Forensic Services
UK Financial Services Industry

Anti-Money Laundering Survey

Summer 2007

*connectedthinking

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Welcome

I am pleased to present PricewaterhouseCoopers' first UK financial services industry Anti-Money Laundering (AML) Survey 2007. Anti-Money Laundering has become a prominent business issue in recent times as legislators and regulators have sought to deny criminals access to the financial system.

One of the Financial Services Authority's (FSA's) statutory objectives is to combat financial crime, and with costs of organised crime currently being estimated to be £20 billion per annum by the Serious Organised Crime Agency (SOCA) there has never been more pressure on financial institutions to ensure their Anti-Money Laundering controls are fit for purpose. Financial institutions are making big investments in this area and want to know whether it is money well spent.

This survey will be of value to the industry in terms of understanding how things are progressing, as well as identifying some common issues and pointing to some of the challenges for the future.

The survey was conducted by PricewaterhouseCoopers' International Survey Unit (ISU), our Global Centre of Excellence for market research within our organisation.

All of the interviews were conducted under the Code of Conduct of the Market Research Society, ensuring complete confidentiality.

Our survey is based on a total of 148 interviews with money laundering reporting officers (MLROs) and other compliance professionals with AML responsibilities from across the financial services sector including retail banks, investment banks, insurers and investment managers, and covering a range of different sized organisations. MLROs accounted for 117 of the respondents. It is one of the most comprehensive surveys of its kind and provides a unique picture of the UK's financial services AML readiness. I would like to thank all those who took part for their willingness to spare their time and for providing a valuable insight into the AML issues they are dealing with.

Andrew Clark

Andrew Clark
Partner
Anti-Money Laundering Services

Executive Summary

PricewaterhouseCoopers set out to ask financial services institutions how they are coping with the FSA's new risk based approach to the anti-money laundering regulations.

We were particularly keen to understand the obstacles and benefits created by the risk based approach, and the present and future challenges facing those tasked with their implementation.

The results were, in the main, positive in terms of organisations' near-universal satisfactory implementation of the risk-based approach to combating money laundering in their organisations.

The survey shows high standards being set across the industry. But there is a negative perception of the cost benefits derived to date, which is emphasised by a widespread inability to quantify the costs of AML measures taken in previous years.

Senior management, in line with the approach expected by the FSA, are engaged with the issue. This strongly indicates that organisations should ensure that key individuals, such as the Money Laundering Reporting Officer (MLRO), are adequately supported and advised so that they can continue to deliver AML value to management.

A key issue highlighted in the responses is that many organisations are experiencing significant inefficiencies from their automated transaction monitoring systems, evidenced by extremely high false positive rates. PricewaterhouseCoopers are of the opinion that this is a key area for many organisations to reconsider in order to establish whether any cost or operational efficiencies can be found.

The six key themes that emerged from the survey are as follows:

Key Themes

Theme 1
Cost benefits of the AML risk based approach

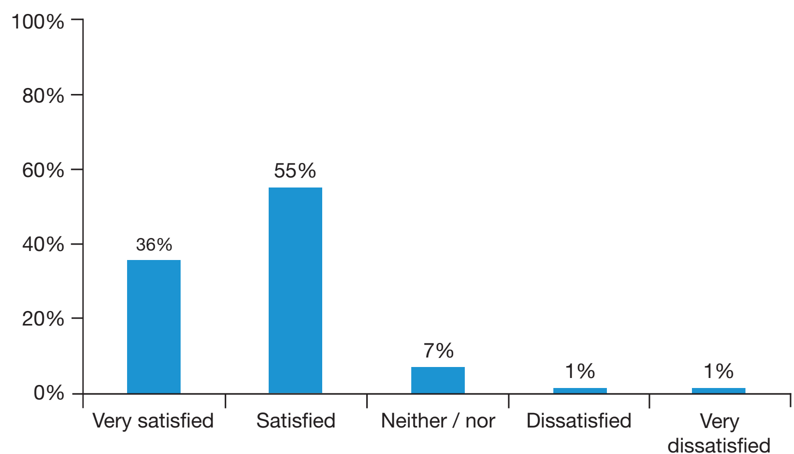
At the beginning of March 2006, the FSA replaced previous AML rules with broader requirements in the Senior Management Arrangements, Systems and Controls (SYSC) sourcebook for organisations to have risk based controls in place to combat money laundering.

As part of the FSA's strategy to simplify the handbook, the revisions were intended to deliver a better, more focused output for all, at a more proportionate cost.

This risk-based approach was expected to enable better targeting of resources to address the areas most likely to deter and detect money laundering within each organisation. The approach recognises that organisations face different challenges and so enables them to tailor their approach to AML accordingly.

With this in mind, it is hugely encouraging that an overwhelming majority of respondents (91%) said they were "very satisfied" or "satisfied" their organisation had successfully implemented the risk-based approach to anti-money laundering requirements.

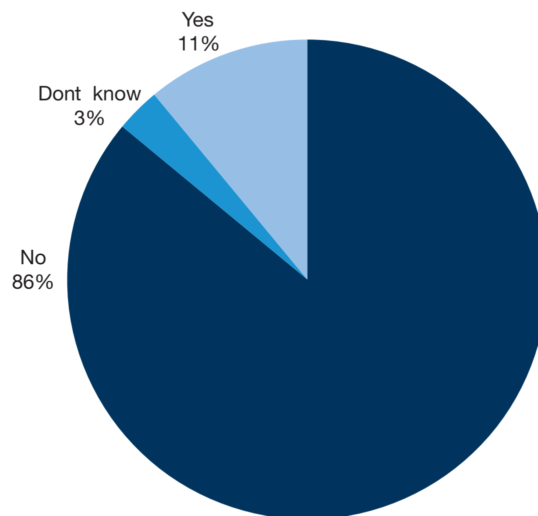
Figure 1: The percentage of organisations that were satisfied that their organisation had successfully implemented the risk based approach.



However, the cost benefits derived from the new approach are less clear. 82% of respondents indicated that they had not noticed any cost benefits of implementing the risk based approach, with six per cent stating that there had been a negative effect on costs. Of more concern was the fact that of those respondents who had not identified any cost benefits to date, 64% never expect to see any benefits.

The backdrop to this rather negative outlook, however, was that a large percentage (86%) of respondents were unable to quantify total spend on AML compliance in the previous year. More than four in ten were unclear about the proportion of their organisation's compliance budget spent on AML regulation.

Figure 2: The percentage of organisations that capture the amount in pounds that anti-money laundering compliance has cost in the past year.



So while respondents consider their AML budgets sufficient to ensure adequate compliance with the AML regime (96% positive) – indicating a growing willingness to commit financial resources to combat money laundering within the industry – it is not clear how they reach this conclusion.

The absence of an accurate measurement of AML compliance cost means that demonstrating the efficiencies that the regime is intended to deliver to businesses will become increasingly challenging. Forward-thinking management should have processes in place to record total cost in this area. These will enable them to evaluate the benefits (or otherwise) they gain from any changes they make in the light of future developments, as well as to monitor the reasonableness of ongoing costs.

Theme 2
The implementation of the AML risk based approach

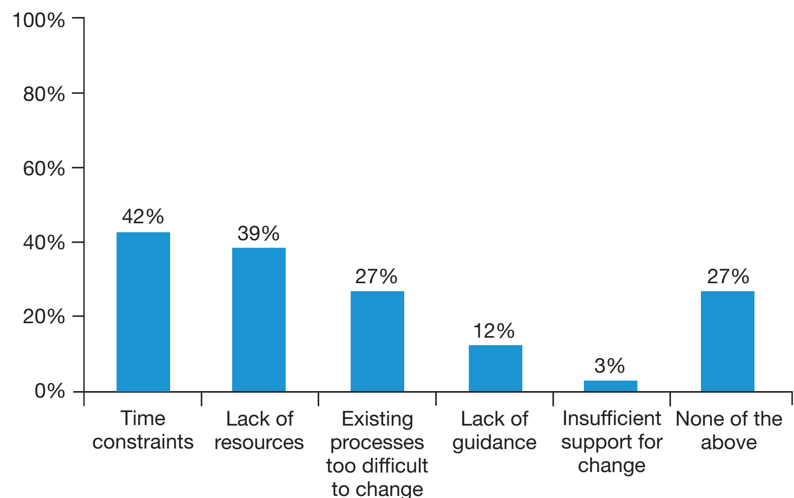
The financial services industry in the UK is focused on the challenges of combating money laundering.

An overwhelming 96% of respondents reported that they have formally risk-assessed their organisation for money laundering risks, and 96% of those have documented these risks. With more than seven in ten respondents indicating that they had, in their view, implemented the risk based approach without encountering any major problems, the overall picture is positive.

These results point to acceptable levels of engagement by organisations but they also highlight that industry benchmarks for implementation of appropriate risk based systems are high.

We hope that these positive statistics are backed up by reality and that organisations have not felt the need to overstate their position. However, we do know that where organisations indicated some problems in implementing the risk based approach, they were most concerned over time constraints (42%), lack of resources (39%) and the fact that existing processes were too difficult to change (27%).

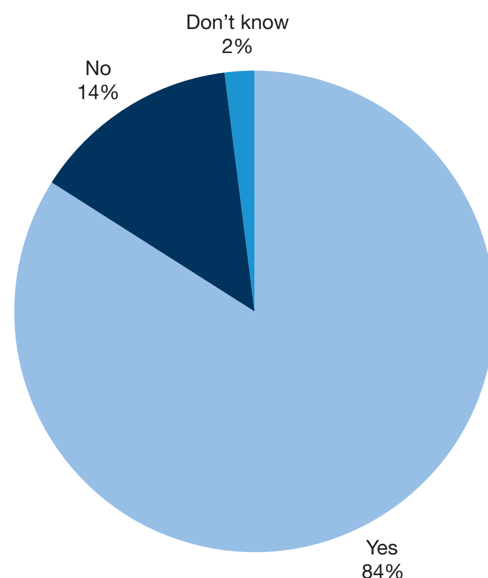
Figure 3: Key issues arising in the implementation of the risk based approach, based upon responses from those respondents that identified having “a few minor” problems or having “major” problems.



In any event, the industry perception will now be that any organisation that is non-compliant in the AML arena is an industry outlier and vulnerable to severe regulatory sanction, such as public censure and financial penalties.

Of course, identification and documentation of risks is not the whole story and the FSA has emphasised the need to manage identified risks appropriately in a number of publications, including its October 2006 Financial Crime newsletter. Therefore, organisations are expected to take proportionate action on the identification of money laundering risks, either potential or crystallised, within their business. However, 14% of respondents that had identified risks within their organisation had failed to ensure that a strategic response to these risks had been considered.

Figure 4: Percentage of organisations that have a strategic response to money laundering threats in place.



36% of respondents recognise that they need to enhance their policies and procedures, specifically in terms of more automation and transaction monitoring, staff training, better systems/computer software and certified/electronic IDs. An AML approach that fails to ensure appropriate action is taken in response to the risks identified will fall well short of the standards expected by the regulator under the risk-based approach. Those organisations that are aware of any current shortcomings in AML policies and/or procedures should therefore take rapid remedial action.

Theme 3
Senior Management Engagement

The FSA places an emphasis on the need for senior management to lead the approach to AML, with clear responsibility for the adequacy of systems and controls resting with the appropriate executive.

Encouragingly, MLROs were overwhelmingly positive about the attention senior management paid to the MLRO's annual report. More than nine in ten respondents said they believed the report was considered "important and useful" or "fairly useful".

Reinforcing this positive message was the finding that more than nine in ten respondents said they had adequate access to senior management to debate AML issues within their organisation.

For the small proportion of those that have failed to take the full responsibility at senior management level, the FSA is likely to use the full range of their powers to ensure that such organisations raise their game.

The results, however, generally indicate an approach of meeting the FSA's requirement for senior management engagement and taking appropriate levels of responsibility. However, they also bring into sharp focus the need for the employee responsible for the oversight of compliance with the FSA's rules on AML systems and controls – namely the MLRO – to deliver flexible, risk based systems that are appropriate for their organisation's business model.

Increased focus from senior management brings with it a need for MLROs to consistently demonstrate professional excellence and sound judgement. To help them achieve this, organisations should ensure that these key individuals receive the right levels of support and advice.

Theme 4
Governance

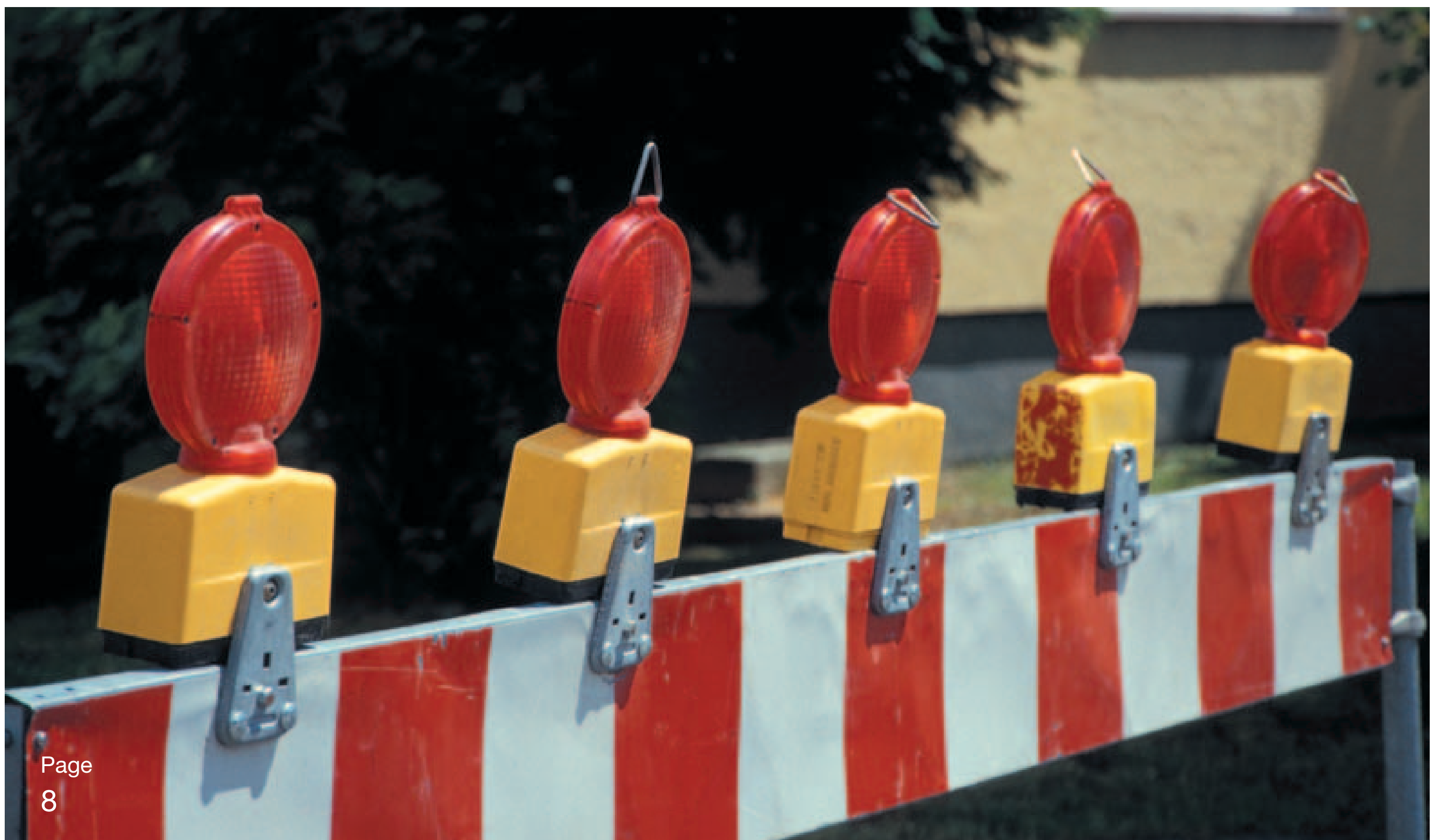
The FSA's statutory objective to combat financial crime creates a need for a cohesive, joined-up approach across all areas of financial crime.

If organisations are to demonstrate compliance with the high-level SYSC requirements, effective governance is key, as is the need for adequate resources in terms of both finance and people.

Effective financial crime governance will always include clear lines of responsibility within an organisation. However, in almost seven out of ten cases organisations said that they did not have a director of financial crime (who could also be the MLRO) or equivalent, which may be contrary to the FSA expectations. The FSA have been very clear in their expectation for senior management to give a clear lead and take ownership of their organisation's anti-money laundering effort, so these results are surprising to us. We also note that for those organisations that do have a director (or equivalent) of financial crime, the majority (75%) have five or fewer people in support, and that 29% have no direct support whatsoever. Therefore, many directors of financial crime will face the challenge of negotiating with other functions within the business for the commitment of resources to meet AML needs.

Though management engagement exists, it does not always follow that appropriate structures are in place to co-ordinate financial crime prevention activities and to ensure that the most cost-effective and productive processes are in place.

The importance of clear accountability cannot be overstated. In PricewaterhouseCoopers' view, clear financial crime governance that delivers focused and value-added AML systems and controls is vital for those organisations who seek to lead the industry in combating money laundering.

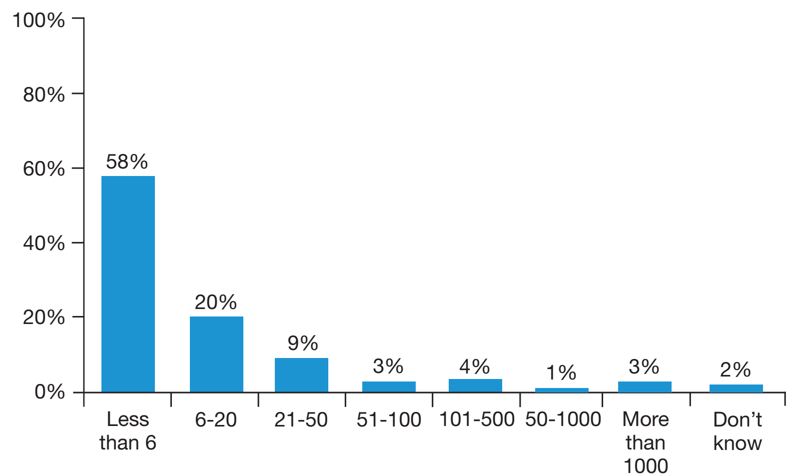


Theme 5
The approach to suspicious activity monitoring

Organisations are aware of their responsibilities to implement systems to monitor, and consequently report, suspicious activities to the Serious Organised Crime Agency (SOCA).

Most respondents generally report low levels of suspicious transactions, with over half (58%) reporting fewer than six per year.

Figure 5: The number of Suspicious Transaction Reports / Suspicious Activity Reports made by each organisation per year.



There are clear synergies between this monitoring for suspicious activities by organisations' clients and suspicious transaction reporting required under the Market Abuse Directive, where applicable. For example, organisations may benefit from ensuring the MLRO is the conduit through which all reports, either market abuse or money laundering related, are made. However, over a third of MLROs (34%) are not currently involved in, or are not aware that they are involved in, the consideration of potentially abusive transactions as per the Market Abuse Directive.

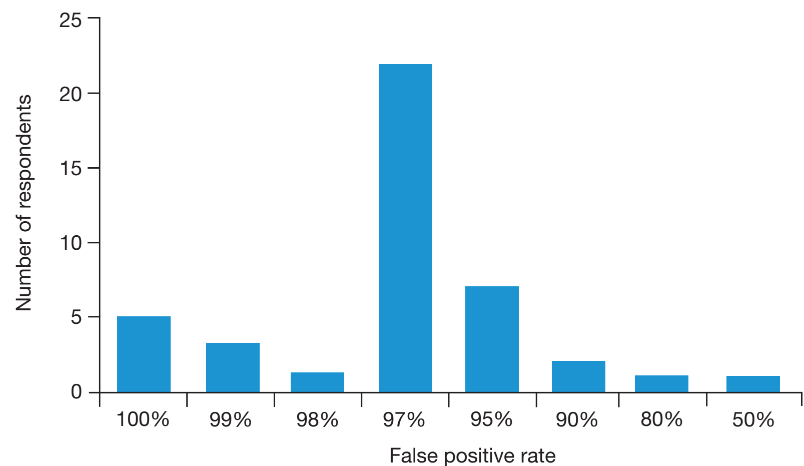
Some 34% of respondents state that their organisations had implemented an automated suspicious transaction monitoring system. The vast majority of these (29% in total) were purchased from third party vendors. Organisations with greater than 100 employees were more likely to have an automated system (42% as opposed to 25% for those with fewer that 100 employees).

Furthermore, from those organisations that have an automated or in-house monitoring system, 47% responded that their systems do not identify potentially abusive transactions under the Market Abuse Directive. Against a backdrop of industry concern that organisations are not yet reaping the cost benefits of the revised AML regime, organisations should consider investigating the potential efficiencies of bringing together their monitoring activity under both regimes. There remains the risk of reporting suspicious activities to one regulatory body but not recognising the need to also report to the other. The most efficient organisations will consider the AML and Market Abuse regimes in tandem, focusing on whether reports to SOCA should also be sent to the FSA, and vice versa.

The resources required to investigate potentially suspicious transactions was also sketchy, with 11% of respondents unable to quantify the average length of time taken from generation of an alert to reporting it to SOCA.

For those that identify suspicious activities through an automated system (34%), there is a clear reminder that this will only add value if those responsible for its implementation and effectiveness interpret the results appropriately. The responsibility for the effectiveness of the automated transaction monitoring system falls to the MLRO in 68% of cases and over four fifths (84%) of respondents stated that their automated systems generated at least 30% false positives. Of more concern was that 96% of these specific respondents indicated that their false positives rate was actually equal to or higher than 90%. Specifically, five respondents told us that they had a 100% false positive rate indicating that they get no value at all from their automated monitoring system. Although the survey does not purport to be exhaustive it is clear that many organisations are undertaking significant levels of monitoring with poor efficiencies.

Figure 6: The rate of false positives experienced for those respondents that indicated a rate in excess of 30%.



This serves as a timely reminder to ensure that the person responsible for the effectiveness of an automated system, usually the MLRO, has proper access to key information and adequate resources to enable the proper execution of their duties. PricewaterhouseCoopers advise all financial institutions to periodically consider the adequacy of the focus of their monitoring systems and the benefits that a reassessment or refinement could bring.

Theme 6
Future Trends

The AML landscape will remain challenging. Organisations must be able to demonstrate that their systems and controls are flexible and can adapt to change.

For example, over one-third of respondents (34%) indicated that one of the biggest challenges that their organisation faces in the future is the Politically Exposed Person (PEP) requirements.

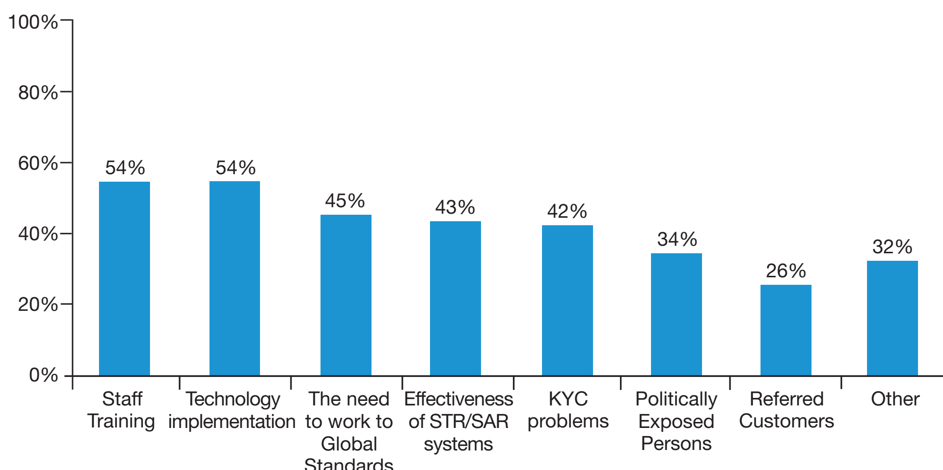
An organisation's business model will generally determine whether the existence of PEPs is an issue for them. However, with almost half (47%) of those surveyed reporting that they do not currently have a list of PEPs for their entire organisation, this issue is likely to be of regulatory interest in the near future.

Despite a wide range of initiatives to train staff - the most popular being training procedures (99%), communicating relevant policies (97%) and computer-based training (72%) - over half of those surveyed (54%) say that training staff presents the greatest AML challenge. We concur with this view as the culture of an organisation is one of the key components to an effective AML regime.

Forward-thinking organisations will take steps to embed the AML regime requirements into key staff consciousness. These efforts will often go beyond a one-off training session. The key to successfully raising staff awareness is to provide support and information on a continual basis.

Other future challenges that a significant number of respondents highlighted included technology implementation (54%), the need to work to global standards (45%), effectiveness of monitoring systems (43%) and Know Your Customer (KYC) problems (42%).

Figure 7: The biggest challenges faced by organisations in meeting anti-money laundering regulations in the future.



The FSA continues to play a vital role as organisations adjust to the new regime. A quarter of respondents said that the FSA had been "very supportive" in helping them combat money laundering, but 39% indicated that they felt either "unsupported" or "neither supported nor unsupported" by the FSA. Organisations with more than 100 employees are more likely to feel supported by the FSA (65% compared to 49% of organisations with less than 100 people) perhaps indicating a common desire across smaller organisations for more prescriptive rules. It is clear that organisations trying to combat the significant challenges of money laundering would welcome greater guidance and clearer explanations of what they are required to do and this presents a challenge to the FSA.

Our survey demonstrates that senior management is engaged and focused on what needs to be done and that the MLROs are alive to the challenges their organisations face. This is a positive contribution towards the FSA's combating financial crime objective and overall a good thing for the integrity of the UK's financial system.

Survey Summary:

Key considerations for Financial Institutions

1. Organisations should ensure that the costs of operating their AML controls are captured so that measurement of efficiency gains, or otherwise, is possible;
2. Successful implementation of the risk based approach to anti-money laundering has been widely reported, so non compliant organisations are clear outliers in the industry and must act now as they are increasingly vulnerable to regulatory sanction;
3. Organisations must continue to provide the appropriate resource and support to the MLROs to enable them to discharge their responsibilities effectively;
4. The co-ordination of financial crime prevention activities through a director of financial crime, or similar, can bring regulatory and cost efficiencies and benefits;
5. Organisations would benefit from periodically assessing the adequacy of their monitoring systems and the benefits that a reassessment or refinement could bring, and synergies exist between the monitoring required for the Market Abuse and AML regimes; and
6. As the AML landscape continues to change, those organisations that do not implement a flexible approach to AML controls will find it increasingly difficult to consider and deal appropriately with the new challenges that present themselves.

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www.pwc.com/uk/AMLsurvey2007

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