

Written Evidence

UK Foreign Affairs Committee Inquiry: Responding to Illicit and Emerging Finance

Submitted: September 27, 2022

Introduction

The ACAMS global community continues to monitor the worldwide evolution of transnational criminal organizations. The financial crime threats from such groups highlight their ability to evolve and adapt, both in terms of continued exploitation of existing governance arrangements and to a new wave of technology, capitalizing on new payment channels and the rise of digitalization. Their operating environment is growing more and more complex, and it will be a significant challenge to reign this in. The data indicates that despite major investment in compliance functions, clear implementation gaps remain. The standards of transparency and beneficial ownership also remain a persistent area of global concern.

The sheer scale of effectively tackling financial crime will require agile and dynamic cooperation of the public and private sectors. In support of this, the purpose of our response is not to answer each question posed in the Call for Evidence, but instead to offer some key observations by those working on the frontlines of compliance.

About ACAMS

ACAMS is the largest international membership organization dedicated to providing opportunities for anti-financial crime (AFC) education, best practices, and peer-to-peer networking to AFC professionals globally. With over 100,000 members across 180 jurisdictions, ACAMS is committed to the mission of ending financial crime through the provision of anti-money laundering/counter-terrorism financing and sanctions knowledge-sharing, thought leadership, risk-mitigation services, ESG initiatives, and platforms for public-private dialogue. The association's CAMS certification is the gold-standard qualification for AFC professionals, while the CGSS certification is its premier specialist qualification for sanctions professionals. ACAMS' 60 Chapters globally further amplify the association's mission through training and networking initiatives.

ACAMS Response

Our response focuses on the following areas:

- International governance regimes and data observations
- UK efforts to counter illicit finance through sanctions and in response to evolving technology

International Governance Regimes and Data Observations

The Effectiveness of International Governance Regimes - What the Data Tells Us

1. Industry makes immense investments for fighting financial crime. By way of context, the UK alone is **estimated** to have spent GBP28.7 billion on compliance in 2020. While opinions on the exact level of investment may vary, it is clear that billions are committed to global compliance functions. Despite this significant outlay, an active debate on whether resources are being targeted in the right way to reduce illicit financial flows remains.
2. A conservative estimate puts the illicit financial economy at **between 2% and 5% of the world's gross domestic product** - between EUR715 billion and 1.87 trillion each year. Although there is little information on the topic, a sizeable portion of the hidden economy is incorporated into financial assets, the real economy, global financial centers, and numerous offshore tax havens in developed markets.
3. Transnational criminal organizations (TCOs) have benefited considerably from emerging technology, e-commerce, and digital finance. The rise in cyber-enabled crimes, such as ransomware, provides new and evolving attack vectors to criminals, the extent of which are difficult to measure.
4. An examination of the Financial Action Task Force (FATF) Mutual Evaluation Results on Effectiveness (**using data from September 13, 2022**) indicates that most nations are severely ineffective at identifying and reducing financial crime. A small portion of the 136 jurisdictions has high efficacy, with almost 80% having low to moderate levels across the eleven immediate outcomes. An examination of immediate outcome 7 (IO7) across all jurisdictions, which evaluates successful criminal investigations and prosecutions, shows that **no jurisdictions received a highly effective rating (HE)**. IO7 is critical to improving the overall state of effectiveness and can be an indicator of progress.
5. Our analysis of anti-money laundering enforcement actions reported on **moneylaundering.com** by ACAMS between January 1, 2019 and August 31, 2022 shows that roughly 76% of the AML fines were issued in six countries: the United States (42%), the United Kingdom (10%), India (9%), Malta (8%), the United Arab Emirates (3.5%), and Hong Kong (3%). According to this report, most jurisdictions employ individually crafted strategies to combat TCOs and other criminal organizations.
6. Despite this, regulators and criminals continue concentrating on the banking sector. Banks are targeted for more than 60% of the fines. However, penalties for companies (19%), non-bank financial institutions (17%), and other organizations that attract regulatory attention have been increasing.
7. Notwithstanding ongoing investments in compliance frameworks, we anticipate continued regulatory enforcement action on financial institutions. The most common deficiencies leading to enforcement actions relate to AML programs in respect to obligations connected with issues such as know your customer, customer identification, customer due diligence, transaction monitoring, and suspicious activity reporting.
8. Regardless of continued enforcement action, many employees from a variety of businesses are increasingly familiar with professional money laundering typologies and procedures, laws and regulations, and ways to spot and prevent financial crime. However, staying up to date with the constant evolution of regulatory frameworks and criminal activity presents an ongoing challenge. Equally, major enforcement actions have consistently demonstrated widescale implementation gaps, loopholes, and weaknesses within overarching governance frameworks.

How the International Framework is Responding to the Evolving Global Threat Landscape

9. Our understanding of the breadth and depth of the international economic crime threat has significantly improved in the last 10 years. A combination of enhanced prioritization by governments, investment by private industry, and revelations by investigative journalists and a string of whistle-blowers has shed light on previously little understood issues. This improvement was fed by a variety of public-private partnerships and multilateral pressure exerted by groups such as the G20 and FATF and public awareness campaigns. These are firm foundations to build on, but require sustained activity to tackle international inefficiencies and ineffectiveness.
10. Some remaining gaps can be reduced by domestic agencies and legislative changes through improvements to intelligence sharing (including the suspicious activity reports (SARs) regime) and efforts to improve transparency (accessible beneficial ownership registers and corporate registration records). However, given the global nature of financial crime, much more should be done to support and improve international structures.
11. A theme regularly raised in our expert-level discussions is the need to improve strategic and tactical intelligence sharing internationally and on a bilateral basis. Further concerted action could be taken to highlight potentially malicious activities to the public (most critically on fraud), by means of international cooperation on breaking events (i.e. kleptocracy, offshore finance, and regulatory arbitrage) and a focus on technological developments through joint exercises to kitemark and stress-test FinTech in an international sandbox and a global warning list of unregulated cryptoasset firms to highlight weak spots.

High-Level Observations on Transparency and Beneficial Ownership

12. It is widely acknowledged within the global anti-financial crime community that a lack of beneficial ownership transparency is a serious impediment to combating illicit finance. Progress has been achieved through the implementation of beneficial ownership registers in the EU and the UK. However, illicit actors continue to extensively abuse legal entities and arrangements to hide and move ill-gotten wealth. This includes using complex legal structures and transferring tainted funds to low-transparency jurisdictions.
13. According to the FATF's latest **summary** of its compliance ratings dated September 13, 2022, only a single jurisdiction (Trinidad and Tobago) out of more than 120 is fully compliant with Recommendation 24 ("Transparency and beneficial ownership of legal persons"). Recommendation 25 ("Transparency and beneficial ownership of legal arrangements") is slightly better.
14. The lack of beneficial ownership information in the US presents a considerable global challenge. As set out in our briefing – **US Beneficial Ownership: Addressing Russia Corruption Risks** – major US beneficial ownership reforms are underway. Specifically, the Corporate Transparency Act (CTA) of 2021 mandates the implementation of a central beneficial ownership database to be administered by the Financial Crimes Enforcement Network (FinCEN). Whilst these are welcome developments, full implementation of the CTA's provisions may take years and, even when implemented, not all information will be publicly accessible and numerous exemptions will remain.

15. A feature of highly publicized money laundering investigations has, among other areas, included the use of US-registered limited liability companies (LLCs). Rather than report their beneficial or nominee owners, US-based LLCs currently disclose publicly the names of registered agents (who may be owners, but in a majority of cases are not), limiting the ability of both financial institutions and the LLCs' non-financial counterparties to identify and assess potential financial crime as well as other risks. More broadly, the often unsatisfactory data quality is a consistent concern across the majority of ownership registries.
16. The hard-to-navigate global regulatory patchwork presents a systemic challenge in respect to the application of beneficial ownership requirements. While FATF has a common beneficial ownership standard, the manner in which it has been implemented across jurisdictions has resulted in multiple legal and regulatory variations. In turn, these variations create a myriad of operational discrepancies. For instance, when dealing with trusts, FinCEN requires US-based financial institutions to record the trustee or, in multi-trustee trusts, one or several co-trustees as beneficial owners. In comparison, the UK requires the recording of the settlor, all trustees, and all beneficiaries as beneficial owners, while the EU's identification requirements also include the protector, if any. Refer to Figure 1 in the annex for a visual illustration.
17. Additional challenges arise from the yet-to-be-addressed lack of balance between customer confidentiality and information sharing. Heavily regulated financial sector organizations often find it difficult to prioritize between these two imperatives and may be compelled to adopt a conservative approach, with direct implications for existing customers and their own ability to grow by attracting new clients. In addition, privacy regulations frequently lead to major jurisdictional differences that pose an immediate challenge for large organizations spanning many geographies. For instance, two financial firms within the same global group but in different countries may be unable to share key customer identification information of the same customer, because one or both jurisdictions prohibit the cross-border transmission of personal data. This undercuts efforts to centralize core enterprise-wide functions and leaves related organizations with no choice but to continue working in silos.

UK Efforts to Counter Illicit Finance through Sanctions and in Response to Evolving Technology

18. Turning specifically to the UK, this response will examine enhancing UK sanctions implementation as well as the threat posed by cryptocurrency and distributed ledger technologies on the UK's financial crime compliance regimes and security.

Enhancing the Countering of Illicit Finance Through Sanctions

19. The use of financial and economic sanctions has risen significantly over the last decade, evolving considerably over this period in both the scope of what is targeted as well as the types of restrictions. As the nature of sanctions changes (e.g. thematic sanctions regimes targeting human rights abusers, malicious cyber actors, and corrupt officials), the global compliance community is faced with new and novel implementation challenges to ensure sanctions are applied correctly and effectively. There are a number of ways in which the UK government could support industry who are on the frontlines of sanctions implementation

20. Public-private dialogue and information sharing is a cornerstone of robust sanctions compliance. While dialogue does take place, this is traditionally between large international financial institutions and government. As new sectors are targeted, there is increasing need for engagement with those beyond the regulated sector (i.e. maritime sector, corporates, tech) as well as further engagement with smaller institutions.
21. Economic sanctions can be incredibly complex, and – particularly in the case of novel and unprecedented measures – there will often be areas where further guidance or clarification is needed. The absence of timely and relevant guidance may even lead to unintended consequences, possibly opposing the intention of the original measures. Accordingly, the issuance of guidance/clarifications from the UK Treasury is critical. For this guidance/clarification to meet the needs of industry, this would benefit from mechanisms enabling industry – not just the largest players – to communicate their compliance challenges to the government, for example through the upscaling of public-private forums.
22. UK sanctions are not implemented in isolation. When allies and partners implement similar restrictions simultaneously, discrepancies, legal conflicts and timing can cause confusion and reduce effectiveness, such as in the case of Russian sanctions following the invasion of Ukraine in February 2022. Early into the conflict, ACAMS created a series of **infographics** setting out many of the measures implemented by different jurisdictions, e.g. regarding restrictions on certain Russian billionaires, Russian banks, commodities, and luxury goods. These clearly demonstrated that while there was political alignment on sanctions, legal alignment was not on parity, and although this has subsequently improved, the initial implementation reality was a patchwork of varying measures. For example, licensing frameworks were often inconsistent and, at times, contradictory, creating further implementation issues and uncertainties.
23. Sanctions evasion can significantly weaken the effectiveness of sanctions regimes, and information sharing, such as providing typologies and red flag indicators, can be beneficial to industry. For example, those provided by the **Office of Financial Sanctions Implementation (OFSI) and the National Crime Agency in July** and **OFSI and the Bank of England in March** in relation to Russian sanctions evasion are a step in the right direction. But these efforts will only be effective through a concerted expansion of domestic and international dialogue. Sanctions evasion often includes cross border elements that involve multiple jurisdictions and entities.
24. The speed and significance of the measures the G7 and allies introduced undoubtedly illustrates the seriousness of the collective response, targeting those perceived as responsible for, and enablers of, the war. However, the aforementioned discrepancies weakened efforts to prevent the movement of funds and asset flight by designated Russian individuals to jurisdictions not implementing sanctions. These measures in relation to Russia also have strong interlinkages with wider financial crime risks, for example corruption, and implementation efforts are seriously affected by the limitations in transparency and beneficial ownership identified above.

The Disruptive Role of Crypto and DeFi on AML/CTF and the UK's Economic Security

25. Cryptoassets have quickly gone from a widely misunderstood means of transferring criminal payments to an asset class with increased institutional and public take-up. A **Financial Conduct Authority research note** published in 2021 estimates ownership in the UK at 2.3 million people. Another **study by Blockdata** suggests that over half of the 100 largest banks by assets under management had invested in cryptoasset services or proprietary technology. Despite the impact of the ongoing “crypto winter”, UK incorporated banks with a global footprint have made a series of investments in cryptoassets whilst making it easier for their customers to access cryptoassets.
26. A series of individual studies and estimates suggest that the rate of criminal abuse of cryptoassets (e.g. money laundering and darknet purchases) has declined significantly in recent years. Research by cryptoasset blockchain forensic firm Chainalysis indicates that the growing legitimate use of cryptoassets is outpacing criminal usage with transactions linked to illicit **wallets accounting for 0.15% of activity**. That said, US\$14 billion worth of criminal activity was also identified.
27. The reality is that we are still learning about the threat posed and the extent of criminal activity linked to cryptoassets. By June 2021, **Elliptic highlighted US\$2.5 billion worth of enforcement penalties imposed against cryptoasset businesses by US agencies**. Whilst there are numerous examples of egregious activity, many are linked to hacks against decentralized cryptoasset platforms targeting customer funds, rather than illicit activity specifically enabled by cryptoassets. This may indicate that the sector has moved to being a target rather than primarily a criminal enabler.
28. Whilst the financial services industry has been regulated for AML/CTF for over 30 years through multiple iterations of FATF guidance, the cryptoasset sector has been subject to similar provisions for only a few years. Again, there are conflicting signals about the extent of progress made by regulated firms. On the one hand, **only 38 firms (as of September 26) have been registered for business in the UK**, indicating an immaturity of approach to regulation.
29. On the other hand, known criminal abuse is on a downward trajectory and incremental actions by cryptoasset service providers would make a real difference. For example, registered cryptoasset exchanges could demonstrate that they take their clients’ deposits seriously by making the results of their cyber security audits public, adopting a consumer protection duty and engaging in voluntary intelligence sharing through public-private partnerships, such as the Joint Money Laundering Intelligence Taskforce (JMLIT).
30. To ensure mitigation of cryptoasset financial crime risks, a proactive response to global regulation, supervision and enforcement must be taken by the international community. Areas such as decentralized finance (otherwise known as DeFi), non-fungible tokens, and stablecoins are currently unregulated in the UK and most other jurisdictions. Pushing for consistent, comprehensive and equitable regulation of these elements of the cryptoasset ecosystem would allow financial crime, fraud, and national security concerns to be addressed within a comprehensive and collective framework response.
31. Whilst there is no clear evidence that cryptoassets have been used to avoid financial sanctions imposed on the Russian regime, some of the wider paraphernalia of blockchain technology, such as privacy coins and mixers, have been exploited by threat actors, such as North Korea. You can read more about crypto risks in relation to Russia in our **Crypto and Ukraine Briefing**. Where sanctions have been used against decentralized cryptoasset services, such as the recent OFAC designation of Tornado.Cash (an open-source software protocol for disbursing and obscuring funds), they have, so far, only been partially effective. This is representative of an asset class and technology at a critical juncture.

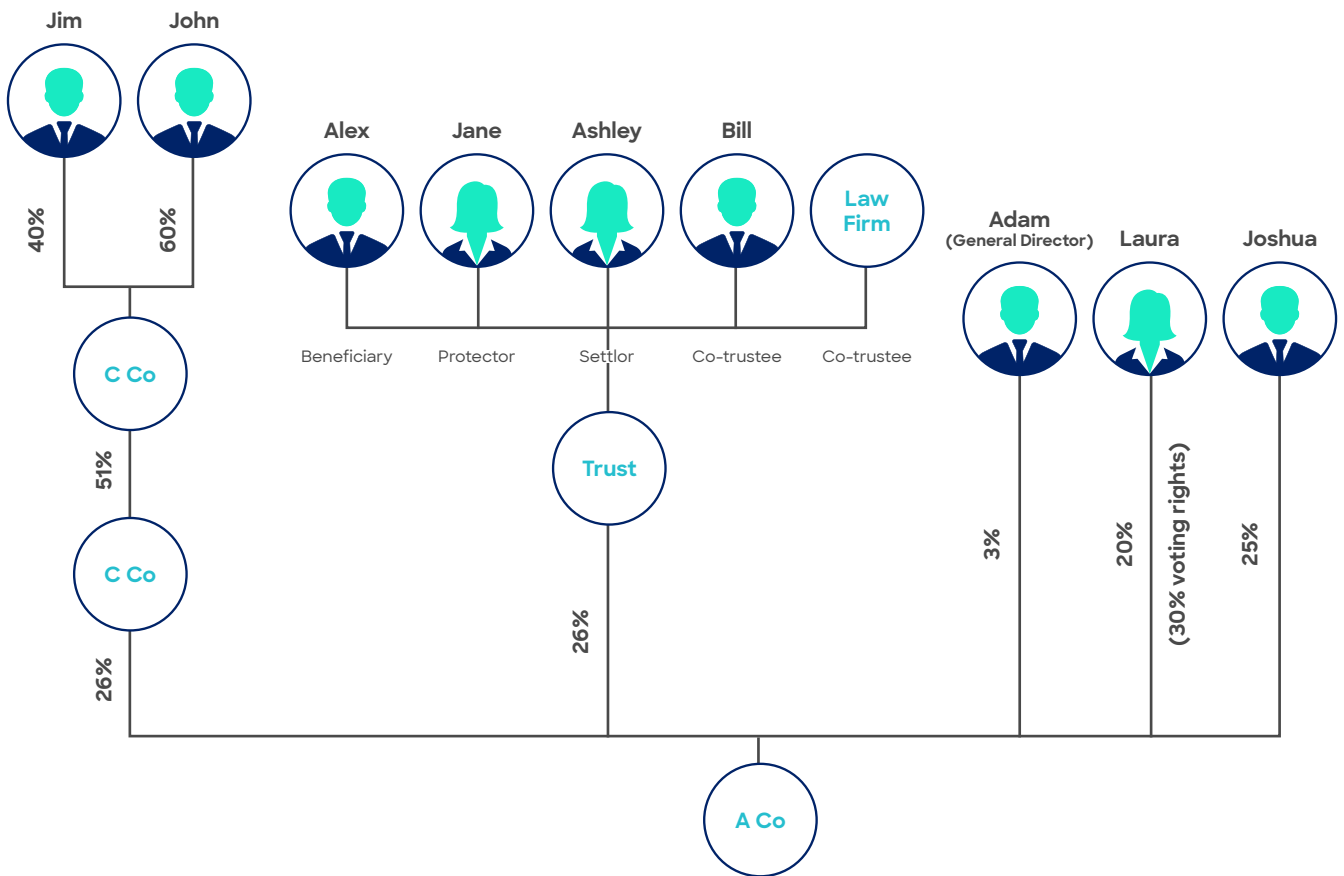
32. The cryptoasset sector in the UK and elsewhere has come a long way since its early role as a payment mechanism for illicit goods on darknet marketplaces. The sector is now regulated to the same standard as other financial institutions (including banks) for AML/CTF. However, it has not fully shrugged off its reputation for enabling criminal activity such as ransomware attacks. As more comprehensive regulation covering consumer protection and other systemic risk is rolled out, the paradigm will continue to shift.

Conclusion

33. As illicit and emerging finance risks and threats continue to grow, significant resources are being applied by the global compliance community to combat these constantly evolving challenges. This response has highlighted a number of areas where further action may strengthen the global response – such as improving transparency and making beneficial ownership registers more accessible, as well as strengthening public-private partnerships and information sharing.
34. In the UK context, sanctions compliance has been hampered by discrepancies and legal conflicts across different sanctioning jurisdictions. Further cross-jurisdiction alignment and coordination would enhance this.
35. The rise of cryptocurrency also presents new financial crime risks, requiring a proactive response both at domestic and international levels, and proactive cooperation with both international and inter-industry partners.

This written evidence was submitted to the UK Foreign Affairs Committee on September 27, 2022, as part of its inquiry "Responding to Illicit and Emerging Finance". You can view the committee's report as well as other written evidence [here](#).

Annex



Who are the beneficial owners of A Co?										
	Jim	John	Alex	Jane	Ashley	Bill	Law firm	Adam	Laura	Joshua
EU (5-6 BOs)		X ¹	X	X	X	X			X	
UK (4 BOs)			X		X	X			X	
US (3-5 BOs)						X ²	X ²	X	X ³	X

¹ Most EU member states mandate the multiplication of ownership stakes to calculate indirect ownership of a legal entity. However, some member states, such as Austria, require that natural persons in control of a legal entity that has more than 25% direct ownership of a customer be recorded as beneficial owners (BOs), whereby control means, among other things, ownership in excess of 50%.

² When dealing with multi-trustee trusts that own ≥25% of a legal entity customer, US-covered financial institutions (FIs) are not required to record more than one co-trustee of choice as a BO. However, they have the option to record more than one such BO.

³ US-covered FIs are not required but may nonetheless decide to record as a BO an individual who owns less than 25% of equity interests in a legal entity but more than 25% of associated voting rights.