



## Introduction by Philip Robinson

Welcome to the seventh edition of our Financial Crime Newsletter. Since October 2006 when we published our last

Newsletter, there has been lots of activity to strengthen the UK's anti-financial crime regime, and a lot of changes to the way that we marshal our anti-financial crime resources.

A key development since our last Newsletter was the creation of the new Financial Crime and Intelligence Division, which we announced at our Annual Financial Crime Conference in January. The new division brings together specialist anti-financial crime resources that were previously distributed across the FSA to create a new centre of expertise. You can read more about the new division and the work it will be carrying out on page two.

We also successfully launched our 'Fighting Financial Crime Website' in December, so that all stakeholders can keep up to date with major financial crime developments. We hope you will use it as a source of information, knowledge and advice, and that you will find our best practice guidelines useful.

As we outlined in our previous edition, the Third Money Laundering Directive has wide consequences for the whole of the financial services industry. Preparation for implementing the directive forms a key part of our work programme for 2007. As more firms will fall under the scope of our supervision from 15 December this year, we thought it would be timely to bring you up to date with our work in this area.

This is also a good opportunity for us to update you on a very topical issue – our work on Politically Exposed Persons (PEPs) and the implications for the industry arising from the changes in this area that the Third Money Laundering Directive will bring.

As ever, it is essential that we work together to combat financial crime. We are always interested to know what you in the industry think about what we are doing, as well as what you are seeing in your business. So we conducted our first Perception Survey to assess how firms perceive financial crime, as well as our work to limit its occurrence and combat its wider repercussions. We were pleased to see the results of the survey were generally positive, but we are listening very carefully to the feedback on areas where we can raise our game and will be using the results of this survey to inform our future work programme.

Following the successful launch of our Reporting System for mortgage intermediaries in April last year, March saw the launch of a new Reporting System for insurance firms and intermediaries. Under the new system, we want these firms to tell us when they suspect criminal behaviour may be taking place.

Both these systems work on a voluntary basis. In order for us to have a positive impact on fighting financial crime in these areas, we need as many firms as possible to provide us with information by participating in the systems. This will enable us to take action where it is necessary to reduce financial crime, protect consumers and maintain confidence in the market. So if you are not reporting already, why not start now? We are keen to continue developing channels of engagement and cooperation, so that a

true dialogue can take place between us and the regulated community.

As you will gather from the contents of this newsletter, our 'Partnership approach' is still very much the flavour of the day. It is only by working together that we will ensure that the financial system is an uncomfortable ground for fraudsters and money-launderers to operate, and that we will make a real difference.

You can find the articles I have referred to as follows:

- The New Financial Crime and Intelligence Division, page 2
- Our Annual Financial Crime Conference, page 3
- The supervision of New Businesses by the FSA under the Third Money-Laundering Directive, page 4
- Our work on Politically Exposed Persons (PEPs) and the implications for the industry, page 4
- The Progress of our reporting system for mortgage intermediaries, page 6
- The Launch of our reporting system for insurance intermediaries, page 6
- Our Perception Survey, page 7
- Our work on consumer awareness, page 7
- The launch of our Financial Crime website, page 8
- The Passport Validation Service: changes of pricing structure, page 8



**Philip Robinson**, Director, Financial Crime and Intelligence Division

## • The New Financial Crime and Intelligence Division

We created the Financial Crime and Intelligence Division at the beginning of 2007 to bring together financial crime expertise that was previously distributed across the FSA. We want to create a centre of financial crime expertise which will enable us to increase the regulatory focus on financial crime and better enable us to achieve our financial crime objective. The Financial Crime and Intelligence Division's mission is to provide the specialist leadership, tools and expertise so we achieve our financial crime outcomes. It is a centre of excellence, rather than a single resource for us – you will not see any reduction in the focus on financial crime in other areas of the FSA, including the supervisory divisions, because of the new division.

The Financial Crime and Intelligence Division is made up of the Policy and Intelligence department that was previously part of the Regulatory Transactions Division, the Financial Crime Sector Team and the newly created Financial Crime Operations Team.

The Financial Crime Operations Team is led by Edna Young (who will be well known to many of you as she was previously the manager of the Financial Crime Sector team) and comprises four specialist teams led by financial crime experts.

The new Operations Team will carry out thematic projects on samples of firms to address key financial crime risks that have been identified, as well as case work where specific financial crime issues have arisen in individual firms. The team will also provide more extensive technical support to colleagues in Supervision and Enforcement as they deal with financial crime issues in individual firms or thematically. This will include providing guidance to supervisors (and firms) on the nature of current financial crime risks, the effectiveness of current mitigation by firms and best practice tips.

When the new Money Laundering Regulations come into force, one of the four teams within Financial Crime Operations will take on the task of supervising the new-scope firms that will be brought within our remit by the Third Money Laundering Directive for Anti-Money Laundering/Counter-Terrorist Financing purposes (you can read more on the Supervision of new

businesses by the FSA under the Third Money Laundering Directive on page four).

## • Our Annual Financial Crime Conference

On 22 January, we held our annual Financial Crime Conference at the Queen Elizabeth II Conference Centre, Westminster. We were pleased to have a programme of very distinguished speakers including: Ed Balls MP, the Economic Secretary to the Treasury; Commissioner Mike Bowron of the City of London Police; and Bill Hughes, the Director of the Serious Organised Crime Agency (SOCA).

Our CEO, John Tiner, opened the conference by summarising the main achievements of the past year in the fight against financial crime. These are namely the move towards a more principles-based anti-money laundering (AML) regulatory regime, the publication of revised Joint Money Laundering Steering Group Guidance, and proposals for a new UK strategic approach to tackling fraud as highlighted in the government's Fraud Review.

He also laid out our strategy to improve the fight against financial crime, including creating the new specialist division mentioned earlier, so that over the next three years we expect to see:

- a better understanding of the scale and incidence of financial crime in the UK financial sector;
- a reduction in the extent of vulnerability to financial crime in the industry; and
- an increasingly risk-based approach to international and domestic financial crime policies and practices.

John Tiner stressed the need 'to get smarter at working together', emphasising the importance of improving data sharing both at the national and international level.

You can find the full text of John's speech on our website at:

[http://www.fsa.gov.uk/pages/Library/Communication/Speeches/2007/0123\\_jt.shtml](http://www.fsa.gov.uk/pages/Library/Communication/Speeches/2007/0123_jt.shtml) .

Ed Balls detailed the government's strategy to fight money laundering. He was keen to hear firms' reactions to the government's efforts to fight

financial crime and Philip Robinson, as Chairman of the Conference, welcomed his engagement with the audience. Later in the morning Bill Hughes summarised SOCA's achievements so far. Speaking in the afternoon, Commissioner Mike Bowron gave a detailed police perspective on the Fraud Review. He welcomed the increase in resources to tackle crime recommended by the Fraud Review and highlighted the vital role the industry has to play in police investigations, through information sharing.

Sir James Crosby and Professor Michael Levi both addressed fundamental questions in the fight against financial crime. Sir James Crosby, Chair of the Public-Private Forum on Identity Management, focused on the topic of the consumer's identity and how to best protect it, while Professor Levi tackled the thorny issue of measuring the size of fraud. Two separate panel sessions were held to discuss, with the audience, money-laundering and terrorist-financing issues, followed by fraud issues. We would like to thank all the speakers and panellists for their valuable and insightful contributions.

Philip Robinson closed the Conference, and re-stated the importance of implementing a successful risk-based approach. He called for the senior management of firms to engage with driving it forward. Referring to the results of our financial crime Perception Survey, Philip Robinson noted: 'I am glad to say that the industry's perception of our work on financial crime has improved over the past two years'. He concluded by emphasising the need to continue pro-actively working together in the fight against financial crime: '...the financial crime problem is growing, not declining. So we all have to raise the bar. The FSA expects to do more over the coming year, with the new Financial Crime and Intelligence Division brigading financial crime expertise. And we will share what we learn going forward.'

Philip's full speech can be found on the FSA website at:

[http://www.fsa.gov.uk/pages/Library/Communication/Speeches/2007/0122\\_pr.shtml](http://www.fsa.gov.uk/pages/Library/Communication/Speeches/2007/0122_pr.shtml) .

If you attended our conference, we would like to thank you for your very useful feedback and continued support and interest. If you have any questions about this Conference or any further similar events, please contact Claire Tatchley on 020 7066 3498.

## • The Supervision of new businesses by the FSA under the Third Money Laundering Directive

The 2007 Money Laundering Regulations, which were published in draft form on 22 January, will be laid before Parliament this summer. These regulations implement the requirements of the EU's Third Money Laundering Directive into UK law. Importantly, from 15 December 2007, many businesses, from casinos to estate agents, will have their anti-money laundering controls monitored by one of over a dozen supervisory authorities for the first time. The government has given us responsibility for supervising 'Annex I financial institutions' (so named because they are listed in Annex I of the Banking Consolidation Directive). In practice, this will mean we will supervise otherwise unregulated businesses carrying out the following activities for anti-money laundering and counter-terrorist financing purposes from 15 December:

- lending;
- financial leasing;
- safe custody services;
- issuing and administering means of payment (e.g. credit cards, travellers' cheques and bankers' drafts);
- offering guarantees and commitments;
- participation in securities issues and providing services related to such issues (this will include registrars); and
- advice to undertakings on capital structure, industrial strategy and related questions and advice as well as services relating to mergers and the purchase of undertakings.

These businesses will need to register with us; registration will be the first step that will allow us to be effective in supervising these businesses. Our approach to supervision under the Money Laundering Regulations will be risk based and proportionate, and we will be giving you more about the detail of our plans over the coming months. A point to note is that firms that we authorise under the Financial Services and Markets Act 2000 will not need to register under the Money Laundering Regulations. If, however, a business is an Appointed Representative of an

authorised firm, and undertakes an Annex 1 activity, it will have to register with us.

If you wish to discuss any of the issues in this article please contact Greg Southall on 020 7066 8512 or Jody Ketteringham on 020 7066 3490 in our Financial Crime and Intelligence Division.

## • Our work on Politically Exposed Persons (PEP) and the implications for the industry

Politically Exposed Persons (PEPs) are individuals whose prominent position in public life gives them opportunities for profiting from corruption. As a result, the money-laundering risk associated with PEP customers is greater than for many other types of client.

Corruption is, of course, not exclusive to PEPs, nor is every PEP corrupt. But the risk is clear, and international organisations like the Financial Action Task Force (FATF) have, for some time, demanded that firms put procedures in place to guard against the risks associated with politically exposed customers.

Domestically, the Joint Money Laundering Steering Group (JMLSG) has, since 2003, issued good practice guidance to firms on how to deal with PEP customers. These provisions will be codified when the new Money Laundering Regulations come into force in December 2007. The Money Laundering Regulations will implement the Third EU Money Laundering Directive, and will, for the first time, provide a legal definition of PEPs in the UK. They will also require firms to have risk-based procedures in place to identify foreign PEP customers, and to apply enhanced customer due diligence (CDD) measures to these customers on a risk-sensitive basis. The Treasury are currently finalising the Regulations and plan to put them before Parliament by the summer.

## Defining PEPs

The draft Money Laundering Regulations define a PEP as 'an individual who is or has, at any time in the preceding year, been entrusted with prominent public functions'. The definition extends to the post-holder's immediate family members and known close associates.

The definition is complemented by a list of PEP categories. These categories provide an aid to the interpretation of the PEPs definition, but are not exclusive: firms will have to decide whether to include additional categories of PEPs on a risk-sensitive basis. For example, it may be appropriate to apply the same enhanced due diligence measures to customers who hold political functions at a sub-national level, but whose political exposure is comparable to that of similar positions at the national level.

The flexibility of the definition is deliberate, and foreseen by the Directive and its implementing measures. A closed list of PEPs would be both counterproductive, and against the principles of the risk-based approach.

Individuals are caught by the PEP definition for one year after leaving public office only. Certain categories – domestic holders of prominent positions, and junior and middle-ranking officials – are also excluded from the definition. However, in the light of a general obligation to apply enhanced customer due diligence measures to situations that present a higher money laundering risk, firms will have to take an informed, risk-based decision on how to treat those customers. For example, it may be appropriate to continue applying enhanced due diligence measures to former PEPs, in particular where the money-laundering risk was high.

## Mitigating the risk

Not all PEPs present the same level of risk, and not all PEPs will require higher risk products and services. So the draft Regulations allow firms to determine the extent to which they apply enhanced customer due diligence measures to PEP customers on a risk-sensitive basis.

In particular, when dealing with a PEP customer, the Regulations require firms on a risk-sensitive basis to:

- obtain appropriate senior management approval for establishing a business relationship with a PEP customer;
- take adequate measures to establish the source of wealth and source of funds which are involved in the business relationship or occasional transaction; and

- conduct enhanced ongoing monitoring of the business relationship.

Applying these measures is not optional – it will be a legal requirement.

## Identifying PEPs

The draft Money Laundering Regulations require firms to ‘have appropriate risk-based procedures to determine whether the customer is a politically exposed person’. This means firms should consider where their PEPs and money laundering risks are greatest and focus their resources accordingly. It does not mean treating every customer as a potential PEP or denying honest PEPs access to financial services.

As a result, identifying a PEP should usually come from a firm’s normal customer due diligence and know your customer (KYC) procedures. In line with the JMLSG Guidance, these should be appropriate to the level of risk associated with the customer, product or service. Where a firm in the course of its normal KYC and CDD measures identifies factors that prompt a more detailed investigation into the customer’s background, it will be able to rely on a number of resources to establish whether the customer is a PEP. These may range from asking additional questions and undertaking a simple internet search to subscription to commercially available databases where the firm has a high level of PEP exposure.

In all cases, firms will need to know how to proceed should a PEP be identified.

The obligation to identify PEPs on a risk-sensitive basis is not an obligation to identify every PEP in a firm’s database, but to identify those who pose a real money-laundering risk and to take measures to mitigate this risk effectively.

We recognise that firms may fail to identify a customer as falling within one of the PEP categories. But unless firms have persistently or significantly failed to implement appropriate systems and controls in relation to PEPs, enforcement action is unlikely.

For many firms, the main change is therefore likely to come from translating current good practice – set out in the JMLSG Guidance 2006 – into a legal requirement. As a consequence, those firms currently

following the guidance may not experience major changes to the way they conduct their business once the Regulations come into force. Others should use the opportunity to consider now how they will meet the PEPs requirement once the Money Laundering Regulations 2007 come into force.

For more information on the PEP issue, please contact Carolin Gardner on 020 7066 7332.

### • **The progress of our reporting systems for mortgage intermediaries**

In April 2006 we launched a reporting system to allow us to use mortgage lenders' information to help us deal with mortgage intermediaries involved in fraudulent activity. Lenders will usually remove intermediaries from their panel if they suspect they are committing fraud. However, the information we previously received from lenders when they removed an intermediary from their panel for this reason came from a limited number of lenders. And there was no consistency in the way lenders supplied this information, which limited the way we could deal with it.

The Information from Lenders project, operated by our Small Firms Division (SFD), was designed to:

- gain buy-in from lenders across the market place to supply intelligence and agree clear guidelines on what information should be reported; and
- develop an effective supervision strategy to deal with cases of fraud.

In setting up the project, we worked closely with the Council of Mortgage Lenders (CML) and a number of lenders to agree the criteria for supplying information and develop a communication strategy to involve other lenders across the market place.

It is worth noting the progress and success of this initiative requires firms' full engagement, since we ask them to voluntarily report cases of proven or suspected mortgage fraud where there is strong suspicion of intermediary involvement.

Guidelines and other details of this project were published in April 2006 and can be found on our website at [http://www.fsa.gov.uk/pages/Doing/Regulated/supervise/mortgage\\_fraud.shtml](http://www.fsa.gov.uk/pages/Doing/Regulated/supervise/mortgage_fraud.shtml) and CML's website (<http://www.cml.org.uk/cml/policy/issues/1164>).

Since its launch, the Information from Lenders project has proved to be a valuable source of intelligence:

- It has led to us taking a range of supervisory action against firms, including referrals to our Enforcement division.
- Up to February 2007, we received almost 150 referrals, around a quarter of which have been referred to Enforcement.
- In 2006, as a result of our enforcement action, and after having identified serious misconduct, we successfully cancelled an individual's permission to carry out regulated activities. We also prohibited another individual from carrying out any functions related to regulated activities.

Although the work has been successful in reducing fraud, not all lenders are taking part and we believe fuller participation from lenders is needed to bring consistent benefits across the mortgage industry, as well as to the financial services industry more generally. We will be looking at why there is a reluctance to participate and how this can be addressed. It is only by working together that we can continue to reduce fraud and raise standards for all mortgage firms.

Reports from lenders should be clearly marked 'Information From Lender – Mortgage Intelligence' and sent to our Firm Contact Centre at [fcc@fsa.gov.uk](mailto:fcc@fsa.gov.uk). If regulated firms have any queries about the new system they should contact Simon Compton or Dominic Clark on 020 7066 1000.

### • **The launch of our Insurance Reporting System**

Following on from the success of the Information for Lenders Project, we launched, in March 2007, a streamlined system for reporting financial crime in the insurance industry. Under the new system, insurance firms and intermediaries are being called on to tell us when they suspect criminal behaviour may be taking place, so we can decide whether to investigate further. This may arise when an insurer terminates an agency agreement with an intermediary where they see doubtful practice or suspect misconduct. It may also arise where an insurance intermediary has concerns about another intermediary they do business with.

Examples of possible financial crime involving insurance fraud include:

- misappropriation of client money or money held under risk transfer agreements;
- failure to pass on premiums, refunds or claims;
- falsifying customer details to obtain insurance business that would otherwise be turned down or be more expensive; and
- issuing false cover notes or false certificates of insurance.

Firm behaviours of this kind have led us to take action against a number of insurance intermediaries. The streamlined reporting system will enable us to target our investigations more efficiently, and where appropriate, take action more quickly against firms which engage in financial crime. We would like to thank the Association of British Insurers (ABI) and the British Insurance Brokers' Association (BIBA) for working with us in shaping the scheme, and for their active support to this initiative.

It is important to note this is a voluntary initiative, so we need the insurance industry to work with us to turn this project into a useful and successful initiative in the fight against financial crime. We are interested in both proven and suspected criminal or fraudulent actions on the part of insurance intermediaries, where the insurer considers the matter serious enough to revoke the agency of the intermediary or a subsequent investigation identifies fraud.

#### **Who to contact for further information**

Information should be clearly marked 'Information From Insurance Firms and Intermediaries – Insurance Intelligence' and sent to our Firm Contact Centre ([fcc@fsa.gov.uk](mailto:fcc@fsa.gov.uk)). If regulated firms have any queries about any of the above please contact Patrick Mulligan, Philip Hays-Nowak or Jackie Chapman on 020 7066 1000.

#### **• Our Financial Crime 'Perception' Survey**

On 27 March we published our first perception survey on how firms see our work on financial crime. We ran this survey to benchmark and track perceived increases or decreases in financial crime and the performance of both ourselves and the industry in tackling it.

The survey showed the general perception of our work on financial crime was positive. It also provided valuable insights into the way in which different types of firms view our performance. Small firms had different views to large firms, particularly with reference to the amount of guidance they would like to receive from us about our expectations in the financial crime area.

When firms and other stakeholders were asked about combating financial crime, generally we compared favourably to government and law enforcement bodies but less well when compared with trade associations. However, an issue we are seeking to address is that firms still find it difficult to share information with us, for fear of supervisory or enforcement action.

We are using the results of the survey to inform the forward work programme of the Financial Crime and Intelligence Division.

The survey can be found on our website at: <http://www.fsa.gov.uk/pubs/consumer-research/crpr58.pdf>

- **Our work on consumer awareness: raising awareness to protect consumers and help us detect fraudulent activities**

#### **Bogus FSA communications – be aware**

We are aware of a number of bogus communications claiming to be from us – and particularly a new recent bogus communication claiming to be from John Tiner, our CEO – which ask the recipient for personal information or money. These bogus communications are often in the form of emails or letters and they sometimes use the name of a current or former employee. They are likely to be linked to organised fraud and we strongly advise that you do not respond to them in any way. We will not ask firms or individuals to pay for their fees via email – we send an invoice with a written letter, and we do not process any payments online. If you are in any doubt about the authenticity of a communication from the FSA, whether that is a letter, email or other form, please contact us by email at: [financial.crime@fsa.gov.uk](mailto:financial.crime@fsa.gov.uk).

## Unauthorised and fraudulent activity

We also maintain a list of unauthorised firms that are currently targeting UK investors. These firms and/or individuals are not approved or authorised by us to conduct regulated activities. Please use the link below to view alerts we have issued. Not all fundraising activities require authorisation or approval by us. However, investors who have given money to, or are considering giving money to, these firms or individuals, should exercise caution as they will not benefit from the UK compensation and complaint schemes if anything goes wrong.

<http://www.fsa.gov.uk/Pages/Doing/Regulated/Law/Alerts/index.shtml>

For more information, please contact:

- our Firms' Contact Centre (If you are an authorised firm in the UK) – 0845 606 9966 (call rates may vary); or
- our Consumer Contact Centre (If you are a member of the public in the UK) – 0845 606 1234 (call rates may vary).

## Consumer Information webpages on Financial Crime risks

We are committed to better equipping consumers to protect themselves from financial crime. Our consumer information webpages were designed to raise consumers' awareness on financial crime issues such as scams and swindles, and tell them how to protect themselves against becoming a victim of financial crime. We explain in these pages the threats of identity fraud, advance fee scams, share scams (boiler rooms), affinity fraud (investment scam targeting members of a given group, within a particular community, professional or religious group for instance), chain letters, fund transfer scams and online fraud (phishing). We aim to work in partnership with other stakeholders on financial crime issues while avoiding duplicating the work we do on similar topics. So, you will find links to our partners in the fight against financial crime such as the Office of Fair Trading (and their campaign to stamp out scams), the Home Office (and their Home Office Identity Leaflet) and the Information Commissioner's Office.

Please visit the pages at:

[http://www.moneymadeclear.fsa.gov.uk/news/stay\\_safe.html](http://www.moneymadeclear.fsa.gov.uk/news/stay_safe.html)

## • The Launch of the FSA Financial Crime Website

In December 2006 we launched the new FSA Financial Crime web pages. These pages have been jointly developed by the Financial Crime Sector Team, Financial Crime Policy Unit and Market Conduct teams.

The new pages bring together existing information on fraud, money laundering and market abuse previously found on different sections of the FSA website. They also hold material on the new anti-money laundering regime, including the risk-based approach to anti-money laundering and a financial crime library. We anticipate that the new Financial Crime web pages will be an invaluable resource for our staff, firms and consumers alike.

Please see the new pages at:

[http://www.fsa.gov.uk/Pages/About/What/financial\\_crime/index.shtml](http://www.fsa.gov.uk/Pages/About/What/financial_crime/index.shtml)

## • Passport Validation Service – Changes to Pricing Structure

Our last edition of this newsletter contained an article about the Identity and Passport Service's (IPS) Passport Validation Service, which help users conduct more effective ID checks. The IPS has recently revised its pricing model to make it more attractive to organisations who would probably carry out smaller volumes of passport validation requests, such as financial advisers. This consists of an initial set-up fee of £750 which includes 200 passport validation checks, to be used within two months of the live date; after that there is an ongoing charge of £2.50 per query.

For more information, please contact Robert Kearney at [pvs@ips.gsi.gov.uk](mailto:pvs@ips.gsi.gov.uk).

## Milestones in 2006-2007

As we mentioned in our last Newsletter, there has been/will be some significant changes to the law on anti-money laundering during 2007, as a result of initiatives by the European Commission. In the build-up to this, there will be some important milestones, which we have set out below.

Date	Milestone
June 2007	FATF UK Mutual Evaluation Final Report
Summer 2007	2007 Money Laundering Regulations laid before Parliament
15 December 2007	Date by which the UK must implementation the requirements of the Third Money Laundering Directive.

### Contact details

As ever, we welcome feedback on our newsletter, ideas for future issues and suggestions of how we might make the newsletter more useful for you.

If you would like to receive this newsletter in future or have any comments on its content or format please contact us by email at: [financial.crime@fsa.gov.uk](mailto:financial.crime@fsa.gov.uk).

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