
FINAL NOTICE

To: **Abbey National plc**

Of: **Abbey National House
2 Triton Square
Regent's Place
London
NW1 3AN**

Date: **9 December 2003**

TAKE NOTICE: The Financial Services Authority of 25 The North Colonnade, Canary Wharf, London E14 5HS (“the FSA”) gives you final notice about a requirement to pay a financial penalty.

1. THE PENALTY

- 1.1. The FSA gave you a Decision Notice dated 9th December 2003 which notified you that, pursuant to section 206 of the Financial Services and Markets Act 2000 (“the Act”), the FSA had decided to impose a financial penalty against you in the amount of £2,000,000 in respect of breaches of Rule 3.2.6 of the FSA's Senior Management Arrangements, Systems and Controls Sourcebook (“SYSC”) and of Rules 3.1.3 and 4.3.2 of the FSA’s Money Laundering Sourcebook (“ML”).
- 1.2. You have confirmed in a letter dated 9th December 2003 that you do not intend to refer the matter to the Financial Services and Markets Tribunal.
- 1.3. Accordingly, for the reasons set out below the FSA imposes a financial penalty on you in the amount of £2,000,000 (“the Penalty”).

2. RELEVANT STATUTORY PROVISIONS AND REGULATORY RULES

2.1. Section 2(2) of the Act includes among the FSA's regulatory objectives the reduction of financial crime.

2.2. Section 146 of the Act states:

The Authority may make rules in relation to the prevention and detection of money laundering in connection with the carrying on of regulated activity by authorised persons.

2.3. Rule 3.2.6 of SYSC states:

A firm must take reasonable care to establish and maintain effective systems and controls for compliance with applicable requirements and standards under the regulatory system and for countering the risk that the firm might be used to further financial crime.

2.4. Rule 3.1.3(1) of ML states:

A relevant firm must take reasonable steps to find out who its client is by obtaining sufficient evidence of the identity of any client who comes into contact with the relevant firm to be able to show that the client is who he claims to be.

2.5. Rule 4.3.2 of ML states:

A relevant firm must take reasonable steps to ensure that any report required by ML 4.1.2 R (1) (Internal reporting) is considered by the MLRO [Money Laundering Reporting Officer], or his duly authorised delegate, and that if, having considered the report and any relevant know your business information to which he has sought access, the MLRO, or his duly authorised delegate, suspects that a person has been engaged in money laundering, he reports promptly to NCIS.

2.6. Section 206(1) of the Act states:

If the Authority considers that an authorised person has contravened a requirement imposed on him by or under this Act, it may impose on him a penalty, in respect of the contravention, of such amount as it considers appropriate.

3. REASONS FOR THE ACTION

Summary

3.1. Prior to November 2000, Abbey National had a system of centralised monitoring of compliance with its anti-money laundering ("AML") policies and procedures. However, from November 2000, due to a re-allocation of resources, the approach was amended so that reliance was placed on a branch self-certification process. The management information that was produced by this self-certification process was not sufficient for the central MLRO function adequately to assess Abbey National's

compliance with ML and the Money Laundering Regulations 1993 (“the Regulations”).

- 3.2. In March 2003 Abbey National’s Group Internal Audit function (“GIA”) carried out a review of Abbey National's compliance with its customer identification requirements. The report identified substantial failures in the adherence to the requirements, including non-compliance rates of 32% in respect of the identification of new customers.
- 3.3. As a result of the findings in the GIA report and other concerns about the adequacy of Abbey National's AML monitoring arrangements, on 18 June 2003 the FSA appointed investigators under section 168 of the Act.
- 3.4. In addition to the substantial failures reported by GIA, the investigators identified serious failures in relation to Suspicious Activity Reports (“SARs”). Of the SARs that Abbey National submitted to the National Criminal Intelligence Service (“NCIS”) in respect of transactions occurring during 2002, over half were submitted more than 30 days after they had been reported internally to the central MLRO function, with the last one not submitted until October 2003.
- 3.5. The FSA has concluded that Abbey National has contravened SYSC Rule 3.2.6 and ML Rules 3.1.3 and 4.3.2.
- 3.6. In so doing Abbey National has demonstrated extremely serious failings that demand a very substantial financial penalty. These failings are viewed by the FSA as particularly serious in light of the following factors:
 - (1) in respect of transactions undertaken or attempted by customers in 2002, the failure to ensure that suspicious transactions were considered and reported promptly to NCIS by Abbey National’s central MLRO function demonstrated that, in the past, Abbey National had shown such a marked lack of regard for its regulatory obligations as to present a substantial risk to the FSA’s statutory objectives, including the reduction of financial crime;
 - (2) the failure by Abbey National adequately to monitor compliance with ML also demonstrated that, in the past, Abbey National had shown such a marked lack of regard for its regulatory obligations as again to present a substantial risk to the FSA's statutory objectives, including the reduction of financial crime;
 - (3) a failure rate of 32% in the identification of customers is of itself very serious;
 - (4) Abbey National's failings occurred against a background where statutory requirements for firms to have in place AML procedures, including procedures to identify their clients, had been in place for over eight years and where, in anticipation of the FSA’s new powers to make Rules relating to the prevention of money laundering with effect from 1 December 2001, there had been a greatly increased emphasis on preventing the use of the financial system for financial crime.

- 3.7. It is a cornerstone of the UK's AML regime that regulated firms must report promptly information about suspicious transactions that their customers have entered into or are attempting to enter into. An essential element of the reporting requirement is that firms obtain and keep sufficient evidence of their customers' identity to enable law enforcement to identify individuals involved in money laundering and to link them with criminal funds attempting to pass through the UK financial system. This is absolutely vital in assisting the detection, investigation and prevention of financial crime.
- 3.8. In failing to ensure that suspicious transactions are reported on a timely basis and to identify their customers properly, Abbey has potentially hindered the ability of law enforcement to detect and prosecute money launderers. Furthermore, its failure to monitor compliance adequately has left it open to abuse by money launderers and consequent reputational risk.
- 3.9. The FSA considers that Abbey's failings are indicative of wider systems and controls failings across the Abbey National Group over a prolonged period of time. The wider failings have included inadequate monitoring of key regulatory risks and inadequate identification and gathering of key management information. The overall control environment and, in particular, overall compliance monitoring has been weak across the Group.
- 3.10. The FSA notes, however, that these wider systems and controls issues are in the process of being addressed by Abbey National through a programme of review and enhancement of its control environment. Although it has decided not to take formal disciplinary action concerning these wider failings, the FSA will be closely monitoring Abbey National's performance against a strict remedial action plan that it has agreed with Abbey National and the work is to be completed within a short, defined timetable. The Abbey National Board has confirmed its commitment to ensuring the full and timely implementation of the remedial action plan.
- 3.11. The FSA also notes that Abbey National reported the findings in the GIA report to the FSA as soon as it became aware of them in April 2003 and took prompt and effective remedial action to address those findings.
- 3.12. Without those effective remedial steps and the remedial action plan now being implemented, and without the co-operation afforded to the FSA's investigation and the early settlement of the case, the financial penalty imposed would have been substantially greater.

Facts and Matters Relied On

The Statutory and Regulatory Background

- 3.13. AML requirements on financial sector firms were first imposed by the Regulations, which took effect on 1 April 1994. The Regulations require financial sector firms to have procedures for, among other things, the identification of their clients and the maintenance of records.

- 3.14. Further, from 1990 the Joint Money Laundering Steering Group, of which the British Bankers' Association is a member, provided advice on best practice in AML controls by issuing Guidance Notes for the Financial Sector ("the Guidance Notes"). Subsequent editions of the Guidance Notes took account of evolving best practice within the financial services industry. Since 1994 the Guidance Notes have provided advice and guidance on complying with the Regulations such that a court may take them into account in considering whether there has been a breach of the Regulations. Both the editions issued in 2001 reflected the provisions of ML that came into effect on 1 December 2001.
- 3.15. Prior to ML coming into force and in anticipation of the FSA's statutory objective to reduce financial crime, the FSA repeatedly stressed the importance of high standards of compliance with UK AML requirements and that, once its new enforcement powers came into effect, they would be rigorously applied to deal with breaches of ML.

Abbey National's Actions

- 3.16. Abbey National is an authorised deposit taking institution undertaking both retail and corporate banking along with a range of other permitted activities. As such it is subject to the provisions of both the Regulations and ML.
- 3.17. Prior to November 2000, Abbey National had a system of centralised monitoring of compliance with its AML policies and procedures. However, from November 2000, due to a reallocation of resources, the approach was amended such that reliance was placed on a branch self-certification process rather than centralised monitoring. Abbey National did not strengthen its arrangements for monitoring AML compliance as a result of the introduction of ML.
- 3.18. In late 2002 Abbey National commenced a programme of work to satisfy itself, among other things, that its control environment was appropriately robust. In March 2003 GIA, as part of Abbey National's wider review of its control environment, conducted a review of compliance with customer identification requirements within Abbey National's Retail banking division.
- 3.19. The field work for the GIA review was performed during March 2003 and a report was finalised on 17 April 2003, a copy of which was provided to the FSA on the same day. The GIA report identified a number of issues, including non-compliance rates of 32% in respect of new customer applications. The GIA report concluded that Abbey National's mechanisms for monitoring compliance with its AML policies and procedures were inadequate.
- 3.20. In addition, as part of Abbey National's wider review of its control environment, Abbey National appointed external advisers to undertake a Group-wide review of its compliance arrangements. In agreement with the FSA, these external advisers were also asked to review Abbey National's arrangements for AML compliance monitoring between 1 January 2001 and 30 June 2003 in order to respond to a series of detailed questions posed by the FSA as part of its investigation.

- 3.21. The external advisers' report set out the arrangements in place during that period within Abbey National's Retail banking division, which comprised:
- a Risk Management Review ('RMR') self-certification process whereby branch managers signed off on a monthly basis as to whether controls across five operational risk areas (one of which was compliance with Legal and Regulatory requirements, which included AML) were being met and submitted an annual certification to confirm that internal controls during the year were adequate and that identified failings had been addressed;
 - independent checks on the RMR process by the Channel Support Service Quality ('CSSQ') team;
 - ad-hoc GIA reviews of certain aspects of the AML arrangements.
- 3.22. The external advisers concluded that they agreed with GIA's overall conclusion about the inadequacy of Abbey National's arrangements to monitor AML compliance, because:
- (1) the self-certification process contained various shortcomings including, inter alia, insufficiently detailed reporting of the findings. It also represented a potential conflict of interest for the staff completing the certificates as the reports had a potential impact on bonuses for the areas making the reports;
 - (2) the checking of the process carried out by the CSSQ team was not adequate to address the concerns referred to in sub-paragraph (1);
 - (3) the central MLRO function received no management information about the process; and
 - (4) there was no monitoring of AML compliance by an Abbey National central control function or GIA.
- 3.23. The FSA considers that the facts described above demonstrate that Abbey National's AML compliance systems and controls were inadequate. It was therefore in breach of SYSC 3.2.6.
- 3.24. The FSA considers in addition that the conclusions of the GIA report regarding the failure of Abbey National adequately to identify its clients demonstrates that Abbey National was in breach of ML 3.1.3.
- 3.25. As part of its investigation the FSA examined SARs that Abbey National submitted to NCIS in respect of transactions undertaken or attempted by its customers during 2002. The investigators found that, of these reports, 58% of the total was submitted to NCIS more than 30 days after Abbey National's branches and other operating units had passed the SARs to the central MLRO function. A further analysis revealed that of the reports comprising that 58%:
- (1) 37.6% were submitted to NCIS between 30 and 90 days after they had been passed to the central MLRO function;

- (2) 8.4% were submitted to NCIS between 90 and 120 days after they had been passed to the central MLRO function; and
 - (3) 12% were submitted to NCIS more than 120 days after they had been passed to the central MLRO function.
- 3.26. The FSA considers that the facts described above demonstrate that Abbey National did not take reasonable steps to ensure that internal reports of suspicious activities were promptly considered or, where the central MLRO function suspected that a customer might be engaged in money laundering, that suspicions were promptly reported to NCIS. It was therefore in breach of ML 4.3.2.
- 3.27. The FSA investigation also examined concerns over the adequacy of the resources available to the central MLRO function. Any failure by Abbey National to provide adequate resources to its central MLRO function may have contributed to the breach of ML 4.3.2. However, after investigating this, the FSA has made no determination and will be taking no further action on the matter.

AML Remedial Action

- 3.28 At the time that the GIA report was finalised, Abbey National senior management developed a remedial action plan to address the issues identified. One of the actions taken was to implement, in May 2003, a new Quality Review team responsible for reviewing new account applications. Non-compliance rates have fallen significantly since the Quality Review Team assumed this responsibility. Since August 2003, non-compliance rates have been in the low single figures. At present the Quality Review Team reviews 100% of new applications; as compliance with customer identification requirements becomes more firmly embedded, this is likely to be progressively reduced.
- 3.29 Abbey National senior management have also taken prompt and effective remedial action to strengthen Abbey National's central MLRO function and to address the issues identified on SARs reporting. The recruitment of additional staff to the central MLRO function in June 2003 has resulted in, amongst other things, a significant reduction in the SARs awaiting internal consideration and, where applicable, reporting to NCIS.

4. RELEVANT GUIDANCE

- 4.1. The principal purpose of the imposition of a financial penalty is to promote high standards of regulatory conduct by deterring firms who have breached regulatory requirements from committing further contraventions, helping to deter other firms from committing contraventions and demonstrating generally to firms the benefit of compliant behaviour.
- 4.2. In determining whether a financial penalty is appropriate and its level, the FSA is required to consider all the relevant circumstances of the case. ENF 13.3.3 indicates the factors that may be of particular relevance in determining the level of a financial penalty. These are discussed below.

- 4.3. As the breaches of ML 3.1.3 also constitute a breach of the Money Laundering Regulations 1993, the FSA has considered whether the case is appropriate for a criminal prosecution. In considering this, the FSA has applied the principles set out in ENF 15.5 and in the Code for Crown Prosecutors, namely the evidential and public interest tests. Having regard to those tests, the FSA has concluded that a prosecution would not be appropriate in this case.

5. FACTORS RELEVANT TO DETERMINING THE SANCTION

- 5.1. In determining that a financial penalty is appropriate and that the amount imposed is proportionate to Abbey National's breaches, the FSA considers the following factors to be particularly relevant.

The duration, frequency and nature of the breaches

- 5.2. The failure to submit SARs promptly occurred from February 2002 to October 2003 (when the last of the 2002 SARs were submitted to NCIS).
- 5.3. The lack of adequate compliance monitoring occurred from 1 December 2001 to April 2003.
- 5.4. On the basis of the GIA findings, high rates of non-compliance with customer identification requirements were prevalent across Abbey National's Retail banking division. The inadequacies of Abbey National's monitoring of compliance before April 2003 means that it is not possible to establish the prior duration of the failings.
- 5.5. The FSA views as particularly serious Abbey National's failure to ensure that SARs were promptly considered and reported to NCIS and the failure effectively to monitor and review compliance with ML and the Regulations. Both failings are fundamental to the effectiveness of the UK's AML regime and the FSA's statutory objective to reduce financial crime.

Conduct following the contravention

- 5.6. Abbey National's senior management took prompt and effective action to address the issues raised by GIA as soon as the findings of the GIA report became known. In addition, the GIA report was provided to the FSA as soon as it was finalised.
- 5.7. On becoming aware of the FSA's intention to investigate, Abbey National's senior management demonstrated at the highest level its willingness to co-operate fully with the investigation and its desire to resolve this matter as expeditiously as possible. This has helped the FSA to work expeditiously towards its regulatory objectives, which include the reduction of financial crime.
- 5.8. Abbey National has acknowledged its wider systems and control issues across the Group, not just those concerning ML, and is undertaking promptly and effectively to remedy these issues. The FSA is monitoring this action closely.

Previous disciplinary action taken by the FSA

- 5.9. This case involves three very significant failings by Abbey National. It failed to:
- (1) report suspicious transactions to NCIS on a timely basis (ML 4.3.2);
 - (2) monitor its compliance with AML procedures, systems and controls (SYSC 3.2.6), and
 - (3) obtain sufficient evidence of the identity of its customers (ML 3.1.3).
- 5.10. The FSA has had regard to previous cases involving breaches of ML. While there are precedents for firms failing to identify clients, there has been no previous disciplinary action in respect of the other breaches. The cumulative effect of the three breaches is such that the seriousness of this case is far greater than those cases involving a single type of breach. The case also demonstrates the marked lack of regard for its regulatory obligations that Abbey National had shown in the past.
- 5.11. Each of the breaches individually merits a substantial penalty. Taken together, they justify a very high penalty.

6. CONCLUSION

- 6.1. Abbey National has demonstrated extremely serious control failings in respect of its AML procedures which occurred within the context of weak compliance controls across the Group. In particular the failure to report SARs on a timely basis undermines a crucial aspect of the UK's AML regime.
- 6.2. The serious nature of the AML breaches and the risk they posed to the FSA's statutory objective to reduce financial crime demand that a very substantial financial penalty be imposed in this case. Without the effective remedial steps taken by Abbey National after April 2003 and the action described in paragraph 5.8, and without the co-operation afforded to the investigation and the early settlement of the case, the penalty would have been substantially greater.
- 6.3. In all the circumstances the FSA has decided to impose a financial penalty of £2,000,000.

7. IMPORTANT NOTICES

- 7.1. This Final Notice is given to you in accordance with section 390 of the Act.

Manner of payment

- 7.2. The Penalty must be paid to the FSA in full.

Time for payment

- 7.3. The Penalty must be paid to the FSA no later than 23rd December 2003, being not less than 14 days beginning with the date on which the notice is given to you.

If the penalty is not paid

- 7.4. If all or any of the Penalty is outstanding on 23rd December 2003, the FSA may recover the outstanding amount as a debt owed by you and due to the FSA.

Publicity

- 7.5. Sections 391(4), 391(6) and 391(7) of the Act apply to the publication of information about the matter to which this notice relates. Under those provisions, the FSA must publish such information about the matter to which this notice relates as the FSA considers appropriate. The information may be published in such manner as the FSA considers appropriate. However, the FSA may not publish information if such publication would, in the opinion of the FSA, be unfair to you or prejudicial to the interests of consumers.
- 7.6. The FSA intends to publish such information about the matter to which this Final Notice relates as it considers appropriate.

FSA Contact

- 7.7. For more information concerning this matter generally, you should contact Andrew Bradley at the FSA (direct line: 020 7066 1450 /fax: 020 7066 1451).

Brian Dilley
Head of Deposit Taking and Financial Stability
FSA Enforcement Division