

# The Law Commission: Anti-Money Laundering and Counter-Terrorism Financing—Reform of the Suspicious Activity Reporting Regimes

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*In July 2018 the Law Commission published a Consultation Paper on proposed reforms to the United Kingdom (UK) suspicious activity reporting (SARs) regimes relating to Anti-Money Laundering (AML) and Counter-Terrorism Financing (CTF). This article argues that, notwithstanding the proposed retention of an “all-crimes” approach to AML, the SARs regime may still be streamlined by way of the proposed amendments to the scope of reporting. The proposals to elevate the thresholds for reporting suspicions of money laundering, whilst conceptually appealing, present operational challenges for those within the reporting sectors.*

## Introduction

Money laundering, where criminal proceeds are processed “to disguise their illegal origin”, and terrorism financing are both issues which have dominated the international agenda in recent decades.<sup>1</sup> That this should be the case is unsurprising given the sheer economic scale attributed to the former (2.7 per cent of global GDP) and the devastating human cost occasioned by the latter.<sup>2</sup> In the UK alone, the National Crime Agency (NCA) note there is a “realistic possibility” that annual money laundering impacting on the UK could be “hundreds of billions” of pounds.<sup>3</sup> The transnational response has been spearheaded by the Financial Action Task Force (FATF) which acts as the global anti-money laundering (AML) and counter-terrorism finance (CTF) standard setter. Evolving recommendations issued by FATF over the years have cascaded down via a series of EU Directives and converged to form a comprehensive AML and CTF framework at a national UK level.<sup>4</sup> That national framework is subject to the peer review process conducted

\* Many thanks to Professor Nicholas Ryder.

<sup>1</sup> FATF, “Frequently Asked Questions: Money Laundering” (FATF), <http://www.fatf-gafi.org/pages/faq/moneylaundering> [Accessed 20 July 2018].

<sup>2</sup> The amount of money available for laundering via the financial system is estimated by UNODC to be 2.7 per cent of global GDP or US\$1.6 trillion; see UNODC, *Estimating Illicit Financial Flows Resulting From Drug Trafficking and Other Transnational Organized Crimes* (UNODC, 2011), p.7.

<sup>3</sup> NCA, *Annual Plan 2018-9* (NCA), p.6.

<sup>4</sup> FATF, *International Standards on Combating Money Laundering and The Financing of Terrorism & Proliferation - The FATF Recommendations* (FATF, 2012, updated February 2018); Council Directive 2015/849 on the prevention

by FATF known as mutual evaluation, the latest results of which are due to be published at the end of 2018/early 2019.

AML and CTF measures have long been characterised conceptually as falling into two categories: prevention and enforcement.<sup>5</sup> The obligation to report suspicions of money laundering or terrorism financing (known as suspicious activity reports or SARs) is a key aspect of the prevention “pillar” on which the AML/CTF framework rests.<sup>6</sup> Such reports may well provide the evidential basis underpinning or enhancing AML/CTF investigations and asset confiscations. Any such framework must therefore take into account a trinity of interests of: (i) those making SARs, (ii) law enforcement agencies, and (iii) those in respect of whom SARs are made. Any comprehensive AML/CTF framework must also look to meaningful enforcement of that regime.

In the UK, the NCA report a continuing upward trajectory in the number of SARs submitted (634,113 from October 2015–March 2017), a volume of reporting which dwarfs levels seen in jurisdictions which the Commission puts forward as comparators in terms of the size of their financial sectors (Switzerland—2,909 SARs in 2016) or economy (France—64,815 reports in 2016).<sup>7</sup> Whilst such “headline” figures may be broadly illustrative, they must also be treated with some caution—for example FATF’s evaluation of Switzerland’s AML/CTF measures in 2016 reported that “insufficient” reports were being made.<sup>8</sup>

Whilst the intelligence potential and capacity to disrupt criminality is incalculable, the abundance of UK SARs does not track through to a plentiful harvest in terms of asset recovery.<sup>9</sup> What it does do, however, is result in considerable resources being deployed both by those making reports, and for the NCA who receive and analyse them. Hence an enduring disquiet has arisen amongst the reporting community that the regime, despite what Ryder calls its “laudable aims”, is hampered by a number of issues ranging in scale and scope which affect its efficiency and proportionality.<sup>10</sup> Practical issues include the high volume of SARs, some of which are submitted defensively to avoid criminal liability, and many of which are of little intelligence value and/or are of poor quality.<sup>11</sup> A cocktail of legal factors also intermingle to impact negatively upon the operation of the regime, namely: (i) an “all-crimes” approach to AML with no de minimis, (ii) the low threshold of “suspicion” which triggers reporting under the regimes, and (iii)

of the use of the financial system for the purposes of money laundering or terrorist financing, amending Regulation 648/2012 and repealing Directive 2005/60 and Commission Directive 2006/70 [2015] OJ L141/73 (4AMLD). 4AMLD is transposed into national law by way of the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (SI 2017/692). See also Criminal Finances Act 2017 for additional AML measures.

<sup>5</sup> M. Levi and P. Reuter, “Money Laundering” (2006) 34 Crime & Just. 289, 297.

<sup>6</sup> Other prevention measures include customer due diligence, regulation/supervision and administrative/regulatory sanctions: see Levi and Reuter, “Money Laundering” (2006) 34 Crime & Just. 289, 297.

<sup>7</sup> NCA, *Suspicious Activity Reports (SARs) Annual Report 2017* (NCA), figs iii–iv, p.7; fig.i, p.6. The total number of SARs lodged in 2016 in Switzerland was 2,909, MROS, *Annual Report 2017* (MROS, 2018), p.9. In France, the figure for 2016 was 64,815, Tracfin, *Tracfin Annual Report 2016*, (Tracfin), p.8.

<sup>8</sup> FATF, *Anti-money laundering and counter-terrorist financing measures Switzerland Mutual Evaluation Report December 2016* (FATF, 2016), p.4.

<sup>9</sup> Restrained sums and cash seizures arising from refused DAML requests between October 2015 and March 2017 total £35,893,941 and £16,183,553 respectively. HMRC indemnified £51,039 and recovered £1,784,845. NCA, *Suspicious Activity Reports (SARs) Annual Report 2017* (NCA), fig.v, p.8.

<sup>10</sup> N. Ryder, *Financial Crime in the 21st Century*, (Edward Elgar, 2011), p.30.

<sup>11</sup> Law Commission, *Anti-Money Laundering: the SARs Regime Consultation Paper* (OGL, 2018), Law Com. No.236, para.1.29.

the individual criminal sanctions surrounding the regime, a feature which Campbell notes fosters “over-recording and over-reporting”.<sup>12</sup>

The “repeated criticism” of the SARs regime is evident from the UK’s first National Risk Assessment in 2015, which fed into proposals for SARs reform in the Government’s AML Action Plan in 2016 where it was acknowledged that “radical changes” to the regime were required.<sup>13</sup> The Law Commission review complements the joint NCA/Home Office SARs Reform Programme and broader Treasury Committee Economic Crime inquiry into AML.<sup>14</sup> It considers the issues with, and potential reform of, the suspicious activity reporting regimes (and in particular the consent regime detailed below), with the overarching purpose of improving the UK’s “prevention, detection and prosecution” of money laundering and terrorism financing.<sup>15</sup> This is a particularly challenging task given that the Commission is constrained from the outset by a number of factors, namely the boundaries of pre-existing legislative structures, the requirements of EU directives pre-Brexit, and the recommendations of FATF.<sup>16</sup>

The position surrounding Brexit is nuanced. Whilst the UK will no longer be subject to EU AML directives post-Brexit, continued harmonisation with EU measures is assumed by the Commission.<sup>17</sup> In any event, the UK will remain a member of FATF and therefore seek to comply with the FATF Recommendations which themselves sit behind and drive the EU framework. Even within these parameters, there is scope for the UK to alter its AML offering, as will be seen in the remainder of this article, given that the starting point for the UK is that it has gone further than the FATF or EU requirements to date.

This article sets out briefly the mechanics of the reporting regimes under review. Thereafter the article focusses upon two key aspects of the SARs regime explored by the Consultation Paper: (i) the “all-crimes”/“serious crimes” approach to AML, and (ii) the proposals with regard to the current suspicion thresholds across the regimes. Whilst the Consultation Paper explores additional aspects of the regime, such as enhanced information sharing and corporate criminal liability, these topics are outside the scope of this article.

## **Anti-Money Laundering Reporting Regime—Proceeds of Crime Act (POCA) 2002 Pt 7**

The suspicious activity reporting regime (SARs Regime) in an AML context refers to the “end-to-end system by which industry spots suspicious activity related to money laundering ... and reports this” to the UK’s financial intelligence unit (FIU)

<sup>12</sup> Law Commission, *Anti-Money Laundering: the SARs Regime Consultation Paper*, para.4.16. The Consultation Paper also highlights confusion by reporters with regard to their obligations, and uncertainties surrounding the concept of “suspicion” as drivers behind high reporting volumes; L. Campbell, “Dirty cash (money talks): 4AML and the Money Laundering Regulations 2017” [2018] Crim.L.R. 102, 107.

<sup>13</sup> HM Treasury and Home Office, *UK national risk assessment of money laundering and terrorist financing* (HM Treasury and Home Office, 2015), p.6; Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* (HM Treasury and Home Office, 2016), pp.12–15 and Annex B.

<sup>14</sup> NCA, *Suspicious Activity Reports (SARs) Annual Report 2017*, p.30; UK Parliament, “Treasury Committee Economic Crime inquiry” (UK Parliament, 2018), <https://www.parliament.uk/business/committees/committees-a-z/commons-select/treasury-committee/inquiries/parliament-2017/economic-crime-17-19/> [Accessed 23 August 2018].

<sup>15</sup> Law Commission, *Anti-Money Laundering: the SARs Regime Consultation Paper*, para.1.28.

<sup>16</sup> See Sanctions and Anti-Money Laundering Act 2018 which makes provision “for the purposes of implementing Standards published by the Financial Action Task Force”.

<sup>17</sup> Law Commission, *Anti-Money Laundering: the SARs Regime Consultation Paper*, para.1.8(3).

within the NCA.<sup>18</sup> Upon submission, SARs are added to the NCA database, mined for useful intelligence, and disseminated to law enforcement agencies (LEAs) to assist with money laundering investigations.<sup>19</sup> The regime is comprised of two complementary but distinct strands—“authorised disclosures” and “required disclosures”.

Under the first strand, should a person deal or propose to deal in some manner with criminal property, which is criminalised under the substantive money laundering offences set out in POCA 2002 ss.327–329, a SAR may be made by way of “authorised disclosure” under POCA 2002 s.338.<sup>20</sup> This situation may arise, for example, where a banker, accountant or lawyer encounters underlying criminal property as part of their customer services or client retainer. NCA consent (either actual consent or deemed consent) may then be obtained to continue with the transaction, depending on the timing of the SAR.<sup>21</sup> Such disclosure and consent provisions are known as the “consent regime”. Deemed consent will apply either on the expiry of the notice period of seven working days if no refusal has been received from the NCA, or, if a refusal has been received, on the expiry of the relevant moratorium period.<sup>22</sup> These time periods provide a transactional hiatus during which the NCA/law enforcement may determine what AML action to take. The Criminal Finances Act 2017 made a number of changes to the regime. It incorporated provisions into POCA 2002 whereby a court may order an extended moratorium period of up to a further 186 days.<sup>23</sup> It also inserted voluntary information sharing provisions which, when fully implemented, will permit disclosures between members of the regulated sector and joint disclosures (“Super SARs”) to the NCA.<sup>24</sup> Further information orders were also imported into the Act enabling the NCA to seek supplementary information from those reporting to it or businesses in the regulated sector.<sup>25</sup>

Such authorised disclosures (and any “appropriate consent”) act as a complete exemption from the substantive money laundering offences set out in ss.327–329 of the Act.<sup>26</sup> The rationale behind the consent regime therefore is that it provides potentially useful intelligence, and the opportunity for intervention, whilst simultaneously shielding reporters from criminal liability for a substantive money laundering offence.<sup>27</sup> Keen to avoid any perception that the NCA are, in effect, legitimising illicit funds by providing consent to a transaction, such disclosures were rebranded by the NCA as DAML SARs (defence against money laundering) in June 2016.<sup>28</sup>

<sup>18</sup> NCA, “The SARs Regime” (NCA), <http://www.nationalcrimeagency.gov.uk/about-us/what-we-do/economic-crime/ukfiu/the-sars-regime> [Accessed 23 August 2018].

<sup>19</sup> NCA, “The SARs Regime” (NCA), <http://www.nationalcrimeagency.gov.uk/about-us/what-we-do/economic-crime/ukfiu/the-sars-regime> [Accessed 23 August 2018].

<sup>20</sup> Authorised disclosures are made to a constable, customs officer or nominated officer under POCA 2002 s.338(1)(a).

<sup>21</sup> For actual and deemed appropriate consent provisions see POCA 2002 ss.335 and 336.

<sup>22</sup> See POCA 2002 s.335(2)–(7) and s.336(3)–(9). Deemed consent will apply where no refusal has been received before the end of the notice period of seven working days (starting from the first working day post disclosure). Deemed consent provisions also apply where a refusal has been received within the notice period and the moratorium period expires. The initial moratorium period is 31 days commencing on the date refusal is received.

<sup>23</sup> POCA 2002 ss.335(6A), 336(8A), 336A–336D. Inserted by Criminal Finances Act 2017 s.10.

<sup>24</sup> POCA 2002 ss.339ZB–339ZG inserted by Criminal Finances Act 2017 s.11.

<sup>25</sup> See POCA 2002 s.339ZH inserted by Criminal Finances Act 2017 s.12.

<sup>26</sup> POCA 2002 ss.327(2)(a), 328(2)(a) and 329(2)(a).

<sup>27</sup> Home Office, *Home Office Circular 029/2008* (2008), para.4.

<sup>28</sup> NCA, *Requesting a defence from the NCA under POCA and TACT* (NCA, 2016).

The second strand of the reporting regime, backed by criminal sanctions, provides for “required disclosures”.<sup>29</sup> The “failure to disclose” offence set out in POCA 2002 s.330 requires those in the regulated sector (such as bankers, lawyers or accountants) to report their knowledge or suspicions of money laundering activity by another to their nominated officer (the Money Laundering Reporting Officer) or the NCA.<sup>30</sup> The information on which the report is based must come to the person in the course of business, and must be made to the MLRO “as soon as is practicable”.<sup>31</sup> An objective standard also applies in this section, imposing a requirement to report where there are “reasonable grounds for knowing or suspecting” someone is money laundering.<sup>32</sup> Comparable provisions applicable to the MLRO in receipt of an internal SAR are set out in s.331.<sup>33</sup> The objective negligence based threshold in s.330/331 has been justified on the basis that higher standards of AML diligence are expected within the regulated sector.<sup>34</sup> Simultaneously however, Goldby contends that the objective test constitutes “a stick to threaten those who may be inclined not to take their legal obligation to report sufficiently seriously”.<sup>35</sup>

“Tipping Off” provisions also apply under the regime. An offence is committed if a person reveals the fact that a SAR has been made (using information obtained in the course of a business in the regulated sector), and such action is “likely to prejudice any investigation that might be conducted following the disclosure”.<sup>36</sup> An offence is also committed if a person reveals that an investigation into allegations that a money laundering offence has been committed is being “contemplated or is being carried out”, if that revelation is also “likely to prejudice that investigation”.<sup>37</sup>

## **Counter-Terrorism Financing Reporting Regime—Terrorism Act (TACT) 2000 Pt 3**

The UK AML regime operates in tandem with its CTF regime, despite the differing quantitative and qualitative indicia of terrorism. For example, terrorism financing may be characterised by different motivations other than concealing illicit funds or maximising profits, involve modest amounts, and constitute “reverse” laundering where clean funds are used to fund terrorist acts.<sup>38</sup> As with the AML regime, the CTF reporting regime encompasses both “prior consent” and “required” disclosures.

<sup>29</sup> See POCA 2002 s.334 for applicable criminal sanctions.

<sup>30</sup> POCA 2002 s.330(2)(a). For the regulated sector see POCA 2002 Sch.9.

<sup>31</sup> POCA 2002 s.330(3) and (4). Reporters must be able to identify the launderer or the location of the laundered property (or they believe, or it is reasonable to expect them to believe, that the information will or may assist in this regard), POCA 2002 s.330(3A).

<sup>32</sup> POCA 2002 s.330(2)(b).

<sup>33</sup> POCA 2002 s.332 creates a failure to disclose offence with regard to disclosures made to a nominated officer outside the regulated sector.

<sup>34</sup> Secretary of State, *Proceeds of Crime Bill Publication of Draft Clauses* (2001), Cm.5066, Pt VIII, para.8.6.

<sup>35</sup> M. Goldby, “Anti-money laundering reporting requirements imposed by English law: measuring effectiveness and gauging the need for reform” [2013] J.B.L. 367, 371.

<sup>36</sup> POCA 2002 s.333A(1) and (2). On summary conviction the maximum prison term is three months and/or a fine. In the Crown Court, the maximum penalty for tipping off is two years’ imprisonment and/or a fine, POCA 2002 s.333A(4).

<sup>37</sup> POCA 2002 s.333A(3).

<sup>38</sup> For comments on reverse laundering see S.D. Cassella, “Reverse Money Laundering” (2003) 7(1) J.M.L.C. 92; see also P. Sproat, “Counter-Terrorist Finance in the UK: a Quantitative and Qualitative Commentary based on Open-source Materials” (2010) 13(4) J.M.L.C. 315.

A person may gain exemption from the terrorism financing offences set out in TACT 2000 ss.15-18 via the prior consent route. Prior to becoming involved in a transaction or arrangement, reporters disclose to the NCA (who consult with the National Terrorism Financial Intelligence Unit (NTFIU)) their suspicion or belief that terrorist property is involved and receive actual or deemed consent to proceed (such disclosure known as a “Defence Against Terrorism Financing SAR” or “DATF SAR”).<sup>39</sup> The same notice period applies to the deemed consent provisions as for POCA 2002—seven working days starting with the first working day post-SAR—but there is no moratorium period.<sup>40</sup> Similar failure to disclose and tipping off offences apply under this framework.<sup>41</sup> Whilst high volumes of reporting are not the issue in this arena, the NTFIU have also expressed concern over poor-quality SARs of little intelligence value.<sup>42</sup>

The preceding paragraphs set out the key features of the AML/CTF reporting regimes. It is against this legislative backdrop that the article considers one of the central aspects of the SARs regime explored by the Commission—the “all-crimes” approach to AML.

## The “All-Crimes” Approach in POCA 2002

One of the drivers behind the current turgidity of the SARs regime is the UK’s adoption of an “all-crimes” approach to AML. The substantive money laundering offences set out in POCA 2002 ss.327–329 criminalise dealings with “criminal property”, a definition widely cast to encompass property relating to *all* crimes.<sup>43</sup> Naturally this design feature of the regime has a consequential effect on the levels of both authorised and required disclosures. In adopting this policy the UK goes further than the FATF Recommendations, which envisage the criminalisation of money laundering relating to serious crimes (albeit “with a view to including the widest range of predicate offences”).<sup>44</sup> It also goes further than the requirements of 4AMLD, which restricts predicate offences to serious crimes identified both by way of a list of specified offences and in addition by reference to length of maximum sentence.<sup>45</sup>

The adoption of this “leave no stone unturned” approach has the advantage that front-line reporters such as bank staff are not required to make any assessment as to the seriousness or otherwise of any underlying offence.<sup>46</sup> This is of considerable assistance to those reporters outside of the legal sector such as banks, which constitute the largest reporting sector by far, submitting 82.85 per cent of SARs

<sup>39</sup> TACT 2000 ss.21ZA and 15–18.

<sup>40</sup> TACT 2000 s.21ZA(2)–(3).

<sup>41</sup> TACT 2000 s.21A; see also s.19; for tipping off provisions see TACT 2000 s.21(D)–(H).

<sup>42</sup> Law Commission, *Anti-Money Laundering: the SARs Regime Consultation Paper*, paras 3.33–3.35.

<sup>43</sup> POCA 2002 s.340(3) provides that “Property is criminal property if (a) it constitutes a person’s benefit from criminal conduct or it represents such a benefit (in whole or part and whether directly or indirectly), and (b) the alleged offender knows or suspects that it constitutes or represents such a benefit.” A deposit-taking institution may avail itself of a de minimis threshold of £250 (s.339A) pursuant to ss.327(2C), 328(5) and 329(2C).

<sup>44</sup> FATF, *International Standards on Combating Money Laundering and The Financing of Terrorism & Proliferation -The FATF Recommendations*, Recommendations 3 and 5.

<sup>45</sup> 4AMLD art.3(4).

<sup>46</sup> R. Stokes and A. Arora, “The duty to report under the money laundering legislation within the United Kingdom” [2004] J.B.L. 332, 355; See also Secretary of State for the Home Department, *Money Laundering and the Financing of Terrorism: the Government Reply to the nineteenth Report from the House of Lords European Union Committee Session 2008–09, HL Paper 132* (TSO, 2009), Cm.7718, pp.11–12.

between October 2015 and March 2017.<sup>47</sup> It also has the concomitant potential advantage of maximising the intelligence available to the authorities via disclosures made to it, and the concrete advantage that prosecutors are not required to identify specific predicate offences. Hence the Law Commission is of the view that moving to a “serious crimes” approach to AML is both “problematic and undesirable”.<sup>48</sup>

One of the disadvantages of the all-crimes approach, however, can be seen with regard to specific sectors, and this can be illustrated neatly by reference to the legal profession. Minor offences and regulatory breaches carrying criminal sanctions (which may be conceived of as “technical” breaches) may come to light in the course of a retainer. Such technical breaches, examples of which are the breach of a tree preservation order or failure to obtain an asbestos survey, will trigger reporting requirements, a process made more challenging by the requirement to identify any notional saving or benefit from the breach under the Act.<sup>49</sup> It is these “technical” reporting requirements, offering little by way of valuable intelligence, which may have a corrosive effect on confidence in and compliance with the regime for the legal sector.<sup>50</sup> Reporters in the banking sector, in contrast, would rarely, if ever, encounter such minor offences or regulatory breaches on the basis that their customer interaction is primarily focussed on the movement of funds.

Notwithstanding the Commission’s stance on the issue, consultees’ views are sought as to whether the UK should adopt a serious crimes approach to the money laundering offences, either by reference to a list of specified offences *or* those offences carrying maximum penalties of more than a year’s imprisonment.<sup>51</sup> Doubtless there are mechanical challenges to be overcome should this approach be adopted, such as formulating and updating the inclusion criteria in relation to any list of specified offences, and ensuring that any threshold penalty does not trade simplicity for arbitrariness.<sup>52</sup> These challenges are not insurmountable however, and it is worth noting at this juncture that 4AMLD combines *both* these approaches with regard to predicate crimes, an approach which has been adopted in other EU jurisdictions such as Germany, and which could provide an appropriate starting point for the UK.<sup>53</sup> Any move to a serious crimes approach would certainly streamline the SARs regime, but also presents additional operational challenges when making a SAR for reporters determining whether an offence is serious or not, and challenges for prosecutors if required to link particular proceeds to particular predicates.

The Commission is also consulting on other permutations spanning the all-crimes/serious crimes divide. An alternative option is the retention of an “all-crimes” approach to the substantive offences, the advantage of which is that it would maximise the options available to prosecutors, whilst utilising a serious crimes approach to disclosures. Again, the challenge here is for those reporters,

<sup>47</sup> NCA, *Suspicious Activity Reports (SARs) Annual Report 2017*, fig.xii, p.12.

<sup>48</sup> Law Commission, *Anti-Money Laundering: the SARs Regime Consultation Paper*, para.5.17.

<sup>49</sup> S. Kebbell, “‘Everybody’s looking at nothing’ – the legal profession and the disproportionate burden of the Proceeds of Crime Act 2002” [2017] *Crim. L.R.* 741.

<sup>50</sup> Kebbell, “‘Everybody’s looking at nothing’ – the legal profession and the disproportionate burden of the Proceeds of Crime Act 2002” [2017] *Crim. L.R.* 741, 752.

<sup>51</sup> Law Commission, *Anti-Money Laundering: the SARs Regime Consultation Paper*, para.5.9. For such a list see for example POCA 2002 Sch.2 and Serious Crime Act 2007 Sch.1.

<sup>52</sup> Law Commission, *Anti-Money Laundering: the SARs Regime Consultation Paper*, para.5.13.

<sup>53</sup> 4AMLD art.3(4).

particularly outside of the legal sector, required to make a determination as to the seriousness of any predicate crime.

One further option envisages the implementation of a voluntary pathway for the regulated sector to flag up non-serious matters to the NCA, whilst requiring disclosures in respect of serious offences. This option may be of benefit to legal sector reporters, certainly the adoption of a “tiered” reporting system was one of the embryonic options previously considered by the Law Society whereby reporters would simply “grade the importance of the SARs they submit”.<sup>54</sup>

### *The extension of a de minimis threshold?*

The all-crimes approach encompasses criminal property of *any value*, the effect of which is to generate SARs which are of no utility in terms of asset seizure, either because the sums involved are too inconsequential to pursue, or because they fall below the seizure threshold of £1,000 provided for in POCA 2002.<sup>55</sup> Incorporating a de minimis reporting threshold would automatically decrease the volume of such SARs and is therefore considered as part of the Commission’s review. This is already a familiar concept in POCA 2002 in that deposit-taking institutions may avail themselves of an exemption to the substantive offences in respect of the operation of customer accounts below a specified threshold.<sup>56</sup> Such a threshold would lead to fewer SARs being lodged, however the Commission is opposed to the insertion of a de minimis threshold across other parts of the regulated sector. Whilst any threshold carries with it the risk that offenders will simply structure around it, the most persuasive justification for this stance is that it may prompt a decline in terrorism-related intelligence given the small monetary amounts that may be involved in terrorism-related activities. Certainly from a reporter’s perspective there may be significant blurring between the AML and CTF regimes—some form of criminal activity may be suspected and an AML SAR submitted without necessarily making any conscious links with terrorism, with such “crossover” SARs providing useful CTF intelligence. An additional issue is that any de minimis threshold with regard to required disclosures would also conflict with the UK’s current obligations under art.33 of 4AMLD requiring reports to a member state’s FIU “regardless of the amount involved”.<sup>57</sup>

## **Amendments to the Scope of Reporting**

Retaining an “all crimes of any value” approach to reporting will, in the absence of further intervention, do nothing to assist with streamlining the SARs regime. So how to deal with those SARs which are recognised as “taking valuable resources to investigate”, but which are simultaneously of “little intelligence value”?<sup>58</sup> The Commission provisionally proposes that, in preference to the constraints inherent

<sup>54</sup> The Law Society, *Response of the Law Society of England and Wales to the consultation issued by the Home Office and HM Treasury on the Action Plan for anti-money laundering and counter-terrorist finance - legislative proposals* (The Law Society, June 2016), p.4.

<sup>55</sup> POCA 2002 s.294(3). Proceeds of Crime Act 2002 (Recovery of Cash in Summary Proceedings: Minimum Amount) Order 2006 (SI 2006/1699).

<sup>56</sup> POCA 2002 ss.327(2C), 328(5) and 329(2C). The current threshold is £250.

<sup>57</sup> See also Interpretive Note to Recommendation 20, FATF, *International Standards on Combating Money Laundering and The Financing of Terrorism & Proliferation - The FATF Recommendations*.

<sup>58</sup> Law Commission, *Anti-Money Laundering: the SARs Regime Consultation Paper*, para.11.1.



in legislative amendment, SARs of limited intelligence value could be excluded from the regime by way of the “reasonable excuse” exemption for non-disclosure which would be supported by evolving statutory guidance.<sup>59</sup> The “reasonable excuse” exemption is a provision of POCA 2002 as yet untested in the courts, and currently attracts differing interpretations across sector-specific guidance.<sup>60</sup>

The challenge of SARs reform is, according to Donald Toon (Director of Prosperity within the NCA), “how we lose that which has no value without throwing the baby out with the bathwater”.<sup>61</sup> Any reduction in the scope of the reporting regime must therefore balance a reduction in the number of SARs submitted whilst retaining those SARs which are of use.<sup>62</sup> To this end, the Consultation Paper incorporates a practical and pragmatic exploration of those SARs which could potentially be excluded following stakeholder consultation, a number of which are detailed below.

### *The banking sector—mixed funds in bank accounts*

One such proposal will assist banks in relation to the conundrum posed by mixed legitimate and illicit funds in a bank account. The issue of fungibility (money being substitutable) and legal precedent (*Causey, N v RBS*) result in a legal position where: (i) mixed funds in an account are indistinguishable and therefore unidentifiable, and (ii) the entire account is then tainted.<sup>63</sup> Many banks will therefore freeze entire accounts rather than ring-fence suspected criminal property (thus preserving the funds available for restraint), the consequences of which may be severe for the subjects of disclosures. The Commission therefore proposes amending ss.327–329 so that, using an approach which is more akin to that deployed in relation to mixed funds within the civil recovery provisions of POCA 2002, banks should be allowed to transfer the equivalent value of suspected funds into a separate account (or ring-fence suspected funds within an account) without committing a substantive money laundering offence, with the intelligence flow to the NCA being preserved by way of required disclosures. The challenge here for the banks is in actually being able to identify which funds are clean and which funds are illicit, a challenge exacerbated in respect of pooled client accounts. An additional proposal by the Commission, which will also assist the banking sector in streamlining their reporting, is by permitting a single SAR with regard to multiple transactions on the same account or linked accounts.<sup>64</sup>

<sup>59</sup> POCA 2002 ss.327(2)(b), 328(2)(b), 329(2)(b); Law Commission, *Anti-Money Laundering: the SARs Regime Consultation Paper*, Ch.11.

<sup>60</sup> For example, accountancy sector guidance takes an *in extremis* approach whilst the Legal Sector Affinity Group Guidance is slightly more expansive. CCAB, *Anti-Money Laundering Guidance For The Accountancy Sector* (CCAB, 2018), paras 2.2.2 and 6.1.19; Legal Sector Affinity Group, *Anti-Money Laundering Guidance for the Legal Sector* (LSAG, 2018), paras 6.5, 6.7.1.

<sup>61</sup> House of Commons, *Treasury Committee Oral evidence: Economic Crime* (HOC, 4 July 2018), HC940, Response to Q242.

<sup>62</sup> Effectiveness and proportionality have been consistent concerns for successive governments, see HM Treasury, *Anti-Money Laundering Strategy* (HMSO, 2004), para.1.9.

<sup>63</sup> *Causey*; unreported 18 October 1999 Court of Appeal (Criminal Division); *N v RBS* [2017] EWCA Civ 253; [2017] 1 W.L.R. 3938. Cf. *Smallman* [2010] EWCA Crim 548; [2010] All E.R. (D) 286 (Mar).

<sup>64</sup> Law Commission, *Anti-Money Laundering: the SARs Regime Consultation Paper*, paras 11.43–11.45. Repayments to victims in respect of fraud notified to Action Fraud from a bank account would also no longer require consent, see paras 11.47–11.49.

## *Further carve-outs from the scope of reporting*

The Commission presents a range of other scenarios to which the reasonable excuse exemption could be appropriately applied. These are designed to remove the necessity for a SAR where: (i) a transaction has no UK nexus, (ii) to avoid duplicate reporting to multiple LEAs, or (iii) where the only suspicion is attributable to enquiries from an LEA.<sup>65</sup> Defining the parameters is the challenge presented by those SARs relating to historical crime, or information in the public domain, and for that reason the Commission proposes a shortened form of SAR to apply to the latter. Further, the Commission proposes that only required disclosures should be necessary in respect of property purchases in the UK on the basis that such property is immovable.<sup>66</sup> Careful consideration must be given to this particular carve out however, on the basis that any property held by a corporate entity is liable to a disposition by way of share sale, in which case the transactional hiatus afforded by the consent regime may be extremely useful.

In summary, the Commission has engaged in a comprehensive review of those SARs which pose practical challenges across all reporting sectors. It is to be hoped that those minor offences and regulatory breaches which are of particular concern to legal sector reporters and of no interest to the NCA may also be dealt with using the reasonable excuse exemption. This on the basis that there are key distinctions to be drawn between all crimes, serious crimes and minor offences.

Having considered the options with regard to the all crimes/serious crimes approach to AML, and the potential SARs that may be brought outside of the scope of the reporting regime, this article now considers the “pivotal concept” of suspicion within POCA 2002, and the proposals made in respect of it.<sup>67</sup>

## **Suspicion**

The concept of suspicion is interlaced throughout POCA 2002, yet at the same time is a concept which “nimblely defies precise identification in practical terms”.<sup>68</sup> It has also nimblely eluded any definition within POCA 2002, TACT 2000, the FATF Recommendations or 4AMLD. The substantive money laundering offences criminalise dealings with criminal property where the alleged offender knows or suspects that this is the case, which is a lower threshold than the knowledge and intent requirements made explicit in 4AMLD and implicit within the FATF Recommendations.<sup>69</sup> In addition, ss.330/331 of the Act require disclosures where a person knows, suspects or has reasonable grounds to know or suspect that another is engaged in money laundering, provisions which are consonant with both 4AMLD and the FATF Recommendations.<sup>70</sup> Yet despite its pervasive nature within the

<sup>65</sup> Law Commission, *Anti-Money Laundering: the SARs Regime Consultation Paper*, Ch.11.

<sup>66</sup> Law Commission, *Anti-Money Laundering: the SARs Regime Consultation Paper*, paras 11.41–11.42.

<sup>67</sup> J. Fisher and J. Bewsey, “Laundering the Proceeds of Fiscal Crime” (2000) 15(1) J.I.B.L. 11, 16.

<sup>68</sup> Stokes and Arora, “The duty to report under the money laundering legislation within the United Kingdom” [2004] J.B.L. 332, 353.

<sup>69</sup> POCA 2002 ss.327–329; For the definition of criminal property see POCA 2002 s.340(3). See art.1.3 of 4AMLD; FATF, *International Standards on Combating Money Laundering and The Financing of Terrorism & Proliferation - The FATF Recommendations*, Interpretive Note to Recommendation 3.

<sup>70</sup> POCA 2002 ss.330(2) and 331(2). The mens rea element of s.332 is knowledge or suspicion. See also art.33 of 4AMLD and FATF, *International Standards on Combating Money Laundering and The Financing of Terrorism & Proliferation - The FATF Recommendations*, Recommendation 20.

reporting framework, the Commission notes that the concept remains “ill-defined, unclear and inconsistently applied”.<sup>71</sup>

The lodestar in terms of judicial guidance on the concept is set out by Longmore LJ in the Court of Appeal case of *Da Silva* which provides that “suspicion” is a purely subjective concept meaning “a possibility, which is more than fanciful, that the relevant facts exist. A vague feeling of unease would not suffice”.<sup>72</sup> In addition, Longmore LJ noted that there was no requirement within the statute for suspicion to be “clear” or “firmly grounded and targeted on specific facts”.<sup>73</sup> The Court of Appeal resisted strenuously the argument to include any “reasonable grounds” concept to “suspicion” when invited to do so by the appellant’s counsel, commenting that to do so “would be to make a material change in the statutory provision for which there is no warrant”.<sup>74</sup> Where appropriate, however, the jury should be directed that the suspicion should be of a “settled nature”.<sup>75</sup> Such a low threshold for reporting has resulted in high-volume/poor-quality SARs being submitted, and inconsistencies in both the application of the concept, and guidance in respect of it, across sectors.<sup>76</sup>

Defensive reporting has also become an intrinsic feature of the regime, understandably so, with a few hours spent submitting a SAR being infinitely preferable to the prospect of more than a few years’ incarceration for a substantive laundering or failure to disclose offence.<sup>77</sup> The failure to disclose offences under ss.330/331 are also broad in scope, perpetuating defensive reporting as a consequence.<sup>78</sup> The “reasonable grounds for suspecting” that another is laundering which will trigger a reporting obligation has been interpreted as an entirely objective test in the limited (albeit first instance) decisions within the jurisdiction.<sup>79</sup> Lord Hughes, in the Supreme Court decision *Sally Lane and John Letts*, also confirmed that this interpretation would be applied in respect of the failure to disclose offence in TACT 2000 s.21A.<sup>80</sup> Nor (on the limited authority available in *Ahmad v HM Advocate*) does it appear that there is any requirement that money laundering is actually taking place.<sup>81</sup>

### *Reporting thresholds for required disclosures*

In order to address the expansive scope of reporting created by the low reporting thresholds within POCA 2002, the Commission proposes amending the reporting

<sup>71</sup> Law Commission, *Anti-Money Laundering: the SARs Regime Consultation Paper*, para.4.16.

<sup>72</sup> *Da Silva* [2006] EWCA Crim 1654; [2006] 4 All E.R. 900; [2007] Crim. L.R. 77 at [16]. This case considered the provisions of s.93A(1)(a) of the Criminal Justice Act 1988, which preceded POCA 2002.

<sup>73</sup> *Da Silva* [2006] EWCA Crim 1654; [2006] 4 All E.R. 900; [2007] Crim. L.R. 77 at [16].

<sup>74</sup> *Da Silva* [2006] EWCA Crim 1654; [2006] 4 All E.R. 900; [2007] Crim. L.R. 77 at [8]. For further application of this test see *K Ltd v National Westminster Bank Plc* [2006] EWCA Civ 1039; [2007] 1 W.L.R. 311; *Shah v HSBC Private Bank (UK) Ltd* [2012] EWHC 1283 (QB); [2012] All E.R. (D) 155.

<sup>75</sup> *Da Silva* [2006] EWCA Crim 1654; [2006] 4 All E.R. 900; [2007] Crim. L.R. 77 at [17].

<sup>76</sup> Law Commission, *Anti-Money Laundering: the SARs Regime Consultation Paper*, paras 6.7, 7.18 and 7.29.

<sup>77</sup> POCA 2002 s.334(1). The penalty for a ss.327–329 offence on summary conviction is a maximum prison term of six months and/or a fine. In the Crown Court the maximum prison term is 14 years and/or a fine. Under s.334(2) the penalty for a failure to disclose offence on summary conviction is a maximum prison term of six months and/or a fine. In the Crown Court the maximum prison term is five years and/or a fine.

<sup>78</sup> Goldby, “Anti-money laundering reporting requirements imposed by English law: measuring effectiveness and gauging the need for reform” [2013] J.B.L. 367, 375.

<sup>79</sup> *Swan* [2011] EWCA Crim 2275; [2012] 1 Cr. App. R. (S) 542; *Griffiths* [2006] EWCA Crim 2155; [2007] 1 Cr. App. R. (S) 95.

<sup>80</sup> *Lane* [2018] UKSC 36; [2018] 1 W.L.R. 3647 at [22].

<sup>81</sup> *Ahmad v HM Advocate* [2009] HJAC 60; [2009] S.C.L. 1093.

threshold in ss. 330-1 (and also s.332) from suspicion to “reasonable grounds to suspect”. Rather than this constituting a purely objective test, as is currently the case under ss.330/331, it is proposed that a cumulative test will be deployed as interpreted by the House of Lords in *Saik* (although this approach is not guaranteed without statutory intervention).<sup>82</sup> This would require both subjective suspicion on the part of a reporter, supported by objective grounds for that suspicion, a test frequently deployed in investigative contexts.<sup>83</sup> It is suggested by the Commission that this revised threshold will foster a decline in defensive SARs of minimal intelligence value, particularly if supported by statutory guidance as proposed by the Commission and discussed below.<sup>84</sup> Whilst a raised threshold may be conceptually appealing with regard to the point at which criminal liability for reporters bites, the challenge here is an operational one—it adds in what the Commission acknowledges may be “a layer of unnecessary complexity” for reporters required to delineate reasonable grounds, albeit one which the Commission envisages would be mitigated with appropriate AML training and guidance.<sup>85</sup> A raised threshold also reduces the number of potential “crossover” SARs, i.e. those SARs submitted under POCA 2002 but which are of use in the CTF sphere.

Compliance with the FATF Recommendations is also an issue here, given that Recommendation 20 provides for SARs where 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”,

thus drawing a distinction between the two concepts.<sup>86</sup> The Commission points to the recent mutual evaluation of Canada in 2016, whose reporting threshold is set at “reasonable grounds to suspect” and note that, whilst assessed as partially compliant, no issue was explicitly raised by FATF with regard to this trigger point, which is a curious argument to raise for potential non-compliance.<sup>87</sup> Article 33(1)(a) of 4AMLD also requires SARs to be made where an obliged entity “knows, suspects or has reasonable grounds to suspect” money laundering or terrorist financing and so raising the threshold would be non-compliant with 4AMLD.

No adjustments are proposed with regard to the terrorism financing reporting thresholds on the basis that a low threshold is commensurate with the level of harm terrorism unleashes across society, and because the CTF regime has not resulted in the same reporting issues as those seen with AML SARs.<sup>88</sup> This does mean that reporters would be using a lower threshold within the CTF arena than for AML, and so the question arises as to what operational challenges this may present when operating two regimes with differing thresholds.

<sup>82</sup> *Saik* [2006] UKHL 18; [2006] 2 W.L.R. 993. In *Saik* the Lords considered the parameters of the wording “reasonable grounds to suspect” in relation to s.93C(2) Criminal Justice Act 1993 which preceded POCA 2002.

<sup>83</sup> See for example Police and Criminal Evidence Act 1984 s.24. Reasonable grounds to suspect that an offence has been committed are required before an arrest can be made.

<sup>84</sup> Law Commission, *Anti-Money Laundering: the SARs Regime Consultation Paper*, para.9.37.

<sup>85</sup> Law Commission, *Anti-Money Laundering: the SARs Regime Consultation Paper*, para.9.30.

<sup>86</sup> FATF, *International Standards on Combating Money Laundering and The Financing of Terrorism & Proliferation - The FATF Recommendations*, Recommendation 20.

<sup>87</sup> FATF, *Anti-money laundering and counter-terrorist financing measures: Canada Mutual Evaluation Report* (FATF, September 2016), p.157.

## *Thresholds within the substantive offences*

The Commission proposes retaining suspicion as the trigger for criminality under the substantive money laundering offences on the basis that this enhances the ability of prosecutors to secure money laundering convictions and reflects the Parliamentary design of the offences.<sup>89</sup> Without further intervention, the combination of an all-crimes approach in POCA 2002, together with a suspicion-based threshold for criminality would do nothing to ameliorate the operation of the authorised disclosure and consent provisions. It may be recalled that such DAML SARs seeking consent to continue with a transaction are the most resource intensive both for reporters and the NCA. For those in respect of whom a disclosure is made, bereft of any funds whilst consent is awaited, and denied any explanation due to the spectre of “tipping off”, a DAML SAR may have catastrophic financial and reputational consequences.<sup>90</sup>

Therefore, in response, the Commission proposes, inserting an exemption within ss.327–329 for reporters in the regulated sector who do not have reasonable grounds to suspect that property is criminal property (although they may still have a subjective suspicion).<sup>91</sup> It is envisaged that, as with the failure to disclose offences in ss.330–332, the cumulative subjective/objective interpretation of the term “reasonable grounds to suspect” deployed in *Saik* will also be used within ss.327–329. The Commission anticipates that this threshold may refine the quality and utility of DAML SARs for the NCA whilst introducing an additional layer of protection for the subjects of disclosures.<sup>92</sup> As for required disclosures, effectively raising the threshold for criminal liability across the regulated sector in relation to the substantive offences is conceptually appealing, although it brings with it operational challenges in implementation.

## *Measures supporting the proposed thresholds*

In support of these measures the Commission invites consultees’ views as to whether the Government should be required to issue statutory guidance on both the suspicion threshold and “reasonable grounds for suspicion” in respect of any revised threshold, together with a prescribed SARs form which would necessitate the delineation of a reporter’s grounds for suspicion.<sup>93</sup> Whilst a flexible “single source of definitive guidance” may assist in addressing both sectoral inconsistencies in interpretation and any confusion surrounding the law (as opposed to what constitutes best practice), it must also be nuanced enough to take into account the very different encounters with potential laundering each sector faces.<sup>94</sup>

The Commission envisages a non-exhaustive list of “those factors capable of founding a suspicion ... and those which should be excluded” (with a similar list in respect of any “reasonable grounds for suspicion”).<sup>95</sup> The potential drawback of any such list is that it may prompt a shift towards a more compliance focussed,

<sup>89</sup> Law Commission, *Anti-Money Laundering: the SARs Regime Consultation Paper*, paras 9.44–9.45.

<sup>90</sup> *Squirrel Ltd v National Westminster Bank Plc (Customs and Excise Commissioners intervening)* [2005] EWHC 664 (Ch); [2006] 1 W.L.R. 637 at [7].

<sup>91</sup> Law Commission, *Anti-Money Laundering: the SARs Regime Consultation Paper*, paras 9.52–9.53.

<sup>92</sup> Law Commission, *Anti-Money Laundering: the SARs Regime Consultation Paper*, paras 9.49–9.51.

<sup>93</sup> Law Commission, *Anti-Money Laundering: the SARs Regime Consultation Paper*, paras 9.18, 9.21, 9.64.

<sup>94</sup> Law Commission, *Anti-Money Laundering: the SARs Regime Consultation Paper*, para.9.9.

<sup>95</sup> Law Commission, *Anti-Money Laundering: the SARs Regime Consultation Paper*, para.9.12.

rather than a risk-based, approach to AML if there is over-reliance on a list of factors.

## **Conclusion**

The Consultation Paper represents a thorough and comprehensive exploration of the issues surrounding the SARs Regime and proposals for reform. This is no mean feat given that any options for reform are made more challenging by a number of constraints in the form of the UK's pre-existing legislative framework, current EU obligations and the FATF standards. This article examined two central aspects of the regime, although it should be noted that the Consultation Paper considers other important features such as improved information sharing and corporate criminal liability.

It is to be hoped that, notwithstanding the proposed retention of an “all-crimes” approach to AML, a number of carve outs from the scope of reporting in respect of those SARs of limited or no utility may still effectively streamline the regime. Whilst proposals to raise the suspicion thresholds for authorised and required disclosures are conceptually appealing as they shift the point at which criminal liability bites for reporters in the regulated sector, this may present operational challenges for reporters and may even prompt more of a compliance focus rather than a risk-based approach to AML should an over-reliance on statutory guidance on reasonable grounds emerge across the sectors. Raising the threshold with regard to required disclosures also gives rise to compliance issues both at EU and FATF level. Perhaps it is worth concluding with the following observation—ultimately, any refinement of the prevention pillar of AM/CTF must be accompanied by meaningful enforcement in order to create a comprehensive regime.