

A SEA CHANGE

Preparing for the new SARs regime

The first UK National Risk Assessment of Money Laundering and Terrorist Financing (the “NRA”) published in 2015 saw the government commit to an AML Action Plan which addresses the risks identified in the report.

One of its priorities was to reform the Suspicious Activity Reports (SARs) regime, with the review due to take place in 2018 when the UK undergoes its mutual evaluation by the Financial Action Task Force (FATF). Here we explore the driving forces behind expected changes to the Suspicious Activity Reports (SARs) regime and how Money Laundering Reporting Officers (MLROs) can prepare for it now.

Background on the current regime

The existing UK SARs regime has attracted criticism from law enforcement bodies and the SARs submitting institutions, with general agreement that it needs to improve the effectiveness and efficiency of current arrangements.

A few key data points:

- The 2015 SARs Annual report states that the number of submissions increased by 20% during the preceding three years; with over 80% submitted by banks. A limited number have been filed by real estate agents which are deemed to be high risk.
- The UK Financial Intelligence Unit (FIU) received 380,882 SARs in 2014/2015 alone, with 14,672 consent requests which require decisions within 7 working days.
- Whilst the volume of items for review has increased, the number of FIU staff has decreased from 100 in 2007 to 80 in 2015. This means each FIU analyst has to review an average of 180 consent SARs in a year or roughly 1 consent SAR every two days.
- There is concern that some financial institutions file SARs as a defensive measure by taking advantage of the “consent

request” mechanism so as to obtain “approval” from the authorities for risky transactions.

- There is a hidden cost as well. For every SAR that is filed a firm will perform a detailed evaluation on a much higher number of other transactions.

What might be changed?

The main focus on the expected changes of the regime is improving the quality of SARs and granting new powers to the National Crime Agency (NCA). It is widely believed that a new reporting structure will be introduced with the potential removal of consent request mechanism and the introduction of de minimis barrier to ensure the new regime will not be misused and to encourage the submission of only high value and meaningful SARs. The establishment of the Joint Money-Laundering Intelligence Taskforce (JMLIT), following the one-year pilot programme for sharing intelligence between the public and private sectors, will lead to increased collaboration between both sides that achieve better outcomes. On the other hand, the NCA might be given more powers to act and freeze funds in bank accounts quickly as currently only a relatively small proportion of consent SARs result in a restraint order and subsequent confiscation.

Focus on quality, not quantity

Why has the number of SARs increased? Currently there is no de minimis barrier for reportable transactions; a SAR must be filed whenever a suspicion is identified. So from a financial institution perspective, there is no downside to filing. The cost of evaluating a potential SAR can be shifted from the firm to the NCA through a filing.

However the NRA noted concerns about the quality of SARs submitted. In particular, it noted that many reports failed to articulate suspicions accurately to enable any money laundering and terrorist finance connotations to be properly assessed by law enforcement bodies in the light of other available information. There is certainty that if the quality of information contained in the SARs submitted was improved the intelligence agencies could make a more valuable contribution to the fight against financial crime.

Technology – a helpful and complicating factor

Many firms (certainly all large financial institutions) are making substantial investments in technological solutions that will enable them to reduce the cost of customer data collection and transaction monitoring. They are some way from applying artificial intelligence and block chain capabilities to the challenge but they are using algorithmic analysis, big data pools, and other techniques to reduce the number of 'false positives' requiring investigation.

The banking 'disrupters', financial technology firms and non-financial firms offering financial service products (e.g. Apple Pay and Google Wallet) are increasing significantly. At the same time payments can be made without a bank being involved at all – e.g. cryptocurrencies such as Bitcoin. The SARs regime was not developed with these types of firms in mind. At a minimum there is a need for the firms, the regulators and law enforcement agencies to gain a thorough and common understanding of the businesses, the financial crime risks involved and how the SARs regime will apply in practice.

What should MLRO's be doing now?

Although the Government is yet to unveil details of the new-look SARs regime, MLROs can begin preparing their stakeholders for the potential changes. Critical steps we recommend include:

Be informed and collaborate with industry peers – Keeping up with announcements from Government and regulators, insights

from commentators, independent think tanks, regulators and industry associations is advisable. Information sharing amongst industry peers is always useful and in this case also reinforces the collective commitment required to effectively combat financial crime. The Home Office together with the Royal United Services Institute held three workshops in September and October 2015, which completed the formal consultation process. However, you will probably have a view on the proposed changes when they are announced. Share your thoughts with your peers and participate in any discussions held by regulators and industry associations.

Think about impacts on your organisation – This includes how the new regime will affect the organisation's compliance policies and procedures, resource planning, the reporting infrastructure in conjunction with training and education requirements. It will also require changes to existing technology so bring your technology team into the information flow now. For example, currently the National Crime Agency has seven days to respond to a "consent request" SAR. If the seven day period is removed, how would this affect the suspicious transaction reporting process and reporting lines within your organisation?

Engage with stakeholders, include the Board and leaders across the three lines of defence – The MLROs should highlight the potential changes in the SARs regime in regulatory updates so that people are aware change is coming. Communication will be most effective if it describes the reality of your organisation. Many firms we see merely circulate the text of the proposed legislation/regulations which does not engage people.

Conclusion

With the implementation of the Fourth Anti-Money Laundering Directive in late 2016 and the upcoming FATA mutual evaluation in 2018, the Government is determined to enhance the current AML regime and a reform to the SARs regime is imperative. Formal proposals are yet to be made public. However, it is possible to anticipate the changes might be based on the points outlined above. Any regulatory change will entail an increased workload and there is no doubt that the overhaul of SARs regime will pose a challenge to MLROs against the background of ever increasing compliance obligations. It is time to start your scenario planning and get ready for a sea change.

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