



Introduction by Philip Robinson

Hi, I'm Philip Robinson, the FSA's Financial Crime Sector Leader. Welcome to the fourth edition of our Financial Crime newsletter, which leads with coverage of our Annual Financial Crime Conference, held on 15 November. Our partners in the fight against financial crime provided excellent speakers and the conference received lots of good coverage, both in the press and in other media.

Other issues covered in this newsletter include:

- money laundering vulnerabilities in insurance;
- the Government's recently-announced Fraud Review;
- our new web-based financial crime training for firms;
- an update on how we are tackling the 'fear factor';
- the FSA's first prosecution for criminal market abuse;
- how fraud can affect consumers;
- the Home Office's new campaign on identity theft; and
- the Office for Fair Trading's (OFT's) work to combat scams.

However, before we get into the detail of these issues, I want to stress that the next

few months will be a challenging time for all of us in the business of reducing financial crime. And we all have important roles to play. The consultation on our proposal to remove the FSA's Money Laundering Sourcebook – outlined in Issue 3 – ended in October. We are now assessing feedback before making a final decision.

In addition, the new Guidance from the Joint Money Laundering Steering Group (JMLSG) – covered in Issue 2 – is expected in the New Year with a likely six-month implementation period. This means that firms and their senior management should now be thinking about how best to manage financial crime risk in a risk-based and proportionate way. We are currently training our staff on the risk-based approach and what firms should be doing. And we will be looking to see that you make a smooth transition to this new, more effective way of managing financial crime risk. So, as well as being challenging, this is also a period in which we can make a real difference to the effectiveness of the UK's anti-financial crime regime. Good luck.

As ever, we would welcome feedback on our newsletter, ideas for future issues and suggestions of how we might make the newsletter more useful for you. Our contact details are on the back page. We aim to publish one newsletter every quarter, but they might be slightly more or less frequent than that, depending on financial crime developments.



Philip Robinson
Financial Crime Sector Leader

Annual Financial Crime Conference: 'Fighting Financial Crime Together'

On 15 November, we held our annual financial crime conference at Congress Hall, London. We were pleased to have a programme of very distinguished speakers including the Attorney General, Commissioner James Hart of the City of London Police, and Sir Stephen Lander, the Chairman of the Serious Organised Crime Agency (SOCA).

Our Chairman, **Callum McCarthy**, opened the conference by stressing the importance of the fight against financial crime. He also welcomed the good work of other organisations such as the City of London Police and SOCA and, in particular, the Government's Fraud Review, which you can read more about later in this newsletter. Callum then spoke of the importance that firms' senior management should attach to financial crime and of the need for firms to recognise that financial crime risk is an important aspect of business risk. This meant senior management 'ensuring that their firm identifies the financial crime risks associated with the type of business they do, the parts of the world where they operate, and those specific to the firm itself...ensuring that they have systems and controls in place to mitigate the risks they have identified, with clear accountabilities for the day-to-day management of those risks, and appropriate reporting to top management and the board. And it means senior management ensuring that the firm has a strong "anti-crime" culture, as part of its overall culture, with a clear and consistent lead being given from the top.' You can find the full text of Callum's speech on our website at: www.fsa.gov.uk/pages/Library/Communication/Speeches/2005/1115_cm.shtml.

The **Attorney General's** keynote address outlined how the Government was taking forward its pledge to overhaul fraud law and the way that fraud trials are conducted to make them quicker and more effective. This was important, he said, because fraud was becoming the crime of choice for organised criminals and terrorist financing. He covered in depth three key elements of the Government's work on fraud: the Fraud Bill; judge-only trials; and the Fraud Review. The Attorney's full speech is available at: www.lso.gov.uk/speeches/financial_fraud_conf_speech_15_11_05.doc.

Later in the morning, SOCA's Chairman, **Sir Stephen Lander** set out the challenges facing SOCA and how it would approach them, making clear that fraud and money laundering would both be on their agenda. And **Commissioner James Hart** of the City of London Police gave a law enforcement perspective on fraud. He set out some of the problems the police face, such as the low fraud reporting levels, which lead to a lack of police resources to fight fraud effectively. He also outlined a number of common and emerging issues and identified insider fraud as the biggest current threat to financial services firms. This echoed comments Callum McCarthy made earlier in the day that there is increasing evidence of serious organised criminal groups placing their people in firms to commit fraud.

Speaking in the afternoon, **Lucy Makinson** of the Treasury covered terrorist financing and the Third EU Money Laundering Directive. **Ian Mullen**, Chairman of the JMLSG, followed and spoke in depth about the JMLSG's revised Guidance and its likely impact on the FSA and the firms we regulate. He also covered the seven key pillars of the revised Guidance:

- senior management responsibility;
- a risk-based approach;
- a reaffirmation of the vital role of the Money Laundering Reporting Officer;
- changes in the area of customer identification;
- a more balanced approach between initial identification and ongoing checks;
- the importance of training; and
- sectoral guidance.

As we have said before, we welcome the revised Guidance, which is consistent with our own views on effective, proportionate financial crime risk management. Ian Mullen's full speech can be found at: www.bba.org.uk/bba/jsp/polopoly.jsp?d=362&a=6435

The Conference was closed by **Philip Robinson** who spoke about the FSA's role in the fight against financial crime, what we have been doing in the last year, what we know about the risks and where we will be going in the months ahead. Referring to the evolving anti-money laundering (AML) regime and the JMLSG's revised Guidance, he said 'The new Guidance is a golden opportunity for firms to review

and, where appropriate, revise their procedures and internal controls: to make life easier for their honest customers and harder for the criminal.

‘I very much hope firms will rise to the challenge. Firms should already be thinking through what a more risk-based approach will mean for them. And I know some of you are already gearing up to change your ID practices, and will be quick off the blocks when the new Guidance is published. Once the Guidance comes into effect our supervisors are sure to be interested in how firms have responded.’

You can read Philip’s full speech on our website at: www.fsa.gov.uk/pages/Library/Communication/Speeches/2005/1115_pr.shtml.

If you attended our conference, we hope you found it interesting. We will, of course, be running another conference on financial crime next year. Among other things, it will be a good chance for us all to assess how successfully the new JMLSG Guidance has been implemented.

Money Laundering vulnerabilities in insurance firms

We take a close interest in the typologies work (i.e. case studies) of the Financial Action Task Force, which looks at trends and themes relating to money laundering and terrorist financing. An important example of this is the work of one of our insurance supervisors, Mike Thorpe, who led an international project team looking at the vulnerability of the insurance sector to money laundering.

The report was published in June 2005. It found that the expansion and increasing sophistication of the insurance sector internationally had not been accompanied by a corresponding widespread awareness that insurance products at the same time have become increasingly more attractive to criminals. The report encourages all those involved to reconsider money laundering risks in the insurance sector. The UK has the third largest insurance market in the world, so it is critical that we all work through the report and see what it has to say for our practices. We will be working with the industry and law enforcement to see what lessons we need to learn. And we are sure that insurance firms will want to be taking on board the comments of the report, which can be found at: www.fatf-gafi.org/dataoecd/16/8/35003256.pdf.

This is not FSA guidance

The Government’s Fraud Review

The Government has commissioned an inter-departmental review into the detection, investigation and prosecution of fraud. The review, which began work in October 2005 and reports to the Attorney General and the Chief Secretary to the Treasury, will consider the scope for improving the current arrangements. Its objective is to reduce the extent of fraud and minimise the harm it causes to the economy and wider society. The review will consider the scale of the problem; the appropriate role for Government in dealing with fraud; and how resources might be spent to maximise value-for-money across the system.

The review team’s work will be overseen by a Steering Committee, with Philip Robinson representing the FSA. The review team will consult widely with stakeholders in the public and private sectors before delivering its report by late spring 2006. In the meantime, they would like to hear your views on how the Government can more effectively tackle fraud. Please note that the review team will not be able to respond about individual cases of fraud. And, although we have made accommodation available to the review team, it is completely independent of us.

For more information, please contact:

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Tackling the ‘Fear Factor’ – an update

In his introduction to the second issue of this newsletter, Philip Robinson said that statements in support of a more risk-based approach ‘were hollow without delivery of a risk-based approach by FSA supervisors on the front line’. So developing training which will enable our supervisors to regulate in a risk-based, proportionate way has been one of our highest financial crime priorities this year.

And we've made a lot of progress. On 17 November 2005, we rolled out web-based **financial crime training** which we require all our staff to complete and be tested on. This will be supplemented by sectorally-focused interactive workshops on fraud and money laundering, aimed primarily at our supervisors, which are due to be rolled out from early next year. This training will be delivered by external specialists with expertise in financial crime risk management in a wide range of firms. We are aiming for a step change in our staff's understanding of the financial crime risks in their particular firms, and how they should be managed. So our message is that you should embrace a risk-based approach to financial crime risk management. Our supervisors will be expecting this of you.

Another way in which we have been trying to reduce the fear factor is by ensuring that our **enforcement policy** is driven by recognition of the risk-based approach. Two recent cases give a good illustration of how we are achieving this in practice.

Case 1

An emerging market bond broker had clients who were corporate vehicles established for trading purposes and operated by non-resident, wealthy individuals. The vehicles were incorporated in offshore jurisdictions, some of which had AML controls weaker than those in the UK. They were therefore seen as having a high risk money laundering profile.

The firm helped its clients to open accounts with a particular bank so they could participate in bond trades. But it failed to provide the bank with the appropriate information about the account users to assess the risks to which it was exposed. As a result of the firm's actions, a small number of individuals were able to operate anonymous accounts and over £8 million entered the UK financial system without the bank knowing the identity of its customers or the source of their funds. In addition, when opening some accounts, the firm used introduction certificates to demonstrate that it had carried out all necessary customer due diligence. However, some certificates contained misleading information.

The firm was fined £175,000 and the firm's Managing Director was fined £30,000 for failing to control the business effectively in relation to AML systems and controls.

Case 2

Earlier this year, we had concerns about a firm and its procedures for complying with its obligations under the Proceeds of Crime Act 2002. Our concerns stemmed from the way the firm dealt with a particular risk, which appeared to be both below the standards we would expect and out of step with its peers.

Following an investigation by our Enforcement department, it became apparent that this was a very complex area, involving the consideration of often conflicting factors. In a number of key areas, the firm had taken a risk-based approach to the issue and the process that it followed. And the steps it had taken were largely what we would expect, even if the final result wasn't.

Although we had clear concerns, senior management had engaged the issue. This was one of the reasons we didn't discipline the firm.

Web-based training programme for fraud and money laundering

Our Financial Crime Sector Team has developed a comprehensive and wide-ranging web-based training programme on fraud and money laundering for firms, very similar to the training developed for FSA staff. This is aimed at firms, their staff, and financial crime and compliance specialists.

By the end of the training, users should have an understanding of:

- the FSA's role in the fight against financial crime and our risk-based approach;
- the impact of fraud and money laundering on financial services and economies as a whole;
- new legislation (we will update the programme as legislation is made);
- individuals' and firms' responsibilities in relation to fraud and money laundering; and
- who the key players are.

The programme costs just £40 for unlimited use. For further details, please see: www.fsa.gov.uk/pages/Doing/Events/learning/crime.shtml.

First FSA prosecution for criminal market abuse

In August 2005, the former Chairman and Chief Executive of software firm AIT, Carl Rigby, and the company's former Financial Director, Gareth Bailey, were found guilty of making a statement, promise or forecast which was misleading, false or deceptive. On 2 May 2002, Rigby and Bailey recklessly issued a statement via RNS that stated that both turnover and profit of AIT were in line with expectations. This statement was misleading, false and deceptive because the forecasted profit depended on the inclusion of the revenue from three contracts which did not exist.

This was the first criminal action we have taken under s397 of the Financial Services and Markets Act (FSMA). This section sets out the criminal offences of making a misleading statement and engaging in a misleading course of conduct for the purpose of inducing another person to exercise or refrain from exercising rights in relation to investments. Rigby was sentenced in October to three and a half years in prison and was disqualified from being a company director for six years. Bailey was sentenced to two years' imprisonment and was disqualified from being a company director for four years.

Following the convictions we invited private and institutional investors who lost money after purchasing shares in AIT because of the misleading information to apply to the Court for compensation. As a result, in November, Rigby was ordered to pay £208,796 in compensation to investors, £381,273 by confiscation of assets and £250,000 toward the litigation costs we incurred. Bailey was ordered to pay £141,686 in compensation.

How can fraud affect consumers

Recently, we carried out a review of the impact of fraud directly on consumers. Our review highlighted the work which the financial services industry is doing to help consumers to protect themselves from fraud and the measures it has in place to help consumers who have become victims. The industry has an important role to play in alerting consumers to the risks of fraud and how they can protect themselves, not least because consumers are most likely to be receptive

to such information when they approach a firm for financial services. We welcome the steps the industry is taking to improve the level of fraud protection it provides, such as the introduction of Chip and PIN and using new technology to prevent online fraud.

In our review, we noted that where a consumer is a victim of fraud, the non-financial loss (eg the stress and inconvenience caused) can have a greater impact than the actual financial loss, which in most instances is temporary. We urge firms to bear this in mind when carrying out their investigations. But consumers, too, need to play their part in protecting themselves against fraud, particularly with many fraud risks on the increase. We welcome current initiatives to help consumers such as 'Get Safe Online'. And we are currently considering other ways to get the message across to consumers to play their part.

Identity theft consumer awareness campaign

It is estimated that more than 100,000 people are affected by identity theft in the UK each year, costing the British economy over £1.3 billion annually. To make consumers more aware of this problem and the steps they can take to protect themselves, we play an active role on the Home Office's Identity Fraud Steering Committee – a public/private partnership chaired by APACS. The Committee recently launched a new leaflet and poster campaign – details of which are at: www.identity-theft.org.uk/.

This campaign has generated great interest and several firms have asked about co-branding the leaflets. If you are interested in doing so, please contact Riten Gohil at APACS: riten.gohil@apacs.org.uk.

Who are the 'Scambusters'?

The Office of Fair Trading (OFT) has set up a new team to investigate consumer complaints about scams. The team has been formed as part of the OFT's commitment to targeting scams as a priority area for the next three years. It is estimated that UK consumers lose up to £1 billion per year to a variety of scams which exploit low-cost, mass-

marketing techniques to target recipients. These include bogus prize draws and lotteries, premium-rate prize promotions, psychic mailings and miracle health cures which mislead recipients.

The OFT's scambusters team brings together two departments within the organisation – one dealing with misleading advertising and the other with international scams. The aim is to stamp out the most prevalent frauds aimed at consumers. While the OFT won't be able to get consumers their money back, its powers and work with other organisations means it can help to shut down fraudsters, disrupt their operations and/or help police investigations.

Here are two examples of action the OFT has taken:

- The OFT has obtained undertakings from several traders who sent out misleading unsolicited prize draw mailings to entice people to phone a premium rate number. In one case, over 190,000 people called the premium rate number.
- The OFT obtained undertakings from a number of promoters of online matrix schemes which promised people the chance of gifts such as mobile phones in return for buying a low value product. The nature of the schemes meant that most people would not receive their gifts.

The Scams Enforcement Group, another OFT initiative, brings together law enforcement and intelligence agencies, private and regulatory organisations from the UK and abroad in an attempt to share information and coordinate action to bring the fraudsters to justice.

The OFT can be reached on 08457 224499 or enquiries@oft.gsi.gov.uk

Contact details

If you would like to receive this newsletter in future or have any comments on its content or format please contact us by e-mail at:
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Further financial crime information is available at:
www.fsa.gov.uk/Pages/About/Teams/Crime/index.shtml