

# Regulatory Approach to Anti-Money Laundering in Online Gambling in the UK

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## Abstract

The chapter analyses the AML regime in the online gambling market in the UK, focusing on the nature of its institutional setup and the evolution of its regulatory approach. The analysis questions which enforcement strategies and styles the sectorial regulator—the Gambling Commission—pursued under the overarching framework of risk-based regulation. The findings indicate two stages in the Gambling Commission's work one characterised by low deployment of responsive regulation coupled with an advisory (conciliatory) enforcement style, and the sub-sequent stage characterised by a shift towards greater use of responsive regulation and a more punitive enforcement style, which was also coupled with capacity-building enrolment of gambling operators through non-mandatory channels. After discussing the implications of the two approaches for the regime's performance, the analysis contextualises them against wider debates about the operation of risk-based regimes and conditions for successful operation of risk-based frameworks.

## 1. Introduction

The online gambling market is a lucrative market, with an estimated global value of USD 53.7 billion in 2019.<sup>1</sup> In the UK, the yield revenue last year only in the online gambling market amounted to about GBP 5.3 billion.<sup>2</sup> With continuing gambling liberalisation across the world and the ever-expanding opportunities created by digitalisation, the gambling market is expected to continue growing in the next decade at a steep rate.<sup>3</sup>

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<sup>1</sup> Grand View Research (2020).

<sup>2</sup> Gambling Commission (2019a), p. 16.

<sup>3</sup> Projections are that its average annual growth for the period 2020 to 2027 will be 11%; see Grand View Research (2020).

Yet, just as it opens up business opportunities, the agility of online gambling platforms represents at the same time a source of major integrity risks. Vulnerability to money-laundering (ML) practices is one of them.<sup>4</sup> Since it enables cross-jurisdictional access for customers and fast money turnover transactions, the online gambling sector makes for a challenging environment for the pursuit of AML. Online gambling wagers provide ample opportunities for remote placement and real-time withdrawal of 'layered' monies, which could then be integrated, as 'laundered' proceeds, back at the 'source'.<sup>5</sup>

This chapter reviews the nature and evolution of the AML regime in the online gambling market in the UK, covering the period from its early days, back in the late 2000s, until the start of the 2020s. The analysis will review the nature of the institutional setup of the regime and how its regulatory approach evolved as it sought to address ongoing and emerging ML challenges. The main focus will be on the regulatory strategy and enforcement style that the sectorial regulator—the Gambling Commission (henceforth: the Commission)—pursued over the observed period, and their implications for the conduct of the gambling industry and its AML performance.

## 2. UK Online Gambling Market, the Role of the Gambling Commission and the Licencing System

The UK was among the first countries to liberalise its online gambling sector, back in 2005. As an early adopter, it has subsequently developed a large and diverse gambling market, which today is home to a gambling industry of more than 2600 registered operators—casinos and sports bookmakers—both online and offline,<sup>6</sup> with about 24 million gamblers overall, 11 millions of which are online gamblers.<sup>7</sup> The UK gambling market features a licensing model based on unrestricted market competition. This is a model shared by several other countries in the European Union<sup>8</sup> and beyond; other models of gambling regulation include markets with limited competition (with a fixed number of licences), markets where the state holds a monopoly in operating the gambling market, and markets where gambling—particularly online gambling—is illegal.

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<sup>4</sup> While HM Treasury and Home Office (2020, p. 131) assessed the overall ML risk in the gambling sector—when compared to other sectors—as low, the Gambling Commission (2020a, p. 4) assesses the online gambling sector as a high-risk area for ML.

<sup>5</sup> Besides 'cleaning' monies gained through criminal activity, the definition of ML in the UK criminal system also covers other activities related to criminal proceeds such as concealment, acquisition, use, and transfer of criminal proceeds; see Section 340 of the Proceeds of Crime Act 2002 (POCA).

<sup>6</sup> Gambling Commission (2020b), p. 12.

<sup>7</sup> Gambling Commission (2020b), p. 17.

<sup>8</sup> See, for instance, Laffey et al. (2016).

The UK operated the ‘point of supply’ system until 2014, when it shifted to the ‘point of consumption’ mode under which gambling operators are subject to the licencing regime based on where bets and wagers are placed rather than where the physical location of the gambling operator is. This means that, to advertise or operate their gambling offers in the UK, foreign-based operators would need a licence from Commission, even if their equipment is physically based in another country.<sup>9</sup>

In the gambling market, licences could be granted to both land-based and remote (online) gambling operators (casinos or betting operators). Licences are also given to individual employees who hold compliance responsibilities in those operators. While licences to gambling operators are one-off, i.e. indefinite, the licences for compliance officers are issued for a five-year period and are subject to renewal.<sup>10</sup> Third parties such as software suppliers, business-to-business (B2B) platforms, game suppliers or sportsbook platforms are all subject to licencing conditions, although ancillary services such as customer verification services or payment processing services are not.<sup>11</sup> To start a business, all gambling operators need to pass the usual criminal background checks conducted by the Commission<sup>12</sup> and financial probity tests by other supervisory bodies in the wider AML framework, such as the Financial Conduct Authority and the HM Revenue and Customs.<sup>13</sup>

Licensing standards for online gambling operators are set and controlled by the Commission. The Gambling Act 2005<sup>14</sup> has mandated the Commission to act in a double capacity: as the sectorial regulator and as an enforcement body for violations of the regulated standards. The Commission thus issues Licence Conditions and Codes of Practices (LCCPs), awards licences to market entrants, monitors their compliance with these standards, and carries out enforcement and sanctioning measures when breaches of licencing rules are identified.<sup>15</sup>

In performing these standard-setting, investigatory and sanctioning roles, the Commission can avail itself of a wide range of powers entrusted by the legislation. It has discretionary powers to decide when and what investigations will be under-taken. Also, to investigate whether a gambling operator has observed the licencing regulations, the Commission can choose between conducting a full or targeted assessment (the latter would focus on checking compliance with part, instead of all of the licence conditions, and/or some but not all operators).

The Commission can conduct criminal and financial investigations, including investigations into ML. The resultant measures could be ‘no further action’, an

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<sup>9</sup> See Section 1 of the Gambling (Licensing and Advertising) Act 2014. For further explanations see Chess and Elliott (2021).

<sup>10</sup> See Financial Action Task Force (2018), p. 128.

<sup>11</sup> Chess and Elliott (2021).

<sup>12</sup> Financial Action Task Force (2018), p. 127.

<sup>13</sup> Financial Action Task Force (2018), pp. 124–125.

<sup>14</sup> For the latest, legislative review of the Gambling Act, which, at the time of writing, is still in progress, see Department for Digital, Culture, Media and Sport (2020).

<sup>15</sup> Sections 22 to 28 of the Gambling Act 2005.

advice, a caution, and a prosecution.<sup>16</sup> The Commission's regulatory and licence reviews can result in 'no further action', a licence surrender, an informal warning, a formal warning, an imposition of additional licence conditions, a financial penalty, a licence suspension, or a licence revocation.<sup>17</sup>

This setup of powers has given the Commission a strong basis for the pursuit of responsive regulation,<sup>18</sup> a mode of regulation which enables a regulator to escalate sanctions over time as it is observed that a regulated operator continues to be non-compliant. The Commission also has enjoyed the possibility to lift the 'base' sanctions if it appraises that the industry as a whole has been showing repeatedly low levels of compliance. With its discretionary power to decide whether to take less or more punitive measures, the Commission could decide how extensively and how fast the regulatory approach will move across the so-called enforcement pyramid<sup>19</sup> whose bottom comprises the most benign and top the most severe sanctions.

### 3. The Architecture of the AML Regime in UK Online Gambling

The online gambling anti-money laundering (AML) regime is part of the wider AML regime in the UK, with which it shares the institutional framework whilst at the same time representing a sub-regime in itself. Although the online gambling sector is seen as posing a high ML risk, the majority of it has not been subject to the Money Laundering Regulations 2017 (MLRs), which covers only casinos (both online and offline).<sup>20</sup> Yet, although not being subject to MLRs, online betting operators are obliged under the Proceeds of Crime Act 2002 (POCA) and the Gambling Act 2005 to keep crime, including ML, out of their sector<sup>21</sup> and, accordingly, develop AML policies and controls and report suspicious activities to the National Crime Agency (henceforth: NCA); failure to do so would bring them in violation of POCA (2002).<sup>22</sup>

The AML framework in the gambling market is centred around two key actors—the Commission and NCA. The Commission is the sectorial regulator, whose remit is tied exclusively to the gambling sector. NCA is the UK's 'nodal' law enforcement agency for AML policy, whose jurisdictions cover the whole of

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<sup>16</sup> Gambling Commission (2012), p. 18.

<sup>17</sup> Gambling Commission (2012), p. 17.

<sup>18</sup> Ayres and Braithwaite (1992).

<sup>19</sup> For more about the concept of enforcement pyramid see Ayres and Braithwaite (1992), pp. 35–38.

<sup>20</sup> Regulation 8 of the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (MLRs).

<sup>21</sup> Gambling Commission (2020c), p. 6.

<sup>22</sup> Gambling Commission (2020c), pp. 6–

the AML regime. Other bodies, such as the National Economic Crime Centre, HM Treasury, and the Joint Money Laundering Intelligence Taskforce can play supervisory and/or coordinating roles in the UK AML policy, including the AML policy in the gambling sector. The focus of this chapter will be on the work of the ‘information gathering system’, centred around the above mentioned Gambling Commission and NCA, whose efforts are oriented towards ensuring that gambling operators have developed systems and practices capable of identifying suspicious customers’ transactions.

There are two main priorities that regulatees, namely the gambling operators, are supposed to meet in relation to their AML obligations. First, they need to develop systems for early verification of customer profiles (customer due diligence—CDD), and identification of suspect customers’ behaviours indicative of ML practices. Where possible, such systems would prevent gambling and withdrawal of money in suspect cases. Second, gambling operators need to deliver to NCA so-called suspicious activity reports (SARs) on such cases, in line with the Commission’s guidelines, legislative requirements and international reporting standards. SARs are known as the main AML instrument for alerting the law enforcement bodies of potential cases of money laundering which enable the latter to detect, investigate, and prosecute such cases.

The main reporting challenge that gambling operators face is to maximise the number of SARs while keeping them well-targeted. This means that gambling operators should not let any of the suspicious cases go unreported, but at the same time they should avoid reporting cases that do not feature sufficiently strong indicators that a customer’s gambling pattern or transaction might have involved ML.

If SARs are ‘under-produced’, the investigative authorities will simply not be aware of some major cases that merit investigation. If, on the other hand, SARs are ‘over-produced’, this will reduce the efficiency of the investigatory process, as it increases the amount of investigators’ resources spent on examining irrelevant details. A credo that might aptly apply here is that—telling everything equals revealing nothing.<sup>23</sup>

‘Under-production’ of SARs by gambling operators can occur for two main reasons. First, gambling operators might be unwilling to produce SARs. This can happen due to the lack of effective sanctions for non-compliance, the prevailing interest of a gambling operator to avoid disrupting customer relationships, or simply the operator’s intention to take in as much betting money as possible. Second, gambling operators might lack the capacity to track and identify transactions and write up reports in an appropriate form before sending them to NCA and/or the Commission.

The most common driver of ‘over-production’ of SARs is the risk-averse attitude of gambling operators who might seek to dispel any risk of being accused

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<sup>23</sup>Takáts (2011).

of 'under-reporting'. The AML regulation is namely predominated by a principles-based<sup>24</sup> rather than a rules-based regulatory approach meaning that the standards for production of SARs are defined by broader principles rather than precise rules. This is because in the gambling market, the dynamic and customers' gambling patterns are often unpredictable, evading easy 'parametrisation'.<sup>25</sup>

Operators have to do CDD when they are establishing a business relationship with a customer, suspecting ML, or doubting the veracity of identification documents provided by a customer.<sup>26</sup> Also, gambling operators are obliged to do CDD, i.e. identify and verify a customer's identity, if (s)he makes a transaction amounting to €2000<sup>27</sup> or makes an occasional transaction of €1000 or more.<sup>28</sup> After applying CDD, a nominated officer in the gambling operator is required to report to NCA, in the form of a SAR, every customer for whom they know or suspect has been or will be engaged in ML; failing to report such knowledge or suspicion makes the official criminally liable.<sup>29</sup>

However, there is a range of patterns in the gambling sector that can raise a suspicion whilst not constituting sufficient grounds to be reported to NCA. A customer may have legitimate reasons to gamble through 'unusual' patterns, for instance by betting 'erratically', with large stakes within short periods of time, followed by longer periods of non-betting and then return to large bets.<sup>30</sup> Addition-ally, gambling operators offer different products, deal with various customers in terms of their spending (high vs low spenders) and geographical locations (the UK vs third countries' customers), and use different means of payment (e.g. cash, pre-paid cards and e-wallets).<sup>31</sup> Hence, rather than providing details on when and how gambling operators should classify customers' activities as suspicious, the Commission's guidelines had to remain somewhat broad and subject to on-spot interpretation by gambling operators. As a result of the specific nature of the sector, as well as the legal requirements related to AML, gambling operators will inevitably have some discretion in developing their AML procedures and controls.<sup>32</sup>

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<sup>24</sup>Black (2008).

<sup>25</sup>See, for instance, Brooks (2012), p. 310.

<sup>26</sup>Regulation 27(1)(a), (c), (d) of the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (MLRs). On certain occasions gambling operators apply enhanced CDD (e.g., if a customer is a politically exposed person or located in a high-risk country) or simplified CDD (this is often the case with UK residents); see Regulations 33, 34, 35, 36 and 37 of the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (MLRs).

<sup>27</sup>Regulation 27(5) of the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (MLRs).

<sup>28</sup>Regulation 27(1)(b) of the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (MLRs).

<sup>29</sup>Sections 330 and 331 of the Proceeds of Crime Act 2002 (POCA).

<sup>30</sup>Gambling Commission (2021), p. 60. See also Brooks (2012).

<sup>31</sup>Gambling Commission (2021), pp. 16–21.

<sup>32</sup>Gambling Commission (2021), p. 14.

At the same time, this can, in practice, pose compliance risks for gambling operators when distinguishing between suspicious transactions and those that are not. Gambling operators cannot always be sure that their assessment of a certain customer's act or transaction as not being suspicious will necessarily be shared by the regulator. This will often drive the operator to adopt reporting practices that prefer erring on the caution side, meaning that they will over-produce SARs.

Another, more malign, and probably less present motivation for 'over-reporting' could relate to deliberate attempts of gambling operators to 'burry' some ML cases within as large a pool of SARs as possible. This would lead to a situation in which the investigative authorities' work would look like a search for the proverbial 'needle in a haystack'. Through such deliberately misleading over-reporting a gambling operator can help money-launderers to reduce the chances of being noticed by the investigative authorities, whilst at the same time displaying compliance with the reporting requirements.

Overall, the main interest of the NCA and the Gambling Commission has been to spur gambling operators to develop such reporting procedures whose 'net' would catch the suspicious cases whilst triaging out less relevant ones. However, developing a system that would in practice align operators' conduct with those priorities is not a straightforward endeavour.

## 4. The Risk-Based Regulation in Practice

### 4.1. The First Decade of Gambling Market Regulation (2007–2016)

The Commission's regulatory enforcement covers a range of areas, from customer protection to tackling socially irresponsible practices such as underage gambling, through cracking down on illegal unlicensed gambling operators to ensuring whether operators have AML checks in place. From its early days, Commission adopted a risk-based approach,<sup>33</sup> in line with the 2005 Hampton Report recommendations which made a system-wide call in the UK for risk-based regulation as an arguably cost-effective and the least burdensome approach for regulated industries.<sup>34</sup> The risk-based approach implies that regulatory activities should be focused on those operators and activities that pose the highest risk to the regulatory objectives.<sup>35</sup> In the beginning, the Commission was paying visits to the majority of gambling operators in order to assess sectoral and operational risks,<sup>36</sup> identifying 40 largest operators in the industry, betting operators and casinos, that represented 80% of the overall

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<sup>33</sup> For more about risk-based regulation see Hutter (2005).

<sup>34</sup> Hampton (2005).

<sup>35</sup> Gambling Commission (2007), p. 6.

<sup>36</sup> Gambling Commission (2007), p. 6.

gambling activity, as those posing the highest risk of ML.<sup>37</sup> These operators became the central focus of the Commission's forthcoming inspections which were under-taken through a recurring cycle.<sup>38</sup> Occasionally, the Commission would act upon information from media reports and customer and police tip-offs, undertaking unplanned on-site inspections.<sup>39</sup> The Commission's control of smaller companies was mainly based on desk reviews, which examined whether the controls in place were adequate.<sup>40</sup>

During the first 10 years, the Commission practiced a light-touch mode of regulation, characterised by limited monitoring activity and prioritisation of regulatees' learning over their sanctioning.

The Commission thus positioned itself more as an advisory body and less as a punitive regulator. Its public statements and published reports sent repeated messages that the goal of the extant risk-based approach was to foster a learning environment within operators as well as across the industry.<sup>41</sup> This approach featured an element of meta-regulation<sup>42</sup>—regulated subjects and industries were expected to understand, within their own individual contexts, where high risks of ML lie, and then develop internal systems to address these risks which they would test, review and revise over time.

The Commission tended to avoid "adversarial licence reviews"; licence reviews were usually undertaken when serious failings in AML compliance were discovered.<sup>43</sup> Where such failures were identified in a gambling operator, the sanction that Commission most frequently imposed was a voluntary settlement, which takes away from the gambling operator removal of the financial benefit stemming from the identified breaches of AML regulation coupled whilst at the same time mandating it to make a payment to Commission to cover the enforcement costs.<sup>44</sup>

Furthermore, although its wide-ranging powers gave it abundant possibilities to undertaking responsive regulation, when it was observed that a regulatory violation has been repeated, the Commission rarely escalated its enforcement. Escalations in sanctions mainly involved financial penalties. Licence suspensions and terminations were rare, as illustrated in the table below Table 1.

Thus, during the first decade of its existence, the Commission's approach was based on limited monitoring and, in the enforcement aspect, rare 'excursions' outside the lower tiers of the enforcement pyramid. In other words, the use of responsive regulation was negligent. The Commission exhibited behaviours that

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<sup>37</sup> Financial Action Task Force (2018), p. 133.

<sup>38</sup> Financial Action Task Force (2018), p. 133.

<sup>39</sup> Financial Action Task Force (2018), p. 133.

<sup>40</sup> Financial Action Task Force (2018), p. 133.

<sup>41</sup> Gambling Commission (2013), p. 4. See also Gambling Commission (2015), p. 18.

<sup>42</sup> Coglianese and Mendelson (2010).

<sup>43</sup> Gambling Commission (2015), p. 8.

<sup>44</sup> Gambling Commission (2015), p. 7.

**Table 1.** The extent of the Commission's remedial actions for casinos' AML-breaches

	2013	2014	2015	2016
Attaching AML-specific licence conditions to a casino's licence	—	0	1	1
Warnings issued to casinos	1	0	1	1
Voluntary settlements	2	1	2	4

Source: Financial Action Task Force (2018), p. 138

Note: Data for betting operators is not available, but trends were probably similar, if not featuring fewer and milder sanctions, since in the 2007–2017 period the Commission's enforcement generally was more extensive among casinos

are characteristic of the so-called conciliatory enforcement style, also known in the regulatory enforcement literature as persuasive enforcement style.<sup>45</sup> This enforcement style features an emphasis on learning and education of regulatees and low use of punitiveness in the sanctioning policy.

Towards the mid-2010s, it was becoming obvious that this approach can hardly ensure compliance with the AML principles across the industry. The Commission's inspections found a considerable extent of repeated operators' breaches of the basic AML requirements. Several high-profile cases that occurred in 2015 and 2016 exposed the existence of blunt breaches of the licencing conditions even in some of the most prominent bookmakers in the industry.<sup>46</sup>

This trend of poor compliance was not easy to reverse in the period to come, even after Commission undertook a shift in its approach. For instance, a later report by HM Treasury and Home Office showed that as much as 48% of casinos subject to an inspection, between 2018 and 2019, did not comply with the AML regulations.<sup>47</sup> After the passage of the first decade, the number of SARs submitted to NCA by the industry still stood extremely low. Between October 2015 and September 2016, only 3054 SARs, including 735 DAML (defence against money laundering) SARs, were submitted by the gambling operators.<sup>48</sup> This made up less than 0.4% of the total number of SARs submitted in all sectors in the UK.

At some point in 2015, the Commission started warning that, if operators continue to “ignore such ‘lessons’”, the Commission “will be forced to act more punitively”.<sup>49</sup> This announced a Commission's regulatory shift towards greater reliance of responsive regulation.

<sup>45</sup> Kagan (1989), p. 92. See also Gunningham (2010).

<sup>46</sup> One of such cases is William Hill's failure to reject repeated bets by its customer worth more than half a million-euro; see Gambling Commission (2018a).

<sup>47</sup> HM Treasury and Home Office (2020), p. 136.

<sup>48</sup> National Crime Agency (2017), pp. 46–51.

<sup>49</sup> Gambling Commission (2015), p. 7.

## 4.2. A Regulatory Shift: The Post-2017 Developments

Amidst growing public adversity and repeated evidence of failure to ensure the basic AML protections in the industry,<sup>50</sup> the Commission announced, in 2018, that there is going to be a rise of standards for the gambling industry,<sup>51</sup> signalling also that its “approach to enforcement is getting tougher”.<sup>52</sup> Indeed, in the period to come, it increased standards for compliance through a series of licencing code and guidelines changes, including those related to gambling operators’ procedures for customer identification (KYC).

The Commission also increased its investigative activity related to ML. Within 1 year only, it doubled the number of investigations, from 75 regulatory and criminal investigations (including 22 ML-related investigations) carried out in 2017<sup>53</sup> to 161 investigations in 2018, including investigations related to ML.<sup>54</sup> In 2019 the number of investigations slightly decreased—to 130<sup>55</sup>—yet, compared to the pre-2017 activity, the focus on ML remained strong, especially in the online gambling sector.<sup>56</sup>

Further, the Commission’s enforcement style became more punitive. In 2019 alone, it suspended 5 and revoked 11 operators’ licences.<sup>57</sup> The Commission also started to impose greater financial penalties. In 2017, it issued over £18 million worth of fines for AML failings and other breaches.<sup>58</sup> During 2018/2019, several online casino operators and their senior management members were fined because of their social responsibility and AML failings.<sup>59</sup> This was followed by investigations of a number of online operators in 2019 that have been in breach of the licence conditions related to AML and social responsibility.<sup>60</sup> As a result, 12 operators received financial penalties or proceeded to make regulatory settlements.<sup>61</sup>

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<sup>50</sup> This followed several public revelations of casinos’ and bookmakers’ failure to ensure the basic social responsibility protections in offering products to their customers. A survey by the Commission from 2018 indicated that 38% of respondents believed that gambling is associated with crime. Stealing by gambling addicts and ML were cited as the most common criminal activities related to gambling. The survey also showed that more than 70% of participants saw gambling as an activity that could jeopardise family life. Failure to comply with AML standards was thus one piece in the emerging picture of regulatory failure in the gambling market; see Gambling Commission (2019b), p. 5.

<sup>51</sup> Gambling Commission (2018b), p. 22.

<sup>52</sup> Gambling Commission (2018b), p. 14.

<sup>53</sup> Gambling Commission (2018b), pp. 22–27.

<sup>54</sup> Gambling Commission (2019a), p. 19.

<sup>55</sup> Gambling Commission (2020b), p. 14.

<sup>56</sup> Gambling Commission (2020b), p. 14 and 21.

<sup>57</sup> Gambling Commission (2020b), p. 14.

<sup>58</sup> Gambling Commission (2018b), p. 14.

<sup>59</sup> Gambling Commission (2019c), p. 3.

<sup>60</sup> See Gambling Commission (2019c), p. 13 and Gambling Commission (2019a), p. 14.

<sup>61</sup> Gambling Commission (2020b), p. 21.

Overall, from 2018 onwards, the Commission moved away from the previously established practice of ‘light-touch’ regulation shifting to a more active and punitive enforcement style. Reliance on responsive regulation increased, as the punitive element increasingly prominent in tackling observed non-compliance in the industry.

Simultaneously with this increase in punitive measures, NCA and the Commission proceeded to strengthen collaboration with the industry. The main step in this direction was the engagement of representatives of NCA and the Commission in the work of the Gambling Anti Money-Laundering Group (GAMLG), later renamed as Betting and Gaming Council,<sup>62</sup> which brought together the two sides—the regulatory enforcers and regulatees (i.e. gambling operators). This forum, nowadays representing more than 90% of the gambling industry, was set up in 2016 to foster a dialogue about the importance of SARs in the fight against money laundering and other malpractices in the sector. It has offered training to representatives of gambling operators in the production of instrumental SARs. GAMLG was set up and chaired by a former Director General of NCA.<sup>63</sup> Since 2017, a series of meetings between GAMLG and NCA were held and these were assessed as successful by all sides in the dialogue, resulting in improvements in intelligence gathering on potential ML practices in the gambling sector.<sup>64</sup>

During 2017–2018, the overall number of SARs submitted by gambling operators amounted to 3768 (including 943 DAML SARs<sup>65</sup>)—an increase from the prior period. This trend of growth in the volume of SARs submitted by the gambling industry continued in the subsequent period, with 7514 SARs, including more than 1800 DAML SARs, being submitted to NCA during 2019–2020.<sup>66</sup> Alongside the volume, the quality of SARs increased too, as testified by NCA.<sup>67</sup>

While those are some early signs of progress, a question remains how far these figures are from the needed volume of SARs. Despite the steep rise, the number of SARs submitted by gambling operators is still low when compared to the quantity of SARs produced by operators in the banking sector.<sup>68</sup> The UK Financial Intelligence Unit has been of the opinion that further progress is needed in increasing the amount of SARs.<sup>69</sup> Another caveat regarding the positive achievements that the recent regulatory shift has generated concerns possible ‘creative compliance’ responses

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<sup>62</sup>National Crime Agency (2020a), p. 17.

<sup>63</sup>National Crime Agency (2020a), p. 17.

<sup>64</sup>National Crime Agency (2021), p. 5.

<sup>65</sup>National Crime Agency (2018), pp. 15–18.

<sup>66</sup>National Crime Agency (2020b), pp. 20–23.

<sup>67</sup>See National Crime Agency (2017), p. 14 and National Crime Agency (2021), p. 15.

<sup>68</sup>In 2019–2020 banks submitted more than 400,000 SARs; see National Crime Agency (2020b), p. 9.

For detailed statistics of the SARs produced by gambling operators see HM Treasury and Home Office (2020), p. 137.

<sup>69</sup>National Crime Agency (2021), p. 5.

by gambling operators that could emerge in the future. Studies in the banking sector have observed that the more a risk-based regime shifts the responsibility from the regulator to the regulatees, the more regulatees start overproducing reports as a risk-avoidance response.<sup>70</sup> Banks, for instance, often resort to such strategies<sup>71</sup> to dispel the risk of being declared non-compliant.<sup>72</sup>

The question, therefore, is whether in the forthcoming period, even if they continue to increase the number of submitted SARs, gambling operators will fall to the same ‘pathology’ as the banking sector often does, exacerbating the potential mismatch between the amount of SARs submitted to NCA and their quality, i.e. how well ‘targeted’ they are. If they do not submit a sufficient amount of SARs, gambling operators might—particularly under the increasingly punitive approach—be declared non-compliant on the grounds of missing to report some transactions that could possibly be interpreted as carrying the risk of ML. Yet, if they start ‘churning out’ SARs at the expense of ‘effective targeting’, this could inhibit rather than facilitate NCA’s analytical work.

## 5. Discussion

Within the broader framework of risk-based regulation, the Commission has enjoyed a favourable setup to pursue responsive regulation, with its wide range of monitoring, enforcement, and investigative powers. What was then its regulatory approach in dealing with AML during the first decade of its operation? The above review offers some preliminary insights that feed into debates about the efficiency of various enforcement strategies and styles in addressing regulatory challenges under a risk-based framework.

We could see that, during the first decade of its operation, the Commission opted for a light touch mode of regulation in tackling ML. With a focus on ‘advice and persuasion’ rather than deterrence through punitive measures, the Commission exhibited the so-called conciliatory enforcement style.<sup>73</sup> The Commission also took little opportunity in this period of its responsive regulation potential to strengthen the punitive-deterrant aspect, making rare and slight escalations of sanctions for instances of repeated non-compliance among gambling operators. This approach could therefore be summarised as a ‘conciliatory and barely responsive ‘approach to risk-based regulation.

This approach however did not lead to satisfactory results, as indicated by repeated cases of operators’ non-compliance, the low number of submitted SARs, and emerging high-profile cases which showed that some of the largest gambling

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<sup>70</sup>Ross and Hannan (2007).

<sup>71</sup>Dalla Pellegrina and Masciandaro (2009), p. 3.

<sup>72</sup>Harvey (2004).

<sup>73</sup>Gunningham (2011), p. 174.

operators were not implementing the basic AML measures. One potential factor that might help explain the recurring non-compliance relates to the resource and commercial costs. Undertaking thorough checks and submitting instrumental SARs is costly in terms of staff and time allocation and constitutes resource drains for the gambling operators. Furthermore, alongside the deployed resources, the costs also involve potentially severed customer relations as reporting procedures tend to trigger which result from the disruption in the gambling and transactional routines. The gambling operators were therefore, facing considerable ‘negative incentives’ to develop adequate AML systems and practice.

At the same—and this adds another layer of potential explanation for the suboptimal regulatory outcomes in the first decade—the operators were not facing strong enough deterrence in the form of sanction threats. The argument of the pro-deterrence camp in the regulatory enforcement scholarship argues that, for motivating actors to adjust their conduct to the intended standards, a credible threat is needed, primarily in the form of severe enough sanctions.<sup>74</sup> According to this view, actors are primarily driven by rational calculations, based on threats and costs, rather than being self-motivated to improve the system through self-inspection. The regulatory environment surrounding the online gambling market between 2007 and 2016 did not provide such a constellation with a strong sanctioning deterrent for gambling operators.

Additionally, the Commission’s light-touch regulatory approach could be interpreted by the operators as an indicator of the its alleged pro-business attitude. This could have reinforced the operators’ expectations of future tolerance for their ‘lax’ compliance practices.

On a broader, enforcement strategy point—of how a system of risk-based regulation needs to be operated to adequately address regulatory challenges—Baldwin and Black suggest that risk-based systems need to have ‘really responsive’ regulation in place.<sup>75</sup> ‘Really-responsive’ regulation is characterised by a regulator’s continuous evaluation of the following five elements: (1) regulatees’ behaviour, attitude, and culture; (2) the institutional environment in which the regulation operates; (3) interactions of regulatory controls; (4) ongoing regulatory performance; and (5) the change that is taking place in the field.<sup>76</sup> A really-responsive regulator is one that continuously reflect on these evaluations and adjusts its approach accordingly. Failure to do so will lead to suboptimal regulatory results undermining the effectiveness of the risk-based approach.

While the above empirical analysis of the online gambling sector in the UK does not offer an exhaustive account of those five components, a cursory look into the above analysis nonetheless provides strong indications that during the decade of its existence the Commission was not even close to the pursuit of a ‘really-responsive’

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<sup>74</sup> See, for instance, Kagan (1989).

<sup>75</sup> Baldwin and Black (2008).

<sup>76</sup> Baldwin and Black (2008), p. 69. See also Black and Baldwin (2010).

mode' of regulation. As a result, the diagnosed risks and uncertainties in the online gambling sector could hardly be adequately addressed.

How could the low rates of operators' compliance with the AML regulations be interpreted? As it became clear that the extant approach was dysfunctional, and as public adversity grew, the Commission started shifting its regulatory approach towards a more punitive one deploying responsive regulation to a greater extend. In the period after 2016, the Commission increased its focus on ML and started issuing harsher fines. This shift has altered the 'cost' calculation of the operators.

Simultaneously, alongside the increase in punitiveness and the growing emphasis on responsive regulation, NCA and the Commission worked to foster regulatees' enrolment<sup>77</sup> too. This was achieved through less mandatory forms of collaboration such as the newly formed Gambling Anti-Money Laundering Group (GAMLG). A platform that provided the operators continuous training in the production of SARs. Alongside gains in capacity building, this form of operators' enrolment lead to a reduction in the relational distance between the key law enforcement agency (NCA) and the sectorial regulator (the Commission), on one hand, and themselves as representatives of the industry, on the other hand.

The post-2017 regulatory intervention, therefore, included parallel processes. The first was greater deployment of responsive regulation, which relied more on punitiveness. The second was the enrolment of regulatees (gambling operators) which was aimed at increasing their capacities to recognise and mark potential ML cases through the production of instrumental SARs. Thus, the emerging regulatory strategy integrated the 'hard' element, that of deterrence, and the 'soft' element, that of voluntary actors' engagement through non-mandatory forums.

This illustrates that in practice a shift in the enforcement style can include simultaneous strengthening of both—the punitive and educational element—rather than necessarily featuring strengthening of one element at the expense of the other. While the Commission's reliance on the advisory attitude inevitably lessened in the formal process, an advisory component nonetheless remained, and even strengthened, outside the formal monitoring and enforcement space.

What were the effects of Commission's post-2017 regulatory shift? Although it is still early to provide a full assessment, there have been indications of progress when it comes to the immediate output, namely industry's engagement and the resultant volume and quality of reports delivered to the police. The fact that the number and quality of SARs increased could be interpreted as a step forward. Still, it is difficult to assess how far this progress is from an ideal point of operators' engagement and, whether the increase in operators' 'meaningful compliance' can be sustained in the long run.<sup>78</sup>

<sup>77</sup> Black (2003).

<sup>78</sup> For a discussion on the difficulty of assessing SARs' effectiveness, see, for instance, Bourton (2020), pp. 53–55.

On a more systemic level, questions about the success of AML policy go beyond the effects of ongoing regulatory activities and the work of the intelligence-gathering ‘complex’ of the AML regime. The key issue, as in any other AML context, is whether having more reports of suspected ML cases, which are of better quality, will eventually translate into effective law enforcement action and judicial processes. Lessons from the banking sector, from periods of improved ML reporting, are not too promising. In an earlier study of one thousand suspicious transaction reports made in the United Kingdom, during the early 1990s, Gold and Levi<sup>79</sup> found that, in a situation in which the number of SARs tripled—from more than four thousand to around thirteen thousand SARs per year—the yield that this improved ML reporting system unambiguously produced was only 13 drug trafficking convictions annually. This indicates that, when the number and quality of SARs increases, absolute efficiency in AML policy cannot be taken for granted, even if the SARs’ increase is drastic. The old question that still remains pertinent is to what extent advances in the regulatory and enforcement regime can lead to major progress in the prevention and suppression of money laundering. Currently, the prevalent mood, based on indicative empirical analyses, is that AML policies are capable of achieving only marginal, if any success, in suppressing and reducing ML.<sup>80</sup>

Once NCA has received a SAR the second part of the AML procedure begins, which will crucially determine the policy effectiveness. In this stage, it is the law enforcement agencies and prosecutors that take control over the process. These actors, however, could face own challenges and ‘alignment’ issues. Each actor in the triangle—the Court, Prosecutor and law enforcement agencies (NCA in the first place)—might have own interests and performance priorities. Due to this mismatch in the police’s, court’s and prosecutor’s incentives, cooperation between these institutions in identifying, investigating and prosecuting offenders is often hampered. This lowers the chances of investigations eventually resulting in a successful trial and verdict.<sup>81</sup>

Further, information sharing among the involved authorities poses considerable challenges.<sup>82</sup> Institutions from the analytical ‘complex’ of institutions in the AML framework often operate in an uncoordinated manner, the individual law enforcement agencies do not always feed their information and analytics into a mutual system which would update its data as an investigation unfolds. The potential for information sharing among the law enforcement agencies will not be realised particularly where inter-institutional rivalries and turf-battles prevail.<sup>83</sup>

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<sup>79</sup> Gold and Levi (1994), p. 64.

<sup>80</sup> See Levi and Reuter (2006) and Levi and Maguire (2004).

<sup>81</sup> See, for instance, the paper by Sittlington and Harvey (2018) which discusses how in practice competing incentives among the three sides tend to diminish the effectiveness of the AML policy in the UK.

<sup>82</sup> Financial Action Task Force (2018), pp. 54–56.

<sup>83</sup> See Brown (2018).

## 6. Conclusion

The modern online gambling market in the UK will soon enter its fifteenth year of existence. This chapter has reviewed the nature and evolution of its AML regime of regulation. Two stages in the regime's operation were observed. The first stage—which encompassed the first decade of the Commission's existence—saw a conciliatory enforcement style with little reliance on responsive regulation. This approach, however, did not lead to satisfactory performance. In line with the expectations of the literature on enforcement strategies, its risk-based approach did not turn out particularly effective without greater deployment of responsive regulation.<sup>84</sup>

In the second stage, we could see a shift towards a more punitive regulatory approach with stronger reliance on the potential of responsive regulation. This was combined with increased enrolment of regulated parties, constituting a shift in the enforcement style that combined increases in punitiveness with a simultaneous strengthening of the advisory component that was achieved through less mandatory channels, outside the formal monitoring and enforcement process. There are early signs that this shift in the enforcement strategy and enforcement style has led to more productive contribution of the gambling operators to the AML policy.

The analysis points to several conclusions regarding conditions under which a risk-based regime is unlikely to perform successfully. First, a risk-based system can hardly operate with success if its regulatory strategy does not include punitive measures to disincentivise regulatees' non-compliance. Second, a risk-based approach assumes an element of regulatees' learning and updating of their compliance systems. A successful strategy therefore, needs to enable regulatees to build their capacities in order to respond to ongoing and changing regulatory requirements. The regulator also needs to perform continuous assessment and adjustment of its regulatory approach, to align with the changing environment and evolving non-compliance or 'creative compliance' strategies of regulatees. Third, punitive and educational in one regulatory strategy. Greater reliance on punitiveness can mean less space for 'correctional' and educational possibilities for regulatees, yet still learning opportunities can be compensated through less mandatory channels. Regulatees could be enrolled outside the formal enforcement process. This sort of regulatees' enrolment by regulatory and enforcement authorities can lead to the enhancement of the regulatees' understanding of how best to understand and address the risks in the sector and lead them to offer positive contributions to the goals of the given risk-based regime.

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<sup>84</sup> See Baldwin and Black (2008) and Black and Baldwin (2010).

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