

Money laundering responses

The steps taken in recent years against banks by regulators and law enforcement bodies in relation to money laundering have garnered a lot of publicity. The year 2015 saw Barclays fined £72m by the FCA over a £1.9bn deal that ran the risk of being used by launderers and those financing terrorism. The size of the fine related to the fact that staff had kept relevant client details in a safe rather than on the bank's software. The case involved Barclays relaxing their assessment regime, and the bank had also broken its own internal controls. There was, however, no evidence that Barclays had colluded in money laundering. This was the seventh penalty imposed on Barclays by the FCA and took the total fines that have been imposed on Barclays by the FCA since 2009 to £500m. Barclays was fined US\$2.4bn in the USA for LIBOR rigging, and the RBS Group was fined US\$395m for the LIBOR scandal by the US Department of Justice and had to pay a further \$205m to the Federal Reserve. In addition to this, Coutts Bank, the Royal Bank of Scotland's private banking arm, was fined £8.75m for breaching money laundering rules in relation to politically exposed persons.

In the USA, matters are more extreme. HSBC was fined US\$1.92bn for allowing itself to be used by launderers in Mexico and terrorist financiers in the Middle East. The bank had also stripped details from transactions that would have identified Iranian entities and potentially put the bank in breach of US sanctions against Iran. HSBC also spent US\$290m on remedial measures. Standard Chartered was fined US\$667m in the USA for breach of laundering regulations. They also hid details from the regulators of certain clients, including Iranian ones.

Deutsche bank was fined US\$258m for violating US sanctions as well. Their employees had handled US\$10.8bn in restricted transactions. The bank's employees had also obscured transactions in relation to Iran, Syria, Libya, Myanmar and Sudan which were also subject to US sanctions at the time.

The biggest fine for sanctions violations was that of US\$8.9bn imposed on BNP Paribas who had breached the International Emergency Economic Powers Act and the Trading with the Enemy Act. The size of the fine related to the size of the transactions concerned, not the size of the profit made. The bank was also seen by the US regulators in dragging its feet in co-operating.

There is an interesting issue here. The USA has officially not been trading with Iran for a number of years, but its own balance of payments figures show a healthy balance of payments surplus for the USA on trade with Iran. The year 2015 saw a surplus of US\$271.4m. A cynic might regard this as reflecting the lobbying power of certain US firms in Washington.

For banks and other financial services firms, there are also the costs of applying pan-European Union (EU) regulations, many of which are not well-designed for the UK market. It has been estimated that Solvency II has already cost the UK insurance industry over £3bn[1], a figure one leading UK regulator described as "shocking"[2] and Andrew Bailey of the FCA described as "frankly indefensible". Nigel Wilson, Chief Executive of Legal and General, has pointed out that the costs imposed on UK financial services businesses by the EU are equivalent to half the cost of Crossrail. Add to that the cost of the fees that have to be paid to the regulators, for example, last year, the biggest

banks and insurers paid £257.8m between them[3], then the fees they will have to pay to cover the PRA's work on ring fencing and on top of that the fines that get imposed by both regulators and criminal courts.

A culture has emerged that whenever there is a failing or perceived failing in an institution, the primary response is to fine it and/or impose costs. The problem is that this does not primarily impact the people at fault, but the shareholders. Typically, these will be pension funds, pensioners investing directly, other investment vehicles and corporate and personal investors. Why should they be made to suffer? Meanwhile, the senior figures in these firms suffer little impact and people lower down the management structure end up being held responsible – a kind of inverse confucianism!

In the case of smaller firms, the regulators are completely uninhibited about holding the directors responsible for wrongdoing. It may be the case that it is more likely in a smaller firm that a director will be directly involved in a way that is provable, but there is clear evidence of there being two playing fields and two regulatory approaches according to the size and power of the regulated firm.

Thus, there is a double-pronged attack taking place on banks and financial services firms. Regulatory costs and burdens on one hand and excessive fines on the other are rendering the financial services market place an unattractive place to do business. Larger firms can cope with these impositions to an extent, but for small and medium-sized operations, business becomes potentially unprofitable. Even for the larger ones, there is a significant impact on their capacity to make profits.

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Notes

1. C. Cheung, *The Actuary*, 18 December 2015.
2. A. Grey, *Financial Times*, 6 February 2013.
3. C. Bingham "Cost of UK regulation rises for banks and insurers". *Financial Times*, 19 March 2015.