

# Cleaning Up Money Laundering

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The rise of money laundering has led regulators around the world to adopt new ways to tackle the problem. In tandem with a renewed focus on accountability and conduct in financial regulations in recent years, increasingly, anti-money laundering frameworks are extending the compliance- and penalty-based approach to include an ethics dimension.



**M**oney laundering is a serious problem. According to the United Nations Office on Drugs and Crime (UNODC), the estimated amount of money laundered in a year is two to five per cent of global gross domestic product, or about US\$800 billion to US\$2 trillion.

Though laws and regulations have been considerably strengthened in recent years to fight it, the corresponding cost of compliance has also escalated.

Existing anti-money laundering laws act largely as a disincentive to commit crimes, rather than an effective deterrent. The UNODC estimated that less than one per cent of global illicit financial flows is currently being seized and frozen.

For this reason, regulators around the world are moving towards ethics-based regulations

to change the status quo, emphasising the importance of the right organisational culture and behaviour in protecting the financial system.

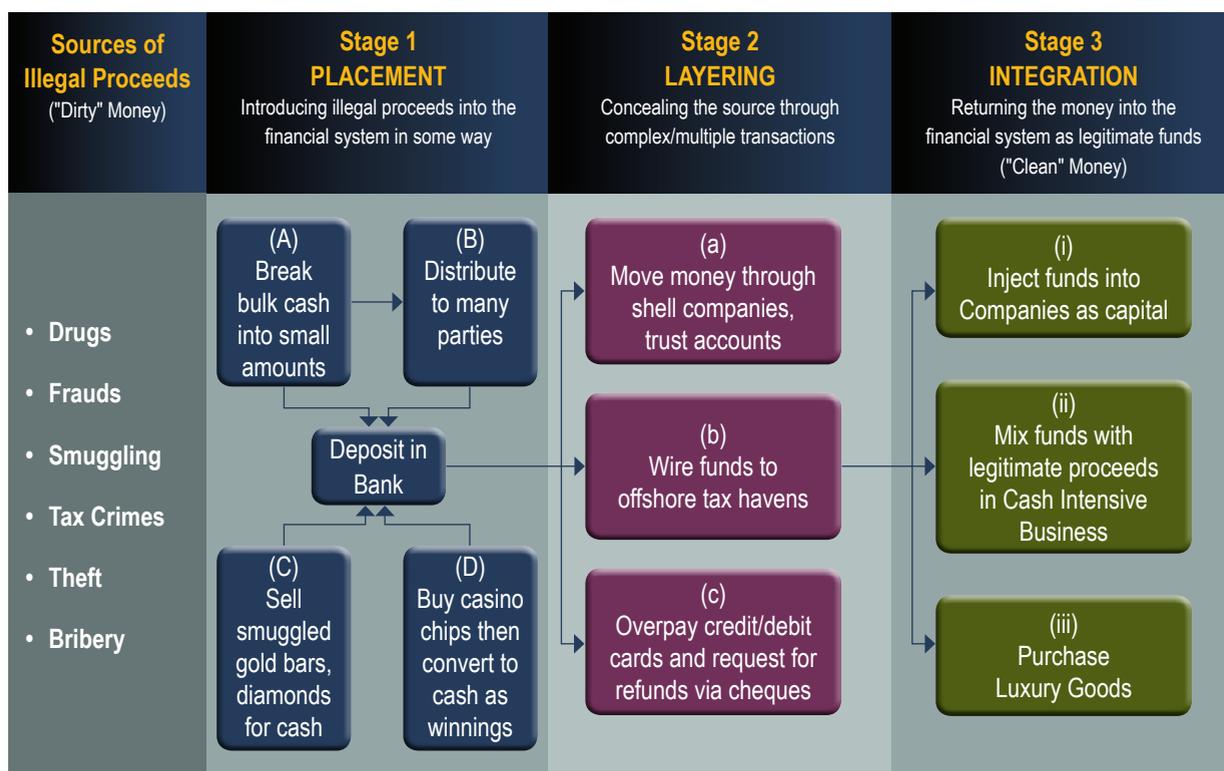
### How money gets laundered

Money laundering is the process by which large amounts of money derived from criminal activities are “cleaned” to make it appear that the money originated from a legitimate source. Drugs, fraud and smuggling are three major acts usually associated with this activity.

See the diagram, “How Money is Typically Laundered” for the three stages (placement, layering and integration) by which “dirty” money gets “cleaned”.

In Singapore, money laundering is a criminal offence under the Penal Code.

## How Money is Typically Laundered



Since almost all money from crimes ends up in a bank somewhere in the world, law enforcement agencies and financial regulators look to banks to implement robust anti-money laundering (AML) programmes.

The Monetary Authority of Singapore (MAS) has established clear guidelines on Anti-Money Laundering and Countering the Financing of Terrorism (AML and CFT) for financial institutions. To meet these requirements, banks implement stringent “know your customer” processes to verify the identity of their customers and their source of funds and wealth. They also monitor bank accounts, and analyse transaction patterns to detect anomalies. Suspicious transactions must be reported to the authorities.

### Money laundering agents

Bank employees are potential agents of money laundering. They could be coerced, bribed or tricked into doing so.

Other professionals such as lawyers, accountants, notaries, financial advisers, stockbrokers and real estate agents could also end up as agents. In 2017, a lawyer and a real estate agent in Singapore were charged and fined for failing to report a suspicious multi-million-dollar property deal in Sentosa Cove that fell apart after a high net-worth client was detained by the Chinese authorities for his involvement in a Ponzi scheme in China.

All professionals need to understand how AML and CFT laws and regulations impact their responsibilities, especially the fact that non-compliance carries the risk of criminal liability.

Of course, compliance poses unavoidable ethical challenges since professionals must strike a balance between reporting suspicious activities and maintaining the confidentiality of their clients. This is why professional bodies such as

the Institute of Singapore Chartered Accountants and regulators such as the Council for Estate Agencies have issued their own guidelines.

### Costs of AML compliance

According to research firm Wealth Insights, banks worldwide spent around US\$8 billion annually on AML compliance. Since 2008, they have been fined in excess of US\$300 billion for regulatory failings (see chart, “Anti-Money Laundering Fines”, on the next page).

Regulators have also intensified their efforts to oversee financial institutions more effectively and comprehensively by investing in technology and setting up dedicated AML departments. In almost all cases, the most commonly cited reasons for companies failing in their AML processes are weaknesses in management culture, professional integrity, and risk consciousness.

Despite the high cost of AML compliance, the UNODC estimates that less than one per cent of money laundering activity is actually detected. Not surprisingly, these numbers raise doubts about whether regulations and enforcement actions are sufficient deterrents in the battle against money laundering.

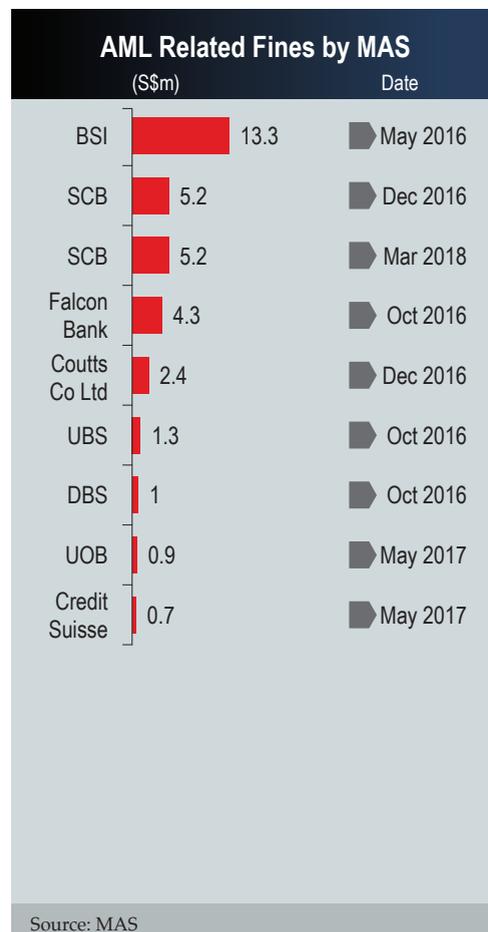
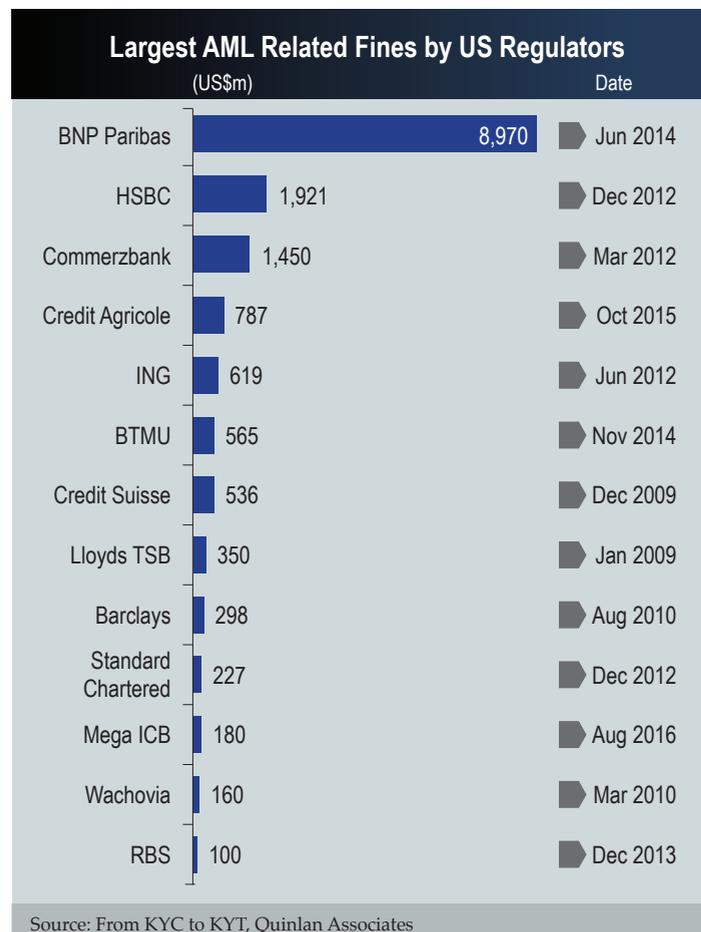
### Ethical issues

Ethics are moral guidelines that direct an individual in his actions. In contrast to laws, ethics deals with the ability to differentiate between right and wrong, and the commitment to do what is right. In any discussion about money laundering, two ethical issues loom.

The first relates to the actions and decisions of regulators against the executives of companies that brazenly flout money laundering regulations.

Take for example the US government’s decision not to criminally prosecute HSBC

## Anti-Money Laundering Fines



and Barclays, despite their admission of fault and the magnitude of their wrongdoings. From a utilitarian perspective, the decision is sound, as it balances regulatory actions with a broader consideration of the stability of the financial system. However, the opposing deontological view asserts that individuals are morally obligated to act ethically, no matter the consequences, so that in failing to mete out punishment, the US government has failed in its duty to carry out justice.

The second ethical issue relates to the somewhat narrow focus on compliance. The culture of an organisation is defined by the shared values, norms and attitudes that guide the behaviours of

its employees, and compliance requires everyone to recognise their regulatory obligations and to follow them. But is it enough that people follow rules simply because they fear the penalties that come with non-compliance? Surely the real test comes when they face situations where the rules are either not clearly defined or do not exist? In such cases, is it not better that an organisation's culture goes beyond mere compliance to include an ethical dimension?

An example of a culture of compliance and ethics in joint action is when staff from a remittance company foiled scams and prevented unwitting victims from transferring their money to con men. In this case, the staff went beyond standard

## Strengthening Individual Accountability



procedures (compliance) because they felt the need to do the right thing (ethics).

### Towards an ethics-based framework

After the finance ministers and heads of the central banks of the G7 countries collectively pushed for a code of conduct for banking professionals in 2015, several jurisdictions introduced ethics-based regulatory frameworks to strengthen individual accountability and conduct in the financial industry. These include the UK's Senior Managers and Certifications Regime and Conduct Rules (2016), Hong Kong Monetary Authority's Managers-in-Charge Regime (2017), and Australia Prudential Authority's Banking Executive Accountability Regime (2018). Underlying these new regulations is the assumption that behaviours are not motivated by a fear of regulatory penalties, but by ethical considerations.

Such ethics-based banking regulations are an effort by regulators to bring to banking a set of commitments that mimics similar values

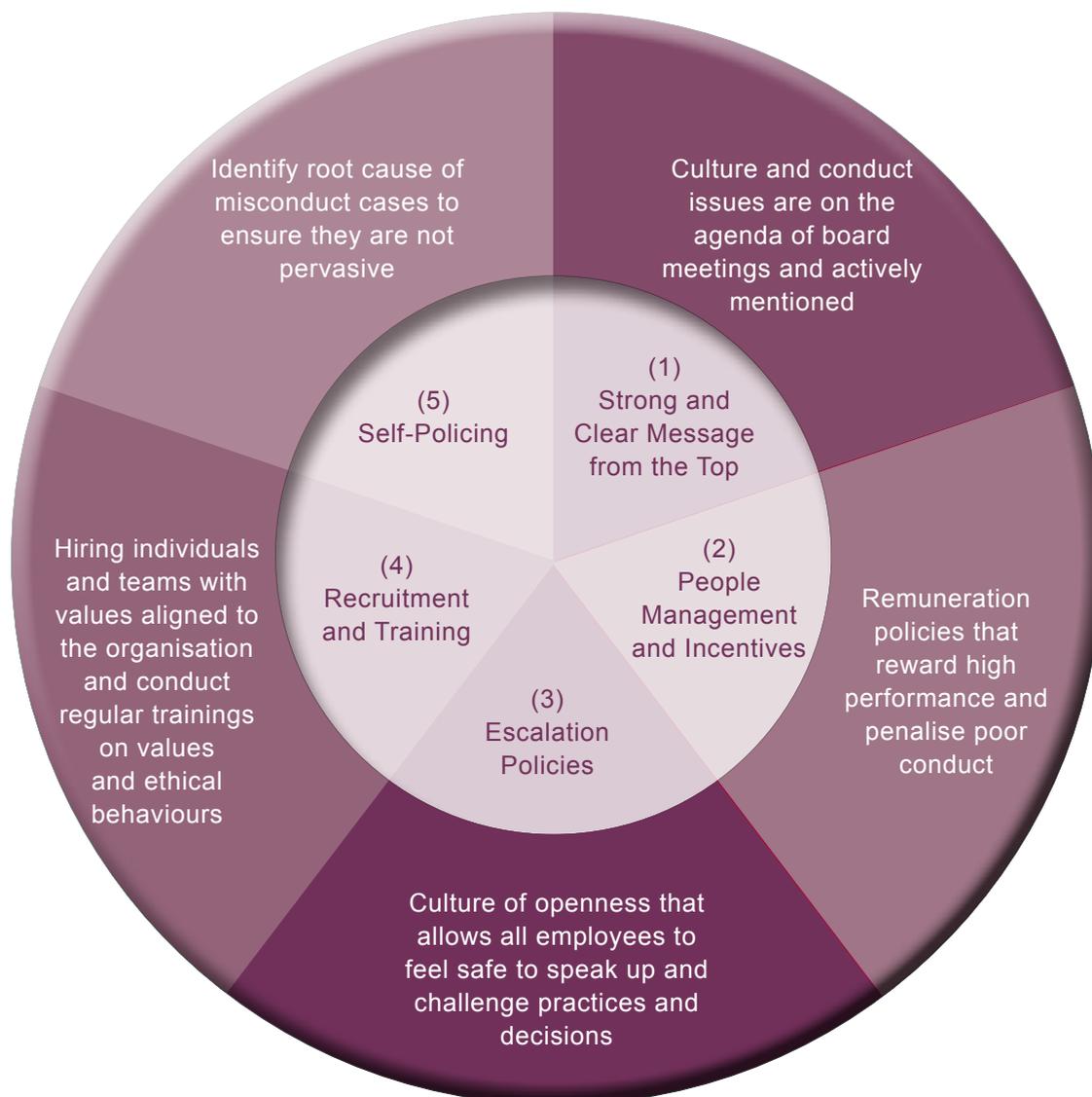
already incorporated into the professional code of ethics of doctors, lawyers and accountants.

In April 2018, the MAS issued a consultation paper that sets out guidelines to strengthen individual accountability of senior managers and to raise the standards of conduct in financial institutions (see above diagram, "Strengthening Individual Accountability").

Interestingly, these proposed regulations apply the underlying deontological principles universally. Not only are banks accountable for promoting an ethical culture, the regulators are also holding themselves accountable by going after the banks' top executives for non-compliance.

The diagram, "Promoting a Positive Culture", on the next page, summarises the key drivers that the MAS recommends banks should focus on to promote a positive ethics-based corporate culture.

## Promoting a Positive Culture



### Focus on organisational culture

Complying with AML and CFT regulations in a way that merely crosses the t's and dots the i's cannot be the end goal of any individual or company. As Richard Bredeen, former Chairman of the US Securities and Exchange, once said, "It is not an adequate ethical standard to aspire to get through the day without getting indicted."

Rather, the mission is to achieve an organisational culture that combines compliance and ethics to direct employees to do the right thing and therefore align their behaviours with the company's values. Whilst the jury is still out on how effective the recently introduced ethics-based regulatory frameworks are, they're certainly a step in the right direction. ■