ACAMS Insights

The FCA's Dear CEO Letter – A Call to Action for UK Retail Banks

The UK regulator, the Financial Conduct Authority (FCA), has increasingly used "Dear CEO" style letters as a means of focusing attention on high-risk areas in financial services. The FCA's **Dear CEO letter**[1], issued in May 2021 to the CEOs of the UK's retail banks, was a call to action for those in charge to address the repeated deficiencies the UK regulator has identified through their recent assessments.

The tone was clear. An expectation that senior managers accountable for these control frameworks promptly look inside their own organization, self-identify their gaps, and demonstrate action and ownership. Inadequate responses will result in regulatory intervention.

The letter clearly puts accountability at the door of those responsible under the Senior Manager Regime and perhaps sets the tone for the FCA's future stance on personal accountability. How those holding this responsibility engage and respond to this letter will be key in demonstrating effectiveness and ownership of anti-financial crime (AFC) regulatory compliance.

What does the letter say?

The issues raised in the letter are not new and are consistent with what has been seen in recent enforcement actions or thematic reviews. Whilst the regulator acknowledges "examples of effective control frameworks and good practice", a distinct lack of patience is evident.

Many of the themes are repeated issues in the industry and in organizations where money laundering risks are high.

Dear CEO letter – key themes

Governance and control

Clear delineation of the three lines of defense, appropriate oversight, and ownership of risk in the first line is not always evident. The FCA expects active AFC risk ownership by senior management, demonstrated by governance committees for key AFC risks and documented evidence and rationale for decision making.

Risk assessment

Business are failing to either adequately assess their risks, or evidence the controls to drive down residual risks. This extends to customer risk assessment, seen as too generic, not tailored to specific risks, and not extending beyond traditional AML and sanctions risks.

[1] https://www.fca.org.uk/publication/correspondence/dear-ceo-letter-common-control-failings-identified-in-anti-money-laundering-frameworks.pdf

Due diligence

The usual themes are called out regarding deficiencies of due diligence, ranging from confusion on Source of Wealth and Source of Funds, and failure to appropriately assess PEP risk, to a lack of evidence of a risk-based approach and lack of assessment of nature of business and activity levels. Nothing new is being asked, and it reads as if the FCA's patience on getting this right may be wearing thin.

Transaction monitoring

The use of group led solutions for UK subsidies or branches, or "off the shelf" products that do not consider the individual calibration needed to effectively manage risks, is the common failure. This is coupled with a lack of technically skilled staff to aide implementation and ongoing review of systems to respond to new and emerging risks.

Suspicious activity reporting (SAR)

Lack of awareness and documentation of internal SAR processes has been raised by the FCA, along with the lack of clear decision making and rationale for raising (or not raising) external SARs. These are both vital aspects to support law enforcement in the fight against financial crime.

Why are UK banks suffering persistent AFC failures?

A recent Lexis Nexis reports estimates the UK's annual cost of AML compliance to be £28.7 billion, with expectations that this will rise to £30 billion by 2023[2]. This begs the question: why are organizations spending so much on AFC compliance but not getting it right? The reasons can be broadly summarized as follows.

The pace of regulatory change

The volume and complexity of regulatory change is time consuming to digest. Financial institutions need to assess the associated impact, and procure funding for resource or technology to work through the required procedural and system-based changes. It takes time and agility to invest in solutions appropriate to address and effectively manage the risk.

The pace of technological change

Delivering large-scale, transformative technology upgrades requires significant investment, time and resource. Often organizations are dealing with fragmented, legacy systems that face interoperability and integration challenges; replacing is not as simple as a "plug and play" approach.

[2] https://solutions.risk.lexisnexis.co.uk/cutting-the-costs-of-aml-compliance?utm_source=google&utm_medium=paid&utm_campaign=bsukifc21.fcc.tcoc&gclid=EAIaIQobChMI3qe3mIvi8QIVtWLmCh2_5A0oEAAYASAAEgJxa_D_BwE

The importance of data

Missing and siloed data, on systems that do not interface with each other, impacts downstream processes. This in turn results in more manual processes or workarounds. Remediating these data gaps can be time consuming and costly, but deployment of new technology to address shortcomings will not work without the right data.

The right skills

Many organizations have suffered through complex system migrations that have not been properly implemented. This is often due to lacking the right change or technological skills. The result is delayed programmes, process failures and increased costs.

The right people

AFC functions have grown significantly in response to regulatory changes and pressure which, dependent on the complexity of the organization, can result in sizable teams. This has put enormous pressure on the labour market. Demand for skilled staff is high, as is competition for experienced professionals, making it difficult and costly to attract and retain skilled teams.

Internal cost pressures

Competing priorities and other regulatory obligations has meant that organizations have not always prioritized investment in AFC unless something has gone wrong. This approach can result in large-scale, expensive remediation exercises, that are heavily people reliant and drive up costs. It may mean that organizations never achieve a "BAU" state, continually trying to "catch-up" with new regulatory requirements while resolving previous issues.

Addressing the letter: what are the key takeaways for CEOs?

In tackling the gap analysis required by the "Dear CEO" letter, retail banks should consider looking beyond the assessment of whether their AFC systems, processes and procedures are fit for purpose. Senior leaders should be addressing areas which have a direct and sustainable impact on the effectiveness of their control environment.

Dynamic and agile risk assessments

Completing risk assessments effectively should make the gap analysis requested by the FCA more straightforward. Risk assessment should be dynamic and agile – identifying where controls are ineffective or immature, and equipping senior managers to manage and prioritize their AFC framework.

Culture

Tone from the top, tone from above, and tone from within are equally important. Senior management should foster an environment where employees understand the importance of combatting financial crime, and feel they can raise risks and issues, and speak up against decisions. This environment reduces the tolerance for process inefficiencies, poor decision making, and the lack of support for AFC investment.

Prioritization

Prioritization is key, particularly when deficiencies are identified. A risk-based approach that enables senior management to understand where their greatest risks and threats lie, linked to its enterprise and national risk assessment, should be the basis of allocation. Organizations should tackle these areas first with the right budget, senior management support, resource, and time.

Harnessing the benefit of technology

Building sustainability into AFC controls through technology drives up efficiency, so organizations should avoid the short-term view to "plug the gap" rather than strategically fix the issues. Whilst RegTech can bring efficiencies, organizations need to invest to realise its potential. Maintaining rich full data should be a priority: the right input feeds better outputs, and unlocks the benefit of technology.

People

Equipping employees with the right tools and training will improve effectiveness and help to retain individual talent. Invest in the right skills – building data and technology capabilities – but remember organizations cannot rely solely on the machine. Human intervention and review is still pivotal.

Adopting a risk-based approach

Move from just meeting regulatory compliance, to managing the specific AFC risks that the organization is facing on all levels. This requires a more fluid, ongoing risk management process, entrenched in the premise of a risk-based approach. Use resources effectively to meet regulatory requirements and make a practical impact in mitigating AFC risk.

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August 2, 2021

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