
Kilvar Kessler: it is time to talk about money laundering

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After the closure of Versobank and the injunction that was issued to Danske, I have read recommendations or hints in various places that Swedbank should be the next to be closed down. But really, people, we should keep cool heads and warm hearts.

It is probable that in the recent past most of the universal banks operating in Estonia provided services to non-resident clients, some of them less so or only passively, others more enthusiastically and actively. They did not analyse, or did not want to analyse, the suspicious behaviour of clients down to the level of where the income came from. In 2013 two bankers confidently told a public seminar that running pension funds brought little income and it was better to deal with the more profitable business of serving non-resident clients, following the example of the Latvian banks. Not long ago the local bankers and correspondent banks did not see anything very wrong with non-resident clients from the east, while supervisory work was mainly technical and did not look so far behind the curtain. Those suspected of certain crimes were given quite strong protection by the law and the practice of the courts. Changes in global trends were in the air however, though they came to us with some delay and sometimes with difficulty.

Firstly the Financial Action Task Force on Money Laundering ([FATF](#)), which sets global standards for countering money laundering, set new rules in 2012 requiring supervisors not just to ensure that the rules of banks were in line with the law, but also to check that risk control measures were adequate for the business risks that banks faced. Risk management should not be left stunted in the shade of flourishing risky businesses.

Secondly, tense international relations brought international financial sanctions into the foreground. These were aimed at pariah states and terrorists, and tried to restrict or block their ability to make financial transactions by imposing restrictions on the financial sector. It may be noted that Eesti Krediidipank was among those subject to sanctions at that time because of its parent company.

Driven by these two factors and its own supervisory experience, the new management of Finantsinspektsioon, which started work in 2014, set supervision of risk controls to counter money laundering as one of its priorities. Finantsinspektsioon is not the Financial Intelligence Unit, which receives notifications about suspicious transactions and analyses the risk environment for money laundering. Nor is it an investigatory body that handles criminal proceedings for money laundering and other suspected crimes.

If you want to play draughts you need to know the rules and that it is played with counters on a squared board. The counters for one side the game at that time were a couple of people working at Finantsinspektsioon against money laundering, while the main work of financial supervision focused on the solvency, organisation and management standards of financial intermediaries, and the compliance of their services with the requirements. The counters lined up on the other side of the

board were the whole of the financial sector and others besides, who were connected to the profits from the non-resident business. These were relatively large, efficient and well-equipped organisations by Estonian standards, with influence in the public space and in legal disputes, and as lobbyists and employers. I still remember the deep bow of a waiter at an elite restaurant to a bank manager who was known for serving non-resident clients and who was a gold client of that restaurant, at the business lunch where I announced that I wanted to close down that bank's toxic business.

The rules of the game were that Finantsinspektsioon was given a fairly toothless set of legislation that had as its crown jewel a 32,000 euro fine that barely counted as petty cash and statute limits that were so short they would surprise any financial supervisor. The board was hidden in shadows for us because the only formal indicators of risk that we could work with were the account balances of non-residents at the end of each month.

Five years, thousands of hours of work, and millions of shredded nerves later Finantsinspektsioon has provoked a sharp fall in the share of deposits held by non-residents. The volume of foreign payments made in dollars has fallen drastically. Finantsinspektsioon has helped the eastern-oriented Eesti Krediidipank to change into the domestic Coop Pank, which has now been removed from the sanctions list. Versobank, which was involved in some quite toxic business, has been closed, and Danske has been made to give up its very wide ranging non-resident business. The more professional credit institutions serving ordinary customers more broadly started to clean up their portfolios of risky non-resident businesses immediately after receiving signals about this from Finantsinspektsioon, and to improve their risk controls, management and organisation. We have seriously reduced these risks to Estonia.

The work goes on, because some financial intermediaries are still involved in non-resident business enough that they need to change their risk controls or reorganise that part of their business. Our universal banks have changed very much how they manage money-laundering risks in these five years though. It has all been done quietly and with no fuss, and stability and confidence have been maintained as these are the most valuable assets of the financial sector. It makes me wonder whether every country in Europe and elsewhere has dealt with the risks of money laundering quite as thoroughly. Finantsinspektsioon has worked to the very best of its ability and knowledge and within the limits of the law. We have learnt a lot during these years, though we keep our eyes and ears open and we learn yet more with every supervisory case. There is of course no way that we can currently predict what the standards and understandings will be 10 years from now, just as in 2009 we could not have forecast the current circumstances.

Newspapers are currently full of salacious details shining a light on the earlier non-resident business of the banks and retrospectively assessing them using the standards of today. Finantsinspektsioon generally does not deal with individual transactions in its work, and we are not surprised to find references to wobbly risk controls in the past and to dubious types of business. We will not be surprised if details of some embarrassing transactions in the past should appear at some bank in the future. It would perhaps be wisest for the banks to draw a clear public line between the past and the very different present, in the way that they have already essentially done for the supervisors.

The main tool that can be used for reasonable financial supervision is the legislation. We have so far had to squeeze every last possible drop out of the existing norms and standards to be able to tackle money laundering in a way that best serves the nation and the state. We can make three simple proposals for legislative changes that would improve this.

Firstly, monetary fines must be brought up to the levels of European Union legislation. Fines should be at a level where they are actually a deterrent for those involved in the financial sector, as we have

repeatedly argued for 15 years.

Secondly we must do away with the misdemeanour proceedings that are too complex to be practically usable and so offer too much protection to the banks. Instead we should follow the example of the European Central Bank and apply administrative proceedings and administrative punishments. This would allow us to operate more firmly and with less formality.

Thirdly protection for whistleblowers must be regulated more broadly in financial supervisory proceedings. Individual ordinary employees working in banks should not have to fear they will lose their job or suffer some other punishment if they inform the supervisors of suspicions about the operations of their employer or about illegal activities.

To everything there is a season, and a time to every purpose under the heavens. (Ecclesiastes 3:1)

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