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Crime-money, reputation and reporting

Jackie Harvey · Siu Fung Lau

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Abstract The emphasis of government legislation on money laundering has been based on the assumption that reporting institutions are able to spot deviant customer behaviour and that implicitly such behaviour is criminal. This paper looks at the drivers for reporting of suspicious or unusual activity, in particular, focusing on the principle of reputation. It considers the evidence over bank disclosure within annual published reports with respect to their money laundering compliance activity; particularly examining whether there was any change in disclosure and hence reputation management reporting by those banks fined by the regulator for lapses of compliance. An attempt is also made to apply the principles of legitimacy theory to evaluate the association between money laundering and reputation looking for evidence of a 'virtuous cycle of compliance'. However, the findings point to limited public awareness of money laundering and to the adoption of a deficit rather than enhancement model of reputation management.

Imagery, rhetoric and ill-guided activism

Governmental efforts to counter money laundering are justified by the argument that they are required in order to preserve the reputation and integrity of the financial system [17]. This belief is most consistently espoused by the IMF who notes that money laundering can "*harm the soundness of a country's financial sector as well as the stability of individual financial institutions*" [31, p II-4]. The current approach to legislating against money laundering is justified on the grounds that it helps to make the UK less attractive to potential launderers "*protecting the financial sector from operational and reputational risks*" [18, Ch. 9, p. 1]. Van Duyne [35, p. 1] draws attention to the new enemies of the financial system as being those "*who do not take moneys[sic] out of the financial system; but bring these into it*"; the focus being very much on the potential damage inflicted by tainted money co-mingling with legitimate funds. However, if, after more than a decade of anti-money laundering

J. Harvey (✉) · S. F. Lau
Newcastle Business School, Northumbria University, Newcastle upon Tyne, UK
e-mail: jackie.harvey@northumbria.ac.uk

legislation the threat rhetoric pervades, then surely financial systems, as pointed out by van Duyne et al. [34], should be on the point of collapse from the effect of so much cross-contamination. The authors also argue convincingly that past bank losses have resulted from operational risk rather than an exclusive influx of crime-money and suggest that arguments over integrity and reputation should be seen as "*mere rhetoric*". They go on to suggest that integrity is important not from the point of view of the source of the funds but because of the trust bestowed in the bank by its customers that it will properly handle their funds irrespective of whether they are criminal or of honest intent [15]. Reuter and Truman [28, p. 60] make the valid observation that "*Banks... are quasi-public utilities, and the public does not want them to be directly involved in handling dirty money*", however, money laundering will only become a public issue when customers lose money [3, 17].

These monies once in the banks, irrespective of provenance, do not lie as cash deposits but form part of the liability base to be used in their normal asset creating activity, contributing to the legitimate expansion of the economy. Geiger and Wuensch [9] remind us that money cannot be classified on the basis of observation as being either tainted or clean as by definition it is abstract, performing its time honoured role of being a store of value and means of exchange. Ross and Hannan [29] offer the suggestion that the activity of moving illegally acquired funds through a bank will be by way of systems and procedures that are entirely legal. Thus the tag of laundering becomes attached by association with something else that is perceived to be illegal. It is, therefore, appropriate to establish that integrity of the financial system is built on trust and it is this element that contributes to reputation, not the fact that criminals might maintain bank accounts.

Banks have always had sufficient incentives to avoid finding their names linked with undesirable elements such that there is already an intrinsic motive for 'due diligence' [17], enforced by existing criminal legislation. This desire can be seen as being a sufficient motive for keeping the financial institution clean without the additional layer of anti-money laundering measures [3]. It would appear that in the absence of evidence relating to the size of the laundering phenomenon, legislation has been based on rhetoric rather than fact [16]. This has the consequence that it is being driven by ill-guided activism responding to the need to be "seen to be doing something" rather than by an objective understanding of its impact on predicate crime.

Does the existence of tainted funds affect the ways banks operate? The answer to this has to be an emphatic 'no'. Indeed, for the most part they will be completely oblivious to the existence of criminal funds irrespective of obligations to report suspicious activity in their role as government created regulatory intermediary. Indeed, Alexander [2] notes that the regulatory authorities have elected to use banks to combat money laundering activity on the assumption that laundering activity will be evidenced via some unusual or anomalous account transaction that the banks will be able to detect through their 'inside knowledge' of all financial transactions. It is, without doubt an immense task to pick out the illegal from the multitude of legitimate financial transactions that pass through the system, this point being made almost a decade ago by Hampton and Levi [13].

Evidence suggests that measures are perceived as too severe relative to the risk of money laundering and that compliance is sanction avoiding rather than viewed as

good business practice [36]. This is an important observation, suggesting that banks are merely going through the procedures as evidence of compliance rather than in the expectation of unearthing criminal activity.

Reputation and the "virtuous cycle of compliance"

Far from being an objective construct, reputation is, like beauty, in the eye of the beholder and thus not easily defined (refer to [14, p336]. It is not the purpose of this paper to address this deficiency in the literature but to explore the extent to which banks perceive money laundering as a risk to reputation.

There is little doubt that for a bank, damage to reputation will result in tangible losses being incurred. This is because reputational damage is often linked to, or is the result of, a perceived impairment in the bank's financial soundness. The immediate manifestation of this is likely to be through the actions of depositors as they move to withdraw their funds, as well as from bank counterparties who withdraw lines of credit. Such actions ultimately translate into a withdrawal of shareholder support and subsequent negative impact on the share price. As suggested by Harvey [14], "*It may be assumed that in order to offset these costs, financial institutions will be prepared to spend effort and resources (the tangible operational costs) to prevent, control and insulate the institution from such tangible losses*".

Cost associated with compliance with anti-money laundering legislation is justified by the belief that non-compliance will damage reputation with a consequent loss of business, even if the involvement of the institution is unintentional. Indeed, respondents to interviews reported by the principal author [17] and included in Table 1 below, noted that reputation was linked to compliance, or more significantly that there was a perceived risk of reputation damage that would arise from non-compliance.

The relevant question to pose, however, is exactly where the association with money laundering fits on the risk scale in the overall risk assessment exercises routinely carried out by banks as part of their operational risk management control processes. Within most financial institutions the usual approach is to model risk by reference to a quantifiable loss associated with probability of risk occurring, such as with value at risk (VaR) models. In so doing the bank effectively asks itself two questions: firstly, how likely is it that the bank might unwittingly facilitate the actions of money launderers? Secondly, in the event that it does, how great would be the negative impact on its reputation? Depending on the answer, and consistent with Harvey [14] above, it would be expected that the normal profit-maximising firm would spend on counter-money laundering compliance only up to the point that the costs incurred are equal to the estimated value placed by the firm on its reputation. Two observations flow from this hypothesis:

1. Firms must be able in some way to quantify the value of their reputation
2. Firms must see a positive link between such compliance and reputation.

In the event that banks view the potential negative impact of association with money laundering to be significant, one might expect to find evidence, as suggested by Harvey [17] of a 'virtuous cycle of compliance'. This implies that banks can see

Table 1 Views on reputation

Respondent	Organisation	Comment regarding reputation
Interviewee 1	Bank	"*Reputation risk is paramount, we do not want to be associated with terrorist financing*" Expenditure on compliance "*was being driven by reputation risk but evidence is that fines do not damage reputation. Reputation risk was only the fear of being fined*".
Interviewee 3	Self regulatory body	"*The risks arising from failure to comply are the financial hit of regulatory damage and the smaller reputational damage together with the threat of jail for their staff*" "*Reputational risk damage so far has been contained as many other institutions have the view 'there but for the grace of God*'"
Interviewee 4	Stock broker	"*The reputational benefits are huge. Paine Webber was fined £350.000 but lost business resulted in its closure ...the reputational costs provide sufficient incentive to comply*".
Interviewee 7	Bank	"*public sanction and reputation damage is enormous... it focus*[es] *the minds of managers on the undesirability of FSA enforcement—investigation is very time consuming—18* months *and that is a huge cost to business. If it goes wrong there is a six figure fine. Financial institutions rely on having a good name; within* [name of bank] *this would be viewed as extremely damaging and serious…this would have a huge impact irrespective of whether we lost customers as a result*".
Interviewee 8	Law enforcement agency	"*Reputation risk is an issue. We have seen a tightening in* [name of fined bank] *in respect of compliance*".
Respondent A	Building society	Benefits of compliance are: "*Protection of reputation*".
Respondent C	Stock broker	Benefits of compliance are: "*compliance with our regulators and secure reputation*".

Harvey [14, 17]

benefit to their reputation in being viewed as more compliant than their competitors. If this was the case then it would be expected that as part of their stakeholder management, information about their anti-money laundering controls and procedures would be made public as an enhancement to reputation. Strangely, however, firms are reluctant to divulge the amount being spent on compliance. Harvey [14] surmised that this might arise from firms viewing compliance as an external cost and as such outside the immediate control of management. This could be a result of a general reluctance for financial institutions to disclose or share information regarding amounts spent on compliance as such expenditure is viewed as a cost overhead rather than providing benefit via enhancement to reputation [20].

This line of reasoning was also applied by Geiger and Wuensch [9] who indicated that banks apply anti-money laundering rules in order to foster their own 'reputation' giving due consideration to minimising risk. However the authors note that the precise definition of reputation risk and hence its subsequent measurement is problematic simply because it would appear impossible to distinguish and hence separate reputation risk linked to money laundering from risks arising from other aspects of the bank's operations. As already noted, most risk management models operate on the basis that the institution is able to quantify the extent of loss that would arise in the event that that the risk occurs. However, this is not possible to do for money laundering. They draw attention to some interesting findings, noting that banks

consider compliance with anti-money laundering legislation as essential and important, however that implementation is costly. Of interest here, however is the observation (p. 91) that the impact of anti-money laundering rules on predicate offences is small. This has resulted in the ludicrous situation highlighted by Harvey [14] of banks using the number of SARs submitted to the regulators as an internal measure of performance.

Geiger and Wuensch [9] suggest that there may even be evidence of banks transferring risk decision making to the regulators simply by filing SARs (p. 100). Such an observation is consistent with Harvey [14, 17], Levi and Reuter [23], and Gill and Taylor [10] all of whom have drawn attention to the tendency to report everything that might appear merely unusual in order to achieve the regulatory equivalent of 'covering their backs'. Issues relating to the gate keeping function of financial institutions are also considered by Ross and Hannan [29, p.106] ".. *the requirements on agencies imposed by the risk-based approach involve a significant element of uncertainty*". They make the point that the advantage for the regulators is that the risk-based approach transfers responsibility for interpretation of the regulations to the financial institutions. One gets the distinct feeling that rather than our virtuous cycle of compliance we have instead a less than virtuous shifting of responsibility.

Reputation risk or fear of non-compliance?

From the forgoing, it might be deduced that the whole discussion of reputation and compliance could be viewed from a deficit rather than enhancement perspective. In other words, measures are put in place to avoid censure (deficit model of compliance) rather than as an enhancement to reputation (enhancement model of compliance). It is, therefore, interesting to further explore the concept of reputation by returning to the content of a number of interviews conducted by the principal author with a range of financial institutions and other relevant bodies. The method employed and extracts from this research are reported in Harvey [14, 17]; however reproduced here (Table 1 above) are all comments in which the word 'reputation' was mentioned. This information is drawn jointly from eight interviews and from 17 responses to a pilot questionnaire giving a total sample size of 25. From this, as shown in the Table, only seven made comments about reputation. This would appear to reinforce the view that compliance is seen to prevent any negative impact on, rather than as a positive enhancement to, reputation. This is significant because it is possible that this perception provides an explanation for the type of information that banks will choose to disclose within their public documents. The implication is that banks will do what is needed to retain their reputation at its existing level rather than engaging with self-promotion with this compliance theme. If this is the case, it should be expected that there will be little to find within annual reports and accounts other than that required by statutory duty.

Theoretical arguments over bank disclosure

If indeed, there is a link that can be established between anti-money laundering activity and a bank's reputation, it might reasonably be underpinned by reference to

academic theory. The focus of this work is to consider the evidence over bank disclosure within annual published reports with respect to their money laundering compliance activity; particularly examining whether there has been any change in disclosure and hence reputation management by those banks fined by the regulator for lapses of compliance. It is thus appropriate to consider both disclosure and legitimacy theories.

Disclosure theory indicates that banks, as highly visible firms, should be more likely to provide information on their activity in order to demonstrate a higher level of corporate citizenship [6, 19, 32].

Legitimacy theory would indicate that as banks are bound by money laundering legislation one should expect a high level of good quality disclosure on their anti-money laundering activity. Bank decisions over disclosure are taken in order to establish their legitimacy in the eyes of their stakeholders. Since legitimacy '*resides in the public opinion*' [5, p. 514] a firm must gain, maintain or repair [26, 33] its legitimacy by satisfying its stakeholders. It follows, therefore, that any challenge to their legitimacy would result in a bank increasing the level and quality of this disclosure.

Companies use their annual reports as a way of providing information and data (both mandatory and voluntary) in a way that enables its stakeholders to interpret its performance and integrity within the community. O'Donovan [25, cited in [26]] noted the use of the annual report by management as a way of correcting misconceptions the public may have formed about a company. It is also seen as the '*main disclosure vehicle*' [24, p. 196].

There is a tendency for legislative requirements and compliance to have a self-reinforcing effect. For example, an increase in media attention focussed on banks fined for insufficient compliance with money laundering regulations could lead to further regulation, particularly where policy makers feel the need to be seen to 'do something' which in turn could lead to a further increase in public awareness. This being the case it might be expected to find a strong correlation between public awareness and content of anti-money laundering statements within bank annual reports. Further *a prior* expectation would be to find an increase in reporting undertaken by firms that were fined for anti-money laundering breaches of compliance as part of 'impression management', contributing to improvement of public perception.

In the event that banks view their anti-money laundering activity as a positive enhancement to reputation it would be reasonable to expect greater disclosure of this activity. More importantly any association in the minds of stakeholders between money laundering and reputation would move banks to adopt an enhancement approach to compliance as providing evidence of a 'virtuous cycle of compliance'. However, if banks only undertake the minimum required to avoid regulatory sanction they are instead operating the deficit model.

Public awareness

Public awareness: there is no proper definition, neither for 'public' nor for 'awareness'. For the purposes of this study it is assumed that a suitable proxy measure of awareness is the media coverage, for the media reflect as well as create public awareness. Therefore, changes in media attention, for our purpose concerning

money laundering, is taken as changes in public awareness. In terms of disclosure, it is expected that an increase in media coverage raises public attention to the issue. Consequently, as a mean of response to the public, banks will signal to stakeholders through annual reports and accounts and by press releases to the media its 'good conduct' by drawing attention to or disclosing the amounts of money spent on compliance as an indicator of the 'cleanliness' of their bank. As a further signal of good practice these banks will wish to disclose increased amounts of information to the media about their compliance with anti-money laundering legislation. Ashford and Gibbs [4] found that proactive actions can 'extend' legitimacy '*as management attempts to win the confidence and support of wary potential constituents*' (p. 180). Of course all of this needs to be set against the evidence of a 'communications gap' [36, p. 50] over public concern with money laundering, such that public awareness remains low.

It is acknowledged that public perception is reflected in a wide range of media, however, for this study the focus is on written newspaper articles, it being reasonable to assume that newspapers will report on matters of public interest and attention. The test material was collected by conducting two searches of the LexisNexis News and Business Database using the search term "money laundering" in the article's title over each of the years for which data is available. This search produced the information contained in Table 2 below.[1] The first focused on the global data base which provided an indication of the number of articles published that contain the phrase 'money laundering' in the title, in all news and business publications across the globe. A second search applying the same criteria was based solely on the UK National Newspapers.

This Table, together with the associated Fig. 1 below, indicates a steady rise in the numbers of articles written on money laundering on a global basis over the period 1980–1990 with a pronounced increase in the period 1999–2001, peaking in 2001. There has been a decrease in reporting in recent years but with a second peak occurring in 2005. It can be seen that the level of reporting is significantly lower in the UK although there is a discernable increase in the same period with a matched decrease in reporting in recent years (except for 2004 and 2005). This seems to support the observation that money laundering may not be a significant issue as far as the British 'public' is concerned. That said, if as would be expected under legitimacy theory, banks are responsive to public awareness as an indicator, they might have increased their disclosure on anti-money laundering within their report and accounts, particularly around the period 2001 and again in 2005.

Content analysis

A rigorous method of qualitative analysis of the content of the annual report is provided via the application of content analysis. Powell [27, p.50] describes content

[1] Although the data base is available for every year during the 1980s, due to the very limited coverage of money laundering during the decade, only selected years are provided here. There is no apparent explanation for the disparity between the UK and the global data that occurs in 1984 nor for the drop in coverage in the UK in 2004. Both of these were checked and appear to be accurate.

Table 2 Number of money laundering articles published in news and business publications by year for the period 1980–2007

Year	Number of hits "Money Laundering" from all newspapers around the world	Number of hits "Money Laundering" from UK national newspapers
1980	0	0
1981	1	0
1984	24	28
1985	82	2
1987	68	1
1990	278	22
1991	224	6
1992	168	5
1993	237	5
1994	410	21
1995	423	11
1996	511	11
1997	596	22
1998	973	30
1999	1761	77
2000	1672	60
2001	2727	112
2002	2553	58
2003	2410	64
2004	2118	7
2005	2763	60
2006	2597	36
2007 (to November 16th)	2236	39

analysis as providing '*a systematic analysis of the occurrence of words, phrases and concepts.*', whilst Krippendorff [21, p.21] notes its value as "*a research technique for making replicable and valid inferences from data according to their context.*"

The most common methods of content analysis focus on volumetric studies that include: word or sentence counting; page proportioning; frequency disclosure; and instance counting. The justification for this approach is based on the argument that '*the extent of disclosure can be taken as some indication of importance of an issue to the reporting entity*' [21, p. 180]. The problem associated with all such quantitative based methods is, however, that whilst they might be accurate and reproducible, they give no indication as to the overall depth or quality of the narrative. Therefore, some authors have used several methods of content analysis [7, 30] in analysing their data, making use of various coding methods, checklists, instruments and decision rules [11, 12], although it is recognised that within this approach there is an implicit subjectivity in relation to the creation of content categories.

An earlier study by the second author, [22] conducted an initial content analysis on the six largest UK banks: Royal Bank of Scotland (RBS); Barclays; Halifax Bank of Scotland (HBOS); Lloyds TSB; Standard Chartered and Northern Rock for the period 2000–2005. This work employed a simple quantitative approach by word counting and sentence counting in relation to a content category of 'money laundering'. His findings, reproduced in Table 3 below, indicate that very little, and indeed frequently nothing, is said on the matter of money laundering.

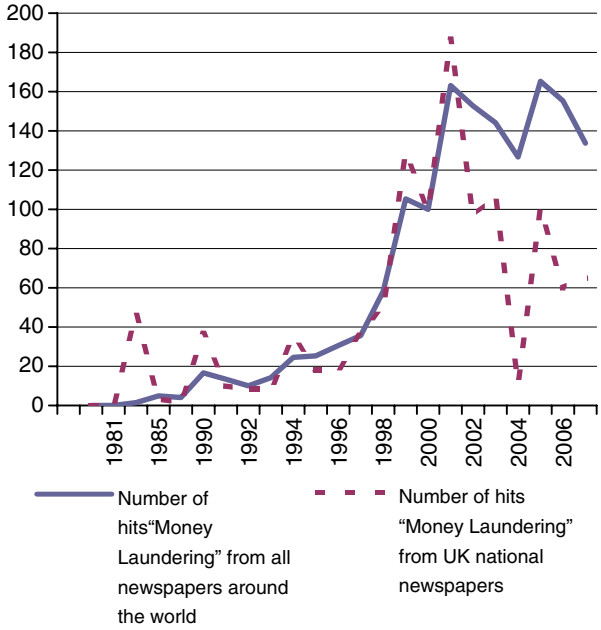

Fig. 1 Number of money laundering articles published in news and business publications by year for the period 1980–2007. *Data is shown as an index with the year 2000 = 100*

It is interesting to consider evidence of any relationship between public perception, as proxied by reporting within the UK National press, and the average number of words used by each bank in relation to its disclosure about money laundering within the annual report, as indicated in Table 3. This is presented in Fig. 2 below. Superficially, the results do appear to lend some support to the theories of disclosure. However, whilst the peaks in media and hence 'public awareness' occurred in 2001 and 2005, the significantly smaller peak in reporting of money laundering by banks appeared to be lagged in 2002 whilst being more coincident in 2005. This represents a very small if not absent correlation between 'public awareness' and disclosure by banks. What we seem to have found is limited awareness of money laundering and minimal reporting by banks.

Evidence on bank disclosure—what is said about anti-money laundering activity

Extending upon the work of Lau [22] and including an additional bank; the findings presented here are based on an analysis of the annual report and accounts for the period 2001–2005, for seven UK banks that were selected on the basis of market capitalisation. They included: Barclays; Halifax Bank of Scotland (HBOS); Hong Kong Shanghai Banking Corporation (HSBC); Lloyds TSB; Northern Rock; Standard Chartered; and Royal Bank of Scotland (RBOS).

Table 3 Total "money laundering" disclosure by the six banks

Year	Total number of words	Average number of words per bank	Total number of sentences	Average number of sentences per bank
2000	0	0	0	0
2001	9	1,5	1	0
2002	374	62	16	3
2003	136	23	6	1
2004	239	40	8	1
2005	469	78	20	3

Lau [22]

It could be argued that those banks that are better at risk management will want to signal their superior risk management abilities to the market place via disclosures in the annual report. This will take the form of written statements about their money laundering compliance activity. For those banks that are committed to '*good practice*' in their procedures [8] disclosing such information to the public could signal their efforts in combating money laundering. Ahmed and Courtis [1] showed that banks with higher levels of risk have a greater incentive to demonstrate that they are actively examining and managing those risks and to ensure they are not penalised by regulators.

For the purposes of this paper the content recording unit was taken as any voluntary disclosure made by the bank within the broad area of money laundering. Such thematic coding allows for the allocation of content units to categories without the restriction of punctuation. For example more than one sentence on anti-money

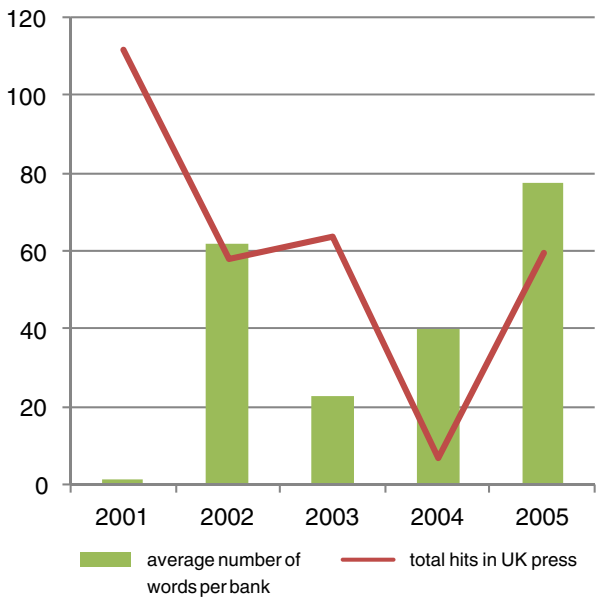

Fig. 2 Relationship between media awareness and disclosure. *Source* Tables 2 and 3

laundering can be coded together as one theme or it is possible to split one sentence on the basis that it addresses different themes. Following on from this, it was possible to identify a number of themes that enabled consistent categorisation of content across all of the different banks. As explained in Appendix 1, which sets out the process employed, these themes addressed (1) general anti-money laundering, (2) training, (3) account related activity, (4) compliance or regulatory activity and (5) any identification of reputation. A final category (6) addressed the related but broader issue of financial crime. All disclosure could be fitted into these categories.

As might be expected, Table 4 demonstrates that banks tend to concentrate their disclosure in two main areas: Firstly by reference to the regulatory framework with which they are required to comply and secondly by reference to the measures in place to counter money laundering. Of significance for the purpose of this study, is the fact that very little is mentioned specifically with respect to reputation. Indeed, reporting is this area is primarily undertaken only by HSBC, with an additional reference to reputation risk from money laundering being made by Lloyds TSB in 2005. Otherwise all banks in the sample were silent in this respect. As explained in "Appendix 1", a method of scoring was devised that would attempt to add qualitative depth to the disclosures in the field. To achieve this a very simple scoring chart was applied to each of the main identified areas of disclosure which allocated a point for each identified issue with a further point if this was supported via any additional explanatory disclosure. Zero indicates that there was no mention in relation to the category.

Ranking of the banks was simply the result of the summative score for each institution, with the total maximum points allocated to each area of disclosure of three points across each of the six themes, providing a possible maximum of 18.

Table 5 indicates that for most of the banks there is little provided in terms of qualitative depth, apart from the 2002 report for Royal Bank of Scotland and the more recent reports for Standard Chartered Bank. If banks see no need to disclose more than the minimum information to stakeholders, it is suggested that reporting in this area is driven by statutory requirement and is not used to enhance reputation; indicating support for the deficit rather than enhancement model.

To reinforce this point, it is interesting to consider this in the context of those banks included within the sample that have been the subject of fines for failure to apply anti-money laundering regulations. The Bank of Scotland (now Halifax Bank of Scotland) received a fine of £ 1.25 million in January 2004 and the Royal Bank of Scotland a fine of £ 0.75 million in December 2002. However, the responses of these two banks do not appear to be consistent with the theory. The most likely explanation for this, in line with the interviewee comment above, is that the reputation of the bank might simply have been unaffected by the fine being imposed, i.e. there was no identified damage associated with the fine that required 'perception management'[2]. It is of course possible that the medium chosen for more detailed analysis might be the Bank's Corporate Social Responsibility (CSR) reports.

[2] Or, alternatively, that 'perception management' consisted of not attracting attention.

Table 4 Money laundering disclosure by all of the banks

Category of disclosure and number of times identified	Year					Total
	2001	2002	2003	2004	2005	
Measures to counter money laundering	1	4	4	3	2	**14**
Training	0	2	1	2	1	**6**
KYC, account monitoring and SARS	0	2	0	2	1	**5**
Compliance and regulation	0	7	6	1	4	**18**
Reputation and risk	0	1	1	1	2	**5**
Financial crime	0	1	0	0	2	**3**
TOTAL	**1**	**17**	**12**	**9**	**12**	**51**

Clearly a limitation of this paper is that it has not been possible to include these reports within the study. However, previous work by the second author [22] did look at disclosures within the CSR reports[3] including those for both of these banks. Unfortunately, his findings did not point to any consistency of response by the fined banks. As already noted, despite being fined in January 2004, Halifax Bank of Scotland failed to disclose any information in the broad area of money laundering within any of their annual reports. They appear to have made some (albeit still limited) attempt to cover money laundering disclosure within their CRS reports with disclosure rising from zero in 2003 to two sentences (58 words) in 2004, and to eight sentences totaling 211 words in 2005. This apparent indifference appears to support the observation that the fine did not impact on public perception and hence on the reputation of the bank. From this it would appear that if a bank is subject to a fine and if no-one pays attention it is not in the interest of the bank to draw attention to its imposition. Indicating perhaps that we have 'perception management' by 'awareness avoidance'.

Disclosure by the Royal Bank of Scotland (fined in December 2002) has already been noted within their Annual Reports with detailed disclosure occurring only in 2002. CSR reports for the bank were available for the period 2003 to 2005 and these indicated extensive coverage in 2004. Disclosure regarding money laundering rose from five sentences (124 words) in 2003, to 59 sentences (1,341 words) in 2004 before significantly decreasing to a total of only 16 sentences (367 words) in 2005. Looking at the specific content of the 2004 CSR report the bank covers the main themes identified above including discussion of: Account Monitoring; the Joint Money Laundering Steering Group (JMLSG); Training; Know Your Customer (KYC) and SARS; and reference to relevant legislation. Given that the increase in disclosure occurred in 2004 rather than in 2003 as might have been expected, it is highly likely that this change is purely coincidental and not as an attempt to manage perception.[4]

[3] Using his approach of sentence and word counts.

[4] The only way that this might have been verified would have been through interview with the fined banks, unfortunately, on approach, whilst the Money Laundering Reporting Officer within one of the banks was willing to explore the impact on the bank of having been the subject of a fine it was disclosed that "*one of the terms of the FSA Enforcement notice was that we would not discuss the matter with any third party other than the FSA*". (e-mail exchange with author).

Table 5 Quality of disclosure by individual banks

Bank	Year				
	2001	2002	2003	2004	2005
Barclays Bank	1	5	5	0	5
Halifax Bank of Scotland (HBOS)	0	0	0	0	0
Hong Kong Shanghai Banking Corporation (HSBC)	0	1	1	1	1
Lloyds TSB Bank	1	0	0	3	1
Northern Rock Bank	0	0	2	3	0
Standard Chartered Bank	0	2	2	14	11
Royal Bank of Scotland (RBS)	0	16	5	0	4

Conclusion

The findings from this work find little support for the enhancement model and its associated 'virtuous cycle of compliance'. Instead it is apparent that very little is disclosed by UK banks about their money laundering compliance activity. This would appear to support the findings from the earlier interviews whereby compliance is undertaken to prevent a negative impact on, rather than as an enhancement to, reputation. This may be because such expenditure is seen as a cost overhead [20] so that compliance is sanction avoiding rather than good business practice [36]. It may also be that money laundering does not feature on the Richter scale of 'public awareness' and as such there is no public perception that needs to be managed.

Discussion

Despite more than two decades of anti-money laundering legislation, public perception of money laundering remains low. Press coverage, although increasing, is at such a low level that the fines metered out to banks shown to be failing in their money laundering compliance did not have any apparent impact on customer perception or on bank image. Indeed this is perhaps to be expected given that the fines were for procedural omissions. This situation is only likely to change when customers lose money as a result of a bank being associated with money laundering.

It is clear that banks have an inherent interest in preserving their reputation with respect to their being able to safely and properly handle the funds entrusted to them by all of their customers. Clearly if banks regarded the link between anti-money laundering compliance and reputation building as significant for business, much more disclosure would occur. However, evidence from the interviews indicated that compliance was undertaken in order to avoid the impact of a fine, whilst the limited disclosure within the annual reports focused primarily on the harmless discussion of the regulatory framework. It would appear, therefore, that banks are adhering to a deficit rather than enhancement model with activity undertaken merely to prevent any possible negative impact rather that as a positive contributor to reputation.

In the light of this, there is no foundation for the application of the 'threat rhetoric' in which anti-money laundering legislation is required for, and driven by

the need to preserve the reputation of the financial sector. From the foregoing, there is little to suggest that compliance is linked to reputation. Instead, legislation must be based on a clear demonstration of its impact on underlying crime not on ill-guided activism. If the regulatory bodies really do wish to operate a risk-based model of compliance then let us have a free and open debate to establish the proper magnitude of such risk. Until this occurs, banks will merely do what is required by statute and far from the desirable 'virtuous cycle of compliance' there will continue to be a less than virtuous shifting of responsibility between the regulator and the regulated, with the latter merely doing sufficient to proverbially 'cover their backs'.

Appendix: approach to classification

Annual reports were obtained for each of the years 2001–2005 for the seven banks selected for the study. The banks included in the analysis were: Barclays; Halifax Bank of Scotland (HBOS); Hong Kong Shanghai Banking Corporation (HSBC); Lloyds TSB; Northern Rock; Standard Chartered; Royal Bank of Scotland (RBOS). Compilation of the Scoring Chart for the analysis follows an iterative process. For each of the reports all sections where identified that directly disclosed information in relation to money laundering or indirectly linked with the issue or money laundering (such as combating financial crime). For each bank it was possible to sort disclosure into a number of main categories as identified by that bank. From this it was possible to identify a number of broad money laundering themes into which each of the identified sections could be classified. As discussed below, these themes addressed general anti-money laundering, training, account related activity, compliance or regulatory activity and any identification of reputation. A final category addressed the related but broader issues of financial crime. As a test for robustness of the system of coding, the initial analysis was conducted by one of the authors and then independently repeated by the other author. Having agreed the classification, all disclosed information was analysed with respect to depth and quality of disclosure. To achieve this a very simple scoring chart was applied to each of the main identified areas of disclosure as follows:

1. Each issue of money laundering disclosed—one point
2. Explanation of such issue of disclosure—one point
3. Explanation of usage of such issue—one point
4. No disclosure—zero points

Ranking of the banks was simply the result of the summative score for each institution, with the total maximum points allocated to each area of disclosure of three points across each of the six themes, providing a possible maximum of 18. The broad categories used for the analysis were:

Measures to counter money laundering included: mention of anti-money laundering; money laundering prevention and combating money laundering.

Training included all references to training within the field.

Know your Customer (KYC), account monitoring and SARs included all discussion of KYC and other account monitoring for the purposes of money laundering including reference to suspicious activity reports (SARs)

Compliance and Regulatory activity included all mention of compliance or regulations and money laundering legislation together with any reference to the Money laundering reporting officer (MLRO) and to the joint money laundering steering group (JMLSG)

Reputation and Risk refers to identification of reputation risk and money laundering risk

Financial crime refers to risk of financial crime and measures aimed at preventing financial crime.

On the basis of this approach it was possible to sort the information contained within the various reports and assign a total score to each of the banks. An example of how this was conducted is included here: Standard Chartered Bank's annual report for 2002 states that: "*The Group continues to strengthen its money laundering prevention policies, procedures and training*". Under our approach to the coding this receives a point for the mention of money laundering prevention and a point for the mention of training. By comparison, Lloyds TSB report for 2005 states the following: "*Group Compliance also provides leadership on compliance with money laundering and terrorist financing legislation and regulation across the Group. It sets group policy and standards on the topic and undertakes high level oversight of anti money laundering risks. A specialist team within Group Compliance provides a centre of excellence on the relevant legislation and regulation as well as interfacing with external public and private bodies in order to evolve the Group's approach and seek to ensure greater effectiveness and focus on key risk areas. Its remit also includes compliance with financial sanctions*".

Using our coding the following would apply. The identified area of compliance is discussed in some detail. It identifies the broad spectrum of money laundering compliance and regulation, it states the approach of the bank (albeit briefly) on how it will carry out compliance activity and adds further explanatory detail regarding the identified specialist team. This is provided with a score of 3. In addition the mention of one of the other classification areas of risk scores an additional point, providing a total score of 4.

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