European Council—

Q223 Lord Hannay of Chiswick: No, there is nothing about it in there.

Ms de Ruiter:— and in the last FATF meeting it most certainly was not raised.

Q224 Lord Hannay of Chiswick: I see. Does this represent a problem, a challenge, a risk in your view *prima facie* or are we just worrying about something we should not be worrying about?

Ms de Ruiter: That is a very difficult question for me to answer, I am afraid. I think the Council reacts immediately to things where we have a suspicion on issues. At the moment I cannot recall whether we have imposed some financial sanctions on Somalia. I do not think we have done anything yet. As far as I am aware we are not raising this.

Q225 Lord Hannay of Chiswick: Since the EU now is involved in trying to prevent the pirates capturing ships, there is an EU/ESDP military operation going on, it does seem a little bit odd that there is no joined-up thinking about finding a whole multiplicity of ways for making life difficult for people who are involved in this kind of crime.

Ms de Ruiter: I note your question and what I can do is to make some inquiries internally in the Council Secretariat General and provide you with some written comments afterwards, because this is a question I have not prepared myself for. I will check with my colleagues in the External Relations Department and the financial sector whether the Ministers of Finance have already discussed this issue or not, and whatever I find out I will let you know through your Clerk.

Lord Hannay of Chiswick: That would be very helpful.

Q226 Baroness Garden of Frognal: You mentioned the world economic downturn and I wonder if you could say to what extent, in the course of the discussions within the Council, you have identified significant concerns relating to current strategy to combat money laundering and the financing of terrorism and whether or not this is adequate.

Ms de Ruiter: The world economic downturn has just recently been discussed in the Council during a lunch discussion. We do not know what is discussed during a lunch meeting because functionaries are not allowed to attend, at least not at my level. I know for sure that it is on the Justice and Home Affairs Council agenda for 6 April 2009 and the Czech Presidency has promised us a paper in which further proposals can be expected for the Commission to work upon on what the effects could be on money laundering and terrorist financing in the EU. Attention was focused on this point in preliminary discussions during the last Justice and Home Affairs Council under the French Presidency and on 6 April there will be another discussion based upon a paper from the Czech Presidency and we expect there will be proposals for the Commission to work on for Member States to take action if necessary. I know that in the FATF they also discussed the economic crisis during their last meeting in February and they have now started a project to find out what kinds of measures might be feasible or necessary for dealing with the economic crisis. It is a Dutch proposal for the Dutch Presidency and the first questionnaires and more outline and detailed proposals will be discussed during the June meeting of the FATF in Paris.

Q227 Baroness Garden of Frognal: So there should be more information after 6 April?

Ms de Ruiter: There should be more information after 6 April, yes, because I have not seen the Czech Presidency's paper yet. They are mostly very late in the day when they are transmitted and so I cannot say anything about the content because they have not informed us yet.

25 March 2009

Ms Mieneke de Ruiter, Professor Gilles de Kerchove and
Mr Hans G Nilsson

Q228 Lord Hannay of Chiswick: Would it be possible for us to have a note after that Council of any material that is in the public domain?

Ms de Ruiter: I will ask my colleagues.

Q229 Lord Hannay of Chiswick: We are not asking for anything that is not permitted.

Ms de Ruiter: No, no.

Q230 Lord Hannay of Chiswick: The Committee has received evidence stressing the important improvements to mutual legal assistance, especially in respect of banking information, which are contained in the 2001 Protocol to the 2000 EU Convention on Mutual Assistance in Criminal Matters. Could you say something about the current status of the protocol and what are the reasons for the delays in its ratification and entry into force?

Ms de Ruiter: The protocol so far has been ratified by 22 Member States. Five have not done so, although Ireland has indicated that it has implemented and ratified it but they have not sent us the documents for notification yet. That leaves only Estonia, Greece, Italy and Luxembourg. (There followed a discussion off the record) I am told Mr Nilsson is coming. We are, of course, constantly pushing countries to ratify and implement and work on it, but, as I told you at the beginning, as a Council we can only push Member States and urge them to implement; we cannot interfere in their internal business. (There followed a discussion off the record) We are trying to get information about why they are so behind. Sometimes the reason is that they are waiting for other framework decisions to be adopted and implemented so that they can change their criminal codes in one go and not in two or three rounds because some countries have a very cumbersome way of amending a criminal code or criminal procedure code.

Q231 Lord Hannay of Chiswick: In your experience has that affected the ability of those four countries that have not ratified to co-operate on mutual assistance and criminal matters or are they effectively doing almost as much as the Member States which have ratified but they just are not in the same legal situation?

Ms de Ruiter: As far as I know we do not have many problems with those countries co-operating on the basis of mutual legal assistance and answering any requests for mutual legal assistance. (There followed a discussion off the record)

Q232 Baroness Henig: At the time of the conclusion in 2003 of the EU-US Agreement on mutual legal assistance there was an expectation that it would make a significant contribution to enhanced

transatlantic co-operation, not least in respect of access to banking information, and I wondered if you could say what is its present status and what is the cause of the delays which have surrounded its full operation.

Ms de Ruiter: First of all, it has not entered into force yet but I think you were aware of that. Belgium and Greece still have to ratify it and we expect that later this year, so we cannot talk about any conclusions on how it has affected transatlantic co-operation. We held an implementation seminar with the US in November 2008 which was very positive but we cannot start implementing all those other provisions because we have to wait for Belgium and Greece. The United States ratified the agreement six months ago, so everything is settled, the implementation seminar has been held and both sides know what can and cannot be done, but we cannot start co-operating on the basis of this agreement because we have to wait.

Q233 Baroness Henig: In this particular case what was the problem with Belgium?

Ms de Ruiter: I think with Belgium it is a political problem. Belgium has been without a government for 11 months or so, and if you knew the cumbersome procedure here in Belgium to get a law or a ratification instrument adopted—it has to go through nine different parliaments or something like that. Do not ask me the specific details because it is so complicated. For Greece we do not have any indication why.

Q234 Baroness Henig: So your estimate of “later this year” could be somewhat optimistic?

Ms de Ruiter: Our estimate is no, because they have a government now and they are pushing it.

Q235 Baroness Henig: So you are fairly certain?

Ms de Ruiter: I think before the end of the year, yes, it will enter into force and then the co-operation will start.

Q236 Chairman: Just going back to the question on the delays in ratification, does this underline the need to place all of the mutual assistance on a mutual recognition basis, and could you tell us what prospects you see for further moves in this direction?

Ms de Ruiter: Would it be possible to postpone this question until Mr Nilsson arrives? Mr Nilsson is more of an expert on the criminal matter issues so I think it would be better for him to answer this question if you do not mind.

Q237 Chairman: Right, let us do that and move on. Let me say at this stage, which perhaps I should have said at the beginning, how grateful we were for the written evidence you sent us on behalf of the Council.

25 March 2009

Ms Mieneke de Ruiter, Professor Gilles de Kerchove and
Mr Hans G Nilsson

In that evidence the General Secretariat of the Council mentions the Council Decision of 20 September 2005 on the exchange of information and co-operation concerning terrorist offences and notes that a more frequent and earlier use of the services of Europol and Eurojust would be helpful. You may know that we did a report on Europol just a few months back. Could you tell us how you would characterise the current level of compliance with this aspect of the Council Decision and what steps have been taken to address this situation and how effective they have been?

Ms de Ruiter: First of all I have to say on behalf also of Professor de Kerchove, the EU Counter-Terrorism Co-ordinator, that we are disappointed at the level of implementation of this Council Decision, which is in our opinion not satisfactory because Member States do not use it that much. I do not know if I have sent you the EU counter-terrorism strategy discussion paper of 19 November 2008. I can send that to you later.

Q238 Chairman: We do not have it.

Ms de Ruiter: Okay, then I will transmit it later. I am not sure whether it has a LIMITE or any codes on it any more. At the time I was given the written evidence it had a LIMITE code on it and I was not allowed to transmit it but now I can. Professor de Kerchove has also paid a lot of attention to this Council Decision and he states that there are three types of obstacle to the systematic transmission of information relating to investigations: first, “the refusal by the judicial authorities in certain Member States to transmit information relating to investigations in progress”; secondly, some agencies with dual competencies as law enforcement and as security services are experiencing legal difficulties in identifying what can be shared with Europol; and, thirdly, the requirement laid down in Article 2(3) of the decision, which says that each Member State shall take the necessary measures to ensure that at least the information concerning criminal investigation and so on is being transmitted and that the information affects or is likely to affect two or more Member States. In his discussion paper he says that all EU Counter-Terrorism can do and will always do is call upon the various Member States and working parties to consider how these difficulties which I have just summarised may be resolved.

Q239 Chairman: I wonder if I can follow that by asking whether you are aware of the attitude of Eurojust, which sent written evidence to us emphasising how important they regard this matter. Has Eurojust transmitted their feelings about this to you?

Ms de Ruiter: In the same discussion paper of the EU Counter-Terrorism Co-ordinator Eurojust states that the implementation from their point of view is very satisfactory. They are satisfied with the implementation with regard to their issues. Maybe Mr Nilsson, who has just arrived, can add something.
Mr Nilsson: Can I first apologise for being late? I was in a meeting with the ambassadors discussing issues like Guantanamo and other things that are high on the political agenda. My name is Hans Nilsson. I used to work with Mieneke here when I was head of the division in the Council Secretariat dealing with money laundering, but since 1 March I have been working for the Swedish Parliament Representation co-ordinating the Justice and Home Affairs issues in view of the Swedish Presidency. Yesterday I was in London and I had the enormous pleasure of having lunch with several of their Lordships, including Lord Mance and Lord Dykes, at the Swedish Ambassador’s residence, so I thought that I would try to come here also today to see you.

Q240 Chairman: May I say how welcome you are. We are particularly grateful to you for coming to share your experiences with us and we perfectly understand how involved you are with the preparations for the Swedish Presidency. If my diary had permitted it I would have been with you at the embassy yesterday because I was invited but was not able, sadly, to go, but thank you for coming. Maybe it would be helpful if we sent to you the evidence we have received from Eurojust, and if you wish to comment on what Eurojust have said to us those views would again be very helpful indeed.

Mr Nilsson: On Eurojust, I do not know what they have said in their report but my general impression in relation to that decision is that, as always in this area, this is something that takes some time. After a very slow start Eurojust is starting to get some information but it is very uneven from what I hear from Eurojust, and I go there regularly. I think that Member States in this entire field could do much more to implement decisions that have been taken at EU level. I do not know the exact statistics but I know that there are some Member States that are sending in quite a lot, including the United Kingdom, if I remember well, and also Spain, but the question here is also at what time do they send in the information? Do they send in the information once when an investigation has finished or do they send it in at the beginning of the investigation? This is a very important factor and I think that Member States in general have a tendency to send it in when the information is, shall I say, dead or expired or no longer so useful for Eurojust, so there is quite some improvement to be made. I once had the honour to give both written and oral evidence on Eurojust to

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your Committee a couple of years ago, so we should also remember that, when it comes to Eurojust, Eurojust is after all rather a new body. It still has to make itself known with judicial authorities that are by tradition quite slow in changing practices, so when it comes to issues which are very sensitive, such as sending information (in particular in relation to terrorist offences), this is something which in my experience will take several years before we can really say that we have a satisfactory result. We have recently adopted a decision on building on this model to amend the Eurojust Decision so that information in relation to other serious offences should also be sent in to Eurojust. However, that also will take several years before it is implemented. There is quite a long time from the time of the decision to the time of implementation by the Member States in this area.

Q241 Lord Hannay of Chiswick: Could I ask you whether in your experience and opinion this is another manifestation of something one comes across quite a bit in this area, namely, that the Member States are readier to exchange information on a bilateral basis with one or two countries in whom either they have great confidence in their confidentiality in terms of the material or who are directly involved in particular matters but are much less willing to exchange information on a 27-Member basis? Is that part of the problem here?

Mr Nilsson: Yes, absolutely it is part of the problem and it is in particular in relation to terrorism that we see it. If you were to say they share—and now I am just speculating—perhaps 80 per cent of their information with the United Kingdom, I think that with France they may share perhaps 40 per cent and with Hungary two per cent, but very often we see in this area bilateral relationships which are built not on institutions or bodies but very much on personal contacts and personal trust, in particular in the terrorist area. We see it also inside the Member States. If you take the issue of the local police officer, I attended with the Swedish Minister of Justice a study visit at Southwark police station yesterday, and if I look at what the policemen there are doing on the ground, so to speak, when they get information, do they share that information with their superiors? Do their superiors share that information with Scotland Yard? Does Scotland Yard share it with others that could be interested in it and do they share it across borders? With all these steps I think you have less and less sharing because it is often very sensitive for a single policeman.

Q242 Lord Hannay of Chiswick: If I can follow that up, this is a difficult question for you who are in a European institution to answer, but do you think this is a bad thing or do you think that in fact, because of

the much greater degree of frankness that exists in various bilateral contacts, it is probably quite effective. Is it seriously an impediment to the working of the Counter-Terrorist Office?

Mr Nilsson: It can be a bad thing if the sharing of information is done in such a way that it may harm, for instance, the sources, but I think that in general if you mutualise the information you may also get a greater impact or use of the shared information, and we have seen in Eurojust and in Europol how cases have been solved by the sharing of information. One example was that through a Europol analysis work file a link was found between the murder of Theo van Gogh in Amsterdam and the alleged terrorists that were arrested later in Milan. That link would not have been found if there had been purely bilateral sharing. It was because you had a database and you could make a link in that database between two seemingly unrelated pieces of information that there was a hit, so to speak. One could see that in two criminal files that were not related there was a common denominator and suddenly the information was there. I know that Eurojust, at some seminar that we had in Lisbon one or two years ago, said that, even with the little information they had, they had already been able to establish links, and that is, of course, the most important thing. The reason why people want to share information bilaterally is in particular that they are afraid for the lives of their sources and they do not want to divulge them, but that is a problem that in my opinion will have to be dealt with by having strict rules on confidentiality, data protection and so on. It should not in itself be an impediment (again my opinion) to the exchange of information, the mutualisation of the information.

Q243 Chairman: Thank you very much. Just before you came in I did say that this Committee has recently done a report on Europol and we had a good deal to say about the matters which you have just been referring to with regard to the sharing of information and the information which never goes through Europol, and particularly the shortcomings of the selection process in various countries of people who are seconded to Europol, which is not satisfactory in terms of security clearance. We can perhaps send you a copy of that.

Mr Nilsson: I am sure it is even on the net.

Q244 Chairman: Before we proceed I wonder if I could go back to a question I asked a few moments ago. We were told that you were probably better able to answer it than Ms de Ruiter.

Ms de Ruiter: Professor de Kerchove has arrived.

Q245 Chairman: Professor, thank you so much for coming.

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Professor de Kerchove: I am so sorry to be late.

Q246 Chairman: We understood that you were not going to be with us so we are delighted you have been able to find time; our witness panel grows by the minute! I want to go back to a question which Lord Hannay asked a little earlier which was referred to Mr Nilsson, and that was with regard to the Protocol of 2001 on the 2000 EU Convention and we were hearing about the delays in ratification. Does this underline the need to place all mutual assistance on a mutual recognition basis? What do you think the prospects are for further developments in this field?

Mr Nilsson: First of all it underlines the very ineffective use that the Member States are making of the Convention as a legal instrument. On that instrument, if I remember off the top of my head, I think that we have still four or five Member States that have not ratified it—Luxembourg and others, so they cannot apply the provisions there, let alone the protocol. It is a token of what I would say is an implicit policy decision of the Council now to no longer work with the instrument of conventions but with the instrument of framework decisions, because in framework decisions at least you can put the time for implementation which you cannot do under the treaty with conventions. Since it is a binding provision you can say to the Member States, “You have to do it within two years”, for instance, which is less than the practice. From the time of the proposal by the Commission to adoption it is usually something like four or five years, it takes that long, but if we have a convention, as we now have with the 2000 Convention, we are nine years after the formal signature of the Convention. It is in force now, in fact, because it came into force with about half of the Member States a couple of years ago, but it is not in force with those other four Member States. To answer your question, it may be like that but it is proof rather of the ineffectiveness of conventions.

Q247 Baroness Garden of Frognal: In the written evidence you submitted you listed the number of working parties within the Council with a mandate in either or both of the anti-money laundering and terrorist financing spheres. I wonder if you could briefly summarise the differences between them, the work they do and quite how they co-ordinate with each other in their work.

Professor de Kerchove: I will not list the groups unless you insist.

Q248 Baroness Garden of Frognal: There is a list on page 13 of the evidence.

Professor de Kerchove: For many years Hans Nilsson and I have tried to streamline the organisation of the Council with very little success, and it is a bit

disappointing, I must confess. I tried once again when we had the revision of the strategy and once again I did not succeed. Why so? I think it is due to the reluctance of the ministries of finance which are opposed to something which—they think—would contribute to remove them from their driving seat in the file, which is wrong. One of the arguments I put last time was that in the FATF—which, by the way, is the place where all the policies are defined; sociologists have even called it policy laundering because the EU’s policy in the field of terrorist financing and money laundering is not defined within the EU; it is defined by the FATF and in the FATF by nearly half of the Member States because the new Member States are not members of the FATF—where do we define an EU position before taking a position in Paris?

Mr Nilsson: We do not do it.

Professor de Kerchove: Nor in the Council, and that is a bit odd because what the EC does most of the time is implement the recommendation defined in Paris. The EC has adopted many directives/regulations implementing the 40 recommendations on money laundering, the 9 special ones on terrorist financing. The Commission prepares the file with some Member States in the margin of a group which is not meant to do that. I am surprised that the Member States which are not members of the FATF do not insist on having at least a discussion in the Council since the policy that will be applied to them is defined somewhere else. Even more, I think, for a question of legitimacy it would make sense that this be prepared within the Council in the normal way as when we prepare common positions in other international fora. That was one reason.

Q249 Baroness Garden of Frognal: And does that have an effect on the effectiveness or the efficiency of the way in which it is planned?

Professor de Kerchove: That is difficult to state. Of course, the ministers of finance are primarily responsible for this but they are not alone. The ministers of justice have a stake, the police have a stake, the intelligence community has a stake, foreign affairs has a stake. All this, I think, would plead for one single place in the decision-making process where one would look at all aspects of it. I suppose it would improve the policy shaping but, of course, I cannot say that because we have not done that. That does not mean that the group themselves are not working very well. They do what they can. I suppose we could be even more efficient by being more streamlined.

Mr Nilsson: I think so, but where we have this co-ordination in terms of FATF meetings it is, and you can say more about that, relatively bland co-ordination, if I can put it like that, because the documents come out late, the people that go there are

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more ministry of finance people and so on, so it is basically run by the ministries of finance with very little consultation with the other ministries that are involved. There is, of course, consultation but everybody has things on their own plate so it becomes more of a finance issue than anything else. I used to go to meetings in the FATF between 1990 and 1996, something like that. There I could see how strong the ministers of finance were in making these issues finance-related, not related to the investigation, to prosecution and so on. It was more the protection of the financial systems and, as you know, the legal basis for the directives is the First Pillar legal basis, Article 95, I think it is. That means that there is probably no real sense of ownership of the file from the other ministries. I do not know if one could make a single committee. We have tried several times over a number of years to set up a money laundering committee within the Council but we have failed so far. This issue could come up if we were to have the Lisbon Treaty because there we need in any case to look at the new legal basis for other issues—civil protection, data protection, integration and so on, so perhaps this issue could be raised in that context and then it would be the Swedish Presidency if we have Lisbon from 1 January or 1 November; one does not know, and now, after what happened yesterday in Prague, I am not sure if we will have Lisbon at all but we will see about that.

Q250 Chairman: I wonder if I could come back to what you said about you both trying to set up a money laundering committee. Why did that fail? Are there certain countries which are strongly opposed to that? It sounds rather a sensible idea but why has it been shot down?

Professor de Kerchove: At the time when I was in Justice and Home Affairs no-one crossed Pillars.

Mr Nilsson: Like me.

Professor de Kerchove: Yes, but you are no longer. It was probably perceived as a sort of takeover by Justice and Home Affairs on a file where the ministries of finance were doing well and that is administratively a tough battle.

Mr Nilsson: And they are stronger inside the national systems, the ministries of finance. If you have two instructions saying two different things you know who will win unless you bring it up to the Prime Minister and then the Prime Minister will always go for the ministry of finance and not the ministry of justice.

Q251 Chairman: Exactly.

Professor de Kerchove: Perhaps I can say something off the record. (There followed a discussion off the record)

Mr Nilsson: Several years ago the idea of a money laundering committee was supported by three or four Member States but several others were against it.

Professor de Kerchove: But it may have a political impact which is not completely without importance if you remember the third money laundering directive (or was it the second?) where lawyers had an obligation put on them to report suspicious transactions. It probably would not have been agreed the same way by ministers of justice as it was by ministers of finance. I think they took the right decision but only ministers of finance could put that obligation on lawyers. Ministers of justice would have been under a much tougher pressure from the lawyers.

Chairman: That is very helpful.

Q252 Baroness Henig: In terms of the revised strategy on terrorist financing of last July I wondered what progress had been recorded in giving effect to other relevant recommendations in that revised strategy on terrorism and finance.

Ms de Ruiter: We are just at the stage of drafting the first implementation report of the terrorist financing strategy. It is due to be issued at the end of this month. I suggest we send it to you and then you will have a complete overview because it is 11 pages and we would have to go through it measure by measure.³

Professor de Kerchove: May I raise one point which if I had been here from the outset I would have mentioned. One of the messages of the revised strategy was that we have done a lot in terms of legislation. I would not say we have exhausted what we can do in terms of legislation but now the challenge is more about implementation, concrete implementation. When I attended a meeting of what is called the Wolfsberg Forum, which is a meeting of the compliance officers of the largest banks in the world which takes place every year in Switzerland, the message I got was that for money laundering we have developed rather good tools to detect suspicious transactions. "We have sophisticated software, we have experience and so on. For terrorist financing it is much more complicated. The process is different. Unless we get quite good background information and intelligence on what we should look at we will not detect that. We are ready to implement a directive. It costs a lot. We do it." I asked the audience in how many Member States had they built that relationship between the intelligence community and the financial sector, and only one has really done that. For obvious reasons it is the UK because of the importance of the City. I do not know exactly how. It may be that many compliance officers are former MI6/MI5 officers

³ Note from the Counter-terrorism Coordinator to COREPER: Implementation of the revised Strategy on Terrorist Financing, document 8864/09, 21 April 2009.

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working in the private sector and it is the old boy network, but I think we have to look at that. I plan to organise in the autumn, and I need to have the support of the key players in the intelligence community for this, a brainstorming session to explore how we can design a mechanism by which the intelligence community can provide interesting background information (which does not, of course, reveal top secrets but gives more than you can find in newspapers) and help these people to focus on some transaction or some countries or some movements, and just collect the best experience and offer it to the other Member States and suggest that they develop the same. It applies not only to terrorist financing. It applies also to the protection of critical infrastructure and transport. I met the person in the UK who is in charge of transport and she said the same thing. She said it is really something where we have to be creative and build some mechanism. You took Eurostar to come here, I suppose. Eurostar is well protected. If you go to Paris you will enter the Thalys with no check at all, so you can carry luggage full of bombs. Nobody will check if you are planning an attack. I think there is a need there also to improve the flow of information. That is something we have to work on. That is what I call implementation. It is not a question of legislation. It has first to be done by sharing best practice.

Lord Hannay of Chiswick: Just to follow up that point, we have taken evidence on this question of what is called in our evidence-taking the feedback that the Treasury, the Home Office, SOCA and others have with the practitioners—the bankers, the accountants and the lawyers. They gave us quite convincing evidence that the feedback in both directions is quite strong and quite structured, so I do not think it is just an old boy network. I suggest that if you look at the evidence, because we will publish our evidence, you will find some material there from what we have gathered that they spoke very strongly about how important this was, and the bankers, the accountants and slightly less so the lawyers said that they were rather satisfied with what, for example, they were given, not only specifics on individual cases on some occasions but also a kind of teach-in about how to set about identifying sources of finance for weapons of mass destruction proliferation and so on, so it may be of use to you.

Q253 Chairman: The evidence that Lord Hannay refers to is already on our website, so it is available now.

Mr Nilsson: If I may just comment on that, again referring to my visit to this police station in London yesterday, I think that you in the United Kingdom are unique in Europe in the way that once you have negotiated an instrument you actually implement it in a serious way, and I could see yesterday in this

police station how one implemented policies dealing with youth gangs and so on, but I have the feeling that in Europe it is not like that, so that when it comes to feedback, feedback is something that has been discussed certainly for a decade or so between the banks and the police and so on, but it becomes a totally different picture if you come out of the UK context and look at what is happening in other countries, such as Italy. In Spain they are trying to do things like this in my experience but there are countries where there is basically nothing. One other thing is that one has to realise that the FIUs look different in different countries. Some FIUs are purely administrative, others are judicial, others are a mixture of administrative and judicial and so on, and if they are judicial authorities it becomes something which is a question of the secrecy of the investigation and so on and issues like feedback are not so easy to deal with in that context.

Q254 Chairman: The Committee has received a certain amount of evidence about the Hawala system and other similar systems for the remittance of funds. I wonder whether you could tell us what particular problems are posed by these systems in addressing the fight against terrorism. I think the revised strategy does refer to these systems but it would be interesting to hear how important you feel they are in providing loopholes which are difficult to block up.

Ms de Ruiter: The problem with the alternative remittance and Hawala systems at the moment is that there is no control. The businesses which are executing these kinds of services are not registered, they are not licensed, there are no customer due diligence procedures at stake, there is no record-keeping, no suspicious transactions reporting and so on, so it is completely in the dark. With the Payment Service Directive which was adopted in November 2007 all those issues are being addressed, so once Member States start to implement the Payment Service Directive all those alternative remittance bureaux or businesses or little shops will have to be registered and licensed and will have to apply all the rules under the Anti-Money Laundering Directive. Then you can get a grip on it and you can try to get it under control. At the moment there is no control and that is the big challenge. How it will work out in the future we do not know yet because all the Member States are in the process of implementing this directive.

Professor de Kerchove: By 1 November of this year.

Ms de Ruiter: By 1 November this year it should have been implemented. To monitor the implementation is, of course, as it is a directive, the task of the European Commission, so it might be that the European Commission has some more information

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or indication on the state of implementation of this Payment Service Directive.

Q255 Chairman: But let us assume that on 1 November everybody has implemented it. What proportion of world traffic is going to be controlled by the implementation of this particular regulation?

Professor de Kerchove: The one link from and to Europe? We have important diasporas in Europe, so I suppose it is important, but I heard Richard Holbrook two days ago in Brussels confirming what we all know, that the financing of the insurgency, both in Pakistan and in Afghanistan, was not only the product of drug trafficking but also private money coming from the Gulf through Hawala and remittance systems. It is less remittance and more Hawala. That is a serious concern because that is where we have to intensify our discussions with the Gulf countries. I do not have any precise figures but I can try to get those for you.

Q256 Chairman: Yes, but these systems are in many cases totally legitimate and a perfectly satisfactory way of people remitting money back to their families, wherever they are, but, of course, the system allows money to be transferred to places maybe not within the European Union but somewhere close by where an attack of one sort or another could be mounted.

Professor de Kerchove: A good example is Sahel, northern Africa.

Q257 Chairman: Exactly what I was thinking of.

Professor de Kerchove: We have in Europe important North African communities. They are not transferring the money, by the way. It is just that the money appears on the other side of the Mediterranean.

Q258 Chairman: That is right, exactly.

Mr Nilsson: In the context of the discussion on migration issues this is also something which has been discussed, not from the security point of view but rather from the point of view that Hawala is a very important tool for moving money back to the countries that have large migration pressures. I have seen figures which suggest that it is something like ten per cent of the GNP of some countries which is being moved back through remittances and Hawala, and without any cost basically or at very small cost, because one of the problems here is the cost of sending money.

Professor de Kerchove: Another example is NPOs, abuse of charities. Once again, 99 per cent of the charities are pursuing legitimate goals and if we start legislating to impose overly burdensome accounting obligations just to tackle one per cent we will put an

additional burden on something which is, socially speaking, very useful.

Q259 Baroness Garden of Frognal: Can I take you on to the implications of the *Kadi* case? The revised strategy was endorsed by the Council several months prior to the judgment of the European Court of Justice in the *Kadi* case. Does that judgment have implications for the pre-existing strategy on targeted sanctions?

Professor de Kerchove: Yes, because it led us to improve the procedure. I do not think it has negative implications. What the Council decided to do after the *Kadi* case was an improvement because it improves the rule of law and the fairness of the procedure. That was the concern of the Court of Justice, and I would say personally rightly so, and the way the Court acted was very well thought out because the Court of Justice could have decided the same but by challenging the whole UN system of designation, which the Court did not do. The Court made a distinction between what is decided in New York and the way we implement those decisions, and limited its review to the way we implement what is decided in New York. It did not question the legally binding nature of the decision in New York, the UN Security Council resolution based on Chapter 7 of the charter, and that is very important because it remains one of the most efficient tools we have, not only for the fight against terrorism but also for imposing sanctions on states which do not comply with international law. I think we were lucky that the Court decided that way. The new procedure which was designed after the *PMOI* case, which was on the EU autonomous freezing mechanism, was just replicated after the *Kadi* decision. I do not see a negative impact. I would say that improving fairness in the procedures can only reinforce the robustness of the mechanism because then you will be faced with fewer cases in Luxembourg. We have had many in the past so I hope that the new procedure will dry up the number of cases in Luxembourg. I would say that is a positive impact. I do not have the latest information on the proposal of the Commission because one pending question is whether the Commission will keep the power to implement the decision taken in New York or whether the process will move to the Council. You know that currently the way we proceed there is via a generic regulation which gives the Commission the power to implement all the decisions taken in New York. The Commission adopts a regulation and as soon as a case is decided in New York. The Commission adopts the regulation in order to implement in EC law the decision in New York. As for whether it should remain the Commission or the Council is a discussion which probably will take place in the coming months and I

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understand the Commission is preparing a draft amendment to the generic regulation but it is not decided yet. That is a question you should ask colleagues from the Commission because I must confess I do not have the latest information. Another question is how we implement UN Security Council Resolution 1822, which was adopted some months or a year ago in New York to improve the fairness of the procedure. You probably know that some Member States plus Lichtenstein really would like to go further than that and add an independent review of the decision of the sanction committee in New York. We will have to look at that very carefully because it is something which might put in question the autonomy of the Security Council to impose sanctions on a state, on a government, on individuals. Resolution 1822 goes in the right direction as well because it improves the way people who are put on the list are informed, gives them the chance to challenge their being put on the list and provides them with a statement of reasons. It improves transparency and the fairness of the procedure, so it is a step in the right direction. Should we undertake another step? Nothing is decided yet.

Mr Nilsson: If I may add one thing, if we have the Lisbon Treaty, which is rather uncertain, there will be a new legal basis in that treaty which will make specific reference to the list and the obligation to have procedures that are in compliance with the rule of law and human rights, procedural safeguards, something like that; I do not remember the exact text, and then it will be put into the context of the Justice and Home Affairs chapter under the Lisbon Treaty, so it will be something that inside the Council will perhaps have the effect of no longer treating this as an external relations issue but rather as an issue of internal security, which may have some consequences in the way that the Council looks at these issues in the future, but there I am speculating.

Professor de Kerchove: The new provision has at least two consequences. The first is that it is very explicit on the need to foresee procedural safeguards, which is good, but the main objective of the provision is to allow the EU in the future to freeze the assets of what we call "internal terrorists". So far the autonomous mechanism of the European Union has only been allowed to freeze the assets of organisations or individuals located outside the European Union because we do not have the legal basis to do it inside the European Union. We have developed that on the basis of Articles 60, 301 and 308 of TEC but it is linked to foreign policy, so we cannot use foreign policy tools to tackle a domestic problem such as the IRA, the ETA, Greek movements and so on. So far, unfortunately, we do not have an EU mechanism (but Member States may have their own) to freeze and put pressure on an EU terrorist organisation.

Mr Nilsson: If I may put on my Swedish hat, may I say that it was in particular Sweden in the negotiations for the Lisbon Treaty that insisted on having a procedural safeguards clause inside this treaty.

Q260 Chairman: I cannot imagine that!

Mr Nilsson: Why? Because the first case was a Swedish one. It caused the Swedish Justice Minister enormous problems in the first headlines every day.

Q261 Lord Hannay of Chiswick: I think I have judged correctly from your answer that you think that the current legislation in the EU is now totally compliant with the European Convention on Human Rights. You cannot say that nobody could ever bring a case, but you are satisfied that the problem has been resolved, as it were, in terms of ECHR compliance?

Professor de Kerchove: My reasoning is probably a bit simplistic but the Court of Justice or the Court of First Instance, I do not remember which, took a decision not that long ago based on a new procedure for autonomous mechanism and considered that the new procedure by which we inform the person, give him or her the chance to challenge the reasons and provide him or her with a statement of reasons, was consistent with the requirements of the rule of law and due process, so since the Court reached that conclusion in relation to the EU autonomous mechanism, and since we replicated the same procedure for the implementation of the decision in New York, I draw the conclusion that normally the Court should reach the same conclusion in respect to New York. That is what I think. You may argue that the two mechanisms are not similar and in New York the remitting process is slightly different, but I think by and large the Court will refrain (but who am I to say that?) from questioning that. Yes, indeed, I do confirm your statement.

Mr Nilsson: I am perhaps a little bit less certain. Was it not a Court of First Instance judgment, the one that you refer to? In any case, I think personally that it is quite unsatisfactory that there is no automaticity of a court proceeding on the issue. I remember that, for instance, Spain in its law, when it comes to listing people, has a clause that says that if someone has been put on a list a court of law has to review that after six months if the person is still on the list, and as a lawyer (and even a judge in a previous life) I think that that is a much more satisfactory system than the system you have today, but, of course, we have made enormous improvements from what we had a couple of years ago.

Q262 Lord Hannay of Chiswick: But it would presumably be really pretty serious if the European Union in any manifestation, the Commission, the

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Council or other, got into a position where it was contradicting a decision by the Security Council?

Professor de Kerchove: Indeed. It is Chapter 7.

Q263 Lord Hannay of Chiswick: It would be a major constitutional problem.

Professor de Kerchove: That is why I said before that we, and by “we” I mean the Member States collectively and in particular the ones sitting in the Security Council, the Permanent Member and the rotating Member States, should keep the sanctions mechanism unchanged because that is one of the few tools that we have and it is pretty efficient so we have to think twice before changing it.

Q264 Chairman: Can I take it from those replies that you are not aware of any cases which are either under way or pending in the Court of Justice, the Court of First Instance or on the Security Council list, and, if I am wrong in getting that implication from what you say, what cases are you aware of?

Professor de Kerchove: Which cases?

Q265 Chairman: Similar cases to the *Kadi* case.

Professor de Kerchove: We have a list of cases I can send you. I do not have it with me but I can send you that this afternoon if you wish.

Q266 Chairman: How many are there?

Professor de Kerchove: My recollection is that we have 20 all in all, but, of course, some have already been decided, so I would say a dozen. We still have another *Kadi* case; I saw that yesterday.

Q267 Chairman: If you have a list that would be very helpful.

Professor de Kerchove: Yes.

Mr Nilsson: It is Legal Services.

Professor de Kerchove: Legal Services keep the list updated.⁴

Q268 Lord Hannay of Chiswick: You have been very frank in answering questions and it has been very helpful to us. One of the things that comes through clearly is that there is at the moment an uneven playing field in the European Union because some countries are applying things strictly, some of them are applying them loosely, some of them are perhaps hardly applying them at all, and so on. How would

you judge the advantages and disadvantages? Is a country like the United Kingdom, which you say applies this more rigorously and more effectively than most, disadvantaged by doing that? Are the countries that do not apply it in any way advantaged by not doing it, or is the main damage to the entity, the European Union as a whole, which is not able to effectively implement what it has willed at the political level?

Professor de Kerchove: In terms of security it may look a bit like that, but since we share the same space we are faced by and large with the same threats to different levels of degree. Having some Member States lagging behind is a problem for all. I was not there when you asked the question on the EU/US Agreement but we launched that the day after 9/11. We are eight years on and this has not yet entered into force. It is shocking. The 2001 Protocol to the EU MLA Convention of 2000 is not in force yet. It is shocking. How is that? It is really important. I remember the discussion we had at the time in order to centralise the information on who is holding a bank account. I remember that one important Member State took the view during the negotiations that it was too costly to set up that sort of mechanism, and the day after 9/11 realised that it should have done that before and so we agreed on tough measures, so how is it that this protocol is not in force yet? To me it is a concern and Hans has said that conventions are no longer an adequate type of legislation because nobody has the power to put pressure on Member States so that they abide by the obligation. I am sorry to say so, but in the First Pillar the infringement procedure remains the best way to ensure a level playing field, not only from the legal aspect but also from the practical aspect. Are the Member States allocating sufficient resources? Are they focusing in an efficient manner? All this should be looked at by someone and it is the role of the Commission to look at this. That is one answer. Are some Member States slow to protect their economic interests? I do not think so. I may be wrong but I think it is more that no-one is interested in a convention at home because it is cumbersome, plus the ministry of foreign affairs has to prepare draft legislation to go to the national Parliament. It does not give you any political benefit, so nobody pushes that, I am afraid. In the country I know best it is like this. It is just that nobody cares.

Mr Nilsson: I am fully in agreement and perhaps I could add a couple of things. When we were young lawyers some of us at least learned *pacta sunt servanda*, so if we have agreed on something at European level we should also implement it. However, it has always been a problem in this particular area, which again the Lisbon Treaty will solve because we will finally have the possibility of

⁴ The list of cases is printed at p. 122–123.

25 March 2009

Ms Mieneke de Ruiter, Professor Gilles de Kerchove and
Mr Hans G Nilsson

having an infringement procedure. The Commission recently, in relation to the Third Money Laundering Directive, took several countries, including Sweden, to the Court of Justice, and rightly so because one should implement what has been decided. Another point is that we have tried also in relation to the so-called Third Pillar to take other measures even though we do not have the infringement procedure. We have set up a peer evaluation system like the FATF has done but we have done that in relation to organised crime, so we have the possibility of evaluating the Member States, sending out teams from other Member States—the Secretariat-General, the Commission, Europol, Eurojust, as members of those teams, and looking at how Member States have actually implemented instruments or policies in relation to this particular area. We have done it in relation to mutual legal assistance, to drugs, to exchange of information, we are in the process of finishing an evaluation on the European arrest warrant and we have just now started the fifth round on the evaluation of financial crime and economic crime. We will not duplicate the money laundering evaluation carried out by the FATF but we will go into other parts of what is financial crime. I think that this system of evaluation is something which is perhaps not as effective as the infringement procedure because there after all it is a court procedure, it is a strong measure—

Professor de Kerchove: With financial penalties.

Mr Nilsson: Exactly, with penalties and so on, but the system of evaluation can mean that you can evaluate not only one particular paragraph in an instrument but the whole system—“How do you do this? Have you set up actors? Have you set up special financial investigators and prosecutors? How do you train them?”, and so on. You can also use this system of evaluation not only as a stick but also as a carrot since you can learn best practice from each other, you can create mutual trust among the people that are involved in the system, and that is also something which I do not think the infringement procedure will do. The infringement procedure is only a stick and not a carrot.

Chairman: Lord Hannay’s question reminded me very closely of the time I was involved in the Council 25 years ago when we implemented milk quotas where French, German and British ministers were not quite hung, drawn and quartered but were pilloried, whereas in some states in southern Europe really nothing was done to implement that at all. It seems to me from what you say that nothing much has changed. You have given us a most interesting morning and I know that some of our witnesses have taken considerable trouble to be with us which we especially appreciate. You have helped us massively, certainly for our afternoon session today when we shall be discussing these matters with the Commission. Thank you very much.

Supplementary memorandum by the General Secretariat of the Council

PROFESSOR DE KERCHOVE’S RESPONSE TO QQ 263–267

Brussels, 21 April 2009

SUBJECT

Update on pending cases before the Court of First Instance and the Court of Justice against restrictive measures adopted by the Council in the context of the fight against terrorism (by category and in chronological order of filing)

I. CASES CONCERNING MEASURES ADOPTED PURSUANT TO UN SECURITY COUNCIL RESOLUTIONS

A) *Before the Court of First Instance*

1. Case no. T-318/01 (*Omar Mohammed Othman v. Council and Commission*)⁹
2. Case no. T-135/06 (*Al-Bashir Al-Faqih v. Council*)¹⁰
3. Case no. T-136/06 (*Sanabel Relief Agency Ltd. v. Council*)¹¹
4. Case no. T-137/06 (*Ghunia Abdrabbah v. Council*)¹²

⁹ OJ C 68, 16.03.2002, p. 13. The Court of First Instance gave judgment on 11 June 2009. Omar Mohammed Othman is also known as Abu Qatada.

¹⁰ OJ C 165, 15.07.2006, p. 29.

¹¹ OJ C 165, 15.07.2006, p. 30.

¹² OJ C 165, 15.07.2006, p. 30.

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5. Case no. T-138/06 (*Taher Nasuf v. Council*)¹³
 6. Case no. T-101/09 (*Elmabruk Maftah v. Council and Commission*)
 7. Case no. T-102/09 (*Abdelrazag Elosta v. Council and Commission*)

B) *Before the Court of Justice*

8. Case no. C-399/06 P (*Faraj Hassan v. Council and Commission*)¹⁴
9. Case no. C-403/06 P (*Chafiq Ayadi v. Council*)¹⁵

II. CASES CONCERNING MEASURES ADOPTED BY THE EU ON AN AUTONOMOUS BASIS

A) *Before the Court of First Instance*

10. Case no. T-37/07 (*El Morabit v Council*)¹⁶
11. Case no. T-49/07 (*Fahas v Council*)¹⁷
12. Case no. T-75/07 (*Hamdi v Council*)¹⁸
13. Case no. T-76/07 (*El Fatmi v Council*)¹⁹
14. Case no. T-157/07 (*OMPI v Council*)²⁰
15. Case no. T-323/07 (*El Morabit v Council*)²¹
16. Case no. T-341/07 (*Sison v Council*)²²
17. Case no. T-348/07 (*Stichting Al-Aqsa v Council*)²³
18. Case no. T-362/07 (*El Fatmi v Council*)²⁴
19. Case no. T-363/07 (*Hamdi v Council*)²⁵
20. Case no. T-276/08 (*Stichting Al-Aqsa v Council*)²⁶
21. Case no. T-409/08 (*El Fatmi v Council*)²⁷
22. Case no. T-85/09 (*Kadi v Commission*)

B) *Before the Court of Justice*

23. Case no. C-576/08 P (*OMPI v Council*)²⁸
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¹³ OJ C 165, 15.07.2006, p. 30.

¹⁴ OJ C 294, 02.12.2006, p. 30.

¹⁵ OJ C 294, 02.12.2006, p. 32.

¹⁶ OJ C 82, 14.04.2007, p. 44.

¹⁷ OJ C 95, 28.04.2007, p. 43.

¹⁸ OJ C 117, 26.05.2007, p. 22.

¹⁹ OJ C 117, 26.05.2007, p. 22.

²⁰ OJ C 140, 23.06.2007, p. 43.

²¹ OJ C 269, 10.11.2007, p. 52.

²² OJ C 269, 10.11.2007, p. 58.

²³ OJ C 269, 10.11.2007, p. 61.

²⁴ OJ C 269, 10.11.2007, p. 65.

²⁵ OJ C 269, 10.11.2007, p. 66.

²⁶ OJ C 236, 13.9.2008, p. 15.

²⁷ OJ C 301, 22.11.2008, p. 54.

²⁸ OJ C 55, 7.3.2009, p. 15.

WEDNESDAY 25 MARCH 2009

Present	Garden of Frogmal, B. Hannay of Chiswick, L.	Henig, B. Jopling, L. (Chairman)
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**Memorandum by the European Commission
DG Internal Market and Services & DG Justice, Freedom and Security**

First of all, we would like to thank the House of Lords for its interest in the effectiveness of the EU fight against money laundering and terrorist financing. This issue is a priority for the European Commission, the Council and its Counter-Terrorism Coordinator, M. Gilles de Kerchove, the European Central Bank, the CEBS-CESR-CEIOPS Anti-money Laundering Task Force, Europol and Eurojust, not to mention Member States of the European Union.

The complexity and international character of money laundering and terrorist financing mean that a multidisciplinary and multilateral approach is essential. This requires the involvement of many stakeholders, be they public authorities or “gate keepers” from the private sector, and requires strong cooperation between all these actors. To be effective, actions against money laundering and terrorist financing have to be undertaken, in a mutually reinforcing way, at all levels: national, regional and international.

The events of 11 September 2001 have brought significant changes to the world. One such change has been a strengthening of global defences against money laundering and their extension to the fight against terrorist financing. The Financial Action Task Force (FATF) with its 34 members from all continents (including 15 Member States of the EU and the European Commission) has been a key actor in this respect. The FATF took immediate action in October 2001 by issuing a series of special recommendations designed to fight terrorism financing. It further reinforced in June 2003 its 40 anti-money laundering recommendations.

The FATF recommendations as well as the UN Security Council resolutions against Al Qaeda and the Taliban have been duly implemented by Member States of the European Union. In many instances, Member States considered that the European level is the appropriate one to adopt measures in order to comply with international obligations: this allows for a level playing field *vis-à-vis* all “gatekeepers” from the private sector, notably banks and money remitters. In some areas, Member States have gone beyond international requirements, for example concerning the recent UN Security Council Resolutions against nuclear proliferation (UNSCRs 1747 and 1803). At the same time, many of the measures adopted at Community level are still relatively recent. In many cases, Member States are still working on the implementation and application of these instruments which require adaptations to be made, new structures to be created and new procedures to be adopted. All this takes time of course and this process is not yet completed.

It should also be noted that the Council of Europe is also an important source of law as well as a tool for European cooperation in relation to more traditional judicial cooperation. In this respect, the European Community is expected to ratify in the coming weeks the Council of Europe Convention of 2005 on laundering, search, seizure and confiscation of the proceeds from crime and on the financing of terrorism.

We understand that the focus of the inquiry of the House of Lords is on the nature and extent of Member States’ cooperation in the fight against money laundering and terrorist financing. This issue is fundamental for both practical and political reasons. Firstly, it is important to ensure that there is no major weakness in the anti-money laundering and counter-terrorist financing defences at Member State level as this could potentially affect the whole EU and beyond. Secondly, fostering coordination and cooperation between Member States is a major objective of the European policy in this area. At this stage, however, for the reason mentioned above, it may be rather early to get a full picture of Member States’ cooperation in this field.

Under this proviso, you will find annexed a coordinated reply from the European Commission services to the questions raised in the inquiry. Ideally, the viewpoint of our services ought to be completed by those of EU Member States as well as those of some major partners of the EU.

Jörgen Holmquist
Director General
DG Internal Market and Services

Jonathan Faull
Director General
DG Justice, Freedom and Security

REPLY FROM THE SERVICES OF THE EUROPEAN COMMISSION

Cooperation with and between Financial Intelligence Units (FIUs)

1. *How effective is cooperation among FIUs, and between FIUs and other authorities? What are the practical results of this cooperation?*

The extent of bilateral cooperation between EU FIUs is closely linked to the applicable legal framework. At the EU level, the exchange of information between FIUs is regulated by Council Decision 2000/642/JHA²⁹, which provides *inter alia* for:

- Their obligation to exchange information, spontaneously or upon request
- The obligation for Member States to ensure that the status of an FIU (law enforcement, administrative, judicial) will not affect their performance under the Decision
- The manner in which requests to other FIUs should be made and handled (including cases when an FIU may refuse to provide information)
- Conditions and restrictions on the use of the information provided
- A legal framework for a spontaneous exchange for information without a request
- An obligation to provide secure communication channels

The Commission facilitates cooperation and promotes the exchange of information between FIUs through the informal EU FIU Platform and the FIU-NET system.

The EU FIU Platform is an informal forum for discussion and the exchange of best practices between FIUs supported by the Commission. The Platform has so far produced reports on feedback on money laundering and terrorist financing cases and typologies and on confidentiality and data protection in the activity of FIUs.³⁰ Future reports should address the content of suspicious transaction reports and international cooperation.

FIU-NET is a secure communication channel for the exchange of operational information between EU FIUs in which almost all EU FIUs participate. The system is managed by the FIU-NET Bureau, hosted within the Ministry of Justice of The Netherlands. 17 Member States are connected (or in the process of being connected) to the system, with a current volume of approximately 3,000 messages (information requests or replies) per year. A project to further improve the FIU-NET system is currently ongoing with the financial support of the Commission (Programme “Prevention of and fight against crime”).

Apart from the information on FIU-NET, the Commission has no overall statistics on the bilateral cooperation taking place between EU FIUs (which often use the global secure system Egmont Secure Web). It is therefore difficult to assess the practical results stemming from this cooperation.

FIUs also exchange information with other authorities (law enforcement agencies, tax authorities, financial services supervisors), but little information is available on these exchanges. Some indications can be drawn from the study on feedback practices described in point 2 below. For example, the majority of EU FIUs receive feedback from supervisory authorities on their annual inspections on reporting entities.

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

An ongoing Commission study analyses the provision of feedback between the reporting entities, the FIUs and law enforcement authorities. Although the study is not yet finalised, there are indications that feedback is not provided to the private sector in a timely manner; that structural case-by-case feedback is provided only in a limited number of instances; and that more substantial feedback is generally required by the private sector. The Commission intends to discuss with FIUs in the EU FIU Platform concrete ways to improve feedback mechanisms, including with regard to the private sector.

²⁹ 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 L 271, p. 4.

³⁰ Available at http://ec.europa.eu/internal_market/company/financial-crime/index_en.htm#fiu-platform

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

The Commission study will not include data on the extent of feedback provided on terrorist financing issues. However, the reporting entities interviewed, particularly banks, highlighted the difficulty of detecting suspicious activities related to terrorist financing and recommended that more information be provided to them by intelligence and security services.

4. *To what extent are alternative remittance systems appropriately covered by obligations of cooperation in this context? What will be the impact of the implementation by Member States of the relevant provisions of Directive 2007/64/EC in this regard?*

Article 36 paragraph 2 of the Third Anti-money Laundering Directive requires that all money transmission or remittance offices in the EU are either licensed or registered in order to operate their business legally. The conditions thereof are determined by the provisions of the Payment Services Directive (Directive 2007/64/EC) which is due to be implemented in national law before 1 November 2009.

In particular, every application for authorisation as a payment institution has to be accompanied by “a description of the internal control mechanisms which the applicant has established in order to comply with obligations in relation to money laundering and terrorist financing under Directive 2005/60/EC and Regulation (EC) No. 1781/2006” (Article 5(f)), by evidence of “good repute” of directors and persons responsible for its management (and, where relevant, persons responsible for the management of the payment services activities of payment institutions) (Article 5(i)) and, if applicable, a description of outsourcing arrangements, including agents and/or branches (Article 5(g), together with Article 17(6) according to which, “if the competent authorities of the host Member State have reasonable grounds to suspect that, in connection with the intended engagement of the agent or establishment of the branch, money laundering or terrorist financing (...) has taken place or been attempted, or that the engagement or such agent or establishment of such branch could increase the risk of money laundering or terrorist financing, they shall inform the competent authorities of the home Member State, which may refuse to register the agent or branch, or may withdraw the registration, if already made, of the agent or branch”. The Directive provides for on-going supervision of payment institutions, which are empowered to carry out controls and deciding on withdrawal of the authorisations if the conditions for authorisation are not met anymore. This licensing regime is valid for the entire EU territory so the fully licensed payment institution gets the right to passport its services, including, where applicable, those of money remittance (see point 7 of the Annex and recital (7)).

Article 26 of the Directive provides for a waiver regime whereby natural or legal persons unable to meet all those strict conditions may nevertheless carry out payment services in the Member State where they have their head office or legal residence (so no passport activities), after having been duly registered. This waiver regime aims to “bring all persons providing remittance service within the ambit of certain minimum legal and regulatory requirements”.

In addition, Article 29 bans payment activities without an appropriate licence or registration and Articles 80 and 81 provide for a regime of complaints and sanctions for breaches of obligations under the PSD. All this system is fully in line with FATF Special Recommendation VI on alternative remittance.

The PSD therefore will allow new payment service providers (including **money remitters**, but also supermarkets, or, in some cases, telecom or IT providers), to compete and offer their services throughout the Internal Market, in full respect of the AML rules.

Alternative remittance providers, such as Hawalas, who would not be registered or licensed according to the provisions of the Payment Services Directive and would nevertheless pursue their activities would be infringing the law.

EU internal architecture

5. *To what extent is the EU internal architecture adequate to counter current and future challenges?*

The internal architecture of the EU reflects the complexity of a fight against money laundering and terrorist financing requiring a multidisciplinary approach as well as of the allocation of competence between the European level and the national level, between the intergovernmental level and the Community one. The internal architecture of the EU is complex. Whether this complex architecture is adequate to counter current and future challenges is difficult to tell. Furthermore, any judgment will depend on the expectations one may have *vis-à-vis* that architecture, in particular what the role of European institutions should be. Should it be

strategic or operational? It also depends, for example, on the criteria for addressing the effectiveness and cooperation between Member States.

The emphasis at European level has thus far been on coordination and programming (*see for instance the EU Counter-Terrorist Financing Strategy*) as well as on legislation (*eg the Third Anti-money laundering Directive*,³¹ *the Regulation on information on wire transfers*³² or *the Cash Control Regulation*³³) and voluntary convergence of practices through soft law (*eg the Commission recommendation for a code of conduct on not-for-profit organisations or the CEBS-CEIOPS-CESR AML Task Force's Common understanding on obligations imposed by European Regulation 1781/2006*) or the availability of platforms (*such as the EU Committee for the Prevention of Money Laundering and Terrorist Financing chaired by the Commission*), more than on the operational side. However, such objectives are not mutually exclusive and the work carried out by Europol and Eurojust present a clear operational component (cf. Europol pan-European analysis of threats and risks). Furthermore, some joint actions have been conducted by a number of Member States, like for instance the 2008 ATHENA joint operation between customs authorities.³⁴

Is the current architecture the optimal one? Systems can be improved. However, it is probably the best one can have under the constraints set by the multifaceted dimension of the issue at stake and by the current EU Treaty. Nevertheless, action at EU level will never be a substitute to the groundwork that has to be carried out at Member State level.

6. *What are the respective roles of Europol and Eurojust in countering money laundering and terrorist financing?*

Europol plays the same role in relation to money laundering and terrorist financing as in relation to other serious offences for which it has competence under the Europol Convention.

Europol aims at improving co-operation at EU level among the competent authorities in preventing and combating terrorism, unlawful drug trafficking and other serious forms of cross-border organised crime.

Money laundering usually represents the final phase of the majority of the organised crime activities. The international dimension of organized crime and the use of global financial systems to channel, conceal, secure and launder the proceeds of crime have led to difficulties being experienced by law enforcement agencies in their endeavors to identify, detect and prosecute perpetrators.

The Europol Serious Crime Department (in particular its Financial and Property Crime Unit) engages in economic and financial investigations, investigations of organised crime and investigations related to money laundering crimes on a European scale.

Efforts to improve the detection of suspicious transactions meant that criminal organisations tend to constantly diversify money laundering processes. In this respect, Europol set up in cooperation with the Member States (based on article 30-1 B of the Treaty on the European Union), a project to collect and analyze EU suspicious transactions or activity reports handled by Police or Justice authorities. This tool, managed as an Analysis Working File (AWF SUSTRANS), aims at establishing links between suspicious transactions reported by a Member State and ongoing investigations carried on by law enforcement agencies of other Member States.

Europol is involved together with some Member States in a project (€STR) aiming at creating a Money Laundering Financial Investigation Unit Network to support the effectiveness of the AWF SUSTRANS and to enhance its value as a basic tool for financial intelligence led policing. This ongoing project received the financial support of the Commission (Programme "Prevention of and fight against crime").

Europol acts as permanent Secretariat for CARIN, an informal network of judicial and law enforcement experts in the field of asset forfeiture. CARIN started as an EU initiative but is expanding globally, with 44 states and jurisdictions and 7 international organisations registered as members. One law enforcement and one judicial contact have been nominated from each of those states and jurisdictions to assist in cross border co-operation in relation to tracing, freezing, seizing and confiscation of assets.

The Europol Criminal Asset Bureau (ECAB) assists Member States' financial investigators to trace the proceeds from crime, when assets have been concealed in other EU Member States. Investigators can request Europol to make international operational asset tracing enquiries if there are factual indications or reasonable

³¹ Directive 2005/60/EC on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing

³² Regulation EC/1781/2006 on information on the payer accompanying transfers of funds

³³ Regulation EC/1889/2005 on controls of cash entering or leaving the EU

³⁴ In the field of customs cooperation, a Joint Customs Operation ATHENA focusing on money laundering linked to terrorism financing and other illicit activities took place in September 2008. The customs administrations of 22 Member States, together with five third countries (Algeria, Croatia, Morocco, Norway and Tunisia), OLAF, the Commission, the World Customs Organisation (WCO), Europol and Interpol have taken part in this operation. Financial Intelligence Units (FIUs) have also been involved in implementing the operation.

grounds for believing that an organised criminal structure is involved in the offence; two or more EU Member States are involved in the criminality; and the offence falls within the mandated crime areas of Europol (which include money laundering).

Eurojust is an organisation consisting of one national member seconded by each Member State (either a prosecutor or judge with experience in judicial cooperation). Eurojust aims at enhancing the effectiveness of the competent authorities within Member States dealing with the investigation and prosecution of serious cross-border and organised crime by coordinating investigations and prosecutions and speeding up judicial cooperation, in particular obtaining information and mutual assistance. Eurojust's main focus is to improve multi-lateral cooperation.

The overall number of money laundering and terrorist financing cases handled by Eurojust is unknown, but in the first eleven months of 2008 it handled 22 terrorism cases (which may include terrorist financing) and 97 money laundering cases. The large majority of its casework (over half) is related to fraud.

Eurojust has internal coordination teams on Financial and Economic Crime and on Terrorism. Both teams play a day-to-day coordination role in concrete cases of cross-border investigations and prosecutions. Eurojust also provides assistance to the Member States in setting up Joint Investigation Teams (JITs).

The European Judicial Network (EJN) is a network of contact points in the Member States (prosecutors, judges or authorities in the Ministries of Justice) which assists judicial authorities to cooperate expediently and coordinate investigations and prosecutions by establishing direct contacts between each other. EJN has a website accessible to all judicial practitioners with information on competent authorities, national legislation etc. The EJN also organises regular meetings for the contact points to meet and exchange best practice. The focus of the work of the EJN is on improving bilateral cooperation.

International cooperation

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

There is as yet no consolidated view of the results of the third round of mutual evaluations of EU Member States carried out by the FATF and Moneyval, as this round has not yet been completed—still five EU Member States remain to be assessed against the 40 + 9 revised FATF recommendations. To date, 10 Member States have been assessed by the FATF and 12 by Moneyval under the third round of mutual evaluations. The FATF recommendations at stake are Recommendations 35 to 40, with all of which assessed Member States in their overwhelming majority are either compliant or largely compliant. A compilation of the ratings and major remarks attributed to the assessed Member States are provided in an annex to this document [*not printed*].

It is worth noting that in the context of the financial crisis, the G20 in its Action Plan of 15 November 2008 has advocated the need for “national and regional jurisdictions to implement national and international measures that protect the global financial system from uncooperative and non-transparent jurisdictions that pose risks illicit financial activity”. Some exploratory work on counter-measures (FATF Recommendation 21) is already being conducted by the FATF. This should lead to a further convergence of Member States' practices in this respect. Further information is provided on related issues under the section entitled “*compliance and equivalence*”.

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

The Council of Europe conventions on Mutual assistance in criminal matters of 1959 and the EU Convention of 2000 on mutual legal assistance, as well as their protocols constitute a formal framework for cooperation in criminal matters within the EU. Between the Member States the 2000 Convention introduced interesting and important novelties. Its 2001 Protocol aims at further improving mutual assistance within the EU *inter alia* concerning the execution of rogatory letters in respect to banking information. Refusal of mutual assistance on the basis of either banking secrecy or commercial confidentiality rules is explicitly denied. Specific provisions were introduced in order to facilitate the transfer of information on bank accounts and banking operations. The fiscal exception is being completely banned, and in as far as serious forms of organized crime or money laundering are concerned, the possibilities of refusal letters rogatory requesting information on the existence of bank accounts are in practical terms much reduced.

Despite numerous novelties, the formal framework for cooperation is far from complete and it shows a certain lack of balance as no global approach has been taken in revising the traditional European mutual legal assistance treaties and some questions were overlooked. The Commission has on multiple occasions announced that the entire mutual assistance *acquis* will need to be replaced in the years to come with mutual recognition schemes, building ideally on full faith and trust between the Member States. In that respect, the Council Framework Decision 2008/978/JHA of 18 December 2008 on the European evidence warrant for the purpose of obtaining objects, documents and data for use of proceedings in criminal matters³⁵ constitutes a first step.

The final report on mutual legal assistance in criminal matters of 2001 made it clear that, while mutual assistance is not without its faults, the criticism habitually levelled at it that it is slow, inefficient and powerless is excessive; in general mutual assistance does not operate as badly as it is reputed to do.

There is also an international framework for cooperation on confiscation of the proceeds of crime. A number of international Conventions include provisions on the confiscation of criminal proceeds in order to promote international cooperation in the identification, tracing, freezing and confiscation of criminal assets. The most relevant are the UN Convention against Transnational Organized Crime (“UNTOC”), the UN Convention against Corruption (“UNCAC”) and the Council of Europe Conventions on Laundering and Confiscation (“Strasbourg Conventions”), to which EC accession is pending. A number of important provisions of these conventions are not yet incorporated into Community legislation. The Commission will continue its efforts to ensure that the Community and the Member States ratify and implement these Conventions without delay.

Council Decision 2007/845/JHA on cooperation between Asset Recovery Offices requires Member States to set up or designate, by 18 December 2008, national Asset Recovery Offices which will act as national contact points for confiscation-related activities and promote expedient EU-wide tracing of assets derived from crime. So far the Commission has received only six notifications from the Member States.

The recent Commission Communication on the proceeds of organized crime³⁶ provides an overview of the EU texts aiming at ensuring a common approach to confiscation. It states that Framework Decision 2001/500/JHA (which harmonised some Member States’ provisions on confiscation and criminal sanctions for money laundering) is relatively well transposed in most Member States.

The Commission issued in December 2008 a report³⁷ on the implementation of Framework Decision 2003/577/JHA, which applies the principle of mutual recognition to orders freezing property or evidence. The report shows that implementation is not satisfactory given the relatively low number of notifications received and because the implementing laws notified indicate numerous omissions and misinterpretations with respect to the Framework Decision.

Little information is available on the practical application of the provisions that should ensure that assets or evidence located in one Member State can be frozen on the basis of a decision taken by a judicial authority in another Member State and transmitted directly to the executing judicial authority by way of a specific certificate. It appears that the certificate to request the execution of freezing orders is rather difficult to complete and does not contain all the necessary fields. Therefore, judicial authorities tend to revert to the standard mutual legal assistance forms.

The Commission published in December 2007 an implementation report on Framework Decision 2005/212/JHA, which aims at ensuring that Member States introduce effective rules on confiscation, including rules on proof with regard to the source of the assets concerned. The report shows that most Member States are slow in putting in place measures to allow more widespread confiscation.

It is too early to assess the implementation of Framework Decision 2006/783/JHA, which applies the principle of mutual recognition to confiscation orders.

The Communication on the proceeds of organised crime concludes that the existing legal texts are only partially transposed. Some provisions of the Framework Decisions are not very clear with the result that transposition into national legislation is patchy. As it is essential to have in place expedient and effective mechanisms to freeze and confiscate assets, the Communication suggests that a recasting of the existing EU legal framework should be considered.

³⁵ OJ L 350 of 30.12.2008, p.72-91.

³⁶ COM (2008) 766 final.

³⁷ COM (2008) 885 final.

The Communication also highlights 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. It recommends an increased and more effective use of confiscation procedures.

A Commission study assessing the effectiveness of the Member States' practices in the identification, tracing, freezing and confiscation of criminal assets is currently being finalized.

EU-UN cooperation

10. *What is the extent of EU-UN cooperation on financing of terrorism? What are the longer-term implications of the Kadi judgment?*

The EU has implemented UN Security Council Resolutions imposing sanctions as part of its Common Foreign and Security Policy. Article 301 of the EC Treaty provides a specific legal base for the application of economic sanctions against one or more third countries. Using an additional legal base, Article 308 of the EC Treaty, this provision has been the basis for implementation of asset freezing measures targeting terrorist groups as required by a series of UN Security Council Resolutions, including Resolutions 1373(2001) and 1390(2002). Council Regulations (EC) No 2580/2001 and 881/2002 are the relevant legislation.

The longer-term implications of the *Kadi* and *Al Barakaat International Foundation* judgment of the Court of Justice of 3 September 2008 (Cases C-402/05 P and C-415/05 P) cannot be fully assessed at present. The Court of Justice held that the EU, when deciding to freeze the assets of an individual or entity designated by the UN Security Council or the Al Qaida and Taliban Sanctions Committee, must communicate the grounds on which that decision is based to the individual or entity concerned, in order to observe the rights of defence, in particular the right to be heard, and the right to judicial review. It should be noted in this regard that the judgment concerns a Council decision to freeze assets which did not include the specific grounds for listing of the individual concerned. The Court of Justice has not yet had to review the substance of any decision to freeze assets based on a designation by the Al Qaida and Taliban Sanctions Committee. Moreover, asset freezing regulations implementing UN country-specific sanctions usually contain specific grounds for listing, which are therefore publicly available.

Some Member States are members of the UN Security Council and of the UN Al Qaida and Taliban Sanctions Committee. Several Member States, including non-members of the Committee, have made proposals for designation to the UN Al Qaida and Taliban Sanctions Committee.

Monitoring implementation

11. *What EU mechanisms exist for monitoring implementation of the relevant legislative measures, and what results in terms of formal compliance and effective implementation have so far emerged from the use of those measures?*

The Commission considers that it is fundamental to ensure a correct and timely implementation by Member States of the relevant **Community measures**. In this respect, the Commission initiates infringement procedures against non-compliant Member States (which are the subject of press releases) and pursues these cases before the European Court of Justice in Luxembourg, if need be. Besides maintaining pressure on non-compliant Member States by referring to legal proceedings, the Commission also makes use of bilateral meetings, scoreboards and in certain cases letters from the Commissioner to the relevant ministers in the non-compliant Member States recalling their obligations and requesting a rapid implementation of the relevant Community measures. By making use of the full toolkit at their disposal, the Commission services have kept the pressure up on the non-compliant Member States.

However, the remedial procedures have long lead times and often lack teeth. Pecuniary sanctions are only imposed by the European Court of Justice if a Member State is brought before it for a second time after having failed to conform to a previous decision of the Court. This is why the Commission has heavily invested in upstream cooperation with and assistance of Member States in the implementation phase of directives, through notably the holding of transposition meetings. In spite of these efforts, there are still instances where for various domestic reasons, Member States fail to implement Community legislation within the agreed deadline. At present, seven Member States still have not fully transposed the Third Anti-Money Laundering Directive. However, this does not mean that no rules at all are in place, as the two previous directives were already implemented in national law. The Commission is expected to publish a report on the application of the directive that will address substantive issues around spring 2010.

Council Regulations (EC) No 2580/2001 and 881/2002 provide for the freezing of assets of individuals and entities included in the EU list drawn up pursuant to Common Position 2001/931/CFSP and in the UN Al Qaida and Taliban list, respectively. The Council has agreed Best practices for implementation of asset freezing regulations, which are set out in Council document 8666/1/08 of 24 April 2008.

These Regulations are enforced and monitored using the mechanisms that are foreseen for all Regulations enacted in accordance with the Treaty establishing the European Community. These mechanisms include the procedure set out in Articles 226-228 of the Treaty. In addition to their obligations under the Treaty, Member States have to report to the UN Security Council, as required by relevant Resolutions.

In its country-specific evaluation reports the FATF reviews, inter alia, Member States' compliance with the FATF Special Recommendations on Terrorist Financings. Special Recommendation III covers asset freezing required by the relevant UN Security Council Resolutions.

For the **legal acts issued under the European Union "third pillar"** (police and judicial cooperation in criminal matters), such as EU Framework Decisions or EU Council Decisions, the Commission does not have the powers to launch infringement procedures and bring Member States in front of the European Court of Justice for incomplete or incorrect transposition. On these texts, the Commission issues implementation reports addressed to the Council of the European Union

The Commission issued in December 2007 a report on the implementation of this Council Decision 2000/642/JHA on the exchange of information and cooperation between FIUs³⁸. The report concluded that Member States can be largely considered as legally compliant with most of the key requirements of the Decision, but that more needs to be done in terms of operational cooperation. The report also underlined a lack of legal clarity on how data protection rules may affect the exchange of information between EU FIUs. It highlights the need for possible complementary measures (in particular operational guidelines). In particular many administrative FIUs cannot exchange police information or can provide such 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. There is no common understanding of what information is accessible to FIUs and what "relevant information" is to be exchanged.

12. *What are the implications of those results for cooperation within the EU, and more broadly?*

Whether this situation has implications on cooperation between Member States is hard to tell, as national authorities tend to shy away from informing the Commission services about intra-EU cooperation difficulties. There have been instances where the Commission has incidentally been informed of such problems. These happened to be addressed at international level too which contributed to their orderly resolution. Measuring effectiveness and evidencing it is now becoming part of the culture of the European Commission. The ex-post evaluation of the third anti-money laundering directive will constitute a first step in this direction in the AML/CFT³⁹ area. Tools as peer review, benchmarking or the sending of "operational audit" teams are more frequently used in international fora than at EU level at in this field. The work of the FATF and Moneyval with the mutual evaluation reports, not to mention the IMF and the Financial Services Assessment Programme, represents a precious proxy for the European institutions with regard to the monitoring and assessment of the effectiveness of the AML/CFT systems in place in EU Member States.

It should be noted that the Commission discussed the conclusions of the report on Council Decision 2000/642/JHA on FIU cooperation with the Member States (Council Multidisciplinary Group on Organised Crime) and with the FIUs within the informal EU FIU Platform. Although discussions are still ongoing, it seems likely that the Commission and the FIUs will develop a set of operational guidelines on Council Decision 2000/642/JHA (covering which information can currently be exchanged and how, what intelligence cannot be exchanged and why). At the same time a reflection is ongoing on the added value of updating the Council Decision.

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

Whilst at the EU level, the third Anti-Money Laundering Directive was not accompanied by an impact assessment; it is the Commission's services intention –in the medium term, once national legislation in place and operational- to provide some ex-post evaluation of the Directive and its effects. Some work is already carried out on the **cost of compliance** with the Directive in the context of a more general report⁴⁰ mandated by the Commission which will soon be published. This report could be sent once available, if so wished.

³⁸ COM(2007) 827 final.

³⁹ Anti-Money Laundering and Counter-Terrorist Financing

⁴⁰ Europe Economics' Study on the Cost of Compliance with Selected FSAP Measures.

Furthermore, the European Commission and a few Member States notably the Netherlands and the United Kingdom have been insisting for international fora and the FATF in particular to conduct impact assessments when proposing new measures. Such a discipline, by forcing the reflexion on the adequacy of the potential solutions to the problems identified and their relative cost/benefit, might allow for more enlightened decisions and hence their greater acceptability by those who have to comply with them notably the private sector. This issue is being discussed at the FATF. Some general reluctance has been expressed within the FATF because of the difficulty to measure the benefits of both preventative and sanctioning measures such as the provisions on anti-money laundering.

At EU level, work is being conducted by the Commission services in relation with Member States to develop basic, homogeneous statistics on anti-money laundering. This project is part of a more ambitious plan to develop statistics on crime and criminal justice⁴¹. Further consideration is given within the Commission to a possible assessment of the effectiveness of anti-money laundering/terrorist financing systems, through cost benefit analysis. The Commission issued in 2008 a study on two alternative methods to identify beneficial owners which provides the first example of cost-benefit analysis carried out on a pan-European scale (although on a single topic). A project on conducting a cost-benefit analysis of anti-money laundering/terrorist financing systems in all 27 Member States has been submitted for co-financing under the Commission funding Programme “Prevention of and fight against crime” and is currently being evaluated.

More generally, both the FATF and the European institutions have engaged into formal or informal dialogues with the private sector. The FATF has conducted such an exercise with the financial industry as well as with the legal professions and all other professions or activities (eg casinos) subject to anti-money laundering requirements, in order to jointly develop guidance on the application of the risk-based approach to combating money laundering and terrorist financing. At EU level, there is a trustful dialogue with the banking industry and the legal professions, notably through their European organisations. This takes the form of regular informal meetings between Commission services and the European organisations.

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

A possible review of the existing EU legislation or international standard is not excluded. This will essentially depend on whether a need arises to address unforeseen issues which are not catered for by the existing measures or standards, or indeed issues relating to the evaluation of the effectiveness of existing measures. In this respect, it should be underlined that the EU legislation regularly evolves over time, most recently because of the very need for the EU to comply with the Resolutions of the UN Security Council on nuclear proliferation which definitely have a bearing on the private sector. Besides this, it should however be emphasized that many countries around the world are still busy with the implementation of the global standard set by the FATF and the third Round of Mutual Evaluations conducted by the FATF, Moneyval and the IMF is not finished yet. At EU level, as mentioned earlier, most of the relevant measures are relatively recent and Member States have hardly completed their transposition into national legislation. In such a context, it is too early to say whether the third Anti-Money Laundering Directive in particular would need to be revisited. This will depend on the outcome of the report on the application of the Directive foreseen for 2010 and, more likely, on a subsequent ex-post evaluation. A need for a review of the Directive may then appear or not.

The private sector and notably banks have a fundamental obligation of vigilance for the good of society as well as for their own reputation. At the same time, commercial organisations have legitimate economic objectives that should not be undermined by the imposition by public authorities of disproportionate requirements in the search for information. Disproportionate expectations could sap the current level of good cooperation between public and private actors in the fight against money laundering and terrorist financing. The challenge here is for the legislator to strike the right balance. A strict application of concepts of necessity, proportionality, effectiveness and efficiency is important to help determine who has to do what and to what extent, between public authorities and “gatekeepers” so that financial or human resources are best applied. On the other hand, the private sector should respect the objectives of the anti-money laundering rules and not refer to them, as this has been the case in one Member State in particular, to hide their commercial policy to refuse the opening of bank accounts to individuals residing abroad on grounds because of, or perception of, a greater risk of fraud.

⁴¹ COM(2006)437—COMMUNICATION FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT, THE COUNCIL AND THE EUROPEAN ECONOMIC AND SOCIAL COMMITTEE—Developing a comprehensive and coherent EU strategy to measure crime and criminal justice: An EU Action Plan 2006—2010

Compliance and equivalence

15. What are the powers and procedures with respect to those third countries which fail properly to implement international standards in these areas? Are these adequate?

With regard to countries which fail properly to implement the international standard, a two-step process is provided in the global standard set by the FATF. First financial institutions should give attention to business relationships and transactions with persons, including companies and financial institutions, from countries which do not or insufficiently apply the global standard. Where these countries continue not to apply or insufficiently apply the global standard, countries may apply appropriate countermeasures. National legal systems provide for a broad range of measures and countermeasures may escalate to restrictions or prohibitions on certain transactions. It seems important to keep in mind that the ultimate purpose of these measures is to protect the international financial system from identified deficiencies and more work in this area is not to be excluded. The work of the G20 in relation with the implementation of its 15 November 2008 Action Plan might lead to an international convergence of the responses toward “failing” countries. The issue of the appropriateness and effectiveness of counter-measures will probably be discussed in this context. Similar discussions might take place at the next FATF Plenary in February 2009.

16. *Does the 2005 Directive adequately encourage non-EU States which have introduced equivalent systems to counter money laundering and the financing of terrorism? How does the system for determining equivalence operate in practice?*

The Third Anti-Money Laundering Directive provides the possibility for Member States in certain situations to give “Community treatment” to third countries complying with certain technical criteria (this is referred to as third country equivalence). In spring 2008, Member States agreed on a Common Understanding on third country equivalence for the purposes of the application of relevant provisions of the Directive. The Common Understanding which includes the list of third countries concerned was published in April 2008 on the Commission’s website upon request of the Member States. This list is the property of the Member States and Member States may foresee a review of this list, if need be. The Directive does not grant the Commission a mandate to establish a positive list of equivalent third countries.

Examination of Witnesses

Witnesses: MR PHILIPPE PELLÉ, Deputy Head, Company Law, Corporate Governance and Financial Crime, MRS AGNETE PHILIPSON and MR MARIANO FERNANDEZ SALAS, Directorate General for the Internal Market and Services (DG MARKT), MR JAKUB BORATYŃSKI, Head of Unit on Organised Crime, MR SEBASTIANO TINÉ, Head of Financial Crime Sector, and MR MICKAEL ROUDAUT, Directorate General for Justice, Freedom and Security (DG JLS), examined.

Q269 Chairman: Welcome. As you know, this Committee is doing a study on money laundering and the financing of terrorism. We have been taking evidence in London and this is our day to be in Brussels. We talked to the Council this morning and we are delighted that so many of you have turned out in force. What in the view of the Commission are the major challenges presently facing European and international efforts to combat effectively money laundering and the financing of terrorism? That is an extremely broad question. Some of you may feel the questions are directed to one side or the other but if any of you want to chip in and follow the main answer we would welcome that very much. Finally, the evidence, as you realise, will be put on to the parliamentary web immediately and if, after this meeting, you have any additions that you think would be helpful to us we would welcome supplementary evidence on paper.

Mr Pellé: I will kick off if I may by introducing myself. My name is Philippe Pellé. I am the Deputy Head of the Unit in charge of Company Law,

Corporate Governance and Financial Crime and that unit belongs to DG Internal Market and Services. Our Directorate General is in charge of EU regulation for financial services in general and the free movement of capital. I chair the Committee for the Prevention of Money Laundering and Terrorist Financing. That is a committee on which Member States sit. We have 27 representatives of Member States and the task of the committee is to assist the Commission in its regulatory task. I also lead the Commission’s delegation to the FATF. I am accompanied today by two colleagues from our department—Agnete Philipson and Mario Fernandez Salas. We would like to thank you for giving us the opportunity to present the views of the Commission Services. We are not in a position to speak for the College of Commissioners because none of us is a commissioner, so we are speaking on behalf of the Commission Services. Also, none of us is a native English speaker either so we crave your indulgence in this respect.

Q270 Chairman: You are doing very well.

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Mr Pellé: We will do our best to provide you with further information in relation to the written evidence we submitted at the end of January.

Mr Boratyński: My name is Jakub Boratyński. I am the Head of the Unit on the Fight against Organised Crime, which is part of Directorate General Justice, Freedom and Security. I am accompanied today by Sebastiano Tiné, Head of our Financial Crime Sector, and Mickael Roudaut, who joined us very recently and who deals specifically with money laundering. To give you a little bit of background in the area of money laundering and terrorist financing and why DG Markt is focusing on the preventive side, we focus our efforts on the law enforcement side. We are responsible in general for harmonisation of penal legislation of the Member States and for law enforcement issues. In that context we are responsible for implementation of the Council's Decision on FIU cooperation as well as dealing with EU legal texts on confiscation of the proceeds of crime. We are also engaged in improving co-operation between FIUs and in particular there is an FIU.NET project and your questions focus on this as well. Finally, thanks to the generosity of the Member States, we have quite some money to spend and our fight against organised crime programme allows us to support numerous efforts in this field.

Mr Pellé: Your question is indeed a challenging one because it is relatively broad and I do not pretend to know the full answer to this. Also, any answer we may give will be a bit speculative because the challenges are many and we have challenges in terms of future threats and some of those challenges we know; others we do not. Some may be in relation to threats we barely perceive at this stage; others relate to the fact that we might need to and should improve the existing systems, and some challenges may be of an organisational nature. In this respect one real challenge is to ensure that different actors and parts of the EU policies do function in a very joined-up and effective way. It is not a secret: even at Member State level, organisations are fighting with this realisation. As to future and existing threats, I would only note that the spring European Council, which took place not long ago, in the context of the current crisis, called for the G20 in London to fight with determination tax evasion, financial crime, money laundering and terrorist financing as well as, and I am quoting, "any threat to financial stability and market integrity". This is a clear political mandate for the Commission, and it will also give us a real impetus in the fight against money laundering and terrorist financing. It is true that the European Council requested proposals from the FATF but we will come back to this later in response to the questions you have raised. As for the threats, all in all the Commission does not have a very different vision

from the Member States or the FATF; we are all in the same boat. What I would like to underline is that the Commission as such has no operational activities. In Member States you have the police and you have operational services. We have no judicial authority as such. We have the European Court of Justice but it is not the Commission. We have no judicial authority to deal with money laundering and terrorist financing. The only operational activity the Commission has is the fight against VAT carousel fraud because VAT is the source of revenue for Community budgets and we want to protect our financial interests. However, things may evolve over time because Europol and Eurojust are soon to become Community agencies and we believe that this operational activity of the Commission will increase over time when we look at it globally.

Mr Boratyński: As Philippe has said, the competence of the Commission on security matters is rather limited. We do have some tools at EU level as regards assessment of threats relating to money laundering and terrorist financing, and this is the activity carried out by Europol and the Joint Situation Centre, which are part of the Council of the European Union Secretariat-General. As far as Europol is concerned, with whom we co-operate very closely, Europol publishes every year an Organised Crime Threat Assessment where money laundering is assessed and part of that report becomes public. The part that is confidential, obviously, is shared only with the Member States. In addition, Europol issued in 2008 a situation report on terrorist financing. If I may come to the challenges, the money launderers and terrorists involved in terrorist financing are using increasingly sophisticated techniques these days, for example, the use of shell companies to avoid detection. Many gatekeepers consider that identifying the beneficial owner of the company is a challenge for them, and we will come back to this in a later question. Therefore, there may be the need to improve the existing tools and procedures in order to increase the transparency of legal entities, and here we mean companies, legal persons in general, foundations and legal arrangements such as trusts. An area which is a challenge and is also an area for possible action is enhancing the capacity of Member States related to financial investigations. This is obviously a horizontal issue which does not specifically deal exclusively with money laundering but also concerns financing organised crime in general, and in that respect the use of financial expertise as part of the investigation undertaken by law enforcement and judicial authorities is very important. Secondly, there is the question of co-operation between FIUs, law enforcement and judicial authorities inside the EU and internationally. Then it is a question of identifying new potential

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vulnerabilities and adapting measures in view of the fight against financing terrorism. More generally, the private sector needs to remain alert to the risk of being used for terrorist financing and this concerns not only financial institutions but also non-profit organisations. Quite recently in Brussels we had an interesting event, with the participation of the non-profit and private sector, on how, in the general effort of the third sector, we could increase transparency and accountability to take account of possible threats related to terrorist financing. In mentioning these specific issues related to money laundering and financial crime, there is in a way a horizontal fundamental challenge at the EU level that we all face in developing the areas of justice, freedom and security as described by the treaties and by the multi-annual programme. The whole concept is based on the idea of mutual recognition. The most recent development, an issue which is not related so much to what we are discussing today but is certainly very well known in the UK, is the European arrest warrant. What is more relevant to what we are discussing here is the European evidence warrant and we have made an impressive effort collectively in the EU to build this kind of legal edifice but at the same time in the day-to-day reality there are numerous obstacles and it comes down basically to the question of mutual trust. Therefore, addressing the question of trust among Member States, among law enforcement services, among judicial authorities, and talking about this among FIUs, is probably at the very core of the challenges we are speaking about.

Q271 Lord Hannay of Chiswick: In the course of our evidence taking we have identified a reasonably new source of illegal money laundering, which is rather large sums of money being transferred to Somali pirates as a result of the hijacking of ships and then their release and yet it does not seem to be on anybody's radar screen at the moment. We talked about it to the British Treasury representatives and to FATF and they said no, FATF had not done anything about that. We talked to your colleagues in the Council Secretariat this morning and they said no, the EU has not really looked at that. Is this something that is of concern to you? It seems to us that there is a fairly anomalous set of issues raised by this. For example, there is nothing illegal, in most Member States at any rate, about transferring large sums of money to people who are known to be criminals in order to obtain the release of ships and their crews, nor does there seem to be any process by which the money is subsequently identified with the criminals and therefore the proceeds may or may not find their way one day to terrorists but in any case it will certainly be a case of money laundering. Do you have any feel for this subject at all?

Mr Pellé: As we said, this is not an issue that has come up on our radar screen, nor at FATF. As far as the Council Secretariat is concerned, I understand that you met with Professor de Kerchove this morning. I do not know whether they are aware of this or whether Europol mentioned it. It seems to me, as you hinted, that the issue would be in the second phase, the recycling of proceeds. For the time being the issue is one of the payment of ransom to those pirates, and indeed it is something we have no position on as Commission officials, and for us at least that is not yet money laundering. If there is a question as to when these funds are recycled, and indeed could end up in hands one would not like to see them in . . . I think we can only take note of the point, discuss it internally and also probably with the UK Treasury. It may be worth having a look at it in the FATF. The FATF does conduct tactical exercises regarding new ways of money laundering, if I may put it like that. It did conduct a very substantial exercise on trade-based money laundering two years ago. It may be a point worth raising with them.

Q272 Lord Hannay of Chiswick: There is after all an ESDP mission of quite an expensive and extensive kind operating in the seas off the Horn of Africa to try to prevent the acts of piracy. It seems slightly odd, to put it mildly, that no effort is being made to squeeze another part of this cottage industry which seems to have been growing rather rapidly until the naval operation was undertaken, that is to say, the side which enables them to get their hands on large sums of money and thereafter make it disappear into thin air.

Mr Pellé: You raise a very interesting point because we are basically dealing with a non-state. Because Somalia is not a state any more. There is no possibility of having a government-to-government talk to ensure that there are appropriate anti-money laundering rules on the spot. Therefore the issue would be for our banks, let us say, in Europe to ensure that funds coming from certain individuals were properly screened. We do not have our colleagues from DG External Relations here, so I do not know at this stage whether there are sanctions against some individuals in Somalia; it is a bit speculative, but it is certainly an issue that would be worth examining.

Chairman: We have sown a seed in your minds.

Q273 Baroness Garden of Frognal: The European Commission and 15 Member States are members of FATF. Could you tell us what procedures and processes exist to co-ordinate an overall EU position in advance of FATF plenary meetings and whether these have proved satisfactory in practice?

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Mr Pellé: The factual description is relatively easy. The second question is more complicated and more difficult for us. On the factual question, only 15 Member States, not the 27, are members of the FATF, plus the Commission. The European Union is not a member, nor the European Community, which indeed is an issue. It is an issue we looked at four or five years ago and we took it into account on the basis that we did not want to overhaul the whole system. We are in a situation where we have 15 Member States in the FATF and 12 Member States in MONEYVAL, which is an FATF-style regional body set up under the aegis of the Council of Europe, so we have a *de facto* divide at international level. How do we try to remedy this asymmetry? We do it at Community level and the Commission does it by making use of the Committee for the Prevention of Money Laundering and Terrorist Financing on which all 27 Member States sit. Every time there is an FATF plenary, a week before that meeting we organise a meeting of the Committee for the Prevention of Money Laundering and Terrorist Financing with the 27 Member States. It is a matter of feedback but we discuss major issues that could be of interest to all 27 Member States, or to one Member State (it does not need to be a common issue), but there is this platform meeting a week before the FATF plenary. In addition, as I said, the 12 other Member States are members of MONEYVAL, and MONEYVAL is represented at the FATF through its chairman and its executive secretary plus three members of MONEYVAL. It does not necessarily mean that they will be three of the 12 Member States but often we will have one of them in the delegation, so there is access. We have MONEYVAL for the 12 Member States and there is reasonable access indirectly through the Commission, the CPMLTF, the committee I was referring to earlier. What do we do when there are major issues for Member States and for us? We try to get a common line for the Community that we can present to the FATF. That was the case when we had to debate Special Recommendation 9 on cash control operations at the border, where we had very divergent views with the FATF and particularly some federal states which do not belong to the EU, so there we used the committee for that purpose. It does not mean that there is a single EU voice. Member States are autonomous at the FATF so they can speak, and sometimes they do speak in a different way. Most of the time they do not but it can happen. As to whether it has proved satisfactory in practice, that is a question we should ask Member States.

Q274 Baroness Garden of Frognal: We understand there are a number of working parties as well within this process and we are just wondering if you could

explain how the views all become co-ordinated. What is the process of communication between the working parties?

Mr Pellé: You are referring to the working parties at the FATF?

Q275 Baroness Garden of Frognal: Yes.

Mr Pellé: It is a matter of resources. You see here almost all the resources of the Commission dealing with anti-money laundering and terrorist financing and most of those resources are only dedicated part-time to that issue, so it is also a matter of human resources. Therefore, when we have the committee meeting we only tackle very major points, which may be points relating to the work of those working parties you were referring to or issues that will be dealt with by the plenary itself; it all depends. On SR9 we were co-ordinating issues that were debated in the working group on terrorist financing and money laundering and then it moved to the plenary, so it really depends. It is thematic more than in relation to a particular working group. That is an issue that is being examined at the FATF where there is a clear willingness to associate more jurisdictions in the world with the work of the FATF, not only those who are members of the FATF but also the other countries, and particularly through regional bodies like MONEYVAL or the Asian-Pacific Group and others throughout the world that apply the FATF standards and do some work. If you like, the FATF is the holding company and the subsidiaries follow instructions from the parent company. There is certainly a willingness at the FATF to involve the regional bodies more in the work of the FATF, including working groups. There was even consideration as to whether or not they could co-chair some of those working groups—this may not be completely ripe at the FATF—to try to associate those regional bodies more and more. Certainly it is the view of the Commission that we do not want to have two divisions like in football, the first division being the FATF members and the second division those who do not belong to the FATF.

Q276 Lord Hannay of Chiswick: A major purpose of European legislation in the anti-money laundering and terrorist financing sphere is, of course, to give effect to these FATF recommendations once they are agreed by the FATF. Have problems arisen in, as it were, transposing the FATF recommendations into European decisions and law, and how are they being addressed?

Mr Pellé: I will give you two examples and they go in different directions. The first one is not really a problem *per se*. The FATF's motive has always been to ensure better implementation of those standards, but at the last FATF plenary, which took place in

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February, the emphasis for better global implementation was on those standards related to confiscation and legal entities and legal arrangements, trusts, for instance, and also on mutual legal assistance where there were a number of recommendations. Perhaps in the past it was very much on the finance aspect and now there is a willingness to rebalance a bit and have another look at those standards on confiscation and mutual legal assistance. They wanted to devote more attention and more time to this, but this is in line with the work that the Commission is carrying out. The Commission recently issued a Communication on confiscation of the proceeds of crime, so it is very much in line with the work that has been happening and is ongoing at Community level. That is why I would not say it is a problem. On the contrary, it is an opportunity for us to contribute to the international standard-setting process. Conversely, we have had some problems with the FATF because in some instances the standards are first of all addressed to nation states and therefore they fail to take into account the EU dimension. For our Member States belonging to the European Union we have had some friction in the interpretation of the standards and the way they should apply to the European Union. There was a case with regard to Special Recommendation 7 where the EU applies the standard in its relation with third countries and has, let us say, a simplified way of applying it within the European Union, but we considered that we had complied with the spirit of the standard. Nevertheless we had to make a demonstration of it. It was a bit of a painstaking exercise but in the end it was recognised by the FATF and language was adopted at FATF level to recognise the specificity of the European Union. The same applied in respect of Special Recommendation 9 on cash controls at the border where some of our Member States were assessed very strictly (too strictly in our opinion) because they did not have controls at what we call the intra-EU border, which is basically the border between two Member States, e.g. between Finland and Sweden. Our reading of the application of the international standard is that it should apply at the external border of the European Union and not start cutting through the economic and political integration process. We had tremendous difficulties in making this understood and accepted by federal states who are not members of the European Union. It took us two years. In the end we managed to get their support and convince the non-EU Member States of the FATF that there were more proportionate means of reaching the same objective than requesting our Member States to re-establish controls at the border as far as cash movements are concerned. That was more the problem and similar problems may still occur because the EU has some

specificity. But we accept, in so doing, that we have to demonstrate that we respect the spirit of international standards.

Q277 Lord Hannay of Chiswick: What I understand you to be saying is that you have had quite a struggle getting the non-EU FATF members to accept the specific way the EU implements the recommendations.

Mr Pellé: Yes.

Q278 Lord Hannay of Chiswick: But you have not had any trouble from the EU Member States who are not members of FATF at the necessary EU decisions to implement the recommendations?

Mr Pellé: No, because that is done through the negotiation at Community level of a directive, which was again the Third Anti-Money Laundering Directive and all 27 were part of the process—25 at the time.

Q279 Lord Hannay of Chiswick: And then the follow-up is done through a management committee procedure?

Mr Pellé: Yes. You have raised a question as to which Member States have not fully transposed the directive, and out of the new Member States only one is late.

Q280 Baroness Henig: In June 2008 the United Kingdom, Brazil and The Netherlands proposed a review of the FATF recommendations and the mutual evaluation process. To what extent, if any, do you think the global financial crisis has made the need for a review more pressing, and also could you tell us what has been the stance of the Commission in relation to this initiative?

Mr Pellé: I am smiling because I would have liked FATF members to respond to your second question as the global financial crisis has made the need for such a review more pressing. That was the view we expressed at the February FATF plenary meeting, but there were very few who shared it. I will come back to this and explain why. We had no support to speed up the process. Basically, the three countries mentioned were the past, current and future presidencies of the FATF and they worked together to prepare what was called a three-presidencies paper which was discussed in June last year. The thing is that the objective was to review the FATF standards and also in the perspective of the fourth round of mutual evaluation. However, Member States of the FATF were not ready to support that project because they thought it was too ambitious at a time when a number of them were still being assessed. Some of them were afraid that they would be assessed on the more demanding criteria. They were not opposed to

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the idea but it was more a matter of timing, so the FATF basically decided that this work should be delegated to one of its working groups, the working group on evaluation and implementation, that would examine a series of issues that might or might not warrant a review of the standards. This process was launched at the last February FATF meeting, so now Member States of the FATF are invited to comment on the paper from the FATF. In relation to the crisis, I would like to say that at the last FATF meeting this group agreed to examine a number of issues, particularly, for instance, the issue of bank secrecy laws, and also to consider the merits and difficulties of considering tax crimes (people meant tax evasion) as a predicate offence to money laundering. These certainly reflect the language of the expectations of the G20. In this respect the global financial crisis is already influencing the thought processes of the FATF and the Commission is contributing to this. We are contributing to the G20 and we are contributing to the FATF process. The Netherlands will have the next Presidency of the FATF. They take over in July the Presidency of the FATF. They tabled a paper in February for an interim report in June and a final report in October. The objective is to analyse the impact of the financial crisis on AML issues in general, of course, the mandate of the FATF, and to have a particular look at non-transparent and non-co-operative jurisdictions. That is where we are. As I said, we, the Commission, would have liked the process to be quicker but many FATF members were waiting for the outcome of the G20 meeting in April.

Q281 Baroness Henig: Can you give any idea of the balance? You said that only a few countries shared your view.

Mr Pellé: Two.

Q282 Baroness Henig: Two?

Mr Pellé: Three.

Q283 Baroness Henig: Three?

Mr Pellé: Counting the Commission.

Q284 Baroness Henig: I see, so it really is quite a problem.

Mr Pellé: Yes. To be clear, people considered that money laundering was not one of the root causes of the crisis so we should take our time examining the issues.

Q285 Chairman: Looking at page 9 of the memorandum you kindly sent us, you were talking about Member States not ratifying various matters, and in that particular section you pointed out to us that seven Member States had still not fully transposed the Third Anti-Money Laundering

Directive. I wonder if you would bring us up to date on that, and what steps have been taken to encourage or require timely implementation by the Member States concerned? Perhaps I can add to that. We heard this morning from the Council. We got the sense of a very significant amount of exasperation because of some Member States not ratifying decisions by the Council. This seems most concerning and it does seem to leave the European Union rather toothless. You say in this paragraph that procedures “have long lead times and often lack teeth”. Could you talk us through this situation as well as the specific matter of the seven Member States and the Third Anti-Money Laundering Directive? This does seem to me a major weakness in the whole of this field.

Mr Pellé: The conversation you had this morning relates, I suppose, to Council decisions. They belong to the Third Pillar and, if I may use that word, a deficiency in the Third Pillar is that the European Court of Justice has no power. There is no enforcement power. It is based on the law of suasion and the ability of, let us say, European institutions and also Member States who adhere to the Council decisions to persuade the others that it would be good for them and for the European Union to implement those Council decisions. That is one point. As far as Community legislation, the First Pillar, is concerned, indeed there is the European Court of Justice, but, as we said in our written evidence, the procedures are very long and this is a reality. Regarding transposition, we are as exasperated as the people you may have met this morning in this respect. Member States may tend to play with the rules and it is not particular to this field. It is indeed hard for citizens to understand, when Member States agree on a piece of legislation at Community level and also on a date for the implementation of a piece of legislation at national level, that when the date arrives one way or another they avoid the rule when they have had 18 or 24 months, the usual period that is granted for Members, to implement it.

Q286 Chairman: Or nine years, as we heard this morning.

Mr Pellé: That is an issue we have been addressing and we have not yet been successful. We have this example of the Third Anti-Money Laundering Directive. We work upstream with Member States, for instance, by organising what we call transposition meetings that take place between the time of the adoption of a directive and before the date for implementation at national level. On this particular directive we had two transposition meetings, but on more complex issues we may have many more. On the Services Directive a very complex mechanism has been put in place to ensure that Member States

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implement it and implement it properly. In this case it is even more surprising because Member States do agree on the international standards and 15 of them are members of the FATF so you would assume that once those standards were translated into Community legislation it would be fairly easy to translate them into national legislation. As a matter of fact, the situation has improved since we gave you our written evidence where we indicated that seven Member States were late. Two of them have now adopted the required legislation. Some are late for various domestic reasons. It is still unacceptable; I do not want to apologise for them. They agreed to a deadline and they should have implemented it, but one of them wanted to improve its AML system in line with the results of the mutual evaluation they had at the FATF, so they wanted to align. Another one had difficulty with having a stable government that would then be in a position to validate the national law and push it to parliament. There are different circumstances. Nevertheless, whatever the circumstances, what the Commission has been doing besides the transposition meeting is to use this Committee for the Prevention of Money Laundering and Terrorist Financing to remind Member States of their obligations. Senior officials of the Commission attended the meeting to pass that message to Member States. What our Commissioner did was to send letters to ministers of finance of the laggard Member States. In June last year, he sent 15 letters underlining the importance of the implementation of the Anti-Money Laundering Directive. As for the seven Member States we referred to, obviously, those that have transposed will be off the hook but they were all referred to the European Court of Justice. Still, when the procedure is launched before the European Court of Justice, once the Court has adopted its opinion, Member States still might not comply or decide to take more time, for whatever reason. It is only when there is a second procedure that pressure comes to bear because there are pecuniary sanctions. That is why we cannot really rely on the sanctioning tool, the stick, but more on the carrot to invite Member States to do what is needed and work upstream. Currently our Directorate General is working on what is called enforcement partnerships. I am not in a position to describe this very fully because it is in the process of being discussed with our Commissioner to see how we can further improve implementation of the legislation. But it is a very sore point for the Commission to admit that the situation is not as optimal as it should be.

Q287 Chairman: You say though that discussion is going on on how to improve things. Just give us a rough timetable for when they may see the light of day.

Mr Pellé: Within the year. As I said, it is based on the willingness of Member States. We need to show the advantage for all of us in building the European Union—in complying with some rules, basically, rules we have agreed.

Chairman: As I said this morning, milk quotas are written upon my heart. We had great problems with those 25 years ago.

Q288 Baroness Garden of Frognal: Following on from that, what are the implications for EU and international co-operation which flow from this delay in transposition and could you also say if the Member States in question are to be treated as “equivalent” for the purposes of the Third Directive in advance of its transposition into international law?

Mr Pellé: This is always an embarrassing question for the Commission.

Q289 Chairman: That is why we are here.

Mr Pellé: The fact is that there are clear time lines in the implementation of the directive and that should definitely be a source of concern. It is a source of concern for the Commission but we would like it to be a source of concern also for Member States, particularly when they want Community legislation because the desire is to achieve a level playing field among those who have to abide by the rules agreed at European level. Therefore, that is your first motivation, to adopt Community legislation when you could go national. You could dwell on Community competences versus domestic ones but that was clearly the message we got from Member States when we were talking about the Anti-Money Laundering Directive: “We want to achieve a level playing field”, yet here we are with a third of them not on time and the banking industry complaining that that imposes on them a higher cost of compliance because there are some differences between the national systems. To be fair, there will still be differences because the directive is a minimum requirement directive, so Member States can have stricter rules. Still philosophically there is a problem here. We have to impress on Member States the need to correct this as quickly as possible.

Q290 Baroness Garden of Frognal: Are there practical examples you can give of how this lack of co-operation has had a negative impact?

Mr Pellé: Funnily enough, it is a bit theoretical. For us it is a very embarrassing situation, but for the time being it is a bit theoretical, although our partners outside the EU are using those arguments to say that the EU is not as homogeneous as it pretends—“Look at the transposition of some texts, so how can you defend a global harmonious EU approach when you have those differences?”. That is an argument that

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belongs more to the realm of argumentation than constituting practical difficulties. We have not met difficulties but this point was underlined at the last FATF meeting, particularly regarding the issue of equivalence. Italy in its report explained very well at the FATF how that should be read. Basically, what we mean by the notion of equivalence in the Third Anti-Money Laundering Directive is that there is a presumption that all Member States will be compliant with the requirements of the directive once it has been fully transposed by all of them into international law. This is a peculiar area because Member States are not starting from scratch. We have already had two directives but the third will present a substantial improvement in the AML/CFT defensive system. Nevertheless, we want all Member States to comply with the directive on time because of the perception issue by partners of the European Union.

Q291 Lord Hannay of Chiswick: Could I follow that up? Are you saying that the fact that not all Member States have transposed the Third Anti-Money Laundering Directive means that the playing field looks uneven but is actually not uneven, and, secondly, is there therefore no material disadvantage to a state in delaying implementation at all over a state that has implemented and transposed quickly?
Mr Pellé: No. That would be denying the value of having a directive, basically. There are a few Member States whose national legislation is relatively solid and whose banks are already complying with the requirements set out in the Third Anti-Money Laundering Directive. That does not mean that this is a general case for all Member States lagging behind the deadline. On top of this, those who are lagging behind the deadline are depriving the banks of the facility of applying the risk-based approach, for instance, so they are in fact applying more rigid rules compared to the ones they could have access to through the application of the Third Anti-Money Laundering Directive. It is all a bit complicated because we are now going from legislation to practical application. In some instances that is an issue and there is an uneven playing field for some parts of industry besides the financial industry. It may be an issue for the non-financial actors, the gatekeepers. It certainly should not be taken as an excuse by Member States not to abide by the deadline.

Q292 Lord Hannay of Chiswick: In its memorandum of 30 January 2009 on page 13 the Commission noted that in the spring of 2008 Member States agreed on a Common Understanding of third country equivalence for the purposes of the directive. Can you say how, if at all, this process differs from what is laid

down in the text of the directive and what powers, if any, the Commission possesses in regulating any such matters?

Mr Pellé: That is relatively clear. The Common Understanding that was shared by Member States on third country equivalence is a voluntary one. It is not based on legal powers that would be granted to the Commission through the directive. The directive does not foresee that. The powers of the Commission in respect of third countries under the directive in relation to Article 40, paragraph 4, are that if the Commission finds that a third country does not have an anti-money laundering regime equivalent to that set by the directive it could propose to adopt the application of a decision-making source, we would say blacklisting, or it could veto a third country which Member States might at national level consider as having an equivalent regime.

Q293 Lord Hannay of Chiswick: And this has never been used?

Mr Pellé: It has not been used for the time being.

Q294 Lord Hannay of Chiswick: And you do not see any cases on the horizon where it might need to be used?

Mr Pellé: This is an issue to do with our stipulation of the risk-based approach, basically. In this respect the directive is of a hybrid nature, as characterised by the FATF. In some instances, we take on board the risk-based approach and we keep some flexibility, but in other instances we define specific requirements, for the application, for instance, of simplified due diligence or, conversely, strengthening customer due diligence. Taking such a decision of blacklisting a third country would be of the same nature as defining enhanced customer due diligence for any customer coming from that jurisdiction. For the time being there has been no debate at the committee, nor any request from Member States to proceed like this.

Q295 Lord Hannay of Chiswick: So you are saying it is a kind of nuclear option?

Mr Pellé: It is a bit. On the other hand, the FATF uses advisories in respect of some third countries. It is no secret that recently a series of advisories have been taken by the FATF regarding Iran or Uzbekistan and a few other territories. For the time being what has been agreed by Member States and what Member States apply is the positive list, which is fairly reduced and we will see how it works.

Q296 Lord Hannay of Chiswick: So it would be very unlikely in your view that the EU would even contemplate blacklisting a third country which FATF was not contemplating blacklisting?

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Mr Pellé: That I cannot say. At this stage I do not know. This power that is enshrined in the directive is an autonomous one. If Member States wanted to blacklist a country we would start the process, so if one Member State or a group of Member States were to come to the committee and say, "Here is an issue we have. What are the views of the committee's twenty-six other Member States?", and we considered that it might be worth applying the powers granted under Article 40(4), we would consider the issue.

Q297 Baroness Henig: The Commission memorandum on page 11 notes that discussions have taken place with national FIUs and the Member States on the December 2007 report from the Commission on the implementation of Council Decision 2000/642/JHA on FIU co-operation. I am sure this is all very familiar to you, much more familiar than it is to me. What are the prospects that the Council Decision will be updated? What are the most significant changes under consideration, and is there a time frame within which the current process of "reflection" will be brought to a conclusion?

Mr Boratyński: Thank you very much for this question and for noting the report on the implementation of the Council Decision from December 2007. Let me first make a general remark. The report is generally positive as far as legal compliance is concerned but it then points to a number of operational problems. Again, it is not a unique situation that a Framework Decision, therefore a Third Pillar instrument which is relatively modest in its ambitions, reflects a readiness by Member States to go only as far as a given moment, which results in instruments that are fairly general and again not as prescriptive as a First Pillar instrument. However, I think there is generally a good atmosphere and understanding that a follow-up is needed to the decision which by now is over eight years old. There was a discussion on the basis of the report in a Multidisciplinary Group on organised crime which is the main Council Working Group that deals with organised crime, where Member States were asked to provide comments first of all, and it seems the majority of Member States were willing to have time lines which would serve a better exchange of information; therefore they would complement the fairly general provisions of the current decision. Also, there is a readiness to examine the possibility of exploring the possible added value of such amended decisions in the future. What stems from that is that at the moment we can talk about 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 from 2000, and in the longer term

recasting the Council Decision. At this stage it is very difficult to be specific, but generally speaking the recasting could address the current shortcomings, for example, the inclusion of the fight against terrorist financing, and what I have already said, the lack of sufficiently detailed provisions which often result in a lack of legal clarity for Member States and also an uneven implementation. In any event, the updating would have to take into account the consequences of the initiative which was about simplifying the exchange of information and intelligence between law enforcement entities of Member States. To sum up, if you are interested we could try to go into more detail, but roughly speaking we would like to have discussions and preparations on possible guidelines with the view of having them adopted in the year 2010, and again develop reflection on whether, in addition to the guidelines, recasting is possible. Discussion about timing at this stage is difficult but it is on the agenda without specific timing.

Q298 Baroness Henig: Your short term sounds to me like a year to 18 months.

Mr Boratyński: Yes.

Q299 Baroness Henig: And your longer term sounds to be anything from 18 months.

Mr Boratyński: Yes, depending basically on the readiness of the Member States. Just to give one example, the current decision stipulates that requested FIUs shall provide all relevant information, including available financial information requested, law enforcement data. This information is based on the material that was gathered as a result of preparation of the report of December 2007. It is quite clear that there is a high degree of diversity in terms of FIUs having access to specific type of information and various databases, FIUs also may be able to communicate openly with one type of authority but not with another. Indeed this diversity across the EU does not serve our purpose.

Q300 Baroness Henig: So in the next year or two basically what you are saying is that it is guidance that you are going to be focusing on and that that will then lay the foundations?

Mr Boratyński: Yes, but again that may not be sufficient, for obvious reasons, because we are talking about law enforcement and the context in which there is a limit to what can be achieved through soft law measures or guidelines in particular, again, depending on specific national traditions. There are some countries which have effective law enforcement without very explicit provisions while others may need specific hard core law when regulating these issues.

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Q301 Chairman: Could I now turn to the FIU.NET system of information exchange? In what manner and to what extent does that system reinforce operational co-operation within the EU and could you tell us what further developments in the view of the Commission are required if it is to achieve its full potential?

Mr Boratyński: There is a long story to FIU.NET because it came in to implement directly one of the specific provisions of the Council Decision of 2000. Currently, as you know, this is a project. It is not any specific agency, it is just a project hosted by the Dutch Ministry of Justice and receives considerable financial support from the Commission under the funding programme Prevention and Fight against Crime. Again, there is progress in terms of subsequent Member States joining the system. In 2009 we expect that 22 Member States will be connected. As of the end of 2008 there were 18. There is going to be a new release of the software for FIU.NET as the core element of the system is a secure platform for communication, so the new version will be fully operational this year. In comparison with previous versions and other existing systems it will allow not just the exchange of information by email but also the sharing of information at the same time with all FIUs connected to the system. There are a number of technical details which I do not want to bore you with but there is indeed an expectation that the practical possibilities for operational co-operation in FIUs will be extended and therefore FIU.NET as such will become more attractive as a platform of choice for FIUs exchanging information. Under a new funding application that is being developed we expect to focus increasingly on co-operation between FIU.NET and third countries and this is very much related to the goal of ensuring compatibility with the Egmont Secure Web system which is international, unlike FIU.NET which is linked to the EU. For us it is obviously a priority project. It is getting a grant so we are going to spend money on this. There is an ongoing discussion among the Member States represented on the FIU board on the future for FIU.NET in terms of FIU.NET as an entity. We expect some decisions to be taken by the end of 2009. As for the Commission, we are neutral on the end result because there is a discussion on which option should be followed and as long as it is effective we will be happy with whatever entity is eventually the FIU approach.

Q302 Baroness Garden of Frognal: You touched on this in your opening remarks, but to what extent have discussions taken place in the EU FIU Platform on enhancing feedback to the private sector, and what improvements, if any, have resulted from the discussions to date? Could you also say what the

scope is of the ongoing Commission study of this subject and when that is due to be completed?

Mr Pellé: Just to remind ourselves of a few facts, the Platform was set up not long ago in 2006 in connection with the FIU.NET project because we thought that with the FIU.NET project being an IT system there was a need for a platform where FIUs could exchange views and discuss how to improve that co-operation. So now we have this platform which covers most FIUs from the Member States and, as I said, the objective is to facilitate co-operation among them. They participate on a voluntary basis. Until recently not all of them attended. However, at the last FIU platform meeting on 10 March, all of them were present. They discussed—because we are only the Secretariat, although we chair the meeting (failing the FIU volunteering for that)—feedback in 2007 and 2008 and they adopted a report on feedback on money laundering and terrorist financing. This report is accessible on the website of the Commission and there you can see what it was about. What is striking for me is that the report is about good practice, not best practice, because FIUs were very hesitant in moving that step further from good to best in starting to benchmark their respective practices. Therefore, we have these discussions on the FIU Platform and their subsequent report. Whether this has led to an improvement in the way they function is hard to say. What we noticed at the time, and I think it is still the case today, was that many FIUs were reluctant to provide case specific feedback to the private sector, targeted feedback, as we call it, because what they are afraid of is that it could undermine pending investigations or, even worse, judicial procedures. On the other hand, we know there is tension here because the private sector, notably banks, would like to get this case specific information in order to improve or validate their own systems. If you have an intelligent system you want feedback so that you can improve it, so we understand that. This tension is very difficult to manage and I think that was recognised in the report, but for the time being the private sector has to make do with the general annual reports from the FIUs on their activities.

Mr Boratyński: Building on what Philippe has said, there are some good practices. We are not sure whether they are best practice but there are some good practices, so to move forward on this the Commission again asked for a very detailed study which would analyse the question of feedback, and we are talking here about the channels of FIUs and reporting entities and law enforcement. The purpose of the study was to assess feedback structures and practices in all Member States and there has been a major effort in getting a lot of evidence and interviews; it was quite a big exercise, and then trying

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to identify what could be the best practices and at the same time what were the shortcomings and obstacles, and, finally, what type of recommendations, both legislative and non-legislative, could be proposed to improve the feedback. The report is now in the process of being finalised and there will be a meeting involving FIUs, then reporting entities, which is, as you know, a very wide pool of financial institutions, banks, et cetera. This meeting is going to take place at the end of April and following that, probably before summer, we should be able to make this report publicly available. As you will have noticed in the written evidence, we made a short reference to the outcome, saying prudently, obviously, that while the study has not been finalised there are indications that feedback is not provided to the private sector in a timely manner. The structural case-by-case feedback, in other words specific feedback, is provided only in a limited number of instances. The study goes to some lengths to define the types of feedback, distinguishing between general feedback, which is easier to get, which is about methodology, and specific feedback, which is basically on cases reported by reporting entities to FIUs and further on to law enforcement. What is very interesting in the study is that it examines not only the practices but also the perceptions and expectations. For example, it identifies the clear need of the private sector to be more involved, to be more trained. There were some examples which I was quite pessimistic about. Some interlocutors were, for example, saying that in some Member States, and one cannot really generalise, this commitment of government structures to develop the training programmes is diminishing, so it is not necessarily that we are always progressing. However, I think the study will provide a very balanced and detailed view of where we are and we are looking forward to it being a good basis for further action.

Chairman: Lord Hodgson, who is a member of this Committee, would have had a great deal to say about the impact of all of this on the private sector. Sadly, he is not here with us today, but the Committee is concerned about this and Lord Hannay would like to pursue this a little further.

Q303 Lord Hannay of Chiswick: I wonder if you could tell us a little bit about the extent and frequency of what you call “trustful dialogue” between the Commission and the banking industry and the legal profession on page 12 of your memorandum. We were slightly surprised that you did not mention the accountancy profession because when we took evidence—we took evidence from the three trade associations—the bankers, the lawyers and the accountants, and the accountants, certainly in Britain, seemed to be very prominent in the work against money laundering and very involved, so

perhaps you could say a little bit about that and whether there are any plans to deepen or otherwise improve the dialogue with the private sector. Could you also cover the point which the Chairman has just mentioned? In the context in which you had the “trustful dialogue”, have any of these entities—the bankers or the lawyers, made representations to you that the burdens imposed on them by this legislation are disproportionate to the benefits which the European Union is getting from these systems? I am sure none of them said that they were in favour of terrorism or anything like that, but have any of them suggested that there could be better ways of doing this than the way the European Union, and indeed the FATF, have identified so far, that a slightly smaller sledgehammer could still crack a nut?

Mr Pellé: It is a fair point. I will go to the question in a minute, but, just to bounce back on your latest comments, none of the directives on anti-money laundering was accompanied by an impact assessment, the first and second because at the time it was not a requirement when issuing Community legislation. This came up with the concept of better regulation at Community level some two or three years ago and now, any time we come forward with a piece of legislation, and sometimes even with what we call soft law recommendations, it is a usual practice to accompany it with an impact assessment. It was not the case at the time of the adoption of the third directive. Therefore, we have not assessed, if you like, the proportionality and the requirements of the instrument in the light of the results. It is true that the legal profession, certainly the lawyers, any time we meet them are making that representation, that there is a certain disproportion in the instrument. That may have been particularly the case also in the UK, where not long ago the lawyers were one of the major providers, alongside the financial industry, of suspicious transaction reports because the penalties in the UK are extremely severe against any person who fails to lodge an STR. It is something like five years’ imprisonment or a very significant sanction, so you have what you could call defensive filing of suspicious transaction reports just to protect yourself. That is a general remark. What we are not trying to push at the FATF and certainly the Commission, the UK and also The Netherlands, is for the FATF to come up with some sort of impact assessment also when coming forward with new recommendations. Hopefully that should also apply to major guidelines that the FATF might issue. I do not think we are yet at that stage and at the last meeting there was an agreement on having short written statements, a cost/benefit analysis, if you like, on any future measures that may be proposed by the FATF. It is an element of your concern that could be taken into account for that exercise. To go back more

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specifically to your question and the trustful dialogue we are having with the banking industry and legal professions and not with the accounting profession, it is because I think there was, and is, an appetite from the financial industry and legal professions to speak to us on those issues, which is perhaps not shared so much by the accountancy professions at the European level. We have had contacts with the European organisation that represents auditors and chartered accountants. They know they have obligations and I understand they have even organised one or two seminars on those issues, but I think for them it is a requirement, they comply with it, they apply it and they do not complain very much about it. The legal professions do apply it to some extent. We produced a report some time ago which is available on our website on the impact of the Second Anti-Money Laundering Directive on the legal professions, lawyers and notaries in particular. They comply and complain, perhaps rightly so, certainly any time we have a debate, but we have a trustful debate also with them. We have regular contacts with the CCBE, which is the European Association of Bars and Law Societies, and also with the Law Society of England and Wales. I took part with some colleagues in a joint meeting with them last June. We understand that we have diverging views but we understand that and it does not prevent a dialogue. The dialogue is more intense probably with the banking industry because there is a large representation of banking organisations at European level and there is also a real pool of expertise located here in Brussels. We tend to meet twice a year, in spring and autumn usually, to do a *tour d'horizon* for issues related to AML/CFT. I believe the last meeting was in December when our colleagues from DG JLS were present and also colleagues from DG External Relations dealing with sanctions. Besides those two meetings we have had focussed meetings on specific issues with the banking industry. There was one organised not long ago on sanctions regarding Iran and there was a previous one regarding Burma. We want to encourage this because if ever we were to come up with a fourth directive, which I hope will not be immediately, we would have to accompany it with an impact assessment, so we also want the feedback and opinion from those who have to apply the requirements. It is the best way to have a tool that works. I would also like to add to something Jakub has already mentioned, that we also have this dialogue with the not-for-profit associations. We have had two conferences with them regarding the risk of abuse of their organisations. As we said, the objective is to increase awareness of the sector and to ensure that we are aware of the risk and that we can take measures to establish the necessary transparency. There are codes of conduct at national

level and we also have in the Communication a code of conduct and guidelines at Community level.

Mr Tiné: We are trying to work around the concept of guidelines with them at the moment.

Mr Pellé: Beyond what we can do at European level, it may be presumptuous to say this but we also try to push through the FATF the need for this dialogue. The UK Presidency of FATF did it even better than we did. Sir James Sassoon, when the UK had the Presidency of the FATF in 2007/2008, changed the attitude at the FATF by promoting the partnership with the private sector. Taking the UK model as an example, we have this joint partnership at the FATF, like, the UK Joint Steering Group on Money Laundering, with the public authorities and the private sector working together on devising practical guidelines on how to comply with anti-money laundering and counter-terrorism financing requirements. The FATF has produced a series of guidelines by profession on the risk-based approach for and with the financial services industry, lawyers, accountants, real estate agents, casinos and so on. This is a change and it is certainly a welcome one. As far as your comments are concerned, we are always open to dialogue in the Commission.

Q304 Lord Hannay of Chiswick: Thank you very much. Our brief experience on this rather mirrors your own, that is to say, of the three professions who gave evidence to us the bankers and the accountants were the most positive about the dialogue and the feedback and the lawyers the least, so it mirrors exactly your own experience, although in our case certainly it seems that in Britain the accountants welcome very much the chance to be consulted and want to be consulted both at the national and the EU level. It seems to me that you are now in a system whereby any new legislation would have to have an impact assessment. But is not what is needed an impact assessment of the system overall, all three directives as they impact now, since, as you say, none of the previous three had an impact assessment done? It is not really going to be sufficient just to have an impact assessment for some new bit of legislation. You need surely to be able to gauge whether the whole system is proportionate and achieving results and so on, and that would be, of course, hugely valuable.

Mr Pellé: Yes, it is work that is being contemplated. This year we will have a study on the application of the Third Directive which replaces the previous two and we are contemplating as the next exercise what we call an ex-post evaluation, which is also nowadays a requirement for legislation after some time to review whether the objectives pursued and as defined by the impact assessment were achieved. We are

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moving towards an ex-post evaluation probably in 2010/2011.

Q305 Baroness Henig: In its Communication of November 2008 on the *Proceeds of Organised Crime* the Commission concludes that the overall number of confiscation cases in the EU is relatively limited and the amounts recovered from organised crime are modest. I wonder whether you could elaborate on the data or other indications of practice which have brought you to that conclusion.

Mr Boratyński: As mentioned in the written evidence, there is again a standard under preparation on the practice of assets confiscation and recovery in Member States and to call into question (and again this is our horizontal weakness) the lack of data and comparable data amongst Member States in a variety of areas of criminal law and law enforcement. Having said that, there are a couple of case studies in the report that have been analysed, and we were able to come up with a few examples. This is the data for 2007 and the figures in the report are €140 million for the UK, €60 million for France, €83 million for Spain, €145 million for Italy. These are, as I said, just examples. This partial and imperfect data still gives us an extremely important message, which is basically the disparity between the quantity of assets seized and the estimates of the scale of the problem. We used as some degree of reference a study by Confesercenti published in Italy in November 2008 which estimated the revenues of Italian organised crime in all its forms at over €130 billion per year. According to the same study, official law enforcement statistics indicate, and again this is a conservative estimate, that in the 15 years from 1992 to 2007 we can talk about €900 million of confiscated assets.

Q306 Chairman: Can we go back and make sure we have got these figures right?

Mr Boratyński: Absolutely; I am sorry. €130 billion is the report estimate of yearly revenue as far as the revenues of organised crime groups in Italy are concerned, while the estimate, based on a different quality of statistics from law enforcement about the quantity of confiscated assets for the 15-year period between 1992 and 2007, is €900 million. This is basically what we can say about the scale of the problem.

Q307 Chairman: In that same Communication, paragraph 3 on page 6, you express the wish to explore various concepts and rules with a view to improving the situation, including measures relating to civil confiscation. Could you tell us what are the prospects for making timely progress with these discussions, and which of the options in your view holds out the greatest prospects for success?

Mr Boratyński: As you have noted, this most recent Communication makes quite a strong case for new legislative action at the EU level and paragraph 3 sets out a number of elements that could be considered. Our intention is indeed, based on that report, to develop the discussion with Member States on this subject. What is very helpful from our point of view is that an informal EU Asset Recovery Offices Platform has been put into operation. Again, to give some examples, reversal of the burden of proof from a law enforcement point of view could be a very effective action, and indeed we see this applied in some Member States, or at least it is in legislation in some Member States, not necessarily applied. Obviously, there is a very important consideration regarding the protection of fundamental rights and the core principles of criminal law, but it is certainly a promising area to explore further. Another one is civil recovery of the proceeds of crime. This does exist in some national legislation but it is very limited. We are just talking about several Member States. We have mentioned that it is being specifically used in the UK, in Ireland and in Bulgaria, and, as I said, while it does exist, that form of the reversal of the burden of proof, in 17 Member States, in many of them it is rarely or never used in practice, again, for the reason that it is very much against the traditional principles of the criminal law—the presumption of innocence, et cetera. As I said, we want to use that here in order to take the discussion forward. The next occasion will be the next meeting of the EU Asset Recovery Offices Platform in Brussels and this will be in May. If there is a favourable mood we will be considering this in the next two years in order to come up with proposals, but we have to reflect on the readiness of Member States to move on. The Commission has expressed its quite strong preference for the adoption of this Communication.

Mr Tiné: Perhaps I could complement this by reminding you where we are coming from. We are coming from an assessment coming from the analysis of the implementation of different legal acts in the Third Pillar, so framework decisions, which shows how the existing instruments, both on substantive law and on acts aimed at facilitating the mutual recognition of judgments, are implemented in a relatively flawed way, either not transposed or simply not applied in practice, so our immediate objective is to decide whether we need at all a recasting of the new legislation, taking into account that there is legislation which is somewhat contradictory, unclear perhaps at European level, which means it could be better specified in order to allow also the national legislature to implement better rules at national level. This is our starting point. In the Communication we say that this recasting may give us an opportunity to go further and enhance the perspective and the

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possibilities for confiscation, and in this sense we are exploring a number of options, which include the one on civil confiscation, on reversal of burden of proof, but, of course, our immediate objective is to put the question to the Member States, “What are we doing? Are we still pursuing the right objective by having a legal framework which is not fully operational?”.

Q308 Chairman: Can I just try to clarify that? When you talk about the reversal of the burden of proof does that mean you reverse what the man in the street would understand as the concept of somebody being innocent till proved guilty? I see nods. If that is what you mean could you just go further and tell us to what extent there is support among Member States for a reversal of that sort?

Mr Boratyński: This is really related to the confiscation of assets, so we are talking about a situation which is understandable to the man in the street. If someone does not have a legitimate revenue which can be documented and at the same time that person has three yachts and five villas and whatever else, then the reversal of the burden of proof would foresee that it is on the person to prove the sources of revenue.

Q309 Lord Hannay of Chiswick: But you would still have to have a crime committed.

Mr Boratyński: Yes.

Q310 Lord Hannay of Chiswick: It is not sufficient to prove why they have got four yachts. There would have to be at the bottom of it a crime, and on the crime you would not be reversing the burden of proof.

Mr Tiné: Yes, indeed, Lord Hannay, you have made a very pertinent comment. All these facts would be analysed within the context of criminal investigations where the person not only has an income or assets which are disproportionate to his or her declared revenues but also has strong links with known exponents of organised crime, so in the national legislation that we have analysed so far which has these instruments this concept is applied in a relatively targeted and focused way, and normally, as we know, is also the subject of high court decisions which have found that fundamental rights, such as the right to defence and the right to property, were not violated. Indeed, there should be a link with serious crime, such as drug trafficking or other crime, which would justify the application of this measure. Another point that was raised before in the discussion is that many Member States already have some form of reversal of burden of proof according to the study. I believe we have given the figures already that about half of the Member States have it in their rule books but do not apply it often. It is

more, as we were speaking before, about the nuclear option.

Lord Hannay of Chiswick: I am an amateur in these matters but I would suggest to you that using the words “reversal of the burden of proof” is extremely dangerous.

Chairman: So would I.

Lord Hannay of Chiswick: You have described a concept that is much more complex than a simple reversal of the burden of proof.

Chairman: That is right.

Q311 Lord Hannay of Chiswick: It is putting up a big red flag if you start using those words.

Mr Boratyński: The meeting in May would be an excellent opportunity to map out the preferences and sensitivities. The point is definitely well taken; we must be extremely prudent, because at the end of the day we are talking about the fundamental principles of the legal system.

Chairman: You will observe that Lord Hannay and I both immediately thought, “Good gracious; what are they up to now?”, when you started talking about reversing the burden of proof. Let us move on.

Q312 Baroness Garden of Frognal: Could you tell us what evidence and experience you have of Hawala and other alternative remittance systems and how you think they may or may not pose particular problems in relation to money laundering and financing terrorism?

Mr Pellé: I have little personal experience of Hawala. What I know is based on what I have read in the press and also the concerns expressed by Member States and FATF that have knowledge about that. The problem is that Hawala is a system used in the Islamic world to provide the same services as a bank. The difference is that there is little or no documentation. The cost of it is usually less and it ensures faster delivery. Money does not necessarily move and it provides anonymity and security for the customer. All those characteristics, especially the last one, create issues in respect of the anti-money laundering rules and the customer due diligence obligations. What we have in our legislation, as we indicated in our written evidence, is that Hawala, or any alternative systems that operate in the territory of the EU, should be registered or licensed according to complex requirements defined in the Payment Services Directive, and if that were not to be the case they would be infringing the law. Then we come to the next issue, which is, who is taking care of this? In our view this is an issue that has to be looked at with particular attention by both supervisors and law enforcement authorities because that is the situation. I cannot say more in this respect. What I can add is that the European Union, certainly the Council, is

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having a regular dialogue with some third countries where Hawala represents a classical or usual form of money transfer. The objective of dialogue is to impress on the authorities of those states the importance of exercising appropriate control over the legality of those Hawalas and those activities in their territory and for it to be fully transparent. This action is not Hawala oriented; it is more a bilateral relation with the region rather than the Union pursuing that policy all across the world regarding Hawalas. It is an opportunistic dialogue, if you like, with the region and on top of this we discuss the Hawala issue.

Q313 Lord Hannay of Chiswick: I am sure you have a regular dialogue with the British authorities but the answer which they gave to this was that the Hawalas in Britain are now all regulated and are filing reports, including SARs, as necessary, and that they therefore believe that they have some handle on this, but whether that is true of all Member States I do not know. I was not quite sure whether you said that it was obligatory on all Member States.

Mr Pellé: It is.

Q314 Lord Hannay of Chiswick: Their answer was that the system does not pose insuperable problems so long as they are all regulated and they submit accounts, which the accountants say is now the case. Then the situation can be managed perfectly well. It is after all in many cases a very beneficial system and helps an enormous amount of remittances to go back to very poor countries, but equally it is open to abuse, like every system.

Mr Pellé: Like every system, as you say.

Q315 Lord Hannay of Chiswick: It probably has some special characteristics which need to be taken into account.

Mr Pellé: It is perhaps because we are not familiar enough with the system that we have some prejudiced view about it but also because of some of those characteristics, it may be more prone to abuse than other systems.

Q316 Chairman: But even if you were able, as you say you are, to have legislation to register and control it within the EU, there is nothing you can do to control the movement of funds round the periphery of the EU to places which could be a base for serious terrorist attacks or drug funding and so on. There is really nothing you can do about that.

Mr Pellé: That is a classic problem of global governance. It is an issue for the FATF and members of the FATF and its regional affiliates to impress on their members the need to ensure that those sorts of systems are properly regulated, but we come back to the issue of the non-states.

Q317 Lord Hannay of Chiswick: But the FATF have not so far grasped this issue at all?

Mr Pellé: No, they have, because there is Special Recommendation 6 based on alternative remittance systems that addresses the issue, and basically we mirror that recommendation in our legislation at Community level.

Q318 Lord Hannay of Chiswick: At several points in your memorandum you noted the absence or unavailability of certain types of statistical data which you said would have been appropriate and useful. I wonder what steps, if any, are being made to address this, considering that there are a number of obligations set out in Article 33 of the Third Directive. What are the implications of the absence of this statistical material for any future policy making at EU level?

Mr Pellé: Here again I think I will start and then Jakub or his colleagues can come in perhaps to shed light on what we may have written and supplement what we have said. It is not the lack of data; there are a number of data existing. The requirement of the directive for Member States is to provide statistics, for instance, the number of suspicious transaction reports, the follow-up given to these, the number of cases investigated, the numbers of persons prosecuted and convicted. This information is available. It is available, for instance, in the FIU annual report. It is available through the mutual evaluations of our Member States for sure. They have evaluations conducted by the FATF or by MONEYVAL. In this respect Member States can already comply with the requirements of the directive because they have information. We are trying to consolidate in Community law a practice that already exists because we thought it would be useful, so it is not so much the issue of the availability of the data as of the comparability and homogeneity of the existing data. We realised that some four years ago when we conducted a little probe of Member States and asked them to provide us with some statistics. We realised fairly rapidly that we were comparing apples and pears. At national level, for instance, the way one Member State counts suspicious transaction reports may be different from another. For instance, in one Member State they become suspicious activities reports and so a suspicious activity may be one that is related to a transaction or multiple transactions or none at all. Therefore, the data we receive from a number of Member States are simply not comparable. That may be an issue, to measure the relative efficiency of the systems in place in Member States or the FIU efficiency, if you want, or the whole chain. That is why we need homogeneous data and a more intimate knowledge of the machinery, because we need to be able to read beyond the statistics. I

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should say that when we did that exercise we were relatively surprised because some Member States did not even want to provide us with that data, although they are fairly innocuous. Why? Because they were afraid that we would start interpreting the raw data in a way that would be inappropriate and we would compare them against each other in inappropriate ways. As I said, the Commission has not given up hope and maybe Jakub can tell you what we do in this respect.

Mr Boratyński: It is a part of the general effort to have more evidence-based policies in the area of the fight against crime and criminal justice that the Commission has adopted the action plan called Developing a Comprehensive View of Strategy to Measure Crime and Criminal Justice, which again treats horizontally the issue of criminal statistics across the EU, and indeed money laundering has been identified as one of two priority areas, the second one being trafficking in human beings. In this context a financial crime sub-group was set up in order to determine the list of indicators that would allow comparability of data among Member States, therefore addressing exactly these practical obstacles that Philippe was describing. The whole idea was to draw these indicators from Article 33 of the Third Directive. Anyway, we will not talk any more about these problems with comparability because Philippe has already given a sufficient number of examples to make you aware of what it is about. In practical terms what do we intend to do now? We are at the stage where these indicators are being discussed. We propose to refine the questionnaire and give additional guidelines to Member States, to national authorities that will be collecting this data. We are also providing our statistical arm of the European Commission, Eurostat, with the list of specific contact points with Member States among other entities that provide relevant data. If everything goes well we hope to have the first batch of comparable data, however imperfect it is, by the end of the year. That is quite ambitious but we hope we will get there, and obviously we are always stressing that this is a gradual process. It is not that we will have completely reliable statistics but it is an important step and for us the exercise is money laundering. It is also a very important exercise in our overall effort to increase the availability of comparable criminal statistics across the EU.

Q319 Baroness Henig: At page 11 of your memorandum of 30 January 2009 there is mention of a 2008 study on alternative methods to identify beneficial owners which “provides the first example of cost-benefit analysis carried out on a pan-European scale (although on a single topic)”. I just wondered whether you could elaborate on the

relevant findings of the study and what the anticipated time-frame would be for the major cost-benefit analysis of AML/CFT systems in all 27 Member States which has been submitted for co-financing.

Mr Boratyński: Indeed there are two issues. One is the study which, while it has not been published, has been extensively discussed with Member States with specific authorities. I will elaborate a bit on the findings of the study. The study is divided into two parts, the first compares the cost or benefit arising from two models of the disclosure system of beneficial ownership of private and public companies. This is the so-called Model Zero, the model that reflects the world as construed by the Third Directive where the critical role is played by intermediary institutions. The possible new model, Model One, is an up-front and ongoing disclosure system based on the obligation first on a beneficial owner to notify the company and then for each company to publicly declare their beneficial owners, so with less burden on intermediary institutions, but, of course, they would still play an important role. This cost/benefit analysis concludes that while Model Zero duplicates a number of anti-money laundering operations and tools and therefore costs, Model One, the new model, can ensure a higher degree of information sharing among the subjects involved in the anti-money laundering effort, therefore also increasing the efforts undertaken by specific entities. One of the elements of the Model One system would be a publicly available central register. The study really goes into great detail. It is quite impressive in terms of the effort which has been invested in taking into account a variety of factors and variables in coming up with conclusions, but it speaks in favour, with all sorts of caveats, of Model One. The second part of the study aims to identify the EU measures that may be taken against those facilitating anti-money laundering and how to improve the regulations of charities, trust associations and foundations. On the first aspect the study concludes that some professions are not supervised and that monitoring is indeed occasional, that the models of self-regulation are not necessarily very effective and the sanctions are either absent or not properly implemented and they formulate some recommendations on how to address such shortcomings. On the second aspect the study concludes that the risk that trusts will be exploited for money laundering or terrorist financing reasons is indeed quite high. On the other hand, foundations, associations and charities in the European Union seem to be sufficiently well regulated from that perspective, and again the study comes up with some formulations. The second element of your question was about a specific project which is part of an open

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call for proposals announced by the Commission, again in the context of our prevention and fight against crime programme. This is a confidential procedure so we will only know whether the project is going to be financed by the fall of this year. If the decision on that specific project, which could be compared with a variety of other projects, is positive the project could start at the end of 2009 but, given the status of this project, we cannot say more about its content.

Mr Pellé: I just want to add something about a study we recently conducted on the cost of compliance of a number of directives in the field of financial services. We conducted that study in relation to six key directives in the field of financial services, including the Third Anti-Money Laundering Directive. The study should be published soon, hopefully, and so we will put it on our website probably by this summer, if not earlier. The study focused on what we call incremental compliance costs originating from the new regulation. As far as the AML Directive was concerned for banks, financial conglomerates and investment banks, what is called a one-off cost of compliance represented approximately ten per cent of all the financial services regulatory costs borne by the banks. On an ongoing basis, because this was a one-off on, let us say, investing in the IT and the training of staff, the cost of compliance represented about 13 per cent of the total regulatory compliance costs as an approximation. We have some figures for a number of banks, absolute figures. It is a bit complicated but nevertheless it might be of interest to you and, as I said, it should become public between now and the summer.

Q320 Lord Hannay of Chiswick: But will you also be analysing the compliance costs of the 27 national regulations which were superseded by the European one?

Mr Pellé: The problem, as I said, is that the Community legislation as far as the Anti-Money Laundering Directive is concerned is a minimum requirement, as we say in our jargon, which does not prevent Member States adding requirements. It is for them to decide whether or not to have additional requirements because by doing this they recreate an uneven playing field for industry when the whole objective of having Community legislation in this field was indeed to establish a level playing field. My

colleague has some notes on that. Gold-plating was not mentioned in this exercise. There was a debate on it and it was decided not to take gold-plating into consideration. We were looking only at the impact of the Community legislation, not the way it is implemented.

Q321 Lord Hannay of Chiswick: The question I was asking also related to cases like the original basic Banking Directive which superseded every Member State having its own banking directive, so that the compliance cost of the EU Banking Directive should properly be netted out to take away the removal of compliance costs of all the national varieties.

Mr Pellé: Yes, I see your point. I do not know whether we studied the displacement of the national legislation by the Community one and the related savings, but that is a fair point.

Q322 Lord Hannay of Chiswick: Otherwise the figures get misused by people who say that this is in all circumstances an additional burden.

Mr Pellé: Indeed, yes, fair point.

Q323 Chairman: If there are no more questions that any of my colleagues want to ask let that be the end of this meeting. You have been exceptionally helpful to us in two ways: first, the document you kindly sent us which we appreciate very much, and, secondly, the helpful way in which you have answered really rather a lot of questions this afternoon. This has been of very serious help to us and we shall be carrying on a number of other witness sessions in the next few weeks. We hope to produce a report before Parliament rises for the summer in mid July and we shall, of course, send you copies of our report as soon as we have published it. It has been a very useful afternoon indeed. Thank you all very much. It seems the burden of answering our questions has fallen in the centre of the panel and we have not heard terribly much from those on the outside but I am sure they were full of all sorts of useful information which we might have had.

Mr Boratyński: It is a collective work.

Q324 Chairman: No doubt they put a lot of the briefs together.

Mr Pellé: Yes.

Chairman: Thank you very much.

WEDNESDAY 1 APRIL 2009

Present	Jopling, L (Chairman) Avebury, L Faulkner of Worcester, L Garden of Frognal, B	Hannay of Chiswick, L Hodgson of Astley Abbotts, L Marlesford, L Richard, L
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Memorandum by the Queen Mary University of London 2008-9 LLM Law of Economic Crime Group

INTRODUCTORY/SUMMARY

The response will deal with some of the specific questions raised by the Committee, in the order in which they are raised. Our major general concerns are as follows.

1. We consider that the EU might accept too uncritically the recommendations and methodology of the FATF. The decision- and policy-making structures of FATF are themselves insufficiently transparent to warrant their uncritical acceptance.
2. We are equally concerned that the procedures of the EU are themselves too complex for transparency in decision- and policy-making.

COOPERATION WITH AND BETWEEN FINANCIAL INTELLIGENCE UNITS (FIUs)

Q. How effective is cooperation among FIUs, and between FIUs and other authorities? What are the practical results of this cooperation?

A. Domestic cooperation

The Review of the Suspicious Activities Reports (hereinafter SAR) Regime (the Lander review) published in March 2006 led to significant changes to the institutional framework of the financial intelligence unit in England and Wales. Most of the recommendations set out in the review were taken up by the government, most notably to create the UK's FIU within the Serious Organised Crime Agency (SOCA) which replaced the NCIS (National Criminal Intelligence Service).

The UK's FIU has authority to disseminate information to UK police forces and law enforcement agencies (amongst other bodies) when there are grounds to suspect money laundering or financing of terrorism. Law enforcement end-users have access to almost all SARs received by the FIU through the SAR database (ELMER) via Moneyweb. The exceptions are SARs relating to particularly sensitive subject matter, such as terrorism or corruption and those received from foreign FIUs. The FIU performs searches on the full database on request.

However, despite being the national body responsible for handling SARs, including receiving, analysing and disseminating SARs, the UKFIU has been criticised by the Financial Action task Force (FATF) for showing insufficient initiative in conducting its own analysis on SARs: largely leaving law enforcement agencies to conduct their own analysis.

Within the UKFIU is a Dialogue Team with responsibility for liaising between other branches of SOCA and domestic law enforcement as well as the reporting sector. Beyond that, the UKFIU also acts as the facilitator of meetings with representatives from domestic law enforcement agencies every quarter to encourage further cooperation between the organisations.

The FIU itself has access to information from other authorities including the Police National Computer and the asset recovery database (JARD). However, it only has indirect access to certain databases requiring the FIU to submit a request such as for tax information from HMRC. The FATF Third Round Mutual Evaluation Report of the UK has suggested that this creates an undue delay and suggests the FIU consider more direct access to such information in order to assist in its SARs analysis.

SARs have been used to initiate and assist in money laundering investigations by end users that have led to arrests, the laying of charges, convictions and the obtaining of restraint and confiscation orders under the Proceeds of Crime Act 2002. The 2008 Annual Report provides some statistics and anonymised case studies to highlight the assistance given by SARs to law enforcement authorities in money laundering cases. The

Metropolitan Police Service had the highest number of convictions for money laundering charges involving use of SARs intelligence—124; where SOCA itself reported only 40. The UKFIU reports of one case of legal action against a corrupt overseas official as a result of SARs intelligence.

In relation to terrorist financing, the proportion of SARs disseminated to the National Terrorist Financing Investigation Unit is very small (under 1000 between October 2007 to end September 2008). To what extent this has yielded practical results is not reported. We suspect little effect.

INTERNATIONAL COOPERATION

Egmont Group

The UK was a founding member of the Egmont Group and continues to play a leading role within the network. Having seen a significant increase in staff numbers since becoming part of SOCA, the UKFIU has been responding more quickly to requests for financial intelligence. In its latest report, the UKFIU reports that requests from Egmont members are completed within 10 days, which compares favourably to the Egmont standard of 30 days. The UKFIU is permitted to enter into Memoranda of Understanding (MOUs) with foreign FIUs, although exchange of information is not limited to such countries. Assistance is requested through an information request form that must contain relevant background information and a clear connection between the subjects and the UK.

The FIU has the authority to conduct searches of other databases it has access to (mentioned above) as well as the SARs database on behalf of foreign FIUs. However, it is not permitted to release information from an outside law enforcement agency before it has received prior consent.

FIU.Net

FIU.Net is a decentralised electronic system allowing bilateral exchange of basic identifying information between a number of European states. Member states and subsequently enquiries made on FIU.Net has increased substantially year on year since its inception in 2002. The European FIUs' Platform has encouraged the use of FIU.net as a means of ensuring speedy feedback about the use of information by the requesting FIU.

It is difficult to determine the practical results flowing from FIU-FIU cooperation, as such information is not readily available to the public. In most cases there are few data on the extent to which exchange of information between FIUs has led to the laying of charges and successful prosecutions or recovery of assets in the state of the requesting FIU.

In this regard, meaningful feedback to FIUs supplying the information on the usefulness of their responses would provide valuable insight into the effectiveness of FIU-FIU cooperation.

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

A. Consulting the representatives of the most directly concerned sectors before the draft legislation is presented to Parliament can have a number of advantages.

First, consulting the private sector offers the government an opportunity to build confidence in the proposed agency on the part of the institutions that will be required to send suspicious transaction and other reports to it. Second, for the FIU, the consultations may help the planners, and later the FIU itself, in developing requirements for reporting transactions that can realistically be expected to be followed by the reporting entities. Third, for the reporting entities, the advance consultations will serve to make the concerned institutions aware of their future obligations and the related need to develop the necessary programs to fulfill their obligations. Fourth, the private sector will be able to make known its compliance costs.

Early consultations with the private sector will also provide an opportunity for the authorities to highlight the benefits of the new system to financial and other institutions that will have to begin reporting transactions to the FIU.

NECESSITY OF FEEDBACKS TO THE PRIVATE SECTOR

The FIU should provide feedback about money laundering and terrorist financing trends and typologies that will assist financial institutions and non-financial businesses and persons to improve their AML/CFT practices and controls and, in particular, their reporting of suspicious transactions. FIUs will also need to maintain comprehensive statistics on suspicious transaction reports (STRs) received and disseminated.

By the nature of their work, FIUs have access to and generate massive quantities of financial information. The resulting intelligence and expertise in analysing such information could provide useful feedback to financial institutions. In most cases, however, feedback tends to be limited to general statistics on reports. It has been suggested that more detailed and specific information on money laundering operations would be more useful. Information could be broken down into such categories as the number of reports received per sector or institution, their monetary value, the geographical areas covered, and the number of cases investigated and referred to prosecution. The use of sanitised cases in which identifying features have been removed is invaluable, as these provide examples of money laundering and the outcome of such cases.

Such feedback would:

- enhance cooperation between financial institutions and the FIU. It would instil confidence in financial institutions that their reports are being taken seriously and are contributing to the fight against money laundering;
- enhance the capacity of reporting personnel in identifying suspicious transactions, including the ability of compliance officers to filter reports that warrant reporting from those that do not;
- provide financial institutions with useful information that would enhance their capacity to keep abreast of money laundering trends and therefore improve their anti-money laundering strategies;
- assist financial institutions to set up improved systems to prevent and detect money laundering and in the process protect the integrity of these institutions against money launderers; and
- enable the reporting institution to take appropriate action regarding its relationship with the customer following the outcome of the report.

The most common type of feedback takes the form of statistics published in periodic newsletters or annual reports. Factors such as the resources allocated by a country to its FIU for the compilation of statistics have a bearing on the frequency of such feedback. The Financial Intelligence Centre (FIC) of South Africa states in its annual report that it exchanges statistical information with supervisory bodies at regular meetings. It also issues statistics on suspicious transactions in this annual report. The centre, however, only reports regular training and feedback to reporting institutions regarding suspicious transaction reports.

The advantages of feedback to financial institutions need to be balanced against prevailing secrecy and privacy obligations. A common complaint of financial institutions is still that they expend time and resources in filing suspicious transaction reports, but they do not know what happens to those reports. This can be disheartening, can contribute to a lack of vigilance in filing reports, and ultimately weakens efforts to fight the scourge of money laundering.

Feedback to the private sector is more important with the introduction of the Risk based approach to reporting. Private sector institutions need advice in setting their reporting thresholds.

EU INTERNAL ARCHITECTURE

Q. To what extent is the EU internal architecture adequate to counter current and future challenges?

A. The institutional architecture of the EU

The development of EU money laundering counter-measures has had to take into account the complex institutional structure of the Union. In the early 1990s, when the (then) European Community was called upon to align its legislative framework with international initiatives such as the 1988 United Nations Convention on drug trafficking and the 1990 FATF 40 Recommendations, the EC Treaty did not include an express legal basis for the adoption by the Community of criminal law measures. The absence of such a legal basis was addressed by framing Community money laundering law not as a criminal law measure, but primarily as necessary to protect the increasingly integrated Community financial system. The first money laundering Directive was thus adopted in 1991 under legal bases relating to the free movement of capital and the internal market. The Directive included a plethora of regulatory provisions addressed primarily towards banks, but also introduced a prohibition (but not a criminalisation) of money laundering. However, money laundering has since been *de facto* criminalised in all EU Member States.

The 1990s saw significant constitutional developments at EU level. The entry into force of the Maastricht Treaty (and its subsequent amendments in Amsterdam and Nice) saw the introduction of a complex three pillar structure for the (now) European Union. The first pillar now deals with the EC Treaty (the core Community competences including free movement and the internal market); the second pillar deals with common foreign and security policy; and the third pillar with police and judicial co-operation in criminal matters. The second and third pillars can be described as more “intergovernmental” in comparison to the supranational

Community pillar. Reflecting the sensitivity of the respective subject matters of foreign policy and crime, the institutional provisions governing these pillars are designed to safeguard to the extent possible state sovereignty in these fields. The compromise between extending the Union's powers on the one hand and maintaining state sovereignty on the other has led to a highly complex and differentiated legal and constitutional framework in the EU.

This institutional complexity has been reflected in the development of a series of EU anti-money laundering measures. The various official justifications for such measures and the chameleon use of the fight against "dirty" money (deemed by policy makers and legislators as necessary to protect not only the financial system, but also society as a whole from drugs, then serious organised crime, and more recently terrorism), have led at EU level to the development of money laundering law in all three pillars of the EU Treaty. First pillar law includes measures such as the money laundering Directives (most recently amended in 2005 via the third money laundering Directive- the first pillar method continued to be used notwithstanding the introduction of an express third pillar criminal law legal basis post-Maastricht) and measures dealing with the monitoring of the flows of money; second pillar law includes measures related to terrorism as a foreign policy threat; and third pillar measures are focused on criminal law, and include measures such as confiscation orders. A number of these measures (such as those related to the freezing of terrorist assets) are cross-pillar, while for others (such as the work of financial intelligence units) there is currently an overlap between first and third pillar law. This overlap is also reflected in the role of the various EU criminal law bodies in the field of money laundering. Such bodies include OLAF (the European Anti-Fraud Office, a first pillar office which proclaims its independence but is still part of the European Commission), SitCen (the second pillar situation centre reporting to Javier Solana) and the third pillar bodies of Europol and Eurojust. As this Committee has noted in previous inquiries, the boundaries between these bodies are not always clear and the danger of competition rather than co-operation is present in this context.

These complex institutional arrangements pose a number of challenges, both in terms of transparency and scrutiny of the relevant EU initiatives, but also with regard to the protection of fundamental rights including privacy (with EU privacy law currently fragmented in the light of the pillars) and judicial protection (the Kadi judicial saga being a prime example of such limits). The pillar structure may also have a significant impact on the coherence of EU anti-money laundering action, with different measures negotiated in different fora and under different rules and procedures. The *prima facie* abolition of the pillars if the Lisbon Treaty enters into force would contribute towards addressing these issues. However, a number of issues relating to institutional architecture will remain post Lisbon. The first issue concerns the continued special nature of the EU foreign policy provisions. The second concerns the continuation of overlaps between Treaty legal bases in the development of money laundering law (the example of economic sanctions for terrorism is central in this context). And the third issue concerns the continuing overlap between the work of EU bodies. With the Lisbon Treaty leaving the window open with regard to the future establishment of a European Public Prosecutor "from Eurojust", the extent of the realignment of the relationship between Eurojust, Europol and in particular OLAF in this context remains to be seen.

Q. What is the role of Europol in countering money laundering and terrorist financing?

A. The EU Organised Threat Assessment 2007 (OCTA 2007) professes money laundering as one of several priorities for Europol in relation to serious and organised crime. With no executive powers of its own, Europol works to support cooperation between law enforcement agencies of Member States through the creation of a network for detecting and seizing assets and interrupting criminal networks. The main purpose of Europol is to provide intelligence to member states and maintain a computerised system of information in the form of the Europol Information System (EIS) and analysis work files (AWF).

Europol focuses on cross-border money laundering investigations, recovery of the proceeds of crime, linking suspicious transactions reported by member states with offences committed in individual member states. The recent extensions of their mandate have enabled Europol to make use of financial data from different sources to develop intelligence-led policing practices in relation to financial crimes.

Since 2001, Europol has developed an AWF on suspicious transactions (AWF SUSTRANS) to conduct analytical work on money laundering in the EU. In this regard SOCA is supporting the project working groups.

Terrorism, especially Islamic terrorism, has been a major focus of Europol. The first Terrorism Situation and Trend report was published in 2007, which describes and analyses the outward manifestations of terrorism in the EU, covering trends relating to terrorist financing. A second report was published in 2008 which showed a marked decrease in arrests for the finance of terrorism from 2006 to 2007 in relation to Islamic terrorism. Europol also conducts two operational analysis work files in relation to terrorism.

MONITORING IMPLEMENTATION

Q. What EU mechanisms exist for monitoring implementation of the relevant legislative measures, and what results in terms of formal compliance and effective implementation have so far emerged from the use of those measures?

A. Due to the EC Treaty, the Member States have an obligation to adopt their legislations according to the EU directives or to achieve the result envisaged by the directive. In the same way, under article 10 EC, the European Commission has the responsibility of taking all appropriate measures to ensure that the fulfilment of EC law is correctly applied by all Member States. The Commission has various authorities to combat non-compliance. Firstly, the pre-litigation administrative procedure may be taken to ask the Member States to apply Community anti-money laundering legislation. The Commission sends a formal letter of notice, requiring the Member State to comply with that community law within a giving time limit. Secondly, the Commission will consider the situation of infringement and why the member state has failed to fulfil that community law and to determine the subject matter of any action, once again requiring the Member State to stop the infringing act or omission within a limited time. Finally, if any Member State has not still to complied with its obligation, the Commission has the power to refer the matter to the European Court of justice (ECJ)(Article 226 of the EC Treaty). This is regarded as the final stage. For example, In October 2008, the Commission decided to refer Belgium, Ireland, Spain and Sweden to the ECJ court for their continuing failure to implement the Third Directive of anti-money laundering law. If the case goes to court and the court finds against the Member State concerned, it will have to implement the Directive. In case of continuing non-implementation, the Commission, once again, can refer the cases to the ECJ together with a recommendation for a financial penalty to be imposed on the Member State, based on the seriousness of the infringement, the duration of the infringement and the need to ensure that the penalty itself will be a deterrent to further infringement.

Q. What are the implications of those results for cooperation within the EU, and more broadly?

A. In principle, cooperation is directed against certain harms. Structural conflicts and competition can impede prevention and control even in countries with adequate legal and regulatory provisions and a desire to avoid involvement in money laundering. Firstly, legitimate banks are influenced by the competitive of offshore banks, of less scrupulous banks and of less closely regulated institutions and business. Second, law enforcement agencies, both nationally and internationally may compete against each other for visibility in a way which detracts from information sharing. An investigative or regulatory agency, in possession of information which could furnish the basic preventive or penal action by a different entity, may not communicate that information as long as it has any possibility of itself taking action which would reflect favourably on its own reputation or program, rather than sharing it with the competitor agency. Finally, dealing between the financial and regulatory communities, or between either of those and the law enforcement community, may be characterized more by mutual suspicion than by mutually profitable trust and cooperation. Internationally, a lack of harmonization of legal and regulatory cultures may make cooperation virtually impossible.

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

A. The revision of the E-Money directive

The Commission adopted on 9 October 2008 its proposal for revising the current rules governing the conditions for issuing electronic money in the EU (COM (2008)627). The proposal provides for a modern and coherent legal framework for issuing electronic money and also updates anti-money laundering requirements by proposing to amend Article 11(5)(d) of the 3rd AML Directive, ensuring consistency with the thresholds of the Payment Services Directive.

COMPLIANCE AND EQUIVALENCE

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

The 2005 Directive adequately encourages non-EU states or third countries which have introduced compliance equivalent systems to counter money laundering and the financing of terrorism. This directive presents the following rules and regulations belonging the directive articles as follows;

- Article 1, 3 there is illustrated that money laundering shall be regarded as such even where the activities which generated the property to be launder were carried out in the territory of another Member State or in that of a third country.
- Article 11 2 (a) and (b) and 4 in the section 2 which is Simplified customer due diligence.
- Article 13 3 and 4 in the section 3 which is Enhanced customer due diligence.
- Article 16 in the section 4 which is Performance by third parties.
- Article 28 and 29 in the Chapter III section 2 which are prohibition of disclosure and
- Article 31 in the Chapter IV which is Record keeping and Statistic Data.

Examination of Witness

Witness: PROFESSOR PETER ALLDRIDGE, Head of the School of Law, and DR VALSAMIS MITSILEGAS, Reader in Law, Queen Mary University of London, examined.

Q325 Chairman: Welcome, Professor Alldridge, I am sorry that we have kept you both waiting, and Dr Mitsilegas who is an old friend of this Committee. Welcome to you both. Perhaps both of you would like to begin by introducing yourselves for the record and then we will start the questioning.

Professor Alldridge: My name is Peter Alldridge and I am Professor of Law and Head of the Department of Law at Queen Mary University of London.

Dr Mitsilegas: I am Valsamis Mitsilegas and I am Reader in Law in the same department.

Q326 Chairman: Thank you very much. I will begin with the first question. In the evidence that you kindly sent us, on the first page you identify as a major concern the fact that the EU might accept too uncritically the recommendations and methodology of the FATF. Will you elaborate on what is the basis for this concern, please.

Professor Alldridge: FATF, in my view, needs a constitution. It was established in 1989 as an offshoot of the G7. It has operated on essentially an ad hoc basis for the last 20 years and a temporary basis for the last 20 years. Its decision-making, its policy-making and its information-seeking practices are by no means clear. I spent some time looking at their website yesterday and asking myself questions like, how exactly do you get to be a member of the FATF, how does it function, how does it make the rules and how does it come up with its recommendations? These matters are not as clear as they should be. If FATF is to be a standing body, it should become a properly constituted body, presumably established by an international convention. What follows from that so far as concerns the EU is that we need to scrutinise carefully the information which the EU is given by FATF. For example, if we take the first recital to the Third Money Laundering Directive, this is information supplied by the FATF, “massive flows of dirty money can damage the stability and reputation of the financial sector”. This looks rather strange

now. The financial sector has actually a very bad reputation. We might very well have been looking in the wrong place. Perhaps we should have been looking to the bankers rather than the criminals. If that is the basis for which we are pursuing money laundering, then, fine, let us have that set out, but let us have it set out in terms so that we can scrutinise it.

Q327 Lord Richard: You have partially answered the question that I have in mind. If you look at the first paragraph of your paper, you say, “We consider that the EU might accept too uncritically the recommendations and methodology of the FATF” and that is fine, you do that. “The decision and policy-making structures of FATF are themselves insufficiently transparent to warrant their own uncritical acceptance”. I think that you have partially answered that but would you expand upon what you see as the insufficient transparency of the decision-making and policy-making structures of the FATF.

Professor Alldridge: You cannot discover from the website for example whether there are debates, whether there are votes, who says what and how the decisions are arrived at. These are matters which in any powerful legislative body, and effectively FAFT is a powerful legislative body, would be published.

Q328 Lord Richard: Has anybody complained about it apart from academics obviously?

Professor Alldridge: Yes. The answer is that people complain who have their financial services sector shut down on the basis of FATF. So, yes, go to a small island in the Caribbean and you will find people complaining.

Q329 Lord Richard: Do governments complain?

Professor Alldridge: Yes.

Q330 Lord Richard: So, the British Government have complained about it?

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Professor Alldrige: I do not know if the British Government have complained. I suspect that they have not, but the governments of many jurisdictions have.

Q331 Lord Richard: Which ones? Can you give examples?

Professor Alldrige: The Bahamas, Grenada and Antigua.

Q332 Lord Richard: Mainly Caribbean?

Professor Alldrige: I am not a criminologist. It just so happens that I have spoken to people from those jurisdictions and they have complained.

Q333 Chairman: It seems that is an opportunity for supplementary evidence.

Professor Alldrige: It might very well be; I would not be the person to furnish it.

Dr Mitsilegas: I would like to add to that. It is not exactly at the government level but at the European Union level. I read with interest the evidence you took from the Counter-Terrorism Co-ordinator last week who explicitly accepted that there is a degree of policy laundering from the FATF to the EU with regard to the anti-money laundering standards and I think in the EU a good example of a body which had complained about the substance of FATF's standards is the European Parliament during the passage of the Second Money Laundering Directive which the Committee may know was agreed at the very last stage of conciliation. So, there was the Commission tabling the proposal for amending the First Directive. As with the First Directive, the main justification was that we have to align ourselves with the FATF standards. It is not really clear how the standards have been produced and what generally they represent. The EU legislative bodies have to deal with this and you already see a certain reaction to having to accept the standards at the EU level uncritically. So, I think that there are issues if we accept this top-down approach.

Q334 Lord Richard: You have commented on there being a lack of transparency whereas, if you knew what was going on, you could judge it better.

Dr Mitsilegas: And if you had the opportunity or advantage of participating in the formation of the standards.

Q335 Lord Hannay of Chiswick: I would like to follow up on that. The course of action which you are proposing, which is the negotiation of an international convention by the members of the FATF, would of course lay the said convention open to the requirement to be ratified by the US Congress which means a two-thirds majority of the Senate. I do not think that anyone in international affairs takes

lightly a move which actually drives a piece of rather effective international counter-terrorism policy into the arms of a body like the US Senate which may or may not approve and which, if it does not approve, the thing then dies. I would have thought that it was a fairly high-risk strategy and perhaps you could comment on that. My second point relates to the EU and I would like to ask this question. Are there not similar considerations in respect of your complaint about the EU too uncritically accepting the FATF conclusions given that the Commission, which is after all the guardian of the treaties and also the guardian of the three Money Laundering Directives, is a member of FATF and is presumably meant, in its membership, to ensure that what FATF does is compatible with what the EU does? Is not the whole concept of the EU criticising the FATF irrespective of the fact that most of its large Member States are members of it a pretty bizarre one?

Professor Alldrige: To answer your first question, I do not know enough about the politics of international relations as administered by the US Senate to take a view. Your second point, as I understand it, is that since the Commission is a member of FATF, it would be absurd for it to criticise.

Q336 Lord Hannay of Chiswick: No, not that it would be absurd to criticise it at the meetings of the FATF. I mean, the Commission is presumably there to put up its hand and say, "I am sorry, this does not seem to be in conformity with the law".

Professor Alldrige: But we do not even know that, do we?

Q337 Lord Hannay of Chiswick: I know that you do not know it, but I am suggesting that the idea that the EU accepts too uncritically the recommendations could be open to a misunderstanding.

Professor Alldrige: Would it be better expressed as, there is not enough information to form a view as to whether or not . . . ?

Lord Hannay of Chiswick: Thank you for that answer.

Q338 Lord Avebury: What I was wondering is whether the EU does not have any consultations before it adopts recommendations of the FATF. Recommendations come forward from the FATF. Surely they do not simply rubber stamp them and issue them as directives. They will be put out to consultation and at that stage there will be the opportunity for the organisations that are affected by the recommendations to make their own suggestions of modification. Is that not the point at which these recommendations should be critically examined?

Professor Alldrige: I think that they should be critically examined before the FAFT recommends them.

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Q339 Lord Avebury: What difference would it make in practice to the end result?

Professor Alldrige: I think the difference it would make in practice is that once you have the document circulated, then it takes on a force and a momentum of its own and it is much less easy to get it changed than at any later stage.

Q340 Lord Avebury: But they do put them out for consultation.

Professor Alldrige: They do.

Q341 Lord Avebury: Do you think that they very seldom make alterations in the documents as a result of the responses to the consultation?

Professor Alldrige: To the best of knowledge, yes.

Q342 Lord Marlesford: My concern is, to what extent is FATF subject to scrutiny by anybody? For example, we have asked them to give us evidence orally and they have refused. They have apparently said that they will give us evidence in writing which they have not as yet done. My concern is that any body which is financed by countries has the obligation to submit itself to scrutiny. How do you suggest that we should achieve that objective if you agree that it should be an objective?

Professor Alldrige: I certainly agree that it should be an objective. I do not know how you would go about doing it.

Q343 Lord Hannay of Chiswick: The Committee has been told by the Treasury representative on FATF in earlier testimony that consideration is currently being given within FATF to a change in its traditional stance on tax evasion issues. What, given the experience of the UK in this area, are in your view the advantages and disadvantages of making tax matters predicate offences for money laundering?

Professor Alldrige: By the traditional stance, I take it you mean the view that tax evasion should not in general or need not in general be treated as a predicate offence?

Q344 Lord Hannay of Chiswick: Yes.

Professor Alldrige: Under the law of the UK, tax evasion is potentially a predicate offence. Whether or not it is in any given set of circumstances I say depends upon whether you can identify the criminal property or not. In the case of for example fraudulently claiming a tax rebate which is the base of carousel frauds and other things, then there will be property; there will be a cheque from the Government. In the case where you simply do not declare a liability to tax, it is not clear to me, even granted section 340(6) of the Proceeds of Crime Act, that tax evasion would operate as a predicate offence for a laundering charge. I think that there is a more

general issue at stake here which is, how closely do we need the system of criminal justice and the system of tax collection to be bound up one with another? Until relatively recently, those responsible for collecting tax took the view that they need not engage much with criminal justice. They had enough shots in their locker and enough mechanisms available to them to collect tax that criminal justice was seen as a rather inefficient mechanism of going about it. That might have changed. We do need to look into different respects in which tax evasion and other forms of criminality can be connected. There are other jurisdictions which take the view that tax evasion should not be a criminal matter at all, just an administrative matter, and, if this is going to change, then that would have to change at the least. The advantages of adopting what is the UK's position of saying that tax evasion should operate as a predicate offence is that it will allow, if you are concerned to do this, the numbers to be increased of proceeds that you can prescribe to laundering. My own view is that we need better mechanisms for collecting tax across jurisdictions but that the mechanism of saying that evasion is a very serious offence and so it should be subject to the laundering mechanism and that it is a crime to launder money and invoking the whole anti-money laundering framework may not be the way to go. There is also a constitutional question. It so happens under English law that proceeds of crime are taxable. If you make your living as a burglar, then in theory you are liable to pay tax on that. That is not the case in many other jurisdictions. That generates a position where, if somebody has unaccounted wealth and the State wants to move against them, then one possibility might be to charge laundering the proceeds of tax evasion. Let us say that the State cannot identify by what crime the unaccounted wealth was generated but the suggestion is that it is one or the other, you then say, all right, it does not matter what the predicate offence is, you are laundering the proceeds of tax evasion because you have not declared the money that you gained by crime for the purposes of taxation. That in a way would be okay, there are always the people who will say, "If you have nothing to hide, then why should you not have to declare it?" but, in a way, it makes a major constitutional change in the relationship between the subject and the authorities because it makes the authorities much more able to call upon people to account for themselves without really any further evidence. So, that is a roundabout way of saying that I would be hesitant about extending AML into the tax arena.

Q345 Lord Marlesford: I am very interested in your reply because tax evasion is a crime, shoplifting is a crime and I understand that speeding is a crime, but would you not agree that they are relatively minor

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crimes in terms of degree? SOCA's name is the Serious Organised Crime Agency and it is a little curious to think that tax evasion should be elevated to the level of the sorts of crimes to which one is hoping SOCA is focusing on. Indeed, we have been given evidence by SOCA which indicates that they welcome all reports and indeed their annual report lists the number of reports they have had from whatever source with many people being required to make reports of any crime—that is the sort of people who are required to make reports—with no de minimis cut-off at all and no proportionality and very little scope for any judgment by those making the report. This seems to me to support your view that it is at least questionable as to whether tax evasion should be reclassified to put it in to this category. Would you agree?

Professor Alldridge: Yes and there is an underlying issue here which is, what do we understand to be wrong with money laundering? If we understand money laundering to be a form of complicity in the original crime, then we should have regard to the predicate offence, but if we understand money laundering to be wrong for the reasons that are set out in the recital at the beginning of the EU Directive, that is to say for reasons which are independent of the original crime, then of course it will not matter whether it is speeding or whatever offence it is. My inclination and certainly the inclination of the English criminal courts at the moment is that we should always have regard to the predicate offence and not lose sight of it.

Q346 Lord Hodgson of Astley Abbotts: This partially covers the ground that Lord Marlesford has just dealt with but because of the all serious crimes approach in the Third Anti-Money Laundering Directive linked of course to the very wide drafting of sections 327 to 329 of the Proceeds of Crime Act, we are getting a very wide range of reports and perhaps you could say a little about the advantage and disadvantage from your point of view of the narrow and wide approach—we are on the wide approach at present—and could we adopt an alternative approach, maybe some carve-out on sections 327 to 329 to deal with the less serious offences, and still comply with FATF standards?

Professor Alldridge: The general issue is, are you going to have a wide category or a narrow category, and I tend to agree with the thrust of the question that we still have not really seen in the United Kingdom the full width of the Proceeds of Crime Act applied and, if it is applied as its text would allow, it is going to have very serious consequences for example for financial markets. If we take a crime that I am sure everybody here remembers, the Guinness takeover of Distillers, what Guinness do is to falsify their accounts so as artificially to inflate their own share

price, they are making a cash and shares offer for Distillers and because the share price is artificially inflated, the shares are overvalued and so the offer is more attractive. As a consequence of that, Distillers accept the offer. Guinness and various people who work for Guinness are subsequently brought to court. This is before the 2002 Proceeds of Crime Act and, under the Proceeds of Crime Act, the entire Distillers company, lock, stock and sinker, would be subject to confiscation as being the proceeds of crime. The all crimes approach will commit you to that sort of slightly absurd consequence—I think that it is an absurd consequence—and, if that were to happen, then the economic consequences might be very serious. So, I would favour, as I think the question implies, a more thought-out list. Obviously, in legislating questions, do you want a general provision or do you want a list and the answer is that you want a general provision if you are prepared to take the risk that something is included that you did not really want to include and you want a list if you want to be more careful. It probably would have been better had there been a list. Can that be done consistently with the current requirements of the FATF? I think the answer to that is probably “no”.

Q347 Lord Hodgson of Astley Abbotts: The proceeds of a crime in the case you gave would be the entire proceeds of Distillers or the amount by which the share price had been inflated?

Professor Alldridge: The entire Distillers company, everything. It is very clear under the UK legislation, unlike legislation elsewhere, that proceeds means proceeds, it does not mean profits. So, you do not get a deduction for, for example, the person you use to defend yourself if you are a drug dealer.

Q348 Lord Hodgson of Astley Abbotts: I am going to press you; is there any value, following again on what Lord Marlesford was saying, in some form of de minimis below which the thing just drops away?

Professor Alldridge: De minimis certainly would be allowed by the FATF guidance but the de minimis would not be the nature of the crime, it would be the penalty.

Q349 Lord Avebury: May I ask you about the exemptions to the reporting obligations of lawyers in Article 20 of the Third Directive covering information obtained before, during or after judicial proceedings or in the course of ascertaining the legal position of requirement. Did these exemptions satisfy representative organisations of lawyers which I think had been concerned with the breaches of professional legal confidentiality which they saw as being imposed by the Second Directive?

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Dr Mitsilegas: This has been one of the most controversial aspects of a revision of European Union law and again this has resulted in the near failure of the Second Money Laundering Directive which would have been something very rare in European Community law and finally a compromise was agreed at a very late stage of the conciliation process and the big issue there essentially is, where is the line between the lawyer representing the client in legal proceedings and the lawyer giving merely financial advice to the client? The Directive, as we see in the Third Money Laundering Directive, tried to reach a compromise saying that lawyers are subject to reporting requirements for money laundering purposes. They are exempt from these requirements, as you mentioned in your question, when they are asserting the legal position for their client and so on and so forth. What is interesting in this wording is that the lawyer is not exempt when he or she is giving legal advice and it is a very careful compromise that the Directive does not exempt the provision of legal advice to the client from the reporting duties. There is a recital in the Third Money Laundering Directive, Recital 20, which says that legal advice is protected unless this means that money laundering occurs. So, there is a very thin line between what we mean by "legal advice" and where does a financial transaction end and where does involvement in legal proceedings begin? So, where does the right to a fair trial kick in because this has been the main objection to the extension of the scope of the Directives to lawyers? Perhaps pre-empting your question, the question is dealt with by the European Court of Justice which has said that the scheme, the compromise, as was agreed during the Second Money Laundering Directive was compatible with Article 6 of the European Convention of Human Rights and the Court took exactly this view. I think that the policy reasoning behind this is that when a lawyer merely acts as a financial intermediary for somebody without really legal proceedings being involved, then they should be subject to the reporting requirement of anti-money laundering law. Lawyers are not happy with it as you mentioned in your question but so far I am not aware of any major cases in courts where we have major problems with this provision thus far. Admittedly, this will mean that the legal profession incurs, as have the banks with regulatory duties, so they have to establish their own mechanism of reporting suspicions. The Directive as a means of compromise also gives Member States the leeway to ask that the lawyers do not report to the normal FIU but they report for example to the Bar Association or to the Law Society, but the Third Money Laundering Directive specifically states in Article 23 that if you report to a self-regulatory body, you must make sure that the information goes to it unfiltered. So, they do not really want law societies to filter too much of the information they get from lawyers.

Q350 Lord Avebury: There does seem to be a very fine line, as you say, between having an obligation to report when you are giving legal advice but not when you are ascertaining the legal position of a crime. I cannot imagine how they make this distinction, but is fundamentally what you are saying that the representative organisations of lawyers were broadly satisfied with the exemptions in Article 20 of the Third Directive?

Dr Mitsilegas: I would not say that they were satisfied. I think that this was an outcome that was achieved after a great deal of effort and I remember that when the Second Money Laundering Directive was on the brink of collapse, 9/11 happened, and then I think that the Council put some pressure on the European Parliament which was heavily lobbied by legal organisations to reach some sort of compromise and still we hear quite a lot of scepticism by lawyers about them having to incur these obligations. So, perhaps this is still a live issue with them. However, we have not really seen any case law thus far that many cases which perhaps cause that many problems with regard to the operation of this obligation in practice.

Q351 Lord Avebury: I had a look on the European Court of Justice website yesterday to see if I could find any cases concerning breaches of confidentiality and I found some that occurred in other contexts such as commercial confidentiality, but you are saying that there have not been any cases before the ECJ which dealt with the question of professional legal confidentiality but, if there have been any, either during the currency of the Second Directive or since the Third Directive came into operation, could you give us the references and how would you summarise the position assuming that the cases are still relevant since the Third Directive?

Dr Mitsilegas: These are two different things. I thought that your question referred to cases arising from the position of lawyers reporting the requirements under anti-money laundering law and, in this context, there has been one case which has been brought forward by the Belgian Bar back in 2007 and, in that case, the Court of Justice said that the wording of the then Second Money Laundering Directive was adequate to satisfy the requirements of a fair trial of the ECHR and, if you read carefully the Court's judgment, the Court there takes the view that although the EU respects fundamental rights and fundamental rights are central to the EU's constitution if you like, the balance struck by the Directive itself was adequate to make it compatible with ECHR and the key is the compromise that the exemption applies when the lawyer ascertains the legal position of the client, but the Court recognised in its judgment that cases where the lawyer merely undertakes financial transactions for the client should not fall under Article 6 of the European

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Convention of Human Rights in this context. So, the lawyers should have some reporting duties because there are public interest considerations at stake. This has been the only case as far as I know where the Court of Justice dealt specifically with the Anti-Money Laundering Directive. As you said in your question, there have been prior cases where the court has dealt with legal professional privilege in the context of mainly EC competition law and EC regulatory law, but these have their own specific context. It has to do with specific aspects of legal privilege such as access to documents and so on and so forth.

Q352 Lord Avebury: However, none of the cases that you know of, the Belgian Bar case for example, has arisen since the coming into force of Article 20 of the Third Directive.

Dr Mitsilegas: Not as far as I am aware. I have not seen any litigation in this context.

Q353 Lord Avebury: Could you also tell us what the practice of law in England and Wales had been before and after Article 20 of the Third Directive came into force and, in your opinion, is the system now operating in a satisfactory manner?

Professor Alldrige: The position of lawyers in England and Wales was extremely difficult until the decision in 2005 and, since then—

Q354 Lord Avebury: Can you give us the reference?

Professor Alldrige: I have it here somewhere. May I give it at the end of my evidence?¹

Q355 Lord Avebury: Yes.

Professor Alldrige: The point there being that, until 2005, the word “arrangement” in section 328 was read so widely that many activities of lawyers not only were not privileged and needed to be reported but were actually criminal on a wide reading of the previous case which was called *P v P*.² Certain legal services have now been brought within the regulated sector for the purpose of the Proceeds of Crime Act, and that means that reporting obligations apply subject to the operation of legal professional privilege which in England and Wales means litigation privilege or legal advice privilege. Is the privilege which has been recognised in England and Wales identical to that which was recognised by the ECJ and the Belgian Bar case? No, it is not quite and this is an area for, it seems to me, some sort of harmonisation. For example, in-house lawyers are covered by privilege in England and Wales. They are not covered under the Belgian Bar case. There may be some differences in the provision of evidence by third parties. Some third party evidence might be

privileged under section 330(11) which again is not covered by the Belgian Bar case and there are some rules that work the other way as well. Is this a case where there should be consistency? It seems to me that the answer is “yes”. Do the legal profession in England and Wales mind as much as they said they were going to mind being subject to reporting requirements in those areas where they are so subject? No. They have buckled to; they have done it.

Q356 Baroness Garden of Frognal: In the Third Anti-Money Laundering Directive, there are several provisions which enable reliance to be placed in certain situations on the money laundering/counter-terrorism systems of equivalent third countries. The Committee has received evidence that this concept is of limited utility and practice. For instance, the Law Society which stated that the list is voluntary, non-binding and does not have the force of law. Is it limited utility because of the way it is treated in the Directive or does it flow from the manner of its domestic implementation in the UK?

Dr Mitsilegas: I will begin and perhaps Peter can follow. I make a comment on the Directive which is that it is true that the structure and wording of the Directive in this regard of the equivalence is highly complex. You will find provisions on equivalence throughout the text and, in a number of the provisions, it is very difficult to systematise. That is one aspect of the issue. The other aspect is that when you go to Article 40 of the Directive which talks about equivalence, paragraph four talks about the Commission’s possibility to find that the third country does not meet the standards to render it equivalent or to render the system equivalent. It is not really clear from that exactly what the powers of the Commission and the Member States are in this context. Paragraph four of Article 40 seems to imply that under a Comitology procedure, the Commission will find that the third country does not meet the equivalence requirements and this is within the committee where Member States do participate. This seems to imply that the actual positive designation of the country as equivalent is a matter for Member States. The practice has shown that Member States under this Committee established by the Directive have agreed that they missed off countries whose systems are deemed to be equivalent. Member States did this at EU level and there is a grey area whether this list which has been agreed within the auspices of the committee on the prevention of money laundering and terrorist financing established by Article 41 of the Directive is actually binding on Member States or not. Presumably this is an EU-wide list which is translated into Member States, but there is nothing in my view perhaps prohibiting Member States from adding further countries to their list if they want to. I think that the issue with

¹ *Bowman v Fels* [2005] EWCA Civ 226

² *P v P* [2003] EWHC 2260 (Fam).

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equivalence is another compromise in the Third Money Laundering Directive. I would link equivalence a lot to the risk-based approach, although this is another unclear concept in my view. The fact that you want to facilitate and streamline the regulatory issues, your customer reporting and so on, on the basis of a risk-based approach, if you did not have a Member State's system which is equivalent to the word of the FATF, then you facilitate those who are called upon to apply the Directive. On the other hand, the problem is that it might be in practice and let us take the UK example, even if a Member State is within the category of equivalence, the private sector still is under the obligation to report the suspicious transactions on a risk-based approach and, in the UK, there is a criminal sanction for non-reporting. I think an area to look at is to what extent the equivalence context actually facilitates the regulatory systems in Member States.

Q357 Baroness Garden of Frognal: Are you able to give us any example of where it has been of help to have this equivalence list?

Dr Mitsilegas: I am not an expert on the domestic law and perhaps Peter can help you on that.

Q358 Lord Faulkner of Worcester: I would like to ask whether our witnesses agree with the view that has been expressed to us by the Institute of Chartered Accountants for example that the private sector in the United Kingdom is placed at a disadvantage compared with other Member States because of the way in which the Third Anti-Money Laundering Directive has been implemented. Are we gold-plating it compared with other countries?

Professor Alldrige: I do agree and there are a number of reasons for this. The starting point is that the threshold for liability for the headline offences, the 327 to 329 headline offences under the Proceeds of Crime Act is much lower than is required by the Directive. In English law, we define the offences as typically being committed by people who know or suspect and the Directive defines money laundering in terms of knowing intentionally and wilfully. So, you commit the offence if it is done with suspicion and then the reporting requirements and in particular the offence of failing to report—and we do not have to have a criminal offence of failing to report, many other jurisdictions deal with it otherwise—is then triggered by the lower threshold. So, if the threshold is lower, there is just more stuff to report and the obligation upon the professions or anyone else who falls within the regulated sector becomes commensurately greater.

Q359 Lord Faulkner of Worcester: What can we do about it?

Professor Alldrige: What you could do about it is change the threshold for liability.

Q360 Lord Avebury: Do you happen to know how many individual prosecutions there have been proposed to report?

Professor Alldrige: No, I do not.

Q361 Lord Avebury: You say that the threshold is much lower but in practice that might not make an enormous difference.

Professor Alldrige: It may not make a difference to the number of prosecutions but it will make a difference to the behaviour of the person who is placed in that position, the money laundering reporting office or the designated person or whatever it was.

Q362 Lord Avebury: Not if he does not think there is very serious likelihood that he is going to be prosecuted.

Professor Alldrige: They do think that. They will always tell them if you speak to them, “Oh, you know, we are facing the prospect of so many years in prison”. They love talking about it!

Q363 Lord Hannay of Chiswick: Following this up if I may, is what you are saying that the British implementation of the Third Money Laundering Directive could have chosen a higher threshold and been fully compatible with the Money Laundering Directive?

Professor Alldrige: Yes.

Q364 Lord Hannay of Chiswick: Are you saying this as a fact or as an opinion?

Professor Alldrige: I suppose that it is a legal opinion.

Q365 Lord Hannay of Chiswick: Are you saying that you are certain that a case could not have been brought by the Commission if the level—

Professor Alldrige: I would be—

Dr Mitsilegas: Can I add to that? Article 39 of the Third Anti-Money Laundering Directive says under “Penalties”: “1. Member States shall ensure that natural and legal persons covered by this Directive can be held liable for infringements of the national provisions adopted pursuant to this Directive. The penalties must be effective, proportionate and dissuasive. 2. Without prejudice to the right of Member States to impose criminal penalties, Member States shall ensure, in conformity with their national law, that the appropriate administrative measures can be taken or administrative sanction can be imposed against . . . ” banks and so on which means that we do not have to criminalise failure to report or tipping off.

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Q366 Lord Hannay of Chiswick: Have you any idea whether the decision by the Government here to put this lower threshold was a decision taken in the interests of the UK because they believed that it was in our interests to have a lower one than was required by the Third Directive or was it just a piece of bureaucratic excess?

Professor Alldrige: It was put in place before the Third Directive.

Q367 Lord Hannay of Chiswick: So, it cannot be called gold-plating at all.

Dr Mitsilegas: It can because a similar provision was done in the 1991 Directive.

Professor Alldrige: This is something that runs through.

Q368 Lord Hannay of Chiswick: But you do not have an opinion as to whether the choice by the Government of the day was made because they believed it was in Britain's national interest to have that lower level or whether it was just a piece of bureaucratic excess?

Professor Alldrige: Certainly neither of those views was expressed in the papers at the time. There is a tendency in the UK to use criminal law where other jurisdictions do not necessarily do that.

Q369 Lord Marlesford: Another aspect that I recollect is that there are criminal sanctions against those who are reporting, making an SAR, if they in any way reveal the person about whom they are making it the fact that they are making it. Is that something that is fully required by the Directive or is that just a British adjunct?

Professor Alldrige: I cannot remember checking the Directive. You are quite right that the provisions which were called the tipping-off provisions and which have been altered in some respects in 2007 are important. I cannot imagine a jurisdiction surviving without some kind of prohibition upon tipping off, whether that was done by criminal means or not, I do not know. I will check the provision in the Directive.

Q370 Chairman: You will let us know?

Professor Alldrige: Yes.³

Q371 Lord Hodgson of Astley Abbots: Following on from these two points, are you saying therefore that the earlier drafting of the Proceeds of Crime Act, sections 327 to 329, had as an unintended consequence a problem as soon as the Third Anti-Money Laundering Directive came in?

Professor Alldrige: No. What I am saying is the standard was always lower. This does not really depend upon the Third Directive; the argument

would have been the same under the First or the Second. The UK defines money laundering more widely than is required by any EU Directive, the First, the Second or the Third, and the necessary inference from that will be that the obligations upon those challenged with reporting in England and Wales are going to be greater than in those jurisdictions where minimal compliance is deployed.

Q372 Lord Richard: Are you saying therefore that the British could actually change the law in the direction you would wish it to be changed without fear of infringing the EU?

Professor Alldrige: Yes.

Q373 Lord Richard: The Commission issued a communication in November of last year which I think was entitled *Proceeds of Organised Crime: Ensuring that 'crime does not pay'* and, in the course of it, they called for increased use of confiscation procedures, they said, given the relatively limited sums presently recovered from organised crime. To what extent do you think the placing of EU co-operation in this area on a mutual recognition basis held out the prospect for improvement and presumably that means for getting more money from that which is presently recovered from organised crime? Do you think that it is an effective way of dealing with it or be written in other ways?

Dr Mitsilegas: To answer this question, my answer will have two parts. One is the theory of mutual recognition and the second is the practice of mutual recognition in criminal law. As you may know, the principle of mutual recognition in criminal matters means that a charge in one Member State or a common authority must recognise and execute the decision by a judge in another Member State on the basis of mutual trust with a minimum of formality and with speed, and some of you may remember that this principle was introduced in the criminal law partly under the initiative of the United Kingdom's 1998 presidency of the European Union as an affirmative to harmonisation or to uniform criminal law. The examples that we have so far on mutual recognition have been the European evidence warrant which is perhaps the only instrument which has been fully implemented in Member States and then a number of mutual recognition instruments dealing with issues such as freezing orders, confiscation and financial penalties and most recently we have seen the formal adoption of the European evidence warrant. The practice that has been conducted on how this principle actually works in the field; there has been a major study funded by the European Commission which was published in Autumn 2008 which demonstrates that, with the exception of the European evidence warrant, the other mutual recognition instruments have not really

³ Professor Alldrige subsequently confirmed that there was no such provision in the Directive.

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been implemented in Member States. So, although in theory you can see the appeal that for example introduction of confiscation orders may be a way forward, in practice you may find that there are many difficulties with that. It was found first of all that the mutual recognition instruments are not found to be very user friendly by practitioners including judges. The example of freezing orders was used whereby a lot of judges would prefer to use the existing mutual legal assistance arrangements rather than this new instrument. A confiscation in my view poses particular challenges because of the wide variety of the national assistance across the EU. There is a framework decision aiming to approximate confiscation rules which accompany the mutual recognition instrument. However, in my view and I think this has come across to other members of the Committee in particular from Mike Kennedy, what may be perfectly normal under the Proceeds of Crime Act in the UK may be unconstitutional in a number of other EU Member States. So, this is a very significant barrier to the operation of mutual recognition on the basis of mutual trust. How can, for example, a German judge recognise almost blindly an order for confiscation coming from a judge or a court in the United Kingdom given the much broader legislative framework in UK law in the criminal lifestyle provisions and so on and so forth? In principle and perhaps in theory, this may provide the solution but I think practice demonstrates that perhaps we have quite a long way to go towards an efficient system in this context.

Q374 Lord Richard: If that does not work, what should we do?

Dr Mitsilegas: I think with confiscation there must be discussion about approximating national law and national practice. Confiscation is very much linked to the right to property and it has constitutional implications. I do not think that you can explain much of this system if you do not have at least a common understanding of the concept and I note that the Commission's communication that you mentioned is very ambitious in this context. One of the 'to do' things for the future is to discuss confiscation and safe recovery, but I think that it is a highly complex area of law.

Q375 Lord Richard: To get a common understanding and quasi harmonisation . . .

Dr Mitsilegas: Or at least a minimum harmonisation. It does not have to be uniform or fully harmonised, but perhaps a minimum harmonisation of what can be confiscated.

Q376 Baroness Garden of Frognal: I think that you have answered the question I was about to ask on mutual legal assistance but perhaps you could clarify

the prospects for further progress. Do I take it from your previous answer that you are not particularly optimistic about further progress?

Dr Mitsilegas: I do not want to sound too pessimistic. I will mention the example of the European evidence warrant which is perhaps the mutual recognition instrument which is most aiming towards mutual legal assistance. This was published after Member States had waited in vain for the Lisbon Treaty to be ratified and it was finally formally adopted in late 2008, so Member States have had a number of months now to implement it. Even EU officials will tell you that this instrument has been a failure even before its implementation and this is because its scope is too narrow and it is highly complex and the exchange of evidence across the EU and also standards upon constitutional principles in Member States, for example can a Member State require evidence from another Member State which it cannot obtain under its own domestic legal system? These are questions which mutual recognition brings about and even at EU institutional level, there is a feeling that this instrument is way too complex with way too many caveats and exceptions to work properly. There is also the feedback from practitioners that we have just learned the new mutual legal assistance requirements and we can call each other and use them and even if it is not at the speed that we would all wish, we can get some results from that. So, perhaps here it could be, let us see how the mutual assistance arrangements work before we embark on a more ambitious mutual recognition programme in this context.

Q377 Lord Faulkner of Worcester: What about arrangements with non-EU Member States? Has the EU made a lot of progress in drawing these up? Does the agreement with the United States on mutual legal assistance of 2003 establish any sort of precedent?

Dr Mitsilegas: I was working with the EU Committee at the time of scrutiny of the EU-USA Agreements in 2003 and it is interesting to see when I had to do some research on these agreements that these are not yet in force because these are conventions which also have to be ratified by EU Member States in accordance with their domestic constitutional requirements. Two Member States have not ratified them yet, so they are not yet in force. The agreements between the EU and the US mutual legal assistance provide for a wide range of information to be exchanged between the EU and the US. We will see how this will operate. In my view, the interesting dimension of these agreements is the extent to which EU-US co-operation will have an impact on bilateral co-operation between EU Member States and the United States, that is would the EU standards limit the freedom of Member States to co-operate with the United States?

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Q378 Lord Faulkner of Worcester: What about other countries outside the EU?

Dr Mitsilegas: There have not really been formal agreements between the EU and third countries specifically on mutual legal assistance as far as I know. Eurojust has been concluding a number of agreements with third countries. The majority of these countries are countries which are EU neighbours or candidate countries, so countries which may become EU Member States.

Q379 Lord Hannay of Chiswick: To what extent, if any, does the current institutional architecture of the EU impede effective action in the AML/CFT area? Would the situation be changed very radically by the entry into force of the Lisbon Treaty?

Dr Mitsilegas: This field is a prime example, in my view, of cross-pillar law. It involves all three pillars; it involves the first pillar directive, second pillar based on foreign policy, and the third pillar which is criminal law. What we can see is that there are issues with the way in which instruments adopted under the different pillars interact with each other and the example I would bring is the legal regulation of financial independence in the EU. We have a third pillar decision which was adopted in 2000 and then we have provisions on FIUs in the Third Money Laundering Directive which is a first pillar instrument and both these instruments seem to be in force. Of course, there are differences in the way you can enforce the law according to the three pillars. One of the fields the Member States wanted to guard in the field of criminal law is that the Commission does not have infringement proceedings if a Member State does not implement the third pillar properly, but the Commission does have infringement proceedings with regard to the first pillar and I am sure that the Committee has heard that the Commission has recently instituted proceedings against a number of Member States for not implementing the Third Money Laundering Directive. So, there are gaps and there are perhaps at times inconsistencies between the pillars. The Lisbon Treaty will in theory abolish the pillars. It will retain specific provisions for foreign policy. It has introduced specific provisions on the issue of sanctions, so specific legal bases on that in order that we will see how this will operate. However, what it has not addressed in my view is the issue of the proliferation of EU bodies and agencies dealing with this. It is not only about money laundering but it is also about criminal law in general. At present, we have Eurojust, Europol, Olaf and to some extent perhaps SitCen, which is a second pillar body, dealing with issues of terrorism, terrorist finance and so on, and perhaps we need to streamline these bodies in the future. This is not something that the abolition of the pillars will necessarily bring about.

Q380 Lord Hannay of Chiswick: The abolition of the pillars will presumably make somewhat less complex the handling of future legislation in this field, the methods of putting it forward, the methods of deciding it in the Council and so on become somewhat less complex and fractured, I suppose?

Dr Mitsilegas: Absolutely. You could have one instrument covering a number of aspects of money laundering.

Q381 Lord Marlesford: May I ask you about the Hawala system and alternative remittance systems. Do they pose particular problems for the administration for the whole of this regime?

Professor Alldridge: I do not think that they pose any significant as it were legal problems in principle because the dealer is under an obligation to register and they fall within the regulated sector and they have a reporting requirement and so on. The question is, is there an enforcement problem and that is, do we suspect that there is a great deal more of this activity going on than is evident and is reported? There is literature on this. Literatures which speculate about unreported crime are notoriously unreliable, so you will get a range of guesses as to how much money is involved. As between them, there is really a choice for the reader. Would it matter if a great deal of money is being transferred by Hawala that is the proceeds of crime? The answer is, yes, but not for the reasons in the first recital to the Third Directive. Yes because then it is more difficult to confiscate it.

Q382 Lord Hannay of Chiswick: The answer you gave there was, I take it, purely in terms of the United Kingdom because, when we were in Brussels last week, it was very clear that they have no evidence whatsoever that any Member State other than the UK regulates Hawala transactions and in fact they were remarkably unsighted about the whole issue of Hawala in Brussels, whether it was a good thing or bad thing, whether it was contrary or liable to be contrary to the Third Directive or not. You answered in a fairly reassuring way the first part of the question, but I presume that you were only answering it in terms of the UK.

Professor Alldridge: Yes.

Q383 Lord Marlesford: I would like to move on to my next point. Would each of you give your view of the major challenges which presently face European and international efforts to combat money laundering and the financing of terrorism.

Dr Mitsilegas: I will mention one pragmatic point in that and, in my view, we have had a plethora of initiatives, recommendations and legal instruments both at international level and at EU level. It is indicative that the Third Money Laundering Directive was adopted only a very few years after the

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expiry of the implementation of the Second Money Laundering Directive. What I would ask is that we give the standards room to breathe, look at how they are implemented in EU Member States and beyond, and base any further reform on the lessons that you get from the implementation of the standards. We have quite a lot of anti-money laundering law which is very sophisticated and at times not entirely clear and the examples of equivalence and risk-based approach and the position of the lawyers are all issues which are in need of further clarification and maybe the practice will show the solution to these issues, so let us wait and look at implementation before we have yet another round of FATF or EU standards in the thing.

Professor Alldrige: I think that there are two wrong turnings that we have gone down. At least anti-money laundering is directed against people who are engaged in acquisitive crime and who want to enjoy the proceeds of their crime. Counter-terrorism financing does not seem to me to be an area of inquiry which is likely to yield very much fruit simply because terrorism is relatively cheap, it can be very cheap indeed, it does not require very much money and because the people involved are frequently not doing it for profit. I think that resources on counter-terrorism are probably better directed in the traditional areas of surveillance and infiltration and so on than against counter-terrorism. The second wrong turning maybe is that I think we emphasise too much the crime of money laundering. We managed to get on until 1990 without money laundering being a crime. Now it has been characterised as a very important crime and it has become increasingly popular with prosecutors in this country and now what 20 years ago would have been charged routinely as handling stolen goods is charged as money laundering and many offences which would not be charged as having any kind of successor offence are charged with a money laundering successor. Let us get away from the idea of the crime of money laundering and let us concentrate on the proceeds of crime and pursue the proceeds of crime.

Q384 Lord Marlesford: Is part of the problem perhaps that money laundering is almost a sort of journalistic phrase which is not easy to translate into law and does not appear from our inquiries so far to have been very precisely translated anyway?

Professor Alldrige: Yes and there is a problem about double punishment. The UK allows primary legislation to be charged with laundering the proceeds of their own crime which seems to me to lead to a problem either of double punishment or of redundancy somehow, if I have committed an offence, I have proceeds and I cannot think of anything I can do lawfully with them, so just prosecute and punish for the original offence. A very

obvious example is the Darwins. Do you remember the couple who faked the disappearance of the husband, bought the flat in Panama and ended up being charged with various frauds and money laundering and, in a sense, they fell within the definition? Thirty years ago, John Stonehouse was just charged with fraud. It does not make that much difference. Let us just concentrate on the original offence.

Q385 Lord Hannay of Chiswick: I would like to follow up on your answer about anti-terrorist finance. Was I right in thinking that your argument that it is not a very useful employment of resources is based on the assumption that there is a finite amount of resources to be devoted to counter-terrorism and that they would be better devoted to infiltrating Islamic groups or whatever it is and not following up money laundering?

Professor Alldrige: Yes.

Q386 Lord Hannay of Chiswick: I think that that is an incorrect premise because I do not think that there is a finite amount. I do not imagine that the US Government would have said that there was a finite amount it was prepared to spend to prevent another 9/11. The second point is this. You are obviously correct when you say that the sums of money are often quite small. The evidence that was amassed by the 9/11 Commission demonstrated what an extraordinarily cheap operation it basically was. On the other hand, the action of moving that money around was one of the few really visible actionable things that existed both before and after the crime had been committed. Is that not a rather relevant consideration too?

Professor Alldrige: It is evidence in respect of the actual offences but to call it a new offence seems to me to be wrong. In every case of terrorism financing where there already is a predicate offence, then AML will operate anyway. So, if it is raising money for the purposes of terrorism, that is an offence under the Terrorism Act, so that will be covered by AML. If it is extortion or if it is drug dealing which typically are ways in which terrorist organisations have raised money, again you do not need a special provision. The one case where the counter-terrorist financing legislation applies and nothing else is the case where somebody has money in an account or has property and they decide—and you have nothing more than the decision—to deploy it for terrorist means. I am not sure that we ought to be directing resources at that. You say of course that the US Government would not admit that the resources are finite. Of course, they would not say it but the resources are finite.

Lord Hannay of Chiswick: Not really.

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Q387 Lord Faulkner of Worcester: Unless he is making his own bomb, you could do him for conspiracy anyway.

Professor Alldrige: Yes.

Chairman: There are no more questions that the Committee wish to ask. May I say to you both that you have been most interesting witnesses. Thank you very much indeed for coming and I again apologise

that we kept you waiting for so long before we began. I think that you have helped us enormously in answering our questions and we are very grateful. We are hoping to produce a report before Parliament rises for its summer recess. We have three more witness sessions and then we shall be putting together our report. We have had a very successful morning thanks to you both. Thank you.

WEDNESDAY 22 APRIL 2009

Present	Avebury, L. Faulkner of Worcester, L. Garden of Frognal, B. Hannay of Chiswick, L. Henig, B.	Hodgson of Astley Abbots, L. Jopling, L. (Chairman) Marlesford, L. Mawson, L. Richard, L.
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Examination of Witness

Witness: SIR JAMES SASSOON, former President of the Financial Action Task Force, examined.

Q388 Chairman: Sir James, welcome. We much appreciate your coming. The Committee has received a document which is a report on money laundering by the Financial Action Task Force Secretariat. They were not content to come and talk to us and we perhaps might ask you more questions about that. We are delighted that you were able to come. Maybe you would like to introduce yourself, but at the same time, if I could link that with the first question with regard to this inquiry, if you could tell us what in your experiences are the main strengths and weaknesses of FATF.

Sir James Sassoon: My name is James Sassoon. I acted as President of the Financial Action Task Force, the FATF, for the 12 months up to June 2008. As you probably know, the presidency rotates on an annual basis and I should hasten to add that I came at this as a non-expert on money laundering and terrorist financing issues. On the strengths and weaknesses of the FATF, let me take three strengths first and then pick out three areas of weakness. First, on the strengths, I think it is remarkable that through an entirely consensus-driven process of standard setting this body has developed a set of 40 plus nine recommendations that have global acceptance and endorsement. Second, linked to that, I think it is a huge strength of the organisation that while it has 34 members, actual full members of the organisation, there are over 180 countries now committed to the FATF recommendations through membership of either the FATF or of the so-called FATF Style Regional Bodies, of which MONEYVAL is one. There are very few countries in the world now that are not at least in principle and by voluntary buy-in to the process committed to the adoption of the full 40 plus nine recommendations. The third strength of the organisation, which I think is unique, is the peer review process which countries, in my experience, take enormously seriously and is a key driver in ensuring that the recommendations are implemented and countries continue to work to implement the standards better as the rounds of evaluation carry on. As I am sure you know, we are ending the third round of evaluations by the FATF within the next two years. On the weaknesses, one of the things that

struck me when I started to get involved in the work of FATF was that it is the area of financial services policymaking where the policymaking was least rooted in hard evidence. We may talk about this a bit later, about some of the measures that the UK under its presidency proposed to try and get the FATF to give more consideration to measuring the outcomes over time of its recommendations and the costs that the recommendations entail. This is a very, very difficult area but I do think it is a major weakness. Second, I think that the organisation, having started as a task force with broad principles, is getting dragged down to a degree of detailed interpretation and guidance, and methodology for the evaluations which now need to be questioned quite hard. There is a danger of a one-size-fits-all approach to the adoption of the recommendations. For example, there are always debates about how you apply the recommendations very differently in civil law and common law jurisdictions and there is a danger that this gets significantly in the way of the substance of what the FATF is trying to achieve. Third, and again linked to that, I would say that there is a danger and a risk that the assessments are getting too much focused on inputs and legal frameworks and forms and not enough on the effectiveness that is the ultimate objective.

Q389 Lord Marlesford: Following that up, Sir James, one of the impressions that some of us, or at least I had from our interrogation of SOCA about their SARs database is that they do not discriminate between what is important and serious and the trivial and I think there is a danger of them having a huge amount of data, much of which is really irrelevant to anything that could be called serious crime, money laundering or terrorism. Is this at all a problem with the FATF?

Sir James Sassoon: I cannot comment on the specifics of SOCA. I do think that it raises a very important general point on which I would hope that over time the FATF could shed some useful light, which is that as there is more global evidence developing of the way that suspicious transactions are reported and the actions that are taken on them, we can learn some

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real lessons by looking across, if not all countries, cross-sections of countries. I would be very keen for the FATF to be promoting much more research in this area. It is something that the revised mandate of the FATF, which was endorsed by ministers during the UK's Presidency year, now places on the table and I think the FATF can help to shed light on what is coming out of this activity, not just in the UK but globally.

Q390 Lord Richard: Sir James, I wonder if I could put to you some of the evidence we have actually been given and perhaps ask for your comments on it. We heard evidence from Professor Alldridge, who is the professor at Queen Mary looking at this, and what he said was: "FATF, in my view, needs a constitution. It was established in 1989 as an offshoot of the G7. It has operated on essentially an ad hoc basis for the last 20 years and a temporary basis for the last 20 years. Its decision-making, its policymaking and its information-seeking practices are by no means clear. I spent some time looking at their website yesterday and asking myself questions like, how exactly do you get to be a member of the FATF, how does it function, how does it make the rules and how does it come up with its recommendations? These matters are not as clear as they should be". I was wondering, do you share that view that they are not as clear as they should be?

Sir James Sassoon: No, I think they are not as clear.

Q391 Lord Richard: Can I just put the second half of the question. If you did share that view do you think it has an effect upon the efficiency of the organisation?

Sir James Sassoon: I read the transcript of that evidence with some interest because it does not bear much resemblance to anything that I recognise. Just to take, in a sense, a trivial point, I double-checked that if you go to the FATF website there is a very clear set of rules for membership which is entirely publicly disclosed. I do not know whether there was some difficulty accessing the website, but even on some of the specific detail I would challenge that evidence. More broadly, the FATF is a very interesting entity. You have much more experience of comparative accountability and transparency of other international bodies, but it did strike me, when I first came at it, as a rather extraordinary entity in a way. When you look at the elements of accountability, there is a mandate which is set for eight years by the ministers of the member countries, that is reviewed at midway through the eight year term, so the mandate is re-looked at every four years, that ministers meet—we convened under our presidency a meeting of ministers in Washington around the fringes of the spring 2008 IMF and World Bank meetings; we got a very high attendance of ministers with a short,

focused, very good discussion about two or three of the key issues, including accountability, private sector engagement and so on; it was a good discussion—and there are annual reports to ministers. So in terms of the accountability, there is a high degree of it. In terms of how decisions are taken within the organisation, there was an implication in the evidence you have had that there is a sort of small black box which is the FATF, out of which recommendations come and then they are uncritically adopted by the EU and other people—and it is all very unsatisfactory. It is perhaps worth saying that as well as the 34 members of the organisation there are associate members, including the regional bodies, one of whom is MONEYVAL, who make very positive and important contributions to all the discussions, and there are some 20 other organisations who attend and speak at the meetings, including the IMF, the World Bank and the relevant agency of the United Nations, and other groupings of international regulators. I have to say as somebody who has chaired three day long plenary sessions where all the decisions have to be made by consensus, when you have 65 organisations and around 120 people in the room, I find this is a somewhat different picture than I have from the one Professor Alldridge gives. Having said that, I do think there are one or two areas in which the FATF could usefully improve its accountability. I think it is very striking that the FATF is the only global standard setting body that is not a full member of the Financial Stability Forum, which will become the Financial Stability Board. Having pushed for membership, I could understand why the Financial Stability Forum was initially unwilling to open up its membership because there were lots of other countries who were pressing to be members. But when the G20 very significantly increased the membership of the Financial Stability Forum at the recent London meeting it seemed to me a missed opportunity for the FATF to have been put on to the Financial Stability Forum because that would create another layer of useful oversight and a sense check on the FATF's processes. That is one area for improvement. The other one is the question of how willing the FATF is to take forward membership applications, quite independent of what the rules say about the membership criteria. The FATF's stance on whether or not it is truly open to increasing its membership over time is something which is perhaps not as clear to non-members as it could be.

Q392 Lord Richard: What is it that not is clear, what you have to do to become a member or qualifications to become a member?

Sir James Sassoon: The technical criteria are laid out with great clarity, but alongside the technical criteria that need to be met there is a question, that I suppose many clubs have as to what is the appropriate total

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size of membership should be; on the one hand to make sure that this consensus-driven organisation is able to make decisions and it does not become too unwieldy; but, on the other hand, to make sure that its membership is sufficiently inclusive of a spread of countries which is reflective of where global financial activity is taking place. The membership of the FATF has evolved over time. China was admitted 18 months ago. It is by no means a closed door, but there are questions that an outsider might justifiably ask as to what the future membership approach of the FATF is going to be.

Q393 Lord Richard: You make it sound like the Garrick! Can you blackball a candidate? Are they blackballed?

Sir James Sassoon: Membership, like everything else, has to be dealt with on a consensus basis.

Q394 Lord Richard: If I can sum up your evidence it is really this: the FATF is sufficiently accountable, sufficiently transparent and the decision-making process is clear, sufficiently clear.

Sir James Sassoon: I have suggested one practical and important enhancement to that, which is through membership of the Financial Stability Forum.

Q395 Lord Hannay of Chiswick: If I could follow up and say how delighted I am that you gave such a masterly response to the Professor, with whom I disagreed strongly. He also said that what he thought would be the right way would be for all this to be turned into a legal international convention, which was the point I most strongly disagreed with because it seemed to me that in the negotiation of this in international legal form you would probably end up with a lot of gaps, let-outs and so on. Moreover, you would come across the problem of ratification by the US Senate, for example, which would probably be very difficult indeed, and therefore this was highly undesirable. Do you agree that is another reason why it is best left on the present basis?

Sir James Sassoon: I prefaced my last answer very carefully with saying that I, unlike several of you here, am not a great expert on this subject. Having said that, I entirely agree with your logic and I do think this interesting constitutional set-up of the FATF has served it well over the last 20 years.

Q396 Baroness Henig: One of the four essential objectives of the FATF under its current mandate is to engage with stakeholders and partners throughout the world. I wonder if you could tell us what was the nature and extent of the FATF's interaction with the private sector at the time you assumed office, and what improvements you were able to bring about? Secondly, what is the scope for extending and deepening that relationship in the future?

Sir James Sassoon: At the time we took over the presidency in 2007 I would say that the engagement with the private sector was patchy, it was not systematic and it was certainly not up to the standards that many of the individual countries would adopt when engaging with stakeholders to set financial services policy domestically. It was a bit of a surprise to me to discover that finance ministries when setting all sorts of domestic rules would engage with the private sector in a completely different way from the way they were content for the FATF to do it. Having said that, there was some engagement, it was not that there was no engagement, but there was very much a view that the FATF was a public sector group of people and we told the private sector down the chain what they had to do. The UK's predecessor holding the presidency was Canada and they actually helped through joint working with the UK to push this agenda forward and, indeed, the South Africans and other presidencies before had all picked this up but had found it very difficult to get any traction. Maybe we came in at the right time, but we certainly made it a priority and we did make some very significant progress. We set up a standing consultative forum through which the private sector can now input ideas for the work plan and the agendas of the FATF and its working groups and through which we can give the private sector more consistent feedback on the work of the FATF. For the first time, and this was perhaps the thing that was most surprising to me, we did joint work on typologies. These are the case study exercises on particular areas of fraud or terrorist financing. We had a very effective, and much appreciated by the private sector, series of workshops in London in December 2007 to look at big areas like VAT carousel fraud, proliferation financing—four or five issues on which the private sector wanted to really understand how the public authorities were coming to them. So we kicked off typology work with the private sector and there is now an agreement that all future typology work that the FATF does will be run past the private sector. We also involved them in a series of streams of work to develop risk-based approaches to different sub-sectors. We initiated a lot of work and I have to say that the very good news is the Brazilians, who hold the presidency now, and the Netherlands that follow are equally committed to private sector engagement. I am optimistic but there is much more that needs to be done. In my answer to the first question I said that much more needs to be done on the whole evidence base that underpins the FATF's work, particularly with the private sector as we put ever more reliance on them to be the frontline in the battle against money laundering and terrorist financing; and we do have to explore with them in much more detail what the cost burden is that the public authorities are putting on them and what the

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results are that are coming out. 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. There are various other important issues that are on the work programme for the coming year, such as the reliance the private sector can place on know your customer due diligence processes that have been carried out by other financial institutions; and I could go on. So I think there is an awful lot more work to be done.

Q397 Baroness Henig: So you are quite optimistic then that this very important relationship is deepening?

Sir James Sassoon: I think it will require committed presidencies who regard this as an important component of the FATF's work because it is discretionary around the core work, which is driving the standards forward in the FATF plenaries. I am optimistic but it is not going to happen unless it is very consciously pushed.

Q398 Baroness Henig: So it is a leadership issue as much as anything in terms of who is driving the FATF's agenda?

Sir James Sassoon: Correct.

Q399 Lord Mawson: What do you regard as the major accomplishments of the 2007-08 UK Presidency of the FATF?

Sir James Sassoon: I have talked about the private sector so I will not repeat that one. That was one that was certainly central to our agenda. I have also talked about the question of the mandate of the FATF and the fact that we conducted the four year review of the mandate. We convened the meeting that I described, for ministers to have a proper discussion because there certainly had not been a ministerial meeting for four years and my sense was that in some of the previous ministerial meetings it had not always been the ministers themselves who attended. Actually getting the ministers to look at a refreshed mandate, which included some new elements, particularly the commitment of the FATF to produce a regular global threat assessment, something that they had not done before, and to get into the mandate references to measuring the impact of the regimes, those were the first two areas. The third thing which was a priority of ours and that we made progress on was helping low capacity countries with the implementation of the FATF recommendations. I think it is quite right that there should only be one set of recommendations that apply globally. We cannot say there is one set of recommendations for countries below a certain level of per capita income or something. On the other

hand, when I went to meetings of two of the African groupings of countries, if you had the justice minister of Sierra Leone, for example, around the table with his fellow ministers from countries which are struggling to be supportive members of the wider group of FATF members, they do need a lot of help. The fact that, under our presidency, we produced guidance for low capacity countries on the implementation of the standards was important to the UK. Two more things. The new approach that we rolled out for dealing with non-cooperative countries started to bear some fruit under our presidency and has borne more fruit in the succeeding nine months. The last thing I would highlight is the launch of the so-called Three Presidencies Paper which was the review that we decided should be kicked off to look at the FATF standards because, as we come towards the end of the Third Evaluation Round, we thought it was important and appropriate for the overall standards to be subject to a periodic review.

Chairman: We are coming to the Three Presidencies Paper in a moment.

Q400 Lord Mawson: This is all about how we make this more effective in the sense that a lot of this behaviour around money laundering is very entrepreneurial behaviour. I am following a particular case of a family that I am aware of that got caught in this because I am always interested in the micro, in what happens to one family in detail as it passes through. In terms of ministers and politicians, how much work have you done with them in terms of this detail about particular individual cases? I am aware that often people get caught in the systems and processes and they talk strategies and documents, they never look at the detail of one example. Entrepreneurs and business people know that the one micro sample is very critical in terms of really understanding what is happening in the system. You have said a bit about case studies with business, but how much of that has been done with politicians in terms of understanding the detail?

Sir James Sassoon: Not very much is the straight answer. What the FATF does is to take problem areas and subject them to case studies, so it has recently, for example, produced a very big piece on casinos and how they operate. And, to give another example, we launched an inquiry into football clubs and other sporting clubs and their exposure to money laundering issues and a report will be produced. There is therefore work focused on the detail which is informed by as many countries as want to participate in each of these studies. How that is then translated into ministerial involvement at the granular level is essentially left to the individual national authorities to brief their ministers as they see fit.

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Q401 Lord Mawson: It is my experience in terms of changes that if particular individual ministers never get hold of the granular detail, what often happens is very little actually changes, as you know, so I just worry about how we enable some of that more granular stuff. This is all about the detail of pretty entrepreneurial behaviour by individuals and groups and organisations and that understanding is not there.

Sir James Sassoon: I do think it has to be done at the national level but there is a huge misunderstanding about the linkages in the chain. One of the things that I use as an example of the granular that we all face and the link through to the FATF is around the frustrations about opening bank accounts. It may all be done for very good purposes but you go into the bank to open an account for a child who is asked for a utility bill when obviously they do not have one. And then the very well-meaning person across the counter in the bank will say “We have to do this because the FSA tells us we have to do it.” Who tells the FSA to do it? It is the Treasury or the Government. And it is the European Union who impose the rules on the UK Government. So who tells the European Union? And of course right back up the chain it is ultimately the FATF that determines the rules. I suspect that even among a lot of ministers in the member countries actually understanding this chain and why it is important to start driving the FATF in some of the ways that would ultimately effect the end of the chain with everyday transactions is something that all involved in the processes need to understand better.

Q402 Chairman: Can I just go back to the UK Presidency? You twice referred to the inhibitions caused by the consensus rule; how limiting is it and in practice is it particular countries who refuse to come into a consensus and are they ones who are reluctant to take on fully the responsibilities which FATF rules impose on them? How much easier would it be to make progress if it was in line with OSCE which, I think I am right in saying, is consensus minus two as I recall—I may be wrong on that. Would it make life much easier and would it be possible to change the rules so that it was easier to get agreement without 100 per cent consensus?

Sir James Sassoon: It is a question that I pondered on a lot as I had to grapple with getting decisions taken. Ultimately for the FATF consensus works very well. But the first thing I said to myself was “I am going to be taking the chair of this organisation; what do I do if somebody is holding out against a decision?” There was no piece of paper anybody could give me, and actually it turned out to be rather a good thing that there was no piece of paper, that said if one particularly large country objects you cannot overrule that one, or if two of this other category of countries object you would be unwise to do that but

if it is three or four of another group it is okay. I developed some informal lines which I thought I should not cross as chairman, but the ability of the Presidency, guided by the secretariat, to be able to sense the mood of the meeting without having strict rules about who we could not overrule worked well. Looking back on it, although it was enormously frustrating at the time, the ability of the organisation to take decisions that neither required unanimity nor where people could play games because there was a set rule that allowed, say, two members to hold out actually, on balance, worked pretty well. If one stands back from it, although a lot of the work does take a very long time to go through the various working groups and then through the plenary, the FATF has shown a very considerable flexibility to take on additional parts of its mandate, most notably the terrorist financing aspects. It has been flexible and pragmatic in its approach to non-co-operative territories, so on balance the impression I would like to leave you with is that the decision-making has worked well. To take your other point about does this reflect countries not being prepared to take on responsibility, I do not think that is right. When the consensus is struck I would say that it is very powerful because it is not that there is anybody who is formally seen to be holding out. The greater difficulty is that there are some issues that different groups of countries tend to coalesce on which are around, most aggravatingly from the perspective of countries like the UK, the approaches that FATF requires countries to take to enforce FATF recommendations. To give you an illustration, the UK was found by the FATF to be non-compliant on the recommendation referring to politically exposed persons. If you look at all the hard evidence the UK does as much if not more than any country to generate activity reports and for there to be clear evidence of follow-up on politically exposed persons. Because of the way the UK had those rules in place in 2007, which was through guidance which the FSA required regulated bodies to adopt, but was not in some formal law or regulation, one side of the FATF was able to ensure that the UK was rated non-compliant. When faced with that sort of issue in an evaluation—and it comes up in almost every evaluation and causes enormous frustration and waste of time—there will be, and everybody knows it, a group that will hold out against allowing countries to be sensibly evaluated in their ratings on an issue like that. So there are fault lines which the consensus approach has helped to foster which are well understood by the FATF members, but the way around it is not to change the voting rules but is actually to look back at the recommendations and see whether the recommendations are being either drawn up or enforced in a way that puts form over substance.

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Q403 Lord Avebury: Does what you said about the preferability of decision-making by consensus over having, for example, an OSCE-type rule, have a bearing on the willingness or otherwise of FATF that you talked about earlier to accept new members and would there have to be changes in the rules if you got much larger membership than you have now?

Sir James Sassoon: I cannot compare it with other organisations because I have not worked closely enough with enough other international organisations but my conclusion is that the consensus is working well with the limitations I have given for the FATF. I do not think that for the FATF now there is a better way of proceeding, but if the membership was significantly enlarged it is something the FATF would have to look at but I would not say it is a pressing issue for the FATF.

Q404 Lord Hannay of Chiswick: Is not the key criterion that none of the current members of FATF in your view, in your experience, were using the requirement for consensus abusively, i.e. to block something that the large majority of members believed should be done. Perhaps you could say whether or not you did have any experience of that and, if not, the answer is perhaps that is why consensus works quite well.

Sir James Sassoon: As you can imagine, in an organisation like this there were always cases when one country might have felt very strongly about something and they would rush around the table and try to get other people to block things, and of course that went on, but that is part of the baggage that goes with the consensus process and the FATF generally manages to work around that. If the secretariat, as they do, do their preparation work well and the Presidency does the work well in advance—these things happen but it is okay.

Q405 Lord Marlesford: Really following up, Sir James, a slightly earlier question, am I right in getting the feeling that you are talking about the importance of FATF acting in countries where there is widespread and systemic corruption, particularly at a political level, and the difficulties of doing so?

Sir James Sassoon: I was making the point about politically exposed persons to make another point which is that it was a very clear example, I would say, where a group of FATF members feels very strongly that legal form is as important, let us say—let us not say more important—as the outcome. I was not wanting to make a point particularly about the approach of different members to politically exposed persons, but of course as a general topic it is an area on which the FATF and individual national authorities could usefully make a huge amount of additional progress, so it is an area of continuing focus of course for the FATF.

Q406 Lord Marlesford: Could it be regarded as quite an important international priority for the FATF to improve the governance of countries where governance has been particularly inadequate due to a note of corruption of various sorts?

Sir James Sassoon: There are limits to what the FATF can do in this or any other area. The FATF can make sure that its broad recommendations impose a requirement on countries to be effective in addressing this issue. It can draw attention in a very practical way to some of the issues that fall out of it, so for example as I mentioned in the joint public/private sector work, one of the things the private sector wanted to talk about in very practical, granular terms was their approach to identifying the telltale signs and what they should do about them in relation to politically exposed persons. When it comes to broader questions of corruption in regimes the question would be, I suppose, would that pose such a risk to the international financial system that a country should be included within the special processes for dealing with non-co-operative countries. That would be the other way that it could bite on the work of the FATF.

Chairman: We must move on but first Lord Faulkner on this point.

Q407 Lord Faulkner of Worcester: Just a quick question on the membership. I am a little puzzled as to what the criterion for membership is because I see, for example—and these are only examples—Israel, India, Taiwan are not members of the FATF and I just wondered why that might be and whether their applications were opposed by other members?

Sir James Sassoon: India and Korea are the two countries that are on the list of prospective members; they are going through a process and if the next evaluations which they go through come up to the required benchmarks then the formal applications for India and Korea will be considered for the FATF. What the FATF has said in essence is that once those two countries have gone through the membership process then the organisation will have a further look at seeing where next it goes on membership, and at that point a whole list of countries would be prospective candidates.

Chairman: Thank you. Lady Garden, who has been most patient.

Q408 Baroness Garden of Frogmal: Not at all, thank you, my Lord Chairman. Sir James, can I take you back to the *Three Presidencies Paper* which you alluded to earlier, which was June 2008 with the UK, Brazil and the Netherlands proposing a review of the standards set by the FATF and of the mutual evaluation process. You have mentioned some of the factors already, but perhaps you could crystallise what were the most important factors which

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prompted this particular initiative, what you hope will result from it and do you have any timescales for when you hope to see results?

Sir James Sassoon: What prompted it was first of all the desirability in any standard-setting organisation like this to do a comprehensive review on a periodic, regular basis of its standards, and such reviews have been done by the FATF in 1996 and 2003. I do not know whether there is a definitive timescale that has now been set on this but typically these reviews in the past have taken a couple of years and so now looks like a good time to kick one off, particularly because the FATF is coming towards the end of its third round of evaluations, and that would be the natural point to look at the whole construct before you then start putting countries through the evaluation cycle for the fourth time. The other thing is we touched on the fact that this an organisation where the Presidency only lasts one year and it seemed to be important and helpful to the organisation to try and give some sort of multi-year sense of direction of travel; that is why we kicked it off. What do I hope comes out of it? I certainly hope and believe that there will be a recommendation by recommendation review and that all the experience over the last six or seven years will be fed into the review. More importantly than that, I hope that the FATF will take the opportunity to consider some of the big picture issues because if there are lessons to come out of the financial crisis one is the danger of losing sight of the wood for the trees, and I would very much hope that big questions like the compatibility of a risk-based approach to more prescriptive guidelines, the question about whether the FATF is going too far down the one size fits all approach to rule-making and some other issues to do with broad questions of law and regulation are going to get looked at. From the latest I hear, I am pleased that the latest plenary session seems to have given considerable impetus to the recommendation by recommendation review. I do not hear that there is much appetite—and maybe there is something else going on that I do not know about—for taking a broad overview and that would be disappointing. I hope over the next year or 18 months they do look at the whole shape of the wood.

Q409 Baroness Garden of Frognal: Did the three countries share the common view, was it relatively straightforward to focus between the UK, Brazil and the Netherlands as to what you hoped to achieve through the review?

Sir James Sassoon: There was a very high degree of common approach. I went to see the Dutch Finance Minister and even at that stage, some 18 months before they were due to take over they were already thinking about what they wanted to get out of their Presidency, so there was a high degree of engagement and forward looking by the Netherlands. I also had

very extensive discussions with the now President from Brazil and we jointly put this together.

Q410 Lord Faulkner of Worcester: I wonder, Sir James, if I can ask you about how you feel the FATF is coping with the global financial crisis. The memorandum they have sent us I have to say for blandness is hard to beat. It contains, for example, phrases like “the FATF will take stock of the consequences of the financial and economic crisis for the FATF and identify issues for further analysis and discussion.” It does not sound like a great deal of urgent attention is being given to this and I wonder whether you feel that particularly the banking secrecy provisions that are contained in the way FATF works are making this job particularly difficult and whether you would like to see them do more.

Sir James Sassoon: I find it difficult to comment on what the FATF is up to and the speed and detail of its current work programme, but they clearly are collecting evidence from their members and I am sure they will be coming back to it at the next one or two plenaries. I would be surprised if, when the research is done and the discussions had, if there is anything in the basic FATF framework about banking secrecy that needs to be changed as a result of lessons from the crisis. My lessons from the crisis would be looking at two different areas. I would be very concerned about the possible diversion of resources within finance ministries and financial regulators, in particular, and maybe in other authorities away from this area of work as the authorities are under enormous and continuing pressure to deal with the day-to-day aspects of the crisis. I have no particular evidence about whether this is happening, but the diversion of resources away from the focus on this area would be one thing that I think needs to be guarded against. The other thing which is really important is whether one of the lessons for the FATF should not be so much about looking at whether the individual rules are still fit for purpose—which I am sure will get looked at—but are there questions about looking at the shape of the wood rather than being lost in the trees. While the situation is very different from straight financial regulation, and how the rise in debt was a key thing that somehow people missed or missed the consequences of, I do think that the commitment that the FATF gave under our leadership to the global threat assessment, for example, should be given more focus and attention post crisis.

Q411 Lord Avebury: My question earlier on about enlargement had in mind the differences between FATF and MONEYVAL and the reasons for the existence of two separate organisations. One thing we have been told is that 12 of the 27 EU Member States are members of MONEYVAL and not of FATF. Is

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there any need for the two organisations and why should they not be merged, apart from the difficulties of having a much enlarged membership?

Sir James Sassoon: One of the principles about the FATF and its membership is that it should be globally balanced and it should be reflective of factors to do with the size and importance of economies, so if one was to say that all the MONEYVAL members could become FATF members if they met the technical membership criteria, the implication of that would be that to all the regional bodies similar to MONEYVAL you would effectively be saying we open up FATF membership, to 180 countries provided they met the criteria, which many of them would. It would completely change the character of the FATF. You are taking evidence from MONEYVAL next week and of course they may say something different to me, but the relationship between FATF and MONEYVAL I would say is extremely close. There is a high degree of mutual respect and co-operation; they are working to absolutely the same standards in terms of their evaluations; and the MONEYVAL non-EU members are actually also assessed to some extent on EU standards, so the evaluation of the non-EU members of MONEYVAL will reflect, for example, the third Money Laundering Directive. It works extremely well and I had a couple of meetings, at his request, with the Secretary-General of the Council of Europe who, as you know, is the sponsoring body of MONEYVAL—Terry Davis—so there is commitment right through the Council of Europe to MONEYVAL; and most importantly in the current context, and it bears on some things we have just been talking about. MONEYVAL is ahead of the FATF in the cycle of their reviews, so they have completed their third round of evaluations and are already leading the thinking about what the fourth round should be. You might discuss this with Mr Ringuth, but I know from my discussions with him last year that they are already very focused on shorter evaluations, looking at effectiveness and outcomes, and I rather hope that if MONEYVAL is committed, as I am sure they are, to driving that through, the FATF will be able to learn from that. I think the construct works pretty well at the moment.

Q412 Lord Avebury: You said that there was use of the same standards in FATF and MONEYVAL; does that apply also to the monitoring mechanisms of the two organisations, are they exactly the same? If you have got the same standards and the same monitoring mechanisms can you really justify the existence and the superstructure of two separate international organisations?

Sir James Sassoon: They are exactly the same and the way they are kept exactly the same is in all sorts of ways. It happens, for example, that the Financial

Services Authority recently seconded somebody into the secretariat of MONEYVAL so there is cross-fertilisation. And I have to say, in parentheses, that the Financial Services Authority is enormously supportive and effective in supporting the wider FATF efforts. It does work exactly the same so why does not one merge the two together? Quite apart from the fact that, as we have discussed, the FATF would become a very large organisation if everything was merged, in every region of the world there are particular challenges. As you know, many of MONEYVAL's members are in Central and Eastern Europe and have very particular characteristics and challenges of their own. Countries in the African region, for example, have particular and very different challenges, the Asia-Pacific region similarly, so one of the benefits of having these regional groupings is that they are able to tailor a lot of their training initiatives and their initiatives to look at particular typologies, for example, to their individual members and they can focus very particularly on the challenges of individual member countries. Again you should ask MONEYVAL directly about this but recently MONEYVAL identified concerns around one of its members, Azerbaijan, and issued a statement of concern on it. That was before the FATF had taken any particular public stance on Azerbaijan so it is an example of where a regional body is able to focus attention on particular regional problems, and I think that is rather powerful and useful.

Q413 Lord Avebury: Have you got any formal agreements between yourselves and MONEYVAL on how the relationship between the two organisations is supposed to function and, in particular, could you say anything about the function of the two EU countries which are appointed by the FATF Presidency to the membership of MONEYVAL. What do they do?

Sir James Sassoon: Again, you should ask MONEYVAL on the first question to make sure I have got it right. What the FATF sets out are some model rules for the regional bodies. MONEYVAL has been a model of what the regional bodies should be—it was one of the first to become an associate member of the FATF so the way it has developed is that the methods of operating of groups such as MONEYVAL, and very much led by MONEYVAL, have been the standards which have been encouraged in the other regional bodies, but you might want to ask them more about that. On the second point, again, they will know more of the background of this but it was just a question of making sure that at any one time, to reinforce the linkages between the two groups, there would be at least two FATF member countries within the EU who were going to all the plenaries, playing a full part, and it was thought that the best way of doing it would be to have this rotating

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approach. So I do not think there is any magic in it, but it was a pragmatic way of making sure that the linkages between the two bodies were kept strong and refreshed.

Q414 Chairman: Two questions about membership of FATF. I was surprised to see that the Gulf Cooperation Council is represented and not the seven Member States; is there any particular reason for that? The other question is the fact that those members of the EU who are not members of FATF, as you say mostly Eastern European states, to what extent is that a product of a consensus rule and to what extent is that due to the influence of Russia?

Sir James Sassoon: I cannot really answer the first question and it may be that you could ask supplementary questions on the specifics of the GCC from the FATF secretariat as that was well before my time. The broad answer to the question is that when the FATF was originally set up 20 years ago it was a creation of the G7 and it has incrementally increased its membership from that point with a view to include at every stage countries or, in the case of the GCC and the European Union, representatives of important groups of countries, that were most significant in terms of economic and financial flows but also to keep a regional balance within the organisation. It has been an incremental process, in stages and it continues.

Q415 Chairman: What about the Russian influence and consensus with regard to the Eastern European countries?

Sir James Sassoon: I saw no particular evidence of anything there.

Q416 Lord Mawson: What strategies are utilised by the FATF to promote global implementation of its standards? What is the nature of the involvement of the International Monetary Fund and the World Bank in this process and how can this process be strengthened and improved?

Sir James Sassoon: I will come back to the IMF specifics and the improvements but in answer to your broad first question I would say, having quickly looked at the FATF secretariat paper, it actually sets out that answer well. On the specifics of the IMF and the World Bank, the FATF works incredibly closely with them; they put a lot of resources into this area and they are particularly effective and important when it comes to helping low capacity countries. There are questions that arise, particularly out of the IMF's involvement—they cut their budget for this area of their work during the UK's Presidency and the FATF quite rightly asked me to express in strong terms the FATF's concerns to the managing director of the IMF. I understand that the IMF's response has been to set up a trust fund to take up some of the slack

from a reduction in the budget in this area and that the UK is one of a small group of donors that has contributed to this trust fund, so actually this may be good news because it means that the UK will have particular influence on where this money is deployed and the areas of activity. So there are issues in particular with the IMF and questions, for example, about the balance in their work between developed countries and low capacity country evaluations that they contribute to. Why are they involved in evaluating countries like Germany and Luxembourg at the moment? I do not know. There are some questions therefore that need to be asked but the broad point is that the FATF relies heavily on the IMF, who are very good partners, as are the World Bank, when it comes to helping countries implement the standards.

Q417 Lord Hannay of Chiswick: Could you say, Sir James, what your assessment is of the current procedures within FATF for identifying and dealing with countries which do not apply, or insufficiently apply, FATF recommendations. Is there a need for counter measures, when called for, to be implemented in a more harmonised fashion—and I was thinking here of the example of Iran?

Sir James Sassoon: As I am sure you know the current process that the FATF is adopting for non-co-operative countries and territories has really only been in operation for 18 months or so now. It needed to be kicked off and we kicked it off under our presidency, but what can perhaps give us confidence that the new processes will deliver results over time is, first, that there was quite an interesting study very recently done by the IMF that attempted a scorecard across various different groupings of countries on the basis of their most recent reviews, and actually the 23 countries that went through the previous process, the so-called NCTT process, which was the previous approach to listing non-co-operative territories, if you take where those 23 countries are now they score almost up with the G7 countries in terms of their overall implementation of the FATF regulations. So the best evidence of how the current process might work is the evidence of the previous process and that is good news. What has been going on in the last year or two is that there is one territory, the northern part of Cyprus, which came into and out of the current process. I am not completely up to date but that clearly reflects work that has been done by the authorities there, so that is encouraging. Another example I would give is Uzbekistan which went as far as completely rescinding all its anti-money laundering laws by presidential decree and they were put on the list. After repeating the concerns that the FATF thought Uzbekistan gave rise to, in the last six months there has been a delegation that has gone out there and, as I understand it, the laws have been or

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are being restored, so that is another bit of progress. Iran is clearly much the biggest challenge; in lots of respects it outweighs all the others and there is clearly an extremely long way to go—Iran does not have terrorist financing as a criminal offence—but as a result of letter-writing and public statements—there was correspondence that I as President had with their ministers—there is now a dialogue and some engagement. There have been meetings with groups of officials on behalf of the FATF member countries and the FATF secretariat and there have been requests from Iran to help with the setting up of a financial intelligence unit. I would not want to overplay the significance of those moves because Iran has a very, very long way to go, but it demonstrates that the FATF, because it applies to Iran, as to all these other countries, absolutely technical criteria on a consistent basis, independent of other broader political considerations, is capable even or particularly, let us say, with Iran of contributing to the wider global effort. On harmonisation—and it is really not for me to be able to go into much of the detail because it is very recent—I do note that the latest FATF statement on Iran does talk about counter measures but leaves it to individual countries to decide what counter measures they implement. Whether that is a pragmatic and sensible way to proceed or whether it is a cop-out I find it difficult to say because I was not involved in the discussions. I certainly think it would be highly desirable in these circumstances if the FATF, since it has a specific ranking of counter measures in its rules—whether it is for Iran or for anybody else—, was actually able to agree where in the ranking of counter measures they would expect their members to be. There are some issues there, therefore, but I am really not in a position to answer on the specifics. When all this is said and done, where the most progress will be made on a lot of these countries is bilaterally with the countries that have the biggest flows, whether they are financial flows, trade flows or political engagement and therefore, yes, there should be harmonisation of the FATF but in the real world it will be the countries that deal most directly with Uzbekistan on a trade and finance basis or with the northern parts of Cyprus or Iran who are bound to have a disproportionate influence and therefore it is up to them to take the strain.

Q418 Lord Hannay of Chiswick: Thank you. Could I just lead you on from that into an area which was not probably quite so active during your chairmanship but which has become in the last months extremely prominent, which is the question of Somalia and piracy and the transfers of funds to Somali pirates basically to get back crews, ships and things like that. This has become much more prominent in the last few months and, to tell you the

truth, we have been pretty puzzled—the polite word—by the lack of response so far by any of the organisations that deal with this. FATF has not uttered a cheep about it as far as I can see; the EU seemed not to know that it existed when we went to Brussels; and the British Government has given us some thoughts on it which can perhaps politely be described as not very substantial. I wonder what you think this says about FATF’s ability to respond to an emerging threat or challenge.. After all, we all understand that Somalia is not only a non-cooperating country it is almost a non-country, but that does not mean to say that there is not a problem here, a problem both in the money laundering sense but also a potential problem in the laundered money getting to terrorists. One cannot possibly assume that none of the millions that are going to Somali pirates are reaching terrorists; could you comment a bit on that and I do understand that this is not related to your period of the presidency. But from someone as skilled as yourself who has seen this whole process from the inside it would help the Committee a great deal if you could tell us a bit about this because we are feeling somehow that there are tricks being missed here.

Sir James Sassoon: I will do my best although I fear that when you next recite this long list of people who have given these inadequate responses I risk being added to the list. Seriously though, as far as the FATF is concerned there are a number of ways in which they can engage with an issue such as this. First of all it would be unfair to say that they are not capable of moving at relative speed to identify threats and deal with them, but if you take something like the Somali pirate issue the first thing is that a lot of what the FATF does depends on being able to engage with a country that has some sort of structure with which you can interface and try and progress issues. You have said what the state of affairs is in terms of the government and governance of Somalia, so by that standard it is quite difficult for the FATF to find the right people to engage with in terms of the public authorities. The second thing is that, linking back very much to the previous question and answer, the question that the FATF should be going through—and I am sure it is—is to ask whether this activity mean that Somalia should be added to the list of territories which require governments and financial institutions to exercise heightened due diligence or whatever other counter measures. I do not know, because I am not there now, what discussion if any there has been to establish how Somalia ranks alongside these other territories and whether it should be brought to attention as a country that people should be wary of dealing with, although I suspect that everybody knows to be wary. The other way that the FATF could get into this sort of topic is through typology work and if it was thought that

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light could be shed on piracy and the flows of money out of pirates as a generic topic then that is the sort of case study that the FATF can usefully do, but that is obviously a slightly longer range activity and I do not have a particular view as to whether looking at piracy would be useful for the FATF to lead work on, but clearly they could get into it that way. Stepping back from that, this seems to me to be much more a question of intelligence operations to try and get at where the money is flowing, for which the FATF on a month by month, year by year basis has no particular locus.

Q419 Lord Hannay of Chiswick: Yes, but national governments do of course.

Sir James Sassoon: Indeed.

Q420 Lord Hannay of Chiswick: And the EU of course does in applying its directives; and that is one direction in which our enquiries are going, not so much in the direction of FATF, though I do think it is surprising that you have a FATF communiqué issued quite recently that had a whole long list of problems for people to be aware of and there was not a cheep about this. As you yourself suggested in your first response that was something they could have done, which was to say watch out, this is an area where money is being laundered. And the evidence we have had so far from the British Government is quite the contrary, they actually told us they would not pursue anyone who did not file an SAR in the context of a payment that was being made that might end up with the pirates in Somalia.

Sir James Sassoon: These are all questions that are well worth asking. I am sorry that I cannot really help you very much.

Lord Hannay of Chiswick: You have actually helped quite a lot by your response; thank you very much.

Chairman: Lord Marlesford on this point?

Q421 Lord Marlesford: It is on a rather similar point, my Lord Chairman. It does seem to me, listening to the dialogue today, that an area where there could be a very useful role for FATF is that the IMF and the World Bank in deciding what help to give to countries whose financial governance is badly lacking could take into account the reports of FATF because that would enable pressure to be put on those countries to put their house in order. Does that happen at the moment?

Sir James Sassoon: I am sure it does actually. As part of the IMF and World Bank's broader support for countries that they are engaged with, whether through direct lending support or through technical assistance programmes, they are pretty good at picking up on issues that come out of this area, so I would be reasonably confident that they do cover that one.

Q422 Lord Marlesford: If it were publicly known that particular countries were failing in this way and they were countries where one is constantly hearing about the diversion of international funds intended for the relief of poverty for very different purposes—if it could be publicised this would be not just good publicity for FATF, which I am not particularly interested in, but it would be a means of putting pressure on countries which do misbehave in a big way—one is thinking I suppose in particular of some African countries where there have been notorious accounts of major embezzlement of funds intended for its citizens.

Sir James Sassoon: My impression is that indeed the IMF and the World Bank do link concerns in this area through to the broader programme of work to support countries to reform their governance. I am sure there is more that can be done but they make every effort they can.

Q423 Lord Faulkner of Worcester: I am afraid I am going to continue with the slightly negative tone as well. I just wonder whether you would agree that in the 20 years of FATF's existence it has not really achieved very much in terms of countering the financing of terrorism or indeed money laundering if you judge that by the number of convictions secured and the quantity of criminal proceeds confiscated. Do you think it could have done better and do you think it will do better in future and, if so, what ought to bring about the change?

Sir James Sassoon: It is a perfectly fair question and implied or actual criticism. In my mind it gives rise to a number of issues for the FATF. First of all, frankly, the data in this area as in so many others is so patchy that it is very difficult, even if you can take a snapshot in time, to be able to get sensible data of the progress of effectiveness across a whole number of measures, of which you have referred to a couple; it is enormously challenging. The first thing is that there needs to be much better measurement over time, and tracking of such data as there is, to see how progress is being made, and then, of course, linking that to questions of which steps that have been taken or need to be taken in the future are the ones that are likely to deliver the best results. I am not remotely an expert on some of the areas that I know you have been discussing which are international co-operation on confiscations, on mutual legal assistance and areas like that where there is, I am sure, extremely practical and critical work to be done, some of which the FATF can do and some of which is for other groups to carry forward. Part of the answer to this is to get bodies like the new public-private sector funded International Centre for Financial Regulation in the UK, set up in the last year by the Government and the banks, to put on its research agenda some very practical issues like this to actually see what the way

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forward is. You are absolutely right, but there is not at the moment a proper road map forward.

Q424 Lord Hannay of Chiswick: I wonder if you could just comment at the end—this is the last of our questions—whether there are any other major challenges presently facing international efforts to combat money laundering and the financing of terrorism, and perhaps within the scope of that you could just offer us a comment on the Hawala system and whether or not that is in any sense a weakness in the present systems. We have found that the British authorities seem to be very aware of the Hawala issue and believe that it does not represent a real problem because the Hawala operators in this country are regulated. When we went to Brussels we found a complete ignorance of the practical existence of Hawala, despite the fact that it clearly does exist in quite a large number of other European countries too.

Sir James Sassoon: It is interesting and anticipating this question I put down four thoughts of things that we might not otherwise have covered. These are things that we have not covered, so not necessarily the most important things, but I did have the law enforcement and effectiveness co-operation issues down as one of them and actually the last one I had was Hawala because I do think that informal money flows are a critical component of what makes economies and has made economies flow in parts of the world for many centuries. There is a very difficult ongoing tension between saying that informal money flows have to be subject to Western-style regulation on the one hand but on the other hand to be sensitive to long traditions of informal flows of money. These are not used to by-pass Western-style banking systems in order to avoid scrutiny; the original purpose of them was because in the absence of good banking systems this was the traditional way that money flowed and it also happened in different ways in Europe until relatively recent times. It is an ongoing tension and you see countries like the UAE where the central bank governor has made very significant attempts to get discussion and debate around what the methodologies are to reconcile the irreconcilable. Frankly, this is going to be a 50-year challenge which is only going to get resolved finally when more sophisticated banking systems come into less developed parts of the world or parts of the world that to a certain extent do not, for understandable reasons, want to lose their traditional approaches. Absolutely it is a big issue and it cannot be resolved quickly. There are two others I would quickly draw attention to. One is an issue you very well understand but is always worth reminding ourselves of, that on terrorist financing the challenge is the needle in the

haystack. The fact is that the direct cost of the 9/11 operation is estimated at no more than half a million dollars, the 7/7 bombings in London were a few thousand pounds direct cost, so one has to be very realistic about the linkages between money flows and terrorist outrages, and there is a lot more to be done to think about that. The last general area where we are only beginning to scratch the surface is what more can and should be done on the electronic filtering of data that is flowing around both the private and public authorities' systems. This is both a question of technical challenges, of the costs that are being incurred, the civil law and liberty issues that are implied by what is going on. There is a whole host of issues here and the world is only beginning to understand what can be properly extracted by sophisticated electronic filtering that might drive forward the effectiveness in this whole area of policy.

Q425 Lord Avebury: I just wondered where there was any particular reason why you had not mentioned the International Co-operation Review Group in answer to this question or the previous question of Lord Hannay about piracy because it seems to me that there is a severe deficiency here in both these sectors, in terms of informal money transfers and the leakage of very large sums of money to pirates, in the weaponry that we have got to combat ML and CFC. Is that not precisely what the ICRG's is attempting to address?

Sir James Sassoon: I did not name the ICRG as part of the process but when I said that the FATF would be looking, should be looking—it may well be looking, I do not know, because they do not publish the discussions of the ICRG—at whether a country like Somalia presents a risk that needs to be highlighted, it is the ICRG which is the working group that would be doing that. It may well have been looking at it, but it only publishes, quite rightly, its outcomes when it decides that it is appropriate to do so.

Chairman: Sir James, that brings our session to an end. I have to say and to put it on the record that the Committee was extremely disappointed and really very surprised when we discovered that the FATF do not go and discuss matters themselves with Parliaments; even the United States Congress fell foul I understand of that. That is as it may be; we have had, as I referred to earlier, a written report from FATF and you have been more than kind in coming here and being very frank with us indeed. Those two together go a long way to giving us the answers that we might have liked to get direct from current management of FATF. We are extremely grateful to you, you have given us a fascinating session and we appreciate the fact that you have come to talk to us. On behalf of the Committee, thank you very much.

WEDNESDAY 29 APRIL 2009

Present	Avebury, L Dear, L Faulkner of Worcester Garden of Frognal, B Hannay of Chiswick, L	Harrison, L Henig, B Marlesford, L Mawson, L Richard, L (Chairman)
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Examination of Witnesses

Witnesses: IAN PEARSON, a Member of the House of Commons, Economic Secretary to the Treasury, MR ALAN CAMPBELL, a Member of the House of Commons, Parliamentary Under Secretary of State, Home Office, MR JAMES ROBERTSON, Head of Financial Crime Team, HM Treasury and MR STEPHEN WEBB, Acting Director of Policing Policy and Operations, Home Office, examined.

Q426 Chairman: Good morning and welcome. We are most grateful to you for coming and giving evidence. It will be very important to our inquiry to hear the evidence from these ministries. Mr Robertson and Mr Webb, not for the first time, we also welcome you to these considerations. Perhaps you would care to introduce yourselves and then we will ask you some questions.

Mr Campbell: I am Alan Campbell, Minister for Crime Reduction in the Home Office.

Ian Pearson: I am Ian Pearson, Economic Secretary to the Treasury.

Mr Robertson: James Robertson, Head of Financial Crime in the Treasury.

Mr Webb: Stephen Webb, Director of Policing Policy and Operations in the Home Office.

Q427 Chairman: In his evidence the EU Counter-terrorism Coordinator has described as “shocking” the fact that two important EU international agreements relevant to efforts to combat money laundering have, after many years, still not entered into force. As I understand it those two are the 2001 Protocol to the EU Convention on mutual assistance in criminal matters, and the 2003 EU-US Agreement on mutual assistance in criminal matters. Will the government perhaps try to use their influence with other Member States concerned to expedite this process? 2001 is now quite a long time ago and it seems a useful protocol if it came into force? What do you think the implications are for EU policy making in this area, the fact that these conventions have not been ratified does that have a fundamental view on your approach to the EU?

Mr Campbell: I will begin with the 2001 protocol which, I think, is widely recognised to be very innovative as a legal assistance instrument. Let me begin by saying that the EU Counter-terrorism Coordinator actually is mistaken with regards to this particular measure because the 2001 protocol entered into force for the United Kingdom on 13 June 2006.

It had originally been entered into force the preceding October but as it stands today I understand that only Estonia, Greece, Ireland and Italy still have to ratify the protocol. Of course we will continue to push with those remaining countries to ratify the protocol as soon as possible.

Q428 Chairman: Are there fundamental objections by those states?

Mr Campbell: I am not sure as to the detail of that.

Mr Webb: We do not have any reason to believe so; the process is just taking longer.

Mr Campbell: Turning to the EU/US Agreement, we very much hope that we will be able to bring it into force towards the end of June of this year. It is quite right that the legal assistance agreement has not been ratified and therefore is not in force, but perhaps I can say why it is a particularly complex process. In fact it requires the United States to conclude and ratify bilateral mutual legal assistance treaties or instruments with each of the individual Member States, including any who have acceded following the agreement being signed in June 2003. That involves 27 different states, each negotiating a treaty or instrument with the United States. That clearly is a time consuming process. It also means that for each of the states domestic legislation may need to be updated and again this process can take a considerable length of time. We signed an agreement with the United States in December 2004 in order to comply with all the provisions of the EU/US agreement which is why we are confident that we can move to ratification quite soon. All of the search of legislation which may need to be updated has indeed been done and any changes made; that had happened by August of last year which is why we are moving towards ratification. Once we have that bilateral agreement between the US and each of the individual states then of course we can move towards the full agreement. In answer to your question what does it mean on a day to day basis, we are confident that

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even if the overall agreement is not in place where there are bilateral arrangements in place it does not have any great practical effect on day to day mutual legal assistance requests, including those involving money laundering, because the bilateral treaty serves, once it is in place, as the conduit for that to happen. You also went on to ask about what it means for a policy and particularly a policy at EU level. We believe that overall the policy making process is in fact sound. There is clearly an issue of where the discussions and negotiations move from the policy making arena to the political arena where Member States are then obliged to get an agreement within their own states in order to ratify, but notwithstanding that it depends upon which individual state we are talking about we will continue to push our colleagues in the EU in that direction.

Q429 Chairman: Can I just come back to the first point. When Mr Webb gave evidence in front of us he was asked by Lord Dear to “look at the Second Additional Protocol to the European Convention on Mutual Assistance in Criminal Matters, a 2001 protocol, which I understand the UK has signed but not ratified”. The answer was, “We would expect to ratify this one by the autumn. 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.” Could you clarify the exact position on that one?

Mr Webb: The 2001 protocol to the European Convention on Mutual Assistance in Criminals Matters?

Q430 Chairman: Yes. Your answer was, “We would expect to ratify this one by the autumn.”

Mr Webb: Are we talking about the same protocols here?

Q431 Chairman: I thought someone said it had come into force on 30 June 2006.

Mr Webb: We believe this is a different protocol we are talking about. We will get back to you on that.

Q432 Chairman: Could you sort it out and let us know what the exact position is.

Mr Webb: Yes.

Q433 Chairman: Could you also let us know how many countries have actually ratified and how many we are waiting for? It is not just three or four; according to your original answer it was about 29.

Mr Webb: Yes.¹

Q434 Lord Avebury: Do I understand that the EU/US agreement is actually in force?

Mr Campbell: No, we are moving towards ratification and we hope to do that this summer.

Q435 Lord Avebury: So there are no requests for mutual legal assistance between us and the US so far. It is not possible for us to make a request of the US for legal assistance at this stage. There is no mechanism by which we can do that until this protocol comes into force.

Mr Webb: I do not believe it adversely affects mutual legal assistance between us and the US. In some of the common law jurisdiction it is often possible to do this through existing powers; it is not necessarily as important as it is for some continental partners. I am not aware of any problems we are having sharing mutual legal assistance either in criminal law CT matters with colleagues in the United States.

Q436 Lord Avebury: So the coming into force of the protocol will not make a great deal of practical difference.

Mr Webb: Not as much for us as it probably will for others.

Q437 Baroness Garden of Frognal: Could I clarify that your previous answers were not in connection with the 2005 Council of Europe Convention? You were not answering on that on the first question.

Mr Campbell: No.

Q438 Baroness Garden of Frognal: We were informed about that in a previous evidence session when Mr Webb was present, that the 2005 Council of Europe Convention on laundering, search, seizure and confiscation of the proceeds from crime and on the financing of terrorism that the UK does now intend to sign and ratify at this convention. Could you tell us when this was agreed and why it could not be done in a shorter time than the 18 months which were indicated to us previously.

Mr Campbell: A precise timetable for implementation has not been finalised because we are talking about an estimate that officials gave and, by its very nature, an estimate is just that and reflects the obstacles that might have to be overcome and the procedures that might have to go through. Of course not all of them might cause such a delay as we perhaps feared at one time. The House of Lords Scrutiny Committee had concerns over aspects of the convention and quite rightly took time to address these concerns and in fact we did not get scrutiny clearance until 25 February this year. Once we got that we were able to begin to prepare to sign and subsequently ratify the convention. Of course, as with any convention, we would also want to ratify when we are in a position to actually implement it so I think there is that practical side to it too. Implementation will involve detailed scrutiny of every article of the convention and it is

¹ See Supplementary memorandum (6) by the Home Office p 191.

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possible, when considering these matters, that we might need to bring forward legislation—indeed primary legislation—to make sure that we are fully compliant with the convention. With the prospect of primary legislation there comes the prospect of public consultation on these matters, then looking at what the responses might be, and then moving to legislation. All of that does take quite some time. It is certainly our aim to move as soon as possible to ratify and implement the convention, certainly within the next 18 months. If it does not require domestic legislation, does not require consultation and does not require all of those things to be overcome then we see no reason why we could not move to it more quickly.

Q439 Baroness Garden of Frognal: There are not specific hurdles then, it is the process of scrutiny.

Mr Campbell: I think it is very much the process, the appropriate level of scrutiny but also, arising from that, what changes we might have to make in our own domestic legislation and everything else that that involves. I think it is a process issue rather than a substantial problem.

Q440 Chairman: Are you saying it can be ratified within 18 months.

Mr Campbell: That is certainly our best intention. I am perhaps saying that that is the longest time.

Q441 Lord Dear: I would like to talk about timing and bring you back to bilateral agreements which have been mentioned already. We have received evidence from the Crown Prosecution Service through their Chief Operating Officer that they emphasise the importance of promoting international cooperation through the medium of bilaterals between two countries. We wondered whether the government see this as a priority and if you do are the necessary resources going to be made available to enable that to happen and over what sort of timescale?

Mr Campbell: We are talking largely about civil recovery.

Q442 Lord Dear: Yes, civil recovery.

Mr Campbell: Can I just place on record, Lord Dear, that whether it is criminal confiscation or civil recovery this matter is a real priority for the government. Let me also say that it is a relatively new concept to use civil proceedings in the High Court and in fact was introduced into the United Kingdom by the Proceeds of Crime Act 2002. I am pleased to say that it has been tested and has passed the test of it being ECHR compliant. It is something that we are particularly keen on. Unfortunately civil recovery does not always have that familiarity and support in other jurisdictions and in fact sometimes does not sit

very comfortably with other jurisdictions. We continue to push civil recovery obviously for our own purposes domestically but we also want to extend the lessons of that and the need for that internationally. We are working with the Serious Organised Crime Agency to develop model agreements relating to mutual assistance in civil recovery matters which we will use with bilateral agreements with individual countries to smooth a way for that and we hope to move to the first bilateral agreements soon. I think we are playing a leading role in the EU in pushing this particular concept in the working groups that are looking at this, whether it be through the G8 group or whether it be more widely. I can report back that the interest, particularly amongst the G8 group, has been very positive to date. You asked about resources and we believe that through the Home Office, the Serious Organised Crime Agency and also the CPS we will continue to make this a priority and we will continue to push with our EU partners, but we do believe we have the necessary resources in place.

Q443 Lord Dear: Can you give us any idea about how many bilaterals exist at the moment?

Mr Campbell: We have not entered into any bilaterals at present.

Q444 Lord Dear: How many have you got on the stocks? Can you give us an idea? Is it one, three, ten?

Mr Campbell: I understand we are working towards the first one quite soon.

Q445 Lord Dear: Towards the first one?

Mr Campbell: Yes.

Q446 Lord Dear: With a timescale or is it one of those things that has to run with no timescale?

Mr Webb: These things have quite complicated administrative negotiations, often with a large political aspect. It is very hard to predict from our side because obviously it depends on the partner. I would not like to say.

Q447 Lord Dear: Do you not even have a wish list on the time?

Mr Webb: We would like them as soon as possible; in the course of this year potentially, but it is going to be quite challenging.

Q448 Chairman: Who are you negotiating with?

Mr Webb: The jurisdictions have already used civil powers; we can often actually share information without an agreement. Certainly those sorts of countries—the Irish, the Americans—states like that—

Q449 Chairman: Sorry, you are negotiating a bilateral at the moment.

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Mr Webb: We have some negotiations going on.

Q450 Chairman: With whom?

Mr Webb: With the UAE. We are looking at that but it is at its very early stages and it is a question of explaining the processes.

Q451 Lord Marlesford: Looking at or negotiating?

Mr Webb: We are discussing it.

Q452 Lord Marlesford: With the UAE?

Mr Webb: Yes.

Q453 Lord Dear: The CPS has said to us that they place a high priority on this. At the moment there is nothing in existence; you are working towards one with the UAE but with no timescale.

Mr Webb: The main authority that is actually using civil recovery under the Proceeds of Crime Act is SOCA who took on all the responsibility of the asset recovery agency. SOCA are reasonably happy that the UAE will be there. CPS has these powers as well for itself. Ultimately we are going to be guided by the prosecutors and by the other agencies as to which the priority countries should be and where we should be working. I have just been handed a note about some other discussions going on including the Cayman Islands, Ireland and the G8. UAE and the Cayman Islands are almost finished; there are preliminary discussions with Ireland.

Q454 Lord Dear: How long have you been at this already? Is it possible to say when you started with UAE?

Mr Webb: A year or so. A year or a couple of years.

Q455 Lord Dear: A year or a couple of years?

Mr Webb: Yes. We probably first raised it about 18 months ago I think.

Q456 Lord Avebury: In one of our earlier sessions Mr Webb told us that the turnover generated by serious organised crime amounted to an estimated £15 billion of which £5 billion was invested in potentially seizable assets and £3 billion of that was held overseas. Then the DPP told us that if you look at the amounts that are actually confiscated as a result of court proceedings, very little relates to overseas assets. I wondered whether you regarded this as satisfactory in the way it was being tackled.

Mr Campbell: First of all let me say that in terms of the size of assets available to be seized again they are very much estimates and I think we need to treat them with some caution. It is trying to measure something which is incredibly difficult to measure and therefore we have to be cautious. What we do know as fact is that the UK's performance since the Proceeds of Crime Act 2002 is around £600 million over the last

six years. If the inference from both your question and perhaps those who have given evidence previously is whether more needs to be done, there is a resounding "yes" to that. In terms of overseas assets, these are particularly difficult to estimate the value. As you would expect there is quite a detailed process to go through. Confiscation orders are in force by the CPS and also by the Revenue and Customs Protection Office. The latest information that we have on unpaid confiscation orders, including overseas or hidden assets, is an estimate a further £535 million. The problem with that of course is that this takes quite a long time and therefore some of those orders might actually date from some time ago. I am sorry if I cannot give a direct answer to your question but it is a rather difficult measurement to take and it is also subject to quite a long timescale. We are talking about criminals—whether they are UK criminals or elsewhere—who will do their utmost, as you would expect, to evade any attempt, whether it is within the UK or abroad, to seize their assets. I think, as I said before, this is a relatively new concept for us and a learning process for us too. Almost as we come up with a new way of tackling it the criminals are thinking about new ways of being able to avoid it. However, we will continue to push. We have agreed a contract with a leading private sector company to enforce some of the confiscation orders involving overseas assets and we are waiting to see the results of that pilot, if you like, of seeing whether this is a better way of getting at them. There is inevitably a cost to that because it is a costly exercise to get the equivalent of international bailiffs to chase those assets. There is a cost to that too which we would need to weigh up. We are working to get multi-lateral agreements in place and bilateral agreements in place too, but that takes time and even then it is a lengthy process that we need to go through.

Q457 Lord Avebury: Do you have any idea of how relatively successful we are in recovering assets held overseas compared with other countries in Western Europe?

Mr Webb: I suppose the best indication we can give is that we get very, very few incoming requests from other countries asking to enforce against assets in the UK. The impression is that we are certainly trying harder, sending more requests outwards than we are receiving in. Certainly our overall performance on recovering proceeds of crime is very large compared to most of our western European partners. The impression we get is that we are at least as successful or more than most of them and the big players in this area would be Ireland and the States.

Mr Campbell: May I just add to that that it is a learning process for us and the criminals but of course we need to be one step ahead. The Police and Crime Bill which is currently making its way through

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the House of Commons has proposals in there around seizure of assets to allow them to be seized subject to judicial oversight at an earlier stage rather than to give time for the criminals actually to dispose of them through their family or their friends or whatever else. It is very much a learning exercise and we hope we are on the front footing.

Q458 Chairman: As I understand it, assets confiscated abroad would normally stay in the hands of the confiscating country. Have we negotiated any asset sharing agreements?

Mr Webb: We have a number—maybe six or eight—with countries such as the US, Canada, Jamaica, the Channel Islands and a few other countries of that description. We have been having discussions with some of our bigger European partners as well. Obviously the flip side is that we can potentially enforce orders in this country and we would retain those assets too. The prime point is obviously that the criminals are deprived on the money so in a sense that is a good thing irrespective but human nature dictates that it is more likely to be enthusiasm to pursue this money abroad if there is an opportunity to share the proceeds and we are very keen on doing that. I think we also have a very old agreement with the Netherlands.

Q459 Lord Mawson: Both the G-20 declaration of 15 November 2008 and the G20 leaders' statement at the London meeting on 2 April 2009 make reference to the FATF. In your view are any of the FATF's standards (as with banking secrecy) or procedures (as with non-cooperative countries) in need of review in the light of lessons learned from the global economic downturn?

Ian Pearson: This is a Treasury lead so let me reply. The first thing I want to say is that both the G-20 declarations have been very positive about the work of the FATF and there is absolutely no suggestion that money laundering and terrorist financing standards as set by it are in any way deficient or played a role in the onset of the financial crisis. The FATF standard correctly requires that banking secrecy laws do not inhibit the implementation of the FATF recommendations and this provision will continue to apply to any future amendment of the standard. It might be helpful if I just explain some initiatives that are currently underway. There is an initiative underway at present that will give the FATF opportunity to ensure that its recommendations and procedures are fit for purpose which is the review that is taking place in preparation for the fourth round of mutual evaluations. We submitted UK priorities for review in January, almost all of which have been taken forward. In addition, at the last plenary in February this year, the Dutch (who will hold the Presidency from July) have proposed to lead a project

examining the implications of the financial crisis, global patterns in money laundering and terrorist financing, and to ensure that FATF measures and procedures remain appropriate. This Dutch project will enable us to develop a comprehensive picture in the changes in established financial crime patterns in response to the financial crisis, assuming that there are any. It would help to give us a clearer picture of how the FATF could respond. I would also highlight a third strand which is that the FATF are committed to reforming the referral process for the international cooperation and review group which reviews countries that do not adequately apply its recommendations and alerts other countries to the risk of doing business in these jurisdictions. They are scoping how to refer a country for a review by the ICRG on the basis of both the money laundering and terrorist financing by jurisdiction and the objective performance against the standards of that jurisdiction. There is going to be an intercessional meeting of the ICRG in May that will be entirely devoted to this issue.

Lord Hannay of Chiswick: I have two points about that. In what you said about the ongoing work of the FATF I did not hear the words "impact assessment" anywhere. Is there any question of the FATF conducting an impact assessment of its systems because both in the case of the EU (where no impact assessment was conducted before the first two money laundering directives were introduced) it seems that there is very little knowledge of what the effects of these controls are on business, whether it be accountants, lawyers, bankers and so on? It would perhaps be useful if that were so. My second question is simply to alert you to the fact that we will come onto this same ground again in the case of the Somali piracy issue. I do not know whether you want to cover any aspect of FATF's handling of that now or leave it to the questions on Somali piracy.

Chairman: We have four questions on that; it is probably easier to take them as a block at the end.

Q460 Lord Hannay of Chiswick: Indeed. I wanted to mention it simply because it was not clear to me whether Somali piracy came anywhere in the rubrics that the minister referred to for future work.

Ian Pearson: I am quite happy to answer questions with regard to Somali piracy and the FATF later on. The point I would want to make clear now, however, is that the FATF is essentially a standard setting body. It is taking forward work on cost-benefit analysis which is a priority for the Dutch Presidency and I have mentioned the work that is taking place in terms of the mutual evaluation process and the review. I think that is helpful and I do think that perhaps the cost-benefit analysis work that has been taken forward by the Dutch is not too dissimilar from

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what you are seeking to achieve and what you are saying about an impact assessment.

Q461 Lord Marlesford: In relation to FATF can I raise another point which seems to be quite an important one? Given that the FATF recommendations were revised in 2003 before the conclusions of the UN Convention on Corruption, should the current view of those standards and the associated methodology for assessment be strengthened in relation to the laundering of the proceeds of corruption and the associated international cooperation? I think that is a question for the Treasury really.

Ian Pearson: As I indicated, there is quite a lot of work underway at the moment to see whether the FATF's recommendations and procedures are fit for purpose. James might want to comment particularly on that point.

Mr Robertson: Our view is that the standards themselves vis-à-vis corruption are relatively robust. The real question, as I tried to bring out before in a previous evidence session, is the effective application of the standards of the countries. There are some legitimate questions about the ways in which countries have put the standards into practice vis-à-vis corruption and issues around politically exposed persons and so on which are issues which the private sector finds quite hard to deal with. So I think there is a legitimate question in terms of examining the extent to which the standards are applied and the methodologies and the mechanisms that countries use for ensuring that the corruption standards are met.

Q462 Lord Marlesford: I think you will agree that there is huge public interest in the frequently reported instances of taxpayers' money, for example, being given through the aid programme to some countries which is siphoned off by the leaders of those countries. This very often applies to African countries which are, in many ways, states. It would seem that that is a very fertile area for FATF to lay down the standards which would constrain the distribution of these funds so they are not siphoned off.

Ian Pearson: As you will be aware through our Department for International Development which disperses UK funds through its aid programme, it has a number of procedures in place to ensure that funds are not diverted from the purposes to which they are intended. In many cases where DFID has substantial concerns it provides funding through NGOs rather than directly through governments where it thinks there is a real risk of a diversion. It might be, as part of your inquiry, you would want to pursue that particular question further; you might want to talk to DFID officials or a DFID minister about them. I am

certainly aware that DFID has rigorous procedures in place to try to make sure that money is not being siphoned off from the good causes that we all want to see in terms of helping development, particularly in Africa as you mentioned.

Q463 Lord Dear: Could I introduce the Third Anti-Money Laundering Directive into the discussion? It would help us if you could focus on one issue at least which is that we have received some evidence already from two different sources suggesting that the private sector here in the UK has been put into a disadvantageous position comparatively to other countries in the EU. I do not know whether you agree with that assessment which has been put to us. If you do agree with it, could you tell us what you are doing or what you will be doing to address that issue?

Ian Pearson: I do not agree that UK firms are placed in any substantial competitive disadvantage as a result of our implementation of the directive. As I understand it the Committee has received evidence from the private sector stating that their approach has been proportionate and cost effective in practice as well.

Q464 Lord Dear: Has the private sector been through to you about this directly? We have had two sources already that there is a professional view that we are disadvantaged compared with some of the other countries in the EU. Are you aware of that?

Ian Pearson: I am certainly aware of it through officials although I have not met private sector companies who have said this to me directly. Certainly if you look at the Institute of Chartered Accountants' evidence that they submitted to you they talked about the very significant improvement in the control of illegal activities that results which makes the regime cost effective. I know that they have some criticisms as well but overall they recognise that. Also the British Bankers Association talked about us doing much more in terms of maintaining our reputation in seeking out those crimes than other countries. I think they accepted that we were doing the right thing and that it is necessary to do it. Of course the approach that we adopt in the UK is very much a risk based one rather than a rules based one. Perhaps you might want to come onto that in terms of some of the questions. There are some differences in the systems. It might just be helpful if I explain our thinking here. Our approach for implementing the directive was to ensure in the first place that there is an effective end to end anti-money laundering system that is as proportionate as possible. Second, that we did not gold plate the requirements of the directive and third, to ensure that we engaged with businesses as part of discussions about how we implement the directive. We believe there has been a strong element of partnership in how we resort to implement this.

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There are always going to be some noises but I think overall businesses have accepted the risk based approach that we have taken. Having said that, the regime applies to many different businesses in many different circumstances and to ensure that it is working best for all we committed during the consultation process to review the effectiveness of the regime after two years. We will be beginning a review later this year. I think the Committee's inquiry and the evidence it is taking will helpfully feed into the review that we will want to conduct later on this year.

Q465 Lord Dear: If I understand the picture correctly from you there are fears but you do not altogether share those fears but you are going to look at it in the light of what we might propose in our report. Would that be a fair summation?

Ian Pearson: We are committed to looking at it anyway and your report will be very helpful. We think that the regime that we have introduced is broadly right and has wide support but we are happy to consider any representations made to us about whether we can further improve it.

Q466 Lord Marlesford: In the Treasury evidence submitted to us by Lord Myners in January in paragraph 21 he says, "While the FATF Recommendations do not include tax offences as a predicate crime for money laundering as some jurisdictions are opposed to this approach, the UK has an 'all crimes' approach and so is able to provide assistance in respect of money laundering offences based on predicate tax offences". One totally understands why it is attractive to HMRC to piggy-back the whole of this activity in order to help with dealing with tax avoidance which we all obviously support, but there are two points here. One is that in order to do that you have taken the all crimes approach which is much wider and secondly, of course, you are effectively, by definition and in fact quite deliberately—given that the whole regime is organised through the Serious Organised Crime Agency—putting tax evasion as a serious crime, which maybe it is. On the other hand, the sorts of things people have the image of SOCA being there for, it is slightly questionable as to whether it quite ranks with terrorism and people trafficking, drugs, stuff and all this. I suppose really my question is, in order to piggy-back it and to include tax in the whole regime, was it really necessary to have an all crimes approach which, of course, widens it even further?

Ian Pearson: We believe that the all crimes approach is the right one. The arguing within the FATF has been to include tax evasion as a predicate offence for money laundering and one of the things that has been our priority for the review has been to include that as well.

Mr Webb: This is something that was quite exhaustively gone through at the time of the Proceeds of Crime Act back in 2002. It is difficult and in many, many circumstances the banking sector will simply not know what the underlying offence is. The problem with the regime that links it to specific crimes is that it creates all kind of possible defences or arguments that this was not actually drug trafficking, it was something else and this enables people to get away with what common sense concludes, ie this is money laundering. However, it requires a whole extra layer of evidence if you require it to be linked to certain sorts of crime. We did go through the all crimes test and we believe it is the right one and broadly speaking the system will settle down.

Lord Marlesford: I will not ask now but I would like to return to this later with the implications of that approach for the database of SOCA.

Q467 Lord Hannay of Chiswick: Could I go back again to this question of comparative advantage or disadvantage? Perhaps you could break it into two and say, is it your view—which is a view which has been expressed to us by quite a number of people—that the UK applies this directive more rigorously and more effectively than many other Member States do? I must say, I would be surprised to hear that it was not your view that that was so, but obviously it is for you to say so. The second part of the question is: does the fact that we apply it more rigorously put our firms and our professions at a disadvantage? The answer to the first could be "yes" and the answer to the second could be "no" but we have not really broken that out in that way and I think it would be helpful if you could answer both parts of that question.

Ian Pearson: Yes, we do apply the directive in a rigorous way. We do it in a risk based and proportionate way which does not gold plate the directive. The way we implemented it is different from the way some other Member States implemented the directive where they have taken more of a rules based tick box approach. No, we do not believe that this puts UK firms at a competitive disadvantage. We have not seen any compelling evidence to suggest that that is the case. If I quote back the evidence that Jonathon Fisher QC gave to you he said, "Far from damaging the country's financial interests, the imposition of robust anti-money laundering and counter-terrorism procedures serves to enhance a financial centre's reputation and make it a more attractive venue for financial services than other financial centres where the compliance regime is less rigorous". As a government we broadly accept that.

Q468 Lord Faulkner of Worcester: Following on the same theme here, I would like to ask about the reliance that is contained in the Anti-Money Laundering Directive on the AML/CFT systems of

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equivalent third countries. The Fraud Advisory Panel and the Law Society have both given us evidence that the way that this is implemented is of very little value to the private sector in practice. I wonder if you could comment on that. If you agree with that, is there anything that can be done to give it greater practical relevance?

Ian Pearson: In many ways this follows on from the decision that we have just been having and I have been discussing this with officials trying to probe the extent to which the reliance in the equivalence provisions do actually benefit businesses. They are designed to do that in determining whether it is appropriate to apply simplified due diligence and whether they might be able to use both due diligence already that has been undertaken by another business. The provisions can help make transactions quicker and potentially cheaper for regulated firms. However, what I would want to say is that in providing for this we have to ensure that the overall effectiveness of the regime is not compromised. UK implementation, in line with our general approach to anti-money laundering, therefore requires firms to continue to apply a risk based approach to these provisions. There are obviously some difficulties where we are applying a risk based approach and other countries are applying a rules based approach. We want UK companies to consider other relevant factors when deciding the correct level of consumer checks. If we were to take an example, obviously if a business is doing business with a bank in the United States you would expect that we would have quite a lot of reliance on the US bank because the UK bank doing business with it would be familiar with it and the equivalence provisions and reliance means that maybe due diligence on that does not have to be as rigorous. However, it is still the case that you would need to take that risk based approach because money laundering goes on in the United States despite the fact that the United States has a good regime. It would be up to the UK entity to ensure that it continues to apply that risk based approach. I think that the way we are implementing it is the right way.

Q469 Lord Faulkner of Worcester: You really believe it does help the private sector.

Ian Pearson: I do believe that reliance and equivalence provisions are of some help to the private sector. I do not think it can be as simple as saying, “This country has got a good and robust regime, therefore you do not have to do anything”. I still think that the UK company needs to take a risk based approach to this.

Q470 Baroness Garden of Frognal: I want to move onto the question of Hawala and other alternative remittance systems. The Committee has been informed by the Home Office and SOCA of efforts to

reach out to those who are involved in these provisions and alerting them to their obligations in countering money laundering and financial terrorism. However, at present the relevant information is provided only in English. Do you agree that it is important that this information should be provided in other relevant languages? It is quite possible that many of the people using Hawala are not particularly familiar with English and, if so, will that be taken forward as a matter of urgency by the government?

Ian Pearson: You are certainly right to say that HMRC’s general approach is to provide information directed at businesses in the English language on the basis that it is command of English that is necessary in order to operate any business in the UK. However, we do recognise in certain circumstances some businesses, particularly small and micro-businesses, may need targeted support in other languages to better able them to meet their obligations. In this case assistance is given to businesses that offer money transmission services to customers in the form of a notice explaining why they may be required to produce evidence of their identity. There is a notice that can be downloaded from the HMRC website, MLR4 it is called, *Protecting society against crime and terrorism*. That can be given to customers and is available in a range of languages. The sector can request, through the Money Services Businesses Forum or through written request, customer information in an additional language. For instance, Somali and Polish translations have been produced following requests and HMRC is certainly open to receiving requests to translate this notice into other languages as well.

Q471 Baroness Garden of Frognal: Do you have a mechanism for following up those requests or is it all on-line?

Ian Pearson: As I say, it can be through a written request to the Money Services Businesses Forum and it could be on-line as well. My understanding is that HMRC are very willing to consider that if there are particular areas where there are problems. There are a range of languages in which this notice is available already—Bengali, Farsi, Hindi, Punjabi, Somali, Polish, Spanish, Urdu—and others can be added if there is a request to do so.

Q472 Lord Hannay of Chiswick: Moving away from the language aspect of Hawala to the wider aspect, although from the evidence we have had it seems that the government believes that because the Hawala operatives are regulated we have a reasonable handle on this issue in this country, when we went to Brussels we found pretty wide ignorance of the whole aspect of Hawala and whether it could be a way in which money could be laundered. There was a complete

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void as to trying to bring Hawala systems within the scope of the Money Laundering Directive in other Member States than here where they are really being brought within it by our own regulatory system. Is this not rather unsatisfactory because I do not believe that Hawala does not exist in any of the other 26 Member States; in some of them it may be quite widespread? Should we not be doing something to alert people to the potential risk in the system and the need to regulate it properly and to bring it fully within the scope of the directive?

Ian Pearson: You make a good point. I am not particularly sighted on what exactly other countries are doing with regards to Hawala and ensuring that they have robust practices. You will be aware of the standard setting approach and compliance with the directive we have taken in the United Kingdom. I would imagine that we would expect other countries to implement the directive in a similarly robust way that does address any potential risk of counter-terrorism, finance and money laundering through Hawala as well. Obviously it is up to those Member States themselves to implement the directive and to be in compliance with it. It is up to the Commissioner himself to ensure compliance with the directive and enforce it in the case of non-compliance.

Mr Robertson: I would just say that the directive obviously requires Member States to enforce regulations as regards money service businesses and Hawala clearly falls within that category. Obviously the UK, because of the nature of communities present, we potentially have, I suppose, greater exposure to Hawala because it is quite common in a number of the communities in the UK. It may just be that we are more aware and it may be that it is a greater issue for us. Certainly for any other Member States where Hawalas are operating, under the directive they ought to be treating that as a money service business, it seems to me, under the directive and they ought to be regulating it. In terms of levels of awareness, Hawala is something that has been on the agenda of the FATF for some time and different members of the EU will either be directly members of the FATF themselves or of MONEYVAL (the FATF regional style body under the Council of Europe who I think are coming to give evidence to you following this session). I have to say I am rather surprised to hear that there was that lack of awareness and that is something we can certainly go and look into and take forward discussions with the commission.

Q473 Lord Hannay of Chiswick: Presumably it would be valuable at the very least to ensure that other Member States are aware of how we are coping with this, given, as you say, that we probably have a more sophisticated involvement with Hawala than any other Member State.

Ian Pearson: I agree with that. The point is well made and we will certainly look into it.

Mr Robertson: As we speak some of my colleagues are in Brussels presenting on how we have implemented the Third Money Laundering Directive and it may be that for a future meeting of the Money Laundering Committee we could suggest we go and give such a presentation on Hawala.

Q474 Lord Avebury: It is up to the Commission to decide how to ensure that other Member States implement the directive in a manner as robust as we do ourselves. Why can we not take the initiative in asking the Commission to undertake a review to ensure that there is sufficiently robust implementation of the Hawala system in other Member States?

Ian Pearson: James' suggestion of actually explaining how we have implemented the directive and maybe having a session on Hawala as part of that is something that is useful to take forward. My understanding is that a review is planned anyway in more general terms so this is obviously something that could well be part of that review.

Q475 Lord Mawson: Are the government satisfied, in the light of the *Kadi* judgment of the European Court of Justice and the response to it in Brussels, that the relevant EU legislation is now ECHR compliant?

Ian Pearson: The Foreign and Commonwealth Office lead on this area but let me try to answer the question as best as I can and for supplementaries it might be best if I write to the Committee. In the government's opinion the EU has addressed the procedural defects identified by the ECJ in the *Kadi* judgment. Mr Kadi and Al Barakaat have been provided with narrative summaries of reasons for their listing and were provided with an opportunity to comment on the information provided. Following this, the council considered all information available and determined that Mr Kadi and Al Barakaat should be re-listed. This was done by means of a commission regulation EC number 1190/2008 of 28 November of that year. The UK has supported on-going due process improvements to the existing UN al-Qaeda and Taliban sanctions regime through the Security Council resolution 1822 adopted in June 2008. 1822 provides that the cases of all individuals and entities on the UN list should be reviewed by June 2010 and that narrative summaries of the reasons for listing should be provided for all persons named. The UN Sanctions Committee is working to provide listed individuals with summaries of the reasons for listing as soon as possible. We believe as a government that 1822 is an important step forward but we need to continue to strengthen procedures to enhance the efficiency and transparency of the regime.

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Q476 Baroness Henig: The work of FATF, a body partly funded by the UK and of which the UK recently held the presidency is central to this Committee's inquiry, but that body has actually declined to give us oral evidence. I should say that we were able to take evidence from the former British president of FATF, Sir James Sassoon, last week and actually that raised a number of very important issues which it would have been extremely valuable for us to take further directly with FATF. Should not a body whose work has a major effect on the public and private sectors in the UK and other States be answerable to the national parliaments of those states? If you agree with me that it should be answerable, what can the government do to change their attitude?

Ian Pearson: With respect I do not think that I do agree with you. Let me try to explain why I do not. I see FATF really as being a body that meets in plenary with decisions being taken through countries rather than through the secretariat of FATF. FATF is accountable to ministers and therefore indirectly accountable to Parliament. As you know, the Chancellor and other finance ministers agreed the revised mandate for it in spring 2008 and the Dutch Presidency intends to hold a future ministerial meeting on the margins of either the October 2009 or spring 2010 IMF meetings and we strongly support the proposal for that because we do believe that there has to be ministerial accountability and through ministers accountability to domestic parliaments. 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. The role of the secretariat is to serve the president and the plenary. It is not usual—and I do not think it would be right—for the secretariat to give opinions on policy matters on behalf of the FATF; this has to be the responsibility of the president and the working group co-chairs and delegations. The secretariat has 34 delegations to attend to and I think you would be quite hard pressed to expect it to give evidence to all committees of this kind. Just so this committee does not feel offended, you might be aware that the secretariat has also declined to give evidence to a US congressional inquiry for the same reasons, that it is a secretariat and the policies are actually determined in plenary or in working groups and by representatives of countries rather than the secretariat itself. I sympathise with the frustrations that the Committee has in not being able to question them directly. I do agree that there are legitimate reasons concerning what more FATF can do to improve its public outreach. Obviously there are some institutional obstacles to participating in this kind of inquiry given the resources that FATF actually has and its status. I hope the Committee understands those.

Q477 Baroness Henig: Can I pursue the logic of that? If they are accountable to governments and to ministers, which British minister is speaking on behalf of FATF? That is the implication, is it not? Do you have FATF as part of your portfolio?

Ian Pearson: The Treasury would lead on this, yes.

Q478 Baroness Henig: So if we have further questions arising from last week's evidence which we wanted to pursue we should then be directing them to you.

Ian Pearson: I am more than happy for you to direct them to me.

Q479 Lord Hannay of Chiswick: Clearly the Somali pirate problem has grown in dimensions and in urgency quite a lot while we have been conducting this inquiry. The first general question I have is, how does the government reconcile the policy where, with our right hand, we are participating in the use of military force and deploying UK naval resources to prevent piracy off the Horn of Africa with, at the same time, what seems from the evidence that we have been given and the note that was produced, a policy of effectively turning a blind eye to monies being paid from the UK—indirectly perhaps—as ransom to the pirates and then, for all we know, being directed to terrorism?

Mr Campbell: I will deal with the right hand first which is our military and naval commitment which is entirely consistent with our responsibilities under international law on piracy. We respect our obligations to the United Nations in this regard but also work with NATO partners and indeed our EU partners too. What we also accept is that tackling piracy—which is a multi-faceted problem—requires a multi-faceted approach beyond the force that we bring to bear on the problem. We played a leading role in January of this year in setting up the contact group on piracy off the coast of Somalia which has the expressed aim of getting better international cooperation on this matter but also I think exploring some of the difficult aspects of the problem. I say at this point that the issue of ransom payments is one of those difficult problems. The United Kingdom does not condone the payment of ransom but it is not illegal under British law and therefore the decision whether or not to pay ransom is one for the shipping company and its insurers to assess. These are very complex issues that are often fast moving and I think we should acknowledge the difficulty that it places both the ship owners and the insurers in, let alone the people who are actually caught up immediately in it. I expect that the contact group will pay particular note to the issue of ransom payment, what we can do to tackle it and whether or not there is a better way in which we can deal with it. In respect of your reference to terrorism, we keep this under review and there is no

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direct evidence of the proceeds of piracy being directed towards terrorism. That would, of course, lift it to an entirely different level because if that were the case then any payment of ransom would be illegal under the Terrorism Act 2000 which criminalises the financing of terrorism. In those circumstances, before an organisation was to pay ransom, they would have to approach our Serious Organised Crime Agency for consent to make such a payment. However, as I say, we have not found any direct evidence of that link but we continue to keep this under close scrutiny.

Q480 Lord Hannay of Chiswick: When you say you have not found it, that merely reflects the fact that presumably we have extremely poor ways and resources for finding out what on earth is going on in Somalia, what purposes the pirates, when they get the monies, put them to; and since our absence of knowledge of this is, I would have thought, fairly profound, it would seem to be a fairly shaky base on which to say that we believe it is not going to terrorism.

Mr Campbell: I have been careful not to say that it is not going to terrorism. What I have said is that we have not found a direct link to that. Of course I understand the particular reference to Somalia which has had a difficult modern history as a failed state and its widely acknowledged links to terrorism. Unusually this issue arises but, as I say, we do keep this under close scrutiny and we do seek evidence upon which to base our response and indeed our policy responses. I assure you that we do keep it under close scrutiny.

Q481 Lord Marlesford: You will I am sure agree that whether or not terrorism is involved the act of piracy is a criminal act and the payment of ransom is therefore inextricably connected with that act. What I find curious is that in the note which you have submitted on this issue on 6 April you say that under the regime whereby consent from SOCA is required to fulfil certain operations financially which might be criminal, “consent may be required when assembling money in order to provide a defence to the money laundering offence under section 328(1) of the Proceeds of Crime Act”. I find it hard to think of an example of where it is not necessary to obtain consent because, after all—I quote from the SOCA evidence of 17 April 2009—“The Proceeds of Crime Act 2002 requires the reporting of an activity that makes a person suspicious”. Surely it is inconceivable that it is possible for consent not to be required, in other words for an SAR report not to be made by those who are approached to assemble money for the payment of ransom.

Mr Campbell: It would be very clear were there direct evidence of links with terrorism.

Q482 Lord Marlesford: We are talking about piracy.

Mr Campbell: Yes. It would be clear but the point I am making is that it is less clear in other situations. I think this takes us into the issue of where SOCA fits in here because, to some extent, the law as it stands put them in a slightly difficult situation. They have an obligation to say to organisations that if they believe that there is a suspicious activity it ought to be reported and this is how to do it. I think that is different, however, to getting consent. I think the best approach is the one that we have, which is to deal with these instances one at a time and to look at each individual case. I am sure that is what SOCA does because although there is something called piracy it may not have all of the same characteristics each time that it occurs and therefore there would not be an obligation under law to seek consent in every situation. I think if there is an obligation to raise concerns about suspicious activity SOCA could be put in a difficult position if it was seen to be giving consent in some circumstances. If it was to proceed to a court situation, for example, and if the organisation that had made the payment had reasonable grounds for doing so, then the statute allows them that as a defence in court. I think we have to be careful that SOCA does not pre-judge and, by giving consent, does not seek to pre-judge a decision which is quite rightly one that should be taken by the courts.

Q483 Lord Marlesford: I think you are agreeing that the law as it is at present requires that anyone who is involved in assembling ransom money in respect of the criminal act of piracy is obliged to ask SOCA for consent. What you are saying is that it would be embarrassing if this was done. That is a totally different matter and I would suggest to you that it really is quite important that we maintain the principle of the law. It may be that the law needs changing in this respect but I cannot understand how you can say that it is not actually necessary for the insurance people to report to SOCA that they are doing this and ask for consent to do it.

Mr Webb: The law is quite a grey area here. It is not generally the government’s job to define the law precisely. If it ever came to that it would be something for the courts to decide and we would not want to pre-empt their judgment. What is clear is that if an insurance company or a shipping firm collected money for a ransom payment the money would be from their own internal resources, it would not be criminal money. If they were preparing it for the payment of a ransom which is not a criminal offence, further down the track the money would fall into the hands of criminals and would become obviously their criminal property. The issue is around the definition of making an arrangement assisting facilitation for what at some stage is going to become criminal money. The basic purpose of the Proceeds of Crime

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Act and the regime is suspicion that can be aroused by transmission of criminal property around the system. As I say, if these actions happen, say, in London, it is not actually criminal property.

Q484 Lord Faulkner of Worcester: I want to ask Mr Campbell or Mr Webb whether they can add anything to the answer that Lord Malloch-Brown gave to sub-Committee C on the question of whether money that is paid in ransom is noted. In other words, the serial numbers of any notes which are passed over are noted down and retained and if an attempt is made later to use that money it is possible to trace it.

Mr Webb: I think it would be an operational matter; it would not be sensible of us to say anything one way or the other on that for obvious operational reasons.

Q485 Lord Faulkner of Worcester: Lord Malloch-Brown said, “I think yes would be a reasonable assumption”. You would not even go as far as that.

Mr Webb: I would not go any further than what I have just said.

Q486 Lord Hannay of Chiswick: If I may say so, some of the replies get close to the sophistical in this matter and it really is necessary to get to the heart of this matter. Nobody in this Committee is trying to challenge the law as it currently is, that it is not criminal to pay a ransom. We are trying to get to the bottom of the application of money laundering provisions which require a notification if there is any reason to believe that monies are going to be transferred to a person or purpose which could be criminal. I think you will agree with that. Thus, irrespective of whether it is legal to transfer this money, it is necessary to notify it. The department has said that consent “may be” required, not “will be” required—that is the point Lord Marlesford made—and then went on to say, “In the event that a person did not seek consent and the money was in all respects legal until it reached the hands of the pirates, it is unlikely that a prosecution for money laundering solely because consent was not obtained would be regarded as being in the public interest”. This is surely perfectly straightforwardly turning a blind eye to the non-application of the requirement that you should notify any payment which you believe could end up in criminal hands. There is absolutely no shadow of doubt that the act of piracy is a crime. It is a crime under international law and has been since the middle of the 19th century. Is this not a case where we really do need to re-think what we are doing or otherwise

we are pursuing incoherent policies? We are trying to stop the pirates by steaming around in the Royal Navy but at the same time making it about as easy as it can possibly be for money in large amounts to be transferred into their hands.

Mr Webb: I understand your frustration and the reason we are not being more forthright about this is because the law is genuinely quite a grey area. I am not a QC or a lawyer at all and it is something I would not like to lay down exactly what I think about it. I do not think it is as crystal clear as you say; it will depend on the circumstances of the case that there may be a reporting requirement. As for the prosecution decisions, those will be done on a case by case basis on the merits of the case. We are continuing to look at this but it is quite a complex area of law and it is quite a complex area of unintended consequences of the law.

Q487 Chairman: Could you give us a note your analysis of what the legal position is.

Mr Webb: We have attempted to do that but we will have another look at it.

Q488 Lord Avebury: I would like to know whether ministers do not agree that the law must be clarified. The law, as stated by Lord Hannay, should be the law of the land and if there is any doubt about it you will make sure that it is.

Ian Pearson: I cannot speak for the Home Office but what I would want to say is that we are taking action on a number of fronts. These Somali pirates are not Captain Jack Sparrows that follow a particular code; we do not have any good information about where the ransom money is spent, we suspect it is spent on even fast boats and even more weaponry, bling and the sorts of things that Captain Jack Sparrow’s pirates spent money on as well. We do not really see that there is a particular role for the FATF as a standard setting body in this area. We would like them to work with a functioning Somali government to set the proper standards in that country, but obviously that is not possible at the moment. The FATF is not an operational body. You have asked a number of questions and we will respond to them as fully as we can.

Chairman: Thank you very much indeed. It is now 11.36. I think that is where we had better leave this session. Can I thank you very much indeed for coming. I think it has been very useful and very helpful. You have given us a fair amount of evidence which we will want to chew over and we look forward to receiving your evidence in writing.

Supplementary memorandum (6) by the Home Office

This memorandum provides further information on the following instruments: the 2001 Protocol to the EU MLA Convention; the 2001 Second Additional Protocol to the Council of Europe MLA Convention, and the 2005 Warsaw Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime and on the Financing of Terrorism.

2001 PROTOCOL TO THE EU MLA CONVENTION OF 2000

- This Protocol is in force for the UK but it has not been ratified as yet by all EU Member States.
- The Protocol was originally signed on 16 October 2001.
- The UK deposited its instrument of accession to the Protocol on 15 March 2006. The Protocol entered into force for the UK 90 days later on the 13 June 2006.
- The Protocol initially entered into force on 5 October 2005.
- The below table shows the dates States deposited their notifications of accession and the date the Protocol entered into force for them. It also shows the States yet to accede to the Protocol.

<i>Party</i>	<i>Notification</i>	<i>Entry into force(*)</i>
Austria	04/04/2005	05/10/2005
Belgium	25/05/2005	05/10/2005
Bulgaria	08/11/2007	01/12/2007
Cyprus	03/11/2005	01/02/2006
Czech Republic	14/03/2006	12/06/2006
Germany	04/11/2005	02/02/2006
Denmark	01/03/2005	05/10/2005
Estonia		
Spain	05/01/2005	05/10/2005
France	10/05/2005	05/10/2005
United Kingdom	15/03/2006	13/06/2006
Greece		
Hungary	25/08/2005	23/11/2005
Italy		
Ireland		
Lithuania	28/05/2004	05/10/2005
Luxembourg		
Latvia	14/06/2004	05/10/2005
Malta	04/04/2008	03/07/2008
Netherlands	02/04/2004	05/10/2005
Portugal	12/12/2006	12/03/2007
Poland	28/07/2005	26/10/2005
Romania	08/11/2007	01/12/2007
Sweden	07/07/2005	05/10/2005
Finland	21/02/2005	05/10/2005
Slovenia	28/06/2005	05/10/2005
Slovakia	03/07/2006	01/10/2006

2001 SECOND ADDITIONAL PROTOCOL TO THE 1959 COUNCIL OF EUROPE CONVENTION ON MLA

- The UK has signed but not ratified this Protocol.
- We are currently moving towards ratification and we would expect to do so this year.
- The table below shows the dates that States signed and ratified this Protocol along with the date it entered into force.

<i>States</i>	<i>Signature</i>	<i>Ratification</i>	<i>Entry into force</i>
Albania	13/11/2001	20/6/2002	1/2/2004
Andorra			
Armenia			
Austria			
Azerbaijan			
Belgium	8/11/2001		
Bosnia and Herzegovina	17/5/2006	7/11/2007	1/3/2008
Bulgaria	8/11/2001	11/5/2004	1/9/2004
Croatia	9/6/2004	28/3/2007	1/7/2007
Cyprus	8/11/2001		
Czech Republic	18/12/2003	1/3/2006	1/7/2006
Denmark	8/11/2001	15/1/2003	1/2/2004
Estonia	26/11/2002	9/9/2004	1/1/2005
Finland	9/10/2003		
France	8/11/2001		
Georgia			
Germany	8/11/2001		
Greece	8/11/2001		
Hungary	15/1/2003		
Iceland	8/11/2001		
Ireland	8/11/2001		
Italy			
Latvia	24/9/2003	30/3/2004	1/7/2004
Liechtenstein			
Lithuania	9/10/2003	6/4/2004	1/8/2004
Luxembourg	30/1/2008		
Malta	18/9/2002		
Moldova			
Monaco			
Montenegro	7/4/2005	20/10/2008	1/2/2009
Netherlands	8/11/2001		
Norway	8/11/2001		
Poland	11/9/2002	9/10/2003	1/2/2004
Portugal	8/11/2001	16/1/2007	1/5/2007
Romania	8/11/2001	29/11/2004	1/3/2005
Russia			
San Marino			
Serbia	7/4/2005	26/4/2007	1/8/2007
Slovakia	12/5/2004	11/1/2005	1/5/2005
Slovenia	7/4/2005		
Spain			
Sweden	8/11/2001		
Switzerland	15/2/2002	4/10/2004	1/2/2005
the former Yugoslav Republic of Macedonia	8/11/2001	16/12/2008	1/4/2009
Turkey			
Ukraine	8/11/2001		
United Kingdom	8/11/2001		

Non-member States of the Council of Europe

<i>States</i>	<i>Signature</i>	<i>Ratification</i>	<i>Entry into force</i>
Israel		20/3/2006 a	1/7/2006

THE EU-US AGREEMENT

- The EU and US signed this Agreement on 25 June 2003.
- The provisions of that Agreement requires the US to conclude and ratify bilateral mutual legal assistance treaties, or Instruments, with each individual Member state, including any who acceded following the Agreement being signed. This is in order to ensure that the assistance envisaged by the Agreement was included in member States' bilateral treaties with the US.
- This involves 27 different State each negotiating a treaty or Instrument with the US and is clearly a time-consuming process, but one the US asked for.
- The UK and US signed an Instrument on 16 December 2004 in order to comply with all provisions of the EU-US Agreement. This will shortly be ratified.
- Prior to ratification of the Instrument the all necessary legislation needed to be updated. This has now been completed (August 2008) and we are moving towards ratification.
- We expect that the EU-US Agreements will be concluded in late June.

WARSAW CONVENTION 2005 (CETS 198)

- Entry in force for this Convention was 1 May 2008. The United Kingdom has not yet signed the Convention.
- The table below sets out the current position of Member States and others with regard to this Convention.

Council of Europe Convention on laundering: CETS 198 (as of 01.05.2009)

Member States of the Council of Europe

<i>States</i>	<i>Signature</i>	<i>Ratification</i>	<i>Entry into force</i>
Albania	22/12/2005	6/2/2007	1/5/2008
Andorra			
Armenia	17/11/2005	2/6/2008	1/10/2008
Austria	16/5/2005		
Azerbaijan			
Belgium	16/5/2005		
Bosnia and Herzegovina	19/1/2006	11/1/2008	1/5/2008
Bulgaria	22/11/2006		
Croatia	29/4/2008	10/10/2008	1/2/2009
Cyprus	16/5/2005	27/3/2009	1/7/2009
Czech Republic			
Denmark			
Estonia			
Finland	16/12/2005		
France			
Georgia			
Germany			
Greece	12/10/2006		
Hungary	14/4/2009	14/4/2009	1/8/2009
Iceland	16/5/2005		
Ireland			
Italy	8/6/2005		
Latvia	19/5/2006		
Liechtenstein			
Lithuania			
Luxembourg	16/5/2005		
Malta	16/5/2005	30/1/2008	1/5/2008
Moldova	16/5/2005	18/9/2007	1/5/2008
Monaco			
Montenegro	16/5/2005	20/10/2008	1/2/2009
Netherlands	17/11/2005	13/8/2008	1/12/2008
Norway			

<i>States</i>	<i>Signature</i>	<i>Ratification</i>	<i>Entry into force</i>
Poland	16/5/2005	8/8/2007	1/5/2008
Portugal	16/5/2005		
Romania	16/5/2005	21/2/2007	1/5/2008
Russia	26/1/2009		
San Marino	14/11/2006		
Serbia	16/5/2005	14/4/2009	1/8/2009
Slovakia	12/11/2007	16/9/2008	1/1/2009
Slovenia	28/3/2007		
Spain	20/2/2009		
Sweden	16/5/2005		
Switzerland			
the former Yugoslav Republic of Macedonia	17/11/2005		
Turkey	28/3/2007		
Ukraine	29/11/2005		
United Kingdom			

Non-member States of the Council of Europe

<i>States</i>	<i>Signature</i>	<i>Ratification</i>	<i>Entry into force</i>
Canada			
Holy See			
Japan			
Mexico			
United States			

International Organisations

<i>Organisations</i>	<i>Signature</i>	<i>Ratification</i>	<i>Entry into force</i>
European Community	2/4/2009		

May 2009

Memorandum by MONEYVAL

Anti money laundering and countering terrorist financing (AML/CFT) are priority areas for the Council of Europe. Our work in the European and global fight to combat money laundering and terrorist financing is concluded at three levels:

- as a standard setter through our anti money laundering and terrorist financing Conventions (the Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime and on the Financing of Terrorism, and our other major conventions covering international co-operation; the 1957 European Convention on Extradition and its two protocols, and the 1959 European Convention on Mutual Assistance in Criminal Matters).
- as a monitor of international standards through MONEYVAL
- as a major provider of technical assistance in this area, often based on the recommendations of MONEYVAL.

Christos Giakoumopoulos
Director of Monitoring

John Ringguth
Executive Secretary to MONEYVAL

I THE COUNCIL OF EUROPE MISSION ON MONEY LAUNDERING AND FINANCING OF TERRORISM

For many years the Council of Europe has promoted domestic action against money laundering in the context of its fight against organised crime. One estimate suggests that most of the billions laundered world-wide is laundered by or on behalf of organised crime groups. Money laundering is said to provide them with their cash flow and investment capital, and fighting money laundering effectively is a major tool with which States can combat organised crime. Money laundering prosecution and deterrent confiscation orders can significantly deprive organised crime of their profits, and disrupt their activities.

The Council of Europe has had a long engagement with the anti-money laundering issue. It was the first international organisation to seriously address the issue. In 1980, the Council of Europe adopted the first international instrument against money laundering [Recommendation No R (80) 10 on measures against the transfer and the safe-keeping of funds of criminal origin]. Since then the Council of Europe has developed its activities on three fronts: as a standard setter, through two international conventions; as a monitor of the effectiveness of anti-money laundering (and now also the countering of financing of terrorism measures) through the MONEYVAL mechanism, under which 29 States are currently evaluated; and as a major provider of technical assistance in this area to non EU member States.

II STANDARD SETTING

The Strasbourg Convention 1990 (ETS No.141)

The 1990 Council of Europe Convention on Laundering Search, Seizure and Confiscation of the Proceeds from Crime (ETS No 141) remains a landmark treaty, which forms an important corner-stone of international anti-money laundering standards. It is a hard law instrument. Currently 48 States are party to this treaty, including all 47 Council of Europe member States and one non-member State (Australia).

The Convention provides a complete set of rules covering all stages of the procedures from investigation to confiscation in domestic criminal cases which generate major proceeds and criminalises money laundering on a wide basis. It also places a positive obligation on States to co-operate with each other “to the widest extent possible” for the purposes of investigations and proceedings aimed at confiscating instrumentalities or proceeds.

“Proceeds” from crime, in the domestic context (and for international co-operation purposes) is also given a very wide definition under the Convention (“any economic advantage from criminal offences”—thus the definition covers both direct and indirect proceeds).

The Convention recognises the links between confiscation and money laundering. Identifying and breaking money laundering schemes should, in an ideal world, lead financial investigators to the real proceeds of crime, that is to say the “indirect” proceeds, the substitutes, the investment yields that make organised crime so profitable.

The Convention invites States to criminalise money laundering domestically on as wide a basis of underlying (predicate) criminal offences as possible. While States are allowed to make declarations that the money laundering offence can apply only to listed offences or categories of offence, States are implicitly encouraged by the Convention to legislate on an “all-crimes” basis and many States have done so. This is helpful to countries domestically, and also assists in permitting a State to provide wide international co-operation on money laundering offences, where dual criminality is required.

The 1990 Convention gives States the legal basis to create wide criminal confiscation regimes domestically, which cover both property and value based confiscation. It provides a positive obligation on States to enact domestic legislation to enable them to confiscate instrumentalities and proceeds (or property the value of which corresponds to proceeds). Similarly it places an obligation on States to have in place effective provisional measures regimes (such as seizing and freezing) to ensure that proceeds are not dissipated before confiscation orders are made.

One of the primary purposes of the Convention is to facilitate international co-operation. Parties are required to afford each other the “widest possible measure of assistance” (judicial co-operation and police to police co-operation at the investigative stage into criminal offences or for investigations for the purposes of confiscation). The 1990 Convention goes further than the 1959 Council of Europe Convention on Mutual Assistance in Criminal Matters, as it allows for police to police co-operation, permits direct contact between competent authorities when no coercive action is involved (Article 24), and covers the provision of spontaneous information relating to proceeds and instrumentalities where this might be of practical assistance, without a prior request (A 10). There is great potential in these provisions to improve the speed and effectiveness of law enforcement.

At the judicial level, Article 14 places an obligation on State parties to confiscate instrumentalities and proceeds on request and Article 11 provides an obligation to take provisional measures on behalf of another Party which has instituted criminal proceedings or proceedings for confiscation. This is vital, as it is well known that major criminals hide their assets outside their own jurisdictions.

THE COUNCIL OF EUROPE CONVENTION ON LAUNDERING, SEARCH, SEIZURE AND CONFISCATION OF THE PROCEEDS FROM CRIME AND ON THE FINANCING OF TERRORISM 2005 (CETS No. 198)

Overview

The Strasbourg Convention has recently been wholly revised and a new treaty was opened in May 2005 at the Warsaw Summit of Heads of State and Government of the Council of Europe. Many of the provisions in the 1990 Convention remain in the 2005 Convention. Moreover, the drafters of the Convention were careful to ensure that the Convention takes due account of other applicable international standards, in particular the Recommendations adopted by the Financial Action Task Force. The 2005 Convention came into force on 1 May 2008, when six States had ratified it. The 1990 Convention remains in force. Currently, 11 States have ratified CETS 198 and there are 20 signatures not followed by ratification. It is understood that ratification procedures are currently underway in several EU States that have not yet ratified it. As noted in the European Commission's submission to this inquiry, it is anticipated that the European Community will accede to the Convention shortly.

There are many new features in the 2005 Convention. The scope of its application covers both money laundering and financing of terrorism. For reasons that are well known, financing of terrorism has assumed considerable importance in recent years, and the 1990 Convention did not apply to it. Specifically, with regard to international co-operation on terrorist financing, the new Convention ensures that financing of terrorism cannot ever be considered a political or fiscal offence, thereby justifying a refusal of co-operation under the 2005 Convention.

Preventive measures have also, for the first time, been incorporated (including questions relating to the postponement of suspicious transactions both nationally and internationally). Important investigative powers are covered, including those that deal with requests for historic information on banking transactions and prospective requests for monitoring of banking transactions (both of which can be particularly helpful in asset tracing and following the money trail domestically and internationally). Other important changes in the context of money laundering criminalisation and confiscation are introduced to better assist effective implementation of these measures. Notably, the possibility to make declarations limiting money laundering criminalisation (and confiscation) to short lists of criminal offences has been reduced. A lengthy list of categories of offence which must be covered in domestic money laundering and confiscation provisions is in Appendix 1 to the Convention. A new, modern provision on corporate liability has been inserted. Several of the improvements are derived from the Council of Europe's experience through the MONEYVAL evaluation process.

The Convention comprehensively addresses the issue of financial intelligence units (FIUs), which were unknown in 1990.

A definition of an FIU is now provided for in this treaty. An FIU is defined in Article 1, according to the definition utilised by the Egmont Group¹. Article 12 requires State parties to establish an FIU, which has access directly or indirectly on a timely basis to the financial, administrative and law enforcement information it requires to properly undertake its functions, including the analysis of suspicious transaction reports.

Article 46 in Chapter V firstly requires FIUs to cooperate with each other. The purpose of FIU co-operation in the context of this Convention is to combat money laundering and terrorist financing.

The Convention then sets out the principles of information exchange.

It makes no distinction in respect of co-operation between different types of FIU. The drafters were anxious that a situation should be avoided whereby FIUs were only allowed to cooperate with counterpart units of a similar internal status, as has frequently been the case in the past. Paragraph 3 of Article 46 ensures co-operation between all types of FIU, whether they are law enforcement, administrative or judicial types of FIU. Moreover, information exchange can be spontaneous or on request.

¹ "A central national agency responsible for receiving (and, as permitted, requesting), analysing and disseminating to the competent authorities, disclosures of financial information concerning suspected proceeds and potential financing of terrorism, or required by national legislation or regulation, in order to combat money laundering and financing of terrorism." The Egmont Group is an international network of FIUs which are recognised as meeting the Egmont definition of an FIU.

The drafters of this Convention underlined that the provision concerning FIUs was different from the ones generally concerning mutual legal assistance requests. They therefore noted that the general grounds for refusal in the Convention apply only to mutual legal assistance requests and do not apply to the provision concerning FIU co-operation.

When a request is made under Article 46 a brief statement of the relevant facts known to the requesting FIU is required. The requested FIU shall provide all requested information including accessible financial information and requested law enforcement data without the need for a formal letter of request under applicable conventions. An FIU may refuse to divulge information which could impair their own domestic investigations or in exceptional circumstances—where divulging the information would be clearly disproportionate to the legitimate interests of a natural or legal person or the Party concerned, or would otherwise not be in accordance with fundamental principles of national law of the requested party. Any refusal has to be explained.

Information or documents obtained under this article shall only be used for investigation and analysis by the receiving FIU and shall not be disseminated to a third party or used for purposes other than analysis, without the prior consent of the supplying FIU.

Paragraph 9 of Article 46 establishes the specific use of transmitted information or documents for criminal investigation or prosecution purposes—subject to consent—which may not be refused unless for justified reasons, mainly restrictions under national law.

These are all very positive measures now enshrined in an international instrument. However there is an additional provision which will also be important for speedy law enforcement responses on money laundering and financing of terrorism. Article 47 provides for international co-operation on the postponement of transactions. It requires provisions to be put in place by States to permit urgent action to be initiated by an FIU at the request of a foreign FIU to postpone a suspicious transaction if they are satisfied that it is related to money laundering or terrorist financing, and it would have suspended the transaction had it been reported domestically.

Finally, in the context of this inquiry, it is noted that A.52 paragraph 4 contains a so-called “disconnection clause” which ensures that members of the European Union apply Community and European rules in their mutual relations, without prejudice to the object and purpose of this Convention and without prejudice to its full application with other parties.

III MONITORING

MONEYVAL: A European monitoring mechanism applying global and European standards

In September 1997, the Committee of Ministers established the Select Committee of Experts on the Evaluation of Anti-Money Laundering Measures (“PC-R-EV”, now known as “MONEYVAL”) 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 Financial Action Task Force (FATF) [the G 7-created body which is the primary global standard setter on anti-money laundering (and now financing of terrorism) issues.

MONEYVAL’s terms of reference were quickly extended in the aftermath of the events of 11 September 2001 to include the financing of terrorism. The fight against terrorism generally is a major Council of Europe priority, and financing of terrorism is a part of this. The present MONEYVAL mandate is annexed.

The MONEYVAL process was based on the practices and procedures of the FATF. MONEYVAL is one of the leading “FATF-style” regional bodies (FSRBs), which take forward the global anti-money laundering message and mutual evaluation beyond the FATF membership. In 2005 the FATF pursued an initiative by which it offered the status of Associate Member of the FATF to FSRBs which met particular criteria. In 2006 the Committee of Ministers of the Council of Europe authorised an application by the Council of Europe/MONEYVAL for Associate Membership of FATF. MONEYVAL became an Associate Member in 2006 in the first set of FSRB accessions to Associate Member status. Associate Membership allows more of MONEYVAL’s membership to participate actively in the work of FATF and to provide input into FATF policy making.

MONEYVAL actively participates in all the FATF Working Groups and plenary meetings through a delegation comprising the President and Executive Secretary of MONEYVAL, and up to five MONEYVAL member States. The Council of Europe/MONEYVAL in 2007 hosted a joint FATF/MONEYVAL plenary meeting in Strasbourg, where reports from both bodies were discussed and adopted jointly for the first time. MONEYVAL States have hosted joint FATF/MONEYVAL typologies meetings in 2004 and 2008. The FATF Secretariat and FATF countries have observer status in MONEYVAL. In this context the United Kingdom

has always been an active participant in MONEYVAL's work since MONEYVAL's inception. As well as participating in each MONEYVAL plenary, the United Kingdom has supported MONEYVAL's activities generously through secondments to its Secretariat, financial voluntary contributions to MONEYVAL's budget, and through the provision of expert evaluators in MONEYVAL's onsite assessments. This continuing support of MONEYVAL's work is greatly appreciated by the Council of Europe. Two FATF States are also nominated by the FATF President to be full members of MONEYVAL for two year periods without being evaluated by MONEYVAL (currently France and the Netherlands). One MONEYVAL State, the Russian Federation, is a member both of MONEYVAL and the FATF.

MONEYVAL's membership covers European countries both within the European Union and outside the European Union. 28 Council of Europe member States are evaluated by MONEYVAL². Additionally, the Committee of Ministers accepted in January 2006 the request of a non-member State, Israel, to join MONEYVAL as an observer undergoing evaluation. Israel has now been evaluated by MONEYVAL. In the context of the European Union, FATF evaluates 15 Member States and MONEYVAL evaluates 12 Member States.

MONEYVAL undertook two rounds of evaluations between 1998 and 2004. Horizontal reviews of the progress of MONEYVAL States at the end of each of the first two rounds of evaluations were produced and are available on the MONEYVAL website: <http://www.coe.int/moneyval>

In January 2005, MONEYVAL commenced its third round of evaluations using the very detailed anti-money laundering/countering the financing of terrorism (AML/CFT) Methodology, agreed in 2004 by the FATF, the FSRBs, the International Monetary Fund (IMF) and the World Bank, which is based on the 2003 revised 40 FATF Recommendations and the 9 Special Recommendations on Terrorist Financing. The third round of evaluations focuses on the effectiveness of the legal, financial and law enforcement measures in place to combat both money laundering and financing of terrorism. All reports contain ratings tables against each of the FATF 40 Recommendations and the 9 Special Recommendations, together with action plans for improvements to national systems.

The IMF and the World Bank can accept MONEYVAL evaluations, as the AML/CFT components in their own comprehensive financial sector assessments in MONEYVAL States.

MONEYVAL's and the FATF's evaluation rounds are not exactly aligned. MONEYVAL will complete its third round evaluations this year, while the FATF third round will continue until approximately 2011. Accordingly, MONEYVAL has, having coordinated with the FATF, decided to conduct a fourth round of shorter, more focused evaluations. These onsite visits will commence in the second half of 2009, following up and reassessing some of the key and important FATF standards, and reassessing the Recommendations which received low ratings in the third round. MONEYVAL's experience with shorter evaluation reports in the coming cycle may help to inform the FATF's own processes, as it considers how any fourth round evaluations by FATF might be conducted. MONEYVAL considers that, before any FATF fourth round, it is timely to reflect on the size and extent of reports that all the assessment bodies are producing, and whether the reports are sufficiently accessible and user-friendly.

Additionally, since its inception, MONEYVAL, uniquely among the AML/CFT assessment bodies, has had the European Union Directives in its terms of reference. For most of the Third round of evaluations, MONEYVAL has included assessments on the two Directives 91/308/EEC and 2001/98/EC. However, from 1 January 2008, MONEYVAL began on-site examinations of all its countries (whether EU members or not) also on the basis of the Third Directive of the European Union (2005/60/EC) and the relevant Implementation Directive 2006/70/EC. A specific additional questionnaire has been prepared covering EU issues where the Third Directive standards depart from FATF standards, and which now forms the basis of a separate appendix to the published evaluation report. No ratings are applied on the EU standards. The fourth round of evaluations will also track progress against the standards embodied in the Third Directive of the European Union and the relevant implementing Directive.

MONEYVAL decided in November 2006 that publication of its third round reports should be automatic. Though no country had ever declined to have its third round report made public, MONEYVAL's Rules of Procedure now ensure that there is no opportunity for any country to decline publication.

MONEYVAL reports are regularly used as the blueprints for technical assistance programmes provided under the auspices of the Council of Europe.

² MONEYVAL has 28 member States: Albania, Andorra, Armenia, Azerbaijan, Bosnia and Herzegovina, Bulgaria, Croatia, Cyprus, Czech Republic, Estonia, Georgia, Hungary, Latvia, Liechtenstein, Lithuania, Malta, Moldova, Monaco, Montenegro, Poland, Romania, Russian Federation, San Marino, Serbia, Slovakia, Slovenia, "the former Yugoslav Republic of Macedonia", and Ukraine. In January 2006, the Committee of Ministers agreed to Israel's request to become an observer State undergoing evaluation.

MONEYVAL follow-up

MONEYVAL has a very developed system of follow-up procedures. One year after the adoption of an evaluation report, a detailed progress report is provided by the country which is subject to analysis by a rapporteur country, followed by peer review by the Committee in plenary. If progress is satisfactory, then the progress report is adopted and published, and updated every two years between evaluation rounds.

MONEYVAL has in its Rules of Procedure a flexible system of “Compliance Enhancing Procedures³” (CEPs). These procedures have been successfully invoked on several occasions over three rounds of evaluations to enforce the standards or to deal with urgent situations which give rise to AML/CFT concerns.

CEPs can also be used in the context of progress reports where progress is too slow or unsatisfactory. MONEYVAL has applied CEPs particularly on legislative inaction or in respect of legislation which conflicts with AML/CFT standards. It is noted that on 12 December 2008, MONEYVAL issued a public statement under Step VI of the CEPs in respect of one of its members (Azerbaijan⁴).

Conference of the Parties

Unlike the 1990 Convention, CETS No. 198 creates a monitoring mechanism. The implementation of the Convention will be monitored by a Conference of the Parties (COP). The first COP will be held on 22-23 April 2009. Further information on the development of monitoring procedures under the Convention can be provided during oral evidence in the light of the conclusions of the first COP. It should be perhaps noted that the intention of the drafters of the Convention was that the COP should not duplicate the work of the existing monitoring mechanisms, and that the COP should take into account the results of monitoring undertaken by FATF and MONEYVAL, where the standards in the Convention replicate the standards in the FATF 40 Recommendations and 9 Special Recommendations.

IV INTERNATIONAL CO-OPERATION ISSUES

The following section draws on adopted and published⁵ third round reports by MONEYVAL in respect of MONEYVAL European Union countries, covering some of the issues on which the Committee requested evidence.

The relevant recommendations referred to are the FATF Recommendations 36-40 on International Co-operation. A table is provided beneath of the ratings given for each Recommendation by MONEYVAL in respect of its EU member countries.

It is followed by an analysis of MONEYVAL’s findings on each of these Recommendations.

Statistics

<i>Members who are also EU Member States</i>	<i>Date of Report</i>	<i>FATF R. 36</i>	<i>FATF R. 37</i>	<i>FATF R. 38</i>	<i>FATF R. 39</i>	<i>FATF R. 40</i>	<i>FATF SR. V</i>
BULGARIA	2008	Compliant	Compliant	Largely Compliant	Compliant	Compliant	Compliant
CYPRUS	2006	Largely Compliant	Compliant	Compliant	Compliant	Largely Compliant	Largely Compliant
CZECH REPUBLIC	2007	Largely compliant	Compliant	Largely compliant	Largely compliant	Largely Compliant	Largely Compliant
ESTONIA	2008	Largely compliant	Largely Compliant	Largely compliant	Largely Compliant	Largely Compliant	Largely Compliant
HUNGARY	2005	Compliant	Compliant	Compliant	Compliant	Compliant	Compliant
LATVIA	2006	Compliant	Compliant	Partially Compliant	Compliant	Largely Compliant	Partially Compliant
LITHUANIA	2006	Compliant	Compliant	Largely compliant	Compliant	Partially Compliant	Compliant
MALTA	2007	Compliant	Compliant	Compliant	Compliant	Compliant	Compliant
POLAND	2007	Largely compliant	Largely Compliant	Largely compliant	Largely Compliant	Largely Compliant	Partially Compliant
ROMANIA	2008	Largely compliant	Compliant	Largely compliant	Compliant	Compliant	Largely Compliant

³ A graduated series of steps to ensure compliance with MONEYVAL’s reference documents.

⁴ An updated Statement on Azerbaijan was issued on 20 March 2009, and appears on the MONEYVAL website.

⁵ All adopted third round reports are published no later than one month after adoption (www.coe.it/moneyval)

<i>Members who are also EU Member States</i>	<i>Date of Report</i>	<i>FATF R. 36</i>	<i>FATF R. 37</i>	<i>FATF R. 38</i>	<i>FATF R. 39</i>	<i>FATF R. 40</i>	<i>FATF SR. V</i>
SLOVAK REPUBLIC	2006	Largely compliant	Partially compliant	Partially compliant	Largely Compliant	Largely Compliant	Partially Compliant
SLOVENIA	2005	Compliant	Compliant	Largely Compliant	Compliant	Largely Compliant	Compliant
Compliant		6	9	3	8	5	5
Largely Compliant		6	2	7	4	6	4
Partially Compliant		-	1	2		1	3

Recommendation 36—Mutual legal assistance in AML/CFT investigations, prosecutions and related proceedings

Recommendation 36 requires that countries should be able to provide the widest range of mutual legal assistance in AML/CFT investigations, prosecutions and related proceedings in a timely, constructive and effective manner without subjecting such assistance to restrictive conditions and that clear processes for the execution of mutual legal assistance (MLA) requests should be in place.

Six countries⁶ received a Compliant rating. These countries have demonstrated that they were able to provide a wide range of mutual legal assistance, on the basis of multilateral and bilateral treaties, and as necessary on the basis of reciprocity, as corroborated by the statistics included in the reports. In a majority of cases, no impediments to cooperation were identified. The processes for executing MLA requests appeared to be efficient, the restrictions on providing MLA did not appear to be unduly restrictive and MLA could not be refused on grounds that it related to a fiscal offence or on the grounds of laws that impose secrecy requirements on financial institutions.

Six countries⁷ received a Largely Compliant rating. The factors giving rise to the largely compliant ratings included:

- the shortcomings of the money laundering and/or the financing of terrorism offence which may limit mutual legal assistance based on dual criminality;
- in one case the country had not demonstrated that it had considered devising and applying mechanisms for determining the best venue for prosecution of defendants in cases that were subject to prosecution in more than one country;
- lack of detailed statistics which did not make it possible to fully assess how effectively or efficiently mutual legal assistance requests were handled;

Recommendation 37—Dual criminality

Recommendation 37 requires that countries should, to the extent possible, render mutual legal assistance notwithstanding the absence of dual criminality, and when dual criminality is required, to consider that it is satisfied regardless of whether both countries place the offence within the same category of offence or denominate it by the same terminology, provided that both countries criminalise the conduct underlying the offence.

Nine countries⁸ received a Compliant Rating, two countries⁹ a Largely Compliant rating, and one a Partially Compliant rating¹⁰. The factors giving rise to less than compliant ratings included:

- shortcomings of the money laundering and/or the financing of terrorism offence which may limit extradition with non-EU countries based on dual criminality;
- requirements contained in reservations to the European Convention on Mutual Assistance in Criminal Matters (ETS. No. 030) related to dual criminality;
- in one case, though there was indication that dual criminality would be widely interpreted, it was not possible to assess how effectively requests were being handled in such cases due to the absence of statistics.

⁶ Bulgaria, Hungary, Latvia, Lithuania, Malta, Slovenia.

⁷ Cyprus, Czech Republic, Estonia, Poland, Romania, Slovak Republic.

⁸ Bulgaria, Cyprus, Czech Republic, Hungary, Latvia, Lithuania, Malta, Romania, Slovenia.

⁹ Estonia, Poland.

¹⁰ Slovak Republic.

Recommendation 38—Mutual legal assistance requests related to identification, freezing, seizure or confiscation

Recommendation 38 requires that countries should have appropriate laws and procedures to provide an effective and timely response to mutual legal assistance requests from foreign countries related to the identification, freezing, seizure or confiscation of laundered property, proceeds from money laundering or predicate offences, instrumentalities used in or intended for use in the commission of these offences or property of corresponding value. There should also be arrangements for coordinating seizure and confiscation proceedings, which may include the sharing of confiscated assets.

Three countries¹¹ received a Compliant rating and the reports indicated that they had appropriate laws and procedures in place and included clear evidence of their experience in dealing with such foreign requests.

Seven countries¹² received a Largely Compliant rating and two countries¹³ a Partially Compliant rating. The factors giving rise to these ratings included:

- legislative shortcomings which raised reservations on countries' capacities to enforce foreign confiscation orders related to certain offences which were not criminalized in the requested country or to execute a foreign request to identify proceeds;
- in the absence of a clear legal basis, procedures or practice, difficulties to ascertain whether a request for confiscation of property could extend to enforcement of confiscation of all proceeds of crime and intended instrumentalities;
- countries had not considered establishing an asset forfeiture fund into which all or a portion of confiscated property would be deposited and used for law enforcement, health, education or other appropriate means;
- absence of arrangements for co-ordinating seizure and confiscation actions with other countries (non EU countries);
- countries had not considered authorizing the sharing of confiscated assets between them when confiscation is a result of coordinated law enforcement action;
- lack of statistics and related data to demonstrate the effectiveness of handling requests relating to freezing, seizing and confiscation.

Recommendation 39—Extradition

Recommendation 39 requires that money laundering should be an extraditable offence and that there should be laws and procedures to extradite individuals charged with a money laundering offence.

Eight countries¹⁴ had Compliant ratings and the reports indicated that their relevant legal structures supported the extradition of individuals for money laundering and that they could demonstrate the effective execution of extradition requests.

Four countries¹⁵ received a Largely Compliant rating. The factors giving rise to the largely compliant ratings included:-

- lack of statistics in three of the four cases meant that it was not possible to assess how effectively extradition requests were being handled.
- under-staffing in departments designated to handle extradition requests had resulted in delays in processing requests in one case.
- lack of an explicit provision in domestic legislation which would, in cases of refusal to extradite a national, require submission of the case, without undue delay, to the competent authorities for the purpose of domestic prosecution of the offences in the extradition request.

Recommendation 40—Other forms of co-operation

Recommendation 40 requires that countries should ensure that their competent authorities (including the FIU and supervisory bodies) provide the widest possible range of international co-operation to their foreign counterparts.

Five countries¹⁶ received a Compliant Rating and the reports indicated that they had mechanisms in place to facilitate international co-operation and that this was carried out in practice.

¹¹ Cyprus, Hungary, Malta.

¹² Bulgaria, Czech Republic, Estonia, Lithuania, Poland, Romania, Slovenia.

¹³ Latvia, Slovak Republic.

¹⁴ Bulgaria, Cyprus, Hungary, Latvia, Lithuania, Malta, Romania and Slovenia.

¹⁵ Czech Republic, Estonia, Poland, Slovak Republic.

¹⁶ Bulgaria, Estonia, Hungary, Malta, Romania.

Six out of 12 countries¹⁷ received Largely Compliant ratings. One country received a Partially Compliant rating. The factors giving rise to the less than compliant ratings were:

- lack of statistics (in five of the countries concerned) meant that it was not possible to assess how effectively or efficiently such requests for international cooperation were handled.
- lack of legal or other provision for co-operation between supervisory bodies and / or difficulties in assessing how effectively supervisory bodies were cooperating with their international counterparts.
- limitations as regards access to some information at an internal level.

Special Recommendation V—International co-operation

Special Recommendation V requires that countries should provide international assistance for investigations, inquiries and proceedings relating to the financing of terrorism, terrorist acts and terrorist organisations. In addition, countries should also take all possible measures to ensure that they do not provide safe havens for individuals charged with the financing of terrorism, terrorist acts or terrorist organisations.

Five countries¹⁸ received a compliant rating and, in those cases, the reports indicated that they had mechanisms in place to facilitate international co-operation on terrorist activities and financing and that this was carried out in practice. There was no indication that any country was providing a safe haven for terrorists.

Four countries¹⁹ received a Largely Compliant rating, and three countries²⁰ received a Partially Compliant rating. The factors giving rise to ratings less than Compliant included:-

- the restricted width of the domestic financing of terrorism offences which could impact on international co-operation possibilities and extradition requests.
- lack of or insufficient information on statistics to demonstrate effective implementation.
- lack of ratification of the United Nations International Convention for the Suppression of the Financing of Terrorism.
- concerns over the sufficiency of resources for timely mutual legal assistance.

V HOW THE EXPERIENCE IN MONEYVAL EVALUATIONS HAS BEEN REFLECTED IN THE NEW CONVENTION

It is considered that the MONEYVAL process has been effective. As a result of its reports over nearly three rounds, preventive laws have been introduced and/or improved, and repressive systems have been developed. Overall the effectiveness of AML/CFT systems in MONEYVAL member countries is gradually improving though it will take longer for all the international standards to become embedded in national operational practice.

That said, in reviews of the first two evaluation rounds, MONEYVAL raised concerns about the small number of major money laundering convictions achieved and deterrent confiscation orders that are made in many of its Member States.

The second horizontal review concluded “it is apparent that while an increasing number of jurisdictions are achieving some concrete results in terms of prosecutions and convictions for money laundering and (though this is less clear) in obtaining serious confiscation orders in respect of major proceeds generating criminal offences, much room for improvement remains. While legislative, technical and resource insufficiencies and restraints play their part, the second round reports serve to demonstrate how far we still have to travel in order to create and entrench a culture within national systems as a whole in which going after criminal proceeds is appropriately expressed as a priority and facilitated in practice”.

Many of the technical legal problems which MONEYVAL identified in this respect, and which inhibit effective money laundering prosecution and confiscation, have been addressed in the new Convention.

Prior to the elaboration of the 2005 Convention MONEYVAL had found, in several countries, that because of the low number of successful prosecutions, and the consequent lack of clear judicial interpretation of complex criminal money laundering legislation, prosecutors were uncertain about precisely what levels and types of evidence courts would accept to establish the elements of a money laundering offence. Moreover, it seemed, in some countries, that they were reluctant to “test the waters”. Where there were successful prosecutions for money laundering, examiners had frequently found that the cases which were being brought were rarely

¹⁷ Cyprus, Czech Republic, Latvia, Poland, Slovak Republic and Slovenia.

¹⁸ Bulgaria, Hungary, Malta, Lithuania and Slovenia.

¹⁹ Cyprus, Czech Republic, Estonia and Romania.

²⁰ Latvia, Poland and the Slovak Republic.

laundering of criminal proceeds by professional launderers or third parties for major criminals or organised crime (such as laundering by accountants or lawyers).

Where third party laundering cases were brought, they tended to be comparatively minor prosecutions of friends and family members of the author of the predicate offence. The underlying predicate offences also were rarely those which the countries identified themselves in their criminal statistics as the major proceeds-generating offences. Moreover in some countries there was a marked tendency to concentrate on fiscal predicate offences, at the expense of those other predicate offences more frequently committed by organised crime (arms trafficking, human trafficking, etc.).

Thus, third party laundering was found not to be pursued very actively. Often, on analysis, prosecution cases were confined to simple self (or “own proceeds”) laundering—usually added to the same indictment as the predicate offence.

Many prosecutors and judges had expressed doubts to evaluators that their systems would allow money laundering convictions without a prior or simultaneous conviction for the predicate offence. While such an approach may result in some convictions for money laundering in the case of domestic predicate offences (by some third parties), such a rigid doctrine could easily exclude from a country’s domestic criminal regime the laundering by third parties in one country of proceeds from predicate offences committed in another. Equally, in countries where a conviction was not thought to be required for the predicate offence, in a money laundering case, there was often still an assumption that a perpetrator of the underlying predicate crime had to be identified before the money laundering offence could proceed. Furthermore it was sometimes argued that domestic jurisprudence would not allow the elements of a money laundering offence (including the existence of underlying predicate criminality) to be drawn by inferences from objective facts and circumstances.

High levels of evidence were also often thought to be required to prove the mental element of the offence to what was perceived as the requisite standard, particularly where the criminal legislation was based on the knowledge standard. This issue appeared to present particular difficulties for those countries which had adopted the list approach to predicate crime. In these situations, knowledge of the particular crime from which the proceeds came (rather than the type of crime or, indeed, whether the proceeds came from crime generally) was thought to be necessary. The problems involved in proving the particular criminal offence from which the proceeds came in a money laundering case are self-evident.

These are all problems that cumulatively can inhibit prosecutors from proceeding with money laundering cases.

The new money laundering provisions in the 2005 Convention

The first important change concerns the *mens rea*. The evaluation process had, as noted, shown that proving the mental element of a money laundering offence can be very difficult, as the courts often require (or are thought to require) a high level of knowledge as to the origin of the proceeds by the alleged launderers.

The addition of paragraph 9 (3) in the 2005 Convention will enable Parties also to establish a criminal offence where the offender (a) *suspected* that the property was proceeds and/or (b) *ought to have assumed* that the property was proceeds.

Paragraph 3a provides for the lesser (subjective) mental element of suspicion, and could cover a person who gives the origin of the proceeds some thought but has not firm knowledge that the property is proceeds. This new provision reflects the position in some countries which already have suspicion in their money laundering criminal legislation as an alternative *mens rea* (with appropriately lower penalties) and which have achieved some success in prosecution on this basis where otherwise no money laundering proceedings might have been brought. Paragraph 3b allows for the criminalisation of negligent behaviour, where the court can objectively weigh all the evidence and determine whether the offender ought to have assumed the property was proceeds, whether or not he or she gave any thought to the matter.

As already noted, there have been significant changes to the possibility of reservations to the “all crimes” predicate base of money laundering. The drafters of the new Convention took into account Recommendation 1 of the FATF 2003 Recommendations, which provides that each country should, at a minimum, include a range of offences within each of the “designated categories of offences”. These categories of offences are contained in the Appendix to the new Convention, which reproduces textually the glossary appended to the 2003 FATF Recommendations. It should be noted also in this context (and also in the context of Article 13) that Article 54 of the Convention contains a simplified amendment procedure to ensure that the Convention can respond to the evolution of international law and standards in this area. More particularly, the drafters stressed that this provision should allow for an all crimes approach, as well as for an enumerated list of offences (and threshold approaches). In any event, all the categories of offences contained in the Appendix to the 2005

Convention have to be considered as predicate offences for the purposes of money laundering and therefore cannot be excluded from the scope of application of the money laundering offence through a declaration provided by this provision. This is an important provision as the Appendix covers most of the offences regularly committed by organised crime.

The Convention also addresses the practical problem in money laundering prosecutions exposed in the evaluations, and discussed above—the perceived need for a conviction for the underlying predicate offence as a basis for a money laundering investigation or prosecution. The 2005 Convention now requires the parties to ensure that a prior or simultaneous conviction for the predicate offence is not a prerequisite for a conviction for money laundering. The drafters of this Convention considered that, by clarifying this, it should then be possible, in a money laundering prosecution, for the predicate offence (whether domestic or foreign) to be established on the basis of circumstantial or other evidence. This was considered by the drafters to be important for the wider prosecution of money laundering by third parties as an autonomous offence.

The 2005 Convention also addresses, in Article 9.6, the related question of proof of the predicate offence in a money laundering prosecution. To facilitate prosecution, the drafters of the new Convention pointed out the importance for prosecutors not to have to prove in money laundering prosecutions all the factual elements of specific particularised predicate offences, if the proof of the illicit origin of the property could be established from other circumstances. Parties may implement Article 9.6 by requiring that the author of the money laundering offence knew that the assets came from particular types of predicate crime, like drug trafficking generally, without it being necessary to prove a specific drug trafficking predicate offence on a particular day.

Improvements in Confiscation in the new Convention

The Committee which drafted the 1990 Convention discussed whether it was possible to define certain offences to which the Convention should always be applicable. When drafting the 1990 Convention, the experts thought that the scope of application of the Convention should in principle be made as wide as possible. For that purpose, the 1990 Convention created an obligation to introduce measures of confiscation in relation to all kinds of offences. At the same time, the drafters of the 1990 Convention felt that this approach required a possibility for States to restrict co-operation under the Convention to certain offences or categories of offences. The possibility of entering a reservation was therefore introduced in the 1990 Convention, and the evaluation process has shown that the reservation procedure was used.

Paragraph 2 of Article 3 of the new Convention substantially limits this approach, by prohibiting parties from making declarations that would have the effect of excluding certain categories of offences. The list of categories of offences contained in the Appendix is, as noted earlier, identical to the one contained in the glossary to the revised FATF Recommendations of 20 June 2003, and now applies (together with money laundering offences themselves) also in the context of offences for which declarations are not possible in respect of confiscation.

Paragraph 3 of Article 3 deals with the important question of whether confiscation should be mandatory or discretionary in particular cases. It should be noted that this provision is not itself mandatory for parties, which are therefore free to decide whether to implement it or not. The drafters of this Convention, however, intended to send a signal, given that the MONEYVAL evaluations had shown in practice the essential discretionary character of criminal confiscation, that it may be advisable for particularly serious offences and for offences where there is no victim claiming to be compensated (such as drug trafficking, trafficking in human beings, or any other such serious proceeds-generating offence, including frauds with a large number of unknown victims) for confiscation to be mandatory.

Importantly, the Convention also in Paragraph 4 of Article 3 requires parties to provide the possibility, in serious offences, for the burden of proof to be reversed, after conviction for the criminal offence, in respect of the establishment of the lawful or other origin of alleged proceeds or other property liable to confiscation. Consideration by States of this issue had regularly been advised in MONEYVAL reports. The definition of the notion of serious offence for the purpose of the implementation of this provision is left to the internal law of the parties. The possibility of reversing the burden of proof is, however, subordinate to the fact that it is compatible with the internal law of the party concerned.

The explanatory report dealing with this new provision specifically draws attention to the case of *Phillips v. the United Kingdom* of 5 July 2001, in the European Court of Human Rights. In the *Phillips* case, statutory assumptions had not been applied by the court of trial in order to facilitate finding the defendant guilty of a drug trafficking offence, but to enable the court to assess the amount at which a confiscation order should be properly fixed after a drug trafficking conviction. The European Court of Human Rights held that the use of statutory assumptions with proper safeguards (which it found to be in place) in such circumstances did not

violate the ECHR or Protocol No 1 to it. The drafters of the 2005 Convention thus intended to send a signal that reverse onuses / statutory assumptions in such circumstances, post conviction, can very helpfully alleviate the prosecutor's burden in this area once a conviction has been achieved. Frequently, the prosecutor still has, after conviction, to establish (perhaps to the criminal standard of proof) precisely the amount of proceeds obtained from the criminal offences which have resulted in convictions, and which should therefore be capable of being confiscated. This can present many practical difficulties, and these difficulties are what this new provision seeks to address to ensure that confiscation of proceeds can be applied effectively by States while respecting ECHR obligations.

These are but a few of the practical improvements under the new Convention.

March 2009

Annex

TERMS OF REFERENCE OF THE COMMITTEE OF EXPERTS ON THE EVALUATION OF ANTI-MONEY LAUNDERING MEASURES AND THE FINANCING OF TERRORISM (MONEYVAL) (OCTOBER 2008)

1. Name of Committee:

Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism (MONEYVAL)

2. Type of Committee:

Committee of Experts

3. Source of terms of reference:

Committee of Ministers, at the suggestion of the European Committee on Crime Problems (CDPC)

4. Terms of reference:

Having regard to:

- the Declaration and the Action Plan adopted at the Third Summit of Heads of State and Government (Warsaw, 16-17 May 2005), and particularly to the Heading II.2 of the Action Plan;
- Resolution Res(2005)47 on committees and subordinate bodies, their terms of reference and working methods;
- the importance of the fight against money laundering and terrorist financing and other forms of serious crime, for the purpose of which the Council of Europe has adopted a variety of instruments, in particular the 1990 Convention on Laundering, Search, Seizure and Confiscation of the proceeds from Crime (ETS No. 141), and the 2005 Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the proceeds from Crime and on the Financing of Terrorism (CETS No. 198);
- the status of the Council of Europe/MONEYVAL since June 2006 as an Associate Member of the Financial Action Task Force on Money Laundering (FATF);
- Under the authority of the European Committee on Crime Problems (CDPC), and in relation with the implementation of Project 2004/DG1/78 (which will subsequently become 2008/DG-HL/1431) "Anti money laundering measure evaluation programme (MONEYVAL)" of the Programme of Activities, and bearing in mind the criteria set out in the document CM(2006)101 final, the Committee is instructed to:
 - i. Taking into account the procedures and practices used by the FATF, the IMF and the World Bank: elaborate appropriate documentation, including questionnaires for self—and mutual evaluations;
 - ii. evaluate, by means of self—and/or mutual evaluation questionnaires (and/or other documentation agreed between MONEYVAL, the FATF and the IMF/World Bank representing a common AML/CFT methodology) and periodic on-site visits, the performance of those member states of the Council of Europe which are not members of the FATF²¹ (subject to

²¹ Council of Europe member states members of the FATF: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Iceland, Ireland, Italy, Luxembourg, Netherlands, Norway, Portugal, Russian Federation, Spain, Sweden, Switzerland, Turkey and United Kingdom.

paragraph 5.A.ii below)²² in complying with the relevant international anti-money laundering and countering terrorist financing standards, as contained in the recommendations of the FATF, including the Special Recommendations on Financing of Terrorism and Terrorist Acts and related Money Laundering, the 1988 United Nations Convention on illicit traffic in narcotic drugs and psychotropic substances, the United Nations Convention against Transnational Organised Crime, the 1999 United Nations International Convention for the Suppression of the Financing of Terrorism, the 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 and the relevant implementing measures and the 1990 Convention on laundering, search, seizure and confiscation of the proceeds from crime, concluded within the Council of Europe, and, where necessary, provide assistance, upon request, to enable them to comply with the recommendations;

- iii. evaluate, by means of questionnaires (and/or other documentation agreed between MONEYVAL and the FATF and the IMF/World Bank representing a common AML/CFT methodology) and periodic on-site visits, the performance of those applicant States for membership of the Council of Europe which are not members of the FATF in complying with the international anti-money laundering and countering terrorist financing standards enumerated in the paragraph above, provided the following requirements are met: the applicant State must make the request in writing; the request must be accepted by the Committee of Ministers; the applicant State must undertake in its request to participate fully in the evaluation procedure and comply with the results and recommendations formulated by the MONEYVAL; and the applicant State must contribute to the cost of the evaluation procedure;
- iv. evaluate, by means of questionnaires (and/or other documentation agreed between MONEYVAL, the FATF and the IMF/World Bank representing a common AML/CFT methodology) and periodic on-site visits, the performance of the State of Israel, a non-member State of the Council of Europe, which has observer status with MONEYVAL and participates in the MONEYVAL mutual evaluation process. The participation of Israel in the mutual evaluation process implies that (a) it participates fully in the evaluation procedure and complies with the results and recommendations formulated by MONEYVAL and (b) it contributes to the cost of the evaluation procedure; adopt reports on each evaluated country's situation as to:
 - v. — the features and magnitude of money laundering, including typologies;
 - the efficiency of measures taken to combat money laundering and terrorist financing in the legislative, financial regulatory, law enforcement and judicial sectors;
- vi. where appropriate, make recommendations to the evaluated countries, with a view to improving the efficiency of their anti-money laundering and countering terrorist financing measures and to furthering international co-operation;
- vii. submit to the CDPC an annual summary of its activities and any recommendations it deems appropriate with a view to furthering the adoption or implementation of anti-money laundering measures.

5. COMPOSITION OF THE COMMITTEE

5.A *Members*

i. Governments of the following Council of Europe member States, not members of the FATF (subject to paragraph 5.A.ii. below): Albania, Andorra, Armenia, Azerbaijan, Bosnia and Herzegovina, Bulgaria, Croatia, Cyprus, Czech Republic, Estonia, Georgia, Hungary, Latvia, Liechtenstein, Lithuania, Malta, Moldova, Monaco, Montenegro, Poland, Romania, Russian Federation, San Marino, Serbia, Slovak Republic, Slovenia, “the former Yugoslav Republic of Macedonia” and Ukraine are, each, entitled to appoint three experts in the anti-money laundering and the financing of terrorism field and with the following desirable qualifications: senior officials and experts with responsibility for regulation or supervision of financial institutions, senior members of financial intelligence units, law enforcement or judicial bodies, with particular knowledge of questions related to money laundering, including national and international anti-money laundering instruments, (eg FATF recommendations).

²² Albania, Andorra, Armenia, Azerbaijan, Bosnia and Herzegovina, Bulgaria, Croatia, Cyprus, Czech Republic, Estonia, Georgia, Hungary, Latvia, Liechtenstein, Lithuania, Malta, Moldova, Monaco, Montenegro, Poland, Romania, Russian Federation, San Marino, Serbia, Slovak Republic, Slovenia, “the former Yugoslav Republic of Macedonia” and Ukraine. See also 5.A.ii. below.

ii. Government of any Council of Europe member State referred to under 5A.i. above which has become a member of the FATF and thus would, save for this paragraph, cease to be a member of MONEYVAL, but decides to remain a member of the latter as well, is entitled to appoint three experts in the same field and with the same qualifications, as mentioned above in paragraph 5.A.i.. Such a State may also agree to submit to the evaluation process of MONEYVAL.

iii. The Presidency of the Financial Action Task Force (FATF) is entitled to appoint two experts from FATF countries for two-year periods.

The Council of Europe's budget²³ bears the travel and subsistence expenses of three experts from each of the member States mentioned under 5.A.i. and 5.A.ii.. These member States may send additional experts at their own expense.

5.B *Participants*

i. The European Committee on Crime Problems (CDPC) may send one representative to meetings of the Committee, without the right to vote and at the charge of its administrative budget.

5.C *Other participants*

i. The European Commission and the Secretariat General of the Council of the European Union may send a representative to meetings of the Committee, without the right to vote or defrayal of expenses.

ii. The following observer States with the Council of Europe may send a representative to meetings of the Committee, without the right to vote or defrayal of expenses:

- Canada;
- Holy See;
- Japan;
- Mexico; and
- United States of America.

5.D *Observers*

i. The following intergovernmental organisations may send representatives to meetings of the Committee, without the right to vote or defrayal of expenses:

- Secretariat of the Financial Action Task Force on Money Laundering (FATF);
- ICPO-Interpol;
- Commonwealth Secretariat;
- International Monetary Fund (IMF);
- United Nations Drug Control Programme (UNDCP);
- United Nations Counter-Terrorism Committee (CTC);
- United Nations Crime Prevention and Criminal Justice Division;
- World Bank;
- European Bank of Reconstruction and Development (EBRD);
- Offshore Group of Banking Supervisors (OGBS);
- Organisation for Security and Co-operation in Europe (OSCE);
- Egmont Group;
- Eurasian Group on Combating Money Laundering and Terrorist Financing (EAG);
- Any other Financial Action Task Force Style Regional Body which is, or becomes, an Associate Member of the FATF on the basis of reciprocity.

²³ A Special Account has been opened for that purpose.

5.E *Other observers*

- i. The following observers with the Committee may send representatives to the meetings of the Committee, without the right to vote or defrayal of expenses:
- Members of the FATF other than those referred to in 5.A.ii.;
 - Israel.

6. WORKING METHODS AND STRUCTURES

The term of office of the Chairman and Vice-Chairman shall be two years. It may be renewed once.²⁴ The Committee may elect a Bureau to facilitate its discussions and adopt internal rules of procedure. It will work with the assistance of four scientific experts, appointed by the Secretary General. The Council of Europe's budget bears their travel and subsistence expenses.

7. DURATION

These terms of reference will expire on 31 December 2010.

Examination of Witness

Witness: MR JOHN RINGGUTH, Executive Secretary, MONEYVAL (Council of Europe's Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism), examined.

Q489 *Chairman:* Mr Ringguth, can I thank you very much indeed for coming today. I know you have come from Strasbourg so thank you. Would you introduce yourself and then we can ask you some questions.

Mr Ringguth: My name is John Ringguth. I am the Executive Secretary of MONEYVAL which is the monitoring arm in anti-money laundering and countering the financing of terrorism of the Council of Europe. MONEYVAL, as I think you know, covers 28 Council of Europe countries that are not members of the Financial Action Task Force and we also evaluate the state of Israel which has active observer status with the MONEYVAL Committee. Since 2006 we are also an associate member of the Financial Action Task Force. This is a new status that the regional bodies can apply for within the Financial Action Task Force and perhaps a little later in the questions we may get into some of the issues in relation to that.

Q490 *Lord Marlesford:* The British government has decided, when implementing the money laundering regulations in Europe, that they would wish tax evasion to be able to be included in the operation and therefore they decided that they would have an all crimes approach to the requirements for reporting suspicious activities. This, of course, has greatly widened the whole ambit of the SARs (Suspicious Activity Reports) submitted in Britain to the Serious Organised Crime Agency. To what extent does the 2005 Council of Europe Convention on laundering, search, seizure and confiscation of proceeds from crime and on the financing of terrorism (the Warsaw

Convention) encourage states to adopt an all crimes approach to the scope of the money laundering offence? What, in your view, are the advantages and disadvantages of adopting the all crimes approach?

Mr Ringguth: Thank you very much for the question. Certainly the Warsaw Convention, like its predecessor, the Strasbourg Convention, does encourage an all crimes approach. Perhaps I should declare an interest here. In Strasbourg we are actually great proponents of the all crimes approach to money laundering criminalisation and particularly in respect of the legal side, if I can put it that way, of money laundering prosecution. The reason I say that is that one of the fundamental reasons that the Council of Europe actually became engaged with the money laundering issue generally was because of its importance in the fight against organised criminality. We know that organised criminals do not just commit one particular criminal offence, they commit a whole range of offences. From the point of view of the prosecution and investigation of money laundering, there are benefits to an all crimes approach. I will give you just two. So far as prosecution is concerned, I think it is self-evident that if you are actually seeking to prosecute a person for money laundering you have to prove the mental element of that offence. One of the problems with short predicate lists is that the mental element can actually be quite difficult sometimes for prosecutors to establish. If you have an extraordinarily short list you could end with a situation, if you are a country which simply prosecutes on the basis of the knowledge standard, that they need to know the particular type of offence that the proceeds were actually laundered for. We take the view that it actually facilitates prosecution if

²⁴ In derogation of Article 12.e of Appendix 1 to Resolution Res(2005)47 on committees and subordinate bodies, their terms of reference and working methods (see also decision of the Committee of Ministers at their 924th meeting on 20 April 2005).

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in fact the international standards simply require—the all crimes approach does this—an approach where the money laundering defendant simply needs to be in a position to have proved against him that he knew that the proceeds came from some crime. The all crimes approach certainly facilitates that. So far as international cooperation is concerned—which is my other major point on the judicial side—clearly with money laundering being probably one of the most international of crimes, the necessity for states to provide the widest measure of international cooperation is paramount. Certainly experience has shown in the evaluation process that those that have narrower predicate lists very often are not in a position, particularly where dual criminality is required for coercive measures, to provide necessary judicial international cooperation in some cases where a state has requested it. I think at that level there are great attractions to the all crimes approach. I have to say I read the evidence that you have received from various witnesses et cetera and I can certainly allow that the all crimes approach can have difficult practical consequences, particularly for the preventive AML/CFT regime, particularly when it comes to FATF Recommendation 13 (reproduced in the European Union Directive) in terms of the reporting obligation. The reporting obligation under the FATF requirements has no de minimis provision in it at all including in relation to tax evasion. Perhaps I might say a word about the UK here. Of course the UK achieved a fully compliant rating when it was assessed by the FATF for this very reason, because all the requirements of the FATF standards were actually covered. I understand the issues that have been raised, that it can potentially flood financial intelligence units with suspicious transaction reports et cetera. That may be more problematical in some of the countries that we deal with in MONEYVAL than perhaps in the United Kingdom where SOCA has a very sophisticated system for dealing with reports. There is to be a review now of some of the FATF recommendations and while I subscribe on behalf of the Council of Europe, to the all crimes approach, it does seem to me that so far as the reporting regime is concerned, to look again at the de minimis provision—or no de minimis provision—might actually be a useful way to go. It does seem to me that actually having to report everything with no threshold whatsoever may be problematic and that having a de minimis provision would not necessarily do damage to the all crimes approach so far as criminal cases are concerned. At the end of the day we are not seeking to prosecute money laundering on the very small types of offence that you have already discussed in this Committee. I think the Crown Prosecution Service made it fairly clear that a sensible exercise of prosecutorial discretion will weed those cases out. However, it does seem to me that this is an

area that can be looked at. I think it is also important in the context of the commitment of financial institutions et cetera to the money laundering preventive regime. The more STRs that the FIU receives the likelihood is that the opportunities for feedback to the private sector as to what has happened to their STR may be reduced. One of the areas we looked at very closely in the evaluation process is the ability of FIUs particularly to actually provide this feedback. I think it has been acknowledged that with the sorts of numbers the FIU receives in the UK you are not going to be able to get case specific feedback on all the reports because of the large numbers. These issues translate to the European theatre that I work in as well. I would simply flag up that I think this is an area you might wish to consider in your report by pointing the relevant authorities to further consideration of this issue.

Q491 Lord Faulkner of Worcester: Can I ask you about tax matters and tax evasion? We have been given evidence that FATF is thinking of changing its traditional stance on tax evasion matters. What would you say are the advantages and disadvantages of making tax matters predicate offences for money laundering?

Mr Ringguth: My starting point here is that under the all crimes approach if tax evasion is a crime in the country—as the situation is here—then for practical purposes it is covered whether or not the FATF requirements specifically require countries to actually have tax offences within their list of predicate offences. I have to say that I think there is a bit of an equivocal stance in FATF on this issue because in relation to the reporting requirement under recommendation 13 states are encouraged to report tax matters largely I suspect if a country actually has tax matters in its range of predicate crimes it is necessary to report it, but there is a push in the methodology to report tax matters in any event, yet tax of course is not currently one of the designated categories of offence. I have to say that I think personally—these are my personal views because we do not have a MONEYVAL position on this particular issue at the moment although we will discuss it if the review takes it further—that tax evasion is clearly an important crime. I have some concerns, however if I can put it this way, that in some countries—we have identified this in horizontal reviews as well—if tax evasion were made one of the designated categories of offence that could be in some ways counter-productive in some countries. Where tax evasion already is a predicate offence we have occasionally seen investigative and prosecutorial resources being concentrated onto the tax predicate at the expense of other offences which are more commonly associated with organised criminality

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such as human trafficking. As I said, I have an open mind on this. At present I tend to favour a balanced score card of designated offences, which perhaps would point to actually keeping tax evasion out but I will follow the discussion.

Q492 Lord Dear: Could I turn to focus on civil confiscation orders and these are always in respect of property which is the product of crime? Do you have a view on whether the Warsaw Convention provides a framework for cooperation in the enforcement?

Mr Ringguth: If our memorandum did not cover this issue I apologise because I certainly consider that there is a very positive advance in article 23, paragraph five of the convention which actually states, “The parties shall” (which is mandatory) “cooperate 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 insofar as such measures are ordered by a judicial authority of the requesting party in relation to a criminal offence” (not a case but a criminal offence) “provided that it has been established that the property constitutes proceeds or other property in the meaning of article 5”. So there is a wide definition of proceeds there and the convention has made it crystal clear in the body of the text that cooperation concerning the execution of measures leading to confiscation which are not criminal sanctions has to be provided to the widest extent possible. There is no reservation procedure under the convention in relation to this which would mean—and this is a positive step—that if more countries actually ratify this convention the possibilities for the UK, for instance, to enforce civil confiscation orders in other parts of Europe et cetera would be considerably widened. I might also say that this is 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. We do have examples in countries like Bulgaria at the moment. In certain parts of their confiscation regimes there is a civil burden. They have an authority which is proceeding against assets and proceeds after a conviction actually on civil standards so it will be of interest to a country like that. The same is true in Georgia, which has looked at these issues and considered reverse burdens and adopted some civil standards. I do think that this is actually a positive development not just for countries like the UK, Ireland and the US et cetera that have established forfeiture procedures for some time, but for other countries that are actually looking closely at

doing something similar which may in fact hitherto have been contrary to their legal traditions. I do think that this is an important provision.

Q493 Lord Dear: Is there anything else you think that the Council of Europe can do to facilitate cooperation in relation to civil confiscation?

Mr Ringguth: I do think there may be, yes. First of all so far as our position as an associate member of the Financial Action Task Force is concerned, in the review I think we should be looking at particularly FATF Recommendation 38 (which perhaps we will talk about a little later) in relation to the enforcement of foreign orders in this area. One of the problems from the perspective of those that have gone down the civil route is that in recommendation 38 the inability of other states to enforce civil orders counts for nothing in terms of ratings because it is actually an additional criteria which is not mandatory and does not count for the ratings. For practical purposes there is no global impetus to enforce civil confiscation under the FATF standards as they are at present. I think this is an issue that MONEYVAL certainly will push in the review of the international cooperation Recommendations. 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. One of the hitherto unused parts of MONEYVAL’s terms of reference, which are given to us by the Committee of Ministers of the Council of Europe, provides that I, as Executive Secretary, have to prepare an annual report to the European Committee of Crime Problems. One of the possibilities is that MONEYVAL can propose recommendations as to how AML/CFT issues could be improved. Indeed, going back in history, recommendations from the Committee of Ministers in the Council of Europe was one of the very first international standards in this particular area. I am not saying that we are necessarily going to that stage but we would like to open up this discussion. It would stimulate perhaps more, at the very least, memoranda of understanding between countries and of course the UK is a very active observer to MONEYVAL and no doubt will contribute very strongly to this discussion and let us see what comes out of that as to whether we actually could perhaps begin the drafting of some form of recommendation which would help to push the standards in this direction.

Q494 Baroness Garden of Frognal: Mr Ringguth, in your very helpful written evidence on page six you mention that the first meeting of the Conference of

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the Parties to the Warsaw Convention was due to take place on 22 April. Could you tell us what decisions were taken at that meeting on the creation of monitoring procedures under the Convention? Given that the intention of the drafters was not to duplicate the work of the existing monitoring mechanisms perhaps you can explain how you will avoid duplication on the work already being undertaken by the FATF and by MONEYVAL?

Mr Ringguth: This time last week we were discussing these issues in the first Conference of the Parties. It was a very well attended meeting. We invited not only those states which had ratified the convention which is currently 14 states (although I have not looked on the website this morning), but all of the Council of Europe states—whether it was the 19 who have already signed the convention—on the basis that we trust that they will sign and ratify the convention in due course. I am pleased to say that the United Kingdom was represented as well at this meeting. We took a number of major steps forward with the monitoring mechanism under this convention and this is one of the added values of this convention because the Strasbourg Convention and conventions generally of that generation tended not to have monitoring mechanisms attached to them. The conference was very conscious of the language of article 48 of the convention itself and drafters were certainly extremely anxious that we should not duplicate work that is done elsewhere and it is not the intention that this new mechanism will duplicate work which is done either by the committee that I am responsible for (which is MONEYVAL) or indeed the FATF. What we have decided—we have now adopted rules of procedure and I trust that those will be public and on the website in a few days and you can look at them—is that we will proceed with a drafting exercise now (and we have appointed a drafting group) which will actually distil the areas of the convention which we consider add value to the existing international standards. I will not go into chapter and verse here but the secretariat has produced a paper which will be a working document for this drafting committee covering areas where we consider the convention actually moves the standards on and we will focus in the evaluation process on those areas and not on areas which are exhaustively covered by the FATF and by MONEYVAL currently under the methodology. That work will be progressed between now and November and we very much hope and anticipate that the second Conference of the Parties will take place shortly after Christmas of this year (probably the second half of January) where we will adopt the questionnaire and move into the beginning of this process. It will essentially be, in the first instance, light touch, if I can put it that way. We will actually send a questionnaire to countries for them to respond to but there will be, as with FATF

and MONEYVAL, an element of peer review actually brought to bear on this. We have adopted in the rules a procedure whereby rapporteur countries will actually go through the report and the report will be constructed by the rapporteurs and the secretariat together. It will be discussed by the Conference of the Parties. If they want more information the country will have the opportunity of providing that. At the end of the day, if there are concerns about the progress in the country or the way that the convention is implemented, at a second stage it will be open to look at what further or more in depth evaluation is needed, which might include on-site visits.

Q495 Chairman: Is that review going to cover civil forfeiture?

Mr Ringguth: It will indeed because the article that I have just referred to is one of the added values of this convention. We shall be looking very closely to see how those ratifying countries have actually implemented the provision.

Q496 Lord Avebury: I want to ask you about the review that was recommended by the UK, Brazil and the Netherlands of FATF recommendations and the mutual evaluation process. I presume this will affect you because you have the same standards and monetary methods as FATF. What has been your reaction to this initiative? How do you intend to participate?

Mr Ringguth: We very much welcomed this initiative of the UK Presidency. We thought it was very timely and we were very supportive of it. So far as the standards—I know that you had discussions last week with Sir James Sassoon on this very issue—although not all MONEYVAL members would necessarily subscribe to a wholesale review of the 40 recommendations. There is certainly a body of opinion, and it is understandable, basically that international standards need some stability unless there are compelling reasons to change them. We do think that there are a number of standards in the current FATF 40 and in the Special Recommendations that do actually require looking at again. I would particularly flag up certainly some of the preventive standards (Recommendation five, recommendations 33 and 34 but especially in the context of MONEYVAL the law enforcement Recommendations. We have placed a great focus on the law enforcement aspects and the prosecutorial aspects of anti-money laundering and countering and financing of terrorism. We do take the view that the balance between law enforcement and preventive issues is actually wrong in the Recommendations as they stand currently. There are actually very few recommendations which focus directly on law enforcement and in our view some of them are

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actually quite weak and could do with strengthening. We have actually offered in the process that is going on at the moment within FATF some renewed wording already to some of the standards. Just to give you a particular example, this was a proposal by one of our very active Member State delegations which feels very strongly that there is no impetus for parallel financial investigation in serious predicate crimes in the FATF recommendations as they stand. Certainly if recommendations 27 or 28 are revised we have a proposal which would actually put the focus a little more clearly on that particular issue. As I hope it is clear to everyone, getting the money off the criminals is why we are in this business in the first place. So that is the standards, but what I would perhaps like to flag up almost as importantly as the standards is the way in which the evaluation bodies—I include MONEYVAL in this—are delivering assessment reports at present. We take the view that the present methodology (which has been extremely helpful in giving greater consistency to the evaluation process) is extraordinarily detailed and extraordinarily complex. I imagine that some members of the Committee have had the opportunity of reading at least the United Kingdom's report by the FATF and you will see the level of detail that we actually go into. A criticism that a number of MONEYVAL Member States rightly make is that because of the complexity and because of the detail you can know—I will use a car analogy here—just about everything that is going on under the hood but you do not really know if the car is actually working. One of the problems with the reports is that you can actually be left with the view: what did the evaluators really feel about the overall effectiveness of the AML/CFT system in the particular country? We think there is more that can be done in looking again at how we deliver these reports. This is a particularly live issue in fact in MONEYVAL at the moment because our evaluation process, as I think Sir James mentioned last week, is coming to the end of its third round and there was certainly no appetite within MONEYVAL countries to embark on a fourth round simply repeating the extremely large methodology that we have at the moment. What we have decided—we have discussed this and coordinated this with the Financial Action Task Force—is that we will actually proceed in the second half of this year with a shorter and much more focussed evaluation round which will, in the first instance, look at those recommendations which did not receive a sympathetic response from the evaluators in the third round (those that got a non-compliant or a partially compliant rating) and we will re-review those particular recommendations. We are also anxious that in the process of this that we do not lose sight of potential backsliding or backtracking by states on the major international standards. Whatever rating a country has received on some of

the core and key FATF recommendations we will look at those again de novo in any event. We have identified a number of them but I will not go into them unless you particularly want me to; I can also send you a copy of the questionnaire we have prepared. We will also ask the countries to analyse a little more closely the particular risks that they are facing in anti-money laundering and countering and financing of terrorism. There are two issues that we want to get out of this. One is a contextual look at the individual country so far as risks are concerned and indeed now, particularly for countries that have gone through three rounds of evaluation, how effectively the systems are working in practice. That is really what it is all about. If we could actually work to some clear conclusions in a report about the systems overall we think that may be a positive way to go forward. We have indicated to the FATF that we will feed back to the appropriate working groups how we are getting on with this and it may be that this may help to inform the process for the FATF's own fourth round going forward.

Q497 Lord Avebury: In a sense you are pre-empting what the FATF decision will be, are you not? You say you have already decided to embark on this fourth round with what I might call a streamlined approach.

Mr Ringguth: It certainly does not pre-empt any decisions the FATF will take. As an associate member of the FATF, if there is to be a different methodology in due course which does not in some way mirror what we are doing, well of course we will embark on that at the appropriate time. We were on the horns of a dilemma as far as this was concerned. Certainly the view within MONEYVAL is that peer evaluation needs to continue. We felt that we could not wait for two or three years for the FATF to decide how the fourth round was to be conducted. As I think I said, there was not a lot of appetite for simply repeating the process that we have already done. The reason I say that though is because all our reports, like the FATF's, are actually transparent and they are on the website. A lot of the detailed information will not have changed as we go into this next round and people can actually refer back to what was said in the previous report. We do not see it in any way as trying to hijack or pre-empt the process but as a logical way forward pending the FATF's decision as to how they will approach evaluations.

Q498 Lord Avebury: It would obviously be much more convenient if FATF, having looked at the model that you are developing, would make the recommendation that other groups should adopt the same procedures, particularly, as you say, if they agree with your premise that the level of complexity and detail in the previous evaluations has really omitted some central conclusions which did not

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become apparent because of that level of complexity and detail. However, if they do not agree with that premise and they continue the same type of mutual evaluation as they have in the past, then either you would have two systems operating in parallel in different groups or you would have to fall into line with whatever the review that FATF finally recommends.

Mr Ringguth: I certainly would not put it as “fall into line” but, as I have said, if indeed there is a methodology which is created which is different from the one that we will embark on—and that is not unlikely—then certainly the MONEYVAL committee will use that methodology at the appropriate time. There is no dispute about that. I think it is fair to say, though, that there is considerable disquiet about the methodology generally within AML/CFT circles and I think that we are not wide of the mark, if I can put it that way, by going for a shorter and more focussed round of evaluations. Sir James, when he gave his evidence last week, made it clear that he had no particular problem with the way that MONEYVAL was taking this forward.

Q499 Lord Avebury: Are you satisfied that the review that FATF is conducting is taking fully into consideration what you have to say about, for example, the standards in recommendations five, 33 and 34 in particular which you mentioned?

Mr Ringguth: As an associate member we have the right to put forward suggestions. At the moment the FATF are at quite an early stage in this process of reviewing the procedures for the evaluations and indeed the recommendations. At the moment we are at the stage collectively of drawing together the issues that need to be discussed. Certainly it is our experience that our voice is heard very clearly in those discussions and I would very much expect that there is considerable support within FATF for a re-opening of some of these issues that I have actually talked about.

Q500 Lord Mawson: In your written evidence on page 11 you note that the review of the first two rounds of mutual evaluations conducted by MONEYVAL had raised concerns about the small number of major money laundering convictions achieved and deterrent confiscation orders made. Do the third round evaluations conducted to date indicate the progress in these spheres is being achieved? You say that getting money off criminals is the core business; are you dealing here with a failing of business really? When I listen to it, a lot of this discussion feels like an elephant trying to catch a snake when actually we need a mongoose. I wonder whether there is a real need for practical innovation here in this whole area otherwise you sort of die of

paralysis by analysis, not getting hold of the issue. Is that fair?

Mr Ringguth: I think it is fair to say that in the view of many MONEYVAL states one of the possible indicators of a performing AML/CFT system is the ability of a state to obtain some serious money laundering convictions—I am thinking specifically of convictions in the case of third parties that launder on behalf of organised crime, et cetera—and to get some serious deterrent confiscation orders. If you were drafting—and no-one has drafted as yet—clear indicators for what a performing AML/CFT system would look like, I would suggest that those would be certainly thrown into the balance. We have looked throughout the life time of MONEYVAL at these issues very closely in the reviews that we have done. We did a review of the first round in 2002 and repeated the exercise after the conclusion of the second round. I think that from the conclusions which you flagged up in the question, it is right to say that at the end of the second round there were certainly a good third of countries—founder members which had been through two evaluation rounds—still had not achieved a money laundering conviction at that time. I am happy to say that that is not the case now. As I say, we have not analysed every report yet and we have actually just launched the beginnings of our review of the third round process which, as I have indicated, is not complete yet in any event. However, a lot of countries that have had problems with a number of the more stubborn issues in relation to money laundering prosecution have actually achieved some convictions and indeed in some cases some quite long and deterrent criminal sentences. That said, I do not want to paint a picture that everything in the garden is suddenly rosy on this. There are still considerable hesitations in some countries about the levels and types of evidence that are needed to obtain successfully a money laundering conviction, particularly in autonomous money laundering cases (laundering by third parties, et cetera). I am thinking of the cases where you do not actually prosecute together with the predicate offence because it is easy to prove the underlying criminality if you are actually prosecuting the predicate crime at the same time. Similarly with self-laundering; self-laundering can be the easy cases to prove. The real test, certainly in the view of some of us at MONEYVAL, is actually how you can successfully prosecute third party laundering, particularly on behalf of organised criminals. There are certainly a larger number of investigations on-going at the moment in MONEYVAL countries than convictions that have been achieved, but a number of the amendments and modifications which we have put into the new Warsaw Convention have been drawn very much from the experience of some of these problems in practice in countries. I will give you one

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example, and that is the vexed question of whether you need either a simultaneous or a prior conviction for the predicate offence before you can obtain a conviction for money laundering. The experience in the evaluation process has shown that in a number of countries there was serious doubt about this particular issue and the doubt actually translates itself into hesitations by prosecutors to even test what their courts actually will consider suitable evidence to establish this part of the offence. We debated it long and hard in the context of the Warsaw Convention drafting and it was felt that there needed to be a clear mandatory provision in the new convention—which there is—which states that for those states that ratify the convention it shall not matter; it states unequivocally that there is no need for a prior conviction or indeed a simultaneous conviction for the predicate offence. If you look in the explanatory report we explain that one of the many ways that countries successfully prosecute these types of case is through inferences drawn from facts and circumstances; it is the way that a lot of prosecutors would approach this in the United Kingdom. Certainly we have experienced what I would call conservative judicial thinking which actually has some difficulties with this particular concept. We hope that with provisions like this we will see more success in the future.

Q501 *Baroness Garden of Frognal:* I think you have largely touched on this particular question which is about the forthcoming fourth round of MONEYVAL mutual evaluation. You have clarified also some of the methodology. You mentioned questionnaires and so on; perhaps you could elaborate a little on that and also the timeframe in which it will be carried out.

Mr Ringguth: We are starting the evaluations in the second half of the year. The normal evaluation cycle is approximately three years, which we would anticipate would actually dovetail with the time at which the FATF will have finished its present evaluation round and indeed decided with the associate members what the shape of future evaluations would actually look like. Perhaps there may have been a misunderstanding in terms of what we are doing in relation to the European Union directive because, for practical purposes, in the fourth round of evaluation what we are doing with the European directives is looking again at areas where the directives depart from FATF standards. We have established a number of areas—about 21 or 22 areas—where there are differences. We do not rate those in the way that we would rate the FATF standards which are the global standards, but we do make recommendations to our countries in relation to that.

Q502 *Chairman:* I wonder if I could ask you to deal with two points and give us some written evidence on them. One is question eight which is on the infrequency with which international cooperation was being sought and obtained in practice. I think that is a very difficult question. We have also asked you about Azerbaijan; could you let us know what happened about Azerbaijan?

Mr Ringguth: So far as the public statements are concerned, I perhaps should make it clear that ever since MONEYVAL was set up we have had within our procedures what we call compliance enhancing procedures. I think we have set out in the memorandum that these are a graduated series of steps. We have used them in relation to a number of jurisdictions over the years. I think it is fair to say that as a result we have actually been able to sort out problems within MONEYVAL in relation to individual jurisdictions using these procedures. Perhaps one of the unique features of MONEYVAL is that it is a Financial Action Task Force regional body but it also works within the institutional framework of an inter-governmental body, the Council of Europe, so at various stages of the compliance enhancing procedures the mechanisms of the Council of Europe are actually brought into play. The president can draw the attention of the secretary general to a particular problem and indeed the secretary general can raise it in his diplomatic contacts with individual countries. In this way we have been able to sort out a number of problems in relation to countries, perhaps going as far as a high level mission, but this is the first time that we have been faced with the decision of going to step six, which is a public statement. I am sure you understand that this step was taken only after very long deliberation in relation to it. I would also say that it was actually a very difficult decision to make. It means that we are the only FSRB to have made a public statement about one of its own members and that is actually quite difficult to do in the context of the people you are working with regularly in the meetings.

Q503 *Chairman:* Did it work?

Mr Ringguth: I am pleased to say that there is progress. We have made a second public statement after the last plenary meeting which recognised that steps had been taken by Azerbaijan after the December statement and an AML/CFT law has now passed and is indeed in force, although the whole legal framework—the enabling measures—is still to be brought into effect as I understand it at the moment in Azerbaijan. We very much wanted to reflect the progress that had been made by the country in the latest statement although the first statement still remains in effect. I am pleased to say that both statements have been prominently

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displayed on the FATF's website. We have had considerable feedback from our own countries as to the steps that they have taken to draw our concerns about the AML/CFT system in Azerbaijan to the attention of their financial institutions. Mainly it has been done on FIU websites et cetera, sometimes by the financial services authorities in the individual countries. Also we are very gratified that a number of FATF countries have also taken similar steps, including the United Kingdom (our statements I think are on the UK Treasury website). We are also very encouraged that last week the Financial Action Task Force asked for feedback from all its members and observers as to the steps that they had taken in respect not only of their own statements in relation to countries like Iran et cetera but also in relation to the MONEYVAL statements on Azerbaijan which will be very welcome and we know that certain FATF countries and a number of European countries have taken similar steps.

Q504 Chairman: What do you see as the major challenges facing European and international efforts to effectively combat money laundering?

Mr Ringguth: I could list a whole range of issues I am afraid.

Q505 Chairman: Would you like to put them on paper?

Mr Ringguth: I could do that. Perhaps if I could sum it up I think one of the major issues going forward is actually embedding all the standards that exist in AML/CFT, particularly on the preventive side, into real, effective implementation in countries. It is very easy to pass laws et cetera in relation to either external stimulus (directives et cetera); it is another thing to actually get effective implementation. Also really linking up all the themes I hope I have tried to get over this morning, we believe that there is actually still much more to do in obtaining major money laundering convictions and major deterrent confiscation orders. For all the expense that goes into the preventive side, what is coming out of law enforcement in a lot of countries is not that great compared with the resources that are being put into this on the preventive side. Those are areas I would certainly flag up.

Chairman: We look forward to receiving your written answers. Can I thank you very much for coming; it has been extremely helpful for the Committee. Speaking for myself I did not know a vast amount about MONEYVAL, now I know a bit more. Thank you very much indeed.

Supplementary evidence by Mr John Ringguth, Executive Secretary, MONEYVAL

QUESTION 1

The same reviews also drew attention to the infrequency with which international cooperation in the restraint and confiscation of the proceeds of crime was being sought and obtained in practice. Given the high compliance ratings in the sphere of international cooperation achieved in the third round of mutual evaluations (your memorandum at pages 6-10) are we to understand that the practice in this area has improved? If not, what is the explanation?

There is a high degree of consistency between the two assessment bodies in their ratings of R.38 in EU countries. Of the FATF EU countries so far evaluated, five countries have received Compliant (C) ratings, and five Largely Compliant (LC) ratings. Of the 12 EU MONEYVAL countries, three received Compliant ratings, seven Largely Compliant and two Partially Compliant (PC) ratings. No country received a Non-Compliant (NC) rating.

For the purposes of evaluations:

- C means that the Recommendation is fully observed with respect to all essential criteria (and the recommendation is implemented effectively).
- LC means that there are only minor shortcomings, with a large part of the essential criteria being met.
- PC means that the country has taken some substantive action and complies with some of the essential criteria.
- NC means that there are major shortcomings, with a large majority of the essential criteria not being met.

Where a European country receives a high rating, there is, or should be, an authority in place in that country to take expeditious action in response to requests for international cooperation in restraint and criminal confiscation. It should be borne in mind that all Council of Europe countries, including the 27 European Union States, have ratified (and have had in force for several years) the 1990 Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime (the Strasbourg Convention), the provisions of which cover in a legal instrument the mandatory requirements of Recommendation 38.

However, meaningful statistical information on the extent of practice on all areas of international cooperation covered by this Recommendation (and which would demonstrate effectiveness of implementation) is frequently either unavailable or available only in part. Sometimes assessors are told that countries have not received relevant requests in this area.

Thus the generally positive ratings across the board do not necessarily mean that the practice in this area is improving across the board.

The question therefore raises two issues:

- should the absence of practice on all or some of the mandatory aspects of Recommendation 38 be reflected more negatively in the ratings the assessment bodies give?
- does Recommendation 38 remain adequate to cover this area of international cooperation?

Usually, 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. Thus, it is our understanding that a country which meets all the essential criteria but cannot demonstrate effectiveness of implementation would normally expect to receive a rating no lower than LC. Double downgrades on effectiveness issues are comparatively rare.

In the forthcoming review, 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. If there are no requests for cooperation in the area covered by Recommendation 38 and none of its requirements have been tested at all, the examiners need to explore fully with the country concerned all the possible reasons for this. In some situations there may possibly be a case in future for considering a double downgrade where the theoretical position has never been tested in practice. Work could also be done on trying to articulate more precise effectiveness indicators than have been developed so far specifically for this Recommendation.

The larger question is the continuing adequacy of Recommendation 38 itself in its present form. In our view the first part of the Recommendation which is in mandatory terms remains appropriate and should continue to be reflected in any revision as it is. However, as noted in answers to earlier questions, the ability to recognise and enforce non criminal confiscation orders is currently an additional element only and does not count for ratings purposes. This critical area of international cooperation also needs, in our view, to be considered for inclusion in the essential criteria for Recommendation 38.

There are other areas of the Recommendation itself which could also be strengthened. Essential criteria 4 and 5 are quite weak. They only require States to consider establishing asset forfeiture funds and to consider authorising the sharing of confiscated assets with other countries where coordinated law enforcement action has resulted in successful confiscation procedures. These requirements could also usefully be revisited. The latter criterion in particular in its present form provides little incentive for States to share such assets, which itself may inhibit the pursuit by national authorities of assets hidden abroad.

QUESTION 2

What in your view are the major challenges facing European and international efforts to combat effectively money laundering and the financing of terrorism?

It is important that States individually and collectively regularly conduct threat assessments and typologies exercises so that they are positioned to respond adequately to new challenges and techniques in AML/CFT.

That said, in our view, the immediate challenges going forward are more basic:

- to embed the existing preventive standards into effective domestic practice in all countries.
- to improve the performance of law enforcement in many countries on AML/CFT issues.

The private sector puts huge resources into compliance systems. By comparison, the results which the private sector sees being achieved by law enforcement are modest at best in terms of major money laundering convictions against third parties who launder on behalf of others, and in terms of deterrent confiscation orders (particularly confiscations which may have a significant disruptive effect on organised crime). A major challenge is to improve results on the repressive side.

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 by investigators skilled in modern financial investigative techniques (in parallel with the investigation of the predicate offences);

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- 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 (and in the enforcement of subsequent confiscation orders);
 - in the negotiation and implementation of asset sharing agreements so that proceeds are shared by the authorities of countries involved in coordinated law enforcement action on confiscation – which itself should act as an incentive to more coordinated law enforcement action in this area.

Additionally, on the law enforcement side, it is submitted that a stronger response is still required by many countries to the continuing challenge of cash smuggling (whether in bulk or by individual cash couriers). Despite the ever-growing sophistication of new money laundering techniques, the identification of simple criminal cash movement across borders remains a significant law enforcement challenge.

WEDNESDAY 13 MAY 2009

Present	Faulkner of Worcester, L Garden of Frognal, B Harrison, L Henig, B Hodgson of Astley Abbotts, L	Jopling, L (Chairman) Marlesford, L Mawson, L Richard, L
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Examination of Witnesses

Witnesses: MR SEAN MCGOVERN, General Counsel, Ms LOUISE SHIELD, Head of Communications, and MR ANDY WRAGG, Senior Manager, International Regulatory Affairs Team, Lloyd's, examined.

Q506 Chairman: Good morning and welcome. Perhaps, Mr McGovern, you would like to introduce yourself and your two colleagues.

Mr McGovern: Thank you. I am Sean McGovern, I am General Counsel at Lloyd's. This is Louise Shield, who is Head of Communications at Lloyd's, and Andy Wragg, who is Senior Manager at Lloyd's who deals with money laundering and financial crimes issues for us. I would like, if I may, to begin with a brief opening statement to set the context for the comments I wish to make but also for answering the questions the Committee may have for me.

Q507 Chairman: That would be most helpful.

Mr McGovern: Lloyd's is the world's leading specialist insurance market-place covering some of the largest, most individual and complex risks around the world, and we can trace our history back some 300 years to Edward Lloyd's coffee house. It is important to understand, however, what the structure of the Lloyd's market is. Lloyd's is not an insurance company but an insurance market where 86 syndicates compete to provide insurance and reinsurance solutions to clients from all over the world. Together the syndicates underwriting at Lloyd constitute one of the largest insurance and reinsurance markets in the world. Each syndicate is made up of one or more members of Lloyd's. Historically, members of Lloyd's were individuals, but today there are less than 800 individual members of Lloyd's who are actively participating, providing less than five per cent of Lloyd's capacity. The remainder of Lloyd's capacity is provided by members who are backed by private and public shareholders, investment funds and specialist insurance investors. Each syndicate is managed by a managing agent. It is the responsibility of the managing agent to employ underwriting staff and manage the syndicate on the members' behalf. All managing agents are regulated by the Financial Services Authority. The Corporation of Lloyd's oversee the activities of the market, admitting new members and new managing agents, approving business plans and ensuring solvency. The

corporation does not carry on insurance business itself but supervises the market's activities. We, the Corporation of Lloyd's, are also regulated by the FSA. I am the General Counsel of the Corporation of Lloyd's and I am responsible for its legal and regulatory affairs. With that as background to the structure of the market, I would like briefly to comment on the areas I believe the Committee would like me to address this morning and then, of course, I will be very happy to take any questions that you may have. First, money laundering. The general insurance sector is regarded as being subject to a low risk of money laundering. To reflect this, general insurance activities fall outside of the money laundering regulations. We are, however, covered by the Proceeds of Crime Act 2002. My views and comments today will be limited to the general insurance sector as, other than a relatively small amount of term life assurance, the Lloyd's market does not write much life business. Notwithstanding the relatively low risk of money laundering, Lloyd's takes the management of the risk very seriously. Each managing agent has its own money laundering reporting officer, and the Corporation issues guidance to the market regularly on legal issues and best practice. With regard to suspicious transactions, as a practical matter it is the managing agents in the market who would usually be the first to identify suspicious transactions. However, once identified, the most common method for reporting that suspicion is for them to pass the report to Lloyd's, who will then pass it on to the Serious Organised Crime Agency. Receiving this data centrally allows us to monitor the risk more broadly within the market and to spot emerging trends. The Corporation will also handle any consent requests on behalf of the market, although, for reasons I can explain, those are a relatively rare occurrence. Second, the payment of ransoms. I understand you would like me to address the question of the role of insurers when ships are seized and ransoms are demanded. It is obviously topical with the escalation of incidents in the Gulf of Aden. There are two points I would like to make at the outset. First, at the risk of stating the obvious, the

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issue needs to be approached with some care. It is a very complicated situation that has its roots onshore. Piracy is a symptom of a much broader problem in Somalia, and, ultimately, there are lives at stake. Whilst the payment of ransoms is unpalatable, to date the human cost has been relatively small. Second, in light of some of the evidence that I have read that has been given to the Committee, I would like to clarify the role of insurers in the payment of any ransom in these circumstances. As a general principle, whether insurance is provided through hull coverage, hull war-risk cover, cargo cover or, in relatively rare cases, stand-alone kidnap and ransom cover, insurers do not get involved in negotiating with pirates and do not get involved in making payment. Insurers stand behind the insured and provide, after the event, indemnification for the insured's loss. That concludes, My Lord Chairman, my introductory comments and I am very happy to take questions.

Q508 Chairman: Thank you. That is most helpful. Before I ask the first question, perhaps I could say, for the record, that many years ago I was a name at Lloyd's but have not been for a long time. The annual SAR (suspicious activity report) for 2008 states that in the year 2007-08 the insurance industry made 1,434 suspicious activity reports. I wonder if you could give us examples of the sorts of matters on which the insurance industry makes reports. In what circumstances does the industry have to seek consent for transactions?

Mr McGovern: It is likely that the majority of the SARs filed by the insurance industry relate to whole life assurance, and, as I said, that is not necessarily an area that the Lloyd's market write. The risk of money laundering around the sale of general insurance is, as I said in my opening remarks, considered a low-risk. That is principally because, once a criminal has successfully disguised the proceeds of crime, they will want to reintroduce those funds back into the legitimate economy, and in general insurance, which does not have the investment aspects that you often find with life insurance products, that is quite a difficult thing to do. The way in which you could introduce those funds back into the real economy, the legitimate economy in general insurance, tends to be either through making a claim or through requesting a return of premium. That added dimension, particularly given the additional scrutiny that the insurance industry would place around the validity of a claim, generally, in our assessment, means that a criminal's flexibility to use general insurance as a means to launder money is quite restricted and they often look for easier routes to bring money back into the economy. Having said all of that, in 2008 Lloyd's filed 70 suspicious activity reports. The majority of those reports were where managing agents had suspicions around the reasons as to why an individual

or a company was seeking insurance cover, and in all cases the cover was declined. A large proportion of those related to international fine art, jewellery, gemstones, cash in transit and those kinds of things, and underwriters are generally suspicious about the criminal either seeking to use the existence of a Lloyd's policy to gain legitimacy with third parties or to inflate asset values within the company by claiming they had assets that they do not have. To give you an example: we often find that we will have approaches from individuals to insure a gemstone, and trying to get clarity over the existence or otherwise of this gemstone is often difficult. That is a fairly regular attempt that is made by criminal entities. The other aspect that we see is trying to buy a Lloyd's policy to cover an asset and either inflate its value or the asset does not belong to the company or individual who is seeking the insurance, and then they will try to use the existence of a Lloyd's policy to go to a financial institution to raise finance off the back of a fictitious or inflated asset. In our experience, seeking consent is relatively rare in general insurance, but we have sought consent from SOCA on a couple of occasions in relation to paying a claim or paying a return premium. To give you an example of one of those: we had a claim for a stolen car, a very expensive car, a Ferrari, and the investigations around that claim led to concerns as to how that individual had come to be able to afford such an expensive car, and also it was clear that the individual had made various misstatements at the point at which the policy was purchased. The insurers wanted to avoid the policy because of those non-disclosures and misrepresentations at the point at which the policy was taken out. In the case of avoidance you would pay the premium back to the policyholder, and so we sought SOCA's consent to return the premium to the individual concerned. Those are examples of where we have seen it. It is pretty rare. I hope that is helpful.

Q509 Lord Hodgson of Astley Abbots: When you say Lloyd's get the SARs from the managing agents, does that mean managing agents are relieved of a duty to make a report to SOCA?

Mr McGovern: This is something we have talked to SOCA about. They can, if they wish, make a report directly to SOCA. If they choose to make a report through Lloyd's, theoretically there is an issue. If Lloyd's did not pass that referral on to SOCA, then it does not necessarily satisfy their obligation to make a suspicious activity report. As a practical matter, SOCA quite like the consolidated role they play because it helps to funnel suspicious activity reports through to them. But we do not do any filtering, we pass them straight on to SOCA, so the risk to managing agents concerned is very low.

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Q510 Lord Hodgson of Astley Abbotts: What is the position where the underwriting is technically done offshore? It might be done in the Channel Islands. Where they have a money laundering agency. Do you liaise with that? Or it might be done, perhaps, in areas which have less heavily policed arrangements.

Mr McGovern: All of Lloyd's underwriting is either done in London or where it is done offshore it is done on an agency basis. A responsibility that we expect managing agents in London to discharge is that all of their activities, wherever it happens, complies with any relevant legislation, whether that is in the UK or any local legislation, and we take steps to give them guidance on that.

Q511 Lord Hodgson of Astley Abbotts: Do you have any evidence of insurance brokers and clients using the system in any way to avoid/evade/minimise their tax?

Mr McGovern: I cannot speak on the part of insurance brokers. Obviously the relationship that should exist between a client and their insurance broker means that brokers should be in a far better system than the insurers to come to a determination about the whys and the wherefores of a request for insurance and any suspicions that may be aroused in that context. However, we have very little experience of notifying to SOCA in relation to potential tax evasion, but we would expect that both the insurance brokers and the managing agents, if they had a suspicion that the purpose of the insurance policy was to evade tax, would file a suspicious activity report, but we do not have much direct experience of that.

Q512 Baroness Garden of Frognal: We have heard from the Law Society, the British Bankers' Association and the Institute of Chartered Accountants in England and Wales that they would like more feedback from SOCA to persuade them of the value of the effort they put into making the SARs, which take quite a lot of work and effort together. What is the position of Lloyd's? How do you rate the feedback that you get from SOCA?

Mr McGovern: I think it is fair to say that we would share those comments. We do not get feedback from SOCA. We are not sure why that is. It may be that because the international dimension of a lot of Lloyd's business means that SOCA is passing that information on to other financial investigation units, but we have no transparency around what they do with the information once they receive it. 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.

Q513 Baroness Garden of Frognal: Does that cause you any difficulty with the managing agents in circumstances where you are being the transit, as it were?

Mr McGovern: No. As I said, because the managing agents are expected to do this as a matter of best practice, they all have money laundering reporting officers. It is something to which we attach a great deal of significance from a reputational perspective, albeit we would agree that general insurance is a low-risk environment for money laundering. We have not had any feedback from our managing agents that would suggest that they are in any way irritated by the lack of feedback from SOCA, but I think it would be helpful to know whether the information we are providing and the effort we are putting in to file those suspicious activity reports is useful in the fight against financial crime.

Q514 Lord Marlesford: I think I should also declare that I was a victim of Lloyd's, until rescued by Equitas in 1993, since when I have taken no part. I understand, thanks to Mr Buffet, I have no further liabilities. I would like to ask about the consent regime, and whether or not you feel that the Home Office's refusal to change the consent regime was acceptable to you or whether you share the disappointment of the British bankers and others at the failure to do so. In particular, one has had the impression that you have been given a sort of nod and a wink that you do not have to comply. Would you prefer to have the consent regime that other people do? Would you prefer that the regime was changed so that it was clear what your position was?

Mr McGovern: As I have said, we do not find ourselves in a situation where we have to apply for consent that often. That is because, rather than us having a nod and a wink around compliances, the nature of the environment means that we are at low risk for this kind of activity. The concerns that have been expressed by the Institute and by the BBA, I suspect are particularly linked to the automation and expectation around speed of payments within the banking sector. Without being pejorative about my own industry, insurance does not have the automation that banks do around payments, and so, in particular, where we have sought consent, it is part of the claims process, and generally the claims process requires a period of adjustment, analysis and settlement. In our experience there is plenty of opportunity to build in time to request consent if that is necessary as part of that claims process, so the fact that the consent regime has not been changed is not a particular problem from our perspective. I can understand that when you get into the banking sector, trying to stop automated payments or, at least, an expectation around the speed at which payments will be made, will cause different issues. Our

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experience, where we have consent with SOCA, has been reasonably good. We have had no consent that has taken any longer than four days to be approved. I understand their concerns but we do not share them.

Q515 Lord Faulkner of Worcester: How burdensome is all this for the private regulated sector? We are getting different views. The Law Society says it is a disproportionate burden, but the British Bankers Association and the Institute of Chartered Accountants, whilst admitting it is quite large, say that it is necessary in order to preserve the reputation of the City. What view do you take about it?

Mr McGovern: We would agree that a robust system of anti money laundering is necessary to protect the reputation of the City. At Lloyd's, although not subject to money laundering regulations, we have said to our market that, as a matter of best practice, we expect them to comply. There are obligations within the FSA handbook around systems and controls for money laundering which do not apply to the general insurance sector, but, again, we have said to managing agents, "We want you to be able to satisfy those requirements, as a matter of best practice". I think that is a measure of how important we take the issue as a matter for Lloyd's reputation but also for the reputation more broadly. The regime is, in our view, proportionate. I think it is proportionate in the way in which the money laundering regulations do not apply to insurance, so there has been an element of a risk-based approach in defining the scope of the regulations, but, notwithstanding that, I do think that having a robust system of anti financial crime in the City is very important.

Q516 Lord Faulkner of Worcester: You think the Law Society is wrong, therefore?

Mr McGovern: I cannot speak for the Law Society. I would agree that I do not have any issues at all in terms of the corporation compliance activity around money laundering or the managing agents' activity around money laundering, and, as I have said, we have had no complaints from our market-place at all around the proportionality of the regime as it stands but, also, the extension of that regime that Lloyd's has applied to the market as an issue of best practice.

Q517 Lord Harrison: Mr McGovern, the payment of ransom is not currently a criminal offence in the United Kingdom law and no-one has suggested to us that it should be. However, the ransom, once paid, becomes the proceeds of crime and may well be used to finance terrorism. Do you believe it is right that shipowners and others collecting ransom money should be obliged to seek consent from SOCA for this? In your answers heretofore you have made

mention about seeking consent and you have offered a couple of occasions, but do you think the shipowners and the others ought to have a responsibility there to SOCA?

Mr McGovern: I have been interested to read and listen to the evidence that has already been put before the Committee around the application of the regime to this situation, and it is obviously a bit of a vexed areas. There does not seem to be any dispute around the fact that the collection and preparation of money for the onward transmission to meet a ransom demand is not a criminal offence. The question is whether or not in doing so they should seek consent. I note that the Government's position is that it is possible that the shipowners may be under an obligation to seek consent under the terms of the Act but that a prosecution in that context would not be in the public interest. I think that is probably the right outcome. I think we would have to think very carefully about the imposition of a consent regime and the extent to which that might hinder the ability of a shipowner to secure, in particular, the safety of crew in what can be quite delicate and time-sensitive negotiations. My assumption is that shipowners, if faced with this situation, whilst they may not be formally seeking consent from SOCA, would be in contact with the police and other relevant authorities to inform them that the situation is arising, but that is just an assumption that I have. There is a very clear distinction between criminal acts such as piracy and where there is evidence of terrorism or terrorist involvement. In that context, I imagine the shipowners would be looking to the Government to give them a very clear steer as to whether or not there is a risk that the activities are funding terrorists. We are, as I said, slightly removed from the situation because any payment we make indemnifying a shipowner is an after-the-event payment to a legitimate party, so from our perspective the issue of consent would not arise.

Q518 Lord Harrison: Do you think it is too mechanistic to have a regime where there would be an obligation, as such, to report to SOCA, given that you have given a very good example of why there ought to be some subtlety in terms of this.

Mr McGovern: I think that would be something that would have to be looked at. Clearly it would be unfortunate if shipowners felt constrained by a timetable that was too rigid. My perspective would be that one would not want to see the shipowners' hands tied in any way in trying to extract themselves from a situation that nobody wishes to be in.

Chairman: That is the sort of issue on which, if you have reflections over the next few days, you might like to come back to us.

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Q519 Lord Faulkner of Worcester: Have you ever had any suspicion that a shipowner who is insured with Lloyd's has colluded with a pirate and has effectively organised his own act of piracy so that he can then claim on the insurance?

Mr McGovern: That would be a suspicion that would arise in the payment of the indemnification. Absolutely, if during the course of dealing with that claimant there was a suspicion that there had somehow been some collusion.

Q520 Lord Faulkner of Worcester: Have you had any examples of that?

Mr McGovern: No.

Q521 Lord Faulkner of Worcester: None at all.

Mr McGovern: No.

Q522 Lord Hodgson of Astley Abbotts: If there was a still more rigorous scrutiny what would the impact be on the competitive position of the London insurance market and Lloyd's in particular?

Mr McGovern: Do you mean more broadly?

Q523 Lord Hodgson of Astley Abbotts: We are talking about seeking further consents. How would this impact the competitive position impact? Are we concerned about how scrutiny is carried out in other countries?

Mr McGovern: As I said, I am not concerned about the impact of the current consent regime because of the nature of the general insurance market. I do not think that if the consent regime is left where it is or is somehow made more onerous, that would have a particularly significant effect on the general insurance sector.

Q524 Lord Richard: Mr McGovern, one of the things which has been with us throughout the whole of this inquiry—and this is, after all, a sub-committee of the Select Committee on the European Union—is the extent to which there is co-operation within the EU on these matters, and particularly, since we have been looking at it, in relation to piracy. The British have one way of dealing with it, the French presumably have a different way, the Germans have a different way, the Italians have a different way. Can you give us some idea of the way in which other countries tend to deal with this situation? Are there any attempts that you know of by Lloyd's or, indeed, by the insurance world generally, to try to produce a more concerted European policy to this problem?

Mr McGovern: Of course the situation is a matter of great concern and of great interest to governments around the world and to the industry, both the shipping industry and the insurance industry. I have had conversations, for example, with the US Treasury, who have been asking exactly the sorts of

questions that you have been asking this morning around piracy and the role or otherwise of insurance in dealing with it. I would say that quite a lot of work has gone on and is still going on amongst governments and industry, and indeed navies, to try to come up with ways of dealing with the threat of piracy in the Gulf Aden, short of bringing the Somali pirates within terrorism legislation. I will give you an example of that. There has been a great deal of work done amongst governments, the shipping industry and the insurance industry, about giving advice to shipowners around how to travel through the Gulf of Aden. There is a very lengthy document, a best practice guide, which essentially has been compiled with advice from naval authorities, security experts, the insurance sector, which is all about trying to make passage through the Gulf of Aden safer. It is advice around navigational channels and advice around techniques that could be used to evade capture, et cetera—all of those things short of arming the vessels, which I do not think is something that the shipowners or the insurance industry would necessarily support.

Q525 Lord Richard: I was rather more concerned with the position where the piracy has taken place and where there is a ransom demand. We deal with it in this country in a certain way. How do the French deal with it? How do the Germans deal with it? Is there any communication between the industry as to how it should be dealt with?

Mr McGovern: Given the role of the insurers in responding to indemnification for payment of a ransom, I am not aware of any steps that are taken at the point of capture, and tactics or process that is applied in dealing with the pirates at the point at which the vessel has been captured. We come into the process at the point at which the ransom has been paid and the owner is looking for indemnification. That is not to say that there is not co-ordination and co-operation. It is just not something that I am personally familiar with.

Q526 Lord Richard: What do you indemnify them for? The ransom?

Mr McGovern: I was going to take the opportunity, if it is acceptable, to walk the Committee through the process by which the loss arises and how the indemnification process works, if that would be useful in answering the question.

Q527 Chairman: I think it would, if you would be good enough to do so.

Mr McGovern: In broad terms, this is how this type of insurance works: shipowners will generally buy annual cover which will cover them for the hull, the basic structure of the ship, and they will also buy separately annual war-risk cover. That is obviously only required to the extent that the vessel is likely to

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be travelling into territories that might be considered a war risk. In the majority of policies that are in the market, coverage for the piracy peril is in the war policy. That means that the underwriters can, during the course of an annual policy, adjust the terms to take account of changes in security situations around the world. For example, the most significant means of doing that is through a system of listed areas which are higher risk zones within which shipping travels. The Gulf of Aden is a listed area and has been a listed area since May of last year. If a ship is intending to travel into a listed area, they are under an obligation to notify the insurers of that intention. The insurer is then able to assess the risk in a more real-time basis, take advice from security consultants and, if necessary, impose additional terms. That may be the addition of some further premium to cover the vessel whilst it travels through the listed area, but it could also be other conditions, such as notifying relevant navies, sticking to fixed navigational channels, et cetera, and they are all designed to help manage the risk of the vessel travelling through the area.

Q528 Lord Richard: Who produces the list?

Mr McGovern: That is produced by the insurance industry. We have, in London, a Joint War Committee which is made up of marine insurers of both the London market and the Lloyd's market. They, together with specialist adviser from security consultants, define what listed areas there are. The process of attaching any conditions to a particular policy as a consequence of it being a listed area, is a matter of negotiation between the insurers and the shipowner. As I have mentioned previously, as well as adjusting terms and requiring notification to navies, et cetera, the industry has produced advice working with shipowners about how to deter pirates and evade capture. However, notwithstanding all of that, if the vessel travelling through the Gulf is attacked and taken by pirates, the process then is entirely driven by the shipowner. It will be the shipowner who will decide whether or not to negotiate with the pirates, to pay a ransom, and ultimately to deliver the payment. That is all handled by the shipowner. Assuming that the shipowner pays a ransom and the pirates release the vessel and it carries on with its journey, ultimately the shipowner has the right to claim the ransom payment through a process that is known as "general average" which is a concept of maritime law that predates the formal advent of insurance. You could substitute the word "average" for "loss," so "general loss". It means that all parties to an adventure at sea, to the voyage of a ship, effectively agree that if one party suffers a loss which is suffered in order to save the whole, then they will indemnify the one party who has suffered a loss to save the whole in proportion to the amount they would have lost if the venture had been lost entirely.

The claim then goes into what is known as general average, and all insurers involved with the venture would share proportionately the cost of paying the ransom. That would be the cargo underwriters, the hull underwriters, and the hull war underwriters. Therefore the insurers are only ever indemnifying the policyholder. In addition to annual hull cover, war cover, and cargo cover, there is another cover which could be in play in this process, although it is relatively rare, and that is stand-alone kidnap and ransom insurance. It is very difficult to get data on kidnap and ransom insurance because one of the key terms of having kidnap and ransom insurance is that you keep the existence of that insurance confidential. Breach of the confidentiality is a breach that could lead to the avoidance of the policy, but it is our understanding that less than ten per cent of the ships travelling through the Gulf are likely to have stand-alone kidnap and ransom cover. Kidnap and ransom cover primarily occupies two additional areas. The first is that the shipowner, on the kidnapping of a ship, would notify the kidnap and ransom insurers, and as part of the policy the kidnap and ransom insurers would procure for the shipowner a third party expert, security consultant, who would help the shipowner and advise the shipowner in handling the situation. Again, it is not something the insurer is involved in but is something the insurer covers the cost of. Kidnap and ransom insurance may also cover the shipowner for cash in transit, so, having decided to pay the ransom, he will then transfer those funds through one or more parties and obviously there is a risk that that cash will go missing during the process of making its way to the Gulf and kidnap and ransom insurance will often cover the shipowner for the potential loss of cash in transit. Again, all of this activity takes place without the involvement of the insurer and a claim would or would not arise after the ransom has already been paid. In terms of tying up all the loose ends, the application of the Proceeds of Crime Act and any terrorist financing legislation would not therefore apply to the transaction between the insurer and the shipowner because that is a transaction between legitimate parties for a legitimate purpose.

Q529 Chairman: Surely, with the 90 per cent of traffic which does not have kidnap and ransom insurance, any one of those people who was subjected to an attack would also use the services of the experts you referred to, the same people as would be assisting those who were covered. Would that be right?

Mr McGovern: That is probably right but they would just be covering the cost themselves. Instead of the shipowner being able to cover the costs of getting that advice through having bought a kidnap and ransom policy, they would just have to pay those security consultants directly.

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Q530 Lord Marlesford: It seems to me that you have made a rather a good case for the insurers not being liable—at any early stage, at any rate to make a suspicious activity report and therefore to ask for consent. On the other hand, you make it very clear that the shipowner is in the driving seat. Shipowners, I think I am right in saying, are not part of the regulated sector, so they would not be subject to the same obligation to make SARs as insurers are. Would that be correct?

Mr McGovern: I believe that is correct. Our assumption is that they are not part of the regulated sector and would not be covered by the same obligations.

Q531 Lord Marlesford: If one wanted to ensure that there was full notification in the case of kidnap and piracy, that would suggest that the regulated sector should be extended to include shipowners.

Mr McGovern: Possibly, if that was something that the Committee wished to recommend.

Q532 Lord Marlesford: The Treasury have indicated to us that their main reason for not wanting consent applications to be made, is that they are worried that they would in some way be compromised in the event of a later legal case, and the *quid pro quo* they have offered is that if a consent were not to be applied for when it would normally be required, they will give an *ex ante* undertaking not to prosecute. How happy are you with that, particularly in the light of the Lord Denning's ruling of January 1977 when he ruled against the Attorney General, in a not wholly dissimilar case, with the famous dictum: "Be ye never so high the law is above you." It was not seen as a discretion that the Attorney General had whether or not to enforce the law. Would it not, from your point of view, be safer if the obligation were made clear in statute, or lack of obligation, rather than a nod and a wink from the Treasury or indeed an exemption which has been given to us?

Mr McGovern: I think ultimately this is an issue for the shipowners and the risk that they are willing to take around the likelihood or otherwise of prosecution. My understanding is that any decision to prosecute for failure to make a report would be taken on a case-by-case basis—although I have seen the evidence that has been submitted by the Government on that point. I think it is a case of judging the objective of getting the kind of clarity that you have outlined versus ensuring, as I have said earlier, that shipowners are not somehow constrained and the flexibility is not constrained in how they extract their ship and, more importantly, their crew from this kind of situation, but I quite understand the point you are making.

Q533 Lord Marlesford: What you are really saying is that, although there would be no problem in making a suspicious activity report, the bit of it which can cause the problem is getting the consent to collect or pay the ransom.

Mr McGovern: I would have thought the issue would be about the timing.

Q534 Lord Marlesford: Yes, but there are two parts to this regime, are there not? There is the SAR.

Mr McGovern: Yes.

Q535 Lord Marlesford: And then, where it is necessary, to get consent. You have indicated that there would be information passed to the authorities as soon as such an incident happened, which often would be publicly known anyway, so there is no need really to change the rules about making a SAR, but maybe it would be necessary to have an exemption from asking consent, which would have to be statutory, from which the Government could be excused from giving consent.

Mr McGovern: That would satisfactorily deal with the issues that I would see with putting the consent regime into this kind of situation, yes.

Q536 Lord Hodgson of Astley Abbotts: Presumably if the vessel is flagged in Panama and the shipowner is operating out of Panama, technically it never touches these shores at all, so there is no SAR to be reported here because the Proceeds of Crime Act will not apply unless it is a British flagged vessel.

Mr McGovern: Yes, I think that is right. One of the problems is that unilateral action taken by individual governments can lead to results which either have intended consequences, create competitive challenges for our jurisdiction, and do not often always deliver the solution that you might like them to.

Q537 Baroness Henig: Neither Government guidance nor the guidance issued by the Financial Action Task Force seems to make specific mention of the financial transfer aspects of piracy. Would the insurance industry welcome such guidance?

Mr McGovern: Clarity would always be welcome. I know that you have heard from Sir James Sassoon who would be certainly in a better position than I to judge whether or not FATF would be an appropriate body to do that. I am aware of the limitations of the effectiveness of their action, given that there is not a stable government within Somalia. I think, given the position of the UK industry in these situations as I have described them, it is difficult to see how we would benefit from that kind of clarity, but that is not to say that clarity should not be sought, but there is then the question about which is the appropriate body to do it.

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Q538 Baroness Henig: Are you suggesting that you might welcome it but it would not necessarily make that much difference?

Mr McGovern: I think that is right. I do not think it would make a tremendous difference to us, but I think it probably would be helpful to others who face these situations.

Q539 Lord Mawson: I think you have answered some of this question, but I will ask it. At what stage might the insurers of shipowners who have paid a ransom become involved in negotiations for compensation? What obligations would be imposed on insurers by the Proceeds of Crime Act 2002 and other AML/CTF legislation?

Mr McGovern: I have set out, as you say, the way in which a shipowner would be identified. In terms of our obligations, we are involved after the event and we would view the payment of any money to the shipowner as part of that indemnification as being a legitimate transaction with a legitimate party. The Proceeds of Crime Act would not apply unless, as has been said, there was suspicion that there might be collusion between the shipowner and the pirates. As regards other anti money laundering legislation, the regulations would not apply to the general insurance sector and the counter-terrorism financing legislation again would not be applicable where we are paying money to a shipowner.

Q540 Lord Mawson: If the core business is about stopping money laundering, it seems to me it feels a bit like an elephant trying to catch a snake. For it to be effective, does there need to be a lot more flexibility and a greater attempt to innovate in this whole area

of the question of money laundering? I wonder what is your business view is on that.

Mr McGovern: Again, looking at this from the general insurance sector, where there is relatively limited application of money laundering, we would say that the way in which the money laundering regulations have been applied in the UK is quite innovative, particularly if you look at the way in which it has been applied in other jurisdictions. The risk-based approach that the FSA have taken and the way in which they have tried to embed the management of financial crime within the overall management of the business is pretty innovative. I think the absence of a rules-based approach to money laundering does give an opportunity, whether it is through bodies such as FATF and others, for there to continue to be room for innovation in how money laundering risk is managed, because we are not boxed in in the same way as other jurisdictions might be where flexibility may be much more constrained.

Chairman: I wonder whether any of my colleagues have any final questions they want to ask at this stage.

Lord Richard: I have a very indiscreet question.

Chairman: Indiscreet? Let us hear it.

Q541 Lord Richard: Do we have any idea or does the general public have any idea how much money has been paid out in these given ransom policies?

Mr McGovern: I doubt the public do and I certainly do not. I am not privy to that information.

Lord Richard: A very discreet answer.

Chairman: Mr McGovern, thank you so much for coming. I am sorry we have not heard from your associates, but you have fully answered our questions. You have been very clear and we are grateful to you for coming. It has been a most helpful session.

Written Evidence

Memorandum by the Association of Chief Police Officers of England, Wales and Northern Ireland (ACPO)

ACPO RESPONSE TO CALL FOR EVIDENCE—INQUIRY INTO MONEY LAUNDERING AND THE FINANCING OF TERRORISM

This paper is the response on behalf of ACPO to the call for evidence from the House of Lords concerning Money Laundering and Terrorist Finance. The questions raised in general concern the anti-money laundering structure within the UK which is predominantly the domain of SOCA.

However, each relevant section is reproduced with appropriate commentary below:

COOPERATION WITH AND BETWEEN FINANCIAL INTELLIGENCE UNITS (FIUs)

How effective is cooperation among FIUs and between FIUs and other authorities? What are the practical results of this cooperation?

This requires a response from SOCA. However, there is a strong relationship between the National FIU in SOCA and local Police Force FIUs which is a vast improvement than a few years ago.

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

This requires a response from SOCA.

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

ACPO have an open and honest relationship with the security services in respect of terrorist finance. ACPO have staff within SOCA to ensure close co-operation in respect of terrorist finance issues. There has been a huge expansion of counter terrorist resources with the creation of Counter Terrorism Intelligence Units and Counter Terrorism Units across regions. Each unit has embedded Financial Investigators with the specific remit of developing intelligence and investigating terrorist finance.

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

ACPO are unable to comment.

EU INTERNAL ARCHITECTURE

To what extent is the EU internal architecture adequate to counter current and future challenges?

ACPO would suggest that there may be scope for better exchange of ideas and methodology across Europe.

What are the respective roles of Europol and Eurojust on countering money laundering and terrorist financing?

Currently the impression within ACPO is that the relationship with these bodies is somewhat superficial. Having said that there is ongoing work to promote Europe wide initiatives to combat the financing of terrorism

INTERNATIONAL COOPERATION

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

This requires a response from SOCA.

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

The difference in legal systems across Europe has caused some problems but they are not insurmountable and are resolved in a pragmatic fashion.

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

This requires a response from HMRC.

EU-UN COOPERATION

What is the extent of EU-UN cooperation on financing of terrorism? What are the longer-term implications of the Kadi judgment?

Much of the European response to Money Laundering is guided, quite rightly, by the UN FATF directives. In that respect the EU is guided by the UN but the Kadi judgement suggests that the EU takes a position that fundamental Human Rights should be guarded across Europe even when terrorist cases are involved. This does not necessarily mean that there is a major conflict, merely that the EU still has to reflect its strong stance on Human Rights.

MONITORING IMPLEMENTATION

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

This requires a response from MLAC. ACPO are closely involved with the SARs Committee and work with other agencies to maximise the use of financial intelligence.

What are the implications of those results for cooperation within the EU and more broadly?

See above.

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

There are complaints from the private sector about the burden of compliance with anti money laundering provisions. However, ACPO would suggest that there needs to be some kind of strong regime to ensure that the UK maintains a good reputation for preventing money laundering. This can only lead to a better economic position and better intelligence to law enforcement to combat criminal activity. The use of suspicious activity reports is developing and useful material is found in many more SARs than previously. SOCA has been working hard with partners to accelerate this progress and that will continue.

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

ACPO are unable to comment as they have no knowledge.

COMPLIANCE AND EQUIVALENCE

What are the powers and procedures with respect to those third countries which fail properly to implement international standards in these areas? Are these adequate?

Does the 2005 Directive adequately encourage non-EU States which have introduced equivalent systems to counter money laundering and the financing of terrorism?

How does the system for determining equivalence operate in practice?

ACPO does not have a view on the three questions above.

Additional to the brief answers given above ACPO would like to add the following. It is true to say that the criminal justice system should review its capability and capacity in terms of money laundering investigation. UK legislation, most notably sections 327, 328 and 329 POCA 2002 are simple and well drafted. The intention was not simply to attack the flow of criminal cash but to legislate against all criminal property. Further, the burden of proof was lower than Section 22 Theft Act 1968 and catered for those instances where funds were moved electronically. Therefore, when discussing money laundering it is important that we maintain the widest focus and not fix investigators' thinking on cash movement but on "criminal property". We must also seek to de-mystify money laundering so that investigators and prosecutors understand that such matters can be reasonably straight forward and not require specialist skills. Certainly there are many cases that include a degree of complexity and specialist knowledge and all police forces have Accredited Financial Investigators to assist staff. These specialist Financial Investigators have all received the same training and must maintain accreditation. This has been one of the success stories since POCA became law. To demonstrate how simple a money laundering case can be, consider the following circumstances:

Child A steals a bag of sweets from a shop. Child B knows they have been stolen (or at least suspects them to be so) and hides the sweets for his friend, having eaten two or three.

Child B hides the sweets and so commits an offence under section 327 of concealing criminal property.

Child A and Child B make an arrangement to retain the criminal property and commit an offence under section 328 of retention of criminal property.

The children also use or possess criminal property—section 329.

Whilst it is unlikely that this legislation would be used in such a case, it merely serves to demonstrate that a case does not need to involve the transfer of millions of pounds worth of funds or goods by international criminals but that the legislation works across all levels of criminality. When considering terrorist financing it is true to say that such acts do not cost a lot to perpetrate. Therefore so such "low level" investigation and use of POCA may be appropriate. The legislation works at all levels of criminality and all law enforcement officers and local prosecutors should have a good basic knowledge of the legislation and its application.

Over the past four years there have been a string of contested money laundering cases and there has been some confusion concerning how to deal with money laundering. This lack of consistency has been problematic and it is only now that the "dust is settling". Further problems have been caused by the lack of quality data concerning money laundering investigation. There is no system to capture the numbers of arrests, prosecutions and conviction so it is difficult to identify transferable good practice and highlight problems for action, in order to try and address such problems, the ACPO team will be taking the following action in 2009:

1. development of clear practice guidance working with senior lawyers;
2. research with forces and CPS concerning current investigative activity and prosecutions;
3. support for the replacement of the Joint Asset Recovery Database (JARD) in order to try to capture better data;
4. re-writing of the 2006 Practice Advice on Financial Investigation to include new guidance and encourage activity; and
5. Renewed discussions with CPS.

If data quality can be improved then better informed field research can be conducted in an effort to improve performance and encourage more active interventions on those involved in the movement and use of criminal property.

In terms of financial information available from suspicious activity reports (SARs), ACPO continues to work with colleagues in SOCA to develop good practice. Changes in access to SARs have been useful and some forces are making as full a use as possible of the "entities" (telephone numbers, associates etc) contained within

these reports as well as examining the reports to see if investigations can be started immediately from the information contained therein. This material can provide a good source of valuable information for a range of investigation types and work to improve their usefulness continues.

As well as SARs, ACPO and NPJA are working to develop products to ensure police officers are constantly aware of opportunities to retrieve financial material for use in money laundering and other investigations. A range of specialised training products is already available and NPJA are working hard to ensure integration across all relevant police training material. This work will continue and should assist in improving the use of financial information and intelligence to improve the quality and number of money laundering investigations. Allied to this is work to improve knowledge of money laundering methodologies to assist staff to recognise opportunities for intervention.

Ian Davidson

Detective Superintendent
National Co-ordinator
ACPO Proceeds of Crime Portfolio

Memorandum by Iain Cameron, Professor in Public International Law, Uppsala University¹

1. In my written evidence, I will concentrate on only the issue of financing of terrorism, and largely on the method used, at UN and EU level, of the “blacklisting” of individuals and organizations suspected of involvement in, or financing of, terrorism. It is this method which was the subject of the Judgment of the European Court of Justice (ECJ) in the *Kadi/al-Barakaat* case² which is, in turn one of the topics the Select Committee requested comments upon.

2. I would like to begin by noting that I have written extensively on the issue of blacklisting. I wrote one of the first legal analyses of the issue, for the Swedish government, published in October 2002.³ I was asked to present my findings to diplomats on the Security Council which I did at a conference organized by the European Commission and the governments of Germany and Sweden in New York in November 2003. I was later asked by the Council of Europe to examine the issue from the perspective of legal safeguards for the individual, in the light of the European Convention on Human Rights.⁴ Most recently, I was asked by the European Parliament to look at EU sanctions more generally, including the question of their effectiveness.⁵

3. Terrorism, generally speaking, is a method for obtaining political objectives. In this it differs from organized crime, the primary objective of which is profit-making.⁶ Naturally, there can be overlap with the objectives of organized crime. The leadership, and/or the rank and file of a terrorist organization can, wholly or partially, be interested in maximizing their wealth. This could have been the original, concealed, motivation of the organization, or this motivation could have developed over the years, in the course of cooperation with organized criminality for common goals, or when the organization has otherwise come to realize what profits can be made. Especially in dysfunctional states where there are areas in which the central authority exercises only limited control, or has abandoned control altogether (occasionally called “state shells”) there can be a symbiotic relationship between organised crime and terrorism (the former can finance the latter, the latter can forward in different ways the goals of the former). Terrorist groups can thus on occasion become indistinguishable from organized crime, both in goals and methods. And the two phenomena also resemble each other in that, absent removal of the root causes, the “wars” against them risk being endless conflicts.

4. But generally speaking, for terrorist groups, money is merely the means to an end: sources of money are developed in order to finance further acts of terrorism. This has an obvious implication, namely that removing the financial means or specific finance channels will not end the danger of terrorism,⁷ or even, which is the secondary aim of countering organized crime, raise the “cost” of money laundering to the point that the criminals go somewhere else. I say this implication is obvious, but the international community did not seem

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² Joined cases C-402/05 and C-415/05 *Yassin Abdullah Kadi and Al Barakaat International Foundation v Council of the European Union and Commission of the European Communities* 3 September 2008.

³ Report to Swedish Foreign Office on Targeted Sanctions and Legal Safeguards, October 2002 (<http://www.jur.uu.se/Portals/5/SIFIR/Dok/sanctions.pdf> Cameron). An updated and reworked version of the report is published as UN Targeted Sanctions, Legal Safeguards and the ECHR, 72 *Nordic Journal of International Law* 1-56 (2003).

⁴ Cameron, *The ECHR, Due Process and UN Security Council Counter-terrorism Sanctions*, Report to Council of Europe, 6 February 2006. http://www.coe.int/t/e/legal_affairs/legal_cooperation/public_international_law/Texts_&_Documents/2006/I.%20Cameron%20Report%2006.pdf

⁵ Cameron, *Respecting Human Rights and Fundamental Freedoms and EU/US Sanctions : State of Play*, European Parliament, Policy Department, External Policies, October 2008, <http://www.europarl.europa.eu/activities/committees/studies.do?languageE>.

⁶ Cf. the definition given in Article 2 of the UN Convention Against Organized Crime, 2000 40 ILM 335 (2001) (Palermo Convention) “‘Organized criminal group’ shall mean a structured group of three or more persons, existing for a period of time and acting in concert with the aim of committing one or more serious crimes or offences established in accordance with this Convention, in order to obtain, directly or indirectly, a financial or other material benefit”.

⁷ See eg M. Kichling, *A Magic Formula which Can Do Away with Terrorism?* *Max Planck Research Bulletin* 1/2002.

to pay it a great deal of attention in the immediate aftermath of 11 September, when it rushed to expand existing money laundering concepts and methods into the area of terrorist financing.⁸

5. The crime of money laundering is built up around the concept of “dirty” money coming into the ordinary economy and being “cleaned”. By contrast, terrorism can use, and often does use, “clean” money for “dirty” purposes. One normal pattern of money laundering is that the income from criminal activity eg narcotics, in a rich Western state (where the profits are to be made), is collected in small accounts and then funneled to a larger account and then an offshore financial centre, whereafter it is then re-injected to the target economy. The anti-laundering monitoring system will thus look for this type of pattern. For the more traditional type of “separatist” terrorism—where, as already mentioned money is collected from supporters in richer countries and transferred out of these—this may be the norm. However, for the type of terrorism of, eg the 11 September attacks, the pattern is the reverse—a transfer of a large lawfully earned sum to a state where the target is situated, whereupon the sum is split into several working accounts used for preparing the terrorist act.⁹ Even this pattern may be lacking where the active cell is home grown and has its own lawful sources of income. Their transaction records, and account “profiles” here will show few, if any, suspicious tendencies.

6. The experiences of at least some European states indicate that the “usefulness” of money laundering as an offence is largely at the investigative level, allowing enquiries to be launched into a suspected criminal enterprise, during the course of which evidence can be amassed on other suspected offences—for which perhaps only limited suspicion might have existed at the time.¹⁰ In many countries with money laundering offences there seem to be relatively few convictions only for money laundering.¹¹ Instead, convictions tend to be for the predicate offence (eg robbery, or selling of narcotics)¹² together with money laundering. This is paradoxical in that the idea behind placing reporting requirements on banks was that an unusual or suspicious transaction report (STR/UTR) would lead to an investigation, the amassing of evidence of illegal transactions and a conviction for money laundering. But, at least in a number of European states this pattern does not seem to be the norm. Instead, evidence of money laundering comes to light during the course of other criminal investigations.

7. Similarly, so far, it does not seem to have been the case that terrorist suspects are identified because of their suspicious transactions, whereupon the accounts are frozen and criminal/forfeiture proceedings are brought against the accountholders. Instead, the terrorist suspects are identified on the basis of intelligence material whereupon the banks are informed, and accounts are frozen. This is not to say that accounts used by terrorists never generate UTR/STR, but these are lost in the vast number of other such reports.¹³ For example, the New York InterBank system handles 200,000 payments totaling \$1.1 trillion every day.¹⁴ Looking for the small sums required to commit terrorist outrages transferred over a period of months is like looking for the needle in the proverbial haystack.

8. The amount of money needed for terrorism obviously varies according to the goals of the terrorist group. A feature of the al-Qaeda sponsored attacks which have been made since 2001 is that they are relatively cheap.¹⁵ Explosives are not expensive, and can be homemade. A detonator is more difficult to make, but this is not overly expensive to buy. Evidence derived from Israeli interrogations of (frustrated) suicide bombers indicate that the major “cost” of a suicide bomber appears to be in delivering him or her to the target, although sometimes a type of pension for relatives is paid by the terrorist group or (if applicable) its state sponsor.¹⁶ In this area, it is not possible to avoid the essentially political issue of distinguishing, in practice, between legitimate and illegitimate uses of violence. This is at the heart of the problem. The fact is that there is, and will continue to be, large amounts of lawfully earned money potentially available to groups, particularly Palestinian groups, which some people (including the previous US administration) regard as being terrorist in

⁸ The FATF was well aware of the differences in tactics and strategies for dealing with the two phenomena. See Report on Money Laundering Typologies (2000–01), Doc. FATF-XII February 2001, at 19–20.

⁹ The National Commission on Terrorist Attacks on the US (the “9/11 Commission” <http://www.9-11commission.gov/report/911Report.pdf>) came to the conclusion that the 11 September terrorists were funded primarily by lawful funds made available by wire transfers from overseas to the US, the physical transport of cash or travellers cheques into the US and the accessing of funds held in foreign institutions by debit or credit card.

¹⁰ Kichling, *op. cit.* note 19.

¹¹ M. Kichling, *Die Praxis der Gewinnabshöpfung im Europa*, 2001, available at <http://www.iuscrim.mpg.de/verlag/Forschaktuell/Gewinnabschoepfung.pdf>.

¹² The term “predicate offence” is commonly used to mean any criminal offence as a result of which proceeds were generated that may become the subject of a money laundering offence.

¹³ As the UN expert group established to monitor the application of Resolution 1267, directed towards al-Qaeda, the 1267/1390 Monitoring Group note, at least one of the transfers to the 11 September terrorists was reported as a suspicious transaction, but this got lost in the mass of such reports. First Report, S/2000/541, 15 May 2002, para. 25.

¹⁴ Judicial Review Commission on Foreign Assets Control, Final Report to Congress, January 2001 (hereinafter, (Judicial Review Commission, 2001), available at www.law.stetson.edu, p. 140.

¹⁵ The Report of the Official Account of the Bombings in London on 7 July 2005, HC 1087, <http://www.homeoffice.gov.uk/documents/7-july-report.pdf?view=Binary> estimated that the London bombings cost less than £8,000, the overseas trips, bomb making equipment, rent, car hire and UK travel being the main cost elements (at para. 63).

¹⁶ L. Napoleoni, *Modern Jihad, Tracing the Dollars Behind the Terror Networks*, (Pluto Press, London/Sterling, 2004), p. 178–180.

character, but which many people, including many in the West, do not. There are groups which most people in the West would definitely regard as terrorist in character, in particular al-Qaeda. However, if even a tiny proportion of the money made available to Islamic charities by wealthy donors in the Middle East is siphoned off (directly or indirectly) to the latter group(s) there is more than enough money to keep a very large group of full-time terrorists in action.

9. So much on the background. To turn now to the specific issue of targeted anti-terrorist sanctions. All targeted sanctions operate by means of blacklists. A small number of “primary” targets are listed and subjected to restrictive measures (assets freezes, travel bans etc). A large group—indeed everyone within the targeter’s jurisdiction—is then made subject to obligations not to transfer, hold etc. funds or facilitate travel for etc. the primary targets. These obligations are backed by the criminal law. In other words, it becomes a criminal offence to assist the targets in any way to circumvent the sanctions.

10. Obviously, the procedure for determining the primary targets is of vital importance. As far as concerns the Security Council, it establishes a subordinate organ, a sanctions body, for each set of targeted sanctions adopted. This body draws up a list of people. In relation to sanctions against governments or quasi-governmental bodies which are engaged in activities threatening to international peace and security, the list is drawn up largely on the basis of diplomatic information. In relation to the anti-terrorism sanctions, that is, the Al Qaeda sanctions under Resolution 1267, intelligence material is the basis for many listings.

11. This material will consist to a large extent, as far as terrorist networks are concerned, of risk analyses. Such analyses, experience shows, can often be wrong. It is possible, and indeed, required by human rights standards, to provide for effective remedies even in such cases. However, there are legitimate national security concerns in maintaining the secrecy of this material. States are extremely reluctant to give this sort of material to each other, and, naturally, an international body. The adaption of targeted sanctions, originally directed at regimes, to apply to suspected terrorists, terrorist supporters, and terrorist groups has thus given rise to a further dimension of accountability problems.

12. Attempts have been made at the UN level since 2002 to improve the UN anti-terrorist sanctions. While marginal improvements have been made, the major problem of accountability continues: the blacklisting is by an executive body with no judicial remedies. As far as the al-Qaeda sanctions are concerned, security officials’ assessments that a particular person or group is financing terrorism are made in a particular state (almost always the United States). This assessment is then channelled through the diplomatic process in the Security Council. The diplomats in question will almost invariably have no understanding of the intelligence basis for the assessment and have no, or little, understanding of the countervailing dimension, namely that the freezing measures in question limit or curtail rights the target may have under constitutional or international law.

13. However, it is the juxtaposition of UN law with EC law which causes the real problem. Until the Kadi/al-Barakaat case, the EU method of implementing these UN sanctions—simply copying them into a common position, and then an EC regulation—gave these decisions direct effect and the status of supranational constitutional law in the 27 EU member states. ECJ case law allows for no constitutional challenges against an EC regulation before the courts of any member state. This situation is obviously absurd. The Kadi/al-Barakaat case has, however, not solved the legitimacy gap in the system. Opposition to the establishment of meaningful, as opposed to cosmetic, review mechanisms at the UN level is considerable. The authoritarian states on the Security Council quite simply do not understand what the fuss is about. The United States has so far also rejected all attempts to establish some form of review mechanism, even of the most modest kind (an ombudsman, a panel of independent experts etc.).¹⁷ The EC Commission, following the Kadi/al-Barakaat case has—supposedly—performed an independent check of the intelligence material forming the basis for the blacklisting decisions in these two cases. However, the EC Commission has no competence to engage in such an exercise, and everyone is aware of this.¹⁸

14. As far as concerns the EU’s own (autonomous) anti-terrorist sanctions, a state, or group of states, takes the initiative to propose a particular person or group for inclusion. Blacklisting proposals are primarily made by states the competent authorities of which are actively investigating a given terrorist organisation. The proposal is then circulated to the other members of the working group, usually at least two weeks before the relevant meeting of the group in Brussels. The representatives of the working group then consult other governmental officials in accordance with applicable national procedures. Whether or not there is any consultation with national parliaments depends upon constitutional mechanisms for control over EU/EC decision-making. Once agreement has been reached (and, as with all common positions, unanimity is required)

¹⁷ See Cameron, 2003 for a detailed treatment of different possible mechanisms. See also Watson Institute Targeted Sanctions Project, Brown University, White Paper Strengthening Targeted Sanctions Through Fair and Clear Procedures, 30 March 2006 www.watsoninstitute.org.

¹⁸ COMMISSION REGULATION (EC) No 1190/2008 of 28 November 2008 amending for the 101st time Council 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 OJ L 322 2.12.2008 p. 25.

the formal decision is taken in the Council, or in COREPER, by written procedure, meaning that a name is added if there are no objections to it. It is not made public which organisations have been the subject of discussions, nor which states have objected to inclusion.

15. Under Article 2 of the Common Position 2001/931/CFSP on the application of specific measures to combat terrorism, the EC, within the limits of the powers conferred on it by the EC Treaty, implements the freezing of funds etc of persons etc listed in the Annex to the Common Position by means of a regulation.

16. Under Article 3 of the applicable regulation,¹⁹ the participation, knowingly and intentionally, in activities, the object or effect of which is, directly or indirectly, to circumvent the freezing obligation shall be prohibited. Under Article 9 of the regulation, each Member State shall determine the sanctions to be imposed where the provisions of this regulation are infringed. However, in line with the standard EC formula, such sanctions “shall be effective, proportionate and dissuasive”²⁰.

17. The effect of this must be stressed. In practice, an EU external organization is made subject to an organizational ban: it cannot receive money or any other assets and it is a criminal offence for anyone to hold money or assets for the organization, or assist it economically in any way. No organization can operate in such circumstances. The EU’s own anti-terrorist sanctions have a “knock-on” effect on the freedoms of association and expression which are considerable (dealt with further below).

18. Where EU internal groups are listed, these are subject only to Article 4 of the Common Position which provides that Member States through police and judicial cooperation within the framework of the PJCC are to afford each other “the widest possible assistance in preventing and combating terrorist acts”.²¹

19. No mechanism of judicial control was established for EU autonomous anti-terror sanctions. However, the Court of First Instance (CFI) of the EC has established some minimum rules in, most notably in *Modjahedines du peuple d'Iran, [PMOI] v. Council of the European Union*.²² The CFI has only set very low standards on the issue of the evaluation of the material evidence for a blacklisting.²³ The Council has been given a large degree of discretion, even if, in the latest case, the CFI found that the Council had overstepped even this wide mandate.²⁴ The EU blacklisting system is essentially a diplomatic device for signaling disapproval of a given organization, but it is one which has very real criminal law effects at the national level. The real issue is the “appropriateness” of blacklisting. This involves looking inter alia at the following issues: that the terrorist acts for which the organization in question is accused are really attributable to the organization, that these are not isolated incidents, but go to the policy of the organization itself, that the “benefits” of making fund-collecting for this organization outweigh the “costs” in terms of the inevitable “overspill” restrictions in freedom of association and expression of people resident in EU states pursuing the same political goal as the organization, but not advocating terrorist means.²⁵ This is the sort of review performed by courts in states where it is possible to criminalize organizations for anti-constitutional activities. However, I think it will be very difficult to have such a type of judicial review at the EU level. Certainly, the CFI or the ECJ are not the correct type of body, applying the correct type of criminal procedure, to engage in such a review. And there are huge evidential difficulties. The sort of intelligence material which states have will quite simply not be submitted to a supranational body.

20. As regards the procedures for both EU and UN blacklisting, it is important to stress the differences between this and the normal procedure followed by the police and prosecutor in freezing assets in investigating crime. In national systems, the freezing of assets is an interim measure taken pending a judicial determination of a person’s involvement in criminality. It is a temporary measure that can be challenged in court before an independent and impartial judge, at the latest, when the criminal trial takes place—a trial which, according to

¹⁹ EC Regulation 2580/2001 27 December 2001, OJ L 340, 28.12.2001 p. 70.

²⁰ See Judgment of 21 September 1989 in C-68/88 Commission of the European Communities v Hellenic Republic [1989] ECR 2965.

²¹ The Council adopted a decision implementing this PJCC duty by providing for an obligation on states to cooperate with each other and Europol and Eurojust in relation to intelligence exchange of the persons and groups listed, 2003/48/JHA on implementation of specific measures for police and judicial cooperation to combat terrorism, [2003] OJ L 68 19.12.2002 p.16.

²² Case T-228/02, [2006] ECR II-4665.

²³ Ibid. at para 159 “Because the Community Courts may not, in particular, substitute their assessment of the evidence, facts and circumstances justifying the adoption of such measures for that of the Council, the review carried out by the Court of the lawfulness of decisions to freeze funds must be restricted to checking that the rules governing procedure and the statement of reasons have been complied with, that the facts are materially accurate, and that there has been no manifest error of assessment of the facts or misuse of power. That limited review applies, especially, to the Council’s assessment of the factors as to appropriateness on which such decisions are based”. See also Case T-256/07, *People’s Mojahedin Organization of Iran v Council*, 23 October 2008 para. 134 “In the case of an initial decision to freeze funds, the burden of proof essentially relates to the existence of precise information or material in the relevant file which indicates that a decision by a national authority meeting the definition laid down in Article 1(4) of Common Position 2001/931 has been taken with regard to the person concerned. Furthermore, in the case of a subsequent decision to freeze funds, after review, the burden of proof essentially relates to whether the freezing of funds is still justified, having regard to all the relevant circumstances of the case and, most particularly, to the action taken upon that decision of the competent national authority.”

²⁴ *People’s Mojahedin Organization of Iran v Council* Case T-284/08, 4 December 2008.

²⁵ Cameron, I., EU Anti-terrorist Blacklisting 3 Human Rights Law Review, 225–256 (2003).

Article 6 ECHR, must occur within a reasonable time. At the UN and EU level, these sanctions are not interim measures pending a judicial determination, they are alternatives to judicial determinations.

21. There is little or no evidence that UN anti-terror sanctions have any significant effect on the financing of terrorism. The efficacy of targeted sanctions in general is highly disputed. A select committee of the House of Lords recently produced a skeptical report on the value of target sanctions.²⁶ To the extent that targeted sanctions have any effect it tends to be on the reputational level. When this already doubtful method is used as a method for combating terrorism little in the way of concrete successes can be expected. For a variety of reasons set out before, the idea that “going for the money” by means of blacklisting in Western states will have any preventive effect on what has been called “Caliphate” terrorism is profoundly mistaken.

22. There is an uneasy co-existence with these supposedly preventive measures and traditional crime detection and prosecution methods. The basis for these measures is suspicion of terrorist financing. However, for all states which have ratified the 1999 UN convention on the matter, financing of terrorism is a crime which should be dealt with by investigation, prosecution and trial. Where a conviction follows, assets temporarily seized pending the trial can be confiscated. The UN measures have now gone on for a very long period of time. The “war against terror” will never end: will the seizures also be permanent? If so, a standard which is quite correct for investigation of crime—suspicion—is being used to justify forfeiture, without, moreover, any judicial involvement whatsoever.

23. The EU measures do not involve the same, Kafkaesque, total absence of judicial safeguards. However, these suffer from major problems too. First there is the point above, that the suspicion standard becomes a forfeiture standard. Second, the blacklisting is an executive decision, with little or no control by the courts. The criminalization (in effect) of an organization is a very blunt instrument of criminal policy. It means that a broad category of activities by people who are, or are suspected of being, linked to a blacklisted organization, also come under the scrutiny of the police and security services. Scrutiny in itself may not be a serious problem, although it can waste the time and resources of the police and security services. However, the use of coercive investigative measures, bugging, telephone tapping, data checks etc. against people linked to a blacklisted organization naturally involve restricting the right of privacy. The effect of being “tainted” with a link to a blacklisted organization can be the denial of employment, immigration and citizenship. Where the issuing and distribution of information is made more difficult, the rights of association and expression are being limited. The state must naturally be able to defend itself. All of the above rights can be, and must on occasion be, limited in democracies fighting against serious crime. However, where an instrument used is too blunt, the price in terms of “collateral damage” can be too great. The legitimacy of a state engaging in all-too wide defensive measures is undermined.

24. The primarily diplomatic and “window-dressing” nature of EU blacklisting sanctions is confirmed by the total lack of an official EU evaluation of the legality, efficacy and appropriateness of these measures. They were not part of the EU evaluation made recently into its money laundering measures. These measures are not integrated into the criminal law paradigm of investigation and prosecution, and, as mentioned above, cannot be.

25. The CFI and the ECJ are pursuing the approach of elaborating, on a case by case basis, supranational judicial review safeguards for EU sanctions. I think that the time is not yet ripe for such a body at the EU level. The way forward I would say instead lies in an acceleration of cooperation within the framework of justice and home affairs, building upon the principle of mutual recognition. If individual states choose to “blacklist”, instead of pursuing allegedly terrorist organisations by criminal means—which is what they really should be doing—then they should be obliged to provide adequate remedies at the national level for such blacklisting. There should be no blacklisting at all at EU level. Instead, a national blacklisting, to the extent that it requires extraterritorial enforcement, can be enforced by means of the principle of mutual recognition (with, if necessary, an *ordre publique* safeguard allowing the enforcing state to refuse cooperation). It is long due for the discussion of anti-terrorist sanctions to be moved from the level of symbolic, diplomatic initiatives and fitted into the wider discussion of how best to ensure effective anti-terrorist cooperation measures in the EU, while maintaining respect for human rights.

30 January 2009

²⁶ House of Lords, Select Committee on Economic Affairs 2nd Report of Session 2006–07, *The Impact of Economic Sanctions* Volume I: Report, 9 May 2007 HL Paper 96-I.

Memorandum by Eurojust

1. OVERVIEW

With this report Eurojust (EJ) wishes to contribute to the Inquiry “EU and international cooperation to counter money laundering and the financing of terrorism” published on 18 December 2008 by the House of Lords (Select Committee on the European Union—Sub-Committee on Justice and Home Affairs).

This report focuses on the specific role of EJ in the fight against both money laundering and terrorism financing, expressly included as one of the key points of the Call for Evidence.

Eurojust, the Judicial Cooperation Unit in Criminal Matters of the European Union, was established by the Council Decision of 28 February 2002²⁷ (EJ Dec) with the aim of improving the coordination of investigations and prosecutions of the Member States of the European Union and promoting the cooperation between their judicial authorities in cases of transnational and serious crime (art. 3 EJ Dec).

Laundering of the proceeds of crime is mentioned in the list of competences of EJ (art. 4.1(b) EJ Dec) and constitutes an area with special relevance to its daily work. Financing of terrorism is not expressly mentioned but it is included in the general competences of EJ, which cover “the types of crimes and the offences in respect of which Europol (EP) is at all times competent to act pursuant to Article 2 of the EP Convention (EP Conv) of 26 July 1995” (art. 4.1(a)). The cited Article 2 of the EP Conv includes the “crimes committed or likely to be committed in the course of terrorist activities”.

Both money laundering and terrorism financing usually have a transnational dimension and require specific and well-coordinated investigations and prosecutions between the Member States of the European Union. EJ provides the competent national authorities with the necessary support, ie, facilitating the execution of mutual assistance requests and European orders based on the principle of mutual recognition. EJ also organises coordination meetings to facilitate the exchange of information and the simultaneous execution in different Member States of searches, seizures or arrests of suspects, and the practical application of special investigative techniques.

The setting up of Joint Investigation Teams (JITs) is highly promoted by EJ, as a useful instrument in the fight against money laundering and terrorism financing. The involvement of EJ in the establishment of JITs is increasing: 12 JITs were set up in 2007 and 28 in 2008, some of them in the specific fields of this report. Annual meetings of national experts on JITs are organised jointly by EP and EJ in cooperation with the General Secretariat of the Council and the Commission. The fourth meeting took place on 15–16 December 2008 at EP and was focused on awareness raising and evidence gathering²⁸.

These meetings represent an important part of the Project on JITs developed by EJ and EP. In the framework of the same Project, a common section on JITS has been published on the websites of both institutions, including a guide on EU Member States’ JITs legislation. An amendment introduced in the new EJ Decision states that the JITs Permanent Secretariat will become a separate unit of EJ.

As a complement of its operational work, EJ frequently organises Strategic and Tactical meetings. In the specific fields of the Inquiry, these meetings are organised by the Financial and Economic Crime (FEC) Team in the case of money laundering or the Counter Terrorism (CT) Team in the case of terrorism financing.

For the adequate development of its tasks, EJ needs information from the National Members, European bodies, Third States and international organisations. Exchange of information between the Member States and EJ must be improved. It is expected that the adequate implementation of the new EJ Decision in the Member States, especially regarding the National Coordination System (art. 12) (art. 9.3, 9b), and some of the powers granted to the National Members (art. 9.3, 9b), will have a positive impact in the quality and quantity of information received by EJ. Practical application of the *Council Decision 2005/671/JHA of 20 December 2005 on the exchange of information and cooperation concerning terrorist offences* should also be strengthened²⁹.

Regarding the cooperation between EJ and other European bodies, cooperation with EP is progressing. Both institutions usually work together in relevant operational cases, in the organisation of Strategic and Tactical meetings and in relevant projects (eg JIT Project, cited above). EJ contributes to the Organised Crime Threat Assessment (OCTA) Report and Terrorism (TE-SAT) Report produced by EP. Essential elements of the EJ—

²⁷ Council Decision of 28 February 2002 setting up EJ with a view to reinforcing the fight against serious crime, OJ L 63, 6.3.2002. Relevant amendments have been introduced in the cited EJ Decision by the Council Decision 2008 on the strengthening of EJ, not yet published in the Official Journal of the European Union.

²⁸ Doc. 17512/08 LIMITE CRIMORG 217 ENFOPOL 265 EJ 118 COPEN 262. Brussels, 19 December 2008.

²⁹ OJ L 253, 29.9.2005.

EP Agreement signed in June 2004 are now under revision, especially regarding the involvement of EJ in the Analytical Work Files (AWFs) of EP.

EJ has concluded cooperation Agreements with some Third States: USA (6.11.2006), Norway (28.4.2006), Iceland (15.11.2005) and Croatia (9.11.2007). Agreements have also been signed with Switzerland and FYROM (not yet in force). Negotiations for an agreement with the Russian Federation, as well as a Memorandum of Understanding with IberRed, are ongoing. Informal contacts have been established with the International Criminal Court (ICC).

The above cited Agreements do not focus on money laundering or terrorism financing *per se*, but constitute an adequate framework for further investigations and prosecutions in these areas of criminality, as they enhance the cooperation between both parties in the combating of serious forms of international crime and facilitate the exchange of information, especially through the secondment of liaison magistrates in EJ. The new EJ Decision authorises the secondment of liaison magistrates posted by EJ to Third States (art. 27.a).

Lastly, in the framework of its cooperation with Third States, EJ has decided to apply for observer status in the Financial Action Task Force on Money Laundering (FATF—GAFI). First contacts with this prestigious inter-governmental body were established in mid-2007 and taken up in January 2008. With the support of the European Commission, a full member of FATF, EJ is now preparing all the required documentation to communicate its interest in attaining observer status in FATF.

1. MONEY LAUNDERING

1.1 *Case-work*

EJ is involved in a considerable number of money laundering cases, especially during the last two years: 104 cases were registered in 2007 and 103 cases in 2008.

Money laundering Cases 2004–08

2004	20
2005	46
2006	72
2007	104
2008	103

As an example, 17 coordination meetings on money laundering were organised in 2007 at EJ. Third States such as the USA, Switzerland and Ukraine were involved in some of these meetings.

1.2 *Strategic and Tactical meetings*

EJ organised a Tactical meeting on best practices for anti-money laundering investigations in Costa del Sol. Spain is the Member State most often involved in money laundering cases and the Costa del Sol has become one of the most attractive European regions for illegal money practices. EJ organised the Tactical meeting and involved delegates representing 14 Member States.

1.3 *Cooperation with European bodies, third parties and international institutions*

Money laundering is one of the areas covered by EJ's contribution to EP's OCTA Report. The last contribution (for the 2009 OCTA Report) was sent by EJ in October 2008 and covers the period from September 2007 to August 2008 (inclusive). It contains information about the geographical distribution of the cases on money laundering, relations and links between different Member States, association of money laundering with other criminal offenses and brief case summaries, illustrating the trends emerging from the casework of EJ.

2. TERRORISM FINANCING

2.1 *Case work*

EJ is increasing and improving its involvement in cases on terrorism financing: five cases in 2007 and eight cases in 2008 were registered in the EJ CMS.

Terrorism Cases 2004–08

2004	33
2005	25
2006	44
2007	34
2008	39

As an example: in 2008, four coordination meetings were organised dealing specifically with terrorism financing.

2.2 Information exchange

The relevant instrument for facilitating useful information to EJ in the fight against terrorism financing is the *Council Decision 2005/671/JHA of 20 September 2005 on the exchange of information and cooperation concerning terrorist offences*. At the request of the EU Counter Terrorism Coordinator³⁰, EJ contributed in May 2008 to the document “Exchange of Information on Terrorist Offences—Report on Compliance with Council Decision 2005/671/JHA”.

The report describes the state of implementation of the cited Council Decision in the different Member States, which can be divided into four main categories:

- 1) Those who have not implemented the Council Decision and do not provide any information to EJ.
- 2) Those who have not implemented the Council Decision but provide information to EJ.
- 3) Those who have implemented the Council Decision but do not provide information to EJ.
- 4) Those who have implemented the Council Decision and provide information to EJ.

According to Article 2 of the cited Council Decision, all the Member States have designated national correspondents for terrorism matters, who have access to and can collect relevant information concerning prosecutions and convictions for terrorist offences and send this information to EJ. Three strategic meetings have been held (June 2006, June 2007, June 2008), to promote the exchange of information between EJ and the national correspondents for terrorism matters.

In a document dated on 20 October 2006, the EJ CMT proposed a methodology for the most adequate exchange of information. A template has been also facilitated to the national correspondents as the best channel to transfer their information to EJ.

Despite these efforts, EJ does not receive sufficient information on terrorist offences, making it impossible to arrive at a quantitative or qualitative perspective. Therefore, it completely shares the approach of the EU Counter Terrorism Coordinator in this respect, who insists in the sharing of information between the national authorities and EJ as one of the key strategies in the fight against terrorism³¹.

2.3 Strategic and Tactical meetings

Most of the Strategic meetings have been organised at EJ, as indicated *supra*, with the goal of improving the practical application of the Council Decision 2005/671/JHA on exchange of information concerning terrorist offences. The majority of the national correspondents for terrorism attended these meetings. The first meeting was devoted to the implementation of the cited Council Decision in the 25 Member States. Strategic meetings in 2007 and 2008 have focused on the practical exchange of information, the processing of the received data by the Case Management Analysts of EJ, and the relevance of the data for the contribution to the TE-SAT report.

Tactical meetings organised by the CT Team are focused in specific types of terrorism. For examples, in March 2006 EJ organised a Tactical meeting to provide information about the European networks and groups that support suspects of terrorist activities entering and leaving Iraq. In December 2006 EJ organised another Tactical meeting focused on the terrorist organisation “Ansar Al Islam/Jaish Ansar Al Sunna”. In March 2007, a Tactical meeting on PKK took place at EJ, with the participation of the USA, EP and Turkey.

³⁰ See discussion paper presented by the EU Counter Terrorism Coordinator to the Council on the implementation of the EU counter terrorism strategy, Doc. 15448/07, Brussels 23 Nov 2007, p. 4–5. See also the European Council Conclusions of 14 December 2007, Doc. 16616/1/07 REV1 CONCL 3, points 27 and 29. By letter of January 2008, the EU CT Counter Terrorism Coordinator requested the president of EJ to provide a detailed report, giving exhaustive and up-to-date information to evaluate the situation and thus allowing the EU Counter Terrorism Coordinator to make further proposals to the Council to improve transmission of information to EJ. In this letter, the EU Counter Terrorism Coordinator provided specific topics which should be contained in the report.

³¹ See note 4 and Doc. 15684/08 JAI 638 ENFOPOL 228, Brussels 14 November 2008. Draft Council Conclusions of the continuation of work on combating terrorism, Annex, p. 4, and Doc. 16325/1/08 REV 1, JAI Council 27–28 Nov. 2008, p. 12.

These meetings usually have an international dimension, and some third States are invited by EJ to share their experiences and information with the Member States that are investigating the same types of criminality. On 10–11 April 2008 EJ and EP organised jointly a US/EU Tactical meeting focused on returning Jihadists, their identities and their methods of operation. On 24–25 November 2008 a Tactical meeting on “Strengthening Operational Cooperation between EJ and MEDA countries” took place at EJ, the goal of which meeting was to be the first step towards a fruitful cooperation between EJ and the so-called MEDA countries (Morocco, Algeria, Tunisia, Egypt, Jordan, Israel, Palestinian Territories, Syria and Lebanon).

2.4 Cooperation with European bodies, third parties and international institutions

One of the most relevant results of cooperation between EJ and EP is the annual EJ contribution to the EU Terrorism Situation and Trend (TE-SAT) Report, prepared by EP. Part 2 of the contribution is devoted to “National Legislation on Terrorism” and provides information on recent proposals and new legislation adopted in EU Member States. In this part, special reference is made to terrorism financing and to the effective implementation and interpretation of the Council Framework Decision 2006/960/JHA on simplifying the exchange of information and intelligence between law enforcement authorities of the Member States.

Taking as a basis the information on terrorism provided by the Member States, EJ prepares its “Terrorism Convictions Monitor”. Three reports are prepared annually, containing information about convictions and acquittals per Member State received from open sources and from the National Members of EJ. The most recent Terrorism Convictions Monitor, published in December 2008, paid special attention to terrorism financing: multiple aspects and implications of this complex phenomenon, applicable legislation and good practices, and the number of convictions on terrorism financing included in the EJ CMS since the beginning of 2008, including a short summary of the cited judicial decisions. It is a EJ internal report, prepared with the goal of informing the National Members and facilitating the drafting of EJ’s contribution to the TE-SAT Report.

Cooperation between EJ and EP is developed in the framework of the Agreement signed by both bodies in 2004, now under revision (as indicated in section 1). The urgent need to create structural links between both European bodies and to involve EJ in EP’s Analysis Work Files, as the EU Counter Terrorism Coordinator has often stated, are two of the main objectives of these negotiations. In addition, access by EJ to EP’s database on terrorism is an interesting point to be discussed.

Also linked to the cooperation between EJ and EP, the Recommendation number 7 of the Revised Strategy against terrorism financing suggests a new field of collaboration between both bodies, related to the participation of EJ in the establishment and development of minimum training standards on financial intelligence and financial investigations. In that respect, “Member States, the Commission and EP are invited to speed up progress in the development of minimum training standards and to involve on the longer term EJ in these developments”³².

EJ has commenced constructive cooperation with the UN Office on Drugs & Crime—Terrorism Prevention Branch (UNODC-TPB), after the exchange of letters of agreement and some meetings attended by delegations on both sides. Cooperation will be focused on the strengthening of the legal regime against terrorism, jointly training activities based on real cases, access to each other’s databases and arrangements for internships at both organisations.

Carlos Zeyen

National Member for Luxembourg
Member of CT Team and FEC Team

Angeles G. Zarza

Legal Officer

Annex 1

SPECIFIC SCOREBOARD OF THE COUNTER TERRORISM TEAM REGARDING TERRORISM FINANCING

1. Full support should be given to the follow-up Strategy on Terrorism Financing and the proposed implementation plan developed in its 5 October 2007 Report by the EU Counter Terrorism Coordinator.
2. Support should be given to the 12 Measures and Actions as described under item 3.5 Terrorism Financing of the Council of 7 March 2007 EU Action Plan on combating terrorism (7233/07).

³² Doc. 11778/1/08 cited, p. 17.

3. More generally, the Objectives and Tasks as described by the CT Team in its “Terrorism Scoreboard” should be supported.
4. EJ should pursue the procedure to become an observer with FATF (EP and Interpol already have this status).
5. EJ should widen the scope of its cooperation and information exchange partners including, whenever legally possible, FIU’s and intelligence services.
6. EJ should insist, at every possible occasion, on the vital need for Member States to fully implement Council Decision 2005/671/JHA of 20 September 2005.

Annex 2

SCOREBOARD OF THE COUNTER TERRORISM TEAM

With the main purpose of becoming a centre of expertise on terrorism, the CT Team of EJ (CT Team) has recently updated the eight points of its Scoreboard. Each of these has a clear job description, a well defined responsibility, a deadline, and requirements for follow-up and debriefing to the College. Cited points are as follows:

1. Judicial cooperation: organisation of all strategic coordination meetings on terrorism. Support whenever necessary in the context of operational and Tactical meetings on terrorism.
2. Improvement of interaction between counterparts dealing with counter terrorism issues: continue regular contacts with, at EU level, national correspondents for terrorism, magistrates specialised in terrorism or in charge of important terrorism cases, EP, the European Border Agency, SitCen, the Counter Terrorism Coordinator, the CPTF Terrorism, counter terrorism liaison officers and intelligence services. Furthermore, continue regular contacts with other European and international organisations involved in the fight against terrorism, such as the Council of Europe, the OSCE, UNODC and Interpol.
3. Improvement of interaction with third States dealing with counter terrorism issues: operational meetings will be held with the USA, Switzerland, Morocco, Algeria, etc. Development of contact points and the gathering of information on legislation of third States are important efforts to be made.
4. Judicial database on terrorism: the Case Management (CM) Team made some recommendations regarding the CMS to provide the database with added value. The real application of the Council Decision on the exchange of information on terrorism would enable EJ to insert all the information in the CMS database, which in turn would allow us to act in a more pro-active way, generating our own EJ cases, based on analyses and links established by the analysts. Currently, all terrorism judgements pronounced since 2005 in the EU Member States are being listed. The CMS will also make an analysis of these lists.
5. Legal database on terrorism: database providing an updated overview of the available national, European and international legal documents/instruments related to terrorism.
6. Cyber-terrorism: establishing know-how in the field and detecting legal blockages, problems of jurisdiction, etc.
7. Financing of terrorism: an elaborate memo on this topic, which is intended to be used internally as a comprehensive document, has been written. In the paper, an overview is given of existing EU and UN instruments in this field. Moreover, cases relating to terrorist financing where EJ has been involved are mentioned. Based on this memo, the CT Team will assess EJ’s added value in this field, and search for possible future actions and for improvement of countermeasures.
8. NBC-terrorism: information on legislation will be gathered and the CT Team will participate in conferences and meetings on the topic.

Memorandum by Europol

1. EU ARCHITECTURE FOR INTERNAL SECURITY

The European Union (EU) Architecture of Internal Security³³ is the reference framework under which the EU intends to develop all activities relating to its internal security, including money laundering and terrorism. In the long term, the objective is to expand this framework to other fields of internal security beyond organised crime, in order for it to gradually become a global approach encompassing other subjects and relevant actors to internal security.

Europol plays an important role in this EU Architecture of Internal Security. The various threat assessments produced by the organisation, on the basis of information and intelligence sent by the Member States and collected from other sources as well (open, private, public, scientific, etc) constitute the cornerstone of a European intelligence-led policing system for the fight against organised crime. Europol's analytical input sets in motion the execution of the European Criminal Intelligence Model (ECIM). Based on the experience of the National Intelligence Model (NIM) currently in use in the UK, the ECIM is a four-step cyclical process which starts by an assessment of the threat at European level from which political priorities in internal security should be drawn. By anticipating criminal developments more effectively, the intelligence-led policing approach enables the political level to decide on priorities while the operational level can use resources more effectively to inspire and steer the investigations accordingly.

Europol actively participates to the first stage of this European intelligence cycle, by collecting, storing and analysing data received from the Member States and other parties, and by producing the Organised Crime Threat Assessment (OCTA). Europol's analytical and assessment role provides a unique operational support by identifying criminal trends as well as future threats at European level.

In the second phase of the ECIM, Ministers in the Council use Europol's threat assessments to set out political and regional priorities for EU internal security.

In the third phase, the priorities set by the Council provide the reference framework for both the work of the different EU agencies and the plans of the Member States' competent authorities. These priorities should be reflected in their strategic planning, working programmes, budgets, annual reporting and external relations. With the support of the Police Chiefs' Task Force (PCTF), EU agencies and Member States' law enforcement authorities implement the priorities by means of the COSPOL³⁴ projects and by using Joint Investigation Teams (JITs) if needed. The intelligence generated by the investigations are reported—as early as possible—to Europol, then “recycled” and used by Europol to produce enlarged and up-to-date analysis for ongoing investigations and other analytical products. The main responsibility for implementing the EU internal security priorities remains at national level.

In the fourth phase of the ECIM, an evaluation is conducted in order to feed the next cycle of the ECIM. Reflections are currently taking place in the Council on how best to conduct this evaluation phase.³⁵

To summarize, Europol's responsibilities in the ECIM mainly lie in the first phase of the process, that is to assess the threat Europe-wide (OCTA). The organisation also plays an important role in the implementation phase by providing an operational support to the PCTF and, generally speaking, by producing intelligence in the framework of its Analysis Work Files (AWFs), based on the contributions of the Member States.

However, it should be borne in mind that the approach taken for developing the EU Internal Security Architecture does not apply yet to terrorism in general, and to its financing in particular. The OCTA produced by Europol does not cover terrorism issues but focuses on the future threats by organised crime in the EU, including money laundering. With regard to terrorism, Europol annually produces the Terrorism Situation and Trend Report (TE-SAT) which provides a comprehensive statistical overview of the terrorist incidents that took place across the EU territory in a given year.³⁶

2. RESPECTIVE ROLES OF EUROPOL AND EUROJUST

Europol cooperates extensively with other Justice and Home Affairs (JHA) EU/EC agencies and bodies, including Eurojust but also Frontex, SitCen, OLAF and CEPOL.

³³ Architecture of Internal Security, Council Secretariat doc. 9596/1/06 JAI 271, approved by the Justice and Home Affairs Council of 1-2 June 2006.

³⁴ Comprehensive Operational Strategic Planning for the Police.

³⁵ The Council Working Groups are currently reflecting on two options to strengthen the evaluation exercise. These options are described in the following document: Council of the European Union, Orientation debate on the fifth round of Mutual evaluation, 65846/1/08, 10 April 2008.

³⁶ See www.europol.europa.eu (publications).

It is worth mentioning the novelties created by the so-called Danish protocol amending the Europol Convention.³⁷ This protocol adds a new paragraph 9 to article 10 of the Europol Convention, which provides for the possibility for Europol to invite third parties to be associated with the activities of an analytical work file (AWF). The association of experts representing third parties is nonetheless subject to two conditions: firstly, the existence of an operational agreement between Europol and the third party concerned; and secondly, an explicit consent from the participating Member States to that specific AWF (that can further define specific aspects of the participation). Eurojust is the only EU body with which an operational cooperation agreement currently is in place. Eurojust currently participates in six Analysis Work Files (see below) and has been formally invited to participate in six more.

Eurojust and Europol signed the operational agreement, which allows for the exchange of personal data, in 2004. A “Europol-Eurojust Steering Committee” was established and meets every three months in order to discuss and to improve cooperation between the two institutions. In addition, the President of the College of Eurojust and the Director of Europol meet bilaterally on a regular basis.

In 2008, two concomitant policy initiatives called for more systematic access for Eurojust to Europol’s AWFs: the Council Working Group reviewing the Council Decision establishing Eurojust and the Counter-Terrorism Coordinator (CTC). The matter is still being discussed in the Council working groups. This resulted in a revision of the cooperation agreement between the two organisations that is currently pending approval by the Council.

Eurojust and Europol have cooperated on the implementation of the legislation on Joint Investigation Teams (JITs). Firstly, they have jointly developed a legislative guide on JIT legislation, on the basis of a questionnaire by which all Member States were asked how they dealt with the JIT legislation. Secondly, Europol and Eurojust jointly established a common website on the issue. Thirdly, they have drafted a JIT manual for practitioners on the establishment of JIT, with the help of national prosecutors. Lastly, they organise an annual meeting for the network of national JIT experts. The meeting takes place in turn at Europol and Eurojust. There have been three meetings so far.

Concerning the TE-SAT, Europol’s cooperation with EU/EC agencies is limited to SitCen and Eurojust. Europol has set up an advisory board consisting of representatives from these two agencies and from the Member States holding the EU Presidency at the time. The advisory board meets three to four times during the production period and provides Europol’s officials with advice on proposed intelligence requirements, collection procedures and Europol’s draft report. It must be noted that Eurojust’s contribution to the TE-SAT is very substantial since it collects relevant data on convictions and penalties.

3. OVERVIEW OF EUROPOL ACTIVITIES

Several Europol Units are directly or indirectly dealing with activities that touch upon money laundering or the financing of terrorism. The main responsibilities on these matters however belong to the Terrorism Unit of the Serious Crime Department (SC5) and to the Financial Crime Unit of the Serious Crime Department (SC4).

The anti money laundering activities conducted by Europol encompass diverse competences and working areas of multidisciplinary law enforcement agencies within the EU, including Customs and Financial Intelligence Units with either Judicial or Police structures. Europol acts as a focal point for the exchange of dedicated financial data in support of money laundering investigations, performing its tasks in cooperation with EU Member States by facilitating the exchange of such information and ensuring analytical assistance to complex cases generated by Suspicious Transactions Reports (STRs) and Currency Transaction Reports (CTRs), as well as ongoing money laundering investigations, regardless of the predicate offence committed.

Europol is proactive in the development of counter-terrorism goals adhering to the Hague Programme response created in 2004, which promotes four parallel strands: Prevent, Protect, Pursue and Respond. These goals follow four axes, namely: Strengthening national capabilities, Facilitating European Cooperation, Developing Collective Capacity and Promoting International Partnerships.

Combating the financing of terrorism forms part of the “Pursue” strand of the Hague Programme. The key elements of this strategy are a targeted intelligence approach, improved designation and listing of terrorist organisations and individuals associated with terrorist groups, improved tracing of financial assets, ongoing monitoring of developing trends and support for EU counter-terrorism financial investigation units. The issue of money laundering, the process of turning “dirty monies into clean monies” is a part of terrorism financing Europol reviews, although as one aspect of terrorism financing only.

³⁷ Council Act of 27 November 2003 drawing up, on the basis of Article 43(1) of the Convention on the establishment of a European Police Office (Europol Convention), a Protocol amending that Convention (Danish Protocol), OJEU, 2004/C2/01.

The list below provides an overview of the various projects currently conducted by Europol concerning the Inquiry in question. Additional information on Europol's functioning can be found in Report "Europol: coordinating the fight against serious and organised crime" that was published by the House of Lords on 12 November 2008.

3.1. *Situation report on the criminal financing of terrorism*

In June 2008, The Council of the European Union together with the European Union Counter-Terrorism Coordinator discussed the revised strategy on terrorist financing. During this review, the Council tasked Europol's Counter-Terrorism Unit to report on links between terrorist financing and other criminal activity in order to assist the Council to update the EU strategy against terrorist financing.

In order to address this request, Europol has produced a strategic situation report into the criminal financing of terrorism based on Member States' intelligence contributions.

This situation report is an initial report and is the first of its kind. Future reports will build on this foundation.

3.2. *Relevant activities within the framework of various Analysis Work Files (AWFs)*

SUSPICIOUS FINANCIAL TRANSACTIONS

In compliance with article 30.1.b of the Amsterdam Treaty 2001, the project aims to analyse suspicious financial transactions and provide investigative leads to the Member States. This AWF is increasingly effective as a service provider to money laundering units in the field.

The analysis work applies the Financial Intelligence Led Policing concept which integrates and synergises criminal analysis techniques with investigative expertise on financial crime. Through the conceptualisation of this working model, Europol is increasingly able to discover new criminal scenarios and target transnational organised crime groups performing money laundering activities, both within and outside the EU.

Within the AWF project, Europol develops and enhances the applied criminal analysis techniques in order to conduct multi-parametric queries and establish operational links between financial data and criminal intelligence held within Europol databases. By doing this, Europol is able to exploit the criminal intelligence contained in the suspicious financial transactions or the currency transaction reports to the fullest extent, and in doing so consolidates its unique position as the EU crime intelligence centre with a pan-European dimension.

The AWF is the only properly designated supranational platform for integrated pro-active analysis of financial intelligence. As such, it enables analytical outcomes to transcend mere national perspectives and provides added value to Europol's partners in the detection and disruption of cross-border organised crime networks. The delivery of ad hoc operational and strategic analytical products allows Europol to integrate ongoing money laundering investigations with the aim of prosecuting offenders.

The application of the horizontal matrix permits an interface with Europol's other AWF projects and therefore enables the development of investigative leads in relation to other crime phenomena. As a result of this integrative working approach, the analysis results provide the Organised Crime Threat Assessment (OCTA) team with reliable data to properly assess crime trends and future threats in relation to the European money laundering landscape.

ISLAMIC EXTREMIST TERRORISM

The relevant AWF focuses on Islamic extremist terrorism by preventing or combating crimes committed or likely to be committed in the course of terrorist activities and related criminal offences associated with terrorism perpetrated by individuals, groups, networks or organisations that evoke Islam to justify their actions. The scope of the project covers Al Qaeda and other religiously motivated terrorist groups.

Most Member States are members of this AWF. Some Member States are still reluctant to share "live" data on ongoing enquiries into Islamist extremist terrorism, but the number of operational cases in which the AWF has been involved is increasing. There has recently been a clear increase in the number of times Member States return to Europol with requests for assistance on investigations—success breeds success. However, data related to the financing of terrorism are seldom contributed to Europol, hence a number of intelligence gaps in this field.

Switzerland and Norway have recently been requested to carry out feasibility studies, as part of the association process to the AWF. Further discussions are expected on this matter and also on the Eurojust request for association to the AWF.

This dedicated AWF has been supporting the Member States on a number of investigations with a financing of terrorism aspect, including a case related to the LTTE (Tamil Tigers) which has evidenced the implantation of this terrorist group in a number of EU Member States.

OTHER POLITICALLY MOTIVATED TERRORIST GROUPS

Another analytical project within the scope of the Europol Counter-Terrorism Unit identifies the activities of terrorist groups listed by the Council of the European Union and by the Working Group on Terrorism (Third Pillar) and associated criminal activities within Europol's mandate. Complementary to the above mentioned analytical project on Islamic extremism, this AWF focuses on politically motivated terrorist groups other than Islamic extremist terrorism. It includes eg left- and right-wing extremism, nationalist terrorism and extremist animal protection groups. The analysis concentrates on organisations where the Member States identify a need for the AWF to be active. The financing of terrorist activities represents a marginal part of the work.

ILLICIT TOBACCO FRAUD

Money laundering is frequently reported and Europol has intelligence available suggesting that cigarette smuggling is used to finance terrorist activities. However, Member States tend to focus most of the time on the criminal offence of cigarette smuggling counterfeiting, in the second place on asset seizure and only in the third place on the money laundering offence. Nevertheless, the internal coordination of several activities at Europol led to good results in the framework of a recent operation.

ETHNIC ALBANIAN CRIMINAL GROUPS

The activity of Europol within this analysis project focuses on warning the Member States of the potential danger represented by the involvement of ethnic Albanian organised crime groups in the laundering of money. Ethnic Albanian crime groups are not yet involved in very sophisticated crimes, even though a tendency to raise their criminal scale has been noticed.

OUTLAW MOTORCYCLE GANGS

According to the relevant analysis project the outlaw motorcycle gangs are involved in money laundering. In general, the investigative focus towards money laundering activities related to outlaw motorcycle gangs has been very rare, despite the insistence of Europol. In the recent past, Member States however appear more open to launch financial investigations in parallel to the criminal ones.

EAST EUROPEAN ORGANISED CRIME GROUPS AND NETWORKS

Within the framework of this analysis project, Europol collects data on the use of shell companies for money laundering purposes.

3.3. High Impact Operations

Europol continually provides logistic and practical support to high impact operations (HIOs). These operations such as the "cash courier operations" held throughout the EU are implemented by Member States and their respective competent authorities. Europol provides real time support through personnel, logistics and analytical response. This includes operations on terrorism and aligned financial factors of funding and support.

In June 2008, the Counter-Terrorism Unit at Europol coordinated a High Impact Operation targeting cash couriers travelling to the Maghreb in support of Al Qaeda in the Islamic Maghreb. Based on the lessons learned from this operation, Europol intends to further develop this concept in the future with the Member States and third states.

3.4. *Training and capacity building*

The application of the Financial Intelligence Led Policing concept also includes the promotion of Europol's work and the provision of assistance to Member States in terms of training and awareness workshops. Europol regularly attends and organises money laundering and counter-terrorism training upon request, both to foster relationships with key law enforcement services and to raise awareness within Member States.

Europol actively participates in meetings held at Commission level, such as the Money Laundering Committee created for the implementation of the Third EU Money Laundering Directive, and the Financial Intelligence Units (FIU) Platform meetings aimed at improving cooperation among FIUs. Europol has also been granted an Observer Status at the Financial Action Task Force (FATF) meetings and provides other international organisations, such as Moneyval (Council of Europe Committee of experts on the evaluation of anti-money laundering measures and the financing of terrorism), with ad hoc expertise and valuable input on the subjects of investigation techniques and money laundering trends.

Europol's forthcoming planning activities foresee the increased integration of existing dedicated European networks (eg FIU.NET) into Europol databases.

18 December 2008

Memorandum by the Financial Action Task Force (FATF) Secretariat

INTRODUCTION

1. The Financial Action Task Force (FATF) is an inter-governmental body with 34 members,³⁸ whose purpose is the development and promotion of policies, both at national and international levels, to combat money laundering and terrorist financing. FATF was established by the G-7 Summit in 1989 to combat the threat of money laundering posed to the banking system and to financial institutions. In October 2001, the FATF's mandate was expanded to incorporate efforts to combat terrorist financing, and further work has been done recently on illicit financing more generally. The current FATF revised mandate (2008–12), which determines the FATF's directions and priorities, was approved at an FATF Ministerial meeting in April 2008 (see Annex 1).

FATF MISSION

2. Since its establishment, the FATF has focused its work on three main activities:

- Standard setting: A core function of the FATF has been to set the international standards for anti-money laundering, and (since 2001), for combating terrorist financing (AML/CFT). The 40 + 9 Recommendations provide a complete set of counter-measures covering the criminal justice system and law enforcement, the financial system and its regulation, certain designated businesses and professions, and international co-operation. The FATF Recommendations have been recognised, endorsed and adopted by many international bodies, including the IMF, the World Bank, and the United Nations (see UNSCR 1617). As set out in the FATF Revised Ministerial mandate for 2008–12, the FATF will continue to revise and clarify its 40 + 9 Recommendations when necessary (see more below).
- Ensuring effective global compliance with the standards: Full and effective implementation of the 40 + 9 Recommendations in all countries is one of the fundamental goals of the FATF. FATF member countries are strongly committed to the discipline of multilateral monitoring and peer review. In this context, the FATF has a process of mutual evaluations that are intended to both monitor progress made by, and encourage, member governments in implementing the FATF Recommendations. The mutual evaluation reports not only provide an accurate technical assessment of the extent to which the evaluated country has implemented an effective AML/CFT system, but also are published, and are enforced through the peer pressure mechanism. Currently, the FATF is more than two-thirds of the way through its third round of mutual evaluations.

3. The FATF has worked to extend and foster this peer review process through the FATF-Style Regional Body (FSRB) network, which is a very important mechanism for promoting timely and effective implementation of FATF Recommendations globally, and for contributing to the creation of a level playing field throughout the membership and beyond (see description of the FSRB Network below).

³⁸ 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, China; Iceland; Ireland; Italy; Japan; Luxembourg; Mexico; the Kingdom of the Netherlands; New Zealand; Norway; Portugal; the Russian Federation; Singapore; South Africa; Spain; Sweden; Switzerland; Turkey; the United Kingdom; and the United States.

- Identifying money laundering and terrorist financing threats: The FATF is uniquely placed to analyse and draw international attention to emerging money laundering and terrorist financing vulnerabilities, and has significantly enhanced its process for the identification of money laundering and terrorist financing threats (the typologies process). Currently for example, the FATF is conducting a typologies exercise to identify the trends and any new threats in the securities sector. The generation and dissemination of in-depth typologies studies is central to the work of the FATF and provides a solid foundation for ongoing policy development at the national and international levels. In pursuing this work, the FATF will continue its expanded co-operation with the FSRBs and other international bodies, and will also harness the experience and expertise which the private sector can bring to this process.

4. Following the same goal, the FATF has commenced a process of surveillance of systemic criminal and terrorist financing risks, so as to enhance its ability to identify, prioritise and act on systemic threats. In this context, and drawing on contributions from the FATF membership, the private sector and the FSRBs, it will support the development of national threat assessments through best practice guidance and establish stronger and more regular mechanisms for sharing information on risks and vulnerabilities.

FATF as the global AML/CFT standard setter has demonstrated its capacity to create new standards and to issue timely policy changes that respond to the ever-evolving practices of money launderers and terrorist financiers. The FATF Recommendations are globally recognized and endorsed, and have also been adopted by many international bodies.

The FATF has developed effective means of monitoring and promoting compliance with its Recommendations among the FATF members. These practices have produced significant improvements in the AML/CFT systems of FATF countries. The FATF has also extended and fostered the peer review process throughout the FATF-Style Regional Body (FSRB) network.

MINISTERIAL ACCOUNTABILITY

5. The FATF is accountable to the Ministers of its membership. To strengthen this accountability, the FATF President reports annually to Ministers on key aspects of FATF work, including on global threats. Given the potentially destabilising effects of criminal and terrorist action against the international financial architecture, occasional ministerial meetings also provide an ongoing accountability mechanism whereby Ministers can shape the strategic direction of FATF policy-making.

The FATF is accountable to the Ministers of its membership and has developed mechanisms to ensure adequate transparency and accountability to Ministers. This is central to the FATF's ability to undertake its mission.

GLOBAL FATF NETWORK

6. Since it was created, the FATF has worked with non-member jurisdictions and organisations to establish a global network for combating money laundering and terrorist financing. The aim of this network has been to promote political support for and ensure the implementation of the FATF AML/CFT standards as broadly as possible beyond the FATF membership. It has done this in several ways: expanding FATF membership, fostering and supporting the eight FATF Style Regional Bodies³⁹ (FSRBs), and enhancing its cooperation with other relevant international organisations.

7. In recent years, the FATF has expanded its membership by adding a number of strategically important countries as members (Argentina, Brazil, China, Mexico, Russia, South Africa), and two countries (India and Korea) are observers, and in the process of moving towards membership. Thus sixteen G20 members are direct members of FATF, two are observers, one is a member of the Gulf Cooperation Council (an FATF member), and one a member of an FSRB.

8. In addition, the eight FSRBs are an important part of the FATF network: as of today, 157 jurisdictions are members of these bodies (including 12 jurisdictions which are also members of FATF). Moreover, the Offshore Group of Banking Supervisors (OGBS) has similar functions to an FSRB and has a similar status within the FATF. OGBS has 16 members (including 12 which are also members of other regional groups). Therefore, there are in total 161 different member jurisdictions in these nine groups⁴⁰ that have committed to

³⁹ List of FATF-Style Regional Bodies: The 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).

⁴⁰ References to FSRBs in this document apply equally to the OGBS.

implementing the FATF standards and undergoing mutual evaluations. When taken together with the FATF, there are at present 181 jurisdictions that directly comprise the FATF global AML/CFT network.

9. The very close relationship that exists between the FATF and the FSRBs (such as Moneyval) is already demonstrated by the close interaction that has existed between these bodies over many years, and by the fact that the FSRBs participate in all FATF work, both confidential and non-confidential. Therefore, FSRBs already de facto benefit from a higher status than the other FATF observers, and have many of the rights that are held by full members. However, with the view of further strengthening the essential partnerships between the FATF and the FSRBs, the Plenary decided in June 2005 to an enhanced status for FSRBs, called “Associate Member”. The creation of this new status seeks to afford members of regional bodies greater participation in the processes within the FATF and provide the regional bodies enhanced access to and influence on FATF policies and decisions. Specifically, regional bodies that are named as associate members are permitted to send a representative number of country member delegates to FATF plenary meetings.

10. Thirteen of the 34 FATF members are also members of one or more of the FSRBs, which provides a close link between the work of the FATF and the work of the FSRBs. Additionally, two of the jurisdictions within the Kingdom of the Netherlands—Aruba and the Netherlands Antilles—are members of an FSRB. Correspondingly two FATF members—France and the Netherlands—are currently members of MONEYVAL. Joint membership by these jurisdictions aids consistency of approach in the work of these bodies and supports effective information sharing between them. The input of joint members has also proven useful when the FATF and an FSRB are collaborating on typologies or other projects and when joint meetings are held.

11. The FATF has always sought to develop close collaboration and cooperation with other international bodies interested in the AML/CFT area. In particular, with the International Monetary Fund and the World Bank, which both conduct evaluations of the implementation of the FATF standard by countries and develop technical assistance programs, the Basel Committee on Banking Supervision (Basel Committee), the International Organisation of Securities Commission (IOSCO) and the International Association of Insurance Supervisors (IAIS). In addition, the FATF has been working closely with the FSF.

12. The IMF and the World Bank (collectively, the “international financial institutions” or “IFIs”) play a central role in monitoring the implementation of the FATF Recommendations among their members. The IFIs are well-positioned to link the FATF with FATF non-members. On the one hand, the IFIs are largely funded and controlled by the same states that founded the FATF. On the other hand, the IFIs have strong working relationships and expertise in areas relevant to FATF non-member developing nations. The robust technical assistance programs of the IMF and the World Bank increase the capacity of FATF non-members to comply with the FATF Recommendations.

13. Amongst its different activities, the FATF has a number of work-streams underway on the issues relating to the reinforcement of international cooperation and the promotion of integrity in the financial markets. It has in particular developed procedures and mechanisms to protect the global financial system from uncooperative and non transparent jurisdictions that pose increased risks of illicit financial activity. More globally the FATF is continuing its work in the fight against money laundering and terrorist financing.

In crafting an international response to money laundering and terrorism financing, the FATF has formed institutional partnerships with the Regional Bodies and various international institutions. Through these bodies and institutions, the FATF is able to indirectly engage FATF non-member countries and advance the universal implementation of the Recommendations. In creating the status of “associate members” for the regional bodies, the FATF has opened its internal functions to greater external participation.

INTERNATIONAL COOPERATION ISSUES

14. Since 2000 the FATF has taken firm action against uncooperative jurisdictions in the AML/CFT area. This effort started with the initiative on Non Co-operative Countries and Territories (NCCTs) and is now being continued through the work of the FATF’s International Co-operation Review Group (ICRG).

a) *The Non Co-operative Countries and Territories initiative (NCCTs)*

15. During the NCCT initiative, 23 jurisdictions were publically listed due to a lack of an effective AML/CFT system. The initiative was successful, as it resulted in these jurisdictions implementing more comprehensive measures to prevent, detect and punish money laundering and terrorist financing. Substantial progress was made in all 23 jurisdictions due to the NCCT process and the last country (Myanmar) was removed from the FATF list in October 2006, though it remains subject to monitoring.

b) *The International Co-operation Review Group (ICRG)*

The ICRG process

16. Following on to the NCCT process, the FATF Plenary agreed to form the International Co-operation Review Group (ICRG), which started its activities in January 2007. The ICRG addresses jurisdictions or cases where international co-operation has been difficult or impossible and/or where severe deficiencies in the AML/CFT regime have been identified resulting in serious vulnerabilities in the AML/CFT framework.

17. At the start of this ICRG process, the FATF decided to review and follow up with several jurisdictions based on the lack of effective AML/CFT controls: Comoros Islands, Iran, São Tomé & Príncipe, and Turkmenistan, as well as the northern part of Cyprus. At later stages, Pakistan and Uzbekistan were referred into the process because of ML/FT risks and lack of adequate controls.

18. Due to a lack of adequate progress in those jurisdictions, the FATF has issued several public statements since October 2007.⁴¹ In these public statements, the FATF called on its members and urged all jurisdictions to advise their financial institutions to take the risk arising from the deficiencies in the AML/CFT systems in certain of these jurisdictions into account for enhanced due diligence.

19. The current ICRG procedures are flexible and have been used successfully so far to engage with these jurisdictions, and to encourage progress in all of them. Nevertheless, FATF delegations have expressed their desire to further refine and enhance the procedures so as to ensure more consistency. In accordance with the FATF's priorities for 2008–09, new procedures will thus be considered by the membership during 2009 to improve how the FATF system responds to threats posed by High-Risk Jurisdictions and how to better achieve a level playing field in this area. Once the procedures are strengthened, it is possible that more jurisdictions will be examined and followed up by the ICRG. This intensification of efforts is meant to reduce the vulnerability of the international financial system to money laundering and terrorist financing and will on a more general level also enhance corporate transparency and market integrity. It should also be noted that the recent G20 statement emphasized the need for FATF to take further action in this area.

c) *Actions taken by members and other jurisdictions (Recommendation 21)*

20. All FATF members have taken actions specifically in response to the FATF public statement of 28 February 2008. Related statements were issued in October 2007 and October 2008.

21. Many FATF members' issued advisories to inform financial institutions of the information in the FATF public statement and specifically called for their financial institutions to take the risks into account, be aware of the increased ML/FT risks, or apply appropriate or enhanced due diligence when dealing with transactions and customers involving all five countries and the area. A significant degree of harmonization thus exists in terms of alerting countries to the potential ML/FT risks and advising the financial sector to take these risks into account.

22. In addition to this enhanced due diligence, FATF Recommendation 21 calls for "additional counter-measures" to be taken where the country fails to respond adequately to the concerns that are expressed. FATF members have flexibility to apply appropriate "counter-measures", but there are also ongoing discussions on the harmonization of these actions.

The FATF has intensified its efforts to reduce the vulnerability of the international financial system to money laundering and terrorist financing. In recent years the FATF has taken a number of actions that are consistent with and support the objectives of reinforcing international cooperation and promoting integrity in financial markets.

d) *Other initiatives in relation to international cooperation*

23. Apart from the NCCT and ICRG processes, which focus on uncooperative jurisdictions, the FATF has also been working to enhance international cooperation relating to money laundering and terrorist financing, including cooperation between financial sector supervisors. The FATF Recommendations (see R.36-40 in particular) set out clear and broad standards that require the widest possible range of international cooperation. As regards financial sector supervision, the FATF also has several Recommendations (R.17, 23,

⁴¹ October 2007, regarding Iran, see FATF's public website: <http://www.fatf-gafi.org/dataoecd/1/2/39481684.pdf>
February 2008, regarding Uzbekistan, Iran, Pakistan, Turkmenistan, São Tomé and Príncipe and the northern part of Cyprus, see FATF's public website: <http://www.fatf-gafi.org/dataoecd/16/26/40181037.pdf>
October 2008, regarding Iran, Uzbekistan, Turkmenistan, Pakistan and São Tomé and Príncipe, see FATF's public website: <http://www.fatf-gafi.org/dataoecd/25/17/41508956.pdf>.

25 and 29) which underpin international cooperation by requiring that there be effective supervisory systems and actions at the domestic level.

24. Through the evaluation process, the FATF, the FSRBs and the IMF/World Bank have now evaluated approximately 100 jurisdictions worldwide,⁴² and the reports, combined with the peer pressure mechanisms and an effective process of follow up, are exerting pressure that will lead to significant improvements in compliance, and in the longer term, an improved capacity to cooperate internationally. To that end, the FATF will continue to work closely with the IMF and World Bank in 2009 to develop ideas for enhancing contributions to each other's work and objectives. Moreover, the FATF will work to strengthen its relationship with the FSRBs and to enhance the ways in which they can contribute to the FATF decision making processes.

25. On a number of occasions the FATF has also worked closely with other international organisations, such as the IMF and World Bank, the Basel Committee, IOSCO, IAIS, and the FSF, to address particular issues that have arisen. Examples include the development of sector specific guidance, preparing guidance on the risk-based approach to AML/CFT (including identifying areas of higher risk), and examining ways in which there could be a more effective and efficient exchange of information internationally.

26. The FATF also works very closely with the Egmont Group—the international body that represents the financial intelligence units (FIUs) of each country. FIUs are responsible for receiving suspicious transaction reports and they are an essential component of the international fight against money laundering, the financing of terrorism, and related crime. The Egmont Group now has 108 FIUs as members. During 2008–09 FATF will be working closely with the Egmont Group to develop ideas that will enhance our respective contributions to each other's work and objectives. The FATF standards in relation to the FIUs and the suspicious transactions reporting requirement are very comprehensive (R.26, R.13 and SRIV). Cross-border cooperation among FIUs is also very much promoted (see R.40) as well as feedback mechanisms from the FIU to the reporting entities within the private sector. The FATF mutual evaluations (in the 3rd round) are looking at the implementation and effectiveness components in relation to FIUs.

In relation to international cooperation, the FATF standards set out clear and broad requirements and the FATF will continue to focus closely on assessing the implementation and effectiveness of the existing international cooperation mechanisms.

27. In recent years the FATF has taken a number of actions that are consistent with and support the objectives of reinforcing international cooperation and promoting integrity in financial markets. These actions have been reaffirmed and reinforced by the current FATF Ministerial mandate for 2008–12. This mandate, together with the priorities of the current FATF Presidency (Brazil), sets out the FATF focus for the immediate future, and include (in addition to the issue of High Risk/Uncooperative jurisdictions):

- Commencing a process to examine the FATF standards and prepare for the 4th Round of Evaluations, while also continuing the work to ensure effective global implementation, with particular attention being paid to the challenges faced by low capacity countries;
- Deepening global surveillance of systemic criminal and terrorist threats identified by the FATF;
- Responding to emerging threats which affect the integrity of the financial system. For example, FATF has already swiftly responded to the emerging threat of proliferation financing through guidance it has published related to UNSCRs 1718, 1737, 1747 and 1803, and has committed to undertaking longer-term analysis in this area related to UNSCR 1540;
- Enhancing the cooperation and coordination with key stakeholders and partners—in 2008–09 concentrating in particular on the relationships with FSRBs and the Egmont Group;
- Building a stronger, practical and ongoing partnership with the private sector which is at the frontline of the global fight against money launderers and terrorist financiers.

IMPACT OF THE GLOBAL FINANCIAL AND ECONOMIC CRISIS ON AML/CFT

28. In February 2009, the FATF agreed to examine the impact of the global financial and economic crisis on efforts to combat money laundering and terrorist financing. Under this initiative, the FATF will take stock of the consequences of the financial and economic crisis for the FATF and identify issues for further analysis and discussion. The FATF analysis will also look at the role AML/CFT measures have in national and global

⁴² See http://www.fatf-gafi.org/document/32/0,3343,en_32250379_32236982_35128416_1_1_1_1,00.html for a list of FATF mutual evaluations and links to FSRB websites with their published reports.

solutions to this crisis. In addition, the FATF will continue to consider the measures which countries are taking to mitigate the impacts of the crisis as such measures should not undermine AML/CFT controls.

The FATF is currently looking at the consequences of the financial and economic crisis for the FATF with the objective of identifying any issues related to AML/CFT that could require further analysis and action.

EFFECTIVE GLOBAL IMPLEMENTATION

29. Over the last 15 years, one of the most effective aspects of the FATF process has been to closely monitor and encourage full implementation of the 40+9 Recommendations in all countries. The current ongoing evaluation process remains a critical mechanism for promoting timely and effective implementation, and for contributing to the creation of a level playing field globally. When combined with the appropriate follow-up action to ensure that countries correct, as quickly as possible, any deficiencies that are identified through the mutual evaluation process, the whole process has expedited and enhanced the implementation of the international standards. FATF members are working hard to enhance their AML/CFT systems so as to bring them closely into line with the FATF standards.

30. However, many countries, in particular low-capacity countries, face challenges in the implementation of FATF standards. In order to minimise both their own vulnerabilities and the associated risks for the international financial system, the FATF works in close collaboration with the FSRBs, the IFIs and the United Nations, to develop strategies to facilitate the implementation of the FATF Recommendations by countries facing capacity constraints.

31. At its meeting in February 2008, the FATF adopted new guidance to support the full and effective implementation of the FATF standards in low capacity countries. This guidance focuses on key implementation priorities such as co-operation, engagement, prioritization and planning. The guidance seeks to assist countries to implement the standards in a manner reflecting their national institutional systems and consistent with the money laundering and terrorist financing risks they face, and in a way which takes account of their sometimes limited resources.

32. Therefore, FATF recognises the key role played by its regional partners in this work, and continues to work to foster and support them, and is currently reviewing how it can further enhance their involvement. Equally, countries that are not FSRB members are encouraged to join the relevant regional body, thus widening the geographic scope of implementation.

33. The FATF is currently looking at the monitoring processes in place in the different FSRBs with the objective to promote results-oriented follow-up mechanisms as a tool to exert pressure on countries to improve their level of compliance with the FATF standards. As the FATF standards were significantly strengthened in 2003 and the EU Directive revised in 2005, many countries have only recently implemented many of the requirements, and it is too early to fully assess the results.

The current ongoing evaluation process remains a critical mechanism for promoting timely and effective implementation, and for contributing to the creation of a level playing field globally. The whole process has expedited and enhanced the implementation of the international standards. The FATF continues to work on strengthening the AML/CFT international network.

INCREASED TRANSPARENCY

34. The FATF has long promoted the need for adequate transparency in combating money laundering, terrorist financing and other illicit financial activity. The concept that competent authorities, as well as the financial sector, should be able to identify not only customers of financial institutions, but also the underlying beneficial owner of the assets, is at the core of the FATF Recommendations. This also extends to those in control of companies and other legal persons. Recommendation 5 requires all financial institutions to identify the natural person that is the ultimate beneficial owner of the property, while Recommendations 33 and 34 require countries to have appropriate laws and systems to ensure that their competent authorities can obtain timely access to accurate and current information on the beneficial ownership and control of legal persons (such as companies) and arrangements (such as trusts). The FATF has been working both with members and with many other countries through the network of FSRBs, to emphasise the importance of identifying the beneficial owner and to improve transparency more generally.

35. The FATF has also significantly increased its engagement with the private sector, through events with industry groups and the production of joint analysis on issues of common concern, soliciting private sector input to the typologies process, and through the establishment of a private sector consultative forum. More generally, in accordance with better regulatory practice, the FATF will maintain high levels of transparency

in its work, through direct communication, outreach and awareness-raising across all stakeholders, and making use of all available channels of communication.

36. Indeed, the FATF has sought to take a lead on the issue of transparency by publishing all its mutual evaluations reports in full, and has strongly encouraged the FSRBs and the IMF and World Bank to take a similar approach for their assessments. This increased transparency has enabled a much better identification of the AML/CFT risks that exist in other jurisdictions.

37. Strengthening communications with the public continues to be an important focus of each FATF Presidency. After each of the plenary meetings, the FATF President releases a Chairman's Summary of key decisions and outcomes of the meeting. In addition, the FATF publishes regular statements on countries for their lack of comprehensive AML/CFT systems (see Annex XXX, the Statement published in February 2009). The FATF also publishes annual reports and Newsletters (see http://www.fatf-gafi.org/findDocument/0,3354,en_32250379_32237245_1_32247548_1_1_1,00.html) as well as all reports on ML/TF methods and trends (http://www.fatf-gafi.org/pages/0,3417,en_32250379_32237277_1_1_1_1_1,00.html).

The FATF maintains high levels of transparency in its work, through direct communication, outreach and awareness-raising across all stakeholders, and making use of all available channels of communication.

ENHANCING THE STANDARDS WHERE NECESSARY

38. The FATF has sought, historically, to review its standards on a regular basis to ensure that they remain up-to-date and relevant in addressing the threats identified in the course of its ongoing work. Revisions of the original 1990 Recommendations were published in 1996 and 2003. The Special Recommendations were originally published in October 2001 and have not yet been subject to systematic review, although they have been expanded significantly in more recent years. This precedent of undertaking regular reviews has served the FATF well, by ensuring that it is comfortable that its standards remain relevant to current global ML/TF environment. It also sends the right message to those directly affected by the standards (not least of all the private sector) that the FATF continues to be dynamic in its thinking.

39. In recent years, the FATF and the regional bodies have undertaken a considerable amount of detailed study of both the global ML/TF threats (through the typologies and similar projects in other working groups), and of the measures adopted in individual jurisdictions to implement the current 40+9 Recommendations (through the mutual evaluation process). In addition, extensive work has taken place, in conjunction with the private sector, on the application of the risk-based approach to AML/CFT. These work-streams, which are all ongoing, have highlighted a number of issues in relation to the current standards. Recently a process has started, whereby in preparation for a 4th Round of mutual evaluations the FATF has agreed to consider possible areas where the standards need to be revised, as well as reviewing its mutual evaluation processes so as to focus on the most important issues. This process will allow FATF to address in a timely way any deficiencies and weaknesses that currently exist and to further reinforce the FATF standards as necessary.

The FATF continues to be dynamic in its thinking and is engaged in an active process of regular review of its standards on the basis of new threats and experiences drawn from the mutual evaluation exercise.

INTERACTION WITH THE PRIVATE SECTOR

40. Over the past year, the FATF undertook a series of outreach and consultation meetings with private sector representatives and industry associations. Meetings were held with major players in the financial sector, including associations and private businesses. Notably the FATF met with key private sector organisations in London in December 2007. This meeting focused on exchange of information on money laundering and terrorist financing techniques and reflects an enhanced commitment by the FATF to engage with the private sector. The response by the private sector has been overwhelmingly constructive and productive. Representatives have noted their support for continued engagement with the FATF.

41. A successful inaugural FATF-private sector meeting of experts on money laundering and terrorist financing methods and trends (typologies) was also held in December 2007. The topics discussed at the meeting focused on: trade finance (with a focus on trade-based money laundering and proliferation financing, corruption, VAT carousel fraud and pre-paid cards. Building on the success of this meeting, the FATF has decided to integrate such joint work into its typologies programme wherever possible. During the year the FATF has increasingly sought out the advice of relevant private sector experts on its typologies reports.

42. In October 2007, the FATF launched a new online forum—the Private Sector Consultative Forum—bringing together the FATF and key private sector bodies. The forum builds on existing outreach activities and has formalised and enhanced dialogue and a partnership approach between the FATF and key private

sector organisations from a wide range of sectors across the globe. Building on useful ideas raised in this forum, the FATF has agreed to initiate a joint project with the private sector on the role of intermediaries and other third parties in performing customer due diligence. The scope for improved information exchange between the public and private sectors, and for applying cost/benefit analysis to AML/CFT systems along with other possible projects, is being explored further with the private sector.

43. Private sector consultation meetings also resulted in the creation of the Electronic Advisory Group on the risk based approach. The Electronic Advisory Group on the risk based approach was set up in March 2006 and includes both public and private sector participants. This group was tasked by the FATF plenary to draft good practice guidelines on the risk-based approach (the RBA) and completed the Guidance on the Risk-based Approach to Combating Money laundering and Terrorist Financing: High Level Principles and Procedures in June 2007 as a joint initiative conducted by financial sector representatives with the FATF. Building on that initiative, a series of meetings have been held with representatives of various designated non-financial businesses and professions and appropriately focused guidance on implementing a risk based approach to combating money laundering is being devised for each business/profession. In June and October 2008 the FATF finalised the joint work and guidance for: (1) accountants; (2) dealers in precious metals and stones; (3) real estate agents; (4) trust and company service providers; (5) legal professionals and (6) casinos.

44. These guidance papers are intended to assist both public authorities and the private sector in applying a risk-based approach to combating money laundering and terrorist financing by: (1) supporting the development of a common understanding of what the risk-based approach involves; (2) outlining the high-level principles involved in applying the risk-based approach and (3) indicating good practice in the design and implementation of an effective risk-based approach.

45. In September 2009, the FATF will meet with representatives of the international banking, securities and insurance sectors to discuss issues of common interest. Such issues will be both technical in nature as well as dealing with broader questions related to measures that could be taken to enhance financial market integrity.

46. As a standard setter, the FATF decided to involve the private sector in the review process back in 2002. In May 2002, the FATF published a “public consultation document,” drafted with collaboration from the Regional Bodies, which addressed the upcoming revision of the Recommendations, proposed potential solutions to the issues, and invited comments from all countries, international organizations, private sector players, and other interested parties. The FATF sought to achieve the widest possible participation in this revision of the Recommendations. In response to the public consultation document, the FATF received more than 150 written comments.

The FATF is engaged in an ongoing dialogue with the private sector. Such dialogue has expanded in the last few years in several areas of work, especially in relation to the standards (including their revision) and emerging ML/TF trends and techniques.

Memorandum by the Financial Services Authority

INTRODUCTION

1. The FSA submits this memorandum in response to the Committee’s call for evidence on its inquiry into money laundering and the financing of terrorism.
2. This memorandum:
 - briefly sets out the FSA’s role in the UK’s collective effort to combat money laundering and terrorist financing;
 - summarises the FSA’s contribution to international anti-money laundering initiatives; and
 - answers three specific questions raised by the Committee.

A. BACKGROUND

3. The FSA is the single statutory regulator for the great majority of financial services in the UK. Its powers are conferred primarily by the Financial Services and Markets Act 2000 (FSMA).
4. FSMA requires the FSA to pursue four objectives:
 - maintaining market confidence in the financial system;
 - promoting public understanding of the financial system, including awareness of the benefits and risks of different kinds of investment or other financial dealing;

- securing the appropriate degree of protection for consumers, while having regard to the general principle that consumers should take responsibility for their decisions; and
- reducing the extent to which it is possible for a regulated business to be used for a purpose connected with financial crime.

5. Financial crime includes fraud and dishonesty, market abuse, and money laundering, as well as other financial crimes such as terrorist financing.

B. THE FSA WORKS TO REDUCE THE FINANCIAL SECTOR'S VULNERABILITY TO FINANCIAL CRIME

6. The FSA's remit is regulatory. We are not a police force and do not act as a mainstream criminal prosecutor. In pursuing our financial crime objective, we focus on firms' risk management systems and controls. In line with our approach to regulation in general, our financial crime regime is based on high-level principles, and promotes a risk-based approach to anti-money laundering (AML) and counter-terrorist financing (CTF). We also act as a gatekeeper by seeking to exclude firms or individuals of doubtful integrity from ownership or control of regulated firms.

7. The FSA works within the context of the UK Government's AML/CTF strategy. We are a competent authority under the Money Laundering Regulations 2007 and work closely with government, law enforcement and the private sector, both in the UK and internationally.

C. THE FSA WORKS CLOSELY WITH INTERNATIONAL STAKEHOLDERS

8. The UK's anti-money laundering regime comprises a complex framework of European law, UK law, regulation, international standards and industry guidance within which the FSA's financial crime efforts are delivered. As a result, we have to keep abreast of, and seek to contribute to, relevant international developments in the field of money laundering and terrorist financing to ensure that outcomes are proportionate and compatible with our aims and approach.

9. The FSA supports the Government in the negotiation of international standards and legislation. For example, we provide support to the Treasury at the Financial Action Task Force (FATF) and have advised the Government in the negotiation of the Third EU Money Laundering Directive. We are also represented in our own right at international regulators groups, including the EU Three Level Three Committee's AML Task Force and the Basel Committee's AML Expert Group⁴³.

10. We work bilaterally with international counterparts to enhance supervisory cooperation and oversight in financial crime matters, to provide technical assistance where appropriate and to exchange experiences and good practice. We also send staff to be assessors of AML/CFT implementation in other countries under the International Monetary Fund financial sector assessment programme and the FATF's own mutual evaluation programme.

SPECIFIC QUESTIONS ASKED BY THE COMMITTEE

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

11. The FSA has a statutory duty to cooperate with other authorities with similar functions in relation to the prevention of financial crime. We are signatory to a number of bilateral and multilateral MoUs and share information on financial crime issues with, and provide a wide range of assistance to, international counterparts. We are also active members of international organisations such as CESR (the Committee of European Securities Regulators)⁴⁴, which promote mutual assistance between their members. The international nature of the markets the FSA regulates, and of financial crime itself, means that international co-operation remains key to the FSA's financial crime efforts.

⁴³ Cf Annex for a brief explanation

⁴⁴ Cf Annex

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

12. The present system represents an international consensus of measures best suited to tackle money laundering and terrorist financing. The FSA advocates private sector consultation and involvement where appropriate so as to ensure that requirements to implement these measures are workable, effective and proportionate. Close collaborative working between the FSA, HMT and the private sector during the negotiation of the Payments Regulation resulted in the adoption of more risk-based and proportionate identification obligations on both the private sector and individuals. This collaborative working was also evident in negotiations for the Third EU Money Laundering Directive and the Payment Services Directive.

13. We also advocate close collaborative working arrangements between the FSA, HMT and the private sector in the transposition of EU legislation into UK law. This is evident in the way the implementing legislation is drafted, the way the FSA discharges its responsibilities under relevant legislation and in particular the prominent role of industry guidance such as the Joint Money Laundering Steering Group (JMLSG) Guidance in the UK's regime.

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

14. While we are not aware of immediate plans fundamentally to review the existing EU legislative framework or the FATF Recommendations⁴⁵, the FATF has started to consult increasingly with the private sector on key issues—including the drafting of guidance on the risk-based approach, where the project was co-chaired by the FSA and the private sector. FATF also recently established a Private Sector Consultative Forum and agreed to conduct an exercise to enable countries to feed in issues relating to the mutual evaluation process, or on its Recommendations. This may involve a furthering of private sector input and consultation.

15. At the same time, some efforts are still under way to clarify aspects of European legislation. These allow some scope for consultation with industry, as evidenced at the recent drafting of a “Common understanding of the obligations imposed by European Regulation 1781/2006 on the information on the payer accompanying funds transfers to payment service providers of payees” by European regulators through the AMLTF⁴⁶. We successfully argued for the need for private sector involvement in its drafting, which changed a document which might otherwise have imposed a substantial burden on the sector concerned.

30 January 2009

Annex

INTERNATIONAL AML AND CFT FORA IN WHICH THE FSA ARE REPRESENTED

AMLTF—The FSA is a member of the EU Regulators' Anti-Money Laundering Task Force (AMLTF), which is chaired by the Committee of European Banking Supervisors (CEBS) on behalf of CEBS, the Committee of European Securities Regulators (CESR) and the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS). The aim of this Task Force is to provide a supervisory contribution to anti-money laundering and terrorist financing issues, in particular to foster the conversion of supervisory practices and to facilitate the exchange of information and good practice relating to the implementation of the Third EU Money Laundering Directive.

Basel Committee AML Expert Group—The Basel Committee on Banking Supervision provides a forum for regular cooperation on banking supervisory matters. It has recently established an AML Expert Group, of which the FSA is a member. Over the last year, the group has focussed on how the international inter-bank payments system can be made more transparent.

CEBS—The Committee of European Banking Supervisors (CEBS) gives advice to the European Commission on banking policy issues, and promotes cooperation and convergence of supervisory practice across the European Union. The Committee also helps to foster and review common implementation and consistent application of EU legislation.

⁴⁵ The Financial Action Task Force (FATF) is an inter-governmental, standard-setting body whose purpose is the development and promotion of policies, both at national and international levels, to combat money laundering and terrorist financing. It established a series of Recommendations that set out the basic framework for anti-money laundering efforts and are intended to be of universal application

⁴⁶ Cf Annex

CESR—The Committee of European Securities Regulators (CESR) works to improve co-ordination among securities regulators, acts as an advisory group to assist the EU Commission, and works to ensure more consistent and timely day-to-day implementation of community legislation in the Member States.

CEIOPS—The Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) provides advice to the European Commission on drafting of implementation measures. It also issues supervisory standards, recommendations, and guidelines, to enhance convergent and effective application of the regulations, and to facilitate cooperation between national supervisors.

Memorandum by Jonathan Fisher QC

Queen's Counsel, specialising in white collar crime and regulatory cases, including money laundering and financial sanctions; Visiting Professor at the London School of Economics (Corporate and Financial Crime); Trustee Director of the Fraud Advisory Panel; General Editor, Lloyds Law Reports: Financial Crime.

1. I have prepared this written evidence mindful of the relatively narrow remit of the Sub-Committee's inquiry, noting in particular the wish to focus on the role of the EU and its member States in the global response to money laundering and terrorist financing, but without examining in depth the legal obligations imposed on member States and the regulated sector by the anti-money laundering framework.
2. In so far as my own field of experience and expertise is concerned, I am unable to shed much light upon matters such as the co-operation between financial intelligence units, the EU internal architecture, international co-operation, monitoring implementation and issues involving the determining of equivalence at an international level.
3. Accordingly, I have confined myself to sharing a small number of points with the Sub-Committee, based upon my experience in practice as a barrister when advising regulated sector and corporate clients on the effective implementation of the anti-money laundering, counter-terrorism and financial sanction regimes, as required by the Third European Directive on Money Laundering and other European and domestic legislation.

DAMAGING THE UK'S FINANCIAL INTERESTS

4. There is no doubt that certain sections of the regulated sector (typically financial institutions, law firms and the larger firms of accountants) are devoting significant financial resources to the implementation of anti-money laundering and counter-terrorism procedures.
5. What is more, there is a clear perception amongst those operating in the regulated sector that compliance costs are greater in the United Kingdom than elsewhere in the world due to the stringent way in which Part 7 of the Proceeds of Crime Act 2002 has been drafted, when read together with the Money Laundering Regulations 2007 and sector guidance issued by the Joint Money Laundering Steering Group and professional bodies.
6. Against this background, two important questions arise.
7. The first question concerns whether the effort made by the regulated sector in terms of time and cost is justified by an increase in the detection and prosecution of organised and financial crime, and if so the extent of this increase. This is a question for the investigation authorities to answer. Some high quality independent research also needs to be commissioned to look at this area.
8. The second question concerns whether the time and costs incurred by the regulated sector are damaging the UK's competitive position as a leading centre for the provision of financial services.
9. It is often said that the stringency of the UK's anti-money laundering and counter-terrorism financing regime leads financial services work to drift away from the UK into the hands of other countries, in particular recognised and stable financial centres such as Frankfurt and Dubai, with the UK's competitiveness damaged as a result. If experiences in the United States are anything to go by, it is recognised that the Sarbanes-Oxley legislation discouraged companies from seeking public listings companies in New York.
10. My experiences as a practising barrister in London, albeit limited and inevitably selective, lead me to doubt whether the conventional wisdom about damage to competitiveness is correct. I am aware of a number of American international law firms and global financial institutions which have opted to implement UK anti-money laundering and counter-terrorism procedures in all the jurisdictions in which they operate, so as to ensure that they can continue to work in London and satisfy the most stringent compliance requirements.
11. It is true that these firms complain, on occasions bitterly, about the increased compliance costs and enhanced administrative burdens encountered in London, but they take the view that these disadvantages are heavily outweighed by the advantages of continuing to operate in London which continues to be regarded as

a leading financial centre offering services at the highest level. There has not been an exodus of financial institutions from London as a result of the new anti-money laundering and counter-terrorism regime being implemented.

12. When the Channel Islands first introduced anti-money laundering legislation in 2000 some financial institutions expressed concern about the low threshold for “reasonable grounds for suspicion” and whether the new regulatory regime would force them to close their operations in the Channel Islands and move to another part of the world where the regulatory environment was less exacting. Experience has shown that financial institutions have continued to thrive in the Channel Islands, with regulators in the Channel Islands imposing compliance standards at the highest level.

13. Indeed, I believe a case can be advanced to say that, far from damaging a country’s financial interests, the imposition of robust anti-money laundering and counter-terrorism procedures serves to enhance a financial centre’s reputation and makes it a more attractive venue for financial services than other financial centres where the compliance regime is less rigorous.

FEEDBACK

14. One area of difficulty which I meet quite frequently in practice concerns the need for greater feedback from the Serious Organised Crime Agency (SOCA) with regard to typologies. In recent times SOCA has made efforts to engage with different sections of the regulated sector and in this regard it is right to recognise that there are obvious operational limits to the extent of information about suspicious conduct which can be divulged.

15. That said, there is much more which could be accomplished in terms of feedback from SOCA on many levels. There is a need for greater contact between SOCA and those operating in the regulated sector, in order to assist the regulated sector in identifying suspicious conduct and developing an awareness of contemporary trends of criminal behaviour.

FINANCIAL SANCTIONS

16. The Sub-Committee’s interest in the potential impact of the decision of the European Court of Justice in *Kadi* is well placed. The use of financial sanctions against individuals as opposed to countries is a comparatively new and rapidly developing area of jurisprudence, and to date the statutory architecture is wholly deficient. In addition to the interesting issues of principle which arise, a myriad of practical difficulties are beginning to surface, for example—what happens where an individual or a company is wrongly listed, how frozen assets can be identified by third parties, how frozen assets are to be managed by third parties holding them, etc.

17. It should not have been necessary for the European Court of Justice to intervene in *Kadi* by laying down elementary principles of justice operating in countries holding themselves out as governed by the Rule of Law. A clear statutory framework for the imposition of financial sanctions and the management of frozen assets needs to be put in place as a matter of some urgency.

18. I am happy to attend to give evidence orally if this would be considered helpful to the Sub-Committee’s work.

20 February 2009

Memorandum by FIU.NET

The inquiry examines the nature and extent of Member States’ cooperation in the field of the fight against money laundering and terrorist financing. FIU.NET is an instrument that supports and encourages this cooperation.

HISTORY

In early 1998, the idea for a mechanism for the automated exchange of financial intelligence information between FIUs was born in the Dutch FIU. The Dutch Ministry of Justice decided to launch a study into the feasibility of such a mechanism. The study was carried out in 1998 and 1999 and a prototype (demonstration) system was built. Together with the Dutch FIU, FIUs from Belgium, Luxembourg and United Kingdom participated in the undertaking.

The study proved that it was technically possible to build a fully decentralised system for the exchange of financial information related to money laundering (ie, without any central database). The system demonstrated that information exchanges could take place in full compliance with national as well as Community legislation.

Immediately following the adoption by the JHA Council of the FIU Decision (2000/642/JHA—Member States are requested to build a system for the automated exchange of financial information) a number of FIUs reached full agreement on the FIU.NET and formally committed to the FIU.NET Initiative. In November 2000, as a first step towards a more concrete set-up, it was decided to start an experiment leading to a Pilot Network. A network was build, connecting five FIUs (from Luxembourg, France, Italy, the Netherlands and United Kingdom). It became operational on 1 January 2002.

By mid 2004, the Commission awarded a grant to the Dutch Ministry of Justice (Agreement Number—SUB/2004/IM/G3/26) for the action entitled FIU.NET (“the action”) to explore, establish and validate the feasibility of a computer network for the exchange of financial intelligence information between the then fifteen Financial Intelligence Units (FIUs) of the EU Member States.

In 2007 a second grant was awarded to the Dutch Ministry of Justice (Agreement Number—JLS/2007/ISEC/591) to improve FIU.NET and to make it available for FIUs of all Member States.

In 2008 FIU.NET is earmarked again for Commission funding after 2009.

STRUCTURE CURRENT PROJECT

In the current project FIUs can participate either as User or Partner. Users are the Member State FIUs that are connected to and use FIU.NET. Partners are connected to FIU.NET as well, but have committed to put in more effort (time and money) and by that gained a decisive role.

The FIU.NET Project is governed by a Board of Partners—FIUs of Finland, France, Germany, Greece, Italy, Romania, The Netherlands and United Kingdom and the Dutch Ministry of Justice. The Partners meet four times a year, set the policy rules, decide upon all proposals, establish priorities and adopt the FIU.NET budget.

The Director FIU.NET is responsible for the financial part and the realisation of the Grant Agreement on behalf of the Dutch Ministry of Justice (delegated responsibility), is responsible for the FIU.NET Bureau and chairs the FIU.NET Board of Partners in order to safeguard the integrity of the ongoing Grant.

The FIU.NET Bureau is part of the Dutch Ministry of Justice and carries out the FIU.NET Project centrally. The FIU.NET Bureau provides assistance to the Director FIU.NET and the EU Member States in accomplishing the set goals, deals with logistical matters, is responsible for the Network Operation Centre and FIU.NET Helpdesk, the development of FIU.NET, provides support to connect the EU Member States and provides public information about FIU.NET (ie general information that is not reducible to one specific Member State). Next to that, the FIU.NET Bureau keeps statistics on the use of FIU.NET and reports them to the Board of Partners. The statistics are used for governing purposes and are not made public, in accordance with the Board’s decision.

OBJECTIVES

This current DG JLS FIU.NET project pursues the impulse FIU.NET gives to the concerted effort against money laundering and financial- and economic crime on a cross-border basis, by:

1. Connecting all 27 EU Member State FIUs.
2. Making the current version as user-friendly as possible.
3. Preparing the grounds for a new version of FIU.NET with a higher ambition level, to be realised in the future.

It is expected that at least 22 EU Member State FIUs will be connected by the end of this year (2009). Three FIUs have declined because of financial reasons and two FIUs are still anticipating a definite decision.

In the first quarter of 2009 a new version of FIU.NET will be implemented that is focussed on strengthening the international cooperation. It allows the FIUs to share information bi-laterally as well as multilaterally and to work together on case-files. Next to that, the new version is highly flexible and extendible. This means that any (future) requirement, either from FIUs or imposed by law, can be implemented.

The “rules of use” of FIU.NET are captured in the User Protocol. This document governs all topics related to exchanging data via FIU.NET; from the legal principles and operational agreements to security measures. The protocol is currently under revision and its final version is expected to be adopted in the EU Heads of FIU Platform meeting by mid 2009.

The future FIU.NET will be focused on enhanced cooperation between Member State FIUs and the policies and strategies of an FIU, bringing FIU.NET to a higher ambition level. The framework for this higher ambition level will be determined by ideas and thoughts of persons who are in some way practiced in topics like information exchange, international cooperation, policy advice etc. This group is called the Think Tank and will come together in February 2009.

ANSWERS TO THE INQUIRY THAT ARE RELEVANT TO THE FIU.NET

COOPERATION WITH AND BETWEEN FINANCIAL INTELLIGENCE UNITS (FIUs)

How effective is cooperation among FIUs, and between FIUs and other authorities? What are the practical results of this cooperation?

FIU.NET statistics show that the information exchange between FIUs is operational. Furthermore, via the FIU.NET project staff members from FIUs are brought together in User Workshops, test sessions for new releases, Board of Partners meetings etc. These get-togethers stimulate working together on developing the optimal tool for information exchange, set off operational projects between two or more FIUs, and keep the information exchange topic alive and into view.

EU INTERNAL ARCHITECTURE

To what extent is the EU internal architecture adequate to counter current and future challenges?

FIU.NET is an EU project par excellence, funded by DG JLS of the European Commission. The EU Member State FIUs participate in the FIU.NET under a coherent legal framework. More specifically, the FIU.NET finds its institutional justification in the 17 October 2000 Council Decision (2000/642/JHA) Article 7 (ie: Member States shall provide for, and agree upon, appropriate and protected channels of communication between FIUs), the Communication from the Commission to the Council and the European Parliament on the Prevention of and the Fight against Terrorist Financing through measures to improve the exchange of information, to strengthen transparency and enhance the traceability of financial transactions [COM(2004) 700 final] and the Directive 2005/60/EC of 26 October 2005 which states, amongst others, that arrangements for cooperation between financial intelligence units of the Member States in respect of exchanging information, including the establishment of an EU FIU-net, should be encouraged to the greatest possible extent.

What are the respective roles of Europol and Eurojust in countering money laundering and terrorist financing?

The FIU.NET Bureau and Europol have close contact with each other.

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Director FIU.NET
Dutch Ministry of Justice
The Hague
Netherlands

Memorandum by the Fraud Advisory Panel

1. INTRODUCTION

1.1 The Fraud Advisory Panel (the “Panel”) is an independent body of volunteers drawn from the public and private sectors. The Panel’s role is to raise awareness of the immense human, social and economic damage that is caused by fraud and to help both the public and private sectors, and the public at large, to fight back.

1.2 Members of the Panel include representatives from the law and accountancy professions, industry associations, financial institutions, government agencies, law enforcement, regulatory authorities and academia. The Panel works to encourage a truly multi-disciplinary perspective on fraud.

1.3 The Panel is a registered charity which is funded by subscription, donation and sponsorship.

1.4 The Fraud Advisory Panel welcomes the opportunity to give evidence to the House of Lords Select Committee on the European Union Sub-Committee F (Home Affairs) inquiry into money laundering and the financing of terrorism.

1.5 This paper has been prepared on behalf of the Fraud Advisory Panel by a special project group lead by Monty Raphael (a Trustee Director of the Fraud Advisory Panel and Joint Head of Fraud and Regulatory at Peters and Peters) with contributions received from Daren Allen (DLA Piper UK LLP), and Brian Dilley, Mark Daws and Patricia Barrameda (KPMG LLP).

2. COOPERATION WITH AND BETWEEN FINANCIAL INTELLIGENCE UNITS (FIUS)

2.1 *Question 1: How effective is cooperation among FIUs, and between FIUs and other authorities? What are the practical results of this cooperation?*

Cooperation among FIUs

2.2 The Egmont Group is an international body of national FIUs that promotes international cooperation in anti-money laundering and counter terrorist financing. FIUs operate under different guidelines but under certain provisions, Egmont Group member FIUs can exchange information with, provide other government administrative data and public record information to, and share expertise and training with their foreign counterpart FIUs.⁴⁷

2.3 In the UK, according to the FATF 2007 report, the FIU had established data sharing arrangements with Egmont partners, and has signed Memoranda of Understanding (“MOUs”) with the following jurisdictions: Australia, Canada, Colombia, Israel, Japan, Korea, Panama, Poland, Russia, Thailand, United Arab Emirates, and the USA.⁴⁸ The FIU facilitates the acquisition of overseas financial intelligence from foreign FIUs.⁴⁹ It also responds to enquiries for financial intelligence from Egmont partners, with a turnaround time of around 11 days.⁵⁰ The UK FIU has received positive feedback on the quality of the intelligence content of these disseminations, particularly from US law enforcement.⁵¹

2.4 The UK FIU also subscribes to FIU Net, an electronic system involving 15 EU countries which allows the exchange of basic identifying information.⁵² This is used as a pre-EGMONT check that may prompt a full, formal EGMONT request if the search results were a positive hit. The UK FIU responds to international subject information requests, as well as using this system to send out requests for information.⁵³

2.5 The UK FIU is also involved in the European Suspicious Transaction Reporting Project, which has been established in order to promote the use of AWF SUSTRANS, the Europol analytical work file on money laundering in the EU.⁵⁴ It supports the project working groups and is a member of the group which is responsible for producing a Statement of Intent.⁵⁵

2.6 In Switzerland, in the 2007 reporting year the MROS or the Swiss FIU received 368 inquiries from FIUs in 55 countries, which it responded to within six working days.⁵⁶ Of these, 96 inquiries were rejected as most of the inquiries either had no direct relation to Switzerland (so-called “fishing expeditions”), or had no relevance to a money laundering offence or a predicate offence to money laundering, or the financial information requested could only be provided by virtue of a request for mutual legal assistance but not through the FIU.⁵⁷

2.7 The Swiss FIU indicated that the processing of incoming SARs takes precedence over processing of incoming FIU inquiries, and the greater volume of incoming SARs led to a corresponding increase in workload.⁵⁸

⁴⁷ “The Egmont Group of Financial Intelligence Units (FIUs)”. About Egmont, www.egmontgroup.org/about_egmont.pdf.

⁴⁸ Third Mutual Evaluation Report Anti-Money Laundering and Combating the Financing of Terrorism, The United Kingdom of Great Britain and Northern Ireland, FATF-GAFI Financial Action Task Force, 29 June 2007, p. 275.

⁴⁹ The Suspicious Activity Reports Regime Annual Report 2007, p. 16.

⁵⁰ Ibid.

⁵¹ Ibid.

⁵² Third Mutual Evaluation Report Anti-Money Laundering and Combating the Financing of Terrorism, The United Kingdom of Great Britain and Northern Ireland, FATF-GAFI Financial Action Task Force, 29 June 2007, p. 275.

⁵³ Ibid.

⁵⁴ Ibid, p. 276.

⁵⁵ Ibid.

⁵⁶ “The Annual Report by the Money Laundering Reporting Office Switzerland MROS 2007. A Publication by the Federal Office of Police,” April 2008, p. 58-59.

⁵⁷ Ibid, p. 58.

⁵⁸ Ibid, p. 59.

2.8 In Germany, the FIU signed MoUs with the FIUs of Poland, and the Russian Federation, Canada.⁵⁹ These MoUs were signed upon the request of the foreign co-operation partners since they need a MoU for the information exchange due to their national laws. The national laws in Germany enable the German FIU to exchange intelligence with any foreign FIU without requiring a MoU to be signed by the German party.⁶⁰

2.9 In Germany, the FIU in 2007 exchanged information with 71 foreign FIUs on a total of 744 case-specific facts.⁶¹

2.10 In Spain, the FIU is able to provide rapid responses to external requests received from other FIUs (the delay in answering will depend upon the priority of the request and the conditions of access to the requested information).⁶²

2.11 In Greece, in 2007 the FATF assessment was that due to the lack of personnel and technical resources, there are serious doubts about the FIU's capacity to provide the widest range of international cooperation to its counterparts in a rapid, constructive and effective manner.⁶³

Cooperation between FIUs and other authorities

2.12 The UK FIU lists ones of its responsibilities as meeting the international obligations to the Egmont Group and other FIUs through the provision of financial intelligence upon request, both for UK law enforcement agencies and for international partners.⁶⁴

2.13 The UK FIU within SOCA facilitates regular dialogue between law enforcement end users and other stakeholders of the SARs regime to ensure that there is constructive communication and input into policy development and into developing and publicising best practice and guidance. The UK FIU facilitates a quarterly dialogue meeting with representatives from UK law enforcement agencies in order to share knowledge (trends and typologies) and best practice; and to encourage joint-working across operational and organisational boundaries.

2.14 The UK FIU has deployed mechanisms to ensure co-operation between domestic law enforcement, the reporting sectors, and other branches of SOCA.⁶⁵ The UK FIU has a Dialogue Team whose core function is to liaise between the sectors outlined above through formal meetings, informal contact, and workshops, and to facilitate feedback and share best practice with the reporting sector in sector specific seminars.⁶⁶

2.15 The UK FIU also has a dedicated International Team whose core responsibility is to liaise with international partners through Egmont, FIU Net, FATF, and the FSRBs. Their primary function is to carry out checks of the ELMER database on behalf of foreign FIUs and request searches from foreign FIUs on behalf of UK Law Enforcement.⁶⁷

2.16 In Spain, the SEPBLAC or the Spanish FIU incorporated Guardia Civil and National Police units in its internal structure.⁶⁸ Based on a review in 2006, the general perception was that each unit worked separately, without a full understanding of the efforts and the results.⁶⁹ For example, the final outcome or usefulness of the individual reports was not communicated to the FIU once they were sent to the competent authorities⁷⁰ Based on the same 2006 review, some of the authorities indicated that they found the reports from the FIU ineffective, but had not formally communicated these concerns with the other participants in the Spanish AML/CFT system.⁷¹

2.17 In 2004, the FIU met with various groups to facilitate co-ordination among these agencies, and the 2006 review indicated there is still room for improvement to promote more effective co-operation.⁷² The Spanish FIU presented its working procedures and tools to the Ministry of Justice, Confederation of Spanish Savings Banks (CECA), the Spanish Banking Association (AEB), the tax authorities and the Directorate General of Insurance and Pension Funds (DGFSP).⁷³ The FIU also entered into co-operation agreements with the Bank

⁵⁹ 2007 Annual Report of the Financial Intelligence Unit (FIU) Germany, Bundeskriminalamt, p. 42.

⁶⁰ Ibid.

⁶¹ Ibid, p. 40.

⁶² Third Mutual Evaluation Report Anti-Money Laundering and Combating the Financing of Terrorism, Spain, FATF-GAFI Financial Action Task Force, 23 June 2006, p. 156.

⁶³ Third Mutual Evaluation Report Anti-Money Laundering and Combating the Financing of Terrorism, Greece, FATF-GAFI Financial Action Task Force, 29 June 2007, p. 13.

⁶⁴ <http://www.soca.gov.uk/financialIntel/ukfiuStructure.html>

⁶⁵ Third Mutual Evaluation Report Anti-Money Laundering and Combating the Financing of Terrorism, The United Kingdom of Great Britain and Northern Ireland, FATF-GAFI Financial Action Task Force, 29 June 2007, p. 246.

⁶⁶ Ibid.

⁶⁷ Ibid.

⁶⁸ Third Mutual Evaluation Report Anti-Money Laundering and Combating the Financing of Terrorism, Spain, FATF-GAFI Financial Action Task Force, 23 June 2006, p. 144.

⁶⁹ Ibid.

⁷⁰ Ibid.

⁷¹ Ibid.

⁷² Ibid.

⁷³ Ibid.

of Spain, the National Commission on the Stock Market (CNMV) and the DGFSP, with the intention of promoting co-operation in the prevention of money laundering procedures.⁷⁴

2.18 In Germany, the FIU in 2007 was in close contact with numerous agencies involved in the prevention and suppression of money laundering.⁷⁵ The FIU provided support to national investigative authorities (police, customs, tax investigation offices etc.) in operational matters and in the form of presentations at special courses or at conferences in the field of financial and economic investigations.⁷⁶ The FIU also conveyed the results of strategic analyses to the national investigative authorities. This was done both for specific cases and in the framework of working groups.⁷⁷

2.19 The German FIU received 653 enquiries from foreign FIUs, which linked to 113 investigation cases conducted in Germany.⁷⁸ The types of crime or crime phenomena, revealed a concentration on fraud (47%), money laundering (21%) and drug offences (15%).⁷⁹ 91 requests for information were addressed to the German FIU by local investigative authorities for onward transmission to foreign FIUs.⁸⁰

Practical results of this cooperation

2.20 Opening and maintaining a line of communication among the Egmont Group of FIUs benefits law enforcement efforts globally by providing another potential source of foreign financial intelligence that may be critical to a national investigation.⁸¹

2.21 Among the benefits of this cooperation is the secure Internet system Egmont Secure Web (ESW), which allows for the members to communicate with one another via secure e-mail, requesting and sharing case information as well as posting and assessing information on typologies, analytical tools and technological developments.⁸²

2.22 FIU.Net is a network for the secure exchange of information between the FIUs at EU level. A review in 2007 indicated the FIU.Net, which was originally developed for the concerns of the administrative FIUs, was user-unfriendly in part.⁸³ However, since then the FIU.Net has received financial support from the EU Commission and the member states, and the Dutch Ministry of Justice has spearheaded a project to improve the system.⁸⁴

2.23 *Question 2: How does the private sector feed into this cooperation? To what extent is satisfactory feedback to the private sector required by international standards, and what happens in practice?*

The international standards

2.24 Feedback is required by the international standards FATF Forty Recommendations and third EU Money Laundering Directive (or Directive 2005/60/EC). FATF Recommendation 25 indicates FIUs should “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.”⁸⁵ The legal requirement set out by the Directive 2005/60/EC compels the Member States to embed into national law that “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.”⁸⁶

The European FIUs

2.25 In response to the international requirements, FIUs have employed various methods to provide more frequent and meaningful feedback to the private sector, through formal and informal information channels.

2.26 In the UK, SOCA’s more formal, structured means include (1) SOCA meeting with a vetted group of representatives of the reporting sectors, of law enforcement and of key policy departments to discuss sensitive casework and reporting issues; (2) holding quarterly sector-specific seminars for MLROs and senior management to discuss improving the quality of reporting, how SARs are used to fight crime, and threats to individual sectors, (3) presentations to financial institutions through SOCA’s liaison team that provide detail

⁷⁴ Ibid.

⁷⁵ 2007 Annual Report of the Financial Intelligence Unit (FIU) Germany, Bundeskriminalamt, p. 35.

⁷⁶ Ibid.

⁷⁷ Ibid, p. 36.

⁷⁸ Ibid, p. 41.

⁷⁹ Ibid.

⁸⁰ Ibid.

⁸¹ “Benefits of Egmont Group Membership,”

http://www.egmontgroup.org/files/library_egmont_docs/egmont_membership_benefit.pdf.

⁸² <http://www.fincen.gov/international/egmont/>

⁸³ 2007 Annual Report of the Financial Intelligence Unit (FIU) Germany, Bundeskriminalamt, p. 43.

⁸⁴ Ibid, p. 43.

⁸⁵ The Forty Recommendations, Financial Action Task Force on Money Laundering, 20 June 2003.

⁸⁶ 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, Article 35, paragraph 3.

relating to typologies and indicators, and (4) the information provided in the SOCA annual reports, website and newsletter which contains statistics, typologies, and other information.

2.27 Regarding SAR feedback, SOCA provides what it calls the “right level of meaningful feedback” and considers feedback may not be appropriate to every individual SAR.⁸⁷ SOCA has made contact with certain SAR reporters if the SAR led to an enforcement action.

2.28 The other European FIUs employ similar methods as that of the UK FIU. In Spain, the FIU also publishes an annual report with statistics and typologies on their website.⁸⁸ The FIU acknowledges receipt of all SARs sent by the reporting parties, but financial institutions are generally not informed of the outcome.⁸⁹ Guidelines with specific examples and indicators of risk activity have also been developed to allow each sector to have direct and actual feedback from Watchdog Commission members (regulators, supervisors, Police, SEPBLAC, etc.) on real cases and examples.⁹⁰

2.29 In Portugal, the FIU participates regularly in working groups with supervising authorities, as well as workshops and seminars with various entities. The FIU regularly provides feedback to the designated entities about their SARs.⁹¹ In 2006, it was reported that the statistics that are maintained are not comprehensive in all areas, making a full assessment of the effectiveness of these regimes difficult.⁹²

2.30 In the Netherlands, the FIU also produces an annual report with details of numbers of SARs per reporting group, new developments in money laundering, and similar information.⁹³

2.31 In Switzerland, the FIU provides a yearly report with statistics, typologies, judicial decisions and updates on the Egmont Group.⁹⁴

Satisfaction levels

2.32 We believe that there remains a desire in the private sector and financial entities for more communication and feedback from FIUs, particularly surrounding SARs. Many recognise there is room for improvement in communication and the relationship between the private sector and the FIUs. Among other things, this lack of communication is perceived to have limited the effectiveness of the intelligence contained in the SARs, undermined stakeholder relationships, and prevented mutual support and understanding.⁹⁵

2.33 *Question 3: What is the extent of the feedback and input on terrorist financing issues from intelligence and security services?*

2.34 The UKFIU receives and analyses SARs related to terrorist financing, which have led to terrorist enquiries. The UKFIU communicates with a wide range of financial institutions and trade bodies on terrorist finance issues, through a number of fora, such as the vetted group, sector-specific seminars for MLROs, and others as outlined in Question 1 above. The result of this has been increasingly useful SARs, as demonstrated by feedback from National Terrorist Financial Investigation Unit (“NTFIU”).⁹⁶ Between a fifth and a third of SARs disseminated to the NTFIU either lead to a longer term investigation or add substantially to an existing investigation.⁹⁷

2.35 We have no further information relating to the feedback and input on terrorist financing issues from security services.

2.36 *Question 4: To what extent are alternative remittance systems appropriately covered by obligations of cooperation in this context? What will be the impact of the implementation by Member States of the relevant provisions of Directive 2007/54/EC in this regard?*

2.37 The Payment Service Directive (Directive 2007/64/EC) (“PSD”) is unlikely to have a major impact on the anti-money laundering processes of regulated firms. There will be new conduct of business requirements relating to, amongst other things, the provision of pre-transaction and pre-contractual information to payment service users and the time by which payment transactions must be executed. Payment transactions must be accompanied with a unique identifier and there are provisions relating to refunds where transactions are not capable of execution. None of this should, however, affect regulated firms obligations to obtain

⁸⁷ SOCA website, SAR Frequently Asked Questions, <http://www.soca.gov.uk/financialIntel/faqs.html#default>

⁸⁸ http://www.seplac.es/espanol/informes_y_publicaciones/informe_anual.htm.

⁸⁹ The Third Mutual Evaluation Report On Anti-Money Laundering and Combating the Financing of Terrorism Spain, 23 June 2006, p. 104.

⁹⁰ Ibid.

⁹¹ Summary of the Third Mutual Evaluation Report Anti-Money Laundering and Combating the Financing of Terrorism Portugal, October 2006, p. 7.

⁹² Portugal: Financial System Stability Assessment, including Reports on the Observance of Standards and Codes on the following topics: Banking Supervision, Securities Regulation, and Insurance Regulation, October 2006, p. 28.

⁹³ http://www.justitie.nl/onderwerpen/opsporing_en_handhaving/mot/index.aspx.

⁹⁴ <http://www.fedpol.admin.ch/fedpol/en/home/themen/kriminalitaet/geldwaescherei.html>.

⁹⁵ Landers, Stephen, “Review of the Suspicious Activity Reports Regime (The SARs Review),” March 2006, p. 1.

⁹⁶ The Suspicious Activity Reports Regime Annual Report 2007, p. 16.

⁹⁷ SAR Frequently Asked Questions, SOCA website, <http://www.soca.gov.uk/financialIntel/faqs.html>.

information to satisfy customer due diligence requirements, either in terms of the nature of the evidence obtained or the point in time when it should be obtained.

2.38 The PSD will have a very minor impact on the nature of firms caught by the money laundering regime. This is because Annex 1 of the Banking Coordination Directive has been amended to include (1) payment services providers and (2) persons issuing and administering means of payment (with effective from 1 November 2009). Persons conducting activities set out in Annex 1 of the Banking Coordination Directive fall within the scope of the money laundering regime. Many payment services providers/persons issuing and administering means of payment will already be subject to the money laundering regime, for example as money transmitters, credit institutions or financial institutions. The change in definition, however, may bring a limited number of new businesses within scope. The PSD covers operating a payment account, executing card payments, direct debits and standing orders, issuing payment instruments and acquiring payment transactions, and money remittance.

3. EU INTERNAL ARCHITECTURE

3.1 *Question 5: To what extent is the EU internal architecture adequate to counter current and future challenges?*

3.2 *Question 6: What are the respective roles of Europol and Eurojust in countering money laundering and terrorist financing?*

3.3 The Fraud Advisory Panel has no comments to make in respect of questions 5 and 6 of the call for evidence in respect of EU internal architecture.

4. INTERNATIONAL COOPERATION

4.1 *Question 7: What have been the results of the third round of mutual evaluations of EU Member States to date carried out by the FATF and MONEYVAL, with particular reference to the effectiveness of international cooperation (including as between FIUs)?*

4.2 *Question 8: To what extent has the formal framework for criminal justice cooperation in this area been effective?*

4.3 The Fraud Advisory Panel has no comments to make in respect of questions 7 and 8 of the call for evidence in respect of international cooperation. However the Panel does believe that more efforts should be made to explain to the regulated sector that the regime is an effective crime prevention measure as evidenced through case studies and/or statistical measurement.

4.4 *Question 9: To what extent are these systems used to enforce compliance with national tax obligations?*

4.5 Mutual Legal Assistance (MLA) in enforcing national tax obligations has traditionally been restricted by the so-called “fiscal offences exception” which permitted MLA requests to be refused in respect of fiscal offences ie offences against laws relating to taxation, customs duties, foreign exchange controls and other revenue matters.⁹⁸

4.6 The fiscal offences exception has however gradually been eroded, in part by instruments to combat money laundering and terrorist financing. For example, the UN Convention against Transnational Organised Crime provides that State Parties may not refuse a request for MLA on the sole ground that the offence is also considered to involve fiscal matters.⁹⁹

4.7 Notwithstanding the decision in *India v Taylor*¹⁰⁰, that the UK will not enforce foreign revenue law, section 340(2)(b) of the POCA 2002 expressly extends the definition of money laundering to include dealings with the proceeds of criminal conduct committed in foreign jurisdictions subject to a qualified double criminality proviso.¹⁰¹ In any event, violations of foreign tax law may involve separate criminal conduct such as false accounting, conspiracy to defraud and obtaining a pecuniary advantage by deception. The proceeds of these offences would similarly fall within the scope of the UK money laundering regime.

4.8 The POCA 2002 further extends the range of MLA that the UK can provide in support of the investigation and prosecution of foreign tax offences to the ancillary orders freezing assets located in England & Wales, where there is reasonable cause to believe that the alleged offender or named defendant has benefited from criminal conduct (which, again, would include foreign tax evasion).¹⁰²

4.9 This passage does not include the ability of the UK to provide MLA in support of the combating of terrorist financing.

⁹⁸ European Convention on Mutual Assistance in Criminal Matters 1959, Article 2(a).

⁹⁹ Article 18(22).

¹⁰⁰ *Government of India, Ministry of Finance (Revenue Division) v Taylor* [1955] AC 491, [1955] 1 ALL ER 292.

¹⁰¹ Proceeds of Crime Act 2002 (Money Laundering: Exceptions to Overseas Conduct Defence) Order 2006, SI 2006/1070.

¹⁰² Proceeds of Crime Act 2002 (External Requests and Orders) Order 2005, as amended.

5. EU-UN COOPERATION

5.1 *Question 10: What is the extent of EU-UN cooperation on financing of terrorism? What are the longer-term implications of the Kadi judgment?*

5.2 The Fraud Advisory Panel has no comments to make in respect of question 10 of the call for evidence in respect of EU—UN cooperation.

6. MONITORING IMPLEMENTATION

6.1 *Question 11: What EU mechanisms exist for monitoring implementation of the relevant legislative measures, and what results in terms of formal compliance and effective implementation have so far emerged from the use of those measures?*

6.2 Formal Monitoring of the Implementation of the Third Directive: The European Commission is responsible for the implementation of all EU law including the Third Money Laundering Directive.

6.3 The EC is defined as “a European Community institution with powers of legislative initiative, implementation, management and control. It is the guardian of the Treaties and the embodiment of the interests of the Community. The Commission shares the right to initiate proposals in justice and home affairs with Member States”.¹⁰³

6.4 Member States are responsible for the implementation of Community law within their own legal system. However, under Article 226 of the EC Treaty and Article 141 of the Euratom Treaty, the Commission of the European Communities is responsible for ensuring that Community law is correctly applied. Consequently, where a Member State fails to comply with Community law, the Commission has powers to try to bring the infringement to an end and, where necessary, may refer the case to the European Court of Justice.

6.5 Under the non compliance procedure, started by the Commission, the first phase is called “Infringement proceedings”. The purpose of these early proceedings is to enable the Member State to voluntarily conform to the requirements of the Treaty.

6.6 The formal stages of the infringement procedure are as follows:

- (a) The first stage is a pre litigation procedure. A letter of formal notice is sent to the member state in which the Commission requests that the Member State submit its observations on its failure to apply Community law and offers a time limit within which it must be received.
- (b) The purpose of this request is to set out the Commission’s position on the infringement of community law and to determine the subject matter of any action, requesting the Member State to comply within a given time limit. The reasoned opinion of the member state must give a coherent and detailed statement, based on the letter of formal notice, of the reasons that have led the EC to conclude that the Member State has failed to fulfil one or more of its obligations under the Treaties or secondary legislation.
- (c) The second stage is referral by the EC to the Court of Justice which opens the litigation procedure.
- (d) The Commission, in accordance with the established case-law of the Court of Justice, enjoys a discretionary power in deciding whether or not to commence infringement proceedings and to refer a case to the Court. The Court has also acknowledged the Commission’s power to decide at its own discretion when to commence an action.

6.7 The implementation of the Third Money Laundering Directive in the member states of the EU is also informally monitored by FATF and MONEYVAL.

6.8 The Financial Action Task Force (FATF). FATF is an inter-governmental body which monitors members’ progress in implementing necessary measures, reviews money laundering and terrorist financing techniques and counter-measures, and promotes the adoption and implementation of appropriate measures globally.¹⁰⁴ In performing these activities, the FATF collaborates with other international bodies involved in combating money laundering and the financing of terrorism. While FATF does not monitor implementation of the relevant legislation measures as such it does measure implementation of its 40 + 9 recommendations which of course form the foundation of the third money laundering directive. The European Commission is a member of FATF. The Commission has also negotiated on behalf of the EU in respect of the relevant money-laundering provisions of the United Nations Convention on Transnational Organised Crime.

¹⁰³ http://ec.europa.eu/justice_home/glossary.

¹⁰⁴ <http://www.fatf-gafi.org>.

6.9 MONEYVAL's aim is to evaluate and adopt reports on the performance of member states of the Council of Europe which are not members of the FATF in complying with the relevant international anti-money laundering and countering terrorist financing standards.¹⁰⁵ Alongside, the performance of applicant states for membership of the Council of Europe which are not members of the FATF (provided certain requirements are met) and the performance of Israel.¹⁰⁶ Where appropriate, MONEYVAL may make recommendations to the evaluated countries with a view to improving the efficiency of their anti-money laundering and countering terrorist financing measures and to furthering international co-operation.

6.10 *Formal Monitoring*: On 16 October 2008, the EU announced that the EC had decided to refer **Belgium, Ireland, Spain and Sweden** to the European Court of Justice over non-implementation of the Third Anti-Money Laundering Directive.¹⁰⁷ This referral officially opened the litigation procedure. The ECJ will decide what sanction to impose on the four countries. The **25th Annual Report from the Commission on Monitoring the Implementation of EU Law** summarised the Justice, freedom and security sector as follows: "*the acquis has been growing significantly. The main challenges lie in ensuring timely and correct implementation of much recently adopted legislation together with managing a high volume of correspondence, complaints and a growing infringements case-load.*"¹⁰⁸

6.11 *Informal Monitoring*: The FATF policy that deals with non compliant members aims at putting peer pressure on member governments to tighten their anti-money laundering systems. The policy first requires the country to deliver a progress report at plenary meetings. Further steps include a letter from by the FATF President or sending a high-level mission to the non-complying member country. The FATF can also apply Recommendation 21, which will result in issuing a statement calling on financial institutions to give special attention to business relations and transactions with persons, companies and financial institutions domiciled in the non-complying country. The final measure is suspending the FATF membership of the country in question.

6.12 Effectiveness of Implementation: Member states have two years to adopt and bring in appropriate measures to implement directives, the deadline to implement the Third Directive was 15 December 2007. It is too early to say how effective the implementation of the Third Directive considering it has only been enshrined in national law for a little over one year.

6.13 *Question 12: What are the implications of those results for cooperation within the EU, and more broadly?*

6.14 Nearly all EU member states have now implemented or promised implementation of the Third Directive and, as stated above, those that have not successfully implemented have been referred to the European Court of Justice.

6.15 *Regulatory Arbitrage*: Implementation of the second directive in the EU was, to say the least, uneven with countries ie France taking up to five years to locally implement the 2001 directive. The impact of such uneven rates of implementation are negative for both the countries that delay implementation (higher risks of money laundering; higher risk assessments of other countries; potential negative declarations by FATF) and countries that implement on time (higher compliance burdens imposed on firms doing business with non-compliant states leading to a competitive disadvantage).

6.16 *Question 13: Has consideration been given within the EU or by the FATF to whether the overall results derived from the present system justify the burdens placed on the private sector?*

6.17 Burdens under the Second Directive: As mentioned above in paragraph 6.13, the Third Directive has only been enshrined in national law for a little over a year; as a result, it is too early to say whether the burdens placed on the private sector are justified.

6.18 KPMG compiled a survey of the impact of the Second Directive on private business in 2004 which was reviewed and updated in 2007.¹⁰⁹ The survey shows how significantly banks have responded to the challenge: in increased investment, senior management focus, and cooperation with governments, regulators and law enforcement. Despite the good intent and strong commitment found in many banks, they are noted as continuing to struggle to design and implement effective AML strategy and they expressed the belief that much more needs to be done internationally to combat money laundering more effectively. The following results were returned:

- (a) The survey shows continued support for global AML efforts by regulators, governments and law enforcement, with 93% of banks saying the burden of regulation is either acceptable or should be increased. However, a 51% majority of banks still believe that AML regulation could be focused more

¹⁰⁵ http://www.coe.int/t/dghl/monitoring/moneyval/About/MONEYVAL_in_brief_en.asp.

¹⁰⁶ Ibid.

¹⁰⁷ IP/08/1522.

¹⁰⁸ Brussels, COM(2008) 777/4.

¹⁰⁹ KPMG, Global Anti-Money Laundering Survey 2007.

effectively, through clearer legislation, better feedback to the industry and a greater endorsement of a risk-based approach.

- (b) Banks reported that senior management were more engaged in AML issues than they had been in 2004, with the percentage of respondents reporting that their senior management and their board of directors take an active interest in AML increasing by 10 percentage points to 71%.
- (c) Average AML costs were reported by the banks to have increased by 58% over the last three years. This was more than the banks had expected when in 2004, at that time, banks predicted costs would only rise by 43% over the following three years. Despite the unexpectedly high increase in AML costs, the banks anticipated that growth would slow, with banks predicting an average increase of 34% in AML costs over the next three years.
- (d) With growth in the proportion of income derived from international business, banks have become more global in their approach to managing AML risk. Nearly 85% of internationally active banks reported that they had a global AML policy in place.
- (e) There was a greater regulatory focus on governance and the resulting increase in the accountability of senior management for AML appears to have increased the need for independent monitoring and testing of AML systems and controls.
- (f) Increased regulatory and industry focus has led more banks to seek to apply additional scrutiny to Politically Exposed Persons (PEP). In the original 2004 survey, a surprisingly low number of banks performed enhanced due diligence on PEPs at account-opening (55%); in 2007, the figure increased to 81%. Moreover, significant numbers of banks have put in place specific procedures to identify and monitor PEPs on an ongoing basis (71% of all banks in the KPMG survey). However, with no universal definition of a PEP, there are likely to be substantial differences between individual banks' interpretation of the requirements in practice. With greater sensitivity to the reputational consequences of dealing with PEPs, banks are likely to be under pressure to examine how robust their procedures for PEPs really are. This is even more relevant in markets where business and politics are closely intertwined.¹¹⁰
- (g) Most of the banks relied heavily on their own people to spot suspicious activity and with banking becoming more electronically based, many are investing in sophisticated IT monitoring systems. Transaction monitoring continues to be the single greatest area of AML expenditure for banks, and is expected to remain so over the next three years.
- (h) The proportion of banks training over 60% of their staff was shown to have grown by nine percentage points since 2004, with face-to-face training, the most commonly used mechanism, and the method regarded as the single most effective.
- (i) Sanctions compliance was a major driver of AML costs between 2004 and 2007, ranked the third greatest area of AML expenditure after transaction monitoring and staff training. This reflects increased focus on counterterrorism, the long arm of the U.S. law, and growth in the number of lists that banks need to monitor against, as well as the tougher enforcement of sanctions requirements by regulators.

6.19 In September 2005, a study was published by Matthew Fleming, Research Fellow at the UCL Jill Dando Institute of Crime Science. It found that reports from the private sector that highlight possible money laundering were not being effectively utilised by law enforcement agencies. *"Members of the regulated sector—such as banks, building societies, lawyers and accountants—are required to file suspicious activity reports (SARs) when they have knowledge or suspicion of money laundering activity (or have reasonable grounds to know or suspect such activity). SARs are sent to the National Criminal Intelligence Service for processing, and are subsequently passed to law enforcement for action. The number of reports received by NCIS has grown considerably in the last few years; 56,000 were received in 2002 and more than 154,000 in 2004. But the extent to which SARs are actually used by law enforcement agencies and the value of SARs in helping to reduce crime has remained unclear."*¹¹¹ Since the time that this study was published, the UK FIU have been expending considerable resources on the improvement of their systems for the dissemination of SARs and promoting their use by law enforcement authorities.

6.20 *Burdens under the Third Directive:* The Third Money Laundering Directive imposes certain burdens on the public as well as the private sector. The types of burdens experienced by the private sector would be the financial, human resources and time requirements involved in moving to the new risk based system and then ongoing operation. The idea of a risk-based approach was introduced with the intention of reducing over-regulation in the instances of low risk whilst maintaining heavy regulation for high risk clients. Therefore, in

¹¹⁰ KPMG, Global Anti-Money Laundering Survey 2007.

¹¹¹ <http://www.ucl.ac.uk/media/library/laundering>.

terms of the operation of the system, the private sector will enjoy a decreased burden in low risk instances alongside an increased burden in high risk instances.

6.21 By way of example, the transition to a risk-based system in terms of the allocation of monies and humans resources (such as a money Laundering Reporting Officer, external consultants and expert advice on potential liabilities) and the resources and expertise required, once the system is operating, to gather and interpret information necessary to analyse the risk posed by a new or existing client.¹¹²

6.22 The Directive sets out three levels of due diligence that must be followed.

- (a) Article 11 relates to **simplified due diligence** which may only be used where there is low risk posed by the client. Basic identification procedures are carried out.
- (b) Article 8 relates to **normal due diligence**. An organisation is required to identify the client and beneficial owner of the transaction, the nature and purpose of the transaction, the client's objectives and ongoing monitoring of the relationship.
- (c) Finally, Article 13 relates to **enhanced due diligence** which must be applied to all clients which pose a high risk.

6.23 Although, on the face of it, it appears that the Directive has simplified the obligations imposed on the private sector by introducing three levels of CDD and a risk-based approach, there is still the burden of risk based analysis to establish which category each client falls under.

6.24 The Directive also imposes hidden burdens such as reliance on an institution with equivalent regulatory procedures. Although it appears that this is reducing an institution's burden by allowing it to "pass the buck", it actually fails to be effective because the principal party remains criminally liable for any omissions committed by the institution relied upon. There is also an argument that the notion of "equivalence" is meaningless because no country is fully compliant with the FATF Recommendations and international standards, therefore, they will be placed in a high risk category and one that would require normal, or even, enhanced due diligence.¹¹³

6.25 In addition, the private sector has expressed concerns relating to the lack of publicly available data¹¹⁴ when carrying out necessary due diligence.

6.26 The FATF and EU have not provided any obvious consideration of the burdens on the private sector. However, it has been noted that a review of the implementation of the Recommendations will be conducted by FATF and the UK government has committed to reviewing the implementation of the Directive (See Paragraph 6.32 below).

6.27 *Question 14: Are there plans to review the existing EU legislation or international standards in a manner which would be more sensitive to the position of the private sector?*

6.28 *EU Legislation:* There has been no indication that the Directive will be reviewed although the implementation of the directive is being both formally and informally monitored (see answer to question 11 above).

6.29 *International Standards:* FATF standards are enforced through a system of mutual evaluations to identify weaknesses in a State's regulatory framework. The evaluations bring to the surface concerns relating to the interpretation and application of certain elements of the Recommendations. FATF is currently completing the last third of their third round of evaluations which are due to conclude in 2011.

6.30 In December 2008, in his keynote address to the Council of Europe Committee of Experts on the Evaluation of MONEYVAL, Antonio Gustavo Rodrigues said that various delegations had raised concerns about the provisions of the 40+9 recommendations. He said that the FATF had, therefore, proposed a mechanism whereby countries could express their concerns in a coordinated way which would, in turn, allow the FATF to decide the issues that need to be addressed. The FATF's aim in this would be to fine tune the standards rather than provide for a wholesale revision of the Recommendations.¹¹⁵

6.31 *The UK Government* has committed itself to a review of the Money Laundering Regulations 2007. The review will focus on the effect that the implementation has had and whether policy objectives are being executed efficiently. Furthermore, the report will investigate whether any simplifications can be made with regard to the monitoring regime in order to minimise the policy and administrative compliance burdens. The review is due to be completed by December 2009.

¹¹² Report: Supporting Solicitors with AML Compliance", LNB News 23/01/2009 38.

¹¹³ David McCluskey, "Getting out of Europe—the 'Equivalence' Question", Mondaq, 28/08/2008.

¹¹⁴ Report: "Supporting Solicitors with AML Compliance", LNB News 23/01/2009 38.

¹¹⁵ http://www.fatf-gafi.org/document/56/0,3343,en_32250379_32235720_41849720_1_1_1_1,00.html.

7. COMPLIANCE AND EQUIVALENCE

7.1 *Question 15: What are the powers and procedures with respect to those third countries which fail properly to implement international standards in these areas? Are these adequate?*

7.2 Despite the global efforts to establish standards with which all countries agree to comply with, certain countries are considered vulnerable and lack the appropriate measures to be considered equivalent to such countries as have implemented the standards to a satisfactory level.¹¹⁶

7.3 The countries that are implementing these standards have an assessor body in relation to anti-money laundering (AML) and counter terrorist financing (CTF). The main objective of such bodies is to achieve the effective implementation of, and compliance with, the FATF recommendations.¹¹⁷

7.4 Examples of such organisations include but are not limited to APG (Asia / Pacific Group on Money Laundering), CFATF (Caribbean Financial Task Force), EAG (Eurasian), ESAAMLG (Eastern and South African), GIAMBA (Africa), GAFISUD (South America), International Monetary Fund, MENAFATF (Middle East and North Africa), MONEYVAL, OGBS (Offshore Group of Banking Supervisors), World Bank.

7.5 The key roles of such organisations are:

- (a) To assess their member's compliance with the global AML / CTF standards through an evaluation programme;
- (b) To coordinate technical assistance and training in order to improve compliance;
- (c) To participate in and cooperate with the international anti-money laundering network;
- (d) To conduct research and analysis into money laundering and terrorist financing trends and methods
- (e) To contribute to the global policy development of anti-money laundering and counter terrorism financing standards.

7.6 As established above assessor bodies do not generally have any powers by which they can enforce the compliance of AML/CTF by a member. They do, however, have a procedure in place for evaluating a member's compliance (see paragraph 6.8 above).

7.7 There is a distinction to be made between those countries with an assessor body and those without. Those without an assessor body are known as Third Countries.

7.8 Countries that are not party to an assessor body or the FATF have no powers or procedures imposed on them in terms of AML/CTF compliance. However, as supported by FATF, where a country chooses not to engage with the FATF recommendations and standards, the FATF would take firm action. In the past, FATF has made public its concerns about certain countries which have allowed others to alert their financial institutions to take into account the increased risk. The effectiveness of this procedure is based on the "peer pressure" aspect of FATF, the other countries will put pressure on the country that has failed to react to the AML/CTF measures which will intrinsically relate to the vulnerable country's international relations. The country will be further effected by the impact on its financial institutions of being considered a "high risk" country to do business with compared to the countries that have complied and are considered low risk. The effectiveness of the assessor bodies is their role in placing non compliant countries at a competitive disadvantage by publicising certain countries non compliance amongst the compliant countries.

7.9 *Question 16: Does the 2005 Directive adequately encourage non-EU States which have introduced equivalent systems to counter money laundering and the financing of terrorism?*

7.10 By Article 14 of the Directive member states may permit institutions in persons to rely on third parties to meet the requirements of Article 8.1 A-C—in essence customer due diligence and the elements of CDD being identifying the customer and verifying his identity, identifying a beneficial owner and obtaining information on the purposes and intended nature of the business relationship.

7.11 Such third parties are defined in Article 16 as broadly, institutions and persons in:

- (a) a Third Country subject to mandatory professional registration recognised by law
- (b) who apply CDD and record keeping requirements "as laid down or equivalent to those laid down in this directive" and their compliance with the directive is supervised or they are situated in a Third Country which imposes equivalent requirements to those laid down in a directive.

7.12 By Article 11, simplified due diligence (in essence a lifting of the CDD requirement) applies where the customer is situated in a Third Country which imposes requirements "equivalent to those laid down in this directive".

¹¹⁶ For an explanation of "equivalence" in the context of AML / CTF please see question 16 and 17 below.

¹¹⁷ <http://www.fatf-gafi.org/dataoecd/23/28/41594298.pdf>.

7.13 In both of the above respect, the directive provides that member states shall inform each other as to who is considered to have met the condition of equivalence.

7.14 The directive contains no definition of equivalence and it is plain that who is equivalent is defined by agreement amongst member states rather than by satisfaction of particular criteria. This in itself is potentially discouraging to third party member states who may feel that they satisfy the equivalence criteria but for one or another reason have not been included on the recognised list. For more on this see the next question.

7.15 *Question 17: How does the system for determining equivalence operate in practice?*

7.16 A representative committee at EU Commission level met during 2007 and 2008 to agree a list of “equivalent countries”. On 12 May 2008 HM Treasury released a “statement on equivalence” stating the agreement of that committee on the list of equivalent Third Countries. The list was described as a “voluntary, non binding measure that nevertheless represents the common understanding of member states.” It is not known whether there are currently any plans to revisit this list. Countries not included on the list or provisionally included (the UK Crown Dependencies “may” be considered as equivalent by member states) may therefore feel aggrieved at not being given full equivalent status with no apparent road map for allowing them to achieve it.

7.17 Of further concern is the effect (or lack of) that equivalent status has on member firms dealing with customers from equivalent countries. The Statement on Equivalence makes clear that the list “does not override the need for them to continue to operate risk based procedures when dealing with customers based in an equivalent jurisdiction”. Industry guidance from the JMLSG has been careful to emphasise that the exemption is based purely on the existence of relevant legislation. What this means in practice is that the risk profile of a customer from an equivalent territory is not of itself affected by the fact that its territory is equivalent. Because equivalence, *per se*, has no effect on the risk weighting of a country, it is at best simply another factor in the risk assessment of a customer and, at worst, meaningless.

February 2009

Memorandum by Lorna Harris, retired Government lawyer, evidence given in a personal capacity

1. Until early 2008, when I retired, I was Head of the Civil Recovery Unit, and Head of the International Co-operation Unit in the Crown Office in Edinburgh. Prior to that I had worked as Head of the United Kingdom Central Authority in the Home Office, and in the General Secretariat of the EU in Brussels. I have considerable experience of international co-operation in criminal matters, especially from a legal, rather than a law enforcement perspective. I am now working as a consultant in the area.

2. Between 2003 and 2005, on behalf of the UK, I chaired the Working Group in the Council of the Europe, in Strasbourg, which led to the finalisation of the 2005 Convention no 198. I am dismayed that the UK has not even signed this Convention, far less ratified or implemented it. This seems to me a major disincentive to effective international co-operation in the area.

3. Some of the international aspects of the 2005 Convention extend to Council of Europe States some provisions which would otherwise only be available to EU Member States. Although the UK does not necessarily need a treaty basis for co-operation to take place, the other state may well have such a pre-requisite. The absence of a signed agreement is a significant barrier to co-operation.

4. The UK has also not brought into force the Second Additional Protocol to the 1959 Mutual Legal Assistance Convention, although it was signed at the earliest opportunity in 2001. This also will exclude possibilities for co-operation with Council of Europe Member States, and is a further barrier to effective and broad ranging co-operation.

5. The FATF evaluation of the UK in 2006–07 highlighted some deficiencies in the UK’s (not Scotland’s) ability to handle routine or non urgent mutual legal assistance work in a timely and effective manner. This led to a marking of only “largely compliant” in this area. I understand that there have been improvements to the workings of the UKCA, and as a consequence I do not know to what extent that comment may remain valid. However, the UK has had a somewhat tarnished reputation in this area for some years, (sometimes unjustifiably) and it is obviously of great importance that as far as possible, the UK is able to provide an efficient service to its international partners.

6. There is the possibility of EU wide monitoring, through a system of peer evaluation set up under a 1996 Joint Action. This was done for mutual legal assistance in 1999–2000, and more recently for the implementation of the European Arrest Warrant, from 2006 onwards. It is an effective mechanism, and the reports, which are published, are thorough and influential. The reports themselves, and also the need to prepare properly for the evaluation, have been the prompt for considerable legislative change throughout the

EU. However, the system is expensive, labour intensive, and slow. Only one topic is dealt with at any one time, and each full cycle of evaluations takes up to three years to complete.

7. With more crime than ever having international aspects, efficient and effective international co-operation is correspondingly more important. The UK's common law system is not a natural ally of the continental civil law systems which predominate in the EU: the two systems do not always lie comfortably together. It is therefore even more important that for the UK working within the EU, strenuous efforts are made to overcome these apparent structural and conceptual barriers to better co-operation. Mutual recognition may provide a partial solution to the problem of different systems, but until it is based on true mutual trust, problems will remain.

January 2009

Memorandum by Professor Andrew Haynes, School of Law, University of Wolverhampton

EXECUTIVE SUMMARY

This response is designed to be brief and covers the following issues:

- the causes of the existing money laundering reporting laws;
- the fact that the laws do not work;
- that the laws make an excessive intrusion into civil liberties with no significant balancing benefit;
- that the laws impose considerable cost on the regulated sector with no significant balancing benefit; and
- that if the laws are retained they contain eccentricities and errors which should be addressed, These are dealt with in turn.

INTRODUCTION

It is worth briefly considering the main reasons why the laws under discussion were originally passed. The U.N. Convention Against Illicit Traffic in Narcotic Drugs and Psycho tropic Substances 1988 (the effective starting point for most of the U.K. law in this area) was passed for the following reasons:

1. A change in policing culture in the 1980's led by a belief that the traditional approach of pursuing the individuals running criminal organisations was ineffective.
2. The evolution of a belief in the U.S. Drug Enforcement Administration that the most effective way of immobilising drug organisations was by removing their financial resources. Locking up the highest level offenders was not on its own sufficiently disruptive, to many drug trafficking organisations and an attack against their assets was more likely to prove effective.
3. The consistent increase in criminal money and in particular illegal drug related money was a cause for concern.
4. A changing criminological climate in which it was believed that a crucial part in deterrence was the fear by criminals that their assets be seized.
5. The belief that, whilst pursuing, drugs, illegal arms or whatever the criminal profit was being derived from could lead the authorities to the criminals dealing with those assets, the key players in large criminal organisations tended not to come into direct contact with those assets but only the financial proceeds of it. Pursuing the proceeds on the other hand could provide a line of attack against the most important criminals.
6. Seizing the proceeds of crime also came to be seen as a way in which law enforcement could be made to pay for itself.

Clearly later events such as the 11 September terrorist attacks both added a sense of urgency and moved a greater degree of the focus to terrorist financing.

THE CURRENT STATE OF AFFAIRS

There seems no convincing evidence the money laundering reporting requirements have made a significant impact on criminals in general or drug dealers and terrorists in particular. Where breakthroughs have been made they normally appear to be the consequence of traditional police and/or intelligence work. The utilisation of asset forfeiture clearly has potential, though it has certainly not yet been fulfilled. However, the

process of seizing criminal and terrorist assets is not predicated by the existence of a money laundering reporting regime.

Another issue that arises is what effect the various developments in this area of law have had on human rights. We now live in a society where banks, building societies, solicitors, accountants and many others are required to spy on their clients on behalf of the state. Indeed, following the 2007 Regulations they must engage in a degree of proactive analysis of the extent to which their clients pose a potential risk of being launderers and make checks accordingly. This is a state of affairs in relation to state surveillance by the professional classes that surpasses anything introduced by either Hitler or Stalin. Both their regimes engaged in domestic surveillance but did not engage almost the entire financial, professional and business class as unpaid spies with a very wide definition of who was to be spied on.

It is now worth turning to the definition of “suspicion” that provides the basis for making a report. It was defined in the context of laundering by Longmore LJ. in *NatWest v H.M. Customs* with the SOCA an intervening party (2006) where he adopted the suggestion in *R v Da Silva* (2006)¹¹⁸ and applied it to both civil and criminal law:

The person must “think there is a possibility, which is more than fanciful, that the relevant facts exist. This is subject to the further requirement that the suspicion so formed should be of a settled nature.”

This is an extremely wide net with which the professional classes are expected to trawl their client base looking for people to report to the state.

The financial cost to the regulated sector has been widely examined by others and this response does not seek to duplicate them. It does however point out that these costs do not seem to have any significant corresponding benefit to balance against them.

The only difference the money laundering laws make to those laundering illegal money is the minor inconvenience of creating false identities, hiding the true owners of the money and distancing themselves from direct contact with the money itself. Drug sales are higher than ever, illegal arms sales, people traffickers and organised crime generally are thriving as never before, terrorist groups continue to develop and in an attempt to combat it internal spying is introduced in a manner and on scale attempted by no liberal society in peacetime in modern history. The reason for this is that for political reasons western governments do not find it congenial to declare a real war on the illegal drugs trade far and away the biggest source of illegal money because so many of their own electorate now consume them. There only appear to be two ways forward. One would be to declare a serious attack on the illegal drugs trade and bring in lengthy prison sentences for first offences of possessing trivial amounts of any illegal drug. The alternative would be to legalise the drug trade and leave it to large commercial drug companies to push to criminal elements out of the market. This response does not make a proposal for either, it merely points out that it is only one approach or the other that will actually make an impact on the problem. The current state of affairs seems a logical parallel to the position the United States found itself in during the Vietnam war. Once they had determined that they would not invade North Vietnam the war could not be won, yet enormous resources were committed to a fight that could not succeed because politicians did not want to perform a public “U turn”. Much the same position exists with regard to the current anti-laundering regime. Civil rights are trampled under foot, a fortune is spent, and no significant success is achieved or on the basis of the approach adopted, achievable.

The Money Laundering Regulations 2007 pose particular problems. Firstly, the requirement to determine that someone is a “politically exposed person” is based on the absurd notion that small or medium sized firms will be able to determine that their client is really the married daughter or illegitimate son, or the member of parliament of an obscure overseas state. The client may not even have the same surname as the person to whom they are related. Entering an overseas client’s name into a search engine such as google may in some cases give reason to suppose that the client may be, or be connected with one of the categories of “politically exposed persons”, but how is it to be proven if the client denies they are related?

In the case of large institutions such as major banks expensive software programmes they have purchased will flag up names that appear to be connected, but even here the problem is not solved. The client may deny that they are related to the key person with the same surname, but even if they admit the fact, the party dealing with them in the U.K. only has to satisfy themselves as to the source of funds. If the client is connected or related to a corrupt overseas official, they will presumably already have made “arrangements” with a corrupt

¹¹⁸ (2006) EWCA Crim 1654

overseas bank official to provide a letter confirming the source of the funds. On one hand the law requires people in this country to achieve what for most of them will be unachievable, and on the other, for the few institutions who can, it is not going to fulfill its objectives.

In addition, the requirement to determine who the “beneficial owner” of funds is again requires the impossible. Those clients who are acting legally will declare all those who have a beneficial ownership of the funds as defined by the statutory instrument.¹¹⁹ Those acting illegally simply will not. The hidden party will function as a shadow director, silent partner or hidden beneficiary, and there is no way the person acting for the client will be able to determine this. That being the case, why require them to?

Indeed where criminals and terrorists are concerned the existence of the laundering laws could be forcing them to bury their true identities, or to remove themselves from direct involvement with the money trail in a way that would not otherwise have occurred. There seems to be evidence that terrorist organizations are running cash economies for this reason. This may obstruct police and intelligence operations in a way that would not occur if the laundering laws did not exist.

PROPOSALS

1. That the current regime be abandoned.
2. A requirement remain for reporting where the reporting party “knows” laundering or terrorist financing is occurring.
3. A bulk reporting system be introduced along the lines of the computerized Australian AUSTRAC system but with a significantly higher base reporting figure due to the much larger scale of the U.K. economy and the need to keep the amount of reported material to a reasonable level.

IF IT WAS DECIDED TO RETAIN THE CURRENT LAWS THEN THE FOLLOWING FACTORS SHOULD BE CONSIDERED

1. *Illogicality*

The history of the law in this area is that it was created from two starting points; the desire to combat organised crime and as a response to terrorism. We are thus left with two sets of laws that alternately deal with these separate problems. Thus, there is a duty to report suspicion on one hand where it is suspected that a client is laundering the proceeds of crime and on the other where it is suspected that the money will be used to perpetrate an act of terrorism. However, there is no such requirement where it is suspected that a client is moving money to commit a criminal offence in the future other than a terrorist one. If someone in the regulated sector were to act for a client where they know or suspected that their client was moving money to commit a criminal offence in the future they may well commit a range of criminal offences: conspiracy to commit the offence planned by the client, aiding and abetting etc. However, there is no reporting requirement. There seems no logic to this. Perhaps the offences should be merged along the following lines:

“A person commits an offence if he handles money knowing or suspecting that it will be used to commit a criminal offence or that it amounts to the proceeds of one (such money shall be deemed as ‘criminal property’). This offence covers:

- (a) acquiring, using or possessing criminal property;
- (b) concealing, disguising, converting, transferring criminal property or removing it from the jurisdiction; or
- (c) entering into an arrangement which will facilitate the acquisition, use, retention or control of criminal property by or on behalf of another.”

The existing defences to sections 327 to 329 of the Proceeds of Crime Act and sections 15 to 18 of the Terrorism Act 2000 could then be added.

2. *Failure of the reporting definition*

S.337 of the Proceeds of Crime Act states that no breach of any law relating to disclosure has been committed provided, inter alia, “(2) . . . the information or other matter disclosed came to the person making the disclosure...in the course of his trade profession, business or employment.”

¹¹⁹ r.6

The same approach is adopted in s.19 of the Terrorism Act 2000 which states:

- (1) This section applies where a person:
 - (a) believes or suspects that another person has committed an offence under any of sections 15 to 18, and
 - (b) bases his belief or suspicion on information which comes to his attention in the course of a trade, profession, business or employment.”

However, in some cases where suspicion arises the key ingredient will come into the reporter’s possession outside their trade or profession. If he then continues to act without making a suspicious transaction report he will commit a criminal offence and if he does do so he no longer has protection from civil proceedings should the client find out. Perhaps s.337 needs amending to read:

“(2) . . . the information or other matter disclosed came to the person making the disclosure... in whole or in part in the course of his trade, profession, business or employment.”

S. 19 could be adapted thus:

“(b) bases his belief or suspicion on information which comes to his attention in whole or in parting the course of his trade, profession, business or employment.”

This should cover virtually all situations as even where the key information was received outside the trade or profession its effect would be as a result of the illumination it cast on the information previously in the reporting person’s possession.

In the event of the change to the law suggested by part 1 immediately proceeding having been adopted s.337 could be altered as suggested as s. 19 would no longer exist.

3. *The misleading nature of the recent statutory instrument (S.I. 200713398)*

December 2007 not only saw the Money Laundering Regulations come into force, but also the Terrorism Act 2000 and Proceeds of Crime Act 2002 (Amendment) Regulations 2007 which inter alia made the changes to s.333 of the Proceeds of Crime Act mentioned above. The effect of the change was to state that the offence of “tipping off” now only applies to those in the regulated sector, primarily those regulated wholly or partly under the F.S.A. regime. However, this is misleading as were someone caught by sections 327 to 329 Proceeds of Crime Act 2002 or sections 14 to 18 of the Terrorism Act 2000 they would potentially commit a string of criminal offences were they to tip off a client they had reported to the SOCA. Obvious examples would be obstructing the course of justice, aiding and abetting a criminal offence and in some cases being an accessory. If this amendment to the section is having no real effect, why retain it?

Memorandum by the Information Commissioner’s Office

The questions you have asked about suspicious activities reports (SARs) on the SOCA database certainly raise some data protection issues.

To answer your questions in turn:

Does the Information Commissioner have jurisdiction over this database (and if not, should he have)?

The Committee will be aware of the response to Lord Marlesford’s written question on this issue. This explained that, under the general remit of the Data Protection Act 1998, the Commissioner does have jurisdiction over the SOCA database. At present his general powers do not give him the right to undertake proactive inspections or audits of personal data processed by data controllers unless the data controller consents. As the Committee will be aware from its previous inquiries regarding Europol, s.54A of the Data Protection Act does give the Commissioner such an inspection power with regard to the processing of personal data in relation to Europol, and this extends to SOCA’s functions in this limited respect. This power would not extend to SAR data held by SOCA for domestic law enforcement or international cooperation purposes.

I would also like to draw the Committee’s attention to the provisions of the Coroners and Justice Bill, and the extent to which they might allow us to audit the processing carried out by SOCA. The data protection provisions of the Bill present a welcome opportunity to put appropriate safeguards in place and to address long-standing deficiencies in the Information Commissioner’s powers.

One of the powers introduced in the Bill is the use of assessment notices. An assessment notice will allow us to inspect an organisation to determine whether it is complying with the data protection principles.

As it stands, the Bill will only allow the ICO to serve an assessment notice on a government department or a designated public authority. It is unclear at this stage whether this will extend to SOCA. If the ICO is to regulate SOCA's processing effectively, it is important that the Bill allows us to inspect and audit their personal data processing activities. We would like to see the provisions of the Bill extended, so that an assessment notice can be served on any data controller, including SOCA. At the very least SOCA should become a "designated public authority".

If we do not have the ability to serve SOCA with an assessment notice, this will weaken our ability to regulate their processing in a sensitive area with potential for unwarranted adverse consequences for individuals.

Should there be very wide access to the database, for example by financial investigators and local authorities?

It is important that the SAR process is operated in a proportionate manner, both in terms of the inclusion of reports and of who should have access to them. In order to avoid unwarranted impact upon the privacy of individuals, who in most cases will not have committed any offence, the SAR database should focus on assisting with the investigation and prevention of serious criminal behaviour. The thresholds for reporting, recording and granting access should reflect this. It may be the case that financial investigators who are investigating serious crime would require access to the database. However, we would be concerned if local authorities were using the SAR database to investigate minor matters or matters which would not ultimately result in criminal prosecution. It is important to incorporate access controls which restrict use of the database to circumstances where it is necessary and proportionate.

Is it right that data should remain on the database even when the suspicion on which the report was based is shown to be unfounded?

The Data Protection Act states that organisations should not hold personal data for any longer than is necessary. The ICO would therefore expect SOCA to have established retention periods for the information held on its database. If there are SARs which are based on financial transactions meeting a particular threshold level rather than on hard evidence of criminal activity, then the prolonged retention of those records would be inappropriate and disproportionate. Although there may be instances where retention of SARs is justified, it should not be the general rule that all SARs are kept indefinitely.

David Smith

Deputy Information Commissioner

28 May 2009

Memorandum by Jonathan Leslie, Partner, Travers Smith (in a personal capacity)

AMENDMENT OF THE PROCEEDS OF CRIME ACT 2002

I have thought quite hard about how one might achieve the objective of removing from the scope of the reporting and consent obligations of POCA all the minor offences that many people believe should be excluded. I do not think that one can achieve the objective in one fell swoop as it is very difficult to capture the essence of what I think underpins the problem, but I think that there are some ways in which we could eliminate a number of the most typical examples.

To set the matter in context, it is a common concern among money laundering officers, and the legal profession as a whole, that we have to make reports of offences that, whilst undeniably being serious in their social consequences and deserving of enforcement, do not seem to have anything other than a somewhat tenuous connection to money laundering. The EC money laundering regime would appear to be intended to be directed, at least principally, to offences such as drugs and people trafficking and terrorist activities. POCA and the Money Laundering Regulations, however, go much wider than that and include, for example, planning, environmental, employment and motoring offences. I suspect that it is those offences that are the ones that are most frequently reported. I doubt that by reporting such offences any significant money laundering is detected, and it would be no real answer to say (as it might be said) that by reporting such offences then some good comes of it, as that should follow by enacting the legislation that makes the offences criminal and by enforcing the law through the usual channels. There is a large number of such offences captured by POCA and I think they should be removed from its ambit. I believe that that view is shared by many other money laundering officers. Doing so would free up a lot of the time spent on reporting such matters, which would leave SOCA free to investigate other matters that would typically be regarded as the real target of the EC Directives.

The problem, I understand, is that HMG specifically intended to cover all offences so as not to omit anything that might conceivably be money laundering. I do not think that we can easily solve the problem by a blanket form of wording that eliminates eg “all statutory offences”, as that would be far too wide and would no doubt leave out of POCA a great many crimes that could involve money laundering.

I have therefore gone at this another way and my thoughts are as follows, working through the various provisions of POCA where it might be possible to make amendments.

1. We might look first at where an amendment might be applied within POCA. I think that there is no point in drafting an exception to the obligations to disclose or to seek consent. I think that we would want these types of offences to be excluded from the POCA offences altogether.

2. I conclude that the amendment should be drafted as an exception to the scope of criminal offences in POCA . All of the offences require criminal property, which is, in turn, defined as a benefit from criminal conduct.

3. Criminal conduct is defined in Section 340(2) as conduct which:

“(a) constitutes an offence in any part of the United Kingdom, or

(b) would constitute an offence in any part of the United Kingdom if it occurred there.”

This seems the most appropriate place to draft a carve-out of the sort of offence that concerns me.

4. I suggest that an exception to the definition of criminal conduct could be inserted in section 340(2) POCA, which simply states that the definition excludes those offences which are identified by the Secretary of State by means of statutory instrument. The offences in question could then be listed in a statutory instrument by reference to the sections of the statutes where they appear and further offences could be added over time as appropriate. There would also probably need to be some enabling provisions added to the end of the Act which grant the Secretary of State the power to make such orders by statutory instrument.

This seems to me to be quite a useful place to start. It would mean that each exemption would have to be argued for individually, but that may be inevitable and would anyway help to get around arguments along the lines that a root and branch amendment would be too broad and would exclude too much. And I think perhaps that if we really focused on the most typical examples of what people complain of (planning, employment and so forth) we would possibly have dealt with the most problematic and repeated examples, by a relatively short list.

There is also a precedent (of sorts) for this approach within POCA, as when the legislation was amended in 2005 to repeal a provision that made it a money-laundering offence to deal in property arising from a transaction that was not a crime in the country in which the transaction was conducted if it would have been a criminal offence if it had been conducted in England. That rule no longer exists in every case, and the law was amended so that it the Secretary of State may by statutory instrument disapply the rule in specific cases. That is the reverse of what I suggest (as the amendment I refer to did introduce a general exemption which could be disappplied in specific cases, whereas I suggest that the general inclusion of all offences should remain subject the power to exclude specific offences) but it would be a useful start and if applied with sufficient specificity could make a big difference.

I should, lastly, make it clear that what I say, particularly with respect to the approach to reform of the legislation, represents my own personal views, but I believe that the views I express about the underlying problems are widely held by others in the legal profession.

Memorandum by Solicitors Regulation Authority

I write in response to the above matter in my capacity as Head of Fraud and Intelligence for the Solicitors Regulation Authority and as their money laundering reporting officer.

COOPERATION WITH AND BETWEEN FINANCIAL INTELLIGENCE UNITS (FIU's)

From my past experience as Head of Economic Crime in the City of London Police and in my current role I can say that cooperation between FIU's is excellent and is achieved primarily through a series of working groups under ACPO portfolio's (from a police perspective). This is then promulgated down through to an operational level where members of FIU's work together on multi faceted enquiries either as a primary ML investigation or as a secondary investigation in support of others where ML offences are associated with other forms of criminality. They often share knowledge, experience and best practise.

As the MLRO for the SRA, I have an excellent relationship with the Serious and Organised Crime Agency (SOCA) FIU who are always available to provide advice and guidance. In addition intelligence and information is shared on a case by case basis.

I have recently taken over as the chair of the anti money laundering supervisor's forum that meets every three months. The forum comprises of various AML experts from a wide variety of legal, accounting and regulatory professions where best practise, strategic, policy and training issues are shared. The meeting is followed by a further meeting with members of the SOCA FIU.

The private sector do not currently feed into any of the work that the SRA or myself do as the MLRO in respect of these particular matters other than being sources of information, primarily because of the lack of necessity and by the nature of the sensitivity of some of the work that we do. However the SRA board are of course aware and approve of what we do.

In relation to feedback on terrorist finance issues then some general information is provided by SOCA and I am aware of a number of general presentations that they and associated groups such as NTFIU have made. I have never received any feedback from the security services. I do believe that more specific and coordinated feedback should be made available and this was the subject of debate at the recent AML supervisor's forum that I chaired. This will keep this particular subject in the forefront of individuals minds, keeping them alert and the information flow maintained. I think that it is a question of seeing at least some kind of result, successful or otherwise or some form of productivity from the initial supply of information into the SARs system fed back to the originator of the SAR. I am aware that SOCA are making some effort in this area through their "pay back" conferences but so far little has information has been provided to my knowledge in relation to the terrorist funding arena although of course this is an extremely sensitive and delicate area in which to provide any feedback that is meaningful. I think also that more advice and guidance could be provided to originators in relation to typologies, warning signs and indicators.

Steve Wilmott QPM

Head of Fraud and Intelligence

22 January 2009

Memorandum by Taylor Wessing

INQUIRY INTO MONEY LAUNDERING AND THE FINANCING OF TERRORISM

We have read the Law Society's submissions and largely agree with them. However, they necessarily address the issues facing a broad spectrum of legal practices from the smallest firms to the largest, global, firms.

Taylor Wessing is a full service law firm with a widely acknowledged strength in industries rich in intellectual property based primarily in the three largest economies in Europe but also in emerging markets in Asia and the Middle East. We act for private and public companies, financial institutions, public sector bodies and wealthy individuals.

Our practice is being saddled with disproportionate costs in complying with UK anti-money laundering rules. Ensuring compliance with the client due diligence ("CDD") procedures required by the Money Laundering Regulations involves significant costs and hinders normal professional activities, especially in the current difficult economic climate. In comparison, the cost that other issues associated with making suspicious activity reports are modest. There is little, if any, evidence to suggest that compliance with the current CDD regime leads to any significant benefit.

The Solicitors' Regulation Authority ("SRA"), the regulatory body for solicitors, requires all solicitors to know their clients and to be able to demonstrate that they know their client. Because of the serious reputational and other risks associated with doing business with "unknown" clients, we question whether the CDD requirements of the Money Laundering Regulations provide any real, added, benefit to the firm or society at large.

The practical differences in the implementation of the EU Money Laundering Directives across the EU is staggering. The UK has gold-plated the legislation and imposed severe criminal sanctions. Conversely, countries such as Germany, France and Belgium, in each of which we have offices, have a much more benign legal regime with almost no requirement to undertake CDD of the same rigour as in the UK. Clients, let alone their lawyers, fail to understand why this is the case in a Single European Market, especially as there as no clearly discernable benefits from the UK regime.

A number of modest changes in approach would lead to a substantial reduction in regulatory burden without, we believe, any negative effect on society. In particular:

1. a photocopy of a passport, national identity card or driving licence should be sufficient evidence to identify and verify an individual in the absence of clear evidence of suspicion. The requirement for an individual's address to be separately verified, as opposed to ascertained, is especially burdensome. Utility bills are frequently in the name of one member of a family making it difficult to identify the other(s). Utility bills are increasingly unreliable as a means of identification or verification. Many families now only have internet generated invoices and not originals delivered by the utility company. We understand that they are easy to forge. A utility bill for a non-UK resident is of limited value. The effectiveness of electronic systems in the UK will frequently depend on whether an individual is on the electoral roll. This is an entirely different test from that required by the Money Laundering Regulations;
2. there are real practical difficulties, with no discernable benefit, in being required to verify the beneficial ownership of a company owned by a private equity house, venture capital fund and other financial institution, especially where these are located outside the UK;
3. the requirement for independent and reliable evidence is burdensome. It precludes companies providing photocopies of their corporate documents to verify identity. In many cases it is a time consuming and lengthy process to obtain these from a company registry or equivalent. In other cases such information is simply not available;
4. the requirement that the work cannot begin until CDD has been completed, except in narrowly defined circumstances, causes real practical difficulty. The reality is that many commercial organisations have complex structures for entirely legitimate reasons. Clients frequently demand immediate advice for entirely normal and legitimate business reasons. This is a clear example of a lack of understanding of the needs of legitimate businesses and a lack of focus and proportionality of the regime. This issue could easily be addressed by expressly permitting advice and preliminary actions but preventing higher risk activities, such as the establishment of companies, trusts, or the acquisition of land, shares or businesses. Much greater certainty and flexibility could easily be built into the UK regime;
5. the current risk based approach to CDD is a big improvement on the previous form based approach. However, a risk based approach only works effectively if those charged with enforcing it have sufficient appreciation of the risk and commercial dynamics of any particular situation. At present, there is a lack of confidence that those charged with enforcing the regime have sufficient experience and skills to apply a genuinely risk based approach, especially as they may have the benefit of hindsight; and
6. the list of equivalent countries causes concerns. It contains names of countries which may be regarded as counter-intuitive. It is very narrow in scope. Its legal status is unclear. In principle, the concept has considerable benefits which are not yet being realised.
7. The requirement for enhanced due diligence to be applied to individual clients who are not met personally is unnecessarily onerous, especially in the context of an overseas practice where many individual clients are often introduced by well established professionals while members of an extended family for whom the firm has acted over many years.
8. The procedure in section 17 of the Money Laundering Regulations, under which reliance can be placed upon introduction certificates simply does not work. No professional firm will accept additional legal obligations by providing an introduction certificate. Indeed, in our experience, many law firms and other professionals, especially substantial and reputable law firms in the USA are not prepared to provide any form of certificate or certification because of the perceived liability issues that may arise.
9. It is hopelessly optimistic to suggest that the rigour of the law can be mitigated by various "administrative" actions such as MOUs or prosecutorial discretion. Such an approach is muddled and fundamentally contrary to the separation of powers between legislature, the courts, and the executive.

We urge the removal of criminal penalties for breach of the many obligations under the anti-money laundering legislation. This would place lawyers in the same position as their counterparts in other EU member states. In any event, the criminal penalties in respect of "administrative functions" are disproportionate. Such matters are already covered by obligations under the Solicitors' Code policed by the SRA which can impose fines and ultimately remove solicitors from the ability to practice. This is a more than sufficient sanction.

We support the change in the definition of “criminal property” away from a list of all crimes. For example, we were recently involved in a transaction between two large and respectable companies with an enterprise value of about £100,000,000 because a subsidiary in one company had failed to obtain licences for a very small part of its business. The criminal property by the saving of the licence fee was a sum of less than £1,000.00.

The criminal provisions regarding failure to report money laundering and the substantive offences in sections 327–329 and 333 of Proceeds of Crime Act 2002 as amended are unnecessarily complex and uncertain in scope.

In conclusion, we urge:

- An end to the gold-plating of the UK anti-money laundering regime. There should be a genuine level playing field between the UK and its main trading partners, especially those in the EU.
 - A proportionate approach should be taken to the anti-money laundering regime and its enforcement in the UK.
 - Legal sanctions are removed for failure to comply with the client due diligence, especially by professionals.
 - The Anti-Money Laundering Regime should be recast in clear and understandable terms. This should be accompanied by legally binding, practical, and, above all, proportionate guidance.
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