

Stimulus Fraud & COVID-19:

Will the taxpayer stomach the inevitable scandal that's coming?

There is an inevitability to it - and the taxpayer knows it's coming. The question is: when does the blame game start, and who will lob the first stone? Will it result from a whistle-blower, an exposé by an investigative journalist, the interrogation of officials in a Select Committee or a Freedom of Information application (or something else)?

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Injecting masses of money into the economy very quickly was not business-as-usual (BAU) for banks and those lenders registered to provide CBIL and BBL (or bounce-back) loans. There was an overriding imperative, an ethical obligation to move fast. And they did.

The FCA has communicated that they have relaxed various rules that normally apply, for example, in relation to assessing an applicant's creditworthiness prior to executing a loan. In their statement on 4th May¹, in the context of managing financial crime risk, the FCA stated: *“We recognise that, currently, the need to manage these risks should be balanced against the need for the fast and efficient release of funds to businesses under the Government's Schemes.”*

But banks are not off the hook, despite government underwriting 80% of the loans (to cover the inevitable and expected high default levels). The Money Laundering Regulations still apply, something the FCA emphasised in their ‘Dear CEO’ letter² in March. The regulator has also made clear that if a firm has information, *“including any relevant flags or alerts – suggesting a customer poses a higher risk, for example, of fraud, money laundering or terrorist financing, it should carry out additional checks.”* In the case of new customers,

¹ <https://www.fca.org.uk/news/statements/uk-coronavirus-business-interruption-loan-scheme-cbils-and-new-bounce-back-loan-scheme-bbl>

² <https://www.fca.org.uk/publication/correspondence/dear-ceo-letter-coronavirus-update-firms-providing-services-retail-investors.pdf>

firms were and are expected to have carried out normal customer due diligence (CDD) processes, in accordance with the Money Laundering Regulations.

Time is ticking

The FCA hasn't spelt out how long financial institutions have before the regulator will start to ask banks questions about who they lent money to, whether the applicants met the schemes' criteria and whether their KYC is in good order. There are also significant challenges that cost-cutting banks will have to gear up to deal with in relation to arrears management. This last point was echoed in a statement by the Chairman of the FCA, Charles Russell, to all UK's lenders, who joined a virtual meeting chaired by UK Finance on 16th June³. In the speech, Russell said: "Lenders will need to scale their arrears-handling functions quickly and invest in training and controls".

It's not clear how long lenders have to take steps to remediate their loan books, if appropriate, and to ensure they've met and continue to comply with their legal and regulatory obligations. It is clear, though, that there have been fraudulent applications, by the opportunistic small business owner, as well as by criminals and organised crime (UK-based, as well as operating from other jurisdictions).

The story is only beginning to unfold and extends to:

- procurement fraud, following the government's call for UK businesses to make ventilators ("we will buy all of them");
- business-capture by organised crime;
- employee padding and tax fraud (related to the furlough scheme);
- furloughed staff being forced to work;
- sham companies and fraudulent or duplicate loan applications;
- BBL loans being used to make down-payments on the purchase of supercars; and
- conduct issues, where financial institutions 'bundled' products and services, so that businesses seeking forbearance over existing debt, or requesting loans, had to sign up to buying other banking products.

This is deeply political. The 'Otello COVID-19 Fusion Cell'⁴, based in the National Economic Crime Centre (NECC) and resourced by law enforcement (and others) and with participation from the UK's main lenders, is looking at these issues. I understand this would include washing the lenders' loans data to identify duplicate applications (nothing prevented a business from applying to multiple lenders at the same time), as well as using the Joint Money Laundering Intelligence Taskforce (JMLIT) information sharing gateway (S. 7 Crime and Courts Act) to interrogate a range of data at banks' and law enforcements' fingertips, to identify more coordinated criminal behaviour.

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Walking the tightrope

The tightrope that is being walked by all involved is that it is going to be deeply unpalatable if the level of fraud turns out to be material - and avoidable. On the other hand, the chasm across which the participants in the Otello Fusion Cell and government walk is the inevitable blame game, driven by taxpayer anger that will commence sooner rather than later - but who will throw the first stone?

The macros don't help. The economy has fallen off a cliff, government borrowing exceeds GDP, and a no-deal Brexit looks increasingly possible - to be avoided only by either a sleight of hand or a play on words. America and China continue to come closer to the brink, and that affects us all. While the international community hasn't been watching, because countries have been too busy managing the crisis at a local level, nefarious actors and regimes have made hay.

Criminal networks have adapted, new relationships have been forged and new techniques learnt, tested and evolved. It will take time to assess and quantify the full impact from an economic crime perspective.

³ <https://www.fca.org.uk/news/speeches/financial-system-support-recovery>

⁴ <https://www.nationalcrimeagency.gov.uk/who-we-are/publications/452-sars-in-action-may-2020/file>

A tectonic shift

Countries locked down at different times and have fought the pandemic with different levels of success. But it would be a huge mistake if the crisis and wider geopolitical (cultural and societal) tectonic shifts result in less cross-border and regional cooperation on fighting organised economic crime. Lessons should be learnt that co-operation is key, whether fighting an invisible virus or combatting the threat faced by serious organised crime, neither respect borders - in fact, they both ruthlessly exploit any weaknesses and gaps.

These are times when we all walk the tightrope. Lessons must be learnt, and action needs to be taken to recover taxpayer funds, where egregious wrongdoing is identified. It is also time to make a step-change in intelligence sharing and operational coordination, at a country-level (public to private), but also regionally and internationally, if we are to meet the increasingly complex threats posed by organised crime and bad state actors.

However, I won't hold my breath.

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