NOTE AS TO EARLIER COMMENCEMENT ORDERS

(This note is not part of the Regulations)

The purpose and expected benefits of the Regulations

1. The Regulations require financial institutions to put in place systems to deter money laundering, and to assist the relevant authorities to detect money laundering activities. They are an essential part of the measures taken by the UK to implement the EC Directive on Money Laundering. Other provisions to implement the Directive are included in the Criminal Justice Act 1993. The Regulations will be made under section 2(2) of the European Communities Act 1972.

Business sectors affected

2. The Regulations will affect the financial and professional services sector. Within this sector, they will apply to:

- all banks, building societies and other credit institutions;
- all individuals and firms authorised to conduct investment business under the Financial Services Act 1986;
- all insurance companies covered by the EC Life Directives, including the life business of Lloyd's of London;
- all other undertakings carrying out any of the range of finanical activities listed in the annex to the Second Banking Supervision Directive. This includes notably bureaux de change and money transmission services.

Compliance costs

3. Costs are likely to increase in the areas of administration, training and provision of storage space for business records.

4. Administration. Institutions will be required to obtain evidence of indentity from their customers when entering into a business relationship or carrying out a transaction or series of linked transactions of ECU 15,000 or more. They will also be required to keep records of identification evidence and financial dealings for five years (the minimum period required by the Directive).

5. Some institutions may have to introduce new systems of control as a result, for example revisions of computer software, which they would not otherwise have introduced, or introduced so quickly.

6. For members of self regulatory organisations which are already required to identify customers, and for other firms which may require identification for professional reasons, the main change is likely to be in the nature of the evidence required and the time for which it must be kept.

7. Most banks and building societies, and some other financial institutions, already have well developed procedures in these areas. The cost of compliance for these firms will be relatively low.

8. Training. The institutions affected will be required to give all relevant staff initial and recurrent training in the reporting and customer indentification requirements of the Regulations, in the legislative position, and in the company's anti-money laundering policies and procedures. There will be one-off costs in producing new procedures and training manuals.

9. Provision of storage space. The record-keeping requirement will have implications for the amount of storage space needed. Records may be stored in any form that is admissible as evidence in court.

Estimated compliance costs for a "typical" business in the sectors principally affected

10. The expense incurred will depend on the nature of existing measures of control and is likely to vary considerably. Furthermore, it is difficult to produce estimates for "typical" institutions as, even within the different areas of financial services activity the Regulations will apply to a wide variety of businesses in terms of staff numbers, volume of transactions, and existing degree of money laundering compliance. The tables at the end of this assessment are derived from figures supplied by a limited number of individual institutions and trade associations. A large majority of those consulted said that they were unable to provide any firm figures for costs. However in no case was the cost of compliance raised as a general concern. Where specific features of the draft Regulations did appear to threaten the viability of particular lines of business or particular financial products, suitable amendments were made.

Total compliance costs

11. The difficulties discussed above apply even more strongly to any attempt to estimate the cost of compliance for the economy as a whole. It is necessary not only to estimate the number and sizes of the firms affected but also the degree to which they are already in compliance with the Regulations. Moreover, some of the measures needed to comply with the Regulations may coincide with steps taken to improve management or quality of service.

12. On the other side, there will be benefits to business from reducing their vulnerability to money laundering.

13. It has not been possible to produce more than very broad brush estimates based on illustrative assumptions.

— Substantial revision of computer programmes may well be needed by most medium and large institutions outside the banking and building societies area. This might affect some 500 firms, at a weighted average cost of around £40,000 each. Ongoing maintenance might be 10 per cent. of this total.

— Identification procedures will require new manuals to be produced by all but the smallest firms, at a total cost of perhaps £3 million, and the procedures may increase ongoing staff workload by perhaps 500,000 man-hours.

— Staff training might amount to some 500,000 man-hours annually, with additional total set-up costs of perhaps £5 million.

— Recurring record-keeping costs might be of the same order.

14. Allowing a margin for other costs, the total might be of the order of £30 million of initial costs and £20 million of recurring costs. This compares with total wage and salary costs alone for the banking, finance and insurance sector in 1992 of £17.2 billion.

Effects on international competitiveness

15. The Regulations require new identification procedures to be followed in transactions involving parties from non-EC countries. Some financial institutions consider that this will lead to some loss of business from non-EC customers. Amendments have been made to the Regulations to ensure that the additional procedures for dealing with non-EC customers are proportionate to the risk of money laundering involved in doing business with customers from the countries concerned.

Extent of consultation

16. Businesses were asked to give their views on the cost of the proposed Regulations in "Implementation of the EC Money Laundering Directive" H M Treasury consultation paper issued in May 1992 for comments by 31 July 1992. One thousand copies were issued to a wide range of regulatory authorities, recognised professional bodies and trade associations, and to a number of individual businesses.

17. Consultees were asked "to identify and quantify any additional direct or indirect costs (recurring and non-recurring)" that would be likely to arise as a result. Of the 60 respondents, fewer than 10 commented on costs, and only one respondent attempted to quantify them. This suggested that costs arising directly from the Money Laundering Directive were not a major cause for concern.

18. 450 copies of the draft Money Laundering Regulations were issued in November 1992, to those bodies most closely affected.

19. In June 1993 a further draft of the Regulations and a draft compliance cost assessment were sent for comment to a range of regulatory authorities, recognised professional bodies and trade associations, and were made available on request to other interested bodies.

Arrangements for monitoring and review

20. It is not intended that actual costs will be actively monitored against estimated costs, not least because of the difficulties referred to above of quantifying costs across the different sectors affected. However the effectiveness of the Regulations will be kept under review, and the compliance burden will be taken fully into account in any revision of them.

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TYPICAL COMPLIANCE COSTS

LARGE BUILDING SOCIETY	
Annual running costs:	£55m
Non-recurring costs:	
computer systems	minimal
new manuals	£10,000
training	£50,000
other	minimal
TOTAL	£60,000
% of total annual running costs	0.11%
Recurring costs:	
maintenance of computer systems	minimal
identification procedures	£16,000
training	minimal
record keeping	£7,000
other	minimal
TOTAL	£23,000
% of total annual running costs	0.04%
LARGE UNIT TRUST AND PEP PLAN MANAGEMENT COMPANY	
Annual running costs:	£35m

LARGE BUILDING SOCIETY	
Non-recurring costs:	
computer systems	£200,000
new manuals	£10,000
training	£20,000
other	minimal
TOTAL	£230,000
% of total annual running costs	0.66%
Recurring costs:	
maintenance of computer systems	£20,000
identification procedures, etc.	£50,000
training	£20,000
record keeping	£10,000
other	£50,000
TOTAL	£150,000
% of total annual running costs	0.43%
LARGE LIFE ASSURANCE/PENSIONS COMPANY	
Annual running costs:	£140m
Non-recurring costs:	
computer systems	£50,000
new manuals	£20,000
training	£100,000
other	minimal
TOTAL	£170,000
% of total annual running costs	0.12%
Recurring costs:	
maintenance of computer systems	minimal
identification procedures	£10,000
training	£20,000
record keeping	minimal
other (audit)	£15,000
TOTAL	£45,000
% of total annual running costs	0.03%
MEDIUM SIZED MOTOR FINANCE HOUSE	
Annual running costs:	£600,000
Non-recurring costs:	

LARGE BUILDING SOCIETY	
computer systems	£10,000
new manuals	£2,000
training	£1,000
other	minimal
TOTAL	£12,000
% of total annual running costs	2%
Recurring costs:	
maintenance of computer systems	£2,000
training	minimal
record keeping	£1,000
other	minimal
TOTAL	£3,000
% of total annual running costs	0.5%