

Guidance on anti-money laundering

How it affects members of the National Housing Federation

Updated in June 2018

This guidance has been issued in cooperation with the national housing federations of Northern Ireland, Scotland and Wales as it is applicable to their members.



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Updated in June 2018

First published in May 2010
by the National Housing Federation
Lion Court, 25 Procter Street, London WCV 6NY

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Introduction

The UK anti-money laundering regime has evolved over a number of years and includes legislation intended to counteract not only criminal money laundering but also terrorist financing.

The offences of failing to report knowledge or suspicion of money laundering when carrying out regulated activities carry severe penalties including heavy fines and prison sentences of up to five years. Money laundering reporting officers and staff have a legal obligation to report such knowledge or suspicion to the National Crime Agency.

The number of these reports from the providers of social housing has been historically low and it is important that management and staff alike are aware of the risk factors in order to ensure that they comply with the legislation including the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (the Regulations). The Regulations are applicable throughout the United Kingdom.

This guidance has two principal objectives:

1. To ensure that members can identify if and how they are subject to the legislation and that they comply with it (see part 3: Money laundering legislation).
2. To protect members from the effects of money laundering (see part 2: Where does the money come from and how does it affect the sector? and part 6: Common methods used to launder money).

Housing associations are only required to comply with the Regulations where they carry out 'regulated activities' as defined by the Regulations. In practice, this is likely to boil down to whether housing associations perform specific lending activities under the Consumer Credit Licence legislation or conduct estate agency work as defined in the Estate Agents Act 1979. Consequently, this document should be read in conjunction with Financial Conduct Authority (FCA) guidance on consumer credit licensing and the Federation's own guide for members on consumer credit: Consumer Credit Authorisation – Guidance for Housing Associations.

Irrespective of whether your association is required to comply with the Regulations, it is important to understand that there are substantial money laundering risks associated with housing management and the everyday course of business in any housing association. Therefore all members are recommended to conduct an assessment of the money laundering and terrorist financing risks which they face across their full operational activities, and to embrace the underlying principles of the UK's anti-money laundering regime.

This guidance is intended to assist members in producing appropriate risk-based systems and controls to enable compliance with their obligations under the regime and the effective mitigation of money laundering and terrorist financing risks. These requirements are detailed in part 5: Compliance, registration, systems and controls.

This document does not provide an exhaustive checklist of the systems and controls required to combat the threats posed to housing associations by criminals and terrorists, but seeks to raise awareness within the sector of where potential risks lie and to give some practical advice on the methods used by money launderers.

Housing associations may need to seek assistance with the practical aspects of producing a policy relevant to their business and with the implementation of risk-based systems and controls to manage compliance.

This guidance has been issued by the Federation in consultation with Trowers & Hamblins LLP and:

1. It is not an FCA or HMRC publication and should not be read as having endorsement from those organisations.
2. You should obtain professional advice on the application of the Regulations to the specifics of your business.

This guidance applies to housing associations in England, Wales, Northern Ireland and Scotland. In this guidance we have used the generic term 'housing associations' to mean:

1. Housing associations under the Housing Act 1998.
2. Non-profit registered providers under the Housing and Regeneration Act 2008. This term replaced 'registered social landlords' in April 2010.
3. Housing associations in Northern Ireland under the Housing (Northern Ireland) Order 1992.

1 What is money laundering and why does it happen?

Money laundering is the process by which funds derived from criminal activity are given the appearance of being legitimate. That means that the proceeds of a crime are 'cleaned up' by various means and then fed back into the financial system after a transaction or series of transactions designed to disguise the original source of the funds. It also covers money, however come by, which is used to fund terrorism.

Money laundering can take a number of forms:

- handling the proceeds of crime
- being directly involved with criminal or terrorist property
- entering into arrangements to facilitate laundering of criminal or terrorist property
- investing the proceeds of crime into other financial products, property purchase or other assets.

Why does it happen?

Criminals launder money in order to enjoy the fruits of their criminality. Most crime is acquisitive in nature and it is necessary to give the proceeds of crime the appearance of being legitimate in order that the source of the funds can be disguised.

The money generated by these crimes needs to be laundered before the criminals can gain the full benefit of it, and law enforcement agencies around the world are keen to make it hard for criminals to benefit in this way. Similarly, the UK terrorism legislation also addresses the issue of the funding of terrorism, much of which is directly related to criminal activity.

What are the sources of the funds for criminals?

Globally the business of transnational crime is valued at an average of USD\$1.6 trillion to USD\$2.2 trillion annually. A report published by Global Financial Integrity in 2017 estimated the global market values for 11 illicit crimes including counterfeiting (USD\$923 billion to USD\$1.13 trillion), drug trafficking (USD\$426 billion to USD\$652 billion) and human trafficking (USD\$150.2 billion). In the UK, the social and economic cost of drug supply in England and Wales is estimated to be £10.7 billion a year.

Terrorism and crime

We are all aware of the effect that terrorism has on society and there are well documented links between terrorist organisations and serious organised crime. These groups are well co-ordinated and many are run on a sophisticated business model, employing professional advisers to assist them.

Does the social housing sector have a role?

The housing association sector has a significant role to play in tackling the problems caused by crime. Real estate is deemed a higher risk area. Property transactions have the capacity to process a large amount of criminal funds which can be 'cleaned' in a single transaction.

Effective use of systems as detailed in part 5: Compliance, registration, systems and controls, the Joint Money Laundering Steering Group (JMLSG) Guidance (as defined below) and sector guidance from HMRC will assist with the recognition of how money laundering occurs and how it affects the sector. That will have benefits for communities in the disruption of criminal activity, and may also help in reducing related antisocial behaviour.

2 Where does the money come from and how does it affect the sector?

How does it affect the sector?

Criminals will target any sector that they see as a soft target and those working in the housing sector may not be as aware of the methods used to launder funds as those employed in financial services. Money launderers are opportunists and will exploit a situation that affords them the opportunity to give their funds the appearance of coming from a legitimate source. As the awareness of the problem within the sector is raised and the number of reports of suspicious transactions increases, it will be more difficult for criminals to target social housing providers.

Many criminals use property purchase as a means of laundering the proceeds of their crimes. Criminals will also use properties for illegal activities such as drug dealing, prostitution and cultivating cannabis. By definition, money laundering involves the proceeds of crime. If you allow criminals to launder their money, you are allowing them to profit from their crimes.

As a result, the sector suffers in a number of ways from the activities of money launderers who misuse properties, often causing serious damage and illegally sub-letting or occupying properties thereby reducing available housing stock. Some of the methods used to target the sector are detailed in this guidance (see part 6: Common methods used to launder money).

How big is the problem?

Estimates vary on the effect money laundering has on the UK and global economy, but by any measure it is a massive problem. In the Government's 'Action Plan for anti-money laundering and counter-terrorist finance' published in April 2016, it was estimated that serious and organised crime costs the UK at least £24 billion annually.

It is worth remembering that whilst the vast majority of transactions are lawful, it is a mistake to assume that a transaction is legitimate solely on the grounds that there is a professional involved in the process.

What is the connection between organised crime and our communities?

Organised crime, street crime and antisocial behaviour adversely affect us all in our daily lives. The funds that criminals launder are generated by crime, and the resultant blight on communities is apparent to us all. Although money laundering is often viewed as an abstract concept, clearly it is a problem that, when seen in the context of how the funds are sourced, undermines every community.

3 Money laundering legislation

The implementation of risk-based systems and controls to mitigate against a business being used by criminals or terrorists to launder funds is a statutory requirement of the Regulations for those businesses in the regulated sector (see part 4: The regulated sector).

However, you should be aware that the Proceeds of Crime Act 2002 (POCA) applies to every individual within the United Kingdom and the commission of offences under POCA and the terrorism legislation carry severe penalties.

Committing one of the principal money laundering offences carries up to 14 years' imprisonment and the penalties for non-compliance with the obligations imposed by the Regulations carry up to two years' imprisonment even when there has been no instance of money laundering.

The Joint Money Laundering Steering Group (JMLSG) and HMRC have produced guidance to assist organisations in meeting their obligations under the Regulations (the JMLSG Guidance). The JMLSG Guidance contains details of the legislation applicable to anti-money laundering and terrorist financing. This is available at www.jmlsg.org.uk.

Money laundering offences

The POCA sets out the primary substantive offences related to money laundering:

- concealing, disguising, converting, transferring or removing criminal property from the UK (s327 of the POCA)
- entering into or becoming concerned in an arrangement which facilitates the acquisition, retention, use or control of criminal property by or on behalf of another person (s328)
- the acquisition, use and/or possession of criminal property (s329)
- staff in the regulated sector failing to disclose knowledge or suspicion of money laundering to the nominated officer/money laundering reporting officer (MLRO) (s330) or, in the case of MLROs, failing to report to the National Crime Agency (NCA) as appropriate (s331)
- tipping off any person that such a disclosure has been made (s333A).

The offences under ss327, 328 and 329 can be committed by anyone becoming involved in the actual commission of one of the primary money laundering offences. 'Criminal property' is defined widely to cover any form of asset which represents the economic benefit of a crime.

To commit an offence a person must know or suspect that the asset represents a benefit from criminal conduct. This test, extending to suspicion as well as actual knowledge, is a low one. Staff should therefore have sufficient knowledge to enable them to identify potential instances of money laundering so that they do not become involved in the commission of one of these offences.

For example, staff could commit the offence under s328 if they know or suspect that a customer is involved in money laundering and go ahead with a transaction that enables that person to purchase a property. The offence under s329 could be committed simply by accepting cash from someone in the knowledge or suspicion that the cash is the proceeds of crime. This is irrespective of the amount of cash accepted.

The POCA provides defences to the commission of the offences under ss327, 328 and 329 where a disclosure is made to the NCA (see part 5: Compliance, registration, systems and controls).

The offences under ss330, 331 and 333A can only be committed by those working in the regulated sector and staff in those roles are expected to have a good understanding of their legal obligations. The offences under ss330 and 331 are punishable by a maximum of five years' imprisonment, while the offence of tipping off under s333A carries a maximum of two years' imprisonment.

Other money laundering offences

Where a business that is not operating within the regulated sector appoints a money laundering reporting officer (MLRO), that person can also commit an offence under s332 of the POCA by failing to report knowledge or suspicion of money laundering.

There is a further offence under s342 of prejudicing an investigation where a person knows or suspects that a money laundering investigation is being conducted or is about to be conducted, and makes a disclosure which is likely to prejudice the investigation or falsifies, conceals, destroys or disposes of relevant documents or causes or permits the same. These offences are punishable by a maximum of five years' imprisonment.

Terrorism Act 2000

The Terrorism Act 2000 (TA) sets out the primary offences related to terrorist funding and requires regulated businesses to report knowledge or suspicion of offences related to terrorist financing:

- fundraising for the purposes of terrorism (s15 of the TA)
- using or possessing money or other property for the purposes of terrorism (s16)
- involvement in funding arrangements (s17)
- money laundering – facilitating the retention or control of property (including money) which is destined for, or is the proceeds of, terrorism (s18 of the Act).

The terrorism legislation also has offences of failure to disclose, which carries a maximum penalty of five years' imprisonment (s21A of the TA), and tipping off (s21D) which carries a maximum penalty of two years' imprisonment.

There are defences to the commission of the principal TA offences under ss21ZA and 21ZB (see part 5: Compliance, registration, systems and controls).

The TA imposes more stringent requirements than the POCA in a number of respects. One is that the legal test for committing an offence is having 'reasonable case to suspect' (i.e. actual knowledge or suspicion is not required). Another is that the disclosure and reporting requirements cover all people in their employment or business (i.e. it is not limited to the regulated sector).

4 The regulated sector

The Regulations, which came into force on 26 June 2017, list certain business activities, including some types of business undertaken by housing associations which, in turn, makes associations 'relevant persons' to whom the Regulations apply. This also includes credit institutions, financial institutions, auditors, accountants, estate agents, trust or company service providers, independent legal professionals and others. These are examples of 'regulated sectors'. How this directly affects housing associations is explained below.

The Regulations appoint supervisors for various sectors and give those supervisors a number of powers in relation to registration requirements on 'relevant persons' and enforcement of the Regulations. Those supervisors include the Financial Conduct Authority (FCA), Her Majesty's Revenue & Customs (HMRC) and The Law Society.

Housing associations are 'relevant persons' in some circumstances and will be supervised for compliance with the Regulations by the relevant regulator in respect of their activities in that sector. The following are examples of the types of business where a housing association would be supervised for compliance with the Regulations:

1. Many housing associations are regulated by the FCA for consumer credit activities and other regulated lending activities. These registered providers would also need to be registered with the FCA for anti-money laundering supervision in respect of these activities where they involve any form of lending.
2. Where an association offers any other form of lending including grant funding which is recoverable in certain circumstances. In the case of some grants, you should seek advice as to whether you may benefit from an exemption from the regime.
3. Money service businesses (i.e. businesses that provide services transmitting or converting money) are regulated by the FCA unless they are an excluded money service business, which are regulated by HMRC.
4. Where housing associations grant second charge mortgages whether under authorisation by the FCA or pursuant to an exemption from such authorisation this activity may be subject to the Regulations. In addition, where an association manages a portfolio of mortgages, even if no further mortgages are granted, this activity may also be subject to the Regulations. Housing associations undertaking the activities mentioned in this paragraph are recommended to seek specialist advice as to whether the Regulations could apply to them.
5. Where an association acts on behalf of another association in the sale of a property or in respect of the sale of a property on behalf of the occupier who is the co-owner, such as in a shared ownership resale context. In these circumstances, an association would be acting pursuant to instructions from another and this would fall within the definition of estate agency work for the purposes of the Regulations, and the regulator would be HMRC.
6. Where an association instructs a third party, such as an estate agent, to sell property on its behalf those actions may also fall into the description of estate agency work where there is shared equity with the resident. Each member should check their particular working practices/methods against the Estate Agents Act 1979 (s1) definition of estate agency work to assess whether they need to comply with the Regulations.

Some other activities would also result in associations being classed as 'relevant persons', an example being where they engage in activities such as audit work for smaller associations or other businesses. The provision of those services may mean that the association would fall into an area supervised under the Regulations by HMRC. Similarly, if a housing association provides legal services or advice, this may be a regulated activity supervised by The Law Society.

The issue of registration and supervision is contained within guidance issued by the various supervisors on their respective websites, but housing associations may wish to seek specific clarification and advice.

It should be noted that the letting and management of properties does not require supervision under the terms of the Regulations. Similarly, the sale or purchase of properties as principal does not require supervision. As noted above, these activities may expose housing association staff to the risk of committing a substantive offence under the POCA and so are not risk free. However, they are not required to be subject to the regime provided for under the Regulations, as described in part 5: Compliance, registration, systems and controls, below.

5 Compliance, registration, systems and controls

The regulations require that 'relevant persons', i.e. businesses in the regulated sector (see part 4: The regulated sector), establish and maintain risk-sensitive policies and procedures covering their activities in that sector.

These policies should detail the business's commitment to anti-money laundering controls and the procedures should cover:

- registration
- the money laundering reporting officer and the officer for compliance
- training for relevant staff on an ongoing basis in how to recognise and deal with relevant transactions and other activities
- staff screening measures for appointed officers and those working within the regulated part of the association
- customer due diligence measures and ongoing monitoring
- reporting of suspicious activity
- record-keeping
- organisation-wide risk assessments
- monitoring and management of compliance with, and internal communication of, such policies and procedures.

Each of these procedures is described below.

Registration

The Regulations impose an obligation on businesses to register with an appropriate supervisor where the supervisor requires registration (Regulation 56).

As noted in part 4: The regulated sector, HMRC is the regulator for estate agency work and the FCA is the regulator for consumer credit activities or other lending. To assist in the registration process, the FCA has issued guidance on completing the form and the registration policy. These are available at www.fca.org.uk/firms/money-laundering-terrorist-financing/registration. Similarly, you can register with HMRC at www.gov.uk/guidance/money-laundering-regulations-register-with-hmrc.

Money laundering reporting officer

The Regulations require that businesses appoint a money laundering reporting officer (MLRO – also known as a ‘nominated officer’) who is responsible for receiving reports of suspicious activity from staff and where necessary making Suspicious Activity Reports (SARs) to the National Crime Agency (NCA). It is also management’s responsibility to establish and maintain risk-sensitive policies and procedures in relation to money laundering and terrorist financing.

It is important that anyone who is appointed to the role of MLRO holds a position of authority sufficient to ensure that they can access any information necessary to fulfil their obligations and to ensure that staff adhere to the systems and controls in relation to the policies and procedures in place. The Proceeds of Crime Act 2002 (POCA) also states that reports of suspicion of money laundering should be made as soon as practicable. With that in mind, it is advisable to appoint a suitable deputy to deal with such issues in the absence of the MLRO.

In any event, it is the responsibility of those directing the business to ensure that the necessary measures are taken to comply with the Regulations (see more specifically below: officer for compliance). The MLRO has a responsibility to put the measures into practice and to report on a regular basis to senior management. It is good practice for the MLRO to produce a document setting out the reports made and activities undertaken annually and to re-visit the risk assessment process on at least an annual basis. It is, however, the responsibility of all employees to report suspicions of money laundering to the MLRO.

Where an association has appointed an MLRO there is a requirement under POCA, which extends to those acting in that capacity outside the regulated sector, to report suspicious activity to the NCA (see part 4: The regulated sector, above).

Officer for compliance

Pursuant to Regulation 21(1)(a) a regulated business must consider, with regard to the nature and size of the business, whether it is appropriate to appoint one individual as the officer responsible for compliance with the Regulations. Unless the association is only carrying out a minimal amount of regulated business, such an appointment is recommended.

This individual must be either a member of its board of directors or, if there is no board, its equivalent management body or alternatively a member of the senior management. It is recommended that the officer for compliance is a different person from the MLRO in order to operate a supervisory role over the MLRO when necessary. Furthermore, if the association considers that it requires an independent audit function (see below: Independent audit), the officer for compliance would receive the audit reports about the MLRO and their functions and make appropriate recommendations.

Staff training

Ensuring that staff are properly trained is an integral part of any effective anti-money laundering regime and it is incumbent on senior management to comply with this requirement. It is vitally important that staff are regularly updated on the methods used by criminals to launder money, as they are constantly evolving.

An important first step in the training process is to ensure that the MLRO and other key staff are aware of what their roles entail, as they will inevitably be approached by staff with questions in connection with customer due diligence, reporting issues and money laundering methods.

A business that does not ensure staff are properly trained not only commits an offence and is liable to civil penalties but is also left vulnerable, as criminals are adept at recognising opportunities to exploit the system. In addition, there is a specific defence in the POCA for an employee who is accused of failing to report knowledge or suspicion of money laundering, where the employee has not received adequate training. This would also leave the employer vulnerable to civil penalties and/or prosecution for failing to comply with the Regulations and may bring adverse publicity with resulting reputational damage.

Staff screening

Regulated organisations must ensure that employees carrying out anti-money laundering functions must be screened, both when they are taken on and during the course of their employment (Regulation 21(1)(b)).

Screening of relevant employees means an assessment of:

- the skills, knowledge and expertise of the individual to carry out their functions effectively
- the conduct and integrity of the individual.

Associations must create an audit trail of how they have decided to screen such employees in addition to records relating to the outcome of such screening processes.

Customer due diligence

There are a number of facets to customer due diligence.

(a) Customer due diligence measures and ongoing monitoring

The JMLSG and HMRC Guidance gives advice on how to identify customers and on the use of appropriate documents to assist in carrying out customer due diligence (CDD) measures (also known as know-your-customer or KYC). One of the most effective methods for protecting a business against attack by money launderers is to carry out stringent checks on the identity of customers and to know who the beneficial owner in any transaction is.

(b) What is customer due diligence?

There are a number of steps which can be taken to identify a customer and the level of verification needed will differ dependent on the nature of the transaction, the client, and the perceived risk of money laundering or terrorist financing. Appendix 1 to this guidance sets out potential scenarios with new and ongoing business relationships and suggested actions.

The basic first step is identifying the customer and verifying the customer's identity on the basis of documents, data or information obtained from a reliable and independent source. In many cases, where the risk is assessed to be low, this may be all that is needed to be satisfied that enough is known about the customer to engage in a transaction. Appendix 2 contains a list of appropriate documents which can be used to identify customers.

It is, however, important to be aware that there are many forged and stolen documents in circulation, such as driving licences, passports and utility invoices, and it may be advisable to use electronic methods of customer identification – individual housing associations need to look at the risks which apply to their business models and implement appropriate protective measures. It is necessary to ensure that any system used meets the requirements in relation to the depth, breadth and quality of data.

The JMLSG Guidance provides useful information on the use of electronic methods of customer identification. In addition, it provides comprehensive advice on the methods used to identify various entities such as trusts, charities, companies and other corporate bodies.

When electronic evidence of identity is sought, it is not necessary to ask the customer's permission to perform a check but the customer must be informed that the check is being done. It may be useful to include mention that this may be necessary in documentation sent to customers along the following lines '...ABC Housing Association is legally bound to comply with the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017, the Proceeds of Crime Act 2002 and the Terrorism Act 2000. We may therefore utilise electronic means of verifying customers' identities...'.

(c) Enhanced due diligence

In some circumstances, it may be necessary to carry out further due diligence on a risk-based approach. This means that in some circumstances businesses may decide that the standard evidence of identification that they require customers to provide is not sufficient and that extra information about a particular customer is required in certain circumstances, such as:

- where the customer has not been physically present for identification, that is non-face-to-face customers (see comments in the paragraph below)
- where the customer is a politically exposed person (PEP) or an immediate family member or close associate of a PEP (see comments in the paragraph below), which automatically increases the risk profile.

(d) Non-face-to-face customers

Where the customer has not been physically present, businesses should take account of the increased risk by doing one or more of the following:

- obtaining additional information or evidence to establish the customer's identity
- undertaking additional measures to verify the documents supplied or requiring certification by a financial or credit institution
- ensuring that the first payment of the operation is carried out through an account with a credit institution in the customer's name.

(e) Politically exposed persons

A politically exposed person (PEP) is an individual who has, or has had in the previous year, a high political profile, or holds, or has held in the previous year, high-ranking public office, whether in the UK or overseas (Regulation 35(12)). Examples of PEPs include heads of state, heads of government, ministers, members of parliaments, members of supreme or constitutional courts or other high level judicial bodies, ambassadors and high-ranking officers in the armed forces. The definition of PEPs extends to cover immediate family members and known close associates.

Businesses should ensure that they have procedures in place to identify whether the customer is a PEP and take steps to establish the source of their funds which will be used during the business relationship or transaction. If a PEP is involved in a transaction, their source of wealth must also be identified. Businesses must put in place procedures for senior managers to approve the establishment of a business relationship with a PEP. Where a business relationship is entered into, businesses should undertake enhanced ongoing monitoring of the relationship. There is no all-encompassing list of PEPs but most electronic customer identification systems will check against their database to provide details of known PEPs.

(f) Persons that businesses must not accept as customers

The Government may direct businesses not to enter into business relationships or transactions with certain individuals who are subject to financial sanctions. A list of all sanctions currently in force in the UK is maintained by the Treasury. This list can be found at: www.gov.uk/government/publications/financial-sanctions-consolidated-list-of-targets/consolidated-list-of-targets.

(g) Ongoing monitoring

A system of ongoing monitoring of existing customers should be established so that enough is known about them to allow money laundering risks to be assessed. For example, a customer who suddenly has the funds to buy a housing association's share of a property or to buy a property outright will, in the vast majority of instances, have a reasonable explanation for the source of the funds. Ongoing monitoring of such activity should however be the catalyst for further enquiries to be made.

Where a PEP is involved, Regulation 35(5)(c) provides that enhanced ongoing monitoring must be applied.

(h) Situations where it is not possible to carry out due diligence

The Regulations are specific in relation to placing a requirement on businesses within the regulated sector to cease transactions where it has not been possible to carry out satisfactory checks in order to identify the customer. In those circumstances, businesses must:

- not carry out a transaction with or for the customer through a bank account
- not establish a business relationship or carry out an occasional transaction with the customer
- terminate any existing business relationship with the customer
- consider making a suspicious activity report to the NCA under Part 7 of the POCA or Part 3 of the TA.

(i) Property purchase and customer due diligence

The system of due diligence will provide some comfort in relation to the mitigation of money laundering and terrorist financing risks. It should be considered however that there are situations that may appear to involve an entirely legitimate transaction but are in fact a cover for money laundering. An example of this would be where a shared ownership customer enters into a transaction to part-purchase a property with the deposit and payments to be made through a bank account. It is a well-known practice for criminals to use front buyers to purchase properties in this way, having provided them with the funds.

In this situation, enhanced due diligence may involve examining the source of funds or looking closely at the prospective purchaser's employment details and income. Those checks may reveal that the purchaser does not fit the profile of a regular customer. Such issues can partly be addressed by risk assessment and management. This example also illustrates the importance of an effective staff training programme, as well-trained staff will prove to be more adept at recognising potential money laundering situations.

The real estate sector is deemed higher risk and property purchase is a common method of laundering the proceeds of crime. This should be a consideration for all housing associations when undertaking an organisation-wide risk assessment.

(j) Reliance on third party due diligence

If for any reason it is not possible to obtain the original documents or certified documents required, then in exceptional circumstances you may be able to rely on copies of due diligence carried out by a third party, such as a solicitor. Before relying on this, you must obtain the prior written consent of the:

- Third party whose due diligence you wish to rely on. The Regulations require that you obtain this consent before you can rely on any third party due diligence.
- MLRO. A request for approval must state the reason for reliance, the third party on whom you are proposing to rely, and including a copy of the written consent of the third party.

In this case you must also:

- Immediately obtain from the third party all the information needed to satisfy the association's own requirements in relation to the customer, the customer's beneficial owner (if applicable), or any person acting on behalf of the customer.
- Enter into arrangements with the third party which:
 - (i) enable the association to obtain from the third party immediately on request copies of any identification and verification data and any other relevant documentation on the identity of the customer, customer's beneficial owner (if applicable), or any person acting on behalf of the customer
 - (ii) require the third party to retain copies of the data and documents referred to in paragraph (i) for as long as the association would be required to hold them had it carried out the due diligence itself.

In practice, most solicitors and other professionals do not permit third party reliance on Client Due Diligence (CDD) documents they have obtained from their customers for these purposes.

Reporting suspicious activity

A system which allows staff to submit internal reports of suspicious activity must be established. Reports must be made by staff to the MLRO as soon as practicable when they know or suspect, or have reasonable grounds for knowing or suspecting, that a person is engaged in money laundering or terrorist financing. Failing to report such knowledge or suspicion is a criminal offence (see s4 of the Act). A template for an internal report form can be found at Appendix 3.

After consideration of the contents of an internal report, the MLRO/nominated officer may decide to report the matter to SOCA using the SOCA online reporting system. It is not necessary to complete the registration process for the system until a report is being made.

It is important that reports of suspicious activity, both internal and external, are treated as confidential and securely stored. The suspicious activity reporting regime operated by SOCA on receipt of reports made by businesses places an emphasis on confidentiality which protects the reporting sector. There are offences of tipping off and prejudicing an investigation which carry severe penalties connected with unlawful disclosure of information following a report having been made (see part 3: Money laundering legislation).

In respect of internal reports where it is decided not to report to SOCA the MLRO should fully document the rationale behind any such decisions and retain those records.

When and how to report to the NCA

Members should familiarise themselves with the JMLSG Guidance which provides extensive practical guidance on the interpretation of the Regulations. Chapter 6 of the JMLSG Guidance gives details of the responsibilities of reporters, including when to report, in what format and what details need to be included. In addition, the NCA website contains helpful information on reporting suspicious activity.

Record-keeping

The JMLSG guidance (chapter 8) and HMRC guidance (part 6) detail the requirements in respect of record-keeping, which are necessary to demonstrate compliance with the Regulations, namely:

- copies of, or references to, the evidence obtained of a customer's identity for five years after the end of the customer relationship, or
- in the case of occasional transactions, five years from the date when the transaction was completed
- it is also necessary to maintain a written record of the risk assessment in relation to the transaction.

In relation to customer identification, businesses must keep:

- a copy of, or details about, the identification document presented and verification evidence obtained, or
- information about where the evidence can be obtained.

If the business employs a third party to undertake its customer due diligence measures, the business must ensure that the third party complies with the record-keeping obligations.

The purpose of keeping these records is to demonstrate the business's compliance with the Regulations and to aid any resulting investigations.

Records can be kept in a variety of methods such as original documents, photocopies of original documents, in computerised or electronic form. Businesses may also keep references as to where original documents can be found. How the records are retained will depend on how the business operates.

Businesses must also keep records of internal and external reports and decisions as part of the suspicious activity reporting.

In practice, it is recommended that the MLRO retains records in relation to staff training and also records of any updates in respect of money laundering methods and legislation which have been disseminated to staff.

If an association has decided to rely on the due diligence undertaken by a third party, it must ensure that the third party complies with the above record-keeping requirements.

Risk assessment and management

In order to assess the risks posed to a business by money launderers and those funding terrorism, it is a basic requirement that the process of risk assessment is applied to the particular risks faced by a business. There is no system of risk assessment which can apply across an entire sector, as different businesses within the sector will encounter diverse risk factors.

It is also important that risk assessment is an ongoing dynamic process which is constantly under review, in particular when dealing in new types of business or with customers who are new to the business.

The Regulations require any organisation operating in the regulated sector to carry out:

- a firm-wide risk assessment, which is kept under regular review, and
- a risk assessment for each transaction, which is subject to ongoing review depending on the nature of the transaction and the duration of the customer relationship.

There is no requirement for risk assessment to be a complicated process but the system should be capable of demonstrating to supervisors that it is effective and addresses the identified risk factors. Decisions taken in respect of initial or ongoing risk assessments should also be documented and retained.

Internal controls

The core obligations in respect of internal controls are that a business must establish and maintain adequate and appropriate policies and procedures to forestall and prevent money laundering. These controls must take account of the risk factors which the business faces, and where activities are outsourced the business should ensure that outsourcing does not result in reduced standards. An example of this would be where client identification procedures are outsourced to another agency in relation to shared ownership schemes.

The monitoring and management of compliance

As previously stated, senior management has a responsibility to ensure that the necessary and effective systems and controls are put in place. Staff have a responsibility to ensure that they use and comply with those systems and controls. It is necessary to demonstrate that regular reviews are conducted and, where needed, adjustments made as part of the risk-based approach. The MLRO should oversee reviews and ensure compliance by staff by an ongoing process of education. A clear and concise policy which is easily accessible to all staff is essential to this process. It is best practice to cross-reference the anti-money laundering policy and procedures to anti-fraud policies and fraud response plans, as the proceeds of fraud are obviously the proceeds of crime and, as such, are laundered by or for the perpetrator.

Independent audit

Pursuant to Regulation 21(1)(c), all regulated organisations must consider whether, with regard to the size and nature of its business, it should establish an independent audit function to examine and evaluate compliance with the Regulations.

The Regulations do not specify whether this means an external auditor, such a firm of accountants, or an in-house internal auditor. Therefore, if it is possible to utilise an audit function internally, this should be adequate to meet this requirement. If an internal audit function is established, the staff carrying out this audit function need to be different from the staff carrying out anti-money laundering functions generally, i.e. the MLRO and his or her team, in order to ensure independence. The association must be able to produce an audit trail setting out the decision-making process relating to the establishment of this audit function.

6 Common methods used to launder money

The list of methods used by money launderers to target the sector and detailed below may assist in the risk assessment process, but no such list can be exhaustive. There are a number of methods which apply to various types of business but experience has shown that there are also methods of money laundering that are specific to the sector.

Property purchase, right to buy and shared ownership schemes

Involvement in property sales or shared ownership schemes carries an increased risk of money laundering. When conducting a property transaction, you may be comfortable in the knowledge that there is a solicitor or conveyancer involved and there is a mortgage in place. Just because there is a professional involved does not necessarily mean that the transaction is legitimate, as criminals often exploit professionals to give transactions an air of credibility.

The following situations may indicate that a customer or transaction is suspect. The list in Appendix 1 gives some examples of categorising and dealing with such risks:

- Checking a new customer's identity is difficult.
- There is reluctance from a new customer to provide details of their identity.
- The size of the transaction is not consistent with previous activity. For example, a customer on housing benefit suddenly has the funds for a deposit to fund a house purchase.
- The financial circumstances of an existing customer have changed dramatically.
- Money is paid by a third party who has no obvious link with the transaction. Money launderers often use front buyers to enter into transactions on their behalf. The money for a deposit or even to pay a mortgage may have come from someone other than the customer and could very well be the proceeds of crime.
- The customer wants to pay a large sum in cash.
- A customer who puts pressure on you to accept his or her business before you can carry out the necessary checks.
- A customer makes an approach to purchase a property then backs off on realising his or her identity will be checked for anti-money laundering purposes.

The misuse of properties for criminal purposes

- Cannabis farms in properties can be a danger to other residents due to an increased fire risk. Staff should be trained in recognising the tell-tale signs of cannabis cultivation.
- Human trafficking and exploitation of women and children is the modern day slave trade and a fast-growing area of criminality. Properties are used as brothels and accommodation for the victims of trafficking.
- Tenancy fraud and sub-letting has resulted in thousands of properties being unavailable for social housing.
- Drug trafficking and illicit laboratories with the related problems of antisocial behaviour and danger to residents.

Fraud (internal and external)

Fraud, whether perpetrated by employees or from another source, creates the proceeds of crime which are then laundered. Housing associations are susceptible to the same risks as any business. Some examples are:

- Collusion fraud by contractors or suppliers to corrupt the tendering process or employees involved in such collusion.
- Gratuities or incentives to employees as an incentive to award contracts.
- Criminals setting up front companies or shell companies to defraud associations.
- Foreign lenders that are fronts for criminality posing as bona fide financial institutions to lend money to associations.

The National Fraud Initiative

The Cabinet Office runs the National Fraud Initiative, which matches electronic data within and between audited bodies to prevent and detect fraud. The document 'Protecting the public purse 2016', published by the European Institute for Combatting Corruption and Fraud in January 2017, provides information which members will find useful in understanding the extent and nature of the fraud problem. It is designed to provide a national snapshot of how local authorities are combatting fraud, risk and financial irregularities. The report can be found at www.teiccaf.com/protecting-the-english-public-purse-2016 (see part 5: Compliance, registration, systems and controls).

Other forms of criminality

There are a number of other criminal acts which have a direct impact on the sector and some examples are:

- vulnerable tenants being targeted by loan sharks (illegal lending)
- identity theft allowing criminals to perpetrate other crimes
- criminals exploiting the lack of adequate financial systems to obtain refunds after making overpayments in cash.

Criminal Finances Act

The Criminal Finances Act 2017 came into force on 30 September 2017 and introduced new corporate criminal offences relating to a failure to prevent facilitation of tax evasion (in the UK or abroad). This Act provides for a defence to the new offences where organisations have put in place 'reasonable prevention procedures'. Such procedures will involve mechanisms to prevent facilitation of tax evasion by the organisation, its employees, agents or other associated persons. Such measures should take account of the size, nature and complexity of the organisation.

HMRC has published guidance that will help housing providers consider how to put in place appropriate procedures, which can be found at:

www.gov.uk/government/uploads/system/uploads/attachment_data/file/672231/Tackling-tax-evasion-corporate-offences.pdf.

7 Conclusion

The implementation of an effective risk-based approach is essential to enable a housing association to mitigate against being used for money laundering or terrorist financing.

It should be borne in mind that money laundering affects the sector as a whole, and whilst the requirements imposed by the Regulations are a legal obligation on the regulated sector, all members should assess their money laundering risks across their full operations and apply proportionate measures to tackle the problem.

Supervisory authorities have many powers to enforce the legislation but the risk of sanctions against an association are likely to be low if adequate procedures and practices, as set out in this guidance, are implemented.

Appendix 1 Practical issues and proposed actions

Customer profile	Risk factor	Procedures in place to manage and mitigate the risks
New customer	Checking a new customer's identity is difficult.	Establish reasons for problem and see if they can be resolved. If suspicions arise, refer to the MLRO.
New customer	There is reluctance from a new customer to provide details of their identity.	Establish reasons for reluctance. Do not conduct business with customer and submit internal suspicious activity report to MLRO. Also be aware of the offence of tipping off.
Existing customer	The size of the transaction is not consistent with previous activity, for example, a customer on housing benefit suddenly has the funds for a deposit to fund a house purchase.	Enquiries as to source of funds, establish who is financing the transaction. Obtain bank statements or other documentation depending on the circumstances as proof of source of funding for transaction. Ensure all payments made through customer's bank account i.e. that you have identified the paying party.
Existing customer	The financial circumstances of an existing customer has changed, for example, the customer wishes to accelerate the purchase of ABC Housing Association's interest in a shared ownership property.	As above.
New or existing customer	Money is paid by a third party who has no obvious link with the transaction.	Establish nature of relationship between customer and third party. Confirm reason for third party involvement in transaction. Ensure that identification checks have been made of the paying party, their source of funds is checked and a risk assessment undertaken.
New or existing customer	The customer wants to pay a large sum in cash.	Where you agree to accept cash, inform the customer of cash limit (and consider an appropriate threshold by reference to type of transactions undertaken). Enquire as to reason for wishing to pay in cash and source of funds. Consider reporting to MLRO in order to obtain consent to proceed with transaction.

Customer profile	Explain how the risk factor applies	Procedures in place to manage and mitigate the risks
New or existing customer	The customer wants to pay a large sum in cash.	Where you agree to accept cash, inform the customer of cash limit (and consider an appropriate threshold by reference to type of transactions undertaken). Enquire as to reason for wishing to pay in cash and source of funds. Consider reporting to MLRO in order to obtain consent to proceed with transaction.
New or existing customer	A customer makes an approach to purchase a property then decides not to proceed on realising his or her identity will be checked for anti-money laundering purposes.	Report to MLRO. Do not undertake any business for customer.
Existing customer/ shared ownership purchase	Property purchase (medium risk).	<p>This is where an existing tenant purchases a shared ownership lease directly from the association. This is not a regulated activity and does not fall within the definition of 'estate agency work' therefore is not subject to the due diligence requirements.</p> <p>Good practice could include:</p> <ul style="list-style-type: none"> Confirming that customer identification data held is current and updating as necessary. Establishing source of funds and obtaining proof of income.
New customer/ shared ownership purchase	Property purchase (high risk).	<p>This is where a new customer purchases a shared ownership lease directly from the association. This is not a regulated activity and does not fall within the definition of 'estate agency work' therefore is not subject to the due diligence requirements.</p> <p>Good practice could include:</p> <ul style="list-style-type: none"> Identifying customer using documents and considering using an electronic check. Establishing source of funds and obtaining copies of bank statements as verification. Ensuring all transactions are conducted through customer's own bank account.

Customer profile	Explain how the risk factor applies	Procedures in place to manage and mitigate the risks
Existing customer/ right to buy purchase	Property purchase (low/medium risk).	<p>This is where an existing tenant exercises right to buy. This is not a regulated activity and does not fall within the definition of 'estate agency work'.</p> <p>Good practice could include:</p> <p>Confirming that customer identification data held is current and updating as necessary. Enquiring as to source of funds and obtaining evidence.</p>
New customer/ new property purchase	Property purchase (high risk).	<p>This is where new customer buys a property directly from the association. This is not a regulated activity and does not fall within the definition of 'estate agency work'.</p> <p>Good practice could include:</p> <p>Identifying customer using documents/electronic check. Establishing source of funds and obtaining copies of bank statements and wage slips. Ensuring all transactions are conducted through customer's own bank account. Check if customer fits the definition of a PEP. Check the Treasury sanctions list.</p>
New customer/ non-UK national/ new property purchase	Property purchase (high risk).	<p>This is where new customer buys a property directly from the association. This is not a regulated activity and does not fall within the definition of 'estate agency work'.</p> <p>Good practice could include:</p> <p>Identifying customer using documents/electronic check. Verifying source of funds and obtaining evidence in documentary form. Checking if customer fits the definition of a PEP. Checking the Treasury sanctions list. Ensuring all transactions are conducted through a UK bank account. Referring to line manager before proceeding.</p>

Appendix 2 List of documents for use in establishing identification

Private individuals

For customers that are private individuals, the business should obtain full names, residential addresses and their date of birth.

Verification of this information must be based on reliable independent sources. This may be by documents provided by the customer or information obtained electronically by the business or both.

If the verification of the customer's identity is done by documents, this should be based on a government-issued document with the customer's full name and photo, with either the customer's date of birth or residential address, such as:

- valid passport, valid photocard driving licence, national identity card, firearms certificate, identity card issued by the Electoral Office for Northern Ireland, or
- where the customer does not have the above documentation you can accept a government-issued document (without a photo) which includes the customer's full name and supported by secondary evidence of the customer's address such as:
 - old style driving licence
 - recent evidence of entitlement to state or local authority-funded benefit such as housing benefit, council tax benefit, pension, tax credit, pension, educational or other grant
 - instrument of a court appointment (such as liquidator, or grant of probate)
 - current council tax demand letter, or statement.

Examples of secondary evidence to support a customer's identity include: a utility bill, bank, building society or credit union statement, most recent mortgage statement from a recognised lender.

Sufficient checks should be made of the documentary evidence to satisfy the business of the customer's identity. This may include checking spelling of names, validity, photo likeness, whether addresses match etc.

Where a member of the business's staff has visited the customer at his or her home address a record of this visit may constitute evidence of corroborating the individual's residential address (for the purposes of a second document).

If the verification of the customer's identity is done by electronic means the business should undertake these checks from two separate sources. A copy of the electronic check should be retained or information recorded as to where a copy of the evidence can be found.

When a member of the association's staff has not been able to meet the customer in person, the association can choose to accept certified copies of identification documents. A certified copy must be no more than three months old, certified by a UK solicitor, who appears on the roll of The Law Society of England & Wales or of Scotland, a chartered accountant on the roll of the Institute of Chartered Accountants of England and Wales (ICAEW), an accountant or a lawyer of another jurisdiction whose credentials you have verified through their relevant professional directory, or certification by a British Embassy or consular official. You must ensure that you receive a hard copy ('wet-ink') of the certified copy, which is signed and dated by the individual certifying it. A scan of the certified copy is not sufficient.

To accept a certified copy certified by any other third party, you must first obtain approval of the MLRO or deputy MLRO. A request for approval must state the reason for using the third party and who it is you are proposing to obtain the certified copy from.

Customers other than private individuals

For customers that are not private individuals, such as corporate customers, partnerships, and private companies, the business must obtain information that is relevant to that entity which includes:

- the full name of the company
- company or other registration number, and
- registered address and principal place of business.

It is also necessary to establish the names of all directors (or equivalent) and the ultimate beneficial owners of such entities.

Verification of identification must be from reliable independent sources (relevant to that entity type) such as a search of a relevant company registry, confirmation of the company's listing on a regulated market, or a copy of the company's certificate of incorporation.

How do businesses identify beneficial owners?

Associations are required to put in place measures to identify the existence of ultimate beneficial owners. Where an association has reason to believe or suspect, or has identified, that a customer is controlled or owned by a beneficial owner they should verify the beneficial owner's identity on a risk-sensitive basis.

In verifying the beneficial owner's identity, the business should be satisfied that it knows who the beneficial owner is and understand how they operate. This may include finding out who has ownership or control over the funds, or who is the controlling mind.

On a risk-sensitive basis the business should decide how it verifies the identity of beneficial owners. This may include requiring the customer to provide information directly, making use of publicly available documents or verifying the identity of the beneficial owner by some other means.

Appendix 3 Template internal suspicious activity report

ABC Housing Association Internal Suspicious Activity Report

Date	
Name and designation of member of staff	
Suspected person(s): Name/address/business address/telephone nos. Name of client if different Details of relevant transaction	
Nature of suspicious activity. Give full details of suspicion and date suspicion first aroused Continue overleaf if necessary Include details of transactions and identity checks Attach any relevant documents	
To be completed by MLRO	
Refer to NCA/do not refer to NCA	
Reason for decision	
Signature	
Date referred to NCA	

Appendix 4 Frequently asked questions

Q. Are we subject to the Regulations?

A. Any person can commit an offence under the Proceeds of Crime Act (as set out in part 3 Money laundering legislation) but the Regulations only apply to the regulated activities which are being undertaken by the organisation. In the social housing sector, these activities are likely to be any kind of lending or estate agency work e.g. shared ownership resale. Therefore, the customer due diligence requirements will only apply to transactions in the regulated part of the business. In addition, offences under the POCA relating to a failure to report or tipping off will only apply to the regulated activities.

Q. Do we need to produce a formal anti-money laundering policy?

A. Yes. It is important that staff have a clear and concise policy to which they can refer. The document should include the organisation's high-level commitment to applying anti-money laundering policies, risk assessment and reporting procedures. Many businesses include the document on the intranet and attach a form which staff can use to report suspicious activity internally. (See part 5: Compliance, registration, systems and controls.)

Q. What areas should the anti-money laundering policy cover?

A. The policy should apply to the regulated activities undertaken by the organisation and the necessary procedures for compliance with the Regulations. In addition, should the MLRO become aware of any suspicious activity in another part of the business, they will be required to consider a report to the NCA just as the report had come to them from the regulated part of the business.

Q. How do we identify which staff need training?

A. Much depends on the role undertaken by the individual staff member. Staff in those parts of the business which are part of the regulated sector are required by law to receive training. The MLRO and their deputy, and the officer for compliance, obviously need to have an in-depth understanding of the subject. Other staff involved in treasury/finance/property sales should also be trained to recognise suspicious activity and be aware of the reporting system. Staff in housing management functions will also benefit. (See part 5: Compliance, registration, systems and controls.)

Q. We do not carry out business in the regulated sector, how should we deal with this issue?

A. Many areas of business carried out by associations carry a risk of being targeted by money launderers. Adequate controls need to be put in place to address those risks and, as can be seen from the section of this guidance relating to money laundering methods, many of the crimes involved also carry health and safety risks to staff and tenants alike. (See the Introduction and part 5: Compliance, registration, systems and controls.)

Q. We have a good working relationship with local police already. Does this system change anything in connection with that relationship?

A. Obviously those relationships need to be maintained and nothing in the system and controls put in place should detract from that. The National Crime Agency disseminates information from suspicious activity reports to law enforcement, including police forces throughout the UK. (See the introduction and part 5: Compliance, registration, systems and controls in this guidance.)

Q. What issues may generate suspicions and concerns relating to money laundering generally?

A. Examples of specific activities which may rise to suspicions or concerns are:

- cash payments including large sums which may be made in payment of rent arrears
- overpayments to sinking funds
- customers receiving unexplained sums into their bank account
- individuals who receive wages/payments on a cash basis
- tenants exercising Right to Buy being hesitant to provide information on the source of funds
- sub-letting of tenanted units in breach of prohibitions on doing so.

Q. Will there be future fees for businesses supervised by the OFT?

A. The supervisory authorities will help business to reduce the risks of being used for money laundering by producing guidance, giving advice to business and raising awareness levels generally. They have powers to take enforcement action where appropriate including to imposing financial penalties against those businesses that fail to put in place the required anti-money laundering systems and controls.

Notes

Notes

Guidance on anti-money laundering - *How it affects members of the National Housing Federation*

- What is money laundering and why does it happen?
- Where does the money come from and how does it affect the sector?
- Money laundering legislation
- The regulated sector
- Compliance, registration, systems and controls
- Common methods used to launder money.

The National Housing Federation is the voice of housing associations in England. Our vision is a country where everyone can live in a good quality home they can afford. Our members provide two and a half million homes for more than five million people. And each year they invest in a diverse range of neighbourhood projects that help create strong, vibrant communities.

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