
FINAL NOTICE

To: **The Governor and Company of the Bank of Ireland**

Of: 36 Queen Street
 London
 EC4R 1HJ

Date: 31 August 2004

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 on 26 August 2004 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 £375,000.
- 1.2. You confirmed on 27 August 2004 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 £375,000 (“Penalty”).

2. REASONS FOR THE PENALTY

- 2.1. In the period from December 2001 to May 2003, the Bank of Ireland (“BoI”) breached SYSC 3.2.6 by failing to take reasonable care to establish and maintain effective systems and controls to counter the risk that BoI’s bank drafts facility might be used to further financial crime and for ensuring that staff understood their anti-money laundering responsibilities in relation to the recognition and reporting of suspicious transactions.

2.2. BoI demonstrated serious failings in that:

- (1) BoI failed to take reasonable steps to detect the misuse of the bank drafts facility provided by a BoI branch (“the Branch”). The misuse concerned forty bank drafts issued between 1998 and 2002 worth approximately £2,000,000. These bank drafts were issued for cash at the request of one of the Branch's largest customers (“the Customer”). All 40 bank drafts were made payable to “Bank of Ireland”. These transactions were in breach of BoI's policy and procedures. Issuing bank drafts in this manner disguised the identity of the beneficial owner of the cash and, as such, was an effective means of laundering money. These transactions were not identified as suspicious by staff at the Branch or by other managers who were aware of the transactions.
- (2) The systems and controls employed by BoI to monitor the issuing of bank drafts at BoI branches were inadequate despite bank drafts being identified by BoI as a potential method of money laundering in 1994. In particular, these controls did not require a full assessment of whether bank drafts were issued in accordance with BoI’s policies and procedures.
- (3) BoI did not take appropriate steps to ensure that it had in place a system to check that staff had understood the money laundering training that was delivered to them, specifically that they had sufficient understanding to recognise and report suspicious transactions. The FSA accepts that the content of the training provided to staff was adequate.
- (4) There was a high risk that these transactions could have been used to facilitate money laundering. The circumstances in which the bank drafts were issued have resulted in an investigation by the appropriate law enforcement agency.

2.3. The FSA recognises that, although the systems to prevent the misuse of drafts and to ensure staff understood their anti-money laundering responsibilities were the same across BoI's branch network, the material misuse of drafts only occurred at the Branch. The FSA considers that the failures demonstrated by the Branch are a material breach of SYSC 3.2.6.

3. RELEVANT STATUTORY PROVISIONS AND REGULATORY RULES

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

3.2. Section 138 of the Act authorises the FSA to make rules applying to authorised persons with respect to the carrying on of their business.

3.3. 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.

3.4. 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.

4. FACTS AND MATTERS RELIED ON

The Statutory and Regulatory Background

- 4.1. Anti-money laundering requirements on financial sector firms were first imposed by the Money Laundering Regulations 1993 (“the Regulations”), which took effect on 1 April 1994. The Regulations require financial sector firms to have, amongst other things, such procedures of internal control and communication as may be appropriate for the purposes of forestalling and preventing money laundering.
- 4.2. Further, from 1990 the Joint Money Laundering Steering Group, of which the British Bankers Association is a member, provided advice on best practice in anti-money laundering 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.
- 4.3. The FSA has repeatedly stressed the importance of effective anti-money laundering controls and has on five previous occasions taken disciplinary action against regulated firms for failing to meet the FSA's anti-money laundering requirements.
- 4.4. It is fundamental to the health of the United Kingdom’s financial services industry that firms establish and maintain effective systems and controls for countering the risk that their products and services might be used to facilitate money laundering.
- 4.5. Firms are required to take special care in relation to high-risk products and services, such as cash transactions. A complete audit trail over the source of funds being placed in the financial system is vital in assisting the detection, investigation and prevention of financial crime. Adequate controls over the entry of cash into the financial system are particularly important.

Bank of Ireland’s Actions

- 4.6. BoI is an authorised deposit taking institution undertaking both retail and corporate banking along with a wide range of other permitted activities.

Issuing of bank drafts for cash

- 4.7. Between January 1998 and October 2002, the Branch issued 40 bank drafts to the Customer. Each bank draft was made payable to “Bank of Ireland” and not to the Customer or to a third party. These transactions meant that BoI was making a payment to itself. The way these transactions were structured was contrary to BoI's internal policy. There was no obvious business reason for the Customer to request a bank draft made payable to BoI.

- 4.8. The bank drafts were exchanged for cash and the total value of these transactions was approximately £2,000,000. Each transaction involved a substantial cash deposit and was outside the normal business activity of the Customer. The cash deposits did not pass through the accounts of the Customer held at the Branch, which was not in line with BoI's policy.
- 4.9. The cash used to purchase bank drafts was deposited in the “drafts outstanding account” of the Branch, an internal account used to pay bank drafts issued by BoI when they were redeemed. When the misuse of bank drafts was discovered in March 2003, drafts to the value of £1.8 million issued to the Customer remained outstanding.
- 4.10. This practice allowed the Customer to use the drafts outstanding account at the Branch as a deposit account; an arrangement which may have resulted in BoI being unable to establish the beneficial owner and source of the funds. In the event that BoI was asked by law enforcement to produce details of transactions undertaken by the customers, it is possible that the cash for drafts transactions would not be identified. In addition, the Customer made clear on a number of occasions to staff at the Branch that the Customer's name was not to be used on cheques or correspondence relating to the draft transactions.
- 4.11. In 2002, BoI managers outside the Branch became aware of the circumstances of the transactions, but did not identify the transactions as suspicious.

Control failings

- 4.12. During this period, in addition to the normal internal controls operated by line management, BoI relied on the supplementary control of an annual peer review by staff of other branches (the Risk Assessment Programme). BoI's Group Audit Department (Group Audit) also conducted periodic reviews to assess the internal control environment in the branch.
- 4.13. However, BoI's systems and controls failed to detect the misuse of the bank drafts facility until it was identified during a branch audit in March 2003. In particular, these failed to ensure that the bank drafts facility was not used in a manner contrary to BoI's own policies and procedures and that staff sufficiently understood their anti-money laundering responsibilities in relation to the recognition and reporting of suspicious transactions.
- 4.14. The Risk Assessment Programme was ineffective in that:
- (1) staff responsible for carrying out the programme were not instructed to examine the drafts outstanding account of a branch for non-compliance with BoI's own policies and procedures. The reviews therefore did not detect that the bank drafts had been made payable to BoI or that the funds used to purchase the bank drafts did not pass through the Customer's account;
 - (2) staff were not required to and did not follow up bank drafts that were outstanding for more than six months even though these were recognised as higher risk and were recorded on a separate register which identified that bank drafts had been made payable to “Bank of Ireland”; and

- (3) whilst the Risk Assessment template instructed assessors to gather evidence of compliance with anti money laundering procedures, including whether staff were aware of checking for suspicious transactions, the awareness of staff at the Branch was not adequately tested. The assessors relied on adequate account opening information as evidence of staff compliance with and understanding of their money laundering obligations.
- 4.15. The Group Audit undertook an audit review of the Branch in 2000 (“the 2000 Audit”) which included a review of the drafts outstanding account. However, the review was ineffective in that:
 - (1) it did not adequately investigate draft transactions; and
 - (2) it did not adequately test the effectiveness of the money laundering training provided to BoI staff and in particular whether staff had sufficient understanding to recognise and report suspicious transactions.
- 4.16. Adequate checks were not built into independent branch reviews or Group Audit work programmes until 2002, when the Audit programme was amended. Thus, the controls did not detect the misuse of the drafts account until the 2003 Audit of the Branch, by which time the practice had been occurring for 4 years. This occurred despite cash for drafts being highlighted by BoI as a potentially suspicious transaction in 1994.

5. CONCLUSIONS AS TO BREACH

- 5.1. The facts and matters described in paragraphs 4.7 to 4.16 demonstrate that BoI did not take reasonable care to establish and maintain effective systems and controls over the issuing of bank drafts and for ensuring that staff understood their anti-money laundering responsibilities in relation to the recognition and reporting of suspicious transactions.
- 5.2. BoI is required to 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. In failing to do so in those areas identified by this Notice, BoI contravened SYSC 3.2.6.

6. FACTORS RELEVANT TO DETERMINING THE PROPOSED SANCTION

Relevant guidance on sanction

- 6.1. 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.
- 6.2. 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. The FSA considers the following factors to be particularly relevant.

The duration, frequency and nature of the breaches

- 6.3. Potentially suspicious transactions were undertaken between January 1998 and October 2002 and were not recognised or detected until the 2003 Audit of the Branch. During this period BoI did not have arrangements in place to ensure that staff understood their anti-money laundering responsibilities in relation to the recognition of suspicious transactions. During the same period the arrangements established by BoI contained inadequate checks to detect misuse of bank drafts. This demonstrates that control inadequacies existed for at least four years.
- 6.4. The bank drafts, each issued contrary to BoI policy, had a total value of approximately £2,000,000. The total value of these potentially suspicious cash transactions demonstrates the serious nature of the breaches.
- 6.5. The circumstances in which the bank drafts were issued have resulted in an investigation by the appropriate law enforcement agency.

Conduct following the contravention

- 6.6. The FSA notes that, since discovering the breaches, BoI has devoted significant resources to investigating the matter and ensuring that the misuse was not replicated elsewhere in the branch network. A number of reviews have been undertaken including a review of the processing of drafts across the UK branch network and an independent review of BoI's anti-money laundering policies and procedures. BoI has also introduced a requirement that drafts outstanding for longer than 6 months and with a value in excess of £10,000 be subject to oversight independent of the issuing branch. BoI has also taken steps to introduce a revised training programme that involves checking that staff understand their responsibility to recognise and report suspicious transactions.
- 6.7. BoI afforded the FSA good co-operation during the investigative phase of this matter.
- 6.8. BoI has taken steps to settle this matter. This has helped the FSA to work expeditiously towards its regulatory objectives, which include reducing financial crime.

Previous action taken by the FSA

- 6.9. The FSA has had regard to previous cases involving breaches of SYSC and ML. The FSA considers that some of the aggravating factors present in those cases are not evident in this case to the same degree and that, where previous cases involved failings demonstrated across business units and branches, the weaknesses in BoI were only demonstrated in one branch.

Conclusion

- 6.10. Taking into account the seriousness of the contraventions and the risk they posed, but also having regard to the remedial steps taken and the co-operation shown, the FSA proposes to impose a financial penalty of £375,000.
- 6.11. The FSA considers the sanction to be a proportionate exercise of its enforcement powers and consistent with the FSA's publicly stated policies

7. MANNER OF PAYMENT

7.1. The Penalty must be paid to the FSA in full.

8. TIME FOR PAYMENT

8.1. The Penalty must be paid to the FSA no later than 14 September 2004, being not less than 14 days beginning with the date on which this notice is given to you.

9. IF PENALTY NOT PAID

9.1. If all or any of the Penalty is outstanding on 14 September 2004, the FSA may recover the outstanding amount as a debt owed by you and due to the FSA.

10. IMPORTANT NOTICES

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

Publicity

10.2. 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.

10.3. The FSA intends to publish such information about the matter to which this Final Notice relates as it considers appropriate.

FSA contacts

10.4. For more information concerning this matter generally, you should contact William Amos at the FSA (direct line: 020 7066 1324 /fax: 020 7066 1325).

Ian Mason
FSA Enforcement Division