ANTI-MONEY LAUNDERING COMPLIANCE ISSUES IN TOP 50 UK HEADQUARTERED LAW FIRMS IN ENGLAND AND WALES

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By

SARAH KEBBELL

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ABSTRACT

Anti-Money Laundering Compliance Issues in Top 50 UK Headquartered Law Firms in England and Wales – Sarah Kebbell

Money laundering is a global issue and there is increasing evidence to suggest that the services provided by law firms are being used to launder the proceeds of crime. In an attempt to combat their use as a money laundering conduit, law firms are required to comply with an array of anti-money laundering (AML) legislation and regulations.

This thesis explores the AML compliance issues encountered by participants from Top 50 UK headquartered law firms (by reference to turnover) when implementing the AML regime in the UK. The thesis draws upon empirical evidence from 40 in depth semi-structured qualitative interviews with participants from 20 Top 50 law firms. Participants comprised 20 solicitors at partner level and 20 compliance personnel who were either money laundering reporting officers (MLROs), Deputy MLROs, or held senior compliance roles within their organisations. Each of these participants was able to provide differing perspectives on the AML regime. Access to this section of the legal profession is challenging in the context of academic research, and therefore this thesis provides an account, seldom heard in academic literature, directly from practitioners in Top 50 law firms.

The thesis uses the research findings to explore and discuss the AML compliance issues faced by this section of the profession. It considers compliance issues relating to customer due diligence, AML training, the client account and the suspicious activity reporting regime. It also considers participants` perception of the regime, and their role within it. The evidence-based findings are then used to recommend amendments to AML policy, legislation and regulation.

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Ad metam contendo - I strive for the goal.

Chapter 1 – Anti-Money Laundering and the UK Legal Profession

1. Introduction

Evidence consistently demonstrates that the services offered by the legal profession are increasingly being utilised to launder money.[1] Whilst no reliable figures exist demonstrating the extent to which money laundering has pervaded the UK legal profession, complying with the UK`s anti-money laundering (AML) measures comes at a significant cost to the sector, with some law firms reporting annual compliance costs of `millions` of pounds.[2] The amount of money laundered globally is estimated by UNODC to be 2.7% of global GDP or US$1.6 trillion, and whilst the National Crime Agency (NCA) state that the amount laundered through the UK is unknown, it has been estimated to be between £36-90billion.[3] Whether or not such figures are accurate, the effects of money laundering are that it `can threaten the stability of a country's financial sector or its external stability more generally`. [4] Therefore any counter-measures respond `not only to a moral imperative, but also to an economic need`.[5]

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[1] `Money laundering` is the term used to describe the mechanism by which criminal proceeds are processed `to disguise their illegal origin`. FATF, 'Frequently Asked Questions' (*FATF*) <http://www.fatf-gafi.org/pages/faq/moneylaundering> accessed 17 November 2014. See FATF, *Money Laundering and Terrorist Financing Vulnerabilities of Legal Professionals* (2013). See also FATF, *Report on Money Laundering Typologies 2003-4* (2004); FATF, *Misuse of Corporate Vehicles Including Trust and Company Service Providers* (2006); FATF, *Money Laundering and Terrorist Financing through the Real Estate Sector* (2007).

[2] The Law Society, *The costs and benefits of anti-money laundering compliance for solicitors - Response by the Law Society of England and Wales to the call for evidence in the Review of the Money Laundering Regulations 2007* (2009) 48. For compliance costs see also The Law Society, *HM Treasury consultation on the transposition of the Fourth Money Laundering Directive -The Law Society Response* (2016) 4.

[3] UNODC, *Estimating Illicit Financial Flows Resulting From Drug Trafficking and Other Transnational Organized Crimes* (2011) 5; NCA, *National Strategic Assessment of Serious and Organised Crime 2016* (2016) 28, para 91.

[4] 'The IMF and the Fight Against Money Laundering and the Financing of Terrorism' (*IMF*, 30 September 2013) <http://www.imf.org/external/np/exr/facts/aml.htm> accessed 11 April 2014 per Min Zhu, Deputy Managing Director of the IMF.

[5] ibid.

The international response to the global money laundering threat is spearheaded by the Financial Action Task Force (FATF) which promotes and subsequently monitors the adoption of the `FATF Recommendations`.[6] These are internationally recognised as representing universal AML standards and have been adopted at EU level, and subsequently implemented at national level, via a series of directives culminating in the Fourth EU Money Laundering Directive (4MLD).[7]

These international and EU measures have converged to form an extensive AML compliance framework at a national level within which the UK legal profession operates. Legal professionals are subject to the Proceeds of Crime Act 2002 (POCA 2002) and the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (MLR 2017), previously the Money Laundering Regulations 2007 (MLR 2007).[8] POCA 2002 criminalises money laundering and imposes reporting obligations upon the legal profession in respect of suspicious transactions, whilst the MLR 2017 and 2007 set out an array of customer due diligence, training and record-keeping requirements. Each piece of legislation is complemented by sectoral guidance issued by, inter alia, the Law Society.[9] Professional conduct rules also prohibit legal professionals from engaging in money laundering, and impose the requirement to comply with all AML legislation pursuant to the Solicitors Regulation Authority (SRA) Code of Conduct.[10] Recent years have also seen an increased focus on the legal profession as

[6] FATF was set up in 1989 and is an inter-governmental body, comprising 36 members (and a panoply of observers and associates), who between them represent most significant financial centres. See `Who we are` (*FATF*) <http://www.fatf-gafi.org/about/> accessed 15 August 2017. For the FATF Recommendations 2012 see FATF, *International Standards on Combating Money Laundering and the Financing of Terrorism and Proliferation* (2012).
[7] Council Directive 2015/849 EC of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, amending regulation (EU) no 648/2012 of the European Parliament and of the Council, and repealing directive 2005/60/EC of the European parliament and of the Council and Commission Directive 2006/70/EC [2015] OJ L141/73. 4MLD is transposed into national law by way of the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017, SI 2017/692.
[8] MLR 2017, SI 2017/692; MLR 2007, SI 2007/2157.
[9] The Law Society, *Anti-money laundering Practice note* (2013) (AML Practice Note 2013).
[10] SRA, *SRA Code of Conduct 2011* (Version 18, 2016). Outcome 7.5 requires solicitors to comply with AML legislation applicable to their business. The SRA are the main UK regulatory body of the legal profession.

`professional enablers ` or `facilitators` of money laundering, with such focus culminating in legislation which targets those professionals such as lawyers who participate in money laundering as part of an organised crime group.[11]

In 2014, the SRA took the decision to elevate the money laundering risk in law firms from an `emerging` risk to a `current priority risk`, ie defined by the SRA as `widespread, current` and posing `a significant risk to the public interest`.[12] The SRA have experienced an increase in reports of money laundering in law firms, some of which are substantial cases involving, inter alia, the Russian mafia.[13] The Channel 4 documentary `From Russia With Cash`, which was aired in July 2015 and hinted at lawyers` complicity in money laundering, triggered a flurry of media scrutiny in this area, and resulted in Transparency International taking the `extraordinary step` of requesting copies of the Law Society`s AML supervisory reports.[14] These drivers all combine to form what Stephen Wilmott, Director of Intelligence at the SRA, has called a `perfect storm` for law firms in relation to money laundering.[15] The UK`s first National Risk Assessment (NRA 2015) was then published in October 2015 which rated legal service providers `high` risk with regard to money laundering, assigning the sector a higher risk rating than either estate agents, money service businesses or digital currencies.[16]

It can be seen from the preceding paragraphs that legal professionals in England and Wales are entwined in an ever shifting AML landscape. The impending FATF evaluation of UK AML compliance in 2018 has also ensured that scrutiny of the

[11] Serious Crime Act 2015, s 45. The legislation flows from the government initiative set out in the Serious and Organised Crime Strategy launched in 2013: Home Office, *Serious and Organised Crime Strategy* (2013).
[12] SRA, *SRA Risk Outlook 2014/15* (2014) 6,10, 21. A composite risk profile for the legal profession is set out in the SRA Risk Index, see SRA, *SRA Regulatory Risk Index* (2014).
[13] SRA, *Risk Outlook: Spring 2014 update* (2014) 4.
[14] Scott Devine, `NGO and media focus on AML is only just beginning`(*The Law Society*, 2 September 2015) < http://www.lawsociety.org.uk/policy-campaigns/articles/aml-policy-update-september-2015/> accessed 3 November 2015. Transparency International UK are the UK chapter of the global anti-corruption NGO Transparency International.
[15] Comments made at SRA Compliance Conference (26 November 2014).
[16] Home Office and HM Treasury, *UK national risk assessment of money laundering and terrorist financing* (2015) 12.

`regulated sector`, of which the legal profession forms a part, continues unabated.[17]

It is against this backdrop that the thesis is situated, complemented by the author`s direct practitioner experience as a senior corporate banking lawyer for several Top 50 UK law firms, which has shaped and informed the research.[18] The thesis endeavours to explore the experiences of professionals within Top 50 law firms when seeking to comply with the UK`s AML regime. The research question posed is deceptively straightforward: what are the compliance issues encountered by the legal profession in Top 50 UK headquartered law firms when implementing the UK AML regime? The answer to that question, which is the subject matter of this thesis, is both complex and multi-dimensional, culminating in a number of recommendations in relation to UK AML policy and regulation.

The research was conducted using 40 semi-structured in depth qualitative interviews with those able to offer multiple perspectives on the AML regime in Top 50 law firms. Participants were drawn from 20 Top 50 UK headquartered law firms, evenly split between those who were solicitors at partner level, and those who were money laundering reporting officers (MLRO), Deputy MLROs, or those undertaking a senior compliance role within their organisation. In this way, AML compliance issues could be identified by those at the `coalface` of legal practice, as well as those viewing AML from a pure compliance perspective. The sample used was not representative in nature; rather a purposive sampling approach was deployed whereby participants were selected according to their relevance to the research question. Those responses, which were rich and multi-layered, were then thematically analysed, which is a means of `identifying, analysing and reporting patterns (themes) within data`.[19]

[17] The `regulated sector` are defined in POCA 2002, pt 1, sch 9.
[18] Top 50 UK headquartered law firms are identified by reference to annual turnover figures produced by `The Lawyer`.
[19] Virginia Braun and Victoria Clarke, 'Using thematic analysis in psychology' (2006) 3(2) Qualitative Research in Psychology 77,79.

Whilst there is a large body of literature relating to money laundering in a general context, there is little by way of academic empirical inquiry in this area. Much existing research on money laundering and the legal profession is either quantitative in nature, and/or focuses on the facilitation of money laundering via the sector.[20] Much research on AML compliance relates to financial institutions as opposed to the legal sector. The significance and originality of this research therefore derives from a blend of three factors: it expands the field by approaching the issue using a qualitative methodology, from a compliance perspective within the legal sector, and draws upon responses from a section of the legal profession that can be extremely hard to access for research purposes. Whilst views on the regime may be represented by bodies such as the Law Society, or The City of London Law Society, this thesis explores the views of those participants directly, which is seldom the case in the academic literature.

The thesis is structured in the following manner. The remainder of this Chapter explores the background to money laundering and examines those money laundering typologies affecting the legal profession. The evidential basis for including the profession within the `regulated sector` will be briefly examined, together with the concerns raised by the profession with regard to the UK AML regime. Chapter 2 details the legislative framework provided by POCA 2002 and MLR 2007, within which the legal profession operates, amplified where relevant by sector-specific guidance. As the interviews were conducted prior to the transposition of 4MLD, the relevant regulations considered are MLR 2007, although the developments brought about by MLR 2017 are discussed, where relevant, in the data chapters. Chapter 2 then outlines the SRA AML supervisory and regulatory regime. Whilst a detailed analysis of the enforcement of the regime is outside the scope of this thesis, a brief synopsis is provided for the sake of completeness.

[20] See for example Stephen Schneider*, Money Laundering in Canada: An Analysis of RCMP cases* (Nathan Centre for the Study of Organized Crime and Corruption 2004).See also Lawton P. Cummings and Paul T. Stepnowsky,`My Brother`s Keeper: An Empirical Study of Attorney Facilitation of Money Laundering through Commercial Transactions` (2011) 1 J.Prof. Law 1.

The methodological approach adopted by this research is considered in Chapter 3, which expands upon the brief methodological outline already provided in this introduction. The Chapter explores the ontological and epistemological stance of the author, explains the rationale behind the choice of semi-structured qualitative interviews as a research method, and describes the purposive sampling technique deployed, together with the ethical considerations encountered. It describes the data collection and data management process and details the way in which the interview data was thematically analysed. The limitations of the research are then considered: both that the interviews were conducted by an `insider` researcher, with the potential for researcher subjectivity that that position may engender, and that the interviews explore AML compliance through a distinct lens – from within a very specific section of the legal profession alone. Notwithstanding these limitations, the interviews still form a rich, detailed and multi-faceted portrait of AML compliance issues within Top 50 UK headquartered law firms. The study is supported throughout by robust and meticulous research processes.

The research findings are presented and explored in four subsequent chapters. Consonant with a research approach which utilises thematic analysis, the chapters are ordered thematically and report on the overarching themes within the interview data. Chapter 4 considers the AML compliance issues encountered by the profession in relation to the UK`s AML legislative regime. Both the exclusion of minor offences and regulatory breaches from, and the inclusion of an intent element within, POCA 2002 are explored. The retention of criminal sanctions within MLR 2007 are then considered.

The focus of Chapter 5 is on the mechanical aspects of day to day practice. It explores, inter alia, the customer due diligence (CDD) issues encountered by participants relating to the following: (i) beneficial ownership, (ii) simplified due diligence, (iii) politically exposed persons, (iv) source of funds, (v) source of wealth, (vi) reliance, (vii) ongoing monitoring, (viii) AML training, and (ix) the client account. Chapter 6 explores participants` experiences of the suspicious activity reporting (SARs) regime, focusing on the meaning of the concept of `suspicion`, which

triggers reporting requirements under POCA 2002. It considers the relationship between the MLRO and those reporting to them, and identifies ways in which the MLRO can be better supported in practice: first by the creation of a bespoke reporting form for the profession and secondly by improved information sharing between the NCA, law enforcement and the sector. The difficulties encountered when managing the client relationship whilst seeking consent from the NCA to continue with a transaction are also discussed.

Chapter 7 shifts the focus of the findings away from the mechanical aspects of day to day practice to explore participants` perceptions of the regime. It discusses the role of the legal professional within that regime, suggesting a shift towards an acceptance of their role within the AML regime as being appropriate, reflecting an underlying maturation of the regime. The Chapter then considers participants` perceptions of the following: (i) the costs and benefits of AML compliance, (ii) SRA regulation and enforcement of the regime, (iii) the identification of money laundering risk, and (iv) UK law firms in a global context.

Chapter 8 draws together the conclusions drawn throughout the thesis and considers the unifying strand presented by the data: that jurisdictional issues pervade every area of practice for many participant firms. This finding highlights further the need for international co-operation in response to the international money laundering threat. The Chapter makes a number of recommendations for policy and regulation flowing from those conclusions, finally considering the limitations of the thesis and potential for future research.

The remainder of this Chapter contextualises the thesis by explaining the background to money laundering, the typologies affecting the profession. The Chapter concludes by identifying a number of overarching concerns raised by the legal profession with regard to the UK AML regime.

2. Background to Money Laundering

The aim of money laundering is to convert criminal proceeds into different assets, conceal its origins or ownership and create a patina of legitimacy.[21] At its most basic, the money laundering process has been categorized into three distinct components: (i) placement, where illicit proceeds are placed into a financial system; (ii) layering, where a series of transactions will obscure the origin of funds, and (iii) integration, where funds are re-integrated into the financial system free from any criminal taint. Schneider identifies one further element to this process, that of repatriation, where the laundered funds are returned to the criminal ready to be used in the legitimate economy.[22] The fact that this process involves far more than the simple conversion of `dirty` assets into `clean` assets has prompted some commentators such as van Duyne to suggest that the term `money laundering` should be replaced with the more expansive concept of `criminal money management`.[23] The money laundering process can be elaborate and sophisticated, and as Veng Mei Leong observes, the typology of every money laundering transaction will be informed by an array of factors including, inter alia, location, the quantity of assets being laundered, the level of intimidation exercised, the `educational, professional and business background of the criminal` and the cost of paying financial experts to participate in money laundering schemes.[24]

The Law Society AML Practice Note 2013 (AML Practice Note 2013) highlights the fact that the legal profession are vulnerable to the risk of money laundering at every stage of the laundering cycle.[25] At the placement stage the lawyer`s client account operates as an entry point into the legitimate economy. Thereafter, money may be layered utilising legal professionals to effect a series of complex

[21] Stephen Schneider, *Money Laundering in Canada: An Analysis of RCMP cases* (Nathan Centre for the Study of Organized Crime and Corruption 2004) 5.
[22] ibid.
[23] Petrus van Dyne `Crime-money and financial conduct` in Brigitte Unger and Daan van der Linde (eds), *Research Handbook on Money Laundering* (Edward Elgar 2013) 232.
[24] Angela Veng Mei Long, `Anti-money laundering measures in the United Kingdom: a review of recent legislation and FSA`s risk based approach` (2007) 28(2) Comp. Law 35, 35.
[25] See generally AML Practice Note 2013.

transactions, with the result that `detection can be difficult` at this stage.[26] The legal profession are still vulnerable at the integration stage as they may be utilised to effect movements of funds back into the legitimate economy via, inter alia, investment in companies, trusts and real property on behalf of the launderers. The Law Society caution its members that this `is the most difficult stage of money laundering to detect.`[27] A further challenge presents itself with regard to the legal profession in that many of the services that are commandeered to perform money laundering functions are used legitimately on a daily basis.[28] For law firms themselves, money laundering activity brings with it multiple potential negative consequences, including both criminal and civil liability, regulatory censure and disciplinary sanction, together with inevitable reputational damage.

As stated in the introduction to this Chapter, it can be consistently demonstrated that the services offered by the legal profession are being utilised to launder money.[29] Launderers will involve the legal profession either because their services are required by statute to effect specific transactions such as conveyancing, or because they wish to access specialist legal services that will assist them in laundering money.[30] Each transaction may also function as part of the layering process outlined above. The legal profession embodies many attractive features for a money launderer, namely respectability, a client account and the belief that legal professional privilege (LPP) will serve to dilute or block the intervention of law enforcement agencies.[31] Where legal professionals are required by law to effect a

[26] ibid para 1.3.2.
[27] ibid para 1.3.3.
[28] FATF, *Money Laundering and Terrorist Financing Vulnerabilities of Legal Professionals* (2013) 7.
[29] (n 1).
[30] In the UK, the Legal Services Act 2007, s12(1)(a)-(f) stipulates a number of `reserved legal activities` which may only be carried out by an `authorised person` such as a solicitor(defined in s 18). See FATF, *Money Laundering and Terrorist Financing Vulnerabilities of Legal Professionals* (2013) 23.
[31] ibid.

transaction, they are rendered `uniquely exposed to criminality, irrespective of the attitude of the legal professional to the criminality.`[32]

The role that lawyers perform means that in much official and academic literature, lawyers are identified as `gate-keepers` ie those who `protect the gates to the financial system`, a concept which will be discussed in more detail in Chapter 2 and in the data chapters of the thesis.[33] This terminology has arisen on the basis that lawyers are uniquely positioned to both effect and prevent money laundering. [34]

There has also been an evolving discourse in recent years, albeit often unsupported by robust empirical data, on the role of legal professionals as `professional enablers` and `facilitators` of money laundering. FATF, for example, identify lawyer involvement in money laundering as an increasing trend in a number of reports.[35] In the UK, the NCA state that money laundering `is reliant on access to the professional skills of . . . lawyers`, and identifies solicitors as one of the professions `posing the greatest risk` in terms of the `high end`, non-cash based laundering effected via the profession.[36] This focus on `professional enablers` has culminated in a new offence under the Serious Crime Act 2015, targeted at professionals such as lawyers, of participating in an organised crime group.[37]

Middleton and Levi observe that a number of `situational opportunities` for money laundering present themselves to legal professionals due to the fact that they hold client monies which they may elect to steal and launder, or the fact that lawyers

[32] ibid 83.
[33] FATF, *Global Money Laundering & Terrorist Financing Threat Assessment* (2010) 44, para 214. It was the `gatekeeper initiative` that culminated in the inclusion of lawyers within UK money laundering regulations. See Kevin Shepherd, `Guardians at the Gate: The Gatekeeper Initiative and the Risk-Based Approach for Transactional Lawyers` (2009) 43(4) Real Prop. Tr. & Est. L.J. 607.
[34] Lawton P. Cummings and Paul T. Stepnowsky,`My Brother`s Keeper: An Empirical Study of Attorney Facilitation of Money Laundering through Commercial Transactions` (2011) 1 J. Prof. Law 1,3.
[35] See for example FATF, *Report on Money Laundering Typologies 1996-1997* (1997) para 16; FATF, *Report on Money Laundering Typologies 2003-2004* (2004) para 86; FATF, *Money Laundering and Terrorist Financing Vulnerabilities of Legal Professionals* (2013).
[36] NCA, *National Strategic Assessment of Serious and Organised Crime 2015* (2015) 21; see also Home Office, *Serious and Organised Crime Strategy* (2013) 19.
[37] Serious Crime Act 2015, s 45.

may act for both the borrower and the lender when purchasing real property. [38] They also comment that more resources are required when investigating claims against lawyers from elite firms because it is `less likely . . . that the claims will be found credible`. [39] They describe this effect as `'professional capital', a sub-set of social capital that makes use of occupational prestige rankings.` [40] Whilst a number of theories and literature exists which explores the rationale behind lawyer involvement in money laundering, such theories lie outside the scope of this thesis, which seeks to explore the experiences of legal professionals when complying with the UK AML regime.

3. Money Laundering Typologies in the Legal Profession

Having established that lawyers may be part of the money laundering process, it is helpful to consider the typologies affecting the profession. Part of FATF`s remit is to produce reports highlighting evolving money laundering typologies in specific sectors, with a report on the legal profession being issued in June 2013 (LP Report).[41] The inclusion of the legal profession in the FATF Recommendations is a relatively recent measure, commencing in 2003.[42] Since then, by FATF`s own admission, there has been much debate as to the evidential basis for such inclusion, intermingled with debate as to whether applying the Recommendations is inconsistent with human rights or breaches the ethical obligations owed by lawyers to their clients.[43]

[38] David Middleton and Michael Levi,`The role of solicitors in facilitating `Organized Crime`: Situational crime opportunities and their regulation` (2004) 42 (2/3) Crime, Law & Social Change 123,125,126.
[39] ibid, 130.
[40] ibid, 130.
[41] FATF, *Money Laundering and Terrorist Financing Vulnerabilities of Legal Professionals* (2013). The SRA advises solicitors to access this source material directly; see SRA, *Cleaning up: Law firms and the risk of money laundering* (2014) 12.
[42] FATF, *FATF 40 Recommendations* (2003).
[43] LP Report 4. Each of these aspects will be explored in Chapter 2.

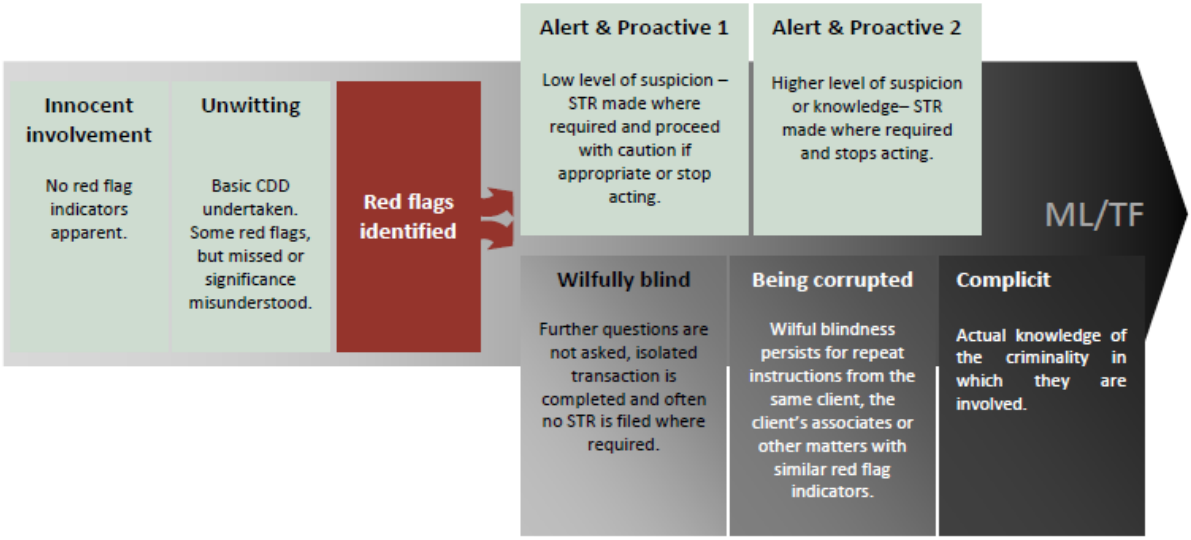
The LP Report does not purport to be guidance or to form any policy recommendations.[44] Indeed, FATF have previously acknowledged the inherent limitations with regard to typologies in the legal sector in that they are constantly evolving, and establishing what is customary or unusual behaviour for a particular client is hard to ascertain.[45] Middleton and Levi report that lawyers criticise the Report as comprising `lightly analysed lists of cases in multiple jurisdictions`, noting that other reports in the area present `closed` and therefore untested source material.[46] Furthermore, the case studies provided in response to FATF questionnaires for the LP Report may not present a full picture of laundering via the sector.

With such caveats in place, the LP Report seeks to ascertain money laundering vulnerabilities within the profession, and highlights so called `red flag indicators`, ie those factors which may be indicative of money laundering.[47] The `red flags` collated in the LP Report are to be considered in the context of each client relationship and are intended to assist the profession in the implementation of risk-based AML provision.[48] The LP Report describes the involvement of legal professionals in money laundering as a continuum, which is a more nuanced approach than the strict dichotomy of complicit or unwitting professionals seen

[44] ibid.
[45] FATF, *RBA Guidance for Legal Professionals* (2008) para 86.
[46] David Middleton and Michael Levi, 'Let Sleeping Lawyers Lie: Organized Crime, Lawyers and the Regulation of Legal Services' (2015) 55(4) Brit.J.Criminol 647,653. See also comments made in the IBA report on AML,IBA, *A Lawyers`s Guide to Detecting and Preventing Money Laundering* (2014) 6.
[47] LP Report 4.
[48] ibid 5.

previously in the literature.[49] This continuum is best illustrated in the diagram below.[50]

Involvement of Legal Professionals in money laundering and terrorist financing (ML/TF)



The LP Report identifies `red flag` indicators emerging in relation to particular clients, particular sources of funds, the kind of legal professional involved and the nature of the work undertaken, which may, depending on the context, trigger risk-based due diligence/external reporting. The LP Report comments that legal professionals who are unaware and uneducated in terms of money laundering risks are more vulnerable in terms of money laundering activity, and both information sharing and AML training are themes present in the interview data.[51] Schneider`s research also identifies a correlation between the complexity of transactions and

[49] See for example David Middleton,`Lawyers and client accounts: sand through a colander` (2008) 11(1) JMLC 34,34. Andrea di Nicola and Paola Zoffi, `Italian lawyers and criminal clients. Risks and countermeasures` (2004) 42(2/3) Crime, Law & Social Change 201, 213. Lankhorst and Nelen use the term `culpable involvement` and refer to `active or `reactive` involvement in money laundering. See Francien Lankhorst and Hans Nelen, `Professional services and organised crime in the Netherlands (2004) 42 (2/3) Crime, Law & Social Change 163,184.The NCA also refer to `negligent` involvement, see NCA, *National Strategic Assessment of Serious and Organised Crime 2014* (2014)12.

[50] LP Report 5.

[51] ibid 6.

the complicity of the legal professionals conducting them.[52] In the UK, the SRA state that the role of law firms is `primarily that of `professional enabler`, rather than direct perpetrator.`[53]

The LP Report also addresses misconceptions surrounding LPP, in that either it will act as a veil behind which the legal profession may continue to act for clients involved in criminal conduct, or that it will block access to evidence by law enforcers.[54] Despite this, there is an acknowledgment that the multitude of differing LPP regimes across jurisdictions has `at times provided a disincentive for law enforcement to take action against legal professionals`.[55] LPP is a feature of legal practice which will be discussed in Chapter 2.

Set out below are the typologies that have been identified in the LP Report, supplemented where relevant by guidance issued to UK legal professionals via the Law Society`s AML Practice Note 2013.[56] Whilst the SRA advocates a review of these typologies as an aid to risk assessment for each law firm, it also recognises the limitations of trend identification, commenting `as authorities become more aware of the latest schemes, criminals develop new approaches to try to evade detection.`[57]

(i) Misuse of Lawyers` Client Accounts

The majority of legal professionals are subject to comprehensive restrictions on the use of their client accounts, any breaches of which will lead to disciplinary action by their respective regulators.[58] Despite this, the misuse of a client account can be

[52] Stephen Schneider, *Money Laundering in Canada:An Analysis of RCMP cases* (Nathan Centre for the Study of Organized Crime and Corruption 2004) 67.
[53] SRA, *Cleaning up: Law firms and the risk of money laundering* (2014) 6.
[54] LP Report 6.
[55] ibid.
[56] AML Practice Note 2013.
[57] SRA, *Cleaning up: Law firms and the risk of money laundering* (2014) 7.
[58] In the UK such restrictions are set out in the SRA Accounts Rules 2011, see SRA, SRA Accounts Rules 2011 (Version 18, 2016).

pivotal for a money launderer as it is capable of performing a variety of key functions. As well as providing a springboard to other money laundering activities such as the purchase of real property, the client account may constitute the entry point through which illicit cash funds may be converted into other assets.[59] The client account may also provide an access route into the financial system for those clients who may find it challenging to become direct customers of financial institutions.[60] In addition, the use of the client account may also assist in masking the true ownership of funds.[61] The LP Report identifies three common techniques utilised by money launderers in relation to the client account:

(a) Transferring Funds without Providing Legal Services

Legal professionals in most jurisdictions (including the UK) are prohibited from acting as bankers to their clients, and an underlying transaction is required to be in place between a lawyer and client to justify the retention of client funds in the client account.[62] Nonetheless, this requirement has been circumvented in a number of case studies reviewed by FATF leading to the categorisation of specific `red flag indicators` in respect of such transactions. Professionals should be suspicious in circumstances where a client unjustifiably avoids face to face contact, urges unjustified haste or is willing to pay fees without any legal services being provided.[63] The receipt of disproportionately large deposits into the client account, or requests for transfers to seemingly unconnected third parties, or to jurisdictions with robust bank secrecy provisions in place should also evoke concern.[64] Perhaps most obviously, the fact that a client has known links to the criminal world should also elicit a cautious response from a legal professional.[65]

[59] LP Report 37.
[60] ibid.
[61] ibid.
[62] SRA, SRA Accounts Rules 2011 (Version 18, 2016) Rule 14.5. See also SRA, *Cleaning up : Law firms and the risk of money laundering* (2014) 8.
[63] LP Report 38.
[64] ibid 39-40.
[65] ibid 39.

(b) Structuring Payments

Launderers may also seek legal assistance in structuring payments either to avoid any `threshold` reporting requirements that apply in some (non-UK) jurisdictions, or to avoid any suspicion being aroused in relation to the transfer of funds.[66] Structuring may also involve channelling transactions through third parties such as family members (without any personal contact with the lawyer) or trust vehicles and into a variety of investments.[67] It follows that the lawyer is usually complicit in money laundering in these circumstances, and at the very least will breach professional conduct rules if they are unable to identify their client, act in their best interests and ensure that they are receiving instructions from those authorised to issue them.[68] In `structuring` type scenarios, the `red flag` indicators identified by FATF also arise where: (i) there is third party funding, (ii) there is private funding of sub-threshold level transactions, (iii) inordinate investment in a dormant company, or (iv) back to back sales involving a significant price increase.[69] Naturally, known links between a client and criminal activity should also raise concerns.[70]

(c) Aborted Transactions

This technique involves a client commencing a transaction and depositing funds in the lawyer`s client account. The sham transaction is subsequently aborted, and the lawyer will then be instructed to remit funds either directly to the client and/or to multiple third parties or even as directed by a third party.[71] Further `red flags` arise where the client uses an intermediary and avoids any face to face contact, requires

[66] ibid 40.
[67] ibid 41.
[68] ibid 40. In the UK, see Principle 4 of the SRA professional conduct principles, SRA, *SRA Principles 2011* (Version 18, 2016).
[69] LP Report 41-42.
[70] ibid 41.
[71] ibid 42.

rapid funds transfers, or when instructions are provided by someone other than the client or their representative.[72]

(ii) Property Purchases

(a) Investment of Proceeds of Crime

The proceeds of crime may be invested in real estate without any attempt to mask its legal ownership, or the buying and selling of property may be used as part of the layering process.[73] Where substantial cash or private funding is involved, underlying case studies in the LP Report state that the legal professional is frequently either complicit or wilfully blind.[74] A professional should be alert to transactions involving, inter alia, significant private funding disproportionate to the economic profile of the client , anomalies in the transaction such as depositing funds early, or multiple/ third party funding.[75] Another facet of this technique is that the legal professional will become embroiled in the predicate offence of mortgage fraud itself.[76] Alternatively, Schneider`s research identified scenarios in which assets are sold at an undervalue, with the balance of the `true` value of the asset being paid clandestinely in cash.[77]

(b) Back to Back/ABC Sales or Intra- Group Sales

This technique utilises successive sales at inflated prices within an organised crime group, assisting the layering process.[78] It can be characterised by a dissonance between the private funding available to an individual when measured against their

[72] ibid 42-43.
[73] ibid 44.In 55.7% of cases in Schneider`s research, criminal proceeds were used to buy real property. See Stephen Schneider*, Money Laundering in Canada: An Analysis of RCMP cases* (Nathan Centre for the Study of Organized Crime and Corruption 2004) 2.
[74] LP Report 44.
[75] ibid 44-46.
[76] ibid 52-53. See also The Law Society, *Mortgage Fraud* (2014) Ch 2.
[77] Stephen Schneider, 'Money Laundering in Canada: A Quantitative Analysis of Royal Canadian Mounted Police Cases' (2004) 11(3) Journal of Financial Crime 282,287.
[78] LP Report 46.

socio-economic profile.[79] Multiple transactions involving identical parties (free from any meaningful commercial relationship), frequent changes in legal professionals and forged documentation are also features of this particular technique.[80]

(c) Obscuring Ownership

This technique involves purchasing real estate using false names, in which the legal professional may be complicit or misled by forged documentation.[81] Alternatively the launderer may purchase properties in the names of business or personal contacts.[82] In either case there may be anomalies in the transaction such as, inter alia, a pre-payment, a delay in payment or efforts made by the criminal to mask the parties to the transaction.

A more sophisticated method of obscuring ownership is via a company or trust structure which may present a complex array of warning signs.[83] Transactions may involve unjustifiably complicated ownership structures in unfeasible jurisdictions, using under-aged shareholders or illogical funding streams.[84] Transactions may also involve funds transfers to high risk money laundering jurisdictions, or the use of intermediaries or legal professionals (with shifting instructions) without a logical basis for the retainer.[85] In one case study the identity of the shareholders and the size of the share capital in a company made the corresponding size of property purchases unlikely to constitute legitimate dealings.[86] In each variant of this technique, the private funds available to the purchaser may also be inconsistent with their socio- economic profile.[87] Schneider`s research also identified that

[79] ibid 46-47.
[80] ibid 46-47.
[81] ibid 47.
[82] ibid 48.
[83] ibid 49-51. See also Stephen Schneider, 'Money Laundering in Canada: A Quantitative Analysis of Royal Canadian Mounted Police Cases' (2004) 11(3) Journal of Financial Crime 282.
[84] LP Report 49-51.
[85] ibid.
[86] ibid 51, case study 18.
[87] LP Report 48-49.

obscuring ownership was a feature in 46.3% of the 149 proceeds of crime cases studied (in relation to real estate, but also in relation to companies, bank accounts and cars).[88] The SRA state that property transactions are particularly attractive to launderers because they can `legitimise a large amount of money in one go` and `preserve access to funds` in situations where bank accounts have been frozen.[89]

(iii) Setting Up Companies and Trusts

(a) Using Trusts to obscure Ownership

Any attempt to obscure beneficial ownership will constitute a `red flag`, and by its very nature, any trust vehicle will have this potential. Of particular concern are transactions where intermediaries, jurisdictions or complex ownership structures are used with no logical justification, or family members become involved in commercial transactions.[90]

(b) Shell and Shelf Companies/ Bearer Shares

Shell companies exist without conducting business or owning any meaningful assets.[91] Their sole purpose in the hands of a launder is to obscure ownership of the company.[92] As a legal professional must establish the purpose of the company in order to act in the best interests of their client, it may be that failure to establish any purpose may be evidence of complicity on the part of the professional.[93]

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[88] Stephen Schneider, 'Money Laundering in Canada: A Quantitative Analysis of Royal Canadian Mounted Police Cases' (2004) 11(3) Journal of Financial Crime 282, 286.
[89] SRA, *Cleaning up : Law firms and the risk of money laundering* (2014) 11.
[90] LP Report 55.
[91] Shell companies do have legitimate uses such as `reserving` a company name, or as a means of facilitating corporate mergers.
[92] See Jim Armitage,`Dirty Money: At least 19 UK firms under investigation for alleged conspiracy to make $20bn of dirty money seem legitimate` (*The Independent,* 16 October 2014)<http://www.independent.co.uk/news/business/news/dirty-money-at-least-19-uk-firms-under-investigation-for-an-alleged-conspiracy-to-make-20bn-seem-a6728431.html> accessed 16 August 2017, where a series of shell companies were utilised by launderers.
[93] LP Report 56.

Warning signs may include the use of multiple companies in high risk jurisdictions, involving secretive clients unwilling to engage in face to face contact.[94]

Shelf companies are frequently used in legitimate legal transactions where a corporate vehicle is needed at short notice. Incorporated by the law firm (with employees registered as shareholders and directors), and kept in readiness, ownership is then transferred as required. From the launderer`s perspective, this may serve to add a veneer of respectability to the shelf company it acquires, as it gives the impression that the company is well established.[95] Launderers may also run legitimate businesses using corporate structures, whereby the proceeds of crime are intermingled with legitimate revenue.[96] Alternatively, companies may be purchased by other launderers (known as `flipping`), incorporated in tax havens, or used to pay salaries to launderers.[97] In 32.9% of the proceeds of crime cases examined by Schneider, `criminally-controlled` companies were utilised.[98]

Title to bearer shares is passed by the physical transfer of share certificates, which are neither registered or tracked by the issuing company, and so ideal in terms of obscuring ownership. Whilst the UK has abolished bearer shares, they are still a feature of several other jurisdictions.[99]

(iv) Management of Companies and Trusts

Legal professionals may act as a trustee and so become liable for managing any proceeds of crime deposited into the trust.[100] In the UK this vulnerability may be countered to a certain extent by an obligation to conduct client due diligence and

[94] ibid.
[95] ibid 55.
[96] Stephen Schneider, *Money Laundering in Canada: An Analysis of RCMP cases* (Nathan Centre for the Study of Organized Crime and Corruption 2004) 46.
[97] ibid 47.
[98] ibid 44.
[99] Bearer shares were abolished on 26 May 2015 pursuant to the Small Business, Enterprise and Employment Act 2015, s84.
[100] LP Report 59.

ascertain the source of funds.[101] Alternatively, lawyers may lend a veneer of respectability to trust/company transactions set up for the sole purpose of laundering, or be asked to hold shares as a nominee in an attempt to obscure ownership.[102] Those shares in turn may be transferred at an inflated price.[103] Lawyers may offer their offices as a service address, act as company officers and even fabricate legal /accountancy documentation.[104]

(v) Managing Client Affairs

The LP Report identities case studies where lawyers either encourage financial institutions to open bank accounts on behalf of their clients (despite the laundering risk they present), or open accounts themselves, thus concealing the true beneficial owner.[105] The very lack of access to financial institutions should be a cause for concern for legal professionals. Such accounts may then be used in a series of complicated layering transactions. Several case studies have also illustrated the use of such accounts where individuals have family ties to politically exposed persons (PEPs), a concept that will be discussed in detail subsequently, and use the accounts to fund private expenditure through corporate vehicles.[106]

Alternatively the lawyer may manage the affairs of the client more generally under a power of attorney or court order, typically where a person lacks mental capacity to conduct their own affairs.[107]Yet in cases utilising this technique, the client typically has full mental capacity and the lawyer is either complicit or wilfully blind to money laundering risks.[108] Lawyers may also be used in a far less sophisticated

[101] MLR 2007, reg 5(b).
[102] LP Report 61.
[103] ibid 62.
[104] Stephen Schneider, *Money Laundering in Canada: An Analysis of RCMP cases* (Nathan Centre for the Study of Organized Crime and Corruption 2004) 69.
[105] LP Report 63.
[106] LP Report 63-64.
[107] ibid 66. See provisions under the Mental Capacity Act 2005 for example.
[108] ibid 67.

manner. Simply referring clients to third parties, on a legitimate basis or not, may mean that the third party does not conduct CDD with appropriate care.[109]

(vi) Litigation

The FATF Recommendations 2012 do not specifically include litigation within their scope, on the basis that its exclusion protects the fundamental human right of access to justice.[110] Despite this, the UK Court of Appeal case of *Bowman v Fels* held that `sham` litigation (where the subject matter of litigation is fabricated or relates to unenforceable contracts based on criminal activity) would be included in the Recommendations as it constitutes an abuse of court.[111] This technique is usually evidenced by the launderers using the legal professional to recover fictitious debts or contract debts arising from criminal activity.[112] Such litigation will frequently be settled swiftly, with a lack of regard for the level of fees the legal professional charges, and with minimal debt recovery work actually being undertaken.[113] Settlement may then be effected by instructions to remit funds to disparate third parties.

(vii) Other Methods

(a) Use of Specialised legal Skills

Specialised legal skills may be commandeered by launderers and used to obscure ownership and transfer assets. Such services may include the drafting of powers of attorney to effect the transfer of property, or a variety of other contractual arrangements.[114] In addition, legal professionals involved in probate or insolvency

[109] ibid 65.
[110] Universal Declaration of Human Rights 1948 UNGA Res 21 A(III). The current FATF Recommendations were issued in 2012. FATF, *International Standards on Combating Money Laundering and the Financing of Terrorism and Proliferation* (2012).
[111] *Bowman v Fels* [2005] EWCA Civ 226, [2005]4 All ER 609.
[112] LP Report 70.
[113] ibid.
[114] ibid 71.

retainers may simply unearth money laundering in respect of their deceased/insolvent client. [115] As with the previous techniques examined, a familiar array of `red flags` may be present : inexplicable third party funding or family involvement, transfers between high risk jurisdictions, or a level of private funding disproportionate to that individuals socio-economic profile.[116]

(b) Providing Legal Services for Charities

Legal professionals can be retained at every stage of a charity`s lifecycle, from its inception, to acting as a trustee, or simply advising on its day to day management. These entities may be used or even set up as vehicles for money laundering. [117] As with corporate structures, the charity may be a foil to carry out transactions incompatible with its stated aims.

(vii) Typologies Identified Outside of the FATF Typology Report

A limited number of studies into lawyer involvement in money laundering were conducted prior to the publication of the LP Report. Middleton and Levi, for example, identified misuse of the client account, real estate transactions and the creation of complex trust and company structures as key typologies affecting the sector.[118] In addition, Bell identifies LPP, the provision of guarantees, powers of

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[115] ibid.

[116] ibid 72-73. In addition to these services, it should be noted that some non UK jurisdictions, such as the United States, sanction the payment of defence fees to legal professionals being made out of criminal proceeds. The caveat to this is that the fees paid must be reasonable, and any surplus may not be remitted to the client or third parties. Unsurprisingly, this exemption may be abused by legal professionals. ibid 73-75.

[117] ibid 75-76.

[118] David Middleton and Michael Levi, `The role of solicitors in facilitating `Organized Crime`: Situational crime opportunities and their regulation` (2004) 42 (2/3) Crime, Law & Social Change 123,145. See also David Middleton, `Lawyers and client accounts: sand through a colander` (2008) 11(1) JMLC 34; David Middleton and Michael Levi, 'Let Sleeping Lawyers Lie: Organized Crime, Lawyers and the Regulation of Legal Services' (2015) 55(4) Brit. J.Criminol ; R. E. Bell, `The prosecution of lawyers for money laundering offences` (2002) 6 (1) JMLC 17; Stephen Schneider, *Money Laundering in Canada: An Analysis of RCMP cases* (Nathan Centre for the Study of Organized Crime and Corruption 2004); Lawton P. Cummings and Paul T. Stepnowsky,`My Brother`s Keeper: An Empirical Study of

attorney, and false legal documentation as areas of risk.[119] More recently, the SRA stated that law firms were being directly infiltrated by launderers, or were being selected for merger, acquisition or partnership in an attempt to create a regulated vehicle through which to launder funds.[120]

The UK`s NRA 2015, which rated the profession as high risk in terms of its money laundering vulnerability, echoes a number of risks already identified in the LP Report.[121] Hence it identifies vulnerabilities arising from the following: (i) professional enablers, (ii) mixed compliance with MLR 2007 and POCA 2002, (iii) real estate transactions, (iv) the misuse of client account, and (v) the challenges surrounding supervision of small firms.[122]

4. Evidence of Lawyer Involvement in Money Laundering

Whilst there is a general consensus that legal professionals can be involved in `organised crime` in a number of ways, the degree and manner in which lawyers are involved in money laundering is unclear.[123] The International Bar Association,

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Attorney Facilitation of Money Laundering through Commercial Transactions` (2011) 1 J.Prof.Law 1; SRA, *SRA Risk Outlook 2017/8* (2017) 34.

[119] R. E. Bell, `The prosecution of lawyers for money laundering offences (2002) 6 (1) JMLC 17. Using Bell`s cases as a framework, Middleton and Levi identify a number of practical ways in which lawyers may become involved in laundering ranging from receiving and distributing cash to passing money through their personal accounts. See David Middleton and Michael Levi, `The role of solicitors in facilitating `Organized Crime`: Situational crime opportunities and their regulation` (2004) 42 (2/3) Crime, Law & Social Change 123,136.

[120] SRA, *Risk Outlook: Spring 2014 update* (2014) 4; see also *SRA, Cleaning up : Law firms and the risk of money laundering* (2014) 9.

[121] Home Office and HM Treasury, *UK national risk assessment of money laundering and terrorist financing* (2015) 12.

[122] ibid 42, para 6.69.

[123] The term `organised crime` in this context bearing the interpretation provided by the Home Office in its *Serious and Organised Crime Strategy*, ie `serious crime planned, coordinated and conducted by people working together on a continuing basis. Their motivation is often, but not always, financial gain . . . organised criminals very often depend on the assistance of corrupt, complicit or negligent professionals, notably lawyers, accountants and bankers` Home Office, *Serious and Organised Crime Strategy* (2013) para 2.5,2.6. For lawyer involvement see para 5.20 which comments that `a small number of complicit or negligent professional enablers such as bankers, lawyers and accountants, can

for example, asserts that the FATF LP Report, `is in danger of creating a misleading impression of the legal profession.`[124] They state that:

> The profession generally believes that, contrary to what the FATF typologies report may suggest, circumstances in which lawyers are knowingly involved in criminal activities are quite rare.[125]

The lack of extensive empirical evidence in the area means that it is difficult to gauge accurately the extent to which legal professionals are embroiled in money laundering. In 2001, NCIS identified `over 200` cases which would have required advice or assistance from lawyers or accountants.[126] In 2002 (pre-POCA 2002), Bell analysed a number of cases from the UK, US and Canada, and noted that `the number of convictions of UK solicitors is small`, a position he attributed to `inadequate` AML legislation coupled with a lack of law enforcement focus on the area.[127] In the UK in 2004, Middleton and Levi examined both reported and unreported cases and identified a range of methods by which solicitors facilitate wrongdoing.[128] They concluded that `evidence demonstrating the level or likely level of laundering which takes place through lawyers is sparse.`[129] They found that the numbers of solicitors convicted for money laundering was `very low indeed`, although they note that such low conviction rates may be due to the fact that

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act as gatekeepers between organised criminals and the legitimate economy.` See also World Economic Forum, *Organized Crime Enablers* (2012)18.

[124] IBA, *A Lawyer`s Guide to Detecting and Preventing Money Laundering* (2014) 6.

[125] ibid.

[126] NCIS, *The Threat from Serious and Organised Crime* (2001) 50.

[127] R.E. Bell, `The prosecution of lawyers for money laundering offences` (2002) 6(1) JMLC 17, 18.

[128] David Middleton and Michael Levi, 'The role of solicitors in facilitating 'Organized Crime': Situational crime opportunities and their regulation' (2004) 42(2/3) Crime, Law & Social Change 123. Other arenas in which solicitors have facilitated crime are identified as mortgage fraud, theft of client monies, high yield investment fraud or bank instrument fraud, legal aid fraud, immigration practice fraud, fraudulent claims on the SCF, tax fraud, financial schemes operated by lawyers, and misconduct by criminal defence lawyers, ibid p130-146. New categories have since been added comprising misconduct triggered by firm financial instability, abusive litigation and direct facilitation of crime,. David Middleton and Michael Levi, 'Let Sleeping Lawyers Lie: Organized Crime, Lawyers and the Regulation of Legal Services' (2015) 55(4) Brit.J.Criminol 647.

[129] David Middleton and Michael Levi, 'The role of solicitors in facilitating 'Organized Crime': Situational crime opportunities and their regulation', (2004) 42(2/3) Crime, Law & Social Change 123, 134.

prosecutors do not always pursue a money laundering charge in addition to any underlying offence.[130] They also noted that bringing money laundering prosecutions against lawyers is also more challenging due to both LPP and client confidentiality.[131] Middleton and Levi reviewed this area in 2015.[132] They noted both that `Little has been written about lawyer wrongdoing in the United Kingdom`, and observed that obtaining evidence against lawyers is `very difficult`.[133] They went on to express concern that `evidence-free headline metaphors can still drive or be used to `justify` control policies.[134]

Middleton and Levi`s work in 2004 was part of a wider study across Europe examining organised crime by legal professionals. The Italian contributors Di Nicola and Zoffi, whilst highlighting the potential risk of laundering by lawyers acknowledged that, `In Italy, from police and prosecution records, lawyers do not appear to be involved in money laundering schemes to any great extent`.[135] The French contributor Chevrier presents legal professional involvement in money laundering as a `reality`, but also acknowledged that there are few cases, and that `inferences from cases are of questionable validity`. [136] The study by Lankhorst and Nelen in the Netherlands found `few cases of culpable involvement` by lawyers and notaries in crime, but emphasised that `the findings of the study should not be used to trivialise the problem. The dark number is probably high`.[137]

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[130] ibid; see also R. E. Bell, `The prosecution of lawyers for money laundering offences (2002) 6(1) JMLC 17, 19. In their later work on this area, Middleton and Levi also note that obtaining evidence against lawyers is `very difficult`.

[131] David Middleton and Michael Levi, 'The role of solicitors in facilitating 'Organized Crime': Situational crime opportunities and their regulation' (2004) 42(2/3) Crime, Law & Social Change 123, 136.

[132] David Middleton and Michael Levi. 'Let Sleeping Lawyers Lie:Organized Crime, Lawyers and the Regulation of Legal Services' (2015) 55(4) Brit.J.Criminol 647.

[133] ibid 649.

[134] ibid 653.

[135] Andrea Di Nicola and Paola Zoffi, `Italian lawyers and criminal clients. Risks and countermeasures` (2004) 42(2/3) Crime,Law & Social Change 201, 211.

[136] Emmanuelle Chevrier, `The French government`s will to fight organized crime and clean up the legal professions: The awkward compromise between professional secrecy and mandatory reporting` (2004) 42(2/3) Crime, Law & Social Change 189,192.

[137] Francien Lankhorst and Hans Nelen, `Professional services and organised crime in the Netherlands (2004) 42(2/3) Crime, Law & Social Change 163,184. For a discussion of

In Canada, Schneider conducted a quantitative empirical study of mounted police cases in 2005. He reported that lawyers came into contact with the proceeds of crime in 49.7% of the cases examined, mainly through their involvement with real estate transactions.[138] However Schneider also noted that:

> In the majority of police cases involving lawyers, they appear to have been unaware of the criminal source of funds provided by an offender.[139]

In the US, Cummings and Stepnowsky` s review of 40 Second Circuit money laundering cases found that `lawyers facilitated money laundering, both wittingly and unwittingly, in twenty-five percent of the cases examined`. [140] Reviewing this body of work on legal professional involvement in money laundering, it becomes clear that there is little clarity with regard to the prevalence of such involvement.

In the UK, it is difficult to present an accurate picture of lawyer involvement in money laundering because there is no systematic collation of such information on the part of law enforcement or the SRA. The SRA for example, collate information on those lawyers who have been struck off or convicted of a criminal offence, but this information will not reveal whether money laundering is involved. The SRA thematic review of AML in 2016 states that it received 237 reports of money laundering by legal professionals between 2012 and 2015, however prosecutions of legal professionals for money laundering offences remain relatively infrequent.[141]

The lack of prosecutions may be attributable to the resources required to secure such convictions.[142] The SRA in their SRA Risk Outlook 2014 acknowledge that

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`financial facilitators` more generally see Melvin Soudijn,`Removing excuses in money laundering` (2012) 15(2/3) Trends in Organised Crime 146.

[138] Stephen Schneider, *Money Laundering in Canada: An Analysis of RCMP cases* (Nathan Centre for the Study of Organized Crime and Corruption 2004) 65.

[139] ibid 67.

[140] Lawton P. Cummings and Paul T. Stepnowsky, `My Brother`s Keeper: An Empirical Study of Attorney Facilitation of Money Laundering through Commercial Transactions` (2011) 1 J.Prof.Law 1, 28.

[141] SRA, *Anti Money Laundering Report* (2016) 5. Such laundering was either as perpetrator or facilitator. 338 reports of breaches of MLR 2007/POCA 2002 were received for the same period.

[142] David Middleton and Michael Levi. 'Let Sleeping Lawyers Lie: Organized Crime, Lawyers and the Regulation of Legal Services' (2015) 55(4) Brit.J.Criminol 647,649.

establishing intentional money laundering is `rare` in the absence of a full multi-agency intelligence investigation.[143] It is this reality which has forged an SRA focus on `ensuring that firms have systems and controls in place to make money laundering difficult`.[144] It is this focus on AML compliance which is the subject matter of this thesis.

5. Conclusion

This Chapter has situated the thesis by describing the background to money laundering and the typologies affecting the legal profession. It has then considered the limited evidence on legal professional involvement in the money laundering process. Against this background, Chapter 2 will explore the legislative framework within which the legal profession operate, under the aegis of POCA 2002 and MLR 2007. It will then provide a brief overview of both AML regulation by the SRA, and the enforcement of the regime within the legal profession.

[143] SRA, *SRA Risk Outlook 2014/15* (2014) 25.
[144] ibid.

Chapter 2 - The UK AML Legislative Regime

1. Background

The AML provisions applicable in the UK flow from the overarching framework recommended by FATF and legislated for under a series of EU Directives culminating in 4MLD.[1] These overarching provisions form the cornerstone of UK AML measures and both inform and shape the UK legislative framework. The AML regime in the UK is underpinned by a trinity of statute, regulations and sector-specific guidance.

Key elements are set out in POCA 2002 and MLR 2017. As the interviews were all conducted prior to the transposition of 4MLD, the relevant money laundering regulations examined in this Chapter are MLR 2007. These provisions are supplemented by Treasury approved sector-specific guidance produced by the legal profession`s representative body, the Law Society, which a court must take into account when assessing a legal professional`s culpability.[2] This Chapter will examine each element of the AML trinity in turn and identify the obligations

[1] Council Directive 2015/849 EC of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, amending regulation (EU) no 648/2012 of the European Parliament and of the Council, and repealing directive 2005/60/EC of the European parliament and of the Council and Commission Directive 2006/70/EC [2015] OJ L141/73.FATF, *International Standards on Combating Money Laundering and the Financing of Terrorism and Proliferation -The FATF Recommendations* (2012, updated June 2017).

[2] The Law Society, *Anti-money laundering Practice Note* (2013) (AML Practice Note 2013). Whilst not compulsory, any deviation from such guidance may need to be justified to the SRA. See also POCA 2002,ss 330(8) and 331(7),MLR 2007,s 45(2). Where a law firm is dual regulated by the SRA and the Financial Conduct Authority (FCA), Law Society guidance may be supplemented by guidance from the Joint Money Laundering Steering Group (JMLSG). The JMLSG is made up of representatives from key trade associations drawn from the financial services sector. See JMLSG, *Prevention of money laundering/combating terrorist financing 2014 Revised Verson* (2014) (JMLSG Guidance Notes 2014). A later version of the guidance was produced in June 2017 following the transposition of 4MLD, see JMLSG, *Prevention of money laundering/combating terrorist financing 2017 Revised Verson* (2017). As the interviews took place prior to the transposition of 4MLD, references in this Chapter are to the 2014 version of the Guidance. This thesis will consider AML regulation of the legal profession on the part of the SRA as the profession`s central AML supervisor.

imposed upon the legal profession in England and Wales. Thereafter it will identify the issues that such obligations give rise to for the profession. In order to fully contextualise the thesis, the Chapter will conclude by providing a brief summary of AML regulation by the SRA, and an overview of the enforcement of the regime within the legal profession.

2. POCA 2002 Overview

POCA 2002 sets out a `complete legislative framework` and heralded a welcome response to what Stokes and Arora termed a `patchwork` of previous AML legislation.[3] Part 7 of POCA 2002 creates three broad categories of offences, comprising: (i) the substantive or nominate money laundering offences (ss 327-9) complemented by, (ii) the failure to disclose a knowledge or suspicion of money laundering (ss 330-2), and (iii) `tipping off` the money laundering suspect as to a disclosure or investigation (s 333).[4] Each of these offences are explored below insofar as they relate to legal professionals operating within the `regulated sector`.[5]

POCA 2002 criminalises money laundering in respect of all crimes as opposed to only serious crimes, and therefore goes further than envisaged by FATF, or provided for under 3MLD and 4MLD.[6] The logic behind the `all crimes` approach in POCA 2002 is to `"leave no stone unturned"` in the quest for useful intelligence.[7] Furthermore, it does not require any assessment to be made as to the seriousness

[3] Robert Stokes and Anu Arora, `The duty to report under the money laundering legislation within the United Kingdom` [2004] JBL 332,340,339. The term `money laundering` is defined in POCA 2002, s 340(11).
[4] In addition to the criminal penalties under these sections, a legal professional may attract civil liability as a constructive trustee.
[5] The`regulated sector` is defined in POCA 2002, sch 9, pt 1.
[6] FATF, *International Standards on Combating Money Laundering and The Financing of Terrorism & Proliferation-The FATF Recommendations* (2012, updated June 2017) recommendation 3; See the definition of `serious crimes` in 3MLD, art 3(5) and the list of serious crimes within the definition of `criminal activity` in 4MLD, art 3(4) 4MLD.
[7] Robert Stokes and Anu Arora, `The duty to report under the money laundering legislation within the United Kingdom` [2004] JBL 332,355.

or otherwise of any underlying criminal offence prior to making a disclosure to the NCA.[8]

3. Substantive Money Laundering Offences – ss 327-9 POCA 2002

The substantive money laundering offences criminalise dealings in criminal property. The concept of `criminal property` is broadly conceived under the Act, referring to property which `constitutes a person`s benefit from criminal conduct or it represents such a benefit`, where the launderer knows or suspects that this is the case.[9] The definition of `criminal conduct` embodies the `all crimes` approach of the Act, encompassing conduct which constitutes any offence in the UK, or would do if it occurred there.[10] Whilst lawyers may be complicit in laundering, the sheer breadth of POCA 2002 means that legal professionals are also at risk of inadvertent laundering when effecting transactions on behalf of their clients.

(i) ss 327-9 POCA 2002 Offences

S 327 POCA 2002 criminalises `own-proceeds` or `self-laundering` where the launderer is the `author of the predicate crime`.[11] It provides that a person commits an offence if he conceals, disguises, converts, transfers or removes criminal property from the UK.[12]

Of far more relevance to the legal profession is the `arrangement` offence set out in s 328 of the Act. This section is applicable to those, such as lawyers, `who in the course of their work facilitate money laundering by or on behalf of other

[8] This rationale is explained in Secretary of State for the Home Department*, Money Laundering and the Financing of Terrorism: the Government Reply to the nineteenth Report from the House of Lords European Union Committee Session 2008–09, (HL Paper 132, Cm 7718, 2009)11-12.* Hence a bank clerk, for example, would not be in a position to distinguish between differing categories of crimes.
[9] POCA 2002, s 340(3).
[10] POCA 2002, s 340(2).
[11] CPS, `Proceeds Of Crime Act 2002 Part 7 – Money Laundering Offences` (*CPS*, 2010)< http://www.cps.gov.uk/legal/p_to_r/proceeds_of_crime_money_laundering/#Section_327_offence> accessed 22 August 2017.
[12] POCA 2002, s 327(1).

persons.`[13] An offence is committed if a person `enters into or becomes concerned in an arrangement which he knows or suspects facilitates . . . the acquisition, retention, use or control of criminal property`.[14] Under this section, a lawyer may become embroiled in laundering when effecting transactions on behalf of their clients.

Whilst the term `arrangement` is not defined under the Act, the AML Practice Note 2013 states that the arrangement `must exist and have practical effects on the acquisition, use or control of property`.[15] The Court of Appeal decision in *Bowman v Fels* confirmed that any step taken in respect of litigation would fall outside the definition of `arrangement` [16] With regard to transactional work, and in the absence of judicial dicta, the AML Practice Note 2013 states that arrangements should be construed in a restricted manner.[17] Thus an arrangement must occur at a `particular time`, must be `actually made` and will exclude `preparatory or intermediate steps` which do not involve the acquisition etc of criminal property.[18]

The final substantive offence is found in s 329, which stipulates that a person commits an offence if he acquires, uses or has possession of criminal property.[19]

(ii) Defences under s 327-9 POCA 2002

A number of defences to the substantive money laundering offences are available, with those relevant to the legal profession considered below.[20] The defence most

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[13] CPS, `Proceeds Of Crime Act 2002 Part 7 – Money Laundering Offences` (*CPS,* 2010)< http://www.cps.gov.uk/legal/p_to_r/proceeds_of_crime_money_laundering/#Section_327_offence> accessed 22 August 2017.

[14] POCA 2002, s 328 (1).

[15] AML Practice Note 2013 para 5.4.3

[16] *Bowman v Fels* [2005] EWCA Civ 226, [2005] 4 All ER 609.`Sham` litigation, where litigation is fabricated to launder criminal property, will still fall within s328.

[17] AML Practice Note 2013 para 5.4.3.

[18] ibid.

[19] POCA 2002, s 329(1).

[20] Carrying out a law enforcement function is a defence under POCA 2002, s 327(2)(c),s 328(2)(c) and s 329(2)(d). Deposit-taking institutions may avail themselves of a *de minimis* defence under POCA 2002, s 327(2C),s 328(5) and s 329(2C). Under POCA 2002, s 334(1) the penalty under ss 327-9 on summary conviction is a maximum prison term of six months and /or a fine. In the Crown Court the maximum prison term is 14 years and/or a fine.

commonly utilised by the legal profession is that provided by the `consent regime`.[21] Where a legal professional deals in some way with `criminal property`, a report may be made by way of `authorised disclosure` under s 338 POCA 2002.[22] Within regulated sector law firms, the initial disclosure must be made to the `nominated officer`, synonymously referred to in practice as the money laundering reporting officer (MLRO).[23] The MLRO will then determine whether or not to make an external SAR to the NCA, which acts as the UK Financial Intelligence Unit (`UKFIU`) for such purposes.[24] Disclosures may be made before, during or after any prohibited dealings with criminal property under ss 327-9 of the Act.[25]Depending on the timing of the disclosure, NCA consent may be obtained to continue with the transaction, and such consent may be provided by way of actual consent from the NCA.[26] Alternatively consent may be provided by way of the `deemed` consent provisions applicable either on the expiry of the notice period of seven working days if no refusal has been received from the NCA, or, if a refusal has been received, on the expiry of the relevant moratorium period.[27]

[21] The majority (75.52%) of legal sector SARs are `consent ` SARs. NCA, *Suspicious Activity Reports (SARs) Annual Report 2015* (2016) 11.

[22] Such disclosures are a statutory exception (under POCA 2002, ss 337 and 338(4)) to the duty of confidentiality owed by a solicitor to their client under Outcome 4.1 of the SRA Code of Conduct 2011. See SRA, *SRA Code of Conduct 2011* (Version 18, 2016).

[23] POCA 2002,s 338(1)(a).

[24] The NCA is the successor body to SOCA and became operational on 7 October 2013 pursuant to the Crime and Courts Act 2013.

[25] For the timing of disclosures see POCA 2002, ss 338(2) and (3).

[26] For actual consent provisions see POCA 202, ss 336(1) and (2). The decision to grant or withhold consent is subject to judicial review. See *R (on the application of UMBS Online Ltd) v Serious Organised Crime Agency* [2007] EWCA Civ 375, [*20*08] 1 All ER 465.

[27] Deemed consent will apply pursuant to POCA 2002, s 336(3) where no refusal has been received from the NCA within the notice period of seven working days (starting from the first working day post-nominated officer disclosure) (s 336(7)). Deemed consent will also apply where a refusal has been received and the moratorium period expires (s 336(4)). The moratorium period is 31 days commencing on the date refusal is notified to the nominated officer (s 336(8). The Criminal Finances Act 2017, s 10 has inserted a mechanism whereby the courts may order an extended moratorium period of up to a maximum of 186 days, see POCA 2002, s 336A(7).

Such disclosure (and receipt of any `appropriate consent`) then acts as a complete defence to the offences set out in ss 327-9 of the Act.[28] Given that POCA 2002 adopts an all crimes approach, this means that SARs are required in respect of minor offences and regulatory breaches in order to avoid potential money laundering offences being committed. This is an aspect of practice which has caused particular concern amongst, and imposes a burden upon, participants in the research. The rationale for the consent regime is outlined by the Home Office as serving a twofold purpose, namely: (i) assisting the gathering of intelligence thus enabling timely intervention, and (ii) protecting disclosers from liability under the substantive money laundering offences.[29] The SRA state that such legal sector consent requests have played a `key role` in a range of criminal investigations.[30]

Concerned that the term `consent` was being viewed as a proxy for `permission` or confirmation that property was `clean`, in 2016 the NCA began to refer to such consent requests as requests for a `defence to a money laundering offence` (DAML Requests).[31] As the dominant industry term at the time of the interviews was the `consent regime`, the term is retained throughout this thesis. Any NCA consent relating to a disclosure is provided to the reporter via the MLRO, who is prohibited from providing such consent unless they themselves have made a disclosure to the NCA and received consent from the NCA, or the deemed consent provisions apply.[32]

[28] The defences are set out in POCA 2002, ss 327(2)(a), 328(2)(a) and 329(2)(a). The substantive money laundering offences carry a maximum term of 14 years imprisonment and/or an unlimited fine pursuant to POCA 2002, s 334(1)(b).
[29] Home Office, *Home Office Circular* 029/2008 (2008).
[30] SRA. 'Making consent requests less painful' (*SRA*,10 July 2014) <http://www.sra.org.uk/sra/news/compliance-news-08-ukfiu-consent-requests.page> accessed 4 November 2014. Consent requests from within the legal sector have assisted in investigations in relation to mortgage fraud, fraudulent trading, fraudulent investment schemes and the disposal of criminal property.
[31] NCA, *Requesting a defence from the NCA under POCA and TACT* (2016).
[32] An MLRO providing consent in breach of such conditions may be liable for a maximum prison term of five years in addition to a fine under POCA 2002, ss 336(5) and (6).

It is also a defence to the substantive money laundering offences if a person `intended` to make a disclosure but has a `reasonable excuse` for not doing so.[33] What constitutes a reasonable excuse remains untested in the courts, however the Law Society contend that this exception will apply where the legal professional`s knowledge or suspicion stem from `privileged information` and the `operation of legal profession privilege (LPP) is not excluded by the crime/fraud exception`.[34] The operation of LLP is explored later in this Chapter.

The `overseas conduct` defence may also be of relevance to those legal professionals dealing with clients on a multi-jurisdictional basis. No offence is committed where a person knows, or believes on reasonable grounds, that the relevant criminal conduct occurred outside the UK, was lawful in that jurisdiction at the time it occurred, and would not carry a prison sentence in the UK in excess of 12 months.[35]

There is one further defence to a s 329 offence: where a person has acquired, used or had possession of criminal property for adequate consideration.[36] In its broadest context, the rationale behind this defence is to protect traders who are paid for goods using criminal proceeds, or who receive payment of a legitimate debt from criminal funds.[37] What constitutes adequate consideration is determined by reference to what constitutes `inadequate` consideration, namely where the value of the consideration is significantly less than the value of the property, use or possession.[38] In addition, section 329(3)(c) provides that `the provision by a person of goods and services which he knows or suspects may help another to carry out criminal conduct is not consideration`.

In the context of the provision of legal services, CPS guidance confirms that payment of a legal professional`s reasonable costs and disbursements will be

[33] POCA 2002, ss 327(2)(b),328(2)(b) and 329(2)(b).
[34] AML Practice Note 2013 para 5.5.1.
[35] POCA 2002,ss 327(2A),328(3) and 329 (2A). The Proceeds of Crime Act 2002 (Money Laundering: Exceptions to Overseas Conduct Defence) Order 2006, SI 2006/1070, reg 2.
[36] POCA 2002, s S329(2)(c).
[37] AML Practice Note 2013 para 5.5.2.
[38] POCA 2002,s 329(3).

covered by this defence, provided that the value of the work undertaken is not significantly less than the fees received.[39]

4. Failure to Disclose in the Regulated Sector – s 330 POCA 2002

AML disclosure requirements are imposed upon businesses in the `regulated sector`.[40] The regulated sector encompasses a predictable list of institutions which deal with client/customer money including, inter alia, banks, credit institutions, casinos, estate agents, insurance companies, tax advisers, accountants, and lawyers offering specified services**.**[41]

(i) S 330 POCA 2002 Offence

The separate and distinct `failure to disclose` offence set out in s 330 POCA 2002 simply requires legal professionals in the regulated sector to report their knowledge or suspicions of money laundering activity to the MLRO.[42] The information forming the basis of the report must come to the legal professional in the course of business, and must be made to the MLRO `as soon as is practicable.`[43] In addition, reporters must be able to identify the launderer or the location of the laundered property (or they believe, or it is reasonable to expect them to believe, that the information will or may assist in this regard).[44]

An objective standard is also introduced in this section imposing a requirement to report where there are `reasonable grounds for knowing or suspecting` someone is

[39] CPS, `Proceeds Of Crime Act 2002 Part 7 – Money Laundering Offences` (*CPS*, 2010)< http://www.cps.gov.uk/legal/p_to_r/proceeds_of_crime_money_laundering/#Section_327_offence> accessed 22 August 2017.
[40] POCA 2002, sch 9, pt 1.
[41] ibid.
[42] POCA 2002, s 330(2(a).
[43] POCA 2002, ss 330(3) and (4).
[44] POCA 2002, s 330(3A).

money laundering. [45] The JLMSG state that this standard is likely to be met where particular facts and circumstances known to the person exist:

> . . . from which a reasonable person engaged in a business subject to the ML Regulations would have inferred knowledge or formed the suspicion that another person was engaged in money laundering.[46]

The objective negligence based test imposed by s 330 has been justified on the basis that ` a higher standard of diligence is expected in anti-money laundering prevention in the regulated sector`.[47] For Goldby, however, the objective test constitutes `a stick to threaten those who may be inclined not to take their legal obligation to report sufficiently seriously`.[48] Nevertheless it is a cause for concern amongst the regulated sector, and whilst in *Swan* it was stated that a legal professional`s culpability in failing to make a SAR will be reflected in sentencing, it was held in *Griffiths* that a custodial sentence is `inevitable`.[49]

The triple cocktail of an `all crimes` approach in POCA 2002, mixed with a suspicion based reporting threshold, and a negligence based limb to s 330/1 means that defensive reporting has become an enduring issue casting a shadow over the regime.[50]

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[45] POCA 2002, s 330(2)(b).
[46] JMLSG, *Prevention of money laundering/combating terrorist financing 2014 Revised Verson* (2014) para 6.15.
[47] CPS, `Proceeds Of Crime Act 2002 Part 7 – Money Laundering Offences` (*CPS*,2010) < http://www.cps.gov.uk/legal/p_to_r/proceeds_of_crime_money_laundering/#Section_327_offence> accessed 22 August 2017.
[48] Miriam Goldby `Anti-money laundering reporting requirements imposed by English law: measuring effectiveness and gauging the need for reform` [2013] JBL 367, 368; see also commentary in Robert Stokes and Anu Arora, 'The duty to report under the money laundering legislation within the United Kingdom' [2004] JBL 332, 346.
[49] *R v Swan* [2011] EWCA Crim 2275,[2012] 1 Cr. App Rep (S) 542,[22] where Moore-Bick LJ expressed the view that `Clearly sentences towards the top of that range are likely to be reserved for those involved in regulated businesses who know that money laundering is going on and that the amounts involved are or may be substantial`. *R v Griffiths* [2006] EWCA Crim 2155,[2007] 1 Cr. App Rep (S) 95,[12].
[50] Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* (2016) Annex B.

(ii) Defences to s 330 POCA 2002

No offence will be committed where a person has a reasonable excuse for not making the required disclosure.[51] As yet, this exception remains unchartered in terms of judicial guidance. However, based on the judicial reasoning illustrated in *Bowman v Fels* it is the Law Society`s view that failure to disclose in circumstances where LPP applies will constitute a reasonable excuse.[52]

Of particular relevance to the legal sector is s 330(6)(b), which provides that no offence is committed where `privileged circumstances` arise. The concept of `privileged circumstances` is a construct unique to POCA 2002 and is separate and distinct from LPP. Privileged circumstances have a wider scope than LPP in terms of giving or seeking legal advice, in that they extend beyond solicitor-client communications to include representatives of clients.

Privileged circumstances arise where information is communicated to a legal professional in three situations: `a) by (or by a representative of) a client of his in connection with the giving by the adviser of legal advice to the client, (b) by (or by a representative of) a person seeking legal advice from the adviser, or (c) by a person in connection with legal proceedings or contemplated legal proceedings`.[53] These exceptions will not apply however `to information or any other matter which is communicated or given with the intention of furthering a criminal purpose`.[54] CPS guidance states that a legal professional forming the mistaken but genuine belief that privileged circumstances exist will be able to rely on the reasonable excuse defence set out in s 330(6)(a).[55]

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[51] POCA 2002, s 330(6)(a).
[52] AML Practice Note 2013 para 5.7.1.
[53] POCA 2002, s 330(10).
[54] POCA 2002, s 330(11).
[55] CPS, `Proceeds Of Crime Act 2002 Part 7 – Money Laundering Offences` (*CPS*,2010) < http://www.cps.gov.uk/legal/p_to_r/proceeds_of_crime_money_laundering/#Section_327_offence> accessed 22 August 2017.

No offence will be committed under s 330 where a person has no knowledge or suspicion of money laundering and has not been provided with AML training by his employer.[56] Should an employee successfully mount this defence, a law firm will then be vulnerable to prosecution or regulatory censure for inadequate training.[57] As with the money laundering offences under s 327-9, a tailored overseas conduct defence also applies under s 330.[58]

5. S 331 POCA 2002 - Failure to disclose: nominated officers in the regulated sector

An MLRO may commit an offence under s 331 POCA 2002 (which mirrors the preconditions in s 330) if they do not make a required disclosure in relation to the information received under a s 330 disclosure to the NCA as soon as practicable.[59]Under Regulation 20(2)(d)(iii) MLR 2007, the MLRO must consider the disclosure in the context of any `relevant information` available to the regulated entity before making a determination as to whether the disclosure provisions are triggered. As with the s 330 offence, no offence will be committed where the MLRO has a reasonable excuse for not making a required disclosure or makes use of the overseas conduct defence.[60]

6. The Role of Suspicion in the UK AML Regime

The substantive money laundering offences under s 327-9 require that a person knows or `suspects` that property is criminal property. In addition, the duty to report under s 330-1 is triggered in part by knowledge or suspicion of money laundering activity. Unsurprisingly then, prior to any clear guidance by the courts, the `pivotal concept`[61] of suspicion was one that resulted in an unresolved tension as to whether the ordinary dictionary definition be used, as was the historical

[56] POCA 2002, s 330(7).
[57] MLR 2007, reg 21.
[58] POCA 2002,s 330(7A).
[59] POCA 2002,s 331(1)-(5). POCA 2002, s 332 creates a failure to disclose offence in respect of disclosures made to a nominated officer outside the regulated sector.
[60] POCA 2002,ss 331(6) and (6A).
[61] Johnathan Fisher and Jane Bewsey. 'Laundering the Proceeds of Fiscal Crime' (2000) 15(1) JIBL 11, 16.

position advocated by Mitchell, Taylor and Talbot, or whether a supplementary definition was required.[62] Brown for example commented, `it cannot be the case that Parliament intended persons to be at risk of prosecution merely because they speculated that something was the case`.[63]

The position has been clarified in a line of authority emerging from the dicta of Longmore LJ in the Court of Appeal case *R v Da Silva.*[64] The defendant had appealed against her conviction under previous AML legislation on the basis that any suspicion held by her had to be on reasonable grounds, and that the trial judge had misdirected the jury as to the definition of `suspicion`. The judge had directed the jury to the dictionary definition of the word but in addition introduced the concept of suspicion as a `fleeting thought`. [65] The Court of Appeal considered dicta from the Privy Council in *Hussein v Chang Fook Kam,* where suspicion was deemed to be a `state of conjecture or surmise`.[66] Longmore LJ concluded that:

> . . . the defendant must think that there is a possibility, which is more than fanciful, that the relevant facts exist. A vague feeling of unease would not suffice.[67]

In addition, Longmore LJ stipulated that there is no requirement for suspicion to be `clear`, `firmly grounded and targeted on specific facts` or based upon `reasonable grounds`.[68] Where appropriate, the jury should also be directed that the suspicion should be of a `settled nature`.[69] This direction would only be applicable in circumstances where a person had entertained a suspicion and then honestly

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[62] Andrew R. Mitchell, Susan M. E. Taylor and Kennedy V. Talbot, *Mitchell, Taylor and Talbot, Confiscation and the Proceeds of Crime* (2nd edn, Sweet & Maxwell 1997).
[63] Alastair Brown. 'Money laundering: a European and U.K. perspective' (1997) 12(8) JIBL 307,309.
[64] *R v Da Silva* [2006] EWCA Crim 1654, [2006] 4 All ER 900.
[65] ibid para 6.
[66] *Hussein v Chang Fook Kam* [1970]AC 942, 3 All ER 1626: see also *Holtham & Another v The Commissioner of Police for the Metropolis* Times, 28 November 1987.
[67] *R v Da Silva* [2006] EWCA Crim 1654, [2006] 4 All ER 900 [16].
[68] ibid.
[69] Ibid [17].

dismissed it (and even then there would need to be some reason to suppose a person had gone through this process).[70]

In *K Ltd* it was confirmed that the *Da Silva* interpretation of suspicion was equally applicable to civil matters, with Longmore LJ noting that suspicion is a `subjective fact` and that there `is no legal requirement that there should be reasonable grounds for the suspicion`.[71]The Court of Appeal in *Da Silva* (which deferred giving its judgment until the arguments in *K Ltd* had been heard) vigorously rejected implying any `reasonable grounds` concept to `suspicion` when invited to do so by the defendant`s counsel, commenting `to do so would be to make a material change in the statutory provision for which there is no warrant`.[72]

A suspicion based AML reporting regime is set at a low threshold. Yet the lack of any requirement to have `reasonable grounds` for suspicion, whilst fuelling debate amongst academics and counsel, may make little difference in practice. The reality is that any prosecution or conviction is unlikely without there being reasonable grounds for suspicion. Furthermore, a legal professional, as Chapter 7 demonstrates, is unlikely to debate the semantic parameters of the term suspicion, but rather transfer their money laundering concerns directly to the MLRO via an internal SAR under s338/s330 POCA 2002.

The Court of Appeal case of *Shah*, whilst confirming the *Da Silva* guidance on the term `suspicion`, raised a very practical issue: that of banks, and by extension legal professionals, being required to provide evidence of that suspicion.[73] Longmore LJ in *K Ltd* had seen no mechanism by which a bank officer would be required to give evidence of their suspicion, noting that this position protected reporters.[74] His view was that such cross examination verged on being pointless as, `Once the employee

[70] ibid.
[71] *K Ltd v National Westminster Bank plc* [2006] EWCA Civ 1039,[2007]1 WLR 311 [21].
[72] *R v Da Silva* [2006] EWCA Crim 1654, [2006] 4 All ER 900 [8].
[73] *Shah v HSBC Private Bank (UK) Ltd* [2012] EWHC 1283(QB),[2012 All ER (D) 155.
[74] *K Ltd v National Westminster Bank plc* [2006] EWCA Civ 1039, [2007] 1 WLR 311 [19-20]

confirmed that he had a suspicion, any judge would be highly likely to find that he did indeed have that suspicion`.[75]

In the first Court of Appeal hearing in *Shah* however, Longmore LJ distinguished between summary proceedings, particularly within the moratorium period, and non-summary proceedings, so that a reporter will now be required to prove on the balance of probabilities the existence of such suspicion at non-summary trial, via the ordinary route of disclosure and cross-examination.[76] This on the basis that the time delay in going to trial will effectively extinguish the possibility of any tipping off offence, and that any witness protection issues may be dealt with before a judge in chambers.[77] Supperstone J determined that a MLRO will now be attributed with the relevant state of mind for the purpose of establishing suspicion.[78]

7. Legal Profession Privilege (LPP)

Lawyers owe a duty of confidentiality to their clients in respect of confidential information.[79] Information to which this duty applies may only be disclosed as permitted or required by law, or with client consent.[80]

As has been explored earlier in this Chapter, POCA 2002 imposes a number of disclosure obligations upon the legal profession.[81] Yet the operation of LPP may act as an absolute bar on any such disclosure of certain information emanating from the lawyer-client relationship. LPP has its genesis in fundamental concepts relating to access to justice and the right to obtain confidential legal representation as laid out in Articles 6 and 8 of the European Convention on Human Rights.[82] In

[75] ibid [20].
[76] *Shah v HSBC Private Bank (UK) Ltd* [2010] EWCA Civ 31, [2010] 3 All ER 477.
[77] ibid [28], [30].
[78] *Shah v HSBC Private Bank (UK) Ltd* [2012] EWHC 1283(QB),[2012 All ER (D) 155 [49] .
[79] The duty of confidentiality is set out in SRA, *Code of Conduct 2011* (Version 18, 2016) Ch 4.
[80] ibid Outcome 4.1. POCA 2002, s 337 provides that a SAR `is not to be taken to breach any restriction on the disclosure of information (however imposed).
[81] POCA 2002, ss 327-9 and s 330-2.
[82] Convention for the Protection of Human Rights and Fundamental Freedoms; see also the Universal Declaration on Human Rights adopted 10 December 1948 UNGA Res 217 A(III).

recognition of these fundamental rights, the FATF Recommendations 2012 specifically provide that no SAR is required in respect of information subject to LPP.[83] Yet it is this very right that makes `surveillance and seizure of documents more difficult than they are for other enforcement targets.`[84]

The extent of material covered by LPP varies across jurisdictions.[85] Consequently, FATF recommend that national bodies such as the Law Society should clarify the parameters of LPP in each jurisdiction.[86] The aims of such clarification are fourfold: (i) to reduce the mutual distrust between lawyers and investigators during investigations, (ii) to deconstruct the myth that LPP is there to shield criminals, (iii) to streamline AML investigations surrounding the legal profession, and (iv) to allay the ethical concerns of legal professionals when making disclosures.[87]

For the legal profession in England and Wales, LPP attaches to two distinct categories of legal services, that is advice privilege and litigation privilege.[88]Advice privilege applies to communications between a solicitor acting in their professional capacity and a client if two elements are satisfied. Communications must be: (i) confidential, and (ii) directly for the purpose of seeking or providing legal advice between a solicitor (using their legal skills) and their client.[89] LPP also covers solicitor-client communications relating to a transaction:

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[83] FATF, *International Standards on Combating Money Laundering and the Financing of Terrorism and Proliferation -The FATF Recommendations* (2012, updated June 2017), Interpretive note to Recommendation 23, para 1. See also FATF, *RBA Guidance for Legal Professionals* (2008) paras 14,16.

[84] David Middleton and Michael Levi, 'Let Sleeping Lawyers Lie: Organized Crime, Lawyers and the Regulation of Legal Services' (2015) 55(4) Brit.J.Criminol 647, 648.

[85] FATF, *International Standards on Combating Money Laundering and the Financing of Terrorism and Proliferation -The FATF Recommendations* (2012, updated June 2017).The matters falling within LPP are particular to each country, however Interpretive Note to recommendation 23, para 2 specifies that LPP should normally cover client information obtained `in the course of ascertaining the legal position of their client, or (b) in performing their task of defending or representing that client in, or concerning judicial, administrative, arbitration or mediation proceedings`.

[86] FATF, *Money Laundering and Terrorist Financing Vulnerabilities of Legal Professionals* (2013) 85.

[87] ibid 85, 86.

[88] AML Practice Note 2013 para 6.4.1.

[89] ibid para 6.4.2.

> . . . notwithstanding that they do not contain advice on matters of law and construction, provided that they are directly related to the performance by the solicitor of his professional duty as legal adviser of his client.[90]

Litigation privilege attaches to confidential information at every stage of litigation from its commencement or contemplation. It protects communications passing between a lawyer and their client, an agent or third party, provided that their `sole or dominant` purpose is the seeking or provision of advice, obtaining evidence, or acquiring information leading to obtaining evidence.[91]

LPP will encompass advice given to a client either to avoid or alert them to the potential commission of a crime.[92] It will not extend to `documents which themselves form part of a criminal or fraudulent act`, or to `communications which take place in order to obtain advice with the intention of carrying out an offence. [93] That exclusion will apply not only to the client themselves, but also to any third party seeking to use the advice for a criminal purpose.[94]

8. Tipping Off in the Regulated Sector - s 333A POCA 2002

(i) The Tipping off Offence under s 333A POCA 2002

A legal professional may also commit a `tipping off` offence. A person commits this offence if they reveal the fact that a disclosure has been made (using information obtained in the course of a business in the regulated sector), and such action is `likely to prejudice any investigation that might be conducted following the disclosure`.[95] An offence is also committed if a person reveals (again, using information on which the revelation is based obtained in the course of a business in

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[90] Ibid.
[91] Ibid para 6.4.3.
[92] See *Bullivant v Attorney General for Victoria* [1901] AC 196, [1900-3] All ER Rep 812; *Butler v Board of Trade* [1971] Ch 680, 3 All ER 593.
[93] *R v Cox and Railton* (1884) 14 QBD 153, [1881-5] All ER Rep 68.
[94] *R v Central Criminal Court, ex parte Francis & Francis* [1989] AC 346.
[95] POCA 2002,ss 333(A)(1),(2). On summary conviction the maximum prison term is 3 months and/or a fine. In the Crown Court, the maximum penalty for tipping off is two year`s imprisonment and/or a fine, POCA 2002, s 333A(4). With regard to the unregulated sector see the Offence of Prejudicing an Investigation, PCA 2002, s 342.

the regulated sector) that an investigation into allegations that a money laundering offence has been committed is being `contemplated or is being carried out` if that revelation is `likely to prejudice that investigation`.[96] No offence is committed however if the person does not know or suspect that such disclosure is likely to prejudice any AML investigation. [97] The `tipping off` provisions do not mean that a lawyer must cease all communication with their client once a SAR is made however. The AML Practice Note 2013 offers some guidance in this respect, stating that preliminary enquiries made of a client at the outset or during the retainer to allay any suspicions or concerns will not constitute tipping off. [98]

(ii) Defences to Tipping Off under s 333A POCA 2002

A number of permitted disclosures are provided for under the Act. Hence under s 333B, a legal professional may make a disclosure to an employee, officer or partner within the same undertaking.[99] Similarly, professional legal advisers and other relevant advisers may make disclosures to their counterparts in undertakings sharing common ownership, management or control (provided equivalent AML provisions are in place).[100]

Section 333C permits disclosure between credit institutions, financial institutions, professional legal advisers or relevant professional advisers of the same kind where the disclosure relates to a mutual client or former client in respect of a transaction or service involving them both. [101] The disclosure must be solely for the purpose of preventing a money laundering offence.[102]

A number of further disclosures are permitted under s 333D. Under this section, a legal professional will be able to make a disclosure to the SRA, or in respect of any

[96] POCA 2002, s 333(A)(3).
[97] POCA 2002, ss 333D(3),(4).
[98] AML Practice Note 2013 para 5.8.3. SARs are exempt from subject access requests under the terms of the Data Protection Act 1998, s 29(1)(a).
[99] POCA 2002,s 333(B)(1).
[100] POCA 2002,s 333B(4).
[101] POCA 2002,s 333C(2a).
[102] POCA 2002,s 333(2)(b),(c),(d).

investigation or enforcement proceedings under POCA 2002.[103]A lawyer may also make a disclosure to their own client for the purpose of dissuading them from `engaging in conduct amounting to an offence`.[104] Since the enactment of the Criminal Finances Act 2017, a lawyer may also make certain disclosures within the regulated sector (in accordance with the provisions of s 339ZB POCA 2002), and disclose to their client that an application has been made to extend the moratorium period.[105]

9. Civil Liability for Breach of Contract

The cases below, whilst dealing with breach of mandate under the banker-customer relationship, are of relevance to law firms in relation to breach of the terms of the client retainer. Such a situation may arise where a law firm is unable to comply with their client`s instructions on the basis that they have a competing duty to comply with their reporting obligations under POCA 2002.

K Ltd highlighted the risk to banks of liability for breach of customer mandate due to freezing an account during the authorised disclosure/consent process.[106] This risk was swiftly dispatched by the Court of Appeal refusing to `require the performance of an act which would render the performer of the act criminally liable`.[107] The Court of Appeal were of the view that the temporary hiatus imposed by the disclosure and consent process constituted a suspension of the banker-customer contract during which `no legal right exists`.[108] Longmore LJ commented that `Parliament has struck a precise and workable balance of conflicting interests`.[109]

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[103] POCA 2002, s 333D(1)(a).
[104] POCA 2002, s 333D(2).
[105] POCA 2002, s 333D(1)(aa),1A; s 339ZB POCA 2002 provides for information sharing between the regulated sector and the NCA.
[106] *K Ltd v National Westminster Bank plc* [2006] EWCA Civ 1039, [2007]1 WLR 311.
[107] ibid [12].
[108] ibid [11]. The Appellant`s contention that this suspension would constitute a breach of art 6 and art 1 of the First Protocol of the European Convention on Human Rights were also dismissed, [24]-[25].
[109] *K Ltd v National Westminster Bank plc* [2006] EWCA Civ 1039,[2007]1 WLR 311 [22].

Shah v HSBC Private Bank (UK) Ltd resolved this particular issue partially by implying a term into the banking contract that a bank will be entitled to refuse to execute payment instructions in the absence of s335 consent.[110] Supperstone J justified this intervention in private contracts on the basis it is a `price Parliament has deemed worth paying in the fight against money laundering`.[111] He also held that there is an implied term in the banking contract that the bank must not disclose any information to its customer which may contravene its duties under s 333A POCA 2002.[112]

Following cases such as *K Ltd* and *Shah*, protection from civil liability for those making authorised disclosures was placed on a statutory footing pursuant to s37 Serious Crime Act 2015, which inserted a new s338(4A) into POCA 2002. This section provides protection against civil liability only in respect of those disclosures made `in good faith`.

10. S 45 Serious Crime Act 2015 (SCA 2015) – Participation in Organised Crime

The increased focus on `professional enablers` such as lawyers and accountants that was highlighted in Chapter 1 culminated in a new offence under s 45 SCA 2015. This offence expands on POCA 2002 by making it an offence to participate in what a person knows or reasonably suspects are `the criminal activities of an organised crime group`, or will help that group to carry on such activities.[113] Criminal activities are defined as those activities which are committed in the UK (or outside the UK provided the activity is a crime in that jurisdiction) and a carry a minimum prison sentence of 7 years.[114] There is a single defence available under s 45(8) of the Act, which applies when participation is necessary for the `prevention or detection` of crime.

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[110] *Shah v HSBC Private Bank (UK) Ltd* [2012] EWHC 1283(QB),[2012 All ER (D) 155 (May) [236].
[111] Ibid [38].
[112] Ibid [238].
[113] SCA 2015, s 45(1)(2). This offence carries a maximum prison term of 5 years, SCA 2015, s 45(9).
[114] SCA 2015, ss 45(3),(4) and (5).

Having explored the statutory provisions which form the UK`s AML framework, and some of the issues that flow from such provisions, this Chapter will now examine the obligations imposed on law firms under MLR 2007.

11. Money Laundering Regulations 2007 (MLR 2007)

(i) A Risk-Based Approach to AML

A risk-based approach to AML was introduced by the Third EU Money Laundering Directive (3MLD) and transposed into national law by the Money Laundering Regulations 2007 (MLR 2007).[115] This approach is intended to allow for flexibility, proportionality and cost effectiveness in that it enables businesses covered by the Regulations to differentiate between clients according to the relative money laundering risk each poses.[116] Resources may therefore be focused more appropriately on those clients who present a high risk.

The MLR 2007 require `relevant persons` to implement an array of AML measures relating to, inter alia, customer due diligence (CDD), record keeping and training.[117] An `Independent legal professional` falls within the definition of `relevant persons`, and is defined as `a firm or sole practitioner who by way of business provides legal or notarial services to other persons`.[118] The definition is restricted to those legal professionals participating in specified financial or real property transactions `where there is a high risk of money laundering occurring`.[119] A legal professional may also fall within the `relevant persons` definition should they provide services

[115] Council Directive 2005/60/EC of 26 October 2005 on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing [2005] OJ L309/15. MLR 2007 SI 2007/2157.
[116] AML Practice Note 2013 para 2.1.
[117] See MLR 2007, reg 3(1) for the definition of `relevant person`.
[118] MLR 2007, reg 3(9).
[119] AML Practice Note 2013 para 1.4.5. Such transactions are specified in MLR 2007,reg 3(9) and comprise : `(a) the buying and selling of real property or business entities; (b) the managing of client money, securities or other assets; (c) the opening or management of bank, savings or securities accounts; (d) the organisation of contributions necessary for the creation, operation or management of companies; or (e) the creation, operation or management of trusts, companies or similar structures.`

as an insolvency practitioner, tax adviser or a trust or company service provider.[120] Breach of the Regulations may result in civil penalties or criminal sanctions being imposed, save where a person `took all reasonable steps and exercised all due diligence` to avoid the breach.[121]

(ii) MLR 2007 – CDD

MLR 2007 impose extensive obligations upon law firms to conduct CDD. The rationale behind CDD is that having in depth knowledge of a client, and the transactions they undertake, assists in the identification of suspicious transactions.[122] Law firms must conduct CDD in the following situations provided for under Regulation 7: (a) when a business relationship is established, (b) when an occasional transaction is carried out, (c) where there is a suspicion of money laundering or terrorist financing, or (d) there are doubts as to the `veracity or adequacy of documents, data or information` already obtained. [123]The extent of CDD will be determined `on a risk-sensitive basis depending on the type of customer, business relationship, product or transaction`, and must satisfy the SRA that it is appropriate.[124] The AML Practice Note 2013 recommends that each law firm should carry out a risk assessment of its own firm`s risks taking into account its size, client demographic and practice area. [125] Thereafter, risk should be addressed

[120] MLR 2007, regs 3(6),3(8),and 3(10).A legal professional may also fall within the definition of `financial institution` if their activities fall within the scope of reg3(3)(a).
[121] MLR 2007, regs 42 and 45. The SRA does not have the power to impose civil penalties in respect of breaches under the regulations, but may take disciplinary action in respect of such breaches on the basis that they contravene the SRA Code of Conduct Outcome (7.5), see SRA, *SRA Handbook* (Version 18, 2016) SRA Code of Conduct 2011.
[122]AML Practice Note 2013 para 4.1.
[123] Existing customers are also subject to CDD at `other appropriate times` on a risk sensitive basis, MLR 2007, reg 7(2); see also AML Practice Note 2013 para 4.10. Under MLRs 2007, reg 2(1) `business relationship` means `a business, professional or commercial relationship between a relevant person and a customer, which is expected by the relevant person, at the time when the contract is established, to have an element of duration`. An `occasional transaction` means a transaction (carried out other than as part of a business relationship) amounting to 15,000 euro or more, whether the transaction is carried out in a single operation or several operations which appear to be linked`. A law firm must cease to act for a client if it is unable to carry out CDD, MLR 2007, reg 11.
[124] MLR 2007, reg 7(3)(a),(b).
[125] See AML Practice Note 2013 paras 2.3.1, 2.3.2. See also FATF, *RBA Guidance for Legal Professionals* (2008) Ch 1, s3.

in respect of each individual retainer, and internal controls applied appropriately.[126]

(a) CDD Requirements

The CDD measures that are stipulated in Regulation 5 MLR 2007 require that a client must be identified, and for such identification to be verified using information from a `reliable and independent` source.[127] In practical terms, the verification process will involve reviewing original documents, electronic material or information from other relevant persons.[128]

This identification requirement is extended to include beneficial owners where they are not the client, requiring verification of such identity using `adequate measures, on a risk-sensitive basis`. [129] Where the client is a legal person, trust or similar entity, measures must be taken to understand their `ownership and control structure`.[130] Beneficial ownership requirements are a key AML weapon in that they seek to unravel those opaque ownership structures which are the hallmark of many money laundering transactions. As the client base of Top 50 law firms is predominantly made up of corporate vehicles in various forms, establishing beneficial ownership is a key issue for such firms.

The various permutations of beneficial ownership are set out in Regulation 6. With regard to unlisted companies, an individual is a beneficial owner if he directly or indirectly `ultimately owns or controls . . . more than 25% of the shares or voting rights in the body` .[131] In the alternative, and applicable to both listed and unlisted body corporates, a beneficial owner is someone who `otherwise exercises control over the management of the body.`[132] Appropriately tailored provisions apply with regard to partnerships, trusts and other entities, each featuring the dual measures

[126] AML Practice Note 2013 para 2.4.
[127] MLR 2007, reg 5(a).
[128] AML Practice Note 2013 para 4.3.3.
[129] MLR 2007, reg 5(b).
[130] ibid.
[131] MLR 2007, reg 6(1)(a).
[132] MLR 2007, reg 6(1)(b).

of beneficial ownership applicable to companies: either by way of a 25% interest in the entity, or by controlling it.[133]

It should be noted that the CDD requirements differ in relation to beneficial owners, in that a law firm is required to take `adequate measures, on a risk-sensitive basis` to verify their identity.[134] So it may decide, depending on the level of risk, to make use of information in the public domain, or ask the customer directly for such information, or obtain it from another source. The AML Practice Note 2013 acknowledges that often beneficial ownership information will only be available via the client or their representatives.[135] With regard to a client, a more stringent requirement exists: to verify their identity using reliable and independent sources.[136]

Law firms are also required to ascertain `the purpose and intended nature of the business relationship.`[137] This is designed to provide firms with a `meaningful basis` for future monitoring, and so may include information as to the origin of funds, copies of financial statements and intended level of transaction activity. [138]

(b) **Identification and Verification**

As the MLR 2007 do not prescribe what is acceptable evidence of identity, each law firm must make its own determination. The AML Practice Note 2013 therefore sets out detailed identification and verification procedures for a range of different entities.[139] It notes that during this process there is no obligation to `be an expert in forged documents` aside from evident forgeries.[140] The Note highlights the fact that CDD may be more challenging in respect of private and unlisted overseas companies or trusts, which is an issue reflected in the data chapters of the

[133] MLR 2007, reg 6(2) - (7).
[134] MLR 2007, reg 5(b).
[135] AML Practice Note 2013 para 4.3.3.
[136] MLR 2007, reg 5(a).
[137] MLR 2007, reg 5(c).
[138] JMLSG, *Prevention of money laundering/combating terrorist financing 2014 Revised Verson* (2014) pt I, para 5.3.20 -21.
[139] AML Practice Note 2013 para 4.6.
[140] ibid para 4.3.3.

thesis.[141] Particular caution is also advised in respect of foundations (the civil law equivalent of trusts) and in respect of those non-UK government agencies where there is a heightened risk of misappropriation of government funds.[142]

The AML Practice Note 2013 provides guidance in respect of identification and verification of any beneficial owner following an assessment of the risk each retainer poses.[143] Rarely will the extent of the beneficial owner CDD match that required for a client, but the AML Practice Note 2013 counsels that `the level of understanding required depends on the complexity of the structure and the risks associated with the transaction`.[144]

(c) **Simplified Due Diligence (SDD)**

Certain clients or products are considered to present a lower risk of money laundering and therefore law firms are permitted to apply SDD.[145] This means that, save where a suspicion of money laundering arises, no CDD will be required where a law firm has `reasonable grounds` to believe that a particular `customer, transaction or product` falls within a number of pre-defined categories.[146] This will arise, inter alia, where the client is a credit or financial institution subject to 3MLD (or equivalent non-EEA institutions subject to and supervised for compliance with equivalent requirements). [147] It will also arise in respect of companies with securities listed on a `regulated market` subject to `specified disclosure obligations`, and public authorities.[148] Whilst some guidance is provided by JMLSG

[141] Ibid para 4.6.3,4.6.4.
[142] Ibid para 4.6.4,4.6.5.
[143] ibid para 4.7.2. Criteria for assessing such risk are listed as `why your client is acting on behalf of someone else (ii) how well you know your client (iii) whether your client is a regulated person (iv) the type of business structure involved in the transaction (iv) where the business structure is based the AML/CTF requirements in the jurisdiction where it is based (v) why this business structure is being used in this transaction
(vi) how soon property or funds will be provided to the beneficial owner`.
[144] ibid para 4.7.2
[145] MLR 2007, reg 13.
[146] MLR 2007,reg 13(1).
[147] MLR 2007, reg 13(2).
[148] MLR 2007, reg 13(3),(5),(6). The terms `regulated market` and `specified disclosure obligations` are defined in MLRs 2007, reg 2. Specific products such as life insurance contracts and child trust funds also qualify for SDD, MLR 2007, reg 13(7)-(9).

on determining equivalence and whether specified disclosure obligations apply, this is by no means definitive, and law firms must still go through the detailed process of determining whether they may apply SDD to such clients. [149]

Pooled client accounts (PCA) operated by independent legal professionals also qualify for SDD, provided client identity information can be provided on request in relation to monies held on their behalf in the PCA.[150] At the time of the interviews, there was considerable debate as to whether PCAs would continue to be eligible for SDD, which in turn created concerns over banks potentially de-risking PCAs.

(d) Enhanced Customer Due Diligence (EDD)

Regulation 14 identifies a number of scenarios which present a higher risk of money laundering. In such scenarios, law firms must apply EDD on a `risk-sensitive` basis and conduct enhanced ongoing monitoring.[151]

Where a client is not physically present for identification, the EDD requirement is to take `specific and adequate` measures to counterbalance this elevated risk. [152] Law firms must take at least one of the following steps (i) gathering additional information to ensure the client`s identity is established, (ii) undertaking supplementary verification procedures or requiring certification by a bank, or (iii) ensuring that any initial payment is made into a bank account set up in the client`s name.[153] The AML Practice Note 2013 states that whilst any client who is not a natural person will never be physically present, as they act through their representatives, EDD will only apply following an assessment of the risks surrounding the retainer.[154]

[149] JMLSG, *JMLSG Guidance Notes 2014* (2014) pt III, para 3.
[150] MLRs 2007, reg 13(4). Exclusions also apply in relation to public authorities meeting specified criteria, and in relation to products such as certain insurance contracts, pension schemes and child trust funds under regs 13(5) -10.
[151] MLR 2007, reg 14(1).
[152] MLR 2007, reg 14(2).
[153] MLR 2007,reg 14(2)(a)-(c).
[154]AML Practice Note 2013 para 4.9.1.

EDD will also apply where a client is a politically exposed person (PEP) on the basis that a PEP may be particularly vulnerable to corruption.[155] A PEP is defined as someone who is or has held a `prominent public function` in the previous 12 months in a non UK state, an EU institution or international body.[156] The definition extends both to `immediate family members` and `known close associates` (in terms of a business, rather than a personal relationship).[157] Whether someone is a PEP may be determined by reference to information that the law firm already has, information which is known to the public, or by way of a commercial service provider.[158]

Once a PEP is identified, the law firm must obtain approval from senior management for that business relationship to exist, take `adequate measures` to establish the `source of wealth and source of funds` in relation to such business relationship or occasional transaction and to conduct enhanced ongoing monitoring.[159] The AML Practice Note 2013 states that clients should be questioned as to their wealth and source of funds and that enhanced ongoing monitoring will involve ensuring funds are paid from a nominated account and are proportionate to such client`s known wealth.[160]

Flexibility is built into Regulation 14, and there is a `catch-all` provision requiring EDD whenever there is a potentially higher risk of money laundering.[161] The AML Practice Note 2013 refers explicitly to policies published periodically by HM

[155] MLR 2007, reg 14(4).
[156] MLR 2007, reg 14(5)(a).
[157] MLR 2007, reg 14(5)(b),(c).
[158] AML Practice Note 2013 para 4.9.2. Law Society survey figures cite that 60% of respondents used third party providers to fulfil their PEP obligations. See The Law Society, *Anti-money laundering compliance by the legal profession in England and Wales* (2009).
[159] MLR 2007, reg 14(4); see also AML Practice Note 2013 para 4.9.2. Senior management is not defined in the MLR 2007 so may include, on a risk-sensitive basis, the head of a practice group, nominated officer, supervising, managing or other partner There is no requirement to proactively ascertain whether beneficial owners of a client are PEPs, however a risk based approach must be applied in respect of those beneficial owners actually known to be PEPs.
[160]AML Practice Note 2013 para 4.9.2.
[161] MLR 2007, reg 14(1)(b).The regulations are silent as to what constitutes EDD under these circumstances.

Treasury and FATF with regard to overseas jurisdictions with unsatisfactory AML provision and provides that EDD should be conducted where such jurisdictions touch on the retainer. [162]

(e) Ongoing Monitoring

As the risk of money laundering is not extinguished at the point of successful client inception, ongoing monitoring of a business relationship is required under Regulation 8. One aspect of ongoing monitoring involves the administrative task of maintaining up to date documentation, data or information on a client.[163] The other aspect of ongoing monitoring requires the `scrutiny of transactions . . . (including, where necessary, the source of funds)` to ensure they are consistent with the law firm`s knowledge of that client.[164] As with the initial CDD, the precise level of ongoing monitoring will be determined on a risk-sensitive basis and must satisfy the SRA that it is appropriate.[165] The AML Practice Note 2013 envisages that ongoing monitoring will be conducted by fee-earners and `involves staying alert to suspicious circumstances which may suggest money laundering`.[166]

(f) Reliance

Reliance provisions within MLR 2007 were intended to ease the CDD process somewhat by providing that a law firm may rely on specified third parties to conduct CDD, provided they consent to this.[167] Consequently under Regulation 17, reliance may be placed upon credit or financial institutions, auditors, insolvency

[162] AML Practice Note 2013 para 4.9.3; see also JMLSG, *JMLSG Guidance Notes 2014* (2014) para 4.2.2, which recommends EDD when a customer is non-resident or a business is cash intensive or has a disproportionately complex ownership structure. Countries that have inadequate AML provisions in place or anonymous transactions may also pose a higher risk.
[163] MLR 2007, reg 8(2)(b).
[164] MLR 2007, reg 8(2)(a),(b). See also MLR 2007, reg 7(2)MLR.
[165] MLR 2007, reg 8(3) provides that the considerations which apply to the level of CDD pursuant to reg 7(3) also apply to the level of ongoing monitoring.
[166] AML Practice Note 2013 para 4.4.
[167] MLR 2007, reg 17(1).

practitioners, external accountants, tax advisers or independent legal professionals.[168]

This provision is rarely utilised by the legal profession however.[169] This is because responsibility for any failure to comply with CDD obligations resides with the law firm. [170] In addition, law firms may be exposed to civil claims from entities relying upon them. It is for these reasons that the AML Practice Note 2013 invites law firms to consider that reliance may not always be appropriate and to `consider reliance as a risk in itself`.[171]

(iii) Record Keeping, Procedures and Training

(a) Record Keeping, AML Procedures and Procedures

A law firm must maintain records of a client`s identity and supporting records for a period of 5 years.[172] The rationale behind the record keeping requirements is to assist in any AML investigation, or in the detection and confiscation of laundered proceeds.[173] In addition, `appropriate` and `risk-sensitive` policies must be in place dealing with CDD, reporting, record-keeping, internal control, risk assessment and management, and monitoring policy compliance.[174] Each policy is intended to maximize a law firm`s ability to combat money laundering. Policies must therefore provide for the scrutiny of, inter alia, unusual or inherently risky transactions or those which `favour anonymity`. [175]

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[168] MLR 2007, reg 17(2)-(5). This is distinct from the outsourcing of CDD provided for in reg 17(4).
[169] The Law Society, *HM Treasury consultation on the transposition of the Fourth Money Laundering Directive – The Law Society response* (2016) 11.
[170] MLR 2007, reg 17(1)(b).
[171] AML Practice Note 2013 para 4.3.4.
[172] MLR 2007, reg 19.
[173] JMLSG, *JMLSG Guidance Notes 2014* (2014) para 8.2.
[174] MLR 2007, reg 20. Compliance with such policies must be monitored and managed, reg 20(1)(d). One of the weaknesses identified by the SRA in their thematic review of 2016 was the `low frequency` with which some firms reviewed their AML policies. Additionally, some firms either had `no or inadequate processes` to test their systems. SRA, *Anti Money Laundering Report* (2016) 12.
[175] MLR 2007, reg 20(2)(a) and (b).

(b) MLROs

The MLRO is a key weapon in the UK`s AML armoury and their significance is drawn out within the data chapters of the thesis. Law firms must appoint a nominated officer (MLRO) whose role is to receive disclosures under Part 7 POCA 2002, determine whether they should be reported to the NCA and, if appropriate, make such reports.[176] The AML Practice Note 2013 emphasises the need for any MLRO to have access to all information held by a firm with regard to a client, and that the MLRO should be of sufficient seniority to make reporting decisions which `must not be subject to the consent of anyone else`.[177] As is highlighted in Chapter 6, the potential impact of each MLRO`s decisions is highly significant both at a firm level and in a wider societal context given the sheer volume of deals transacted by Top 50 law firms alone.[178] Furthermore, the SRA commented that those MLROs who were either inadequately trained or inexperienced were found to have a `detrimental effect` on the firm`s AML standards.[179]

(c) AML Training

The FATF typology report issued in relation to the legal profession noted that those lawyers who were uneducated as to money laundering risks are more vulnerable to misuse.[180] Its concluding section also highlights the potential for more AML education of legal professionals both at law school and on a continuing education

[176] MLR 2007, reg 20(2)(d). In FCA dual regulated law firms, the MLRO performs a `controlled function` under the Financial Services and Markets Act 2000 ,s 59 and must be approved by the FCA.
[177] AML Practice Note 2013 paras 3.3.2. and 3.3.3.
[178] Top 50 law firms alone recorded deal volumes of £1,021billion in the first half of 2016. See The Law Society, *City Legal Index* (2016) 4.
[179] SRA, *Anti Money Laundering Report* (2016) 14.
[180] FATF, *Money Laundering and Terrorist Financing Vulnerabilities of Legal Professionals* (2013) 6.

basis.[181]The Government`s AML Action Plan published in 2016 also highlights the utility of education as an AML tool.[182]

The ongoing obligation imposed upon a law firm under Regulation 21 is to take `appropriate measures` such that `relevant employees` are made aware of AML legislation and are regularly trained to recognise and handle potential AML scenarios. The importance of AML training is such that the Law Society calls staff members `the most effective defence against launderers`.[183] It may also be recalled from earlier in this Chapter that an employee who does not know or suspect another is engaged in money laundering, and has not received AML training may use this as a defence to the failure to report offence by virtue of s330(7) POCA 2002. Regulation 21 is not prescriptive in its requirements as to the form of AML training, however the AML Practice Note 2013 recommends training at `regular and appropriate intervals` and `some type of training for all relevant staff every two years is preferable`. [184] The SRA also suggest that AML training should be considered as an integral part of its continuing competence regime, a concept which is discussed later in this Chapter.[185]

12. SRA AML Supervision

The Law Society is the AML supervisory authority for solicitors in England and Wales, and whilst it has retained its representative role within the profession, it has delegated its regulatory role to the SRA. [186] The SRA must therefore `effectively

[181] ibid 85; see also FATF,*RBA Guidance for Legal Professionals* (2008) para 102 where the inclusion of AML training is recommended at all levels of legal education.
[182] Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* (2016) 25,47.
[183] AML Practice Note 2013 para 3.9.
[184] ibid para 3.9.3.
[185] SRA, *Cleaning Up: Law firms and the risk of money laundering* (2014) 16.
[186] MLR 2007 reg 23(1)(c) sch 3. Some solicitors may be `dual` regulated. For example, solicitors may also be regulated by the FCA, The Insolvency Practitioner`s Association, The Council of Licensed Conveyancers or the Chartered Institute of Taxation. MLR 2007, reg 23(2)-(4) provides that where dual supervision applies, either the supervisors will agree who to appoint as supervisor (who will notify the relevant person or publish the agreement), or will co-operate with one another. As at 31 July 2016, there were 136,176 solicitors holding practising certificates, and 9,430 private practice law firms in England and

monitor` and take `necessary measures` for `securing compliance` with the MLR 2007.[187]

(i) The SRA Handbook 2011

SRA regulatory requirements are set out in the SRA Handbook .[188] As the Handbook covers all aspects of practice, the material set out below does not present an exhaustive account of SRA regulation, but focuses upon those areas of relevance to AML regulation.

(a) SRA Authorisation and Practising Requirements

The SRA Practice Framework Rules 2011 govern the types of business which may offer legal services, those services which may only be offered by authorised bodies and solicitors, and the requirements that must be in place for authorisation. [189] SRA regulatory compliance is required as a condition of authorisation.[190]

At an individual level, trainee solicitors and those seeking admission to the profession must meet the outcomes of the SRA suitability test, in addition to `authorised role holders` within law firms (comprising COLP, COFA, owners and managers).[191] The test is designed to uphold `the level of honesty, integrity and the

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Wales, see The Law Society, *Trends in the solicitors` profession Annual Statistic Report 2016* (June 2017) 2; see also MLR 2017, reg 46.

[187] MLR 2007, reg 24(1).

[188] SRA, *SRA Handbook* (Version 18, 2016).

[189] SRA, *SRA Handbook* (Version 18, 2016), SRA Practice Framework Rules 2011 (SRA Practice Framework Rules 2011). Under rule 8, solicitors are permitted to undertake `reserved work` and `immigration work`; under rule 19, compliance with SRA regulatory requirements is compulsory.

[190] SRA, *SRA Handbook* (Version 18, 2016), SRA Authorisation Rules 2011 (SRA Authorisation Rules 2011), rules 8.1(a) and 8.2. Compliance with statutory obligations is also required under rule 8.1(a)(ii). Law firms must appoint an SRA approved designated compliance officer for legal practice (COLP) who is tasked with ensuring compliance both with SRA authorisation requirements and with statutory obligations. They must also appoint an SRA approved designated compliance officer for finance and administration (COFA) who is tasked with ensuring compliance with the SRA Accounts Rules, ibid rule 8.5.

[191] See SRA, *SRA Handbook* (Version 18, 2016), SRA Suitability Test 2011 (SRA Suitability Test 2011); ibid, SRA Training Regulations 2014 (SRA Training Regulations 2014), reg 6; ibid,

professionalism expected by the public`, thus applications will be refused where there is, inter alia, evidence of dishonesty on the part of the applicant.[192] Ongoing regulatory control is exercised via the requirement for each solicitor to hold a current practising certificate which is renewed annually.[193] This may not be granted, inter alia, where the solicitor is suspended.[194]

The SRA comment that `education and training underpins the regulation of solicitors – it ensures the creation of competent and ethical practitioners.` [195] To that end, the SRA have adopted a `continuing competence` regime, defining the competencies required from solicitors in the SRA Statement of Solicitor Competence.[196] This is underpinned by the Statement of Legal Knowledge requiring knowledge of, inter alia, ethical concepts pertinent to the role of solicitor, solicitor`s accounts, and money laundering.[197]

SRA Admission Regulations 2011, reg 6; SRA Authorisation Rules 2011, rule 15. Those applying to be solicitors must have the requisite `character and suitability` (SRA Suitability Test 2011, Outcome (SB1); Solicitors Act 1974,s3) whilst authorised role holders must be `fit and proper` (SRA Suitability Test 2011, Outcome (SB2).

[192] SRA Suitability Test 2011, Overview. Applications will be refused `unless there are exceptional circumstances` when an applicant is, inter alia, convicted of a criminal offence involving either a custodial or suspended sentence (pt 1, para 1.1(a)), or involving dishonesty or fraud, perjury and/or bribery (pt 1,para 1.1(b)) or which the SRA consider sufficiently serious (para 1.1(i)).Regulatory history is also taken into account under para 6.

[193] Solicitors Act 1974, s 9; SRA, *SRA Handbook* (Version 18, 2016) SRA Practising Regulations 2011 (SRA Practising Regulations 2011), reg 2; SRA Practice Framework Rules 2011, rule 9.

[194] SRA Practising Regulations 2011, reg 2.2(b),3,2(a). The remaining provisions of regulation 3 grant the SRA the discretion to refuse to issue a certificate or to impose conditions under reg 7 should certain circumstances apply. Pertinent examples include where the applicant is subject to SRA disciplinary sanction, rebuke or fine (reg 3.1(a)(i),(ii)).

[195] SRA Training Regulations 2014, Overview.

[196] SRA, *Statement of solicitor competence* (2015). The Statement comprises: (i) the statement itself, (ii) the threshold standards applicable on qualification and beyond, and (iii) an underpinning statement of legal knowledge. Section A1 states that a solicitor is required to `act honestly and with integrity, in accordance with legal and regulatory requirements and the SRA Handbook and Code of Conduct`. This is supported by the requirement to explain the solicitor`s ethical framework to clients (C2(h)). Other provisions which complement a solicitor`s AML obligations include record keeping requirements (D2) and `applying the rules of professional conduct to accounting and financial matters` (D3(c)).

[197] SRA, *Statement of legal knowledge* (2015) para 1(a),(f) and (d).

(b) The SRA Principles and the SRA Code of Conduct 2011

All SRA regulation is underpinned by ten mandatory Principles (Principles) which `define the fundamental ethical and professional standards` the SRA expect from the profession, and operate in addition to any legislative requirements.[198] Those Principles require legal professionals to, inter alia, uphold the rule of law, act with integrity, and comply with their legal and regulatory obligations, including AML obligations.[199]

The SRA Code of Conduct 2011 (Code of Conduct) contextualises the Principles within practice, exemplifying them via a series of mandatory `Outcomes` and expanding on them via a series of non-mandatory illustrative `Indicative Behaviours` (IB).[200] Within the Code of Conduct, there is an explicit, overarching requirement for solicitors to comply with anti-money laundering legislation.[201] In addition, many provisions of the Code of Conduct support AML regulation in that they either promote ethical conduct towards clients and third parties, or promote the orderly management of a law firm.

A number of obligations govern the relationship between a solicitor and their client. Hence, solicitors must comply with the law and the Code of Conduct when deciding whether to accept or terminate a retainer, and may not act for a client

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[198] ibid, Introduction, para 3(a); see also ibid, SRA Principles 2011. The Principles apply to both individuals and firms regulated by the SRA; see SRA Principles 2011, note 2.3(a)).
[199] The Principles state that a solicitor must: `1. uphold the rule of law and the proper administration of justice; 2. act with integrity; 3. not allow your independence to be compromised; 4. act in the best interests of each client; 5. provide a proper standard of service to your clients; 6. behave in a way that maintains the trust the public places in you and in the provision of legal services;7.comply with your legal and regulatory obligations and deal with your regulators and ombudsmen in an open, timely and co-operative manner; 8. run your business or carry out your role in the business effectively and in accordance with proper governance and sound financial and risk management principles; 9. run your business or carry out your role in the business in a way that encourages equality of opportunity and respect for diversity; and 10.protect client money and assets.` SRA, *SRA Handbook* (Version 18, 2016), SRA Principles 2011. Principles 1, 2 and 6 extend to a solicitor`s activities outside of their practice, including in any `private capacity` (ibid pt 2, para 5.1).
[200] SRA, *SRA Handbook* (Version 18, 2016) SRA Code of Conduct 2011.
[201] ibid ch 7, Outcome (7.5).

where a conflict of interest exists or there is a significant risk of conflict arising.[202] Solicitors also owe a duty of confidentiality to every client which, whilst surviving both the termination of the retainer and the death of the client, is expressly overridden in favour of the requirements of any money laundering legislation under Outcome (4.1).[203]

The Code of Conduct also governs the relationship between a solicitor and third parties. Hence, a solicitor must not `attempt to deceive or knowingly or recklessly mislead the court`, or be complicit in a third party doing so. [204] They must comply with any notification and reporting requirements in the SRA Handbook and co-operate fully with the SRA.[205] Solicitors are required to self-report `serious failure` to comply with the SRA Handbook, any action taken by another regulator, any `material changes to relevant information` about them, and `serious misconduct by any person or firm authorised by the SRA`.[206]

The Code of Conduct sets out provisions intended to promote the orderly management of law firms.[207] A `clear and effective governance structure and reporting lines` are required, coupled with systems to achieve, monitor and deal with risks to compliance with the provisions of the SRA Handbook .[208] As stated earlier, compliance with AML legislation is expressly required as part of a law firm`s governance provisions.[209]

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[202] ibid ch 1, Outcome (1.3); ch3, Outcomes (3.4) and (3.5).
[203] ibid, ch 4, Outcome (4.1) provides that `you keep the affairs of clients confidential unless disclosure is required or permitted by law or the client consents`. IB(4.4)(c) illustrates an exception to the duty of disclosure to the client of `all information material to the client`s matter`, when `legal restrictions effectively prohibit you from passing the information to the client, such as the provisions in the money-laundering and anti-terrorism legislation`; see also POCA 2002, s 337 which protects disclosures made under the Act.
[204] SRA, *SRA Handbook* (Version 18, 2016) SRA Code of Conduct 2011, ch 5, Outcomes (5.1) and (5.2); see also ch 5 generally.
[205] ibid ch 10, Outcomes (10.1), (10.2) and (10.6).
[206] ibid Outcomes (10.3) and (10.4).
[207] ibid ch 7.
[208] ibid Outcomes (7.1)-(7.3).
[209] ibid Outcome (7.5).

(c) SRA Accounts Rules 2011

Solicitors, unlike many other professionals in the regulated sector, operate a client account, the misuse of which has been identified as a key money laundering typology.[210] Consequently, detailed rules on solicitors` accounts are set out in the SRA Accounts Rules 2011 (Accounts Rules 2011), the paramount objective of which is to keep client money safe.[211] Client money must be held separately, either in a designated separate account or in a pooled client account, with each client`s funds being used exclusively in relation to their retainer with the law firm.[212] The circumstances in which payments may be made to and from any client account are strictly regulated.[213]

Of key relevance in terms of AML provision is the operation of Rule 14.5, which prohibits the use of the client account to provide banking services, thus offering what the SRA call `an important `first line of defence` to clients who may seek to take advantage of your client account to launder money` .[214] Any movement of funds to or from the client account must be linked to an `underlying transaction` or a service which is part of the solicitor`s `normal regulated activities`.[215] Guidance note (v) to Rule 14.5 expands on the significance of the provision, warning

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[210] FATF, *Money Laundering and Terrorist Financing Vulnerabilities of Legal Professionals* (2013) 37.

[211] SRA, *SRA Handbook* (Version 18, 2016) SRA Accounts Rules 2011, pt 1, rule 1.1. For the definition of `client money` see pt 1, rules 12.1(a) and 12.2.

[212] ibid pt 1, rules 1.2(a), (b) and (c).

[213] ibid pt 2; see also pt 1, rule 1.2(e) which states that `proper accounting systems, and proper internal controls over those systems` must also be in place.

[214] SRA `Warning Notice: Improper use of a client account as a banking facility` (*SRA*,18 December 2014) < http://www.sra.org.uk/bankingfacility/> accessed 15 July 2015. Any breach of rule 14.5 may also constitute a breach Principles 1,3,6 and 8 as well as Outcome 7.5 of the Code of Conduct. Between 2012-5 the SRA received 65 reports related to the breach of Rule 14.5, SRA, *Anti Money Laundering Report* (2016) 5.

[215] SRA Accounts Rules 2011, pt 2, rule 14.5. The SRA state `it is not sufficient that there is an underlying transaction if you are not providing legal advice to one of the parties` and that there must be a `reasonable connection between the underlying legal transaction and the payments`, SRA `Warning Notice: Improper use of a client account as a banking facility` (*SRA*,18 December 2014) <http://www.sra.org.uk/bankingfacility/> accessed 15 July 2015.

specifically against providing any assistance to money launderers. Note (v) also comments that Rule 14.5 mirrors the stance of the Solicitors Disciplinary Tribunal (SDT): that offering banking facilities is not a `proper part of a solicitor`s everyday business`.[216] Non-compliance with Rule 14.5 was identified as a `current priority risk` by the SRA in July 2014, and was also pinpointed as a risk affecting large law firms in particular.[217]

The `obvious risk` of money laundering associated with breaches of Rule 14.5 was highlighted in the recent and high profile case of *Fuglers.*[218] The earlier SDT Tribunal decision of *Wood & Burdett* had also acknowledged the underlying risk that offering banking facilities (in this case cashing third party cheques through client account) `could have been utilised by an unscrupulous person as a vehicle for money laundering`, an action which Moore-Bick LJ would later referred to as `an obvious invitation to money laundering`.[219]

Given the money laundering risks that client accounts present, it is unsurprising that such accounts have been the subject of much debate in recent years, both as to their very existence, and as to how they should be treated.[220] Client accounts are therefore considered extensively in the data chapters of this thesis.

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[216] *The Attorney General for Zambia v Meer Care & Desai and others* [2008] EWCA Civ 1007 [234] per Lloyd LJ with regard to a defendant solicitor `it is plain that he was providing the service of a bank account, albeit only in credit, or, . . . a `short-term money park`, with almost none of the payments through the client account being related to any legal work done by the firm. It is equally plain that this was not a proper thing for a firm of solicitors to do.` [2008]All ER (D) 406 (Jul); see also *Patel v SRA* [2012] EWHC 3373, [18] per Cranston J, `movements on a client account must be in respect of instructions relating to an underlying transaction which is part of the accepted professional services of solicitors.`, [2012] All ER (D) 354 (Nov).

[217] SRA, *SRA Risk Outlook 2014/15* (2014) 24-25. See also SRA `Warning Notice: Improper use of a client account as a banking facility` (*SRA*,18 December 2014) <http://www.sra.org.uk/bankingfacility/> accessed 15 July 2015.

[218] Fuglers LLP v SRA [2014]EWHC 179 (Admin),[41] per Popplewell J, [2014] All ER (D) 91 (Feb). In this case Fuglers LLP had passed £10million through their client account on behalf of their insolvent client Portsmouth City Football Club Ltd.

[219] See *Wood & Burnett* (8699/2002), para 58. For comments of Moore-Bick LJ see Patel v SRA [2012] EWHC 3373,[40]; see also SDT v Clyde & Co 2017 460690.

[220] Pooled client accounts automatically qualified for SDD under MLR 2007, reg 13. Such qualification is no longer automatic under MLR 2017, reg 36(4).

(ii) AML Regulation by the SRA

The SRA regulates the conduct of solicitors in England and Wales in accordance with the regulatory objectives (RO) set out in s 1 Legal Services Act 2007: objectives which include, inter alia, protecting and promoting the public interest and supporting the rule of law.[221] The SRA deploys `outcomes-focused regulation` (OFR) which it describes as regulation `in line with the intent of the regulatory objectives.`[222] OFR is intended to operate in a `risk- based, proportionate and targeted` manner so that once the level of risk is identified, regulation is `prioritised and applied proportionately` against any `unacceptable threat`.[223]

(iii) SRA Assessments of Money Laundering Risks

In its capacity as regulator, the SRA has produced a number of reports which identify the money laundering risks faced by the sector.[224] The SRA published an AML thematic review in 2016, concluding that `most of the firms we visited had

[221] The regulatory objectives are: `a) protecting and promoting the public interest;(b) supporting the constitutional principle of the rule of law;(c) improving access to justice;(d)protecting and promoting the interests of consumers;(e) promoting competition in the provision of services . . . ;(f) encouraging an independent, strong, diverse and effective legal profession;(g) increasing public understanding of the citizen's legal rights and duties;(h) promoting and maintaining adherence to the professional principles.` A new Office for Professional Body Anti-Money Laundering Supervision has been proposed, which will oversee SRA supervision, see HM Treasury, `UK tightens defences against money laundering (*HM Treasury*, 13 March 2017) https://www.gov.uk/government/news/uk-tightens-defences-against-money-laundering accessed 31 August 2017.

[222] SRA, *SRA Regulatory Risk Framework* (2014) 2.

[223] SRA, 'Outcomes-focused regulation at a glance' (*SRA*, 10 October 2011)< http://www.sra.org.uk/solicitors/freedom-in-practice/OFR/ofr-quick-guide.page> accessed 30 June 2014; SRA, *SRA Regulatory Risk Framework* (2014) 2, 5. For the assessment of risks see ibid; see also SRA, *SRA Regulatory Risk Index* (2014); SRA, *Severity – the relative harm of risks* (2013).

[224] See for example SRA,*Cleaning up:law firms and the risk of money laundering* (2014) 7-9, which identified the following risks (i) the involvement of multiple firms, (ii) using the client account as a banking facility, (iii) failures in CDD, and (iv) infiltration of law firms by launderers; SRA, *Risk Outlook 2014/5* (2014).

effective compliance frameworks in place.[225] A number of weaknesses were identified, however, with regard to the following: (i) applying EDD, (ii) dealing with PEPs, (iii) establishing the source of wealth and source of funds, (iv) ongoing monitoring, and (v) sanctions requirements. [226] In addition, MLROs who were `inexperienced or inadequately trained` were found to have a `detrimental effect` on AML provision.[227]

The earlier SRA Risk Outlook 2015/6 identified specific AML compliance issues relating to large commercial law firms, namely (i) ensuring that EDD is conducted on PEPs and high net worth individuals, and (ii) understanding the source of funds on a retainer.[228] Prior to that, the SRA Risk Outlook 2014/5 identified that large corporate firms were at risk of (i) PEPs, and those clients with connections to organised crime, laundering through intermediaries, and (ii) breaches of SRA Accounts Rule 14.5 whereby banking facilities are offered which are not directly linked to an underlying client retainer.[229]

13. Enforcement

Whilst a detailed examination of the enforcement of the regime remains outside the scope of this thesis, this section seeks to provide a brief overview of enforcement provisions by way of context. AML enforcement against legal

[225] SRA, *Anti Money Laundering Report* (2016) 10.
[226] ibid 11.
[227] ibid 11. In addition, some firms did not have a deputy MLRO, or the MLRO did not have oversight on AML training attendance. A `general lack of appropriate training for finance staff` was also identified as a weakness; see also SRA, *SRA Risk Outlook 2017/8* (2017) 37. Since 2015/6, the SRA report receiving around 175 AML-related reports per annum, ibid 34.
[228] SRA, *SRA Risk Outlook 2015/6* (2015) 39.
[229] SRA, *SRA Risk Outlook 2014/15* (2014) 25.

professionals takes place by way of regulatory action by the SRA, and criminal prosecution. [230]

In terms of regulatory action, the SRA have an extensive disciplinary arsenal at their disposal. [231]They may issue a rebuke or impose a fine.[232] At an individual level, a lawyer may have their practising certificate suspended, or conditions imposed. [233]The SRA may also enter into regulatory settlement agreements with legal professionals, which have the effect of terminating disciplinary proceedings.[234] At a firm level, authorisation may be revoked, suspended, or conditions may be imposed or modified.[235] Alternatively, the SRA may intervene directly in a law firm.[236] Serious matters may also be referred to the SDT, an independent tribunal that may suspend or strike off solicitors, or impose fines in excess of the maximum that may be imposed by the SRA.[237] Despite its wide ranging powers, the number of solicitors involved in SDT proceedings in respect of money laundering offences or breaches of the regulations is small.[238]

Middleton and Levi argue that it is regulatory intervention rather than criminal sanctions which are more likely to be effective against wrongdoing by legal

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[230] Unsuccessfully laundered assets may be the subject of civil recovery and confiscation. See POCA 2002,pts 2 and 5. Lawyers may also be subject to civil action as constructive trustees.

[231] Measures will be taken in accordance with the SRA enforcement strategy, SRA,`SRA enforcement strategy` (SRA, 26 October 2015) < https://www.sra.org.uk/sra/strategy/sub-strategies/sra-enforcement-strategy.page> accessed 31 August 2017.

[232] SRA Handbook (Version 18, 2016) SRA Disciplinary Procedure Rules 2011 (SRA Disciplinary Procedure Rules 2011), rules 2.1(a),(b); Solicitors Act 1974, s 44D; Administration of Justice Act 1985, sch 2, para 14B; Legal Services Act 2007, s 95.

[233] Solicitors Act 1974, s 13B; SRA Practising Regulations 2011, reg 7.

[234] SRA `Regulatory Settlement Agreements` (*SRA*) < https://www.sra.org.uk/sra/decision-making/guidance/disciplinary-regulatory-settlement-agreements.page> accessed 31 August 2017.

[235] SRA Authorisation Rules 2011, rules 22,9 and 10. Approval of COLPs, COFAs, owners and managers may also be withdrawn, or conditions imposed, rules 17 and 14.5.

[236] Solicitors Act 1974, s 35 and sch 1.

[237] SRA Disciplinary Procedure Rules 2011, rule 10. For SDT powers see Solicitors Act 1974, s 47.

[238] In 2011, 1 solicitor was struck off, and 2 refused restoration to the roll for a POCA 2002 conviction. In respect of other AML breaches, the SDT imposed the following penalties on solicitors: 6 struck off, 2 suspended, 8 fined, 2 reprimanded, 2 non-solicitor conveyancers barred from employment in SRA regulated practices, 2 had no orders made against them, The Law Society, *Annual Anti-Money Laundering Supervisor`s Report* (2012) 15.

professionals, particularly those protected by LPP.[239] This view rests on the basis that professional rules can focus on `underlying behaviours`, and a regulator will be empowered to suspend or freeze the business of any law firm, consequently protecting the public, and doing so without the stringent requirements of criminal law.[240]

Legal professionals may also be subject to criminal prosecution under POCA 2002 and MLR 2007 (and MLR 2017). As highlighted in Chapter 1, as details of AML prosecutions within the profession are not systematically collated, it is difficult to determine how many lawyers are prosecuted for AML offences. Nevertheless, the number of prosecutions of lawyers for money laundering offences is low for a number of reasons. FATF identifies several practical challenges when prosecuting legal professionals, in addition to the difficulties in proving the *mens rea* element of an offence, namely:

> . . . uncertainty about the scope of privilege, the difficult and time-consuming processes for seizing legal professional's documents, and the lack of access to client account information.[241]

The likelihood therefore is that law enforcement will only ever be able to prosecute a small proportion of money laundering offences by legal professionals, given that these practical difficulties in obtaining evidence `disincentivises criminal investigations`.[242]

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[239] David Middleton and Michael Levi, `The role of solicitors in facilitating `Organized Crime`: Situational crime opportunities and their regulation` (2004) 42(2/3) Crime, Law & Social Change 123, 137.
[240] ibid 137.
[241] FATF, *Money Laundering and Terrorist Financing Vulnerabilities of Legal Professionals* (2013) 31,32.
[242] David Middleton and Michael Levi, 'Let Sleeping Lawyers Lie: Organized Crime, Lawyers and the Regulation of Legal Services' (2015) 55(4) Brit.J.Criminol 647,649.

14. Concluding Comments

The AML obligations explored in this Chapter were imposed upon the legal profession in response to FATF`s `gate-keeper initiative`, and have been deployed across multiple jurisdictions.[243] In response, many objections have been raised by the sector, exemplified by the Joint Statement that was issued to FATF on behalf of the legal professions in the US, Europe, Japan and Canada.[244] The Statement notes that `we can accept neither inroads into professional confidentiality and our duty of loyalty to clients, nor obstacles in access to justice.` [245]This has resulted in multiple challenges to the regime in jurisdictions such as Belgium, France, and Canada.[246]

In the UK, the combined features of the `all crimes` approach in POCA 2002, together with a reporting threshold based on suspicion, and a negligence based limb to the failure to report offence in s 330 of the Act, imposes wide-ranging obligations upon the profession, which will be explored in the data chapters. Inevitably, compliance with the array of CDD and AML policy measures within MLR 2007 also imposes a cost burden upon the profession, and although no `headline` figures are available across the sector as a whole, annual compliance costs can run into millions of pounds for the largest firms.[247]

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[243] FATF, *Global Money Laundering & Terrorist Financing Threat Assessment* (2010) 44, para 214 ; Kevin Shepherd, `Guardians at the Gate: The Gatekeeper Initiative and the Risk-Based Approach for Transactional Lawyers` (2009) 43 (4) Real Prop. Tr. & Est. L.J. 607.
[244] Letter from ABA & Others to FATF (3 April 2003).
[245] ibid.
[246] Colin Tyre, `Anti-Money Laundering Legislation: Implementation of the FATF Forty Recommendations in the European Union`, 2010 J. Prof. Law. 69,72; Ronald J. MacDonald, `Money Laundering Regulation-What Can Be Learned from the Canadian Experience` 2010 J.Prof.Law. 143, 144.
[247] The Law Society, *The costs and benefits of anti-money laundering compliance for solicitors - Response by the Law Society of England and Wales to the call for evidence in the Review of the Money Laundering Regulations 2007* (2009) 48;see also The Law Society, *HM Treasury consultation on the transposition of the Fourth Money Laundering Directive -The Law Society Response* (2016) 4.

This Chapter has contextualised the thesis by examining the AML legislative and regulatory provisions with which the legal profession must comply, and the penalties that may be applied for non-compliance. Chapter 3 will outline the methodological approach of the study before turning to a consideration of the research findings in the subsequent data chapters.

Chapter 3 – Methodology

1. Introduction and Research Aims

This thesis has its genesis in three key areas. First, the thesis stems from a zeitgeist involving the unparalleled scrutiny of legal profession vulnerability to and complicity in money laundering.[1] Recent years have seen the discourse surrounding legal professional involvement in money laundering shift from that of `gatekeeper` to `professional enabler` and `facilitator`.[2] As detailed in the preceding Chapters of the thesis, the UK response has been to impose an array of AML obligations upon the profession. These range from the requirement to report suspicions of money laundering under POCA 2002, to the CDD and record-keeping obligations under MLR 2007 and MLR 2017. It is the challenges surrounding compliance with these AML obligations that are the focus of this research. Much research on money laundering and the legal profession is quantitative in nature, or focuses on the facilitation of money laundering via the sector. This research expands the field by approaching the issue from a compliance perspective, with a focus on a section of the legal profession that can be hard to access for the purposes of research.

The second key influence on this thesis is the author`s extensive practitioner experience in Top 50 UK headquartered law firms as a senior transactional corporate banking lawyer, which provided invaluable insight into the practicalities of the AML regime. It is this practitioner background which partly determined the focus of the thesis on Top 50 UK law firms. Furthermore, such firms form a customary grouping within the profession and, due to the size and nature of their businesses, experience particular AML compliance issues which may not be a feature within smaller firms.

[1] See introduction to Chapter 1 of the thesis.
[2] Lawyers were brought within MLR 2003 and MLR 2007 following the EU `gatekeeper` initiative. Thereafter, Serious Crime Act 2015,s 45 criminalised participating in the activities of an organised crime group, an offence which was targeted, inter alia, at lawyers.

Finally, the thesis is informed by an undercurrent of social obligation. The hope is that the thesis, and the publications flowing from it, may have a positive impact on AML compliance in Top 50 law firms, if only by raising awareness further amongst participants.

It is set against this background that the thesis aims to answer the following research question: what compliance issues do Top 50 UK headquartered law firms in England and Wales encounter when operating within the UK AML regime? In order to answer this question a qualitative methodology was adopted. A series of semi-structured qualitative interviews were conducted, both with transactional lawyers at partner level, and with participants fulfilling senior compliance roles within their organisations. The interviews elicited multiple in depth perspectives of the AML regime as it applies to Top 50 firms, which were then thematically analysed.

This Chapter explores the methodological approach of the thesis. It outlines the ontological and epistemological considerations underpinning the research and the rationale behind using semi-structured interviews as a research method. Both the sampling strategy deployed and ethical considerations applied are then discussed. A reflexive account of the researcher`s position, both as a former practitioner `insider` and as an academic `outsider` is provided. The chapter then recounts how the data was collected, managed and analysed. The limitations of the research are considered, concluding with a brief introduction to the subsequent data chapters.

2. Research Strategy and Research Method

The thesis sits within a qualitative research paradigm, the essential feature of which is that it `uses words as data`, or that `it records the messiness of real life, puts an organising framework around it and interprets it in some way`.[3] Whilst the

[3] Virginia Braun and Victoria Clarke, *Successful qualitative research: A practical guide for beginners* (SAGE Publications Ltd 2013) 3,20.

detailed analysis of words or `thick descriptions` forms the cornerstone of much qualitative research, the qualitative paradigm is multifaceted and draws upon other defining elements such as : collecting data in context, interpreting meaning and generating theory inductively.[4] The multi-layered complexity of the topic under examination, with all its nuances in practice, together with the use of technical language throughout meant that an in depth qualitative exploration was imperative. Flowing from this overarching paradigm the thesis adopts an interpretivist epistemological position such that `the stress is on the understanding of the social world through an examination of the interpretation of that world by its participants`.[5] It also espouses a constructivist ontological stance which holds that `social properties are outcomes of the interactions between individuals`.[6]

The selection of semi-structured qualitative interviews as a research method was informed by the author`s ontological and epistemological stances in combination with the research question posed. Qualitative interviews have the capacity to provide a `depth and roundedness of understanding` in contrast to the more superficial data that other data generation methods are able to provide.[7] Such interviews can also facilitate the in depth exploration of a topic on the basis that they provide a forum within which `additional information can be obtained by probing the initial responses.`[8]

The qualitative interview method was also selected for pragmatic reasons. The Law Society themselves report low response rates to their requests for survey

[4] The term `thick description` has its roots in ethnography where it is used to refer to a detailed account of events in a particular context. See generally Clifford Geertz, *The interpretation of cultures: Selected essays* (22nd edn, Basic Books 1977). Virginia Braun and Victoria Clarke, *Successful qualitative research: A practical guide for beginners* (SAGE Publications Ltd 2013) 6. See also David Silverman, *Interpreting Qualitative Data* (SAGE Publications Ltd 2015) 5.
[5] Alan Bryman, *Social Research Methods* (4th edn, OUP 2012) 380.
[6] ibid.
[7] Jennifer Mason, *Qualitative Researching* (SAGE 1996) 41.
[8] Daphne Keats, *Interviewing - a practical guide for students and professionals* (OUP 2000) 20

information.[9] Prior to commencing the thesis the author informally questioned a number of Top 50 lawyers as to the likelihood of them responding to a questionnaire from a researcher either known or unknown to them. The overwhelming response from these informal enquiries was that a survey would simply be deleted if sent via e-mail, or ignored.

This method also showcases one of the strengths of qualitative research in that its exploratory nature meant that the research was not limited by `the researcher`s imagination and existing knowledge in the field`.[10] For example, in addition to responding to questions on specific aspects of the regime, participants were given the opportunity to comment freely on any other aspects of the AML regime relevant to their day to day practice. Notwithstanding this exploratory element of the research, the interviews were semi-structured in their design in order to ensure that key aspects of the UK AML regime were considered. According to Berg, the advantage of using semi-structured interviews is that it:

> . . . allows for in-depth probing while permitting the interviewer to keep the interview within the parameters traced out by the aim of the study.[11]

3. Purposive Sampling

All participants were selected using a non-probability purposive sampling approach. The central tenet of this strategy is that `those sampled are relevant to the research questions that are being posed.`[12] Some participants were recruited using a `snowball` sampling technique whereby existing participants suggested

[9] See for example The Law Society, *The costs and benefits of anti-money laundering compliance for solicitors - Response by the Law Society of England and Wales to the call for evidence in the Review of the Money Laundering Regulations 2007* (2009).
[10] Virginia Braun and Victoria Clarke, *Successful qualitative research: A practical guide for beginners* (SAGE Publications Ltd 2013) 24.
[11] Bruce Berg, *Qualitative research methods for the social sciences* (6th edn, Pearson 2007) 39.
[12] Alan Bryman, *Social Research Methods* (4th edn, OUP 2012) 418.

other contacts having `the experience or characteristics relevant to the research.`[13] 40 Interviews were conducted with two categories of participants from Top 50 law firms: (i) 20 solicitors (referred to as `transactional participants`), and (ii) 20 MLROs, Deputy MLROs, or those fulfilling senior compliance roles within their organisations (referred to as `compliance participants`). The data generated from this sample must therefore be contextualised as offering the perspectives of professionals from within Top 50 law firms, who may also have a potential vested interest in the UK AML regime by virtue of their roles. Within this overarching sampling framework, participants were selected according to their relevance to the thesis in terms of their seniority, practice area and firm type.

(i) All Participants selected from Top 50 UK Headquartered Law Firms

The thesis focuses on Top 50 UK law firms headquartered in the UK as determined by annual turnover figures published in `The Lawyer UK 200` (Top 50).[14] This annual commercial publication is widely utilised across the industry given that neither the Law Society nor the SRA publish data on turnover. Top 50 firms are a customary grouping within the legal profession and Paul Philip, chief executive of the SRA commented in November 2014 that `the profession fragments after the first 50 or 60 firms`.[15] Such firms are considered `large` firms by the Law Society both in terms of turnover and according to the more traditional measures of partner count (where over 26 partners is considered large) or solicitor count (where over 41 solicitors is considered large).[16] The firms from which participants were drawn had their headquarters in the UK. Whilst a number of international law firms have a strong presence in the UK via their London offices, such firms are outside the scope

[13] ibid 424.
[14] See for example The Lawyer, `UK 200 2016: The Top 100` (*The Lawyer*, 24 October 2016) < https://www.thelawyer.com/knowledge-bank/white-paper/uk-200-2016-top-100/>accessed 8 August 2017.
[15] Comment made during SRA Compliance Conference on 26 November 2014.
[16] The Law Society, *The Legal Services Industry - Part 2 Main Sectors* (2012).

of this study, although their perspectives on the UK AML regime may well form the subject matter of future research.

The SRA have identified money laundering risks specific to large firms.[17] The SRA do not have a formal definition of the term `large` as firms are typically classified according to a blend of factors such as the risk they present to clients, in addition to the number of solicitors they employ or their turnover. The SRA have confirmed that a Top 50 firm would undoubtedly also constitute a large firm for their purposes.[18] Each Top 50 firm is regulated by the SRA for AML compliance, although such firms may also be dual regulated by the Financial Conduct Authority with regard to other business activities. The scope of this thesis is restricted to AML regulation by the SRA.

(ii) Firm Type Within Top 50 Law Firms

Top 50 law firms may be broken down into a number of subcategories. Whilst it is important to stress that a purposive sampling strategy does not attempt to assemble a representative sample of participants, drawing participants from a range of firms enhanced the gathering of multiple perspectives of the UK AML regime. Hence participants were drawn from `Magic Circle`, `Silver Circle`, international and national firms within the Top 50.[19] Furthermore, participants were drawn from each of the following numerical groupings ranking annual turnover figures: 1-10, 11-20, 21-30, 31-40 and 41-50. A detailed anonymised breakdown of participants is set out at Appendix 1.

[17] SRA, SRA Risk Outlook 2014/15 (2014) 25.
[18] Telephone conversation between the author and SRA on 27 November 2014.
[19] These terms are loosely identified within the industry. `Magic Circle` firms comprise 5 of the most prestigious law firms, and is a term first used in the 1990`s by legal journalists, see Chambers Student,`Magic circle law firms` (*Chambers Student*)< http://www.chambersstudent.co.uk/law-firms/types-of-law-firm/magic-circle-law-firms> accessed 1 September 2017. `Silver Circle` laws firms denote 6 law firms outside the Magic Circle. The term was first used by The Lawyer in 2005, see for example Matt Byrne,`The Lawyer 100 shows success of silver circle` (2005) 19 (34) The Lawyer 1,1.

(iii) Seniority and Practice Area

The research focused on solicitor participants at partner level on the basis they have sufficient seniority to structure and oversee client matters, and to authorise payments from client account. Participants were selected from key transactional practice areas, which may be vulnerable to money laundering attempts.[20] Participants were drawn from the following practice areas: corporate, banking and finance, real estate, tax and litigation. Whilst litigation technically falls outside the scope of MLR 2007, there is evidence that `sham` litigation has been utilised as a money laundering typology via the sector.[21] These `transactional` participants were selected in order to provide their perspective on AML at the coalface of legal practice.

Compliance participants were selected who were MLROs, Deputy MLROs or those performing a senior compliance role. Such participants were selected in order to provide invaluable insights on the AML regime from a compliance, as opposed to transactional, perspective.

4. Ethics and Reflexivity

(i) Ethical Considerations

Ethical approval was obtained in accordance with the University of Liverpool`s policy on research ethics on the basis that human subjects were being interviewed.[22] A participant information sheet was provided and written consent

[20] FATF, *Money Laundering and Terrorist Financing Vulnerabilities of Legal Professionals* (2013).
[21] ibid 71.
[22] University of Liverpool, *Policy on ethical approval for research involving human participants, tissues or personal data* (2016).

was obtained from all participants prior to the interviews taking place. As all participants were highly articulate professionals, there were no concerns as to whether such consent was sufficient to constitute `informed` consent.[23]

Ethical concerns conjured up by the use of the phrase `money laundering` within the title of the thesis were also minimal: the focus of the thesis is on the compliance issues that the legal sector face when working within the UK AML regime, as opposed to uncovering previously undisclosed money laundering activity. Whilst it was possible that during the interview process participants might disclose money laundering offences which had not previously been disclosed to the relevant authorities, the risk of intentional disclosure was remote. Such a disclosure could trigger, inter alia, imprisonment of the individual making the disclosure for either: (i) a substantive money laundering offence, or (ii) a `failure to report` offence, each under POCA 2002. Participants were also self-selecting in the sense that complicit money launderers would naturally decline to participate in the research. There remained a minimal risk of inadvertent disclosure of previously undisclosed offences, either in relation to the participant themselves or to third parties. However, the participant information form made it clear that any such disclosure would trigger a reporting requirement on the part of the author.

(ii) Researcher Reflexivity

The thesis evolved out of the author`s former practitioner experience as a senior transactional corporate banking lawyer in several Top 50 law firms, giving the author invaluable insight into AML provisions and their application within the

[23] Bryman states that informed consent applies where participants are in receipt of `as much information as might be needed to make an informed decision` to participate or not. Alan Bryman, *Social Research Methods* (4th edn, OUP 2012) 712.

regulated sector. This background meant that the author occupied the role of an `insider` with a common professional background and immersion in legal culture. [24]

The author`s role as an `insider` former practitioner was pivotal in a number of ways. The author was able to draw upon a pre-existing professional network to gain access to many participants, who then suggested other contacts from their networks for inclusion in the research. In the absence of this professional network, many participants would not have agreed to being interviewed. Furthermore, the subject matter of the interviews was technical in nature and acronym laden. Therefore a detailed practical knowledge of the area was essential.

The `insider` status of a researcher may shape the way in which data is both generated and analysed. A shared professional background meant that it was easier to establish `credibility and rapport` with interviewees, which is a key benefit of `insider` research in addition to facilitating access to participants [25] Corbin Dwyer and Buckle, for example, note that when interviewed by `insider` researchers, `participants are typically more open with researchers so that there may be a greater depth to the data gathered.`[26] The converse may also apply, and participants may be less candid when being interviewed by an insider.[27] It may also mean that `the participant will make assumptions of similarity and therefore fail to explain their individual experience fully.`[28] Furthermore, a number of interviews were `acquaintance` interviews, where a professional relationship existed prior to

[24] Griffith defines an insider as someone with a `lived familiarity with the group being researched.` and an outsider as `a researcher who does not have any intimate Knowledge of the group being researched, prior to entry into the group.` See Alison Griffith, `Insider / Outsider: Epistemological Privilege and Mothering Work` (1998) 21(4) Human Studies 361, 361.

[25] Justine Mercer, `The Challenges of Insider Research in Educational Institutions: Wielding a double-edged sword and resolving delicate dilemmas`,12 < https://lra.le.ac.uk/bitstream/2381/4677/1/Justine_Mercer_Final_Draft_Insider_Research_Paper.pdf> accessed 10 August 2017.

[26] Sonya Corbin Dwyer and Jennifer L Buckle, `The Space Between: On Being An Insider-Outsider In Qualitative Research` (2009) 8(1) IJQM 54*,58.*

[27] Saeeda Shah, `The researcher/interviewer in intercultural context: a social intruder!` (2004) 30(4) British Educational Research Journal 549, 569.

[28] ibid.

the research.[29] Garton and Copland note that `data in these interviews are generated in a particular way.`[30] In particular, they note that the `shared worlds` of participants can be used `as a resource to co-construct the interview.`[31]

Insider researchers also have to `contend with their own pre-conceptions` and biases.[32] This may also have an impact on the data analysis process should the researcher, for example, place `an emphasis on shared factors between the researcher and the participants and a de-emphasis on factors that are discrepant`.[33] In short, `familiarity may blunt criticality.`[34] Therefore part of the research process involved a reflexive awareness of the challenges presented by `insider` research and their potential impact on the thesis.

Two further points are worthy of note. First, the insider/outsider dichotomy has been rejected by many authors in favour of a continuum whereby the researcher`s status shifts `back and forth across different boundaries`.[35] The fact that the author is an academic researcher rather than a current practitioner in a competitor law firm has the effect of shifting the author`s position somewhat away from a purist insider position. This may well have the effect of reducing researcher subjectivity.

Secondly, Corbin Dwyer and Buckle reject the primacy of an insider/outsider position as a determinant of quality research. They conclude that:

> . . . the core ingredient is not insider or outsider status but an ability to be open, authentic, honest, deeply interested in the experience of one's

[29] Sue Garton and Fiona Copland, ``I like this interview; I get cakes and cats!`: the effect of prior relationships on interview talk` (2010) 10(5) Qualitative Research 533.
[30] ibid 548.
[31] ibid 547.
[32] Justine Mercer, `The Challenges of Insider Research in Educational Institutions: Wielding a double-edged sword and resolving delicate dilemmas`, 25 < https://lra.le.ac.uk/bitstream/2381/4677/1/Justine_Mercer_Final_Draft_Insider_Research_Paper.pdf> accessed 10 August 2017.
[33] Sonya Corbin Dwyer and Jennifer L Buckle, `The Space Between: On Being An Insider-Outsider In Qualitative Research` (2009) 8(1) *IJQM 58.*
[34] Saeeda Shah, `The researcher/interviewer in intercultural context: a social intruder!` (2004) 30(4) British Educational Research Journal 549, 569.
[35] Alison Griffith `Insider / Outsider: Epistemological Privilege and Mothering Work` (1998) 21(4) Human Studies 361, 368.

research participants, and committed to accurately and adequately representing their experience.[36]

5. Data Collection

(i) Interview Preparation

Prospective participants were contacted by e-mail with an invitation to take part in the research. The initial e-mail gave brief details of the study and attached a recruitment flyer. It was emphasised that the research would not touch on any confidential client information and that the interviews would be anonymised, both on an individual and firm basis.

Prospective participants were either already known to the author, or contacted directly following an internet search of their firms` website. Some participants then suggested other contacts during the course of the research. Very few contacts declined to take part in the research and those that agreed to participate typically responded within 24 hours. Prior to the interviews, participants were e-mailed copies of a participant information sheet setting out further details of the study, together with a consent form, hard copies of which were brought to the interviews for signature.

Interview schedules for transactional and compliance participants were created. Many of the questions included on the schedules concerned those issues raised in the numerous consultations in the field by the Government and FATF. The schedules started with general AML questions, then moved through the various elements of the AML framework as a structure to guide the interviews. Questions relating to participants` perceptions of the regime were interwoven throughout. The use of interview schedules ensured that key areas were covered in the interviews, but also allowed for flexibility in the interview process. For example, participants were asked many open questions throughout and the last interview

[36] ibid 59.

question was a `catch-all` question designed to capture anything further that participants wanted to add.

(ii) Conducting The Interviews

A pilot interview was conducted with a participant well known to the author, which provided an opportunity to refine and rephrase some of the interview questions, as well as providing an indication of the duration of the interviews. The data from the pilot interview was not analysed and does not form part of the data chapters of the thesis.

The interviews took place between 15 November 2015 and 16 June 2016 and, with the exception of the pilot interview, took place at participants` offices. 40 interviews were conducted in total with participants from 20 firms. As stated earlier in this Chapter, 20 participants were solicitors at partner level, and 20 were participants who were MLROs, Deputy MLROs, or those performing a senior compliance role within their organisations. As the interviews took place prior to the transposition of 4MLD via MLR 2017, the provisions considered in the interviews are those under MLR 2007, although topical issues under discussion as part of the 4MLD transposition process were considered. The interviews were typically an hour long.

The interviews began with the author providing a brief introduction to the research. Participants were then asked a series of general questions on the AML regime before turning to more specific aspects of the regime such as CDD, training and the SARs regime. Notwithstanding this ordered structure, the interviews allowed for flexibility by asking a number of open questions, by re-ordering the questions in response to each participant`s train of thought, and by probing participants` responses further. It is this fluidity that led Kvale to liken the interview process to a game of chess where each move restructures the chessboard.[37] One of the key skills of an interviewer is therefore the:

[37] Steiner Kvale, *Doing Interviews* (SAGE 2007) 64.

> . . . ability to sense the immediate meaning of an answer, and the horizon of possible meanings that it opens up. [38]

The author was therefore very much an active listener during the interviews in order to be able to ask further questions and elicit the fullest responses from participants. The interviews were a hugely enjoyable part of the research process.

6. Data Management

(i) Transcription

Each interview was audio recorded digitally with consent, and transcribed orthographically by the author using voice recognition software trained to recognise both the author`s voice and the specialist terminology deployed. The audio tapes were then replayed to ensure the accuracy of the transcripts. The verbatim form of transcription was selected as being appropriate for a thematic analysis of the data.

Adopting the role of researcher-transcriber was undoubtedly a time-consuming process but its benefits are well documented. Qualitative researchers report that it engenders a `greater familiarity with the data and deeper insight` whilst Jovchelovitch & Bauer state that transcription `is actually the first step of analysis` which `opens up a flow of ideas for interpreting the text`.[39] Research has also demonstrated that each transcriber `subtly interprets and changes the kind of text produced` ` and that professional transcribers lack `theoretical sensitivity`, namely a sensitivity to the nuanced meaning of the data.[40]

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[38] ibid 60.

[39] Sandra Jovchelovitch and Martin Bauer, `*Narrative interviewing*` in Martin W. Bauer and George Gaskell (eds), *Qualitative researching with text, image and sound: A practical handbook* (SAGE 2000).

[40] D Thomas Markle and Richard E West and Peter J Rich, 'Beyond transcription: Technology, change, and refinement of method' (2011) 12(3) Forum Qualitative Sozialforschung / Forum: Qualitative Social Research citing Judith C. Lapadat and & Anne

(ii) Anonymity and Confidentiality

A range of overlapping measures was employed to ensure both anonymity and confidentiality. All participants were ascribed pseudonyms in the transcripts and any identifying features removed both on an individual and firm basis. All recorded interviews and transcripts were uploaded to the university`s secure storage facility and all material was deleted from the digital voice recorder immediately.

7. Data Analysis

The interview data was analysed by way of thematic analysis, which is a method developed by Braun and Clarke of `identifying, analysing and reporting patterns (themes) within data `.[41] The analysis was conducted using the six stages outlined by Braun and Clarke as a guiding framework comprising: (1) familiarisation with the data, (2) producing initial codes, (3) searching for themes, (4) reviewing those themes, (5) defining and naming themes; and (6) writing up analysis.[42]

Braun and Clarke describe the familiarisation stage, with the immersion of the researcher into the data in search of pattern and meaning, as the `bedrock` of subsequent analysis.[43] Familiarisation began with the author conducting the interviews and subsequently transcribing them. Each transcript was then read several times in order to identify potential themes, a stage which Braun and Clarke

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C. Lindsay,`Examining transcription: A theory-laden methodology`(*Annual Meeting of the American Educational Research Association,* San Diego, April 1998).<http://www.qualitative-research.net/index.php/fqs/article/view/1564/3249> accessed 16 August 2016. Theoretical sensitivity is a concept developed within grounded theory by Glaser and Strauss, see Barney G. Glaser and Anselm L Strauss, *The discovery of grounded theory: Strategies for qualitative research* (Weidenfeld and Nicolson 1968).

[41] Virginia Braun and Victoria Clarke, 'Using thematic analysis in psychology' (2006) 3(2) Qualitative Research in Psychology 77,79. Braun and Clarke utilise thematic analysis as a stand-alone method of analysis in its own right.

[42] ibid Table 1, 87.

[43] ibid.

frame as being purely `observational and casual, rather than systematic and precise`.[44] Each transcript was then analysed by way of `complete coding`, an all-encompassing method of coding whereby `*anything* and *everything* of interest or relevance` to the thesis was coded.[45] Data analysis software (QSR NVivo 10) assisted with this process.[46] Complete coding produced a mass of codes from which the author created a series of overarching themes and sub-themes from the patterns identified in the data, which were reshaped as the analysis unfolded.[47] It is those themes which form the subject matter of the data chapters of the thesis.

8. Limitations of The Research and Quality Criteria

(i) Limitations of the Research

This thesis draws upon views on AML compliance from multiple different perspectives. Whilst not attempting to obtain a representative sample, participants were drawn from different types and sizes of firms within the Top 50, and transactional participants were drawn from varied practice areas. The even split between transactional participants and compliance participants enhanced further the depth of the research as it provided perspectives from those at the `coalface` of legal practice, in addition to those fulfilling a compliance role.

The limitation of the research is that it does not explore AML compliance issues from the perspective of the SRA, NCA or law enforcement agencies. This means that the research explores AML compliance issues from a very specific perspective: that of a solicitor or compliance professional within a Top 50 law firm, who may have a potential vested interest in the UK AML regime. The `insider` status of the

[44] Virginia Braun and Victoria Clarke, *Successful qualitative research: A practical guide for beginners* (SAGE Publications Ltd 2013) 205.
[45] ibid 206. Complete coding produces codes derived both at a purely semantic level and at an interpretative level determined by the researcher.
[46] The decision to use QSR NVivo 10 was driven by the size of the data set and researcher preference.
[47] ibid 224. Braun and Clarke state that a theme is a combination of codes and will exhibit a `central organising concept` ie will capture different aspects of the theme, in contrast to the more granular level code which `will capture one idea`. Themes may then be organised hierarchically (with overarching themes, themes and subthemes) or laterally, ibid 231.

author also shaped and informed the way in which the data was generated and analysed.

(ii) Quality Criteria

The quality criteria which apply within a quantitative paradigm, such as reliability and validity, are not considered as appropriate criteria within a qualitative paradigm.[48] Nevertheless, the research may be considered to be `transferable` in the sense envisaged by Lincoln and Guba, where the reader makes a determination as to whether or not the research is transferable given their particular context and in response to the `thick description` provided by the researcher.[49] Furthermore, the research is compliant with a quality checklist for thematic analysis produced by Braun & Clarke, which covers all aspects of the research process from transcription to writing up. [50] Hence the interviews were accurately transcribed then exhaustively coded and analysed.

9. Concluding Comments

This Chapter has outlined the ontological and epistemological positions informing the research, which sits within a qualitative paradigm and used semi-structured interviews as its research method in order to access multiple views on AML compliance within Top 50 law firms. A purposive sampling strategy was deployed and ethical approval obtained for the research. The interview transcripts were anonymised, transcribed by the author, and thematically analysed. A reflexive account of the author`s position as an `insider` was also considered. A limitation of the research is that it views AML compliance through the distinct lens of those who are either partners in Top 50 law firms, or fulfil a senior compliance role in

[48] Virginia Braun and Victoria Clarke, *Successful qualitative research: A practical guide for beginners* (SAGE Publications Ltd 2013) 279-80.
[49] Yvonna Lincoln and Egon Guba, *Naturalistic Inquiry* (SAGE 1985) 316 cited in Virginia Braun and Victoria Clarke, *Successful qualitative research: A practical guide for beginners* (SAGE Publications Ltd 2013) 282.
[50] ibid 287.

such firms. Therefore it does not represent the perspectives of either the SRA, NCA or law enforcement.

The following four data chapters present the research themes, accompanied by analysis and discussion of each theme. Chapter 4 explores the overarching AML legislative regime within which participants operate. Chapter 5 focuses on the mechanical aspects of the regime surrounding CDD, training and the client account. Chapter 6 explores participants` experiences of the SARs regime. Chapter 7 examines participants` perceptions of the regime including, inter alia, their perception of money laundering threats, their views on the costs and benefits of compliance, and Top 50 firms in a global context.

Chapter 4 - The UK AML Legislative Framework

1. Introduction

The UK legal profession operates within the AML legislative framework provided for under POCA 2002 in tandem with the MLR 2007, the detail of which has been examined in earlier chapters. This Chapter will explore key features of the overarching legislative framework and its impact on the profession in practice. An overarching theme present in the interview data is that the regime imposes a disproportionate burden on the profession, a position which is largely attributable to the way the legislation is structured. Accordingly, this Chapter will consider key issues raised by interview participants as to: (i) the scope and breadth of POCA 2002, (ii) the inclusion of an `intent` element in the substantive money laundering offences, and (iii) excluding criminal sanctions from the MLR 2007. Subsequent chapters will then explore the more granular level mechanical aspects of the regime under the MLR 2007 as they apply to the profession.

It should be noted that in this and subsequent chapters, where notable or relevant, interview participants may be categorised as `compliance participants` or `transactional participants`. As detailed in Chapter 4, the former category comprises 20 participants operating as MLROs, deputy MLROs or holding a senior compliance role, whereas the latter category comprises 20 participants drawn from transactional practice areas at partner level.

2. POCA 2002 – the `all crimes` approach[1]

(i) Background

Historically, the UK has elected to `gold plate` its AML regime and transposed the Third EU Money Laundering Directive (3MLD) into UK law in a manner which went

[1] This material was first published by Thomson Reuters in Sarah Kebbell, `"Everybody`s Looking at Nothing" - the Legal Profession and the Disproportionate Burden of the Proceeds of Crime Act 2002` (2017) 10 Crim.L.R 741 and is reproduced by agreement with the Publishers.

further than the strict requirements of the Directive.[2] Hence POCA 2002 criminalises dealings with `criminal property`, a definition so widely cast that it encompasses *all* crimes, and extends to any direct or indirect `benefit` derived from criminal conduct.[3] The concept of `benefit` adds a further layer of complexity to the Act as the term includes any notional saving made pursuant to criminal conduct in addition to the more classical concepts of `property` and `pecuniary advantage`.[4] The rationale behind the adoption of an `all crimes` approach is a purely practical one: it does not require any assessment to be made as to the seriousness or otherwise of any underlying criminal offence.[5]

The effect this drafting has in practice is that an array of minor offences and regulatory breaches with criminal sanctions attached to them (referred to as `technical` offences throughout this thesis) will trigger a substantive money laundering offence under POCA 2002.[6] Examples often cited by the profession are the failure to comply with a tree preservation order, or to obtain an asbestos-related environmental licence, both of which will constitute predicate offences under the Act.[7] Such offences may come to light when effecting transactional work

[2] Council Directive 2005/60/EC of 26 October 2005 on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing [2005] OJ L309/15. This was transposed into UK law by way of the MLR 2007 and the Terrorism Act 2000 and Proceeds of Crime Act 2002 (Amendment) Regulations 2007, SI 2007/3398.

[3] POCA 2002, s 340(3) provides that `Property is criminal property if (a) it constitutes a person's benefit from criminal conduct or it represents such a benefit (in whole or part and whether directly or indirectly), and (b) the alleged offender knows or suspects that it constitutes or represents such a benefit. Only a deposit taking institution may avail itself of a *de minimis* threshold of £250 (s 339A) pursuant to ss 327(2C), 328(5), and 329(2C).

[4] For the definition of `property` see POCA 2002, s 340(9). Pecuniary advantage is not expressly defined but is referred to in ss 340(6) and (7) of the Act.

[5] This rationale is explained in Secretary of State for the Home Department*, Money Laundering and the Financing of Terrorism: the Government Reply to the nineteenth Report from the House of Lords European Union Committee Session 2008–09, (HL Paper 132, Cm 7718, 2009) 11,12.* Hence a bank clerk, for example, would not be in a position to distinguish between differing categories of crimes.

[6] Such minor offences and regulatory breaches are typically referred to by participants as `technical` breaches in that they trigger the requirement to make a notification to the NCA, whilst not being perceived by such participants as posing a concrete risk of money laundering.

[7] See provisions under the Town and Country Planning Act 1990 and Town and Country Planning (Tree Preservation) (England) Regulations 2012, SI 2012/605 in relation to tree preservation orders. See also *R v Davey* [2013] EWCA (Crim) 1662, [2014]1 Cr App Rep (S) 205, where a confiscation order under POCA 2002 had been granted in an amount of

on behalf of a client. Any notional saving made by an offender due to their failure to obtain an environmental licence for example will then constitute `criminal property`. In respect of such criminal property the law firm must make a Suspicious Activity Report (SAR) to the NCA, and/or seek consent to continue with the relevant transaction on the basis that such `authorised disclosure` under the `consent regime` is a complete defence to the substantive money laundering offences.[8]

In terms of reporting levels, solicitors submitted 3,461 SARs in 2014/5, (constituting under 1% of all SARs submitted to the NCA), although concerns have been raised by the NCA and the SRA over declining numbers of SARs from the sector in recent years.[9] The NCA has not published a more detailed breakdown of SARs from the sector, and so it is not possible to identify whether specific sections of the profession predominate in terms of the number of reports they make. The majority of legal sector SARs are `consent ` SARs (75.52%) however, and this may suggest that such reports are more likely to be `technical` in nature on the basis that law firms are seeking `consent` to continue with a transaction rather than declining to act.[10]

This issue has received sustained attention from the Law Society over the years, who are of the view that the `definition of criminal property lies at the heart of the anomalies and unintended consequences of the UK`s anti-money laundering regime`.[11] The Society raises concerns that the definition results in `unending tainting` of individuals where criminal property tracks through from one

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£50,000. This sum reflected the increased property value resulting from the felling of a tree protected by a tree preservation order. For asbestos related offences see, inter alia, Health and Safety at Work Act 1974.

[8] For reporting obligations and authorised disclosure provisions see POCA 2002, ss 330, s 331 s 327(2)(a), s 328(2)(a), and s 329(2)(a). Since June 2016, consent requests have been referred to as `requests for a defence to a money laundering offence`, see NCA, *Requesting a defence from the NCA under POCA and TACT* (2016).

[9] NCA, *Suspicious Activity Reports (SARs) Annual Report 2015* (2016) 11; SRA, *Anti-Money Laundering Report* (2016), 32; 3,935 legal sector SARs were submitted in 2012/3, 3,610 were submitted in 2013/4, NCA, *Suspicious Activity Reports (SARs) Annual Report 2014* (2015) 12.

[10] NCA, *Suspicious Activity Reports (SARs) Annual Report 2015* (2016) 11.

[11] The Law Society Money Laundering Task Force, *Law Society response to the SARs Regime Review `Call for Information`* (2015) 2.

transaction to another such that `it can make it almost impossible for them to conduct their affairs lawfully again`.[12] It is on this basis that the Law Society has repeatedly argued for several amendments to POCA 2002, including the exclusion of minor offences and regulatory breaches.[13]

Such exclusions would not have any effect on other sectors obliged to report to the NCA under POCA 2002. For a financial institution, for example, money laundering concerns are typically raised in connection with the movement of funds through a bank account. In contrast to law firms then, such institutions will be unaware of the underlying features of a transaction. This means that, even under the existing regime, banks are unable to assess whether there have been any `technical` breaches on the part of their customers, such as the failure to obtain an environmental licence. The multiplicity of consultations during the transposition of the Fourth EU Money Laundering Directive (4MLD), together with the enactment of the Criminal Finances Act 2017 and the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (MLR 2017) have failed to temper the `all crimes` approach of POCA 2002.[14]

The retention of the `all crimes` approach following the transposition of 4MLD has been influenced in part by the recommendations made by FATF, the global AML standard setting body, of which the UK is a member.[15] One of the measures put forward in the FATF Recommendations 2012 was that countries should criminalise money laundering in relation to `all serious offences, with a view to including the

[12] The Law Society, *Financial Action Taskforce Consultation Response Reviewing the standards – preparing for the 4th round of mutual evaluations* (2011) 19, 22.
[13] The Law Society Money Laundering Task Force, *Law Society response to the SARs Regime Review `Call for Information`* (2015) 2. The Law Society also argue for: (i) a definition of `criminal property` whereby property constitutes an asset rather than any notional savings, (ii) for consideration of a *de minimis* threshold in POCA 2002 applicable to the legal profession.
[14] Council Directive 2015/849 EC of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, amending regulation (EU) no 648/2012 of the European Parliament and of the Council, and repealing directive 2005/60/EC of the European parliament and of the Council and Commission Directive 2006/70/EC [2015] OJ L141/73.
[15] FATF, *International Standards on Combating Money Laundering and The Financing of Terrorism & Proliferation - The FATF Recommendations* (2012, updated June 2017).

widest range of predicate offences.` [16] Nevertheless, whilst 4MLD seeks to align itself with the FATF Recommendations 2012, its provisions oblige member states to criminalise money laundering in respect of `serious crimes`, and do not require the `all crimes` approach which the UK has adopted.[17]

The consent regime remains intact despite proposals to remove it and replace it with an `entity` rather than `transaction` based reporting system. Such a system would require SARs to be made in respect of organisations and individuals, as opposed to each transaction undertaken by them. Nor has the UK acted upon an alternative proposal set forth by the Law Society whereby a `tiered` reporting system could apply to the legal sector. Under this system, lawyers would simply `grade the importance of the SARs they submit`.[18]

Set against this background, analysis of the responses from participants highlights the negative effects the expansive scope of POCA 2002 has on the legal profession in practice. Participants raised a number of practical issues with the `all crimes` regime, in addition to several conceptual issues, culminating in an overall perception that the regime imposes a disproportionate burden upon the profession. Each of these responses from participants is more fully explored below.

(ii) The Burden of POCA 2002 on the Legal Profession - `Everybody`s looking at nothing`[19]

(a) The Lack of Distinction between Minor Offences and Serious Crimes

Participants reported that, owing to its structure, POCA 2002 had far too broad a reach, which had the effect of creating a `cumbersome regime`.[20] Participants felt

[16] ibid recommendation 3 (emphasis added).
[17] See para 4 of the preamble to 4MLD which states that, `Union action should continue to take particular account of the FATF Recommendations`. Serious crimes are listed within the definition of `criminal activity` in 4MLD, art 3(4).
[18] Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* (2016) paras 2.7, 2.8. See also The Law Society, *Response of the Law Society of England and Wales to the consultation issued by the Home Office and HM Treasury on the Action Plan for anti-money laundering and counter-terrorist finance – legislative proposals* (2016) 4.
[19] Compliance interview 18 dated 08/04/16.

that the Act was disproportionate in its effect in that minor infractions were dealt with in the same way as serious crime, with those minor offences automatically escalated into money laundering scenarios merely by virtue of the definition of `criminal property` under the Act. This inequitable approach was highlighted by, for example, the participant who commented with regard to such minor infractions, `throwing in those offences with very serious criminal offences is the wrong approach . . . because they`re trying to do very different things.'[21] This view, that a distinction should be drawn between minor and more serious offences, was echoed by many participants, reflected by the MLRO who added:

> . . . if you compare a minor regulatory breach to let's say a very large scale fraud, they are very different in quality, quantity and character`.[22]

Whilst participants may have formed their own, differing, views as to what constitutes a serious crime, it should be noted that 3MLD took a broad approach to the definition. In addition to predicate offences such as fraud and corruption, all offences carrying a prison sentence in excess of one year fall within the definition of `serious crimes`.[23] The same broad approach to the definition is adopted in 4MLD, with tax offences included as a predicate offence, and both Directives are underpinned by a wide definition of criminal `property`. [24]

The majority of participants expressed the clear view that minor offences and regulatory breaches attracting criminal sanctions should be excluded altogether from the ambit of the Act, with virtually all participants performing a compliance role holding this view. These minor offences and breaches of regulations were typically referred to by participants as `technical` breaches in that they trigger the requirement to make a notification to the NCA, whilst not being perceived by such participants as `real` money laundering, a distinction which will be explored further later in this Chapter.

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[20] Compliance Interview 12 dated 26/02/16.
[21] Compliance Interview 9 dated 15/12/15.
[22] Compliance Interview 19 dated 24/05/16.
[23] For the definition of `serious crimes` see 3MLD, art 3(5). The serious crimes which comprise `criminal activity` are listed in 4MLD, art 3(4).
[24] For the definition of `property` see 3MLD, art 3(3) and 4MLD, art 3(3).

Despite the UK Government explicitly choosing to adopt the `all crimes` approach reflected in the Act, and whilst participants were aware that the legislation was drafted in this manner, its effect is so draconian that several participants simply assumed that the inclusion of technical offences represented an unintended consequence or by-product of the legislation, encompassing offences which the Act `was never designed to pick up`.[25] As one transactional partner summarised in respect of regulatory breaches, `that`s not what I would imagine the legislation intended to catch`.[26]

(b) The Administrative Burden of Technical SARs

Submitting SARs in respect of technical breaches is both time consuming and resource intensive, resulting in an additional administrative burden on law firms. As one participant observed, `the amount of time that is spent dealing with minor regulatory offences, you know, I think clouds everything`.[27] In practical terms, the amount of time and resource spent making a technical report as opposed to a more substantive report can be the same, and potentially even greater where the notional saving or benefit is difficult to identify and therefore harder to articulate to the NCA. Participants also spoke of making defensive technical reports `covering our backs`, ie complying with the technical requirements of the Act to avoid liability under the substantive money laundering offences, an enduring issue which has been a feature of the AML arena for many years now.[28] Such defensive reporting can be seen as an inevitable consequence of combining an `all crimes` AML approach with criminal sanctions of up to 14 years imprisonment under the substantive money laundering offences.[29] Cumulatively, the submission of multiple technical reports across the sector as a whole can result in what one participant memorably deemed to be nothing more than a large scale `paper pushing` exercise

[25] Compliance Interview 6 dated 08/12/15.
[26] Transactional Interview 13 dated 01/12/15.
[27] Compliance Interview 12 dated 26/02/16.
[28] Compliance Interview 1 dated 17/11/15. For defensive reporting comments see SRA, *Anti-Money Laundering Repor*t (2016) 32.
[29] The substantive offences are set out in POCA 2002, ss 327-9. Criminal sanctions are set out in POCA 2002, s 334 (1) (b).

on the part of the profession and the NCA.[30] In short, `everybody`s looking at nothing`.[31]

(c) Transactional Interruption

In addition to the administrative burden created by the Act, making a `technical` report may also have a more serious and disproportionate commercial impact on transactions being effected by law firms. Should a technical breach causing property to become criminal for the purposes of POCA 2002 come to light in the course of a transaction, a SAR must be submitted to the NCA and consent sought to continue with the transaction. As no `prohibited act` in respect of which consent is sought may take place prior to such consent being granted, this may result in the commercial transaction being halted.[32] It was this concern that was voiced by the transactional partner who, whilst fully supporting the aims of POCA 2002, said:

> . . . the notion that you have to stop a £1 billion deal for a £100 fine . . . to actually halt that transaction is disproportionate and it can also have quite a serious commercial effect . . . if you're actually working to a serious commercial deadline.[33]

In summary, a number of participants felt that the requirement to make SARs in respect of technical breaches serves simply to `generate far more administrative difficulty and transactional interruption than is justified` for law firms.[34]

(d) The NCA and Technical SARs

For their part, the NCA were perceived by some participants as being `overwhelmed by issues like . . . listed building consent` or swamped with a `deluge` of technical notifications from law firms.[35] As one participant noted:

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[30] Compliance Interview 18 dated 08/04/16.
[31] Compliance Interview 18 dated 08/04/16.
[32] POCA 2002, s 336(10).
[33] Transactional Interview 7 dated 25/11/15.
[34] Compliance Interview 9 dated 15/12/15.
[35] Compliance Interview 3 dated 25/11/15, Compliance Interview 1 dated 17/11/15, Transactional Interview 2 dated 18/11/15.

> I get the sense that the NCA is drowning under the weight of notifications which are not real in the sense, you know, they're sort of tax or the environmental or the data protection ones.[36]

This perception was amplified by another participant who said of the NCA that, `pure regulatory breaches isn't something that they're really focusing on`. [37] Whether this perception is accurate or not is unclear. Whilst the NCA have expressed concern in recent times over both the decline in quantity and poor quality of legal sector SARs, the NCA have made no public comment suggesting any chagrin over the potential multitude of technical SARs submitted to them by law firms.[38]

(e) POCA 2002 Detracts from the Aim of the Legislation

The detrimental effect of POCA 2002 on the legal profession extends further than purely administrative inconvenience or transactional interruption. It has a corrosive effect on the confidence that the profession have in the AML regime more broadly, with many participants forming the view that the inclusion of technical offences actually detracted from or did not fulfil the purpose of the Act.

Following the transposition of 3MLD into national law, the UK has embraced a `risk-based` approach to AML, the central tenet of which is that resources should be appropriately targeted to the areas of greatest money laundering risk. This approach is reiterated in the Government`s AML Action Plan published in 2016 (Action Plan 2016) which expressly states:

[36] Compliance Interview 8 dated 14/12/15.
[37] Compliance Interview 14 dated 10/03/16, Compliance Interview 18 dated 08/04/16.
[38] The concern over the decline in SARs is raised in the National Risk Assessment 2015, see HM Treasury and Home Office, *UK national risk assessment of money laundering and terrorist financing* (2015) paras 6.91- 6.93; see NCA, *Suspicious Activity Reports Annual Report 2014* (2015) 13, 27 and 28 whereby the NCA liaised with the SRA and the Law Society with regard to poor quality SARs.

> We expect the banks and other firms subject to the Money Laundering Regulations to take a proportionate approach, focusing their efforts on the highest risks, without troubling low risk clients with unnecessary red-tape.[39]

The inclusion of technical offences within the regime however militates against a risk-based approach in practice. Some participants noted that resources were being channelled into making technical reports which could be better utilised in addressing more serious money laundering concerns. One participant observed:

> . . . it`s just muddying the waters so that people stop concentrating on what we should really be looking at and what actually are the issues as opposed to . . . reporting on somebody not having carried out an asbestos survey.[40]

This concern was echoed by the participant who regretfully noted that:

> We`re spending all this time reporting – well, you know, then you're going to miss, or there is a much greater chance that you will miss the bigger stuff because, you know, you're not being able to target your resources to . . . the *real* areas of risk.[41]

This diversion of resources is an issue that was acknowledged by the Government in its Action Plan 2016 by stating :

> . . . too much resource at present is focused on dealing with regulatory compliance, and too little is focused on tackling financial crime risk.[42]

Nevertheless, the position remains that technical offences still fall within the ambit of POCA 2002 following the transposition of 4MLD, and therefore resources will still be channelled into dealing with technical SARs.

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[39] Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* (2016) 3.
[40] Compliance Interview 1 dated 17/11/15.
[41] Compliance Interview 12 dated 26/02/16 (emphasis added).
[42] Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* (2016) 12.

(f) The Questionable Intelligence Value of `Technical` SARs

Concerns were also raised that the more technical SARs submitted to the NCA do not have any intelligence value. This was an issue raised by several participants. As with many aspects of the AML regime, which remain shrouded in guesswork and estimates, it is difficult to establish a clear link between legal sector technical SARs in isolation and the prevention of money laundering or the facilitation of the confiscation of criminal property. The participants` views on the questionable utility of technical SARs supports the view expressed by the Law Society that the `all crimes` approach under POCA 2002 spawns a multitude of SARs, the `vast majority being of limited intelligence value`.[43] It also reflects the complaints of their membership as to `receiving minimal feedback from the SARs they make`. [44] This is an issue that has been considered recently in the Government`s Action Plan 2016, where the Home Office conceded that, `we need radically more information to be shared between law enforcement agencies, supervisors, and the private sector`.[45] There has been some concrete action in this area, and improved information sharing procedures amongst the regulated sector and NCA are enacted within the Criminal Finances Act 2017. [46]

Several participants went further and expressed doubts as to whether making technical reports actually achieved their AML purpose in a wider sense, such as the MLRO whose view of the Act was that:

> I think it`s lost proportionality . . . is it helping identify and/or stop crime ? - I don't see any evidence of that from my perspective.[47]

[43] The Law Society Money Laundering Task Force, *Law Society response to the SARs Regime Review `Call for Information`* (2015) 4.
[44] ibid 6.
[45] Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* (2016) 3.
[46] Criminal Finances Act 2017, s11.
[47] Compliance Interview 8 dated 14/12/15.

The cumulative effect of the blanket inclusion of all criminal offences within the ambit of the Act has been to diminish the regard for the AML regime held by some members of the profession. Ultimately it has led to POCA 2002 becoming, in the view of one MLRO, `so discredited in the minds of most people that it's actually damaging the regime.`[48]

(g) `Real` versus `Technical` Laundering

One further effect of the `all crimes` approach in the Act is that many participants drew a clear distinction between what they considered to be `technical` money laundering as opposed to `real` laundering. This is reflected by the participant who referred to the Act as a `crazy piece of legislation which captures things that you would not ordinarily think of as money laundering`.[49] The breaches of these regulatory types of offence trigger notification requirements under the Act for both law firms and their clients. Participants framed `real` money laundering, in contrast, as having a genuine link to serious organised crime in some manner and posing an actual risk to the integrity of the law firm in question or economy at large.

This split between `technical` and `real` laundering is best illustrated by the participant who categorised risks into `actual and significant and real, to the wasting my time`. [50] The concern that this binary categorisation may engender in practice is that the practitioner may not perceive a particular issue as being reportable under the Act due to its technical nature, or that it may be dismissed as too inconsequential to report. This may give rise to the risk of law firms not reporting technical breaches at all. This issue of non-reporting was raised by one participant whose concern was that firms may well take the view that '"it's just ludicrous"' and went on to say:

[48] Compliance Interview 13 dated 10/03/16.
[49] Compliance Interview 14 dated 10/03/16.
[50] Compliance Interview 6 dated 08/12/15.

> . . . so then you`ve got a you know regime that is even more broken because some people are just saying "well that's stupid why would I report a lack of an asbestos survey?"[51]

(h) Non-Compliance with POCA 2002 as an AML Firm Level Risk

The reach of POCA 2002 is so great that breaches of its `technical` reporting and consent provisions may also trigger money laundering offences within law firms themselves. Law firms subject to the MLR 2017 will be required to undertake a risk assessment in respect of the money laundering threats to their business.[52] Ironically, given the whole purpose of the Act, non-compliance with the technical reporting and consent aspects of the Act was identified by some participants as a money laundering risk to their firms in its own right, separate and distinct from the more traditional external categories of jurisdictional or funding risks. Minor breaches by a law firm of customer due diligence procedures provided for under MLR 2007 (and MLR 2017) attract criminal sanctions, thus constituting a predicate offence under POCA 2002. As one participant commented in relation to POCA 2002:

> . . . it is so wide-ranging that . . . it is . . . difficult to ensure that the firm as a whole is adhering all of the time . . . to the letter of that . . . legislation.[53]

(i) POCA 2002 `Remainers`

Despite the groundswell of support for exclusions from POCA 2002, particularly amongst compliance respondents, a number of participants still welcomed the `all crimes` approach adopted in the UK. In part this was attributable to the perceived practical difficulties which would be involved in drawing a distinction between minor and more serious offences or, as one MLRO put it, distinguishing between `big, bad crime and regulatory offences`.[54] In a purely practical context, several

[51] Compliance Interview 12 dated 26/02/16.
[52] MLR 2017, reg 18(1), `A relevant person must take appropriate steps to identify and assess the risks of money laundering…to which its business is subject`.
[53] Compliance Interview 1 dated 17/11/15.
[54] Compliance Interview 15 dated 10/03/16, Transactional Interview 12 dated 01/12/15 and Transactional Interview 14 dated 01/12/15.

participants also felt that a clear cut rigour around small compliance matters fostered a broader ethos of good professional conduct within a firm.[55] The vast majority of participants who supported the `all crimes` approach of POCA 2002 were transactional participants. This predominance may be attributable to the fact that their role in the SARs regime is limited to making an internal SAR to their firm`s money laundering reporting officer. It is therefore only the compliance participants who are responsible for the submission of external SARs to the NCA in connection with technical breaches. Those SARs submitted in respect of technical matters may well be challenging to report, particularly where they require the identification of notional savings or benefits.

Some participants also felt that minor offences should not be allowed to `slip through the net` but that there should be some room for discretion in the way offences are handled thereafter.[56] As one transactional partner commented:

> I think it's better to have a wider net, and then perhaps more discretion within that net, as opposed to having a smaller net and then just hoping that those minor offences are indeed just minor offences or just regulatory trips.[57]

This instinctive desire to retain an `all crimes` approach was articulated best by the transactional partner who observed:

> . . . my sense is that the direction of travel in legislation in this space isn`t to make it easier, and I think people would rather just leave it as quite tough.[58]

(iii) How might exclusions from POCA 2002 be achieved in Practice?

Given the level of support from the legal profession for exclusions from POCA 2002, some consideration should be given as to how this could be effected in practice. Participants themselves suggested various methods by which exclusions

[55] Transactional Interview 10 dated 26/11/15, Transactional Interview 12 dated 01/12/15 and Transactional Interview 14 dated 01/12/15.
[56] Transactional Interview 20 dated 11/03/16, Compliance Interview 15 dated 10/03/16.
[57] Transactional Interview 16 dated 08/12/15.
[58] Transactional interview 2 dated 18/11/15.

could be achieved, any of which could fulfil the aim of removing minor offences and regulatory breaches from the ambit of the Act.

Several MLROs and transactional partners suggested inserting a *de minimis* threshold into POCA 2002, a proposal touched upon in the Action Plan 2016, and which could be achieved by recasting the interpretation section of the Act (s 340).[59] A *de minimis* threshold is already a familiar concept within the confines of POCA 2002. Deposit taking bodies, for example, can avail themselves of a *de minimis* defence to the substantive money laundering offences set out in ss327-9 when operating accounts below a specified threshold amount.[60] The same principles could therefore be expanded upon to cater for the legal profession.

Several compliance participants proposed excluding specified offences by reference to the length of sentence they attract, which is the approach taken in both 3MLD and 4MLD, and could also be achieved by recasting the interpretation section of the Act.[61] Despite the drafting challenges surrounding which offences should be included or excluded, expressly carving out specified offences from the Act was also proposed as a workable way forward.[62] In the alternative, and whilst acknowledging `it would be a huge task to do it`, minor criminal offences could be reclassified as civil offences.[63] This is an approach that would be effective in curtailing the notionally criminal predicate offences which trigger offences under POCA 2002.

Whilst attempts to formulate exclusions from POCA 2002 may involve administrative or legislative challenges, they are not insurmountable. As one MLRO put it, `I`m sure it would not be beyond the wit of man to produce something`.[64]

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[59] Compliance Interview 13 dated 10/03/16, Compliance Interview 8 dated 14/12/15, Transactional Interview 11 dated 26/11/15 and Transactional Interview 7 dated 25/11/15. Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* 42.

[60] POCA 2002, ss 327(2C), 328(5) and 329(2C). The current threshold is £250 (s 339A).

[61] See the definition of `serious crimes` in 3MLD, art 3(5) and the list of serious crimes within the definition of `criminal activity` in 4MLD, art 3(4). Compliance Interview 14 dated 10/03/16 and Compliance Interview 6 dated 08/12/15.

[62] Compliance Interview 6 dated 08/12/15.

[63] Compliance Interview 3 dated 25/11/15.

[64] Compliance Interview 8 dated 14/12/15.

Regardless of the mechanical route by which such exclusions could be achieved, and in contrast to many other jurisdictions, the UK has not availed itself of the opportunity to recast POCA 2002, or use other means to address its disproportionate burden upon the legal profession.

3. The Inclusion of Intent in the Substantive Money Laundering Offences

(i) The Intent Element

The lack of any intent element in the principal money laundering offences was also raised as an area of concern amongst participants in that it too imposed a disproportionate burden upon the profession. The offences set out in ss 327-9 POCA 2002 criminalise dealings with criminal property, with the *mens rea* requirement that a person `knows` or `suspects` that they are doing so. [65] As there is no requirement to demonstrate that a person actually intended to launder money, this position has fostered some disquiet amongst the legal profession in that less culpable involvement in laundering based on mere suspicion may result in a sentence of up to 14 years in prison.[66] This lack of any intent requirement is made more acute by the `all crimes` approach adopted by POCA 2002 explored earlier in this Chapter. It is of little comfort to the legal professional that, as a matter of public policy, such lengthy prison sentences are unlikely to be utilised in the absence of clear intent.[67] This approach also goes further than the strict requirements of both 3MLD and 4MLD, which require member states to criminalise money laundering acts `when committed intentionally`.[68]

This unsatisfactory position, where lawyers may become unintentionally embroiled in money laundering, has prompted the Law Society to lobby for the inclusion of

[65] Where `knowledge` means actual knowledge, and judicial guidance provides that `suspicion` means ` a possibility, which is more than fanciful, that the relevant facts exist. A vague feeling of unease would not suffice` *R v Da Silva* [2006] EWCA Crim,[2006] 4 All ER 900 [16].
[66] POCA 2002, s 334(1)(b).
[67] High profile cases such as the involvement of solicitor Mr Gohil in connection with money laundering activity connected to James Ibori are typically cases where the solicitor is complicit. See *CPS & Anor v Gohil* [2012] EWCA Civ 1550, [2013] 2 WLR 1123.
[68] 3MLD, art 1(2). Art 1(5) provides that `Knowledge, intent or purpose. . . may be inferred from objective factual circumstances.`; 4MLD, arts 1(3) and (6).

intent in the substantive offences.[69] In practical terms, the intent element sought by the Society is `the intent to avoid the legal consequences of the fact that the property has been illicitly obtained`.[70]

The majority of participants reflected the Law Society`s view and wanted to see an intent element included within the substantive offences, although several participants did acknowledge the accompanying practical difficulties surrounding proving intent.[71] The same lack of proportionality attributable to an `all crimes` approach under the Act can also been seen here, in that both inadvertent and complicit laundering are caught within the substantive offences. The objection to this lack of any distinction being drawn between inadvertent and culpable laundering is typified by the participants who stated, `I think it's pernicious and dangerous to have people criminalised when they're doing the best they can`, and that the current provisions represent `a worrying blurring between those who try, and get it wrong, and those who are willingly complicit`.[72] As an alternative proposal, several participants raised the possibility of including some manner of recklessness or negligence based test as a means of assessing liability under the Act which would have the effect of creating a more equitable regime.[73]

Inadvertent laundering in the context of a high pressure, fast paced deal was identified as a dynamic giving rise to real concern by several transactional participants, one of whom commented, `I think it's actually really easy to fall foul of money laundering regulations in the heat of the deal`. This dynamic was expanded upon by the partner who reflected:

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[69] The Law Society Money Laundering Task Force, *Law Society response to the SARs Regime Review `Call for Information`* (2015) 3. The Law Society cite the 2009 Italian tax amnesty as an illustration of the anomalies under the current legislation, whereby repatriation of untaxed property triggered s 327 and s 329 offences in respect of which reports to SOCA (the NCA predecessor) were required.

[70] ibid 3. The Law Society suggest that a list of avoidance activities should be drawn up for clarity.

[71] Compliance Interview 6 dated 08/12/15, Compliance Interview 8 dated 14/12/15, Transactional Interview 12 dated 01/12/15, Transactional Interview 12 dated 01/12/15, Transactional Interview 5 dated 25/11/15, Compliance Interview 3 dated 25/11/15.

[72] Compliance Interview 5 dated 07/12/15, Compliance Interview 6 dated 08/12/15.

[73] Compliance Interview 14 dated 10/03/16, Transactional interview 7 dated 25/11/15, Transactional Interview 16 dated 08/12/15, Transactional Interview 10 dated 26/11/15.

> . . .you're busy doing your job and yes you should be aware of what's going on around you, but sometimes you know I'm sure people just think "oh, . . . I didn't", and suddenly they get the whole force of, it`s strict liability isn't it you know, you`re dead.[74]

For the minority of participants who felt that culpability should extend beyond pure intent, this view tended to focus upon the status of the lawyer as a `sophisticated` individual.[75] Participants felt that a high standard should be expected from the profession at large. It was felt that, `the lawyer on the front line ought to be able to recognise when money is being laundered`, or as one participant colourfully put it, `if *we* can't understand what the legislative regime is then, you know, God help the rest of the population`.[76]

(ii) Consequences of the Inclusion of Intent

Including an intent requirement within the substantive offences in ss 327-9 will address the effects of the legislation on those legal professionals unwittingly drawn into money laundering scenarios. It will also have a consequential effect upon the consent regime such that law firms and their clients will no longer seek consent to effect intentional money laundering. This will reduce the number of reports made to the NCA, allowing them to divert resources elsewhere, whilst retaining the intelligence flow to the Authority via reports made under s 330 of the Act. As the Law Society state, the proposal, if adopted:

> . . . will ultimately either render the consent provisions obsolete or limit the need to apply for consent to a handful of very extreme cases.[77]

[74] Transactional Interview 4 dated 20/11/15.
[75] Transactional Interview 18 dated 16/12/15.
[76] Compliance Interview 16 dated 14/03/16; Transactional interview 9 dated 26/11/15 (emphasis added).
[77] The Law Society Money Laundering Task Force, *Law Society response to the SARs Regime Review `Call for Information`* (2015) 4. The operation of the consent regime is explored in detail in Chapter 2.

4. Criminal Sanctions and the Money Laundering Regulations 2007

(i) Removing Criminal Sanctions from MLR 2007

One further area of concern for the profession in relation to the overarching legislative regime is the inclusion of criminal sanctions within the MLR 2007. As detailed in Chapter 2, MLR 2007 stipulate an array of AML obligations, ranging from customer due diligence to training staff. Failure to comply with such requirements may attract civil penalties but also criminal sanctions of up to two year`s imprisonment.[78] As with the other aspects of the UK legislative framework examined in this Chapter, the requirement to impose criminal sanctions in respect of such breaches goes further than the strict requirements of 3MLD or 4MLD.[79]

The Law Society argue that such penalties should be removed on the basis that they are disproportionate and serve to distort the aspirational risk-based approach of the regime.[80] This lack of proportionality arises due to the interplay between the Regulations and POCA 2002 explored earlier in the chapter, whereby a single inadvertent breach of the Regulations may result in a notional saving representing `criminal property` under the Act, thus triggering a substantive money laundering offence. The Society dismiss as an irrelevance the fact that such offences may not be prosecuted as a matter of public policy, stating:

[78] MLR 2007 reg 45. See also reg 42 in relation to civil offences. The SRA do not have the power to impose civil penalties under MLR 2007, but a breach of the regulations will trigger a breach of the SRA Code of Conduct, enabling the SRA to apply a range of penalties, see SRA, *SRA Code of Conduct 2011* (Version 18, 2016), Outcome 7.5.
[79] 3MLD, art 39(2); see also 4MLD, art 58(2).
[80] The Law Society also argue that the inclusion of criminal sanctions in the regulations does not accord with the `Hampton Principles` ie that a more risk-based approach to regulation should be adopted, as advocated by the Hampton Report see Philip Hampton, *The Hampton Report* (HM Treasury 2005).See The Law Society, *Response to the HM Treasury Consultation on the Money Laundering Regulations 2007* (2011), 4-8.

> The simple fact is that these legitimate businesses are facing the same criminal sanctions and reporting consequences as if they were a drug dealer, fraudster or human trafficker. [81]

Consequently, the Law Society state, `most` regulated persons are not making SARs in respect of breaches of the MLR 2007.[82]

The distortion of the risk-based approach is said to arise from the fact that a defence is only available where a person `took all reasonable steps and exercised all due diligence to avoid committing the offence`, a position which the Society perceive as inconsistent with adopting a truly risk-based approach.[83]

(ii) Retention of Criminal Sanctions in MLR 2007

In contrast to the view of the Law Society, there was a strong body of support voiced by many participants for the retention of criminal sanctions under the Regulations, with many others ambivalent on the matter. The rationale informing support for the retention of criminal sanctions stemmed largely from the belief that such sanctions constitute a more persuasive tool ensuring AML compliance than other, weaker penalties. Hence one compliance participant observed that:

> . . . it is in many ways one of the few sticks that MLRO have to scare and motivate people to take it seriously.[84]

As another participant phrased it, `if it was just something that was nice to do you can see why people wouldn't want to be bothered about it`.[85] Several participants expanded on this view, noting that money laundering was a serious issue and therefore deserved serious sanctions in response.

Several participants remained unperturbed by the threat of criminal sanctions on the basis that they were trying their best to be AML compliant in any event – as

[81] The Law Society, *Response to the HM Treasury Consultation on the Money Laundering Regulations 2007* (2011) 6.
[82] ibid 6.
[83] MLR 2007, reg 45(4), The Law Society, *Response to the HM Treasury Consultation on the Money Laundering Regulations 2007* (2011) 6.
[84] Compliance Interview 6 dated 08/12/15
[85] Compliance Interview 2 dated 24/11/15.

one MLRO said with regard to the criminal sanctions, ` you know it`s there, you just trust that if you do a decent job it`s never going to be an issue for you`.[86] The retention of criminal sanctions was even vigorously defended by the transactional partner who emphasised that:

> . . . a direction of travel where we`re effectively saying we need to dilute or water down various regulations seems to me to potentially deliver the wrong message.[87]

Fewer participants felt that the criminal sanctions should be removed from the Regulations. Of those that did, several felt that the criminal sanctions were disproportionate, either because they criminalised what amounted to administrative failings or had the effect of `putting criminal liability on individuals who are not ordinarily criminals`.[88] A number of alternative sanctions were suggested by these participants such as regulatory censure, civil penalties and fines.

(iii) Do Criminal Sanctions make lawyers more cautious more generally?

The specific issue of whether criminal sanctions should be removed from the Regulations fed into a broader consideration as to whether criminal sanctions under the regime as a whole, ie under POCA 2002 as well as the Regulations, made lawyers more cautious in practice. The majority of participants felt that the presence of criminal sanctions did make lawyers more cautious in their day to day dealings. Whilst many participants did not elaborate further, those that did felt that criminal sanctions acted as a deterrent or focused the mind on AML compliance. As one partner reflected, ` anything that can come and touch you personally in that way I think would make you be a little bit more cautious`, a sentiment echoed by the participant who stated `I think a regime which says actually you could end up in prison over this if you're not careful, it's always going to be a good deterrent.`[89]

[86] Compliance Interview 17 dated 08/04/16.
[87] Transactional interview 19 dated 10/03/16.
[88] Compliance Interview 14 dated 10/03/16.
[89] Transactional interview 13 dated 01/12/15, Transactional interview dated 16/12/15.

Several participants did note however that the criminal sanctions under the regime were rarely deployed in practice, a perception that will be revisited in Chapter 7.

Several participants also raised the spectre of sanction by the SDT or their law firms as being a compelling driver of AML compliance, as was the case with the participant who stated:

> I think perhaps the thing that makes a lawyer the most cautious if I`m perfectly honest is the . . . possibility that either he's thrown out of his partnership or that he's struck off because either way he ceases to be able to earn a living from that which he does.[90]

5. Conclusion

The effect of the `all crimes` approach of POCA 2002, and the lack of any intent requirement in the substantive money laundering offences, imposes a disproportionate burden upon the legal profession. Consequently, each proposed change to the Act raised by participants reflects an underlying desire to address and redress that disproportionate burden.

The regime creates needless administrative burden for law firms in relation to `technical` SARs, with minor infractions also capable of forcing disproportionate transactional interruption. Practical consequences aside, the breadth of POCA 2002 has led to a number of participants perceiving the regime to be either discredited or broken, on the basis that it treats serious crime and nominally criminal offences in the same way. More troubling still is the fact that making technical SARs of questionable intelligence value serves to divert law firm resources away from those areas that present a `real` risk of money laundering, thus detracting from the effectiveness of the regime still further.

The operation of the UK AML regime has led to the compartmentalisation of `real` and `technical` laundering in the minds of many participants. This may have a negative impact on compliance with the regime in that technical offences may remain unreported simply because they are not identified as reportable by the

[90] Transactional Interview 9 dated 26/11/15.

legal professional in question or considered too inconsequential to report. The failure to identify and report matters which are technically reportable under the Act has a further negative effect on the regime overall.

Many granular level amendments have been made to the UK`s AML regime during the 4MLD transposition process in an attempt to further embed a risk-based approach. Set against this backdrop, the failure to carve out technical offences during the transposition process represents a wasted opportunity to add in proportionality to the regime. Minor offences and regulatory breaches could and should have been excluded from the ambit of POCA 2002.

Exclusions from POCA 2002 could be achieved using any of the pathways put forward by participants. Such pathways include inserting a *de minimis* threshold into the Act or recasting the definition of `criminal property` according to length of sentence. Simply recasting the current definition of `criminal property` within the Act would be an elegant way of achieving exclusions. Alternatively, specified criminal offences could be reclassified as civil offences or expressly excluded from the ambit of POCA 2002. These latter options would be far more labour intensive, however, and present significant drafting challenges.

Similarly, the desire on the part of participants for the inclusion of an intent element with regard to the substantive money laundering offences is a desire to address the disproportionate effect of the Act. As currently drafted under POCA 2002, inadvertent laundering by a legal professional falls within the scope of the substantive money laundering offences in the same way as complicit laundering. The inclusion of an intent requirement would address this lack of proportionality. Such inclusion would also curtail the number of SARs made under the consent regime on the basis that lawyers would not, other than *in extremis* be seeking consent for intentional laundering.

One of the surprising findings with regard to the overarching AML legislation however, was that there was a strong body of support from participants for the retention of criminal sanctions under the MLR 2007 (and by extension, MLR 2017). This sits in contrast to the position held by the Law Society, which has lobbied

repeatedly for their exclusion. The rationale behind this support flowed out of a belief that criminal sanctions operate as an effective AML compliance tool, necessary to address the societal ill that is money laundering, and unlikely to concern professionals who were trying their best to comply with the regime.

The expansive approach adopted by POCA 2002 may not be too surprising however, given the UK`s previous history of `gold-plating` previous EU AML directives transposed into UK law, or as one participant colourfully put it, `we do extra jam on top and lashings of extra sort of "to be sure, to be sure" type stuff`.[91] The retention of an `all crimes` approach, together with the lack of any intent element in the substantive offences, may have much to do with what can be expressed as the AML `zeitgeist`. Recent years have seen an increased spotlight on money laundering in preparation for the FATF evaluation of the UK in 2018, coupled with numerous pledges to tackle money laundering on the part of a panoply of high profile figures.[92] In the midst of such scrutiny the UK published its first National Risk Assessment in 2015 (NRA 2015), which identified the legal sector as a `high` risk in terms of money laundering, a rating vehemently contested by the profession.[93] This combination of factors alone may well have extinguished any political will to be seen to relax the AML regime in relation to the legal profession, particularly in light of the sector`s rating in the NRA 2015.

The UK`s unwavering devotion to an `all crimes` approach and the lack of any intent element in the substantive money laundering offences may also be influenced by political considerations at a supra-national level. It may be recalled that the UK could elect to move away from an `all crimes` approach and insert an

[91] Transactional Interview 4 dated 20/11/15.

[92] See for example, Patrick Wintour and Heather Stewart, `David Cameron to introduce new corporate money-laundering offence` *The Guardian* (London, 12 May 2016) < https://www.theguardian.com/politics/2016/may/11/david-cameron-corporate-money-laundering-offence-anti-corruption-summit> accessed 5 April 2017.

[93] HM Treasury and Home Office, *UK national risk assessment of money laundering and terrorist financing* (2015) 12. For the Law Society response, see, `Intelligence shortcomings render anti-money laundering report findings misleading, warns legal sector ` (*The Law Society,* 15 October 2015) < http://www.lawsociety.org.uk/news/press-releases/intelligence-shortcomings-render-anti-money-laundering-report-findings-misleading-warns-legal-sector/> accessed 21 November 2016.

intent element within the substantive offences whilst still complying with 3MLD, 4MLD and the overarching FATF Recommendations 2012 which sit behind them.[94] Yet the effect of Brexit is that the UK will stand alone in many respects from 2019 onwards, requiring it to seek out strong partnerships and forge new alliances wherever possible. It enters this new arena tainted somewhat by a widely held perception that has gained traction in recent years: that the UK is, despite its ornate and elaborate regulatory regime, the money laundering capital of the world.[95] If the NRA 2015 was the flesh wound, Brexit may therefore prove to be the fatal blow in terms of any political will to remove technical offences from, or include an intent element within, the provisions of POCA 2002.[96] The legal profession, therefore, looks set to remain overburdened by an AML regime which is entirely disproportionate in terms of the money laundering risks it is trying to address.

Having explored the issues encountered by participants with regard to the overarching AML legislative regime within which the profession operates, the subsequent data chapter examines the mechanical aspects of the AML regime relating to CDD, AML training and the operation of the client account.

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[94] 3MLD, art 1; 4MLD, art 1; FATF, *International Standards on Combating Money Laundering and the Financing of Terrorism and Proliferation -The FATF Recommendations* (2012, updated June 2017) Interpretive note to recommendation 3, para 7(a).

[95] The Government recognises that the UK is `unusually exposed to international money laundering risks`, see Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* (2016) 7. Press reports abound to the effect that the UK, and London in particular, is the money laundering capital of the world. See James Hanning and David Connet, `London is now the global money laundering centre for the drugs trade, says crime expert` *The Independent* (London, 4 July 2015)<http://www.independent.co.uk/news/uk/crime/london-is-now-the-global-money-laundering-centre-for-the-drug-trade-says-crime-expert-10366262.html > accessed 1 July 2017. Transparency International UK has also raised concerns with regard to money laundering via the UK. See for example, Transparency International UK*, Corruption in the UK: Overview and Policy Recommendations* (2011).

[96] Some commentators suggest that the UK may elect to move away from its AML `gold standard` in an attempt to attract business to its shores post-Brexit, see Bill Tupman,`Editorial` (2017) 20(2) JMLC 102.

Chapter 5 - The Mechanical Aspects of the UK AML Regime

1. Introduction - Customer Due Diligence (CDD)

The MLR 2007 act as the companion piece to POCA 2002 and require law firms to comply with an array of AML obligations surrounding, inter alia, CDD, training and record keeping. It is to these mechanical aspects of the regime that this thesis now turns, focusing on the compliance issues that participants face upon client inception, and when dealing with their clients on a day to day basis. In line with an empirical thesis of this nature, this Chapter and the ensuing chapters do not attempt to draw out the provisions of every single regulation that law firms in the regulated sector are required to comply with. Rather, the material covered in these chapters reflects those key concerns raised by the participants themselves in the context of large, typically international, commercial law firms.

This Chapter will explore a number of issues raised by participants relating to: (1) CDD, (2) Beneficial Ownership, (3) Simplified Due Diligence, (4) Politically Exposed Persons (PEPs), (5) Source of Funds, (6) Source of Wealth, (7) Reliance, (8) Ongoing Monitoring, and (9) AML training. The Chapter will conclude by considering the operation of the client account by a law firm, together with the AML issues that such accounts present. As many disparate aspects of the regime are considered in this Chapter, concluding comments will be provided immediately following each topic under consideration, with a summary provided at the end of the Chapter.

Prior to exploring the discrete CDD issues referred to in this Chapter, it is worth situating these obligations within the overarching CDD context. MLR 2007 set out the CDD requirements that a law firm in the regulated sector must apply to its clients. Whilst the details of CDD were explored fully in Chapter 2, the starting point for CDD bears repeating here: under Regulation 5, a law firm must identify and verify the identity of their clients, using information from a `reliable and independent source.` Furthermore, any beneficial ownership of a client must be identified and `adequate measures` taken:

on a risk-sensitive basis, to verify his identity so that the relevant person is satisfied that he knows who the beneficial owner is.[1]

This requirement is the central tenet of CDD, and many of the obligations discussed in this Chapter flow from that overarching requirement. A number of provisions are then included to address those issues relating to particular client groups, of which PEPs are an example.

Many participant firms had an international, if not global, presence, and this had an impact on CDD in a number of ways. First, the CDD challenges such firms faced frequently involved jurisdictional or cultural issues which other types of law firms may not encounter in the usual course of their business. Many of these issues are drawn out within this Chapter. Secondly, such global law firms are also required to comply with an array of AML regimes across multiple jurisdictions, some of which, such as Qatar, Dubai and Oman for example, operate more draconian regimes than the UK. A number of participants reported that unless the requirements in other jurisdictions were more stringent, their firms applied UK CDD standards on a global basis, even where such standards were more stringent than local laws.

One of the most challenging and prominent compliance issues raised by participants related to the CDD requirements on beneficial ownership and it is to these provisions that this Chapter now turns.

2. Beneficial Ownership

Beneficial ownership transparency requirements have been implemented in the UK with the express intention to `deter and prevent the misuse of corporate vehicles`.[2] Consequently, Regulation 6 MLR 2007 sets out a series of detailed definitions of beneficial ownership applicable to a variety of corporate or trust structures. With regard to a client that is an unlisted company for example, a law firm must identify the ultimate beneficial owner(s) of over 25% of the shares or voting rights in that company, or alternatively (for all companies) any individual who `otherwise`

[1] MLR 2007, reg 5(b).
[2] FATF, *FATF Guidance: Transparency and Beneficial Ownership* (2014) 3.

exercises management control.[3] Similar, albeit adapted, provisions apply to partnerships, trust structures and other legal arrangements.[4] For UK unlisted companies, the starting point for establishing beneficial ownership typically involves the law firm obtaining a company search at Companies House, which is limited to revealing the purely legal ownership of shares.

In a move towards greater transparency with regard to beneficial ownership and to `support law enforcement agencies in money laundering investigations`, the Persons with Significant Control Register (PSC Register) was implemented in the UK in April 2016.[5] The Register is designed to build on the information that was previously required to be submitted to Companies House. It necessitates the submission of information with regard to share ownership and voting rights above a 25% threshold, the right to appoint or remove directors, and details of those individuals who do or may exercise significant influence or control over the company.[6] Whilst the interviews were conducted prior to the implementation of the PSC Register at Companies House, and a number of its key features were yet to be finalised, interviewees were nevertheless asked to consider the potential impact of the PSC Register on their day to day practice. The interviews also took place prior to the consultation on proposals to introduce a beneficial ownership register of those overseas entities owning property in the UK, or involved in UK government procurement (Overseas Entity Beneficial Ownership Register).[7] Therefore its provisions were not considered by participants.

[3] MLR 2007, regs 6(1)(a) and (b).
[4] ibid reg 6(2)(ff).
[5] Companies House, *PSC Register Summary Guidance* (2016) 1. See pt 21A (as amended by the Small Business, Enterprise and Employment Act 2015). The PSC Register went live at Companies House on 30 June 2016; see also Register of People with Significant Control Regulations 2016, SI 2016/339; The European Public Limited Liability Company (Register of People with Significant Control) Regulations 2016, SI 2016/375; and The Limited Liability Partnerships (Register of People with Significant Control) Regulations 2016, SI 2016/340.
[6] Companies House, *Company Statutory Guidance for the PSC Register* (2016).
[7] Department for Business, Energy & Industrial Strategy, *A Register of Beneficial Owners of Overseas Companies and Other Legal Entities: Call for Evidence on a register showing who owns and controls overseas legal entities that own UK property or participate in UK government procurement* (April 2017).

(i) Beneficial Ownership – The Practical Challenges

Described as the `single most difficult aspect` of the UK AML regime, beneficial ownership requirements presented a `huge number` of issues for participants.[8] As one participant stated, `Is it difficult? - yes. Is it time-consuming? - absolutely.`[9] Complying with UK beneficial ownership requirements is resource intensive for law firms in every sense. As one compliance participant recounted:

> We spend a lot of money and time trying to get beneficial ownership information, it's what takes the most time for us.[10]

As all participant firms were large commercial law firms, their client base was predominantly corporate in nature. Yet the beneficial ownership challenges do not lie with listed companies, as confirmed by the transactional partner who said, `if the ownership is simple, like it's a listed company, it's dead easy.`[11] Nor do they lie with EU private companies on the basis that:

> . . . in jurisdictions like the UK where there's a lot of shareholder information available on corporates, those are not difficult.[12]

Rather, beneficial ownership issues arose in relation to two features: (a) the involvement of clients in non-EU jurisdictions, and (ii) in respect of certain types of clients: namely trusts and private equity clients. Each of these features will now be explored.

(a) Beneficial Ownership Challenges in Non-EU Jurisdictions

The majority of participant firms had an international practice and therefore there was a general acknowledgment that, `any firm with an international practice or with international clients is going to have issues around beneficial ownership.`[13] The majority of participants also stated that complying with beneficial ownership

[8] Compliance Interview 2 dated 24/11/15; Compliance Interview 9 dated 15/12/15.
[9] Compliance Interview 12 dated 26/02/16.
[10] Compliance Interview 2 dated 24/11/15.
[11] Transactional Interview 8 dated 26/11/15.
[12] Compliance Interview 5 dated 07/12/15.
[13] Compliance Interview 9 dated 15/12/15.

requirements in non-EU and/or offshore jurisdictions was challenging. Those issues stem from a blend of both legislative and cultural differences.

In terms of global AML legislation, many non-EU and offshore jurisdictions do not impose comparable beneficial ownership disclosure requirements.[14] Therefore, according to one participant, `it can be a challenge because there are countries that don't really ask people to understand who the beneficial owners are.` [15] This was echoed by the interviewee who reported, `we have significant issues in certain jurisdictions where there is no requirement to record that information.`[16] Consequently, law firms will need to rely on their own clients and their advisors to obtain such information. This challenge is exacerbated where there are holding company and subsidiary groups in place forming `extremely ornate global structures`, or as one transactional partner recounted, `when you've got convoluted holding structures which are set up for tax purposes.`[17]

In addition to the practical difficulties presented by the lack of easily available on-line information, the lack of comparable filing obligations in non-EU jurisdictions may also lead to what one participant described as a more generalised, ` lack of understanding as to why you are even asking the question` with regard to beneficial ownership.[18] This lack of understanding serves to exacerbate the difficulties participant firms face in obtaining the requisite beneficial ownership information. These challenges may also be more acute in jurisdictions, such as the Middle East, less familiar with the EU AML regime, and where there may be more cultural sensitivity to the disclosure of such information.[19]

[14] BVI or Cayman Islands for example.
[15] Compliance Interview 14 dated 10/03/16.
[16] Compliance Interview 18 dated 08/04/16.
[17] Transactional Interview 2 dated 18/11/15 and 20 dated 11/03/16.
[18] Compliance Interview 1 dated 17/11/15.
[19] Compliance Interview 9 dated 15/12/15.

(b) Beneficial Ownership Challenges Relating to Trusts and Private Equity Funds

In addition to jurisdictional challenges, certain client groups present further beneficial ownership challenges: namely trusts and private equity funds.

(i) Trusts

It may be difficult to establish beneficial entitlement to trusts, particularly with regard to family trusts which may be `secretive` by their very nature.[20] As one MLRO noted:

> . . . if you're talking about complex trust structures, there is reluctance by clients to actually disclose who the beneficial owner is . . . sometimes it takes quite a lot of pushing to actually ascertain who the owner is at the end of the day.[21]

Whilst it may be difficult to establish the beneficial ownership of trust structures in any event, adding in an offshore element provides an additional layer of complexity such that, `it is harder to find the answers` to beneficial ownership questions.[22] This prompted one participant to determine in relation to CDD that, `the *most* difficult aspect is when you've got an overseas trust.`[23] When faced with the prospect of an offshore trust, one participant recollected:

> if [the client is] saying "oh it's a Cayman Islands trust" you just groan, because you just know that it's going to take quite a lot of work to get that done.[24]

Such structures represent the pinnacle of CDD difficulty for law firms, `where it's opaque and you just can't get the information.`[25]

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[20] Compliance Interview 2 dated 24/11/15.
[21] Compliance Interview 20 dated 16/06/16.
[22] Transactional Interview 13 dated 01/12/15.
[23] Transactional Interview 12 dated 01/12/15 (emphasis added).
[24] Transactional Interview 8 dated 26/11/15 (words in brackets added).
[25] Transactional Interview 8 dated 26/11/15.

(ii) Private Equity Funds

Participants also reported challenges surrounding the beneficial ownership requirements for private equity fund clients, attributable to the disparate shareholder base involved. As one transactional participant stated, `the funds structures are . . . the ones where you really have to drill down.`[26] This challenge was highlighted by the transactional partner who noted:

> . . . it`s more complicated, the time when I sort of find it a bit of a burden is when I act for a joint venture and there's say, you know, 20 people investing and they`ve, some of them you know, they`ve all got a stake.[27]

The beneficial ownership resource requirements in relation to such clients on a transaction may be acute. Indeed, it prompted one transactional partner to comment that CDD can be `a job in itself on a transaction.`[28]

The importance of obtaining beneficial ownership details was highlighted in a number of interviews, and several participants reported declining to act for clients where beneficial ownership information was not forthcoming. As one transactional partner summarised:

> . . . it tends to be binary, so either they say `I'm not going to tell you`, and I say `thanks very much, I'm not going to act`, which has happened a couple of times or, I say `this is what I need to know` and they go `oh, okay`.[29]

Several participants also reported what can be deemed as a an evolving `sophistication in the market`: an understanding on the part of clients that provision of beneficial ownership information is, `a necessity of being able to do business` in this jurisdiction.[30] This development in the maturity of the regime has made it easier for law firms to obtain the requisite information required under the

[26] Transactional Interview 7 dated 25/11/15.
[27] Transactional Interview 18 dated 16/12/15.
[28] Transactional Interview 4 dated 20/11/15.
[29] Transactional Interview 1 dated 18/11/15.
[30] Transactional Interview 6 dated 25/11/15.

UK AML regime, which has the effect of streamlining the CDD process to a certain extent.

(c) The Prohibitive Costs of Beneficial Ownership Requirements

Inevitably, there are costs implications for law firms collateral to the client demographics outlined above. This was highlighted by the transactional partner who stated in relation to a transaction involving a client with a disparate shareholding base, `I think it's nothing short of a nightmare in terms of my time.`[31] Several participants reported that the costs of establishing beneficial ownership in some non-EU jurisdictions or for certain types of client were so prohibitive that the law firm may well decline to act for such clients. This stance is reflected by the transactional partner who stated:

> . . . some of the really complex tax driven offshore structure clients, it's all right if you're going to have a long happy relationship, on a one-off it's just not worth it sometimes so we would actively push them away.[32]

(d) The Beneficial Ownership Threshold of 25% and the Importance of `Control`

Participants were asked to reflect on whether the 25% threshold for shareholding or voting rights was appropriate for the UK beneficial ownership disclosure requirements. EU proposals to amend 4MLD, which were published following the interviews and are yet to be implemented as at September 2017, may require this threshold to drop to 10% in respect of high risk entities.[33] A few participants felt that the threshold requirement under MLR 2007 could be lowered expressly in the legislation, although one other participant firm reported that, `we go lower than

[31] Transactional Interview 4 dated 20/11/15.
[32] Transactional Interview 14 dated 01/12/15.
[33] Proposal for a Directive of the European Parliament and of the Council amending Directive 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing and amending Directive 2009/101/EC.

the threshold sometimes as an enhanced measure, particularly in offshore jurisdictions.'[34] Only a few participants felt the threshold should be raised.[35]

The majority of participants had no view, were ambivalent, or found the threshold satisfactory. The reason behind such ambivalence may be influenced by the view, vocalised by a number of participants, that beneficial ownership issues lie not in any threshold percentage, but rather in the level of control exercised over an entity. As one compliance participant explained:

> I think you could put any figure on it and actually if somebody wants to control a company they can, and still keep their ownership apparent at a certain percentage.[36]

Identifying beneficial ownership purely in shareholding terms may not reveal who is actually controlling that company, and this aspect of the regime was drawn out by the participant who reflected:

> . . . sometimes you can track through multiple layers of companies, just to find somebody who has . . . got absolutely nothing to do really with the running of the company.[37]

This tension between a shareholding percentage and control of a company was also drawn out by the participant who formed the view:

> . . . so the 25% - yes, I think it gives you a flavour of who's in charge, but you do have to think about on a day-to-day basis who is really pulling the strings in this organisation.[38]

Several participants observed that any dedicated money launderer will simply phish under any beneficial ownership threshold that is put in place. This particular

[34] Compliance Interview 2 dated 24/11/15.
[35] Compliance interview 4 dated 03/12/15;Transactional Interview 12 dated 01/12/15.
[36] Compliance Interview 18 dated 08/04/16.
[37] Compliance Interview 1 dated 17/11/15.
[38] Compliance Interview 14 dated 10/03/16.

loophole prompted one participant to state, `I think the 25% threshold is entirely meaningless.`[39] Another Deputy MLRO explored this feature of the regime more fully as follows:

> I think whatever threshold you have, it's very easy to game – so we`ve seen in Cyprus, in you know all of those, the `usual suspects` regimes, you just have beneficial ownership, corporate beneficial ownership of 20% - and you just have five of them and then they go up to another set and then that`s it, your due diligence obligations as a practice stop.[40]

(ii) **Persons of Significant Control Register**

Flowing on from a consideration of the beneficial ownership thresholds, participants were asked for their views on the PSC Register, outlined at the start of this Chapter, which was yet to be fully implemented at the time of the interviews. Many participants felt that the PSC Register would proffer some benefits, although many participants also expressed their reservations. As one Deputy MLRO noted, `it will make it easier, but is it a panacea? – no, it`s definitely not.`[41] The PSC Register will undoubtedly assist law firms in fulfilling their beneficial ownership obligations in respect of UK entities: comparable registers will also exist across EU nations, although these may not contain publicly available information. The register will not assist, however, in respect of those non-EU jurisdictions which pose the greatest compliance challenge for law firms operating an international practice. As one Deputy MLRO noted, reflecting on their firm`s client demographics, the PSC Register would probably make, `not a huge amount of difference based on the profile of who we act for.`[42] As at September 2017, the form of the Overseas Entity Beneficial Ownership Register (OEBO Register) was yet to be determined and so it is not possible to make any meaningful assessment of its provisions.

[39] Compliance Interview 5 dated 07/12/15.
[40] Compliance Interview 9 dated 15/12/15.
[41] Compliance Interview 9 dated 15/12/15.
[42] Compliance Interview 11 dated 19/02/16.

(iii) Vulnerabilities in the UK Beneficial Ownership Requirements

Participants raised a number of issues in relation to the UK`s beneficial ownership provisions, ranging from the benign and practical, to the complicit and illicit. Such vulnerabilities are explored below.

(a) Beneficial Ownership Changes Constantly

The ownership of business organisations and the identity of trust beneficiaries are constantly evolving and shifting for entirely legitimate reasons. What this moveable feast means for the practitioner however, is that any beneficial ownership register, from whatever source, may become outdated, potentially on a daily basis. This feature was highlighted by the MLRO who said:

> . . . beneficial ownership can vary from day-to-day and so you know even with pukka blue-chip clients, very reliable clients you, you can't say to them `well every time there's a change in the beneficial ownership you've got to notify us`.[43]

Ultimately therefore, the same MLRO continued:

> . . . the extent to which you can actually reach baseline and say `right, I`m there, I've got it, it's objectively proved` is very difficult.[44]

Article 30 of 4MLD requires that `current` company beneficial ownership information should be held on a central register, and in the UK any changes must be notified to Companies House within 14 days.[45] Trusts are treated slightly differently, however, and from the summer of 2017 HMRC will operate a central register of those express trusts with tax consequences. These are not publicly available registers however, and so the CDD challenge for law firms with regard to

[43] Compliance Interview 15 dated 10/03/16.
[44] Compliance Interview 15 dated 10/03/16.
[45] Companies House, `Changes to UK anti-money laundering measures` (*Companies House,* 19 April 2017) < https://www.gov.uk/government/news/changes-to-uk-anti-money-laundering-measures> accessed 12 September 2017.

UK trusts, and trusts in foreign jurisdictions, continues unabated.[46] Proposals to amend 4MLD, yet to be finalised as at September 2017, may require that beneficial ownership information on all `business-related` trusts is made available to the public, which may assist law firms when conducting CDD, with information on all other trusts restricted to those with a legitimate interest.[47]

(b) Complicit Launderers Will Make False Declarations on the PSC Register

With regard to the PSC Register, the position is such that, `if you are on the right side of the law you are going to do your best to comply with it`, thus providing a detailed and accurate picture of beneficial ownership and control.[48] The complicit launderer, in contrast, will inevitably make false declarations with regard to the PSC Register so as to falsify the extent of their control of the company, or indeed, obscure their involvement altogether. This facet, whilst not unique to the PSC Register, was outlined by the compliance participant who stated:

> The bad guys, the actual crooks, well what are they going to do?, they're going to say "okay well there`s this register, but guess what, nobody's actually checking the information that I'm supplying, so I can pretty much write anything on it, so that's what I'm going to do and see if I can get away with it".[49]

(c) **Company Formation**

Some participants highlighted the fact that there was a lack of scrutiny with regard to beneficial ownership at the company formation stage, either by Companies House or by trust or company service providers (TCSPs), a scenario which was described by one participant as a `hole in the regulations`.[50] That participant went

[46] See 4MLD, art 31. Details of such express trusts will only be available to law enforcement agencies and the NCA, see HM Treasury, *Money laundering Regulations 2017: consultation* (2017) para 9.2.
[47] Proposal for a Directive of the European Parliament and of the Council amending Directive 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing and amending Directive 2009/101/EC.
[48] Compliance Interview 14 dated 10/03/16.
[49] Compliance Interview 14 dated 10/03/16.
[50] Compliance Interview 6 dated 08/12/15.

on to elaborate further with regard to TCSPs and the CDD threshold in place under MLR 2007:

> . . . if they consider it's a one off transaction under 10,000, there's no obligation for a company service provider to carry out client due diligence – and they would argue that`s wholly appropriate because neither does Companies House which does effectively the same thing, but I think that is where there is a big hole because unless you do it upfront or at the very beginning, you`re always playing catch-up.[51]

Under MLR 2017, company formation has now been reclassified as a `business relationship` and therefore CDD must be conducted on company formation by TCSPs.[52] The position remains however, that Companies House does not verify the information submitted to it on company formation, so to a certain extent, this issue also remains current. This remains the position as it is the government`s view that, due to the public nature of the information held by Companies House, such information `can be policed on a significant scale by a variety of users.`[53]

(d) Lack of Transparency

A number of participants felt that the lack of transparency over corporate and trust structures on a global basis undermines the entire UK AML regime. One of several mechanisms by which such opacity can be achieved is by the use of nominee beneficial owners. Whilst the use of nominees may be used entirely legitimately, one such example being where a stockbroker holds listed securities as a nominee on behalf of their customers, their use is also open to abuse.[54] The misuse of nominee beneficial ownership provisions was a feature highlighted by the compliance participant who concluded:

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[51] Compliance Interview 6 dated 08/12/15.
[52] MLR 2017, reg 4(2).
[53] HM Treasury, *Money Laundering Regulations 2017: consultation* (2017) para 9.1.
[54] E van der Does de Willebois, E Halter, R Harrison, J Won Park and J Sharman, *The Puppet Masters How the Corrupt Use Legal Structures to Hide Stolen Assets and What to Do About It* (The World Bank and UNODC 2011) 59. See also, FATF, *FATF Guidance: Transparency and Beneficial Ownership* (2014) 3.

> . . . until you can actually stop situations where you have nominee beneficial owners, and there are some countries that advertise this, you know to bring in business saying `well it's great because our country offers nominee beneficial owners as an option` . . . you're basically not really going to achieve the purpose.[55]

There are, in fact, a number of UK providers offering this service, although some of these providers make it clear that they operate within the parameters of the PSC Register. A beneficial owner could potentially achieve complete opacity even in the UK therefore by appointing a nominee beneficial owner and restricting their shareholding to a holding under 25%, whilst failing to declare any other forms of control over the company. Banning nominee beneficial ownership holdings, however, will not deter the truly committed launderer. As one transactional partner pondered, ` I may well say I'm the beneficial owner, but I may have declared a trust which I haven't told anybody about.`[56]

The heart of the beneficial ownership challenge is the opacity of trust and corporate structures in non-EU jurisdictions which do not have comparable disclosure obligations. This on the basis that:

> . . . if you are an actual money launderer and you're not unbelievably stupid then you will put in place a halfway convincing structure.[57]

The position is best summarised by the Deputy MLRO who concluded:

> If developed countries or all countries who signed up to FATF were serious about tackling money laundering, they would prevent these non-transparent ownership structures you know and areas like Cyprus and the BVI, Mauritius and you know the Netherland Antilles would all . . . need to have, you know, full disclosure of their information.[58]

[55] Compliance Interview 14 dated 10/03/16.
[56] Transactional Interview 7 dated 25/11/15.
[57] Compliance Interview 9 dated 15/12/15.
[58] Compliance Interview 9 dated 15/12/15.

(iv) Concluding Comments on Beneficial Ownership

Establishing the beneficial ownership of their clients is undoubtedly costly, time consuming and challenging for participants, particularly in relation to those jurisdictions that do not have comparable disclosure obligations in place. Dedicated money launderers will always try and circumvent any AML regulatory system in place, or simply fail to declare their ownership interests in an act of pure deceit. Nor will the inevitable and frequent changes in ownership interests that form part of a legitimate business economy cease to be effected, meaning that any beneficial ownership register will almost immediately be out of date.

The majority of participants had no view, were ambivalent, or found the 25% beneficial ownership threshold satisfactory. The reason behind such ambivalence may be influenced by the view, vocalised by a number of participants, that beneficial ownership issues lie not in any threshold percentage, but rather in the level of control exercised over an entity. This finding suggests that the proposed amendment to 4MLD lowering the beneficial ownership threshold to 10% in respect of high risk entities, such as holding company structures, is of some, albeit limited, utility.[59]

There are a number of issues that need to be addressed in order to enhance the transparency that the beneficial ownership requirements were set up to achieve. One is dispensing with nominee shareholdings altogether, with the limited exception of those trading in listed securities or other narrowly defined categories. This would serve to swing the transparency pendulum in favour of a legitimate economy as existing nominee shareholding arrangements are able to achieve opacity at a stroke.

[59] Proposal for a Directive of the European Parliament and of the Council amending Directive 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing and amending Directive 2009/101/EC, art 1(2). The proposal targets `entities that function as intermediary structures, do not create income on their own, but mostly channel income from other sources (defined as *Passive Non-Financial Entities* under Directive 2011/16/EU).`,para 5(f)(i).

The other response required is an increased global move towards transparency in other non-EU jurisdictions. Under the current AML regime, the incorporation of a holding company in an opaque jurisdiction may defeat the aim of the beneficial ownership requirements. This hampers the efficacy of the UK AML regime, although it may also have the effect of driving potential launderers away from the UK and EU to other jurisdictions. Since the establishment of FATF, there has been an increased global focus on tackling money laundering: indeed FATF is itself a *global* AML standard setting body. Central beneficial ownership registers are currently in place across the EU as a result of the transposition of 4MLD, albeit with differing levels of access. Furthermore, the EU proposals to amend 4MLD mandate greater levels of interconnectedness between centralised registers across member states.[60]

It may well be possible in years to come therefore, to implement a global register of beneficial ownership interests in relation to those nations implementing FATF recommendations. This is the route contemplated by the compliance participant whose view was that, `if you could get a proper register globally you know well that would be really helpful but you, it'll be years before you get that.`[61] What may seem unworkable at present however, may well become a workable solution in the decades to come.

3. Simplified Due Diligence

Under Regulation 13 MLR 2007, law firms are not required to conduct CDD in respect of certain restricted categories of entities or products considered to represent a low risk of money laundering, a feature of the regulations known as simplified due diligence (SDD). Some of these categories are self-explanatory: for example SDD will apply where the client is a public authority or the product is a

[60] Proposal for a Directive of the European Parliament and of the Council amending Directive 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing and amending Directive 2009/101/EC, art 1(10)(g).
[61] Compliance Interview 12 dated 26/02/16.

certain type of life insurance contract.[62] SDD also applies to a law firm`s pooled client account, which is explored later in this Chapter.

The issue that arises for law firms, particularly those with an international client base, arises in relation to non-EEA credit or financial institutions and listed companies. For listed companies, SDD will only apply where its securities are listed on a `regulated market subject to specified disclosure obligations.`[63] The terms `regulated market` and `specified disclosure obligations` are themselves defined by reference to a number of EU directives. For a non-EEA regulated market, the definition requires such market to have `disclosure obligations which are contained in international standards and are equivalent to the specified disclosure obligations`.[64] As there is no definition of `equivalent`, law firms themselves are required to ascertain which markets have equivalent disclosure obligations. Similarly, law firms may only apply SDD to those non EEA credit and financial institutions applying requirements `equivalent` to those found in 3MLD.[65] Prior to discussing equivalence with regard to non-EEA entities, it is worth noting that a small number of participants felt that the blanket equivalence automatically applicable in respect of EU countries under the MLR 2007 may not always be appropriate. This concern was expressed by the compliance participant who reflected:

> I might think Germany's equivalent but I`m not sure I'd think some of the other member states had equivalence to the UK standards.[66]

[62] See, MLR 2007, regs 7(5) and 7(7) respectively.
[63] MLR 2007, reg 13(3). See definitions of `regulated market` and `the specified disclosure obligations` set out in the interpretation section of the regulations: ibid, reg 2.
[64] See, para (b) of the definition of `regulated market`, ibid, reg 2.
[65] MLR 2007, reg 13(2)(b) provides that SDD may apply to `a credit or financial institution (or equivalent institution) which (i) is situated in a non-EEA state which imposes requirements equivalent to those laid down in the money laundering directive; and (ii) is supervised for compliance with those requirements. Equivalence is also relevant in the context of the Reliance provisions set out in MLR 2007, reg 17 whereby a law firm may `rely` on the CDD conducted by a range of entities, some of which are discernible by reference to being subject to `equivalent` AML provisions. See, for example, reg 17(2)(d)(iii) and (iv).
[66] Compliance Interview 1 dated 17/11/15.

(i) The Administrative Burden of Equivalence

This quest for `equivalence` undoubtedly imposes a burden on law firms in that it requires detailed analysis of the listing rules and AML regimes of non-EEA jurisdictions. Whilst some guidance exists, most notably that produced by JMLSG, such guidance does not feature a definitive equivalence list and is scattered with caveats throughout.[67] As one participant noted with regard to establishing equivalence, `it's not easy and you just have to try and work your way through on a case-by-case basis.`[68] The challenge with regard to equivalence was detailed by the compliance participant who said:

> . . . to work out whether or not a market qualifies for equivalence you`ve got to look at three different pieces of European legislation and each, within those three different pieces about six specific sections and it's just next to impossible . . . [69]

Despite this challenge, participants were fairly evenly split between those who desired a list of equivalent jurisdictions and markets to be produced, and those who either had no view or no issues with the application of SDD. With one exception, however, those participants who either had no view on, or no issues with, equivalence were transactional participants. This view may be attributable to the fact that in a large commercial law firm with a developed compliance function, such participants are typically not personally tasked with establishing whether equivalence provisions apply or not. Furthermore, the single compliance participant who held no view on equivalence did so on the basis that, `we would on very few occasions represent a foreign-based listed entity`: equivalence was simply not relevant given that particular firm`s client demographics.[70]

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[67] See, for example, JMLSG, *Prevention of money laundering/combating terrorist financing 2017 Revised Version* (2017), pt III;The Law Society, *Anti-money Laundering Practice Note* 2013 (2013) para 4.6.
[68] Compliance Interview 12 dated 26/02/16.
[69] Compliance Interview 6 date 08/12/15.
[70] Compliance Interview 20 dated 16/06/16.

The views of those participants who wanted an equivalence list were typified by the MLRO who commented simply that any such list would be `enormously helpful` on the practical basis that, as expressed by another participant:

> . . .there is so much that is left to the firms to grapple with and understand . . . that's one less thing to try to work out.[71]

A number of participants noted that ultimately, political considerations may serve to block the creation of an equivalence list produced at a national level. As one MLRO pointed out with regard to those jurisdictions which were not included on such a list, `the ones who weren't on it would be up in arms.`[72] This stance was taken up by another MLRO who commented in relation to any such list:

> I think politically it`d be difficult . . . because it may change, you know, when Russia is in favour or out of favour.[73]

(ii) A Holistic Approach to SDD

Some participants reported adopting a far more holistic consideration of their clients, with their qualification for SDD forming only one aspect of several in terms of risk factors attaching to a client. This was expanded on by the compliance participant who explained:

> A list of exchanges is helpful but it`s only helpful to the degree that you caveat it and say `well this actually gives you some indication of what the requirements are, and what the disclosure obligations are`, but you've always got to say `okay well it's prima facie low-risk`, but you need to look at the other factors to make sure that you`re comfortable.

This holistic approach was echoed more bluntly by the Deputy MLRO who said:

> . . . we`re not just going to say because you`re listed on an exchange in, you know, Moscow that you are now simplified due diligence . . . the very low hurdle is regulatory compliance, but then the higher hurdle is reputational

[71] Compliance Interview 19 dated 24/05/16; Compliance Interview 2 dated 24/11/15.
[72] Compliance Interview 3 dated 25/11/15.
[73] Compliance Interview 8 dated 14/12/15.

> risk management . . . when you`re looking at things like Russia we want to have a higher bar and, you know, we'll raise it ourselves.[74]

(iii) Concluding Comments on SDD and Equivalence

Any prospect of an `equivalence` list being produced at a national level, whilst desired by many participants, has been firmly swept aside by the MLR 2017. Under Regulation 36 MLR 2017, the preordained categories formerly attracting SDD are replaced with provisions enabling a law firm to apply SDD:

> . . . if it determines that the business relationship or transaction presents a low degree of risk of money laundering.[75]

Such determination will be made, inter alia, by reference to a number of risk factors surrounding any given client, product or jurisdiction. This approach was supported by many respondents during the 4MLD consultation process as an approach that fosters a risk-based approach to AML, whilst providing for emerging risks and avoiding a `tick-box` approach.[76] The term `equivalence` is still retained in this context within the definition of a `regulated market`.[77]

In terms of non-EEA jurisdictional risks, the term equivalence is dispensed with in favour of more fluid concepts. Hence law firms must consider whether a non EEA country has `effective systems to counter money laundering`, has been `identified by credible sources as having a low level of corruption or other criminal activity` or whether `credible sources` indicate that FATF Recommendations are implemented.[78] The responsibility for assessing whether SDD applies to their clients now lies exclusively with the law firm itself, and no automatic categories apply. The

[74] Compliance Interview 9 dated 15/12/15.
[75] MLR 2017, reg 36.
[76] HM Treasury, *Money Laundering Regulations 2017: consultation* (2017) para 3.3.
[77] MLR 2017, reg 3 provides a definition of `regulated market` as `(a) within the EEA, has the meaning given by Article 4.1(14) of the markets in financial instruments directive; and (b) outside the EEA, means a regulated financial market which subjects companies whose securities are admitted to trading to disclosure obligations which are equivalent to the specified disclosure obligations.`
[78] MLR 2107, reg 36 (3)(c)(ii),(iii) and (iv).

production of a national equivalence list would therefore sit at odds with this approach. Therefore participant law firms will continue to undertake their own in house SDD categorisation and due diligence on equivalence. At the time of the interviews, SDD provisions were being debated as part of the 4MLD transposition process. Therefore it was not possible, as it has been with some of the more static provisions of the regulations, to canvass the views of participants as to the SDD provisions of the MLR 2017.

Going forward, it is the author`s view that law firms, who may be unwilling to tie themselves to their own determinations of SDD, which may prove to be erroneous, may simply opt to conduct standard CDD on all clients.

4. Politically Exposed Persons (PEPs)

Regulation 14 MLR 2007 provides that a law firm must `apply on a risk-sensitive basis enhanced customer due diligence measures and enhanced ongoing monitoring` in a range of scenarios.[79] The EDD scenario raised by participants, and explored in this Chapter, relates to the requirements surrounding PEPs.[80] In summary, a PEP is a person who has performed a `prominent public function` within the last year for a non UK state, EU institution or international body, together with immediate family members and close associates. [81] The PEP risk is best outlined by the Deputy MLRO who observed:

> . . . what makes a PEP high risk is the bribery risk for us and the risk that they are going to be using their influence improperly to obtain or confer an unfair or illegitimate advantage and then receive remuneration for that conduct.[82]

[79] MLR 2007, reg 14. EDD scenarios relevant to law firms arise where the client is not physically present for identification (reg 14(2)) or there is an inherently higher risk of money laundering (reg 14(1)(b)).
[80] For the legal profession as a whole, the Law Society figures cite that 67% of their survey respondents did not have PEPs as clients. See The Law Society, *Anti-money laundering compliance by the legal profession in England and Wales* (2009). There are no more detailed figures available for specific sections of the profession such as the Top 50.
[81] MLR 2007, regs 14(4),(5),(6).
[82] Compliance Interview 9 dated 15/12/15.

The rationale driving the focus on the foreign aspects of a PEP is that additional questions should be asked where an individual transacts outside their own jurisdiction. Once a PEP is identified, senior management must approve them as a client and `adequate measures` must be taken to `establish the source of wealth and source of funds` related to a transaction. [83] Issues surrounding source of wealth and source of funds are aspects of the regime that were raised by many participants and will be explored later in this Chapter.

The automatic application of EDD to all PEPs has been vigorously opposed by the Law Society as a costly measure presenting difficulties for law firms with regard to the source of wealth/ source of funds requirements, and potentially dissuading law firms from acting for legitimate clients.[84] This stance was exemplified in their response to FATF`s consultation on the FATF AML Standards in 2011 where the Society concluded:

> . . . there is no evidentiary-based assessment of the actual risks posed by PEPs of money laundering in the UK, to enable a proper assessment of how to effectively and proportionately tackle those risks. [85]

This view was formed on the basis that, despite a series of reports on PEPs by each of the World Bank, Transparency International and Global Witness:

> In all of the examples provided the regulated entity simply needed to comply with legal and ethical imperatives not to engage in money laundering. . . . None of the examples required the use of expensive commercial lists, daily screening of client databases for emerging PEPs or extensive reviews of source of wealth or source of funds.[86]

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[83] MLR 2007, reg 14(4).
[84] The Law Society, *HM Treasury consultation on the transposition of the Fourth Money Laundering Directive: The Law Society response* (2016) 17.
[85] The Law Society*, Financial Action Taskforce Consultation Response Reviewing the standards - preparing for the 4th round of mutual evaluations* (2011) 13.
[86] ibid 12; See also, T Greenberg, L Gray, D Schantz, M Latham and C Gardner, *Stolen Asset Recovery, Politically Exposed Persons, A policy paper on strengthening preventive measures*

Participants themselves expressed a range of views with regard to PEPs which will now be explored.

(i) The Definition of PEPs and Identifying PEPs

The majority of law firms use third party service providers in order to identify PEPs.[87] Many of those providers in turn apply a more expansive interpretation of the concept of a PEP to their searches. This expansion was identified as a source of `intense annoyance` to one MLRO, and a feature which leads to `significant over-compliance` according to the Law Society, resulting in `high levels of false-positive identification of clients as PEPs`.[88] The effect of this, as several participants noted is that, `our service providers sometimes seem to use a wider definition` with the result that they are:

> . . . operating with a completely different set of PEP definitions . . . I mean they go to any sort of link to any level of government – they`ll put a PEP label on there, so there are aspects of that that are becoming quite tricky to deal with.[89]

In contrast, several participants reported that their firms were actively electing to expand upon the strict definition of a PEP in the MLR 2007. Hence some firms were already applying EDD to domestic PEPs on the basis that they were operating an international practice. One compliance participant expanded on this approach as follows: `the reason we've always done that is because when we take a client in any given country, we want them to be transferable to another country.`[90]

(The World Bank, 2009); Transparency International UK, *Combating Money Laundering Recovering Looted Gains* (2009); and Global Witness, *Undue Diligence* (2009).

[87] Law Society survey figures cite that 60% of respondents used commercial service providers to fulfil their PEP obligations. See, The Law Society, *Anti-money laundering compliance by the legal profession in England and Wales* (2009).

[88] Compliance Interview 8 dated 14/12/15; See also, The Law Society*, Financial Action Taskforce Consultation Response Reviewing the standards - preparing for the 4th round of mutual evaluations* (2011) 13,14.

[89] Compliance Interview 2 dated 24/11/15.

[90] Compliance Interview 5 dated 07/12/15.

Others still were choosing to operate their firms using a wider PEP definition as a matter of course, as illustrated by the participant who noted:

> . . . we tend to widen that out a bit to incorporate oligarchs and people that have a very large footprint in the countries in which they operate.[91]

A wider approach was also adopted on a case by case basis according to the MLRO who concluded:

> . . . if we feel that there is something that goes beyond, has a wrong smell about it, but isn't strictly within the PEPs definition, then we'll take the cautious, cautious approach.[92]

(ii) Should EDD Apply Automatically to PEPs?

A number of participants felt that EDD should apply to all PEPs automatically due to the nature of the ill it is designed to address, and on the basis that it is difficult for any law firm to effectively distinguish between PEPs. This issue was highlighted by the MLRO who noted:

> . . . it is very difficult to find a line which enables you to draw a distinction between one PEP and another, but I think politically exposed persons because they have power to influence money and government and do an awful lot of damage . . . I think you just look at the lot.[93]

This aspect of PEP identification was expanded on by the MLRO, who in respect of the difficulties surrounding drawing distinctions between PEPs stated:

> . . . trying to sort out good PEPs from bad PEPs would be difficult but you know a good PEP and a bad PEP broadly, I mean it's much easier in the European context, but in the Chinese context, the fact that so-and-so is political commissar . . . for the region`s industry wing and he's on the board

[91] Compliance Interview 2 dated 24/11/15.
[92] Compliance Interview 15 dated 10/03/16.
[93] Compliance Interview 15 dated 10/03/16.

> of this company we want to act for – what does that mean? Very difficult for me to gauge.[94]

Others felt that automatic EDD in relation to PEPs was one aspect of a more generalised sense of professional good practice. On this basis, automatic EDD was deemed to be, `rightly rigorous`, `a good standard for us all to be setting` and appropriate.[95] As one transactional partner added:

> . . . it's inherent in the definition that there is higher-risk so it's, you`ve already passed a risk threshold of sorts.[96]

A larger number of participants, however, felt that EDD should *only* apply to PEPs using a risk-based approach. This view was typified by the MLRO who recounted:

> I get a lot of PEPs escalated to me who are technically PEPs within the meaning, and frankly there is absolutely no reason for the escalation to me.[97]

A couple of participants went on to highlight the fact that the automatic application of EDD actually served to detract from other areas of risk for the profession. This was articulated best by the compliance participant who said:

> . . . it's a huge source of frustration, I think in many ways the PEPs thing disguises the importance and risks of other elements of money laundering because people think `Ah, good news, it's not a PEP therefore I probably don't need to push on source of wealth`.[98]

(iii) What Counts as EDD?

Several participants expressed concern over the lack of any real clarity as to what measures actually constitute EDD once a PEP had been identified in any event, or

[94] Compliance Interview 8 dated 14/12/15.
[95] Transactional Interview 6 dated 25/11/15; Transactional Interview 10 dated 26/11/15.
[96] Transactional Interviews 6, 10 and 2 dated 25/11/15, 26/11/15 and 18/11/15.
[97] Compliance Interview 17 dated 08/04/16.
[98] Compliance Interview 6 dated 08/12/15.

as one MLRO said, `what the exact requirements are around the extent of the enhanced due diligence.`[99] As one highly experienced MLRO added:

> Heaven alone knows how you're supposed to do enhanced due diligence - it's a phrase that's used, but quite what it means in practice is a bit difficult to understand.[100]

The temptation therefore, as highlighted by several participants, is to simply request further identification documents almost as a `go to` EDD measure, a response that one Deputy MLRO deemed to be, `of no utility whatsoever, let alone limited utility.`[101] The issue is one of establishing the underlying bona fides of a transaction, not, `oh well I need to see a copy of your utility bill now because you`re high risk.`[102]

(iv) Including Domestic PEPs in the PEP Definition

During the consultation process for 4MLD, a number of proposals were considered with regard to PEPs, one of which was the inclusion of domestic PEPs within the PEP definition. This was strongly opposed by the Law Society on the basis that, ` we do not believe there is sufficient evidence of unmitigated risk in this area` to merit the inclusion of domestic PEPs.[103] There are inevitable cost implications of such inclusion, which was the focus of one Deputy MLRO who observed:

> . . . obviously as soon as you broaden the class of person that you have to investigate, the administrative burden becomes greater.[104]

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[99] Compliance Interview 4 date 03/12/15.
[100] Compliance Interview 3 dated 25/11/15.
[101] Compliance Interview 9 dated 15/12/15.
[102] ibid.
[103] The Law Society*, Financial Action Taskforce Consultation Response Reviewing the standards - preparing for the 4th round of mutual evaluations* (2011) 15. The Society expressed the view that there were human rights implications relating to such an extension.
[104] Compliance Interview 11 dated 19/02/16. The Law Society estimates increased costs of between £2,000 to £20,000 pa for each commercial electronic verification service provider, in addition to an increase in staff costs as a result of the inclusion of domestic PEPs in the regime. See, The Law Society, *Development of a 4th Money Laundering Directive Response to the European Commission's review of the third money laundering directive* (2012) 10.

Cost implications aside, many participants reported that their firms were already applying EDD measures to domestic PEPs: this on the basis explored in preceding paragraphs, that their firms operated an international practice. This view can be summarised by the compliance participant who explained, `what might be a domestic PEP for our UK office is not a domestic PEP for our Hong Kong client.`[105] As a result, the proposed inclusion of domestic PEPs within the PEP regime was of little concern or consequence to such participant firms.

(v) Producing a List of PEPs

Historically, the Law Society have argued for the government or European Council to produce lists of PEPs arguing that:

> We consider it ethically questionable to threaten private citizens with civil liability and criminal sanctions for failing to do what governments will not or cannot do. [106]

However, only one participant expressed a desire for such a list, articulating a practical desire to minimise EDD costs for the profession as a whole. In other words, with the availability of PEP lists at a national level, `the amount of money that's being spent on some of these electronic systems might change` in relation to law firms.[107] It should be noted that commercial service providers in relation to PEPs are unregulated in terms of the fees they can charge, and the firms they service are legally obliged to comply with the UK`s AML regime with regard to PEPs, so market forces alone are unlikely to push down on such costs.

(vi) Concluding Comments on PEPs

The MLR 2017 include domestic PEPs within its scope, in contrast to the exclusive focus on foreign PEPs seen in the MLR 2007. This new feature was of little concern

[105] Compliance Interview 1 dated 17/11/15.
[106] The Law Society*, Financial Action Taskforce Consultation Response Reviewing the standards - preparing for the 4th round of mutual evaluations* (2011) 14.
[107] Compliance Interview 12 dated 26/02/16.

or consequence to participants, however, reflecting the fact that many international participant firms have included domestic PEPs in their PEP searches as a matter of course, even before the MLR 2017 came into force. What has changed however, is that a risk-based approach to EDD and PEPs has been implemented.[108] Law firms must `form their own view of the risks associated with individual PEPs on a case by case basis`.[109] Thus, under MLR 2017, law firms must now have in place `appropriate risk management systems and procedures` enabling them to `manage the enhanced risks` of having PEPs as clients.[110] The corollary to this is that law firms will be required to follow industry guidance from the Law Society stipulating appropriate levels of EDD governing a range of scenarios.[111] By implementing a more effective risk-based approach to EDD and PEPs, the new provisions only partially address the issues raised by participants and the Law Society alike, although the related costs implications attributable to the inclusion of domestic PEPs within the regime are unavoidable.

Law firms will still be required, as before, to ` take adequate measures to establish the source of wealth and source of funds` with regard to PEPs.[112] It is these two features of the regime that will now be considered.

5. Source of Funds

The requirements around establishing a client`s source of funds or source of wealth are at the epicentre of a law firm`s AML response. Ultimately, the entire UK AML regime can be crystallised into one dominant concept: that of preventing illicit funds being placed into or moved around the legitimate economy. As detailed in Chapter 2, the focus of the substantive money laundering offences in ss 327-9

[108] MLR 2017, reg 35. It should be noted that, at the time of submission of this thesis, the EU were still debating further amendments to 4MLD. One such proposed amendment is that there should be a further distinction drawn between PEPs such that low risk domestic PEPs would attract CDD, as opposed to EDD.
[109] HM Treasury, *Money Laundering Regulations 2017: consultation* (2017) para 8.
[110] MLR 2017, reg 35(1).
[111] MLR 2017, reg 35(4)(b).
[112] MLR 2017, reg 35(5)(b).

POCA 2002 is to criminalise dealings with `criminal property`. CDD failings around source of funds/wealth within the legal profession were also specifically highlighted as an area of concern in the UK`s National Risk Assessment 2015.[113] It is this focus that informed the view of the Deputy MLRO who opined:

> You really need to be absolutely understanding the source of wealth and source of funds being used for a particular transaction, you know that's the money laundering risk – where did it come from? How did you get it? I need provenance. I need to go through your banking records and understand where that came from and be satisfied that it is legitimate – that's the *only* substantive money laundering issue.[114]

It may be recalled from earlier in this Chapter that Regulation 14(4)(b) MLR 2007 obliges law firms to `take adequate measures to establish the source of wealth and source of funds` on a transaction involving PEPs, a feature which is tracked through to the new regulations.[115] In addition, Regulation 8 imposes standard ongoing monitoring obligations requiring law firms to scrutinise their client`s transactions `including, where necessary, the source of funds`.[116] Whilst there is significant overlap in terms of some of the issues that arise in this area, it is important that a distinction is made between the source of funds and the source of wealth in relation to a particular client. This nuance is best set out by the compliance participant who made the distinction as follows:

> . . . source of wealth - I`m talking about how does, you know, the entity or the individual . . . make their money . . . source of funds - what`s the actual way in which the transaction is being funded.[117]

[113] HM Treasury, Home Office, *UK national risk assessment of money laundering and terrorist financing* (2015) para 6.77.
[114] Compliance Interview 15/12/15 (emphasis added).
[115] MLR 2017, reg 35(5)(b).
[116] MLR 2007, reg 8(2)(a).
[117] Compliance Interview 14 dated 10/03/16.

It should be noted that concerns over source of funds will be informed by each participant`s client profile and practice area. Hence those participants with a PEP client base will always be concerned with both source of wealth and funds as a matter of course. For those practicing in corporate banking, for example, or dealing exclusively with large Plc clients receiving bank funding, the source of funds requirement is very easy to satisfy and unlikely to present any difficulties. This on the basis that, `it's obvious where the funds come from`.[118] Therefore many participants from such practice areas reported that they had no difficulties establishing source of funds.

(i) Establishing Source of Funds is Challenging

However, many other participants reported that establishing the source of funds on a transaction could be challenging, particularly with regard to overseas jurisdictions, and difficult to verify. Clients could also be sensitive to requests for such information.

The difficulties around verifying such information were apparent, on the basis that source of funds information is `completely self-certified` (although it should be noted that the requirement in MLR 2007 is to take `adequate measures` as opposed to actually verifying the source of funds).[119] This was pinpointed by the compliance participant who stated:

> . . . ultimately that information`s got to come from your client, and you can do online searches in terms of looking into somebody's background, but as a law firm we don't have access to the financial records.[120]

This vulnerability was also touched upon by the compliance participant who reflected, `we`re largely dependent on assurances that we get from intermediaries

[118] Transactional Interviews 16 dated 08/12/15.
[119] Compliance Interview 9 dated 15/12/15.
[120] Compliance Interview 1 dated17/11/15.

who are not always entirely reliable.`[121] This is a vulnerability that will not be addressed until global bank secrecy laws are revised to afford a greater degree of transparency. As one Deputy MLRO said:

> Until you introduce the transparency, having professional advisers simply ask an individual, you know, where they got their source of wealth and funds from is of no utility whatsoever.[122]

Requesting source of funds information is also seen by some clients as ` a very sensitive question` such that `clients don't like doing it sometimes.`[123] As for the lawyers themselves, `it`s a difficult question to ask and lawyers feel very uncomfortable asking.`[124] For one participant, this client relationship aspect was so prominent that they said in relation to source of funds information, ` the *main* issue actually is a practical one, is you know, how do you . . . ask about that without causing offence, it's really tricky.`[125] Prominent importance is not paramount importance however, and several firms reported cases where they had declined to act, stating in one case that, ` we do actually turn work away on a reasonably regular basis because we can't get comfort on the source of funds.`[126]

(ii) Guidance on Source of Funds

Several participants commented on the lack of explicit guidance on the source of funds, such as the compliance participant who stated, `the information is very, very sparse on what you actually get`.[127] This was echoed by the MLRO who noted in relation to source of funds requirements, ` it's quite apparent that the Law Society does not have a precise answer` as to exactly what is required.[128] This prompted one participant to state that the:

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[121] Compliance Interview 5 dated 07/12/15.
[122] Compliance Interview 9 dated 15/12/15.
[123] Compliance Interview 1 dated 17/11/15.
[124] Compliance Interview 9 dated 15/12/15.
[125] Transactional Interview 8 dated 26/11/15 (emphasis added).
[126] Compliance Interview 20 dated 16/06/16.
[127] Compliance Interview 2 dated 24/11/15.
[128] Compliance Interview 4 dated 03/12/15.

> . . . source of funds point is still one of the biggest challenges for the profession. Level of awareness - what do you mean? How far do I have to go?[129]

This prompted many participants to express a desire for more guidance in this area as to, ` what exactly is meant, what would be the evidence that would be acceptable in a range of situations.`[130] It is submitted however, that exhaustive guidance would not be possible or appropriate. First, there are multitudinous deal permutations that could arise which militate against the provision of regimented guidance. As one compliance participant reflected:

> I don't think it's possible [to provide more explicit guidance]. . . just because there are so many different circumstances and so many different types of transactions.[131]

Secondly, a significant element in relation to source of funds requires a judgement call on the part of the law firm, which could not be managed by way of an explicit list. It is this judgement call with regard to source of funds that will now be explored.

(iii) Source of Funds Information is a Judgement Call

Many participants acknowledged that law firms must make a judgement call themselves on source of funds information. As one compliance participant put it:

> You could probably give more guidance, but a lot of it is down to individual judgement.[132]

This stance was echoed by the participant who expanded as follows:

[129] Compliance Interview 12 dated 26/02/16.
[130] Compliance Interview 2 dated 24/11/15.
[131] Compliance Interview 6 dated 08/12/15 (words in brackets added).
[132] Compliance Interview 12 dated 26/02/16.

> It`s a real judgement call because you're just looking at business history effectively, you know, where have they made their money, where's it come from, what's happening?[133]

Participants` comments on source of wealth tended to follow a similar pattern to those related to source of funds, and it this aspect of the regime that will now be considered, prior to an overarching consideration of those issues affecting both source of funds and source of wealth for the profession.

6. Source of Wealth

As with source of funds information, participants reported that source of wealth information is often challenging to obtain and difficult to confirm.[134] Similarly, those participants acting exclusively for large institutions and banks were unlikely to encounter any concerns related to source of wealth due to their practice area.

(i) Source of Wealth Information is Challenging to Obtain

A number of participants reported difficulties in obtaining source of wealth information from their clients. Several observed that obtaining information on `source of wealth can be a bit trickier` or `a little bit more difficult` than obtaining source of funds information.[135] The increased level of difficulty can be crystallised by the MLRO who commented as follows:

> . . . happy that these funds are coming from the sale of that asset, fine, but how on earth is he, this individual, who is not anywhere on, there`s no public record of him, almost no high profile - how come this individual seems to be the point person for all these assets worldwide?

[133] Compliance Interview 18 dated 08/04/16.
[134] As with source of funds it should be noted that there is no obligation in MLR 2007 to actually verify the source of wealth.
[135] Compliance Interviews 10 and 14 dated 15/12/15 and 10/03/16.

Source of funds may be easier to establish therefore since it may track through directly from the sale of an asset or company. The same, potentially `deeply offensive`, general and cultural sensitivity around asking a client for source of wealth information was also duplicated as it was for source of funds such that, `asking for source of wealth is still quite sensitive, especially in some jurisdictions.`[136] This sensitivity was once more drawn out by the compliance participant who recounted:

> you have regimes you know, like in the Middle East where it's just incredibly difficult to get information and of course culturally they`re very different , so they're not going to, you know, give you the information, and all of those things make life incredibly difficult.[137]

As with source of funds information, law firms are therefore reliant on a mixture of self-certification from their clients or publicly available information. This vulnerability was raised as an issue by the MLRO who noted:

> . . . in a sense it's a sort of fatuous question [on source of wealth] because you know if you've got some, some rich individual . . . and you need to know the source of his wealth, you can ask him and he's either going to be offended and he won't tell you, or he`ll lie.[138]

The reality of this position means that law firms will need to make what is effectively a judgement call on their clients` source of wealth, an aspect which is drawn out in subsequent paragraphs.

(ii) The Judgement Call on Source of Wealth

A number of participants were of the view that more detailed guidance on source of wealth `would be extremely useful`.[139] As one Deputy MLRO expanded:

[136] Compliance Interviews17 and 6 dated 08/04/16 and 08/12/15.
[137] Compliance Interview 12 dated 26/02/16.
[138] Compliance Interview 17 dated 08/04/16 (words in brackets added).
[139] Compliance Interview 11 dated 19/02/16.

> . . . everyone likes lists, you know, to have a list of `this is what you would have to satisfy your provenance of funds point`, if you can prove these and you're satisfied as to the bona fides of these points that would be exceptionally useful. [140]

To date, however, no such explicit guidance has been forthcoming, a point noted by the compliance participant who stated, `we've been asking for years and nobody wants to commit.`[141] As with source of funds however, this may be attributable to the fact that, as also acknowledged by a number of participants, such guidance is `never going to be able to cover every single situation` and will even vary from `client to client`.[142]

Consequently, decisions surrounding the credibility of source of wealth information were seen by a number of participants as a judgement call on the part of participant firms, or as one MLRO concluded, `I think at the end of the day it`s instinctual.`[143] This view is best summarised by another participant who reflected:

> . . . you have to make a judgement call as to whether you think you have enough information, and you make sure you document.[144]

Detailed guidance may not be forthcoming therefore in light of the factors highlighted above.

Whilst law firms may remain reliant on their own judgement in this area, this is not to say that there is no action that can be taken in respect of source of wealth in a more general context. The most notable shift in this area has occurred by way of Unexplained Wealth Orders (UWOs) brought in under the aegis of the Criminal Finances Act 217 (CFA 2017).[145] UWOs provide for civil action by enforcement agencies against individuals `whose assets appear disproportionate to their known

[140] ibid.
[141] Compliance Interview 14 dated 10/03/16.
[142] Compliance Interviews 14 and 8 dated 10/03/16 and 14/12/15.
[143] Compliance Interview 15 dated 10/03/16.
[144] Compliance Interview 12 dated 26/02/16.
[145] Criminal Finances Act 2017, pt 1, ch 1 inserted a new s 362A into POCA 2002.

income.`[146] Such individuals will either be PEPs, or have an involvement with serious crime.[147] Whilst a more detailed exploration of enforcement provisions under POCA 2002 remain outside the scope of this thesis, should law firms decide to report suspicions with regard to a client`s source of wealth, UWOs now provide an additional tool available to law enforcement to unravel potentially illicit funds.

(iii) **Issues Surrounding Source of Funds and Source of Wealth**

The discussion in this Chapter in relation to the source of funds and source of wealth requirements under MLR 2007 has so far centred around the purely practical difficulties participants encounter when trying to obtain pertinent information from their clients. However, there are a number of issues that overshadow these concerns, which are the focus of this section of the Chapter. As the comments participants made relate both to source of funds and source of wealth considerations, they are dealt with together. The overarching issues pertaining to source of funds and source of wealth are as follows: (i) a lack of clear parameters around the obligation to obtain such information, (ii) prior criminality and source of wealth, (iii) ongoing monitoring and source of funds/wealth, and (iv) third party funding and the client account. Each of these aspects will now be explored in turn.

(a) The Shifting Parameters of Source of Funds/Source of Wealth Information

The effect of the lack of prescriptive guidance on source of funds/source of wealth is that there are no concrete boundaries in place as to what information law firms are required to obtain. As one Deputy MLRO phrased it, `where do you draw the line? . . . in my experience there`s different views.`[148] Participants reported a lack of consensus as to what information to ask their clients for. Hence law firms might ask for three or six month`s bank statements from a client, whilst contemporaneously acknowledging the limited value of such statements on the basis that, `even if the money`s coming out of a first class bank account you never

[146] Dominic Thomas-James, `Unexplained Wealth Orders in the Criminal Finances Bill: a suitable measure to tackle unaccountable wealth in the UK?` (2017) 24(2) JFC 178, 178.
[147] POCA 2002, s 362B(4)(a),(b).
[148] Compliance Interview 11 dated 19/02/16.

know how it got there.` [149] This prompted one compliance participant to reflect that:

> Source of wealth is probably the biggest challenge that you`ve got because do you take a bank statement that might only show the funds going in or out, it doesn't show how they've earnt them.[150]

The same issue exists with regard to how far back in time a law firm is required to make enquires as to the source of funds. As guidance in the area remains generalised rather than prescriptive, and no consensus was evident from participants, this is a judgement that law firms must make themselves.

In a wider context, an additional challenge can be observed, as articulated by the compliance professional who noted:

> the other challenge is also do you establish the source of wealth used for the transaction you're doing or their source of wealth in its entirety? . . . I think that's slightly vague and unclear.[151]

There is no explicit guidance on this point from the Law Society. It is this wider issue that was raised by a number of participants and will form the subject matter of the following paragraphs.

(b) Prior Criminality and Source of Funds/Wealth

As the previous quotation illustrated, a number of participants expressed disquiet in relation to how source of funds/source of wealth should be treated by law firms. More precisely, how should law firms proceed where there is either reported or suspected criminality in a client`s past? Does historic criminality result in unending tainting of all assets? The debate around source of funds/wealth is best expressed by the compliance participant who stated:

> When you start to look at some of the oligarchs, that's a challenge because you know how, . . . everybody knows the history of the oligarchs and you

[149] Compliance Interview 15 dated 10/03/16.
[150] Compliance Interview 6 dated 08/12/15.
[151] Compliance Interview 6 dated 08/12/15.

> know how they managed to get to where they've got to, but the question is therefore, well how do I get comfortable as to source of wealth here given that history, and that's the particular challenge and there's no guidance on that. [152]

This tension was explored further by the MLRO who reflected:

> I think the Law Society are saying it does matter, whereas I think the City view, who are acting for a lot of Russians for instance, would be the opposite: that it doesn't matter once they`re established and wealthy people . . . and I think it`s an issue that I don`t know the answer to.[153]

To put it even more bluntly, in the words of another participant, `you can`t not deal with people who have some question marks in their past.`[154] The issue therefore is whether a `question mark` over a client`s past should become a full stop in terms of declining instructions or ceasing to act for that client.

The answer to that question may be found in the wording of the source of funds/wealth obligations in the MLR 2007 themselves, and related sector specific guidance from the Law Society. It should be recalled that, in relation to PEPs, the obligation upon law firms is limited to taking `adequate measures` to establish the source of funds/wealth.[155] Furthermore, the ongoing monitoring obligations in Regulation 8 MLR 2007 provide that a client`s transactions should be scrutinised (including `where necessary` the source of funds) to ensure the transactions are consistent with the `customer, his business and risk profile`. Neither of these provisions provides that such information must be verified by the law firm or investigated further.

The Law Society AML Practice Note 2013 provides very little guidance on source of funds or wealth generally, and no guidance on historic criminality specifically. [156] In respect of establishing source of funds or wealth, law firms are advised that,

[152] Compliance Interview 14 dated 10/03/16.
[153] Compliance Interview 4 dated 03/12/15.
[154] Compliance Interview 5 dated 07/12/15.
[155] MLR 2007, reg 14(4)(b).
[156] The Law Society, *Anti-money laundering Practice Note* (2013) paras 11.2.3 and 4.9.2.

`Generally this simply involves asking questions of the client about their source of wealth and the source of the funds to be used with each retainer.`[157] Further online advice to law firm MLROs states that law firms are not required to prove that client funds are `clean` adding:

> . . . if a person is clearly wealthy from legitimate means and is engaging in a transaction which is consistent with that wealth, you are not required to dig through their entire financial history to see if they ever committed an offence of any description.[158]

There is some distinction drawn in this quotation between current legitimate funds and historic offences. However, the same note also clarifies that a high risk client who then presents with a high risk source of funds cannot simply be marked as `consistent` with their risk profile: at that point a lawyer must consider their ethical and reporting obligations.[159] Given the exact wording of the MLR 2007 and extremely generalised Law Society guidance, it is the author`s view that decisions on source of wealth and previous criminality rest firmly with the law firm, and do not require an investigation on the part of the law firm into previous alleged criminality. However, law firms may elect to decline instructions from clients with questionable sources of wealth on reputational or brand protection grounds: this is a feature of practice which is explored in Chapter 7.

Furthermore, there is a balance to be struck between vigilance as to the credibility of information received from clients on source of funds, and an obligation upon law firms to conduct actual investigations into provenance. For one MLRO, the burden was all too apparent:

> . . . actually being able to do the detective work to say `ah, you're telling us a lie about this` is just too much of a burden I'm afraid, is the reality of it.[160]

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[157] ibid para 4.9.2.
[158] The Law Society, `Help! I'm a new MLRO: Tips on sources of funds` (*The Law Society*, 17 April 2012) https://www.lawsociety.org.uk/support-services/advice/articles/help-im-a-new-mlro-your-firms-compliance-culture/ accessed 12 June 2016.
[159] ibid.
[160] Compliance Interview 15 dated 10/03/16.

Decisions surrounding source of wealth also need to be made pragmatically in legal practice. As Transparency International UK themselves acknowledge:

> . . . little can be done to act on highly suspicious wealth unless there is a legal conviction in the country of origin.[161]

In the absence of any criminal convictions in a client`s home territory, therefore, many law firms are taking the decision to continue to act notwithstanding alleged prior criminality.

(c) Source of Funds and Ongoing Monitoring

For `standard` clients (ie not PEPs) Regulation 8 MLR 2007 imposes an ongoing monitoring obligation, `where necessary` with regard to a client`s source of funds. The timing of this requirement was heavily criticised by one participant as being too late in the client relationship. They argued that introducing the source of funds requirement at the ongoing monitoring as opposed to the initial CDD stage made ongoing monitoring more difficult for the legal professional. This stance is evident from the following extract:

> The regulations don't specify source of wealth as a requirement for CDD, they only specify source of wealth as a requirement for ongoing monitoring, which I think is one of the fundamental flaws in the way in which things are set out because obviously you can't do the ongoing monitoring if you haven't established what the source of wealth was at the beginning.[162]

Technically, this observation is entirely correct. This point may well be purely academic, however, in the sense that, as a matter of professional conduct, a lawyer will always ascertain the source of funds for any given transaction at the outset of a retainer in order to be able to properly advise their clients. Failure to do so may well constitute professional negligence. Should that source of funds then arouse

[161] Rachael Davies Teka, `Unexplained Wealth Orders` (Transparency International UK, 2017) < https://www.transparency.org.uk/wp-content/plugins/download.../download.php?id.> accessed 12 June 2017.

[162] Compliance Interview 6 dated 08/12/15. Whilst the participant refers to source of wealth in this extract, MLR 2007 specify ongoing monitoring with regard to source of funds.

suspicion in the mind of the legal professional, they will also need to comply with their reporting obligations under POCA 2002 and related ethical requirements.

(d) Source of Funds and Third Party Funds

One further issue where `the cracks could emerge` with regard to funding considerations was raised by another compliance participant who felt the current position left a `hole in the system`.[163] The issue for law firms is as follows:

> under the Law Society guidance and the ML regs, we don't have an absolute obligation to identify the source of funds landing into our client account so, . . . if you're working a transaction, third parties, other parties paying the money in, we don't *have* to go off and get, actually ID that entity because they're not a client.[164]

It should be noted that law firms still need to understand the source of funds reaching their client account under MLR 2007 and ensure that it is consistent with that particular retainer, but that there is no strict obligation to conduct CDD on third party funding sources. Law firms may elect to rely to a certain extent on the fact that the third party`s bank and/or lawyers may have conducted CDD on their own client, but this is no guarantee as to the standard or rigour around such CDD. Some law firms therefore, do decide to conduct CDD on third party funders as a matter of course. Ultimately, therefore, whether to conduct CDD on third party funders is a decision that will be driven entirely by the risk appetite of each firm in relation to each retainer.

(iv) **Concluding Comments on Source of Funds/Source of Wealth**

It is clear from participant responses that practical difficulties abound with regard to the interrelated issues of source of wealth and source of funds. The requisite

[163] Compliance Interview 18 dated 08/04/16.
[164] ibid (emphasis added).

information is often difficult to obtain and can be a delicate matter to raise, causing embarrassment to lawyers and their clients alike.

Those practical challenges are exacerbated by the lack of concrete parameters set out in MLR 2007 or sector specific guidance from the Law Society with regard to source of funds and source of wealth. Although some participants expressed a desire for more specific guidance, there was also an understanding that the multitudinous client scenarios that could arise, and the risk appetite of each firm essentially meant that decisions on source of funds/wealth were, in essence, a judgement call on the part of each law firm. Therefore, legal practitioners must form their own view as to the information they obtain to satisfy their own enquiries.

Nowhere is the lack of guidance felt more keenly amongst participants, however, than when considering alleged prior criminality, a feature most notable amongst retainers concerning Russian oligarchs. The issue at stake is whether funds which originate from `questionable` sources then taint all the funds which that individual utilises many years later. It is the author`s view that the wording of the MLR 2007 and related Law Society guidance do not oblige law firms to undertake detailed investigations into prior criminality. This is not to suggest that law firms can simply adopt a cavalier attitude with regard to the information they receive from their clients with regard to source of funds/wealth. Sufficient protections are in place authorising or requiring law firms to report their suspicions of money laundering pursuant to the provisions in s 338 and s 330/1 POCA 2002. It should also be recalled that the `failure to disclose` offence in s 330/1 contains a negligence-based test backed by a maximum prison term of 5 years, which could result in liability for those legal professionals attempting to turn a blind eye to criminality.[165] Brand protection and reputational risk may also see law firms declining to act for clients with dubious credentials. This is a feature of practice considered in Chapter 7.

[165] POCA 2002, s 334(2).

One participant noted that imposing an ongoing monitoring requirement with regard to source of funds for `standard` risk clients as opposed to at the client inception stage was concerning, as it put legal professionals in a weaker position in terms of obtaining such information once the retainer had already started. It is suggested however, that despite this omission in the provisions of the MLR 2007, it is implicit in the retainer that a lawyer will determine the source of funding on any given transaction as a matter of professional conduct in order to be able to properly advise the client.

Of more concern, however, is the lack of any absolute obligation in the MLR 2007 to apply CDD to third parties providing funding for a transaction, although law firms are obliged to understand where the source of funding is coming from. In response, a number of participants reported that they actively chose to conduct CDD on third party funders, despite the absence of any strict requirement to do so, particularly when funds were flowing through the client account.

7. Reliance

Regulation 17 MLR 2007 provides a mechanism by which law firms may rely on certain other entities to conduct CDD on their behalf.[166] The entities that may be relied upon by consent comprise regulated sector entities such as other banks or other law firms.[167] In theory, such reliance provisions were introduced in an attempt to `reduce the regulatory burden on businesses`.[168] In practice, however, such provisions are `very rarely, if at all, utilised in practice by solicitors in England and Wales`, to the extent that the UK`s National Risk Assessment 2015 comments that `poor use` is made of the reliance provisions.[169]

[166] As distinguished from outsourcing those obligations, see MLR 2007, reg 17(4).
[167] MLR 2007, regs 17(2),(3),and (5).
[168] HM Treasury, *Consultation on the transposition of the Fourth Money Laundering Directive* (2016) 25.
[169] The Law Society, *HM Treasury consultation on the transposition of the Fourth Money Laundering Directive – The Law Society response* (2016) 11. See also, HM Treasury and Home Office, *UK national risk assessment of money laundering and terrorist financing*

The reason for such limited use of these provisions within the legal profession is clear: notwithstanding Regulation 17 reliance on a third party to conduct CDD on a client, a law firm `remains liable for any failure to apply such measures.`[170] For their part, those law firms being relied upon may find themselves exposed to civil claims from those entities seeking to rely upon their CDD. For these reasons, the reliance provisions in the MLR 2007 were little used and approached with `great caution` on the part of participants when (a) relying on other entities, and (b) being relied upon by third parties.[171] Each of these scenarios will now be explored in the following paragraphs.

(i) Reliance on Third Parties

The vast majority of participants who expressed a view on reliance either refused to rely on third parties at all, or only very occasionally. One of the main reasons for this stance was that those law firms seeking to rely on third parties still retained both criminal and civil liability for any CDD failings, a position best illustrated by the MLRO who stated:

> If we tried to rely on someone else we`d still have the responsibility and the obligation to make sure that information is correct, so why bother to rely on someone.[172]

Several participants expressed an unwillingness to rely on other entities whose CDD standards may not match those of the law firm seeking reliance. Put simply, `you don't know how thorough the other firm has been.`[173] This potential gradation in the quality of CDD was a drawback expanded on further by the Deputy MLRO who commented:

(2015) para 6.77. Misuse of the reliance provisions is identified as a specific vulnerability in the estate agency sector, ibid para 6.155.

[170] MLR 2007, reg 17(1)(b).

[171] Compliance Interview 12 date 26/02/16.

[172] Compliance Interview 3 dated 25/11/15.

[173] Compliance Interview 15 dated 10/03/16.

> . . . it`s a bit like sub-prime you know, you need to make sure that the fundamentals are right before you get this chain of reliance, and what you end up with is this long chain that's based on shifting sands.[174]

There was also a perception that each law firm should conduct due diligence according to its own risk parameters, as articulated by the compliance participant who said:

> we just feel we need to understand and identify our own risk and therefore do the due diligence on that basis, and we feel we cannot sort of farm that out to somebody else.[175]

Such principled objections to the use of reliance provisions were supplemented by entirely practical ones: participants reported that many entities do not permit law firms to rely on them in any event. This was highlighted by the transactional partner who commented on reliance as follows: `in practice it doesn't tend to happen `cos I think people don't like to expose themselves to the risk.` It is this aspect of practice that will be considered next.

(ii) Reliance on Law Firms By Third Parties

That law firms are unwilling to be relied upon by third parties under Regulation 17 MLR 2007 was borne out by participants` responses. The majority of participants who expressed a view on reliance said that they would never consent to being relied upon. This position reflects concerns over potential `tortious liability` for any CDD failings.[176] This issue is best summarised by the transactional partner who commented:

> . . . it's one thing to get your own due diligence wrong - it's another thing then to say `right, you can rely on ours` and then they suffer some sort of detriment and, you know, come back and say `right, you were negligent and you`re liable`,

[174] Compliance Interview 9 dated 15/12/15.
[175] Compliance Interview 2 dated 24/11/15.
[176] Compliance Interview 14 dated 10/03/16.

so why expose yourself to that when you can simply say `well I'm sorry, you`ll have to do your own.`[177]

In addition to potential negligence claims against them, some participants felt that the obligation to keep such CDD information updated was too onerous in the context of Regulation 17 reliance.

A number of participants said that they might occasionally consent to being relied upon in restricted circumstances, a typical scenario referred to being where foreign lawyers had been instructed on behalf of a common client. The Law Society note that reliance provisions may also be utilised in very particular circumstances where a firm elects to passport clients within the same firm across jurisdictions.[178] Whilst participants were largely unwilling to provide formal reliance certificates for the reasons explored in the paragraphs above, a number did confirm that, with the consent of their clients, they were happy to provide copies of their CDD documentation to third parties.

(iii) Concluding Comments on Reliance

Revised reliance provisions under Regulation 38 MLR 2017 incorporate a number of new features. For example, the categories of entities that may be relied upon are expanded to include, inter alia, any entity subject to the MLR 2017. Written arrangements with third parties must also specify a time limit of two working days within which the entity being relied upon must supply copy CDD documentation to those seeking to rely on them.[179] None of these amendments, however, address the fundamental issues that participants experience in relation to the reliance provisions, and which the government themselves acknowledged in their consultation response on 4MLD: that `the risks of relying on a third party are generally greater than the benefits.`[180] The issue is one of retained criminal liability for those relying on third parties, and potential tortious liability together with

[177] Transactional Interview 8 dated 26/11/15.
[178] See The Law Society, *HM Treasury consultation on the transposition of the Fourth Money Laundering Directive – The Law Society response* (2016) 11.
[179] MLR 2017, reg 38(2)(b).
[180] HM Treasury, *Money Laundering Regulations 2017: consultation* (2017) para 3.5.

onerous updating obligations for those being relied upon. Whilst this remains the position, as it does under Regulation 38(1) MLR 2017, reliance will remain a little used tool for the legal profession.

It should be no surprise whatsoever that `poor use` is made of reliance provisions unless and until the regulations move to a position where reliance can occur without retained liability. It is the author`s view, however, that each law firm should determine its own risk parameters and appetite, and therefore reliance should not be used routinely in any event, but restricted to those exceptional circumstances referred to in the preceding paragraphs.

8. Ongoing Monitoring

Law firms are required to conduct ongoing monitoring of their business relationships under Regulation 8 MLR 2007. This process involves the `scrutiny of transactions . . . (including, where necessary, the source of funds)`, to ensure that such transactions are consistent with the law firm`s knowledge of their `customer, his business and risk profile`.[181]

A number of participants highlighted the importance of ongoing monitoring as a key component in the fight against money laundering. The significance of this aspect of the regime was emphasised by the Deputy MLRO who said:

> Ongoing monitoring is from my perspective and from the firm's perspective is probably the most important part of the regime which is making sure that people are aware of what the money laundering risk could be, and who the client is, and are able to assess every transaction, every matter, every action through that lens.[182]

That ongoing monitoring is `the hardest thing` was also highlighted by a number of participants, one of whom reflected:

[181] MLR 2007, reg 8(2). Law firms must also keep CDD documentation up to date.
[182] Compliance Interview 9 dated 15/12/15.

> . . . everyone says it's the biggest challenge and you know it's the area of greatest concern – you keep saying you've got to stay alert . . . but what does that actually mean to the fee earner?[183]

In purely practical terms, very few participants expressed a desire for more specific guidance on ongoing monitoring, and many participant firms utilised automated ongoing monitoring reminders to assist in the process. Automated, periodic e-mail reminders to a fee earner can only achieve a limited amount in the context of fast paced deals however, and the real challenge lies in retaining AML considerations at the forefront of a fee earner`s mind. This dynamic was expanded on by the MLRO who concluded:

> As a lawyer your mindset is `solve my client`s needs` and you might have your antennae set to say `well if something feels fishy I`ll react to it`, but you don't necessarily have your antennae set to say `right, I haven't asked them whether their ownership has changed in the last three months, I must have that conversation when I'm next on the phone` it`s just . . . not in the DNA.[184]

This potential vulnerability could be addressed in part by way of raising awareness amongst fee-earners through AML training, an aspect of the regime considered below.

9. AML Training

Under Regulation 21 MLR 2007, law firms in the regulated sector must take `appropriate measures` to train `relevant employees`. Such employees must have an awareness of AML legislation and be trained regularly to `recognise and deal with` potential money laundering.[185] MLR 2017 impose comparable training

[183] Compliance Interviews 10 and 12 dated 15/12/15 and 26/02/16.
[184] Compliance Interview 13 dated 10/03/16.
[185] MLR 2007, reg 21(a) and (b).

obligations, but expand upon the previous provisions to clarify what is meant by the terms `relevant employee` and `appropriate measures`.[186]

(i) Delivery of AML Training

Prior to examining participants` views on their AML training, the mechanics of delivering such training will be summarised in brief. The majority of participants were trained in AML using either online training programmes in isolation, or a blend of online and face-to-face training.[187] In terms of frequency, many participants reported that trainees and new staff received AML training on induction, which was then refreshed either annually or every two years. A number of participants also received supplementary AML information by way of e-mail alerts or via departmental meetings. Several participants noted that refresher training had been implemented prior to visitations by the SRA as part of their thematic review of AML in the legal sector.[188] These findings reflect those in the SRA Anti-Money Laundering Report published in 2016 which concluded that `most firms had provided appropriate and relevant training to staff.`[189]

Many participants recognised the importance of AML training, education and awareness, with a number of participants expressing a desire for more tailored training using examples which would resonate with large commercial law firms. It is these perspectives on training that will now be explored.

(ii) The Importance of AML Training, Education and Awareness

Many participants acknowledged the value and importance of AML training on the basis that with `good quality training you raise awareness.`[190] That poor levels of

[186] MLR 2017, reg 24(2) and (3). Written training records must also be maintained under reg 24(1)(b).
[187] A number of participants were of the view that face-to-face training was superior to other forms of training.
[188] Transactional Interview 11 dated 26/11/15, Compliance Interviews 8 and 17 dated 14/12/15 and 08/04/16.
[189] SRA, *Anti-Money Laundering Report* (2016) 27ff. In addition to the findings reported above, the Report (i) stressed the importance of conforming AML training when law firms merge, (ii) stressed the importance of maintaining training records, and (iii) queried whether generic training was appropriate for finance staff.
[190] Compliance Interview 12 dated 26/02/16.

AML awareness posed a money laundering risk to the law firm itself was drawn out by the compliance participant who commented:

> We as a business have spent a lot of time recently communicating and trying to raise and improve awareness because I think that's the reality of where a lot of our exposure is.[191]

An appreciation of the value of AML training and awareness was not limited to compliance participants, and a number of transactional participants emphasised its importance. Participants voiced an appreciation that, in the words of one transactional partner, `criminals become increasingly sophisticated so therefore our training and procedures have to match those.`[192] Few participants referred to AML training as a `tick-box` exercise.[193] The NRA 2015 highlights the importance of AML education for negligent legal professionals, noting that ` regulatory intervention or education may be a more appropriate response [than criminal sanctions] in order to increase awareness and reduce money laundering . . . risk.[194] Campaigns to raise awareness targeted at the legal sector were also implemented in 2014/5 by the Home Office, working in conjunction with supervisory authorities, law firms and law enforcement agencies.[195] In the responses to the government`s Call for Information on the SARs Regime, training was `seen as vital.` [196] With a general sense of the importance of AML training established from many participant responses, a more granular level consideration of the content of AML training was then invited.

[191] Compliance Interview 5 dated 07/12/15.
[192] Transactional Interview 8 dated 26/11/15.
[193] Transactional interview 16 dated 08/12/15.
[194] HM Treasury and Home Office, *UK national risk assessment of money laundering and terrorist financing*, (2015) para 6.97(words in brackets added).
[195] Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance*, (2016) paras 2.19 and 2.20.
[196] ibid Annex B.

(iii) Improvements to Training – Bespoke Training and Relevant Examples

Participants were asked to consider improvements to their AML training. Whilst a number of participants felt no improvements were required, many participants focused on the need for more bespoke AML training, utilising relevant examples of money laundering that were drawn from real life.

A number of participants emphasised the need for bespoke AML training, tailored both to the law firm itself and to specific practice areas. The position was outlined by a compliance participant as follows:

> . . . you can do the sort of online training . . . but there`s a limit to how much that really sinks in on a sort of, you know, well how does it affect me?[197]

A more targeted approach was also advocated by the compliance participant who was implementing a move away from a general, `sheep dip` form of AML training in their firm to one providing `bespoke training for different groups.`[198] To that end, a small number of participants were actively developing their own training tools as opposed to using third party providers.

A number of participants were of the view that face-to face training was more effective than on-line delivery, such as the MLRO who stated `you can`t beat face-to-face training for half a day.`[199] As one compliance participant commented:

> we try to do more sort of face-to-face training because it is a pretty dry subject, so it's much easier if you can see the whites of people's eyes.[200]

Similarly, a preference for face-to-face training was also expressed by a number of transactional partners, one of whom reflected, `actually being forced to sit through somebody giving you an update is more likely to sink in`.[201] Notwithstanding this stated preference for face-to face training, many participants took a pragmatic

[197] Compliance Interview 12 dated 26/02/16.
[198] Compliance Interview 2 dated 24/11/15.
[199] Compliance Interview 20 dated 16/06/16.
[200] Compliance Interview 1 dated 17/11/15.
[201] Transactional Interview 20 dated 11/03/16.

view, acknowledging that `cost, time and resourcing` effectively curtailed its use in practice.[202] One partner also reported a further practical challenge surrounding face-to-face training, namely that, `conventional face-to-face training means that a lot of people cancel, they`ve got client work on and so forth`.[203]

Training scenarios should be `relevant to their day-to-day life` or in other words `more aligned to one's own practice`.[204] Such examples, expressed by one MLRO as `somebody telling you stories about home` were perceived to be a more effective means of raising awareness amongst the profession than generic, untailored AML training.[205] The utility of relevant, real world money laundering examples in AML training is best illustrated by the senior compliance participant who concluded that, `the best training is effectively giving them war stories`.[206]

(iv) Concluding Comments on AML Training

AML training was valued highly by many participants, and a desire for bespoke training, preferably face to face, using relevant examples was vocalised frequently. The issue with AML training to date has been the limited availability of money laundering case studies and examples relevant to much of the profession, particularly large commercial law firms. Hence there are very few pertinent `war stories` to tell, rather a collection of what could be considered as distant tales from far shores. There have been repeated calls from the profession for better information sharing between law enforcement agencies and the regulated sector, and it is improvements to this aspect of the regime that will better support legal sector in practice. Such improved information sharing will do much to raise AML awareness within the profession, both for MLROs and for those reporting to them. Such training may have the effect of refining the judgement of both MLROs and those reporting to them, thus enhancing the effectiveness of the SARs regime overall. The SARs regime is a topic that will be discussed in detail in Chapter 6.

[202] Compliance Interview 6 dated 08/12/15.
[203] Transactional Interview 8 dated 26/11/15.
[204] Compliance Interview 12 dated 26/02/16 and 15 dated 10/03/16.
[205] Compliance Interview 16 dated 14/03/16.
[206] Compliance Interview 18 dated 08/04/16.

10. The Client Account and Money Laundering

The remainder of this Chapter will consider those AML issues relating to the operation of a law firm`s client account, the misuse of which has been identified as a money laundering typology by FATF, and was examined in Chapters 1 and 2.[207] In particular, this section of the Chapter will address: (i) attempts made by clients to use the client account as a banking facility, (ii) the practical effect no longer holding a client account would have on participants, (iii) SDD and the client account.

Under the SRA Accounts Rules 2011, money is categorised as either client money or office money, the former being defined as `money held or received for a client or as trustee` and the latter being defined as money which belongs to the law firm.[208] Client money, such as the funds required to complete a property purchase for example, must be held in a separate account and is usually held in a pooled client account with a financial institution (PCA).[209] Thus the client is the beneficial owner of those funds.

As outlined in Chapters 1 and 2 of the thesis, misuse of the client account has been identified as a money laundering typology by FATF, and it may be recalled that such misuse may arise either by law firms effecting transfers in the absence of an underlying transaction, structuring payments under relevant thresholds in other jurisdictions, or by way of aborted transactions.[210] Despite this evident typology, PCAs have historically been designated as a low money laundering risk, a view adopted on the basis that there are robust controls on the profession at large and the client account in particular.[211] Consequently, PCAs qualify for `simplified due diligence` whereby, under Regulation 13(4) MLR 2007, banks are not required to

[207] See Chapter 1, Money Laundering Typologies in the Legal Profession.
[208] SRA, *SRA Handbook* (Version 18, 2016) SRA Accounts Rules 2011, rule 12.
[209] ibid. Rule 13.5 specifies two kinds of client account: (a) a `separate designated client account` holding funds for an individual client, or (b) a `general client account`.
[210] FATF, *Money Laundering and Terrorist Financing Vulnerabilities of Legal Professionals* (2013) 37.
[211] For example under the solicitors accounts rules, SRA, *SRA Handbook* (Version 18, 2016) SRA Accounts Rules 2011. Under these rules, and rule 14.5 in particular, the client account may not be used as a banking facility and must be connected with an underlying transaction.

conduct customer due diligence in respect of PCAs, only in respect of the law firm itself. This is not a license to operate anonymous bank accounts however, and there are constraints built in to this provision such that:

> . . . information on the identity of the persons on whose behalf monies are held in the pooled account is available on request.[212]

In recent years there has been considerable focus on the client account. The first issue to be considered is its potential misuse as a banking facility. The second issue to be considered is whether solicitors should continue to operate client accounts, or alternatively use a third-party provider as is the approach in other areas of the profession.[213] Finally, the transposition of 4MLD has prompted detailed consideration of PCAs and SDD. Each of these aspects of the client account is explored further below.

(i) Clients Attempting to Use the Client Account as a Banking Facility

In England and Wales, use of the client account is governed in part by the Solicitors Accounts Rules, the most relevant feature of which in the context of this thesis is Rule 14.5, prohibiting the use of the client account in the absence of an underlying transaction.[214] Abuse of this rule has prompted targeted Warning Notices from the SRA in addition to a number of High Court actions.[215] As the judge in one such case commented:

> . . . allowing a client account to be used as a banking facility, unrelated to any underlying transaction which the solicitor is carrying out, carries with it

[212] MLR 2007, reg 13(4)(b).
[213] The Bar handle funds by way of a third-party provider.
[214] SRA, *SRA Handbook* (Version 18, 2016), SRA Accounts Rules 2011, rule 14.5.
[215] See SRA, `Warning Notice: Improper use of a client Account as a banking facility` (*SRA*, 18 December 2014) < http://www.sra.org.uk/solicitors/code-of-conduct/guidance/warning-notices/Improper-use-of-client-account-as-a-banking-facility--Warning-notice.page>accessed 12 April 2017. See also, SRA, `Warning Notice: Money laundering and terrorist financing` (*SRA,* 8 December 2014)< http://www.sra.org.uk/solicitors/code-of-conduct/guidance/warning-notices/Money-laundering-and-terrorist-financing--Warning-notice.page> accessed 12 April 2017.

> the obvious risk that the account may be used unscrupulously by the client for money laundering.[216]

Many participants were extremely alert to the money laundering risks posed by the operation of their firm`s client account. The emphasis by firms on client account risk is best illustrated by the participant who commented in respect of their firm, `it`s something we`ve really put our arms around`.[217] A small majority of participants reported that clients *had* attempted to use the client account as a banking facility. The majority of those participants stated categorically that any such requests were swiftly dismissed by their firms, a position typified by the participant who stated bluntly in relation to such client account usage, `we do not allow that`.[218] This stance was emphasised by the MLRO who confirmed, `we're pretty adamant you know you can't use us as a bank account`.[219] This point was expanded on by another MLRO who said:

> . . . we've just been you know saying `no - we can't` so that everyone`s very clear that now it`s one area that`s absolutely adamant.[220]

Attempts to use the client account as a banking facility were framed by a number of participants as being requested by the client purely on the basis of administrative ease or commercial efficacy. Illustrative examples where such requests are made include where a transaction is effected by way of a Special Purpose Vehicle (SPV) and, prior to that SPV having their own bank account, attempts are made to use the client account to hold monies on behalf of investors. Alternatively, the client account may be suggested as a vehicle to hold funds in connection with a crowdfunding project, or it may simply be quicker to use a UK based client account rather than transmitting funds across multiple jurisdictions. In other words, according to one participant:

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[216] *Fuglers LLP and others v SRA* [2014] EWHC 179 (Admin) QB, per Popplewell J, [41].
[217] Compliance Interview 2 dated 24/11/15.
[218] Compliance Interview 18 dated 08/04/16.
[219] Compliance Interview 3 dated 25/11/15.
[220] Compliance Interview 10 dated 15/12/15.

> it`s not intentionally trying to circumvent anything by the client, they're just trying to do, find [the] easiest route of doing something.[221]

This framing was more directly expressed by the MLRO who recounted:

> . . . the client hasn't thought, `ha ha I'm going to use [name of firm redacted] as a bank`, but we have had occasion when effectively the effect of what is being proposed is to use us as a bank and we've had to decline to do it.[222]

Several participants noted that a particular dynamic could arise in relation to client account services, such that its use could be perceived by both client and practitioner as forming part of a more general client care package. This dynamic was highlighted by several participants who referred to the provision of client account services, albeit blocked by the firm, as either a potential `add-on`, or as a `favour` to the client.[223] Several participants also highlighted challenges surrounding establishing whether there was, in fact, an underlying transaction as envisaged by the `grey and fuzzy` Rule 14.5.[224] This challenge is best summarised by the participant who said:

> . . . there are some that it's a very tenuous link with a particular matter or transaction that we are working on for a client, and it's not so clear-cut, and we've . . . really been cautious about that sometimes, extremely cautious and we`ve said no.[225]

Participants were acutely alive to the money laundering risk presented by the client account, as was emphasised by the MLRO who observed:

> . . . people who want to launder money will see that as the absolutely crystal clear way once it`s in of laundering that money.[226]

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[221] Compliance Interview 1 dated 17/11/15 (word in brackets added).
[222] Compliance Interview 17 dated 08/04/16 (words in brackets added).
[223] Compliance Interviews 2, 5 and 7 dated 24/11/15, 07/12/15 and 08/12/15.
[224] Transactional Interview 12 dated 01/12/15.
[225] Compliance Interview 2 dated 24/11/15.
[226] Compliance Interview 10 dated 15/12/15.

Nevertheless, only a tiny minority of participants perceived attempts to use the client account as a banking facility as potential money laundering: in most cases it was simply perceived as an attempt to channel money via the most efficient route possible. [227]

(ii) Solicitors No Longer Holding Client Accounts

One potential response to the money laundering vulnerability of PCAs is to stop law firms operating client accounts altogether. Certainly, misuse of the client account in a much broader sense than simply money laundering has received significant attention in recent years, culminating in the Legal Services Board (LSB) deeming such misuse to be `one of the biggest regulatory risks in the legal sector`.[228] This in turn has prompted consideration of possible alternatives to PCAs, either by migrating to third party escrow providers, or by using a blend of client account and escrow facilities.[229] Surprisingly grand claims are made by the LSB in support of such alternatives. For example, the LSB state that the potential cost savings from the reduction of risk in this area may be passed onto clients and therefore result in an increase in access to justice.[230] In addition, the LSB state, clients would no longer be vulnerable in term of the `rogue minority` of lawyers `dipping into` client account funds, and would benefit from increased choice and transparency in terms of payment mechanisms.[231] For their part, law firms would benefit from a decrease in regulation and audit requirements by electing not to operate a client account, together with reduced practising certificate fees and solicitors` compensation fund contributions.[232] It is in this context that participants were asked to consider

[227] Only tangential references were made to participant law firms offering escrow facilities to clients, with such facilities deemed to be both unpopular and risky.
[228] Legal Services Board, *Alternatives to handling client money* (2015) 3. 2014 figures document more than 140 cases of misuse each month. There were 1,699 claims totalling £24.69milliom paid from the solicitors` compensation fund.
[229] ibid. Precedents already exist for such third party escrow arrangements: UK barristers for example may use the BARCO system as they are prohibited from holding client money, and French attorneys already utilise the Carpa escrow system.
[230] ibid.
[231] ibid 5.
[232] ibid 6. It should be noted that law firms do benefit from cheaper loan and overdraft facilities as a consequence of operating their client accounts with the same bank.

whether no longer operating a client account would have any impact on the money laundering risk to their firms.

(a) The Absence of a Client Account Makes No or Minimal Difference to Money Laundering Risk

Many participants expressed the view that no longer holding a client account would have no or little effect in terms of reducing money laundering risks to their firms. This view was attributable in part to the way in which the `arrangement` offence set out in s 328 POCA 2002 operates to criminalise legal professionals who become `concerned` in an arrangement which facilitates money laundering on the part of their clients. [233] The effect of this drafting is that law firms will become involved in facilitating arrangements when they effect transactions, regardless as to whether funds pass through the law firm`s client account or not. This point was emphasised by the compliance participant who stated:

> If we were going to get involved in a money laundering scandal inadvertently, we'd have been involved by facilitating the deal first and foremost, not because the money came in and the money went out.[234]

Several other participants viewed client account involvement as a collateral issue on the basis that:

> . . . money`s either good money or it's not, the fact that you're then operating the account is probably just perpetuating a bad situation rather than creating a bad situation.[235]

This stance was expanded on by several participants who were of the view that robust CDD and source of funds checks should militate against illicit funds flowing through client account. As one MLRO reflected:

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[233] POCA 2002, s 328(1) criminalises any person who ` enters into or becomes concerned in an arrangement which he knows or suspects facilitates (by whatever means) the acquisition, retention, use or control of criminal property by or on behalf of another person.`

[234] Compliance Interview 18 dated 08/04/16.

[235] Transactional Interview 15 dated 08/12/15.

> I think the risk is not so much having a client account, it's what steps you take to ensure as best you can that what comes into the client account is clean, so I think . . . the tests are earlier.[236]

Hence the dominant view of many participants was that the client account money laundering risk was almost a secondary concern in terms of legal professional liability for an `arrangement` offence, on the basis that such liability will accrue in any event due to the legal professional`s involvement in the transaction.

Some participants, however, did feel that the lack of a client account would decrease their firm`s money laundering risk, acknowledging that, `historically those accounts have been used to clean the money up`.[237] This view was typically confined to those instances where a legal professional is knowingly complicit in laundering. This fatalism with regard to deliberate launderers is best summarised by the compliance officer who said:

> I think if you're corrupt and wanting to do something with your account that you know you shouldn't, then you will do that, and therefore taking that away will help.[238]

(b) Lack of Client Account Makes Transactions More Cumbersome

Many participants reported that the lack of a client account would make commercial transactions harder to effect in practical terms or would be, in the words of several participants, `a nonsense`, `a nuisance` and a `daft idea`.[239] As one partner commented, `it is very difficult to operate effectively without a client account`, with another MLRO adding that, `it would slow down the process of the law something terribly`.[240]

A number of transactional participants raised the use of solicitors` undertakings as a key feature of many commercial transactions, which necessitate the retention of

[236] Compliance Interview 15 dated 10/03/16.
[237] Transactional Interview 20 dated 11/03/16.
[238] Compliance Interview 2 dated 24/11/15.
[239] Compliance Interview 8 dated 14/12/15, Transactional Interview 18 dated 16/12/15 and Compliance Interview 20 dated 16/06/16.
[240] Compliance Interview 12 dated 26/02/16 and 3 dated 25/11/15.

a client account.[241] Solicitors` undertakings are commonly used in transactions where a solicitor undertakes to another solicitor to perform a specified act, typically transmitting funds on satisfaction of the conditions precedent to a transaction. Failure to comply with an undertaking will constitute a breach of the SRA Code of Conduct and may result in disciplinary censure, as well High Court enforcement action.[242]

This focus on the operation of solicitors` undertakings in practice was drawn out by a transactional partner who commented:

> . . . lawyers can give undertakings and other lawyers accept an undertaking . . . They know absolutely they can rely on that, it`s as good as cash – now are you going to get that from third party escrow providers, `cos they're not under the same professional rules – I don't think so.[243]

It is crucial therefore that a solicitor gives undertakings within their control, which would remain the case in respect of a law firm`s client account, but would not be the case in respect of a third-party escrow account requiring dual authorisation from both the client and solicitor prior to any funds transfer.

(c) Lack of Client Account Shifts Money Laundering Risks Elsewhere

The previous quotation touched upon the professional conduct rules which lawyers are subject to, and the professionalism of lawyers was a further aspect participants raised when considering money laundering risks and the client account. A number of participants felt that legal professionals would be better placed to view transactions holistically and identify potential laundering. This is in contrast to banks or third party escrow providers acting as a mere conduit for funds, without

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[241] An undertaking is defined by the SRA as ` a statement, given orally or in writing . . . made by or on behalf of you or your firm, in the course of practice . . . to someone who reasonably places reliance on it, that you or your firm will do something or cause something to be done, or refrain from doing something.` See SRA , *SRA Handbook* (Version 18, 2016), Glossary.

[242] See, SRA, *SRA Handbook* (Version 18, 2016) SRA Code of Conduct 2011, Outcome 11.2 which requires that, `you perform all undertakings given by you within an agreed timescale or within a reasonable amount of time`.

[243] Transactional Interview 8 dated 26/11/15.

exposure to any underlying transactions. The effect of dispensing with the client account is to shift the money laundering risk connected purely to the flow of funds away from the legal profession. This view was articulated by the participant who observed with regard to dispensing with a client account:

> I think it will make life harder because the bank will now be responsible for those money laundering obligations in relation to funds passing through, but without the background and client history that the lawyer will have.[244]

As one MLRO stated in respect of funds flowing through the client account:

> . . . it's probably going to get a lot better scrutiny by a bunch of professionals in this firm than it may have in the bank.[245]

Therefore, whilst the lack of a client account may well decrease the money laundering risks to the legal profession itself, it simply diverts that risk to other entities, namely banks and third party escrow providers, each of whom have less contextual background to transactions. In the words of one MLRO, `aren't you simply passing that risk of money laundering back to the bank?`[246]

(iii) Pooled Client Accounts No longer Qualifying for SDD

One further issue that arises in relation to the client account is whether or not simplified due diligence can be applied to the pooled client account. One of the proposed changes under 4MLD was that PCAs would no longer qualify for simplified due diligence, a move which would see banks having to identify and verify beneficial ownership in respect of every single client whose funds were held in the account, a position which would shift daily, nor would it provide any contextual information to the banks in terms of assessing any money laundering risks. This would also require financial institutions to conduct beneficial ownership checks in relation to funds connected to matters outside the scope of MLR 2007 altogether, such as settlement funds in litigation for example. It is for these reasons

[244] Compliance Interview 6 dated 08/12/15.
[245] Compliance Interview 15 dated 10/03/16.
[246] Compliance Interview 15 dated 10/03/16.

that the Law Society state that the `retention of SDD measures on PCAs is crucial to maintain proportionality`.[247]

This particular issue has received sustained attention throughout the 4MLD transposition process, and the position has shifted multiple times through the consultation process. Removing simplified due diligence for PCAs was vehemently opposed by the Law Society as `unworkable` on the basis that it would `complicate the CDD process while increasing costs with no benefit to the fight against money laundering.`[248] This rationale may be explored further as follows:

> It is the transaction on which the legal professional is advising which will determine whether or not there is a risk of money laundering in respect of the funds being paid into the pooled account.[249]

When contemplating this issue, several participants focused on the practical challenges this position would create for the profession, deemed a `massive problem` by one participant or `a headache nobody wants` and pinpointed by another who said:

> If we don't maintain the exemption, then I think that there are very real challenges for the legal profession because what are we going to have to do? Hold each client's money in a separate client account? Logistically it's huge.[250]

Flowing from this debate, fears have been raised that banks may well de-risk by declining to operate PCAs if the SDD exemption is no longer applicable, a trend which has already been witnessed elsewhere in the banking sector, particularly in

[247] The Law Society, *HM Treasury consultation on the transposition of the Fourth Money Laundering Directive: The Law Society Response* (2016) 7.
[248] ibid 5-8. The Society also note that resources could be diverted away from higher risk areas to address PCA issues.
[249] ibid.
[250] Compliance Interview 18 dated 08/04/16; Compliance Interview 6 dated 08/12/15; Compliance Interview 12 dated 26/02/16.

relation to the de-risking of accounts held by charities.[251] Despite the extensive, albeit shifting, debates on SDD and PCAs during the 4MLD transposition process, hardly any participants thought that the banks would actually de-risk PCAs in practice. Many participants either had no view on de-risking or did not perceive it as a likely outcome. Some participants felt that banks would not de-risk on the basis that loss of client account business would also result in the bank`s loss of profit-making facilities made to law firms such as loans and overdraft facilities.[252]

One participant positioned the debate over SDD in a political context, framing the issue in the same way that attempts to seek exclusions from POCA 2002 or removal of criminal sanctions from MLR 2007 have been framed by a number of participants earlier in the thesis. Referring to the UK`s National Risk Assessment in 2015, the participant noted:

> I think the problem that now comes is it is difficult for Treasury to be able to say `yes we should be able to apply simplified due diligence to pooled client accounts` while at the same time indicating that law firms are the third highest risk.[253]

These shifting debates have culminated in the hybrid position set out in the MLR 2017. Under Regulation 36(4), PCAs no longer *automatically* qualify for SDD. Rather, SDD is only available by applying a risk-based approach.[254] Such a position was reached by the government on the basis that there was `no consensus` as to

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[251] FCA, `FCA Research into the issue of de-risking` (*FCA*,24 May 2016)< https://www.fca.org.uk/news/news-stories/fca-research-issue-de-risking> accessed 14 April 2017. See also, The Law Society, *HM Treasury consultation on the transposition of the Fourth Money Laundering Directive: The Law Society Response* (2016) 7.

[252] Compliance Interview 19 dated 24/05/16; Transactional Interview 19 dated 10/03/16.

[253] Compliance Interview 6 dated 08/12/15.

[254] MLR 2017, reg 36(4) states that, `A relevant person may apply simplified customer due diligence measures where the customer is an independent legal professional established in an EEA state and the product is an account into which monies are pooled (the "pooled account"), provided that:

(a) the business relationship with the holder of the pooled account presents a low degree of risk of money laundering or terrorist financing, and
(b) information on the identity of the persons on whose behalf monies are held in the pooled account is available, on request (and at the latest within two working days of the day on which the request was made) to the institution where the pooled account is held.`

whether PCAs were always low risk and that, `the risks were as high or low as the quality of the firm`.[255] Therefore the issues raised above are of enduring relevance in that banks may conclude their law firm customers do not qualify for SDD. Whether the de-risking phenomenon, as observed in the charity sector, then occurs in the legal sector remains to be seen.[256]

(iv) Concluding Comments on the Client Account

A small majority of participants reported that clients *had* unsuccessfully attempted to use the client account as a banking facility, either on the basis of commercial efficacy or in the belief that client account services formed part of a wider client care package. Several participants reported challenges surrounding establishing whether there was an underlying transaction in some cases. A curious dynamic arises here - participants were acutely alive to the money laundering risk presented by the client account and yet only a tiny minority of participants perceived attempts to use the client account as a banking facility as potential money laundering. In most cases it was simply perceived as an attempt to channel money via the most efficient route possible.

In the author`s view, the client account should be retained, a view echoed by the compliance participant who said, `I think to get rid of client accounts you're using a sledgehammer to crack a nut.`[257] Many participants felt that dispensing with the client account will do little in any event to decrease any liability attaching to legal professionals in respect of any `arrangement` offence under s 328 POCA 2002 : such liability will attach in any event due to the legal professional`s overarching involvement with any given transaction. Moreover, its lack would make transactions more difficult to effect in that third-party escrow providers require dual authorisation from both the law firm and the client to effect a funds transfer, adding a layer of cost and complexity to transactions. In addition, many transactions are customarily completed using solicitors` undertakings to transfer

[255] HM Treasury, *Money Laundering Regulations 2017: consultation* (2017) para 3.4.
[256] James King, `How Derisking Became a Humanitarian Issue` (2017) 180 (1093) Banker, 48; See, generally, Amber Scott, `If Banks Can`t Solve the Derisking Dilemma, Maybe the Government Will` (2015) 180(60) American Banker.
[257] Compliance Interview 14 dated 10/03/16.

funds on completion, which solicitors would no longer be willing to provide in respect of accounts which were not exclusively under their control.

At a wider societal level, the loss of the client account would see funds flowing exclusively through entities less able to assess whether money laundering was a feature of those transactions, namely banks and third-party escrow providers. Arguably then, the loss of the client account could serve to increase the money laundering risk across other sectors. Neither banks or third party escrow providers have the holistic oversight on transactions that law firms do and may be less able to identify potential laundering whilst acting as a mere conduit for funds.

What is crucial with regard to the operation of the client account is that sufficiently robust CDD measures are undertaken and the source of funds identified to curtail any instances of illicit funds reaching the account in any event. Both these topics were explored in detail earlier in this Chapter.

With regard to simplified due diligence and the client account, the position reached under Regulation 36(4) MLR 2017 is that those in the regulated sector must determine whether or not SDD can be applied to PCAs in respect of each law firm client. Whether this means that the de-risking phenomenon witnessed in the charity sector becomes a feature of the legal sector remains to be seen.

11. Chapter Summary

The CDD challenges raised by participants were shaped by the international, frequently global, nature of their businesses. Operating on an international basis gave rise to a number of jurisdictional issues, together with the requirement to comply with an array of AML regimes across multiple jurisdictions. A number of firms elected to apply UK CDD globally, even where such obligations were more onerous than local laws. Thereafter, ongoing monitoring was seen as a crucial part of the AML regime.

The beneficial ownership requirements under the UK AML regime spawned an array of issues for participants both in terms of cost and time, with the beneficial ownership challenge exacerbated in respect of jurisdictions with less extensive

disclosure obligations. The majority of participants had no view, were ambivalent, or found the 25% beneficial ownership threshold satisfactory. Such ambivalence may be attributable to the fact that a percentage threshold may not definitively reveal the underlying controllers of an entity in any event. Furthermore, it was acknowledged that truly committed launderers will inevitably circumvent any beneficial ownership regime in place, and that constant changes in beneficial ownership which are part of the operation of a legitimate economy means that such information is difficult to keep up to date.

Despite these challenges, beneficial ownership transparency may be enhanced in a number of ways. Nominee shareholdings, for example, may be dispensed with, with the exception of narrowly defined categories such as those trading in listed securities. In addition, a move towards global transparency is required, building upon those centralised registers of beneficial ownership currently in place across the EU under the aegis of, inter alia, 4MLD.

One of the changes effected by MLR 2017 is that law firms must make their own determination as to which clients qualify for SDD, the preordained categories under MLR 2007 having been dispensed with. As the SDD position was yet to be determined at the time of the interviews, it was not possible to ascertain the views of participants on this aspect of the regime. Nevertheless, it is the author`s view that particularly risk averse law firms may well elect to apply standard CDD on all clients in preference to the potential erroneous application of SDD provisions.

The inclusion of domestic PEPs within the scope of MLR 2017 was of little concern to participants, many of whose firms operated internationally and therefore made no distinction between domestic and foreign PEPs in any event. The implementation of a risk-based approach to the application of EDD with regard to PEPs has only partially addressed the concerns raised by both participants and the Law Society.

Participants reported that obtaining source of funds and source of wealth information was both a difficult and sensitive matter. This exercise was more challenging in the absence of clear parameters within MLR 2007, or within Law

Society guidance, although it was acknowledged that the infinite permutations in transactional fact patterns meant that each law firm was required to make a judgement call with regard to such matters.

There is also a dearth of guidance with regard to those funds potentially tainted by prior criminality. The author is of the view that the wording of MLR 2007 and related Law Society guidance do not require law firms to carry out detailed investigations into prior criminality. This is not to suggest a lax approach however, given the potential criminal liability that may attach to lawyers under the substantive money laundering offences, or a failure to disclose offence under POCA 2002.

Whilst law firms are required to understand where the source of funding is coming from on a transaction, they are not technically required to apply CDD to third-party funders. This was identified as a potential vulnerability in the regime, which prompted a number of participants to elect to apply CDD on third-party funders.

The reliance provisions set out in Regulation 17 MLR 2007 and Regulation 38 MLR 2017 are infrequently used by the profession. This is attributable to the fact that the relying party retains criminal liability for any CDD failings, and parties being relied upon may be liable in tort and are required to update the CDD information they supply. It is the author`s view that reliance provisions should be used sparingly in any event, on the basis that each law firm has its own unique risk appetite and parameters.

AML training was a highly valued aspect of practice, and a desire for bespoke training was expressed frequently. The dearth of money laundering examples relevant to those law firms from which participants were drawn was raised as an issue. This finding accords with the repeated calls from the profession for improved information sharing between law enforcement agencies and the regulated sector. Improved information sharing of relevant case studies may then cascade down to the profession via AML training, thus enhancing the effectiveness of the regime.

A small majority of interviewees stated that their clients had unsuccessfully attempted to use the client account as a banking facility. Nevertheless, in most cases this was perceived as an attempt to route money in the most efficient manner possible rather than as potential money laundering.

Many participants felt that the lack of a client account would make transactions harder to effect given that solicitors would no longer be willing to provide undertakings in respect of the transfer of completion monies, and that using third-party escrow providers requiring dual authorisation from law firms was less efficient. Moreover, lawyers would still be caught by the `arrangement` offence under s 328 POCA 2002, even in the absence of a client account. The lack of a client account may also have the effect of shifting money laundering risks to entities, such as banks or third-party escrow providers, lacking the holistic oversight that law firms have on transactions, and therefore less able to spot potential money laundering.

One final aspect with regard to the client account remains, namely the lack of availability of automatic SDD with regard to law firm pooled client accounts under Regulation 36(4) MLR 2017. The effect of this is that the legal sector may well become subject to the de-risking phenomenon already seen within the charity sector.

This Chapter has explored the many disparate mechanical aspects of the UK AML regime as they apply to legal professionals during the course of day to day practice. The subsequent data chapter will consider a further key weapon in the fight against money laundering, the SARs regime, under which lawyers must report their knowledge or suspicions of money laundering to the NCA.

Chapter 6 - The Suspicious Activity Reporting Regime

The previous chapter focussed on some of the mechanical aspects of the UK AML regime surrounding CDD, AML training and the client account. The focus in this Chapter is on one of the `central` weapons in the UK`s AML armoury, that of the SARs regime.[1] Under this regime, legal professionals are obliged to report their knowledge or suspicions of money laundering, on the basis that such SARs have `the potential to be a critical intelligence resource`.[2] Thereafter, with an exploration of the compliance issues relating to the mechanical aspects of the AML regime complete, Chapter 7 will then highlight the perceptions that participants had of the UK AML regime in practice.

1. Background to the SARs Regime

The SARs regime is the `end-to-end system by which industry spots suspicious activity related to money laundering . . . and reports this` to the NCA.[3] On receipt, SARs are logged onto the NCA database, mined for information, and disseminated to law enforcement agencies in order to be able to commence or enhance money laundering investigations.[4]

A detailed account of how the SARs regime under POCA 2002 operates is set out in Chapter 2 of the thesis. In summary, it may be recalled that the mechanism features two complementary strands. Under the first strand, known as the `consent regime`, where a legal professional deals in some manner with criminal property, a report may be made by way of `authorised disclosure` under s 338 POCA 2002. This scenario may arise during the course of a client retainer where underlying criminality on the part of a client potentially triggers a s 328 `arrangement` offence on the part of the lawyer. The report is made initially to the firm`s MLRO, who will

[1] Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* (2016) 12.
[2] ibid.
[3] NCA, `The SARs Regime` (*NCA*) http://www.nationalcrimeagency.gov.uk/about-us/what-we-do/economic-crime/ukfiu/the-sars-regime accessed 13 September 2017.
[4] ibid.

then determine whether or not to make an external SAR to the NCA. Depending on the timing of the SAR, NCA consent may then be obtained to continue with the transaction, with such consent being provided either by way of actual or deemed consent from the NCA.[5] Such disclosure (and any `appropriate consent`) then acts as a complete defence to the substantive money laundering offences set out in s 327-9 of the Act.[6] Since June 2016, the NCA have been referring to such requests as DAML Requests (defence to a money laundering offence).[7] At the time of the interviews however, and during the consultation process relating to 4MLD, the phrase `consent regime` was the dominant term of art, and is therefore retained in this thesis.

There is a complementary but distinct strand in the form of the `failure to disclose` offences set out in s 330/1 POCA 2002, which does not seek consent to continue with a transaction, but simply requires legal professionals in the regulated sector to report their knowledge or suspicions of money laundering activity to their MLRO, who in turn determines whether or not to make an external SAR to the NCA.[8] In the alternative, a negligence-based objective element is introduced in these sections, imposing a requirement to report where there are `reasonable grounds for knowing or suspecting` someone is money laundering.[9] The inclusion of the objective limb in the `failure to report` offences serves a dual purpose in that it imposes both a `higher standard of diligence` upon the sector, and addresses `negligence and wilful blindness` on the part of lawyers.[10]

A number of concerns have been raised in recent years with regard to legal sector SARs however, relating to the decline in both number and quality of SARs

[5] For actual consent provisions see POCA 202, ss 336(1) and (2). For deemed consent provisions see s 336(3)ff.
[6] POCA 2002, ss 327(2)(a),328(2)(a) and 329(2)(a).
[7] NCA, *Requesting a defence from the NCA under POCA and TACT* (2016).
[8] POCA 2002, s 330(2(a), s 331(2)(a); see also Ch 2, `Failure to Disclose in the Regulated Sector`.
[9] POCA 2002, s 330(2)(b), s 331(2)(b).
[10] CPS, `Proceeds Of Crime Act 2002 Part 7 – Money Laundering Offences` (*CPS*,2010) < http://www.cps.gov.uk/legal/p_to_r/proceeds_of_crime_money_laundering/#Section_327_offence> accessed 22 August 2017; Miriam Goldby `Anti-money laundering reporting requirements imposed by English law: measuring effectiveness and gauging the need for reform` [2013] JBL 367, 371.

submitted by the sector. Both these aspects of the SARs regime will now be examined.

(i) Decline in Number of Legal Sector SARS

The SRA AML review stated that generally there was compliance with the reporting regime under POCA 2002.[11] Notwithstanding this overall portrait of compliance put forward by the SRA, the first area of concern presented in relation to legal profession SARs is a decline in the number of SARs submitted to the NCA by solicitors over the years, falling from 6,460 in 2007/8 to 3,328 in 2012/3 (albeit with a slight increase to 3,461 in 2014/5 constituting under 1% of all SARs).[12] The legal sector is not the only sector in which there has been a decline in the number of SARs, and the NCA data for the accountancy sector also demonstrates a significant decline in SARs submitted by that sector, from 7,354 in 2007/8 to 4,834 in 2013/4.[13] This decline in the number of legal sector SARs does, however, sit in contrast to an overall national increase in the numbers of SARs submitted year on year.[14] This concern over the decline in number of legal sector SARs is one which has also been raised in the NRA 2015.[15]

In response, multiple factors for this reduction have been cited by law firm MLROs, including a general decrease in transactional work following the financial crisis, shifts in client demographics and changes in tax legislation.[16] For their part, the NCA do acknowledge that the reduction in SARs is partially attributable to a general decline in transactional work, both in terms of mergers and acquisitions and

[11] SRA, *Anti Money Laundering Report* (2016) 30.
[12] ibid 32; see SOCA, *The Suspicious Activity Reports Regime Annual Report 2008* (2009) 40 for 2007/8 figures; see NCA, *Suspicious Activity Reports Annual Report 2014* (2015) 45 for 2013/4 figures; see NCA, *Suspicious Activity Reports (SARs) Annual Report 2015* (2016) 11 for 2014/5 figures.
[13] SRA, *Anti Money Laundering Report* (2016) 32; see SOCA, *The Suspicious Activity Reports Regime Annual Report 2008* (2009) 40 for 2007/8 figures; NCA, *Suspicious Activity Reports (SARs) Annual Report 2014* (2015) 44 for 2013/4 figures.
[14] NCA, *Suspicious Activity Reports (SARs) Annual Report 2015* (2016) 6.
[15] HM Treasury and Home Office, *UK national risk assessment of money laundering and terrorist financing* (2015) paras 6.91 and 6.92.
[16] SRA, *Anti Money Laundering Report* (2016) 32,33.

residential conveyancing.[17] The reduction may also be a by-product of the maturity of the regime, bringing with it a better understanding of the AML legislation and the accompanying parameters of privilege, better client on boarding processes and less defensive reporting.[18] A number of MLROs were also of the view that the decline in legal sector SARs reflected a dampening down of risk appetite within law firms, whereby firms decline to act on suspicious or high risk transactions. [19] In some instances, however, it may simply denote poor practice and lack of skill or judgement on the part of an MLRO.[20]

(ii) Poor Quality Legal Sector SARs

In addition to concerns over a decline in the number of legal sector SARs, the NCA have repeatedly voiced concern over the poor quality of SARs submitted to them from the legal sector, with the director of the NCA`s Economic Crime Command Donald Toon even identifying the sector as `the worst offenders for submitting unsatisfactory suspicious activity reports`.[21]

In 2014 the SRA were asked by the NCA to provide guidance on submitting consent SARs following an NCA sample of 952 legal sector consent requests over a four

[17] NCA, *Suspicious Activity Reports Annual Report 2014* (2015) 12.
[18] SRA, *Anti Money Laundering Report* (2016) 32. A `small number` of MLROs displayed poor understanding of the crime/fraud exception to LPP, 33.
[19] ibid.
[20] See comments in HM Treasury and Home Office, *UK national risk assessment of money laundering and terrorist financing* (2015) para 6.96 where the report identifies as a `principal risk` those `negligent legal professionals' failure to comply with their obligations under POCA and the regulations leading to failure to conduct effective due diligence and identify suspicious activity.`
[21] For comments of Donald Toon see Jonathan Rayner, `Solicitors `prickly` - economic crime chief` (*The Law Society Gazette*, 20 November 2014)< https://www.lawgazette.co.uk/news/solicitors-prickly-economic-crime-chief/5045241.article > accessed 18 January 2017; the NCA have issued a series of guidance notes in relation to the submission of SARs. The SARs Twice Yearly Reporter Booklets produced by the NCA and aimed at reporters also details advice on submitting better SARs.

month period.[22] The review revealed various issues, namely: (i) there was, in fact, no prohibited act under s 327-9 POCA 2002 requiring consent (14%), (ii) additional information was required in order for the NCA to make a determination, such as the basis for the suspicion or failure to identify the launderer (33%), and (iii) difficulties in contacting the reporter (24%).[23] SARs guidance has been available to the profession prior to this in each iteration of the Law Society`s AML practice notes, and the NCA have also issued a series of guidance notes in relation to the submission of SARs. Despite this flurry of guidance from multiple sources, the NCA still reported that as many as 42% of legal sector consent SARs were incomplete and that some SARs even `indicated a lack of understanding or compliance` with the AML regime.[24] From October 2014, the NCA began to return consent SARs submitted with insufficient detail to reporters, without granting or withholding consent. [25] Consequently, the SRA raise the concern that lawyers may well take a risk and fail to resubmit a returned consent request.[26] Following the adoption of this procedure, 408 consent requests across all sectors were simply returned to reporters (2.8% of all SARs from all sectors) in the 2014/5 reporting period.[27]

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[22] SRA, `Making consent requests less painful` (*SRA*,10 July 2014) < https://www.sra.org.uk/sra/news/press/compliance-news-08-ukfiu-consent-requests.page>accessed 12 September 2017.

[23] ibid.

[24] ibid; see NCA, *Suspicious Activity Reports Annual Report 2014* (2015) 13, 27,28 where the NCA liaised with the SRA and the Law Society with regard to poor quality SARs: see also HM Treasury and Home Office, *UK national risk assessment of money laundering and terrorist financing* (2015) para 6.93.

[25] NCA, *Closure of cases requesting consent* (2014).

[26] SRA, *Anti Money Laundering Report* (2016) 34; see NCA, *Closure of cases requesting consent* (2014). In relation to Home Office awareness campaign see HM Treasury and Home Office, *UK national risk assessment of money laundering and terrorist financing* (2015) para 6.82. The SRA issued a Warning Notice to the profession in December 2014 in relation to poor quality SARs, see SRA, `Money laundering and terrorist financing – suspicious activity reports` (*SRA*, 8 December 2014) <http://www.sra.org.uk/solicitors/code-of-conduct/guidance/warning-notices/Money-laundering-and-terrorist-financing---suspicious-activity-reports--Warning-notice.page> accessed 18 January 2017. The legal sector are earmarked as a `priority sector` see NCA, *Suspicious Activity Reports (SARs) Annual Report 2015* (2016) 14 and 19.

[27] NCA, *Suspicious Activity Reports (SARs) Annual Report 2015* (2016) 15. Improving the quality of SARs remains one of the ongoing key areas that fall within the remit of the NCA-run SARs Regime Committee, a committee which is composed of representatives from AML supervisors, the regulated sector and law enforcement agencies to improve the regime.

Reform of the SARs regime was given much prominence in the government`s AML Action Plan published in 2016 (Action Plan 2016), in response to the findings relating to the regime in the NRA 2015.[28] The proposals, which will be explored throughout this chapter, suggested a move away from transactions based reporting to a focus on high risk entities, the removal of the consent regime, and an upgrade of the NCA`s capabilities.[29] The Plan also highlighted the need for an improved IT system, better analysis of SARs, and improved information sharing, all of which were identified as issues by participants.[30]

It is set against this background that participants were asked for their views on the operation of the SARs regime. An overarching caveat applies here, as it does to all the data chapters of this thesis. As explored in the methodology chapter, the responses from participants provide insights on the regime through a very distinct lens, that of professionals within Top 50 law firms, some of whom have a vested interest in the regime by virtue of their roles. It is also research conducted by an `insider`, which shapes and informs both data generation and analysis. It is in this overarching context that participants` responses must be read.

In terms of structure, this Chapter will address the issues participants raised with regard to the regime in general, prior to a consideration of the consent regime in particular.

2. Participants` Experience of the SARs Regime

The majority of participants reported that they had no issues with regard to the non-consent element of the SARs regime: that is SARs made pursuant to s 330/1 POCA 2002. In addition, a majority of participants had no suggestions as to how the

[28] Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* (2016) 5. The Action Plan 2016 included the findings from the Home Office, *Suspicious activity reports regime: call for information* (2015) at Annex B.
[29] ibid paras 2.7, 2.8 and 2.9.
[30] ibid paras 2.9, 2.10 and 2.11.

non-consent SARs regime could be improved. Such responses must be treated with extreme caution however, as many of the participants who reported having no issues or no views on improvements were transactional participants who had never used the SARs regime in practice. A number of features of the regime were highlighted by participants as set out below.

(i) Excluding Minor Offences and Regulatory Breaches from the ambit of POCA 2002

One of the main issues participants raised with regard to the UK`s AML regime as a whole was the disproportionate effect that the `all crimes` approach of POCA 2002 had in practice. This was an issue that was explored in detail in Chapter 4. To summarise briefly here: the majority of participants expressed the clear view that minor offences and regulatory breaches attracting criminal sanctions should be excluded altogether from the ambit of the Act, with virtually all participants performing a compliance role holding this view. Removing such `technical` offences from the ambit of the Act would streamline the SARs regime insofar as it relates to the legal profession, as SARs would no longer need to be submitted in respect of such offences.

(ii) The Meaning of Suspicion

POCA 2002 imposes reporting obligations on the legal profession in respect of their knowledge or suspicions of money laundering, with s 330 adding in a series of preconditions to making an internal report to the MLRO. Whilst `knowledge` is interpreted by the courts as actual knowledge, judicial guidance from *R v Da Silva* provides that `suspicion` is a purely subjective concept which means `a possibility, which is more than fanciful, that the relevant facts exist. A vague feeling of unease would not suffice`.[31] Reporting on the basis of suspicion imposes an extremely low reporting threshold upon the profession, a position noted by a handful of

[31] *R v Da Silva* [2006] EWCA Crim 1654, [2006] 4 All ER 900 [16].

participants, one of whom confirmed, `when I`m looking at whether or not I`m suspicious, I do think it's a really low bar`.[32] Several compliance participants also drew a distinction between a suspicion comprising a `wild concern` or `speculation`, and a suspicion which is reportable under the provisions of s 330/1 POCA 2002. Whilst a small number of participants observed that suspicion was a low reporting threshold, none of those participants expressed the desire for the definition to be changed. This sits in contrast to the responses from the government`s Call for Information on the SARs Regime, which reported that many respondents `wanted strengthening of the definition of "suspicion", to allow better judgements to be made.`[33]

Participants` views were canvassed as to their interpretation of the word `suspicion` in practice, a word which, according to Arora and Stokes, `nimbly defies precise identification in practical terms`.[34] A number of participants automatically referred to the *Da Silva* guidance as their working definition, such as the compliance participant who commented, `it means what it says on the page for me.`[35] It is noteworthy however, that all but one of these participants were compliance participants, some of whom had an active role in training their firm`s fee earners. It may be the case therefore, that such participants encounter the *Da Silva* guidance on a regular basis as part of their day to day practice. As one participant recounted, `I'm so used to parroting out in training . . . that suspicion is a "possibility that is more than fanciful that the relevant facts exist".` [36]

(a) Suspicion As Instinct

For a small majority of participants, their concept of suspicion was determined by reference to instinct as a starting point. Many participants linked suspicion to a

[32] See, for example, Robert Stokes and Anu Arora, `The duty to report under the money laundering legislation within the United Kingdom` [2004] JBL 332; Compliance Interview 6 dated 08/12/15.
[33] Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* (2016) Annex B.
[34] Robert Stokes and Anu Arora, `The duty to report under the money laundering legislation within the United Kingdom` [2004] JBL 332, 353.
[35] Compliance Interview 18 dated 08/04/16.
[36] Compliance Interview 14 dated 10/03/16.

sense of `gut wrenching`, a `gut instinct` or `gut feel`.[37] As one Deputy MLRO commented, `you *know* when it doesn't feel right . . . and it's a gut feeling, you know, it's an instinct.`[38] Other participants continued with this instinctive interpretation of suspicion as a concept as determined by reference to the `sniff test`, the `smell test` or where something `doesn`t smell right`.[39] In the words of one participant, suspicion is where `something is fishy, smells like it`s something that is not quite right.`[40]

(b) The Fact Pattern of Each Transaction

It is important to note that this instinctive measure of suspicion was seen by many participants simply as a starting point on the continuum ultimately leading to a SAR. A number of participants highlighted discrete aspects of practice that would automatically arouse suspicion including, inter alia, last minute changes to or unusual sources of funding, defensive clients, or clients unwilling to provide CDD information.[41] For a number of other participants however, suspicion was inextricably linked to the fact pattern relating to each particular retainer. As one MLRO expanded on this aspect of the suspicion continuum:

> . . . you`ve got to have the whole knowledge of the background of the matter and the clients, the money, the transaction, to get a real sense of . . . whether you`re suspicious.[42]

This view was reiterated by the participants who reflected, ` it's how all the different bits and pieces interplay and how you feel` or a `combination of circumstances` that will ultimately determine whether a suspicion is raised.[43]

[37] Compliance Interview 10 dated 15/12/15; Compliance Interview 17 dated 08/04/16; Transactional Interview 9 dated 26/11/15 and Transactional Interview 12 dated 01/12/15.
[38] Compliance Interview 9 dated 15/12/15 (emphasis added).
[39] Transactional Interviews 10, 6 and 17 dated 26/11/15, 25/11/15 and 16/12/15.
[40] Compliance Interview 7 dated 08/12/15.
[41] Transactional Interviews 17 and 11, Compliance interview 11 and Transactional Interview 4 dated 16/12/15, 26/11/15, 19/02/16 and 20/11/15.
[42] Compliance Interview 10 dated 15/12/15.
[43] Compliance Interview 2 dated 24/11/15; Transactional Interview 5 dated 25/1//15.

This generalised sensitivity in relation to the specific facts of each retainer cascaded down to each practice area. At the practice area level, many participants stated that they would be suspicious if a particular transaction was both `out of the ordinary` or `not stacking up` for that practice area and/or without a credible commercial rationale driving such departure from market norms.[44] This dynamic is best represented by the partners who reported that their suspicions would be roused where a transaction was both `unusual and inexplicable`, or where there was `a transaction structure that`s different from the norm for no obvious reason.` [45] This connection between market practice and suspicion was deconstructed further by the practitioner who said:

> We act in a market where there is accepted market practice the way lots of things are done, so I suppose it would be something that is not in accordance with what is market, or it would be without any coherent explanation as to why we`d be doing it differently.[46]

What the market norms are for each practice area will also differ, as was highlighted by the participant who recounted:

> . . . there are some structures . . . in my world which are, to me, totally unsuspicious but if somebody who didn't understand them saw them they'd say ` . . . what on earth is going on here!`[47]

Where a transaction is out of the ordinary then, the seeds of a suspicion may be formed in the mind of a practitioner. As with the instinctive interpretations of the word `suspicion` encountered above, an unusual transaction may well provide a starting point for further enquiry. This feature was explored by the compliance participant who explained in relation to transactions that:

[44] Compliance Interview 4 dated 03/12/15; Transactional Interview 1 dated 18/11/15.
[45] Transactional Interviews 5 and 1 dated 25/11/15 and 18/11/15.
[46] Transactional Interview 18 dated 16/12/15.
[47] Transactional Interview 5 dated 25/11/15.

> . . . `not usual`, nothing wrong with that , you have no reporting obligations because something is unusual, but if it's unusual and *can't be explained* you then need to question whether or not it's pushing you into suspicious.[48]

Where a transaction is unusual, however, a number of participants referred to then making an assessment as to the credibility of the explanations clients proffered. This scenario was explained by the compliance participant who said:

> It`s a kind of suspicion, cause for concern continuum, you either ask the questions, you get a credible explanation and your concern falls away, or you raise it to the level of suspicion.[49]

This was echoed by the compliance participant who added, `if you ask and the answer you get doesn`t make sense, you need to question what you`re doing.`[50] A small number of participants expressed concerns however, as to whether subtle suspicious activity would penetrate their consciousness during the course of a transaction, with one such participant questioning, `would it really be on my radar?`.[51]

(c) The Interplay Between Suspicion and Experience

A number of participants highlighted the value of experience in terms of refining their suspicions. For some participants, whether initial suspicions were aroused or not was an aspect of practice `built on very many years` experience.`[52] This prompted one MLRO to conclude that, ` suspicion is . . . the accumulation of experience over the years.`[53] The value of experience was also highlighted by another MLRO who reflected:

[48] Compliance Interview dated 6 dated 08/12/15 (emphasis added).
[49] Compliance Interview 12 dated 26/02/16.
[50] Compliance Interview 6 dated 08/12/15.
[51] Transactional Interview 15 dated 08/12/15.
[52] Compliance Interview 12 dated 26/02/16.
[53] Compliance Interview 3 dated 25/11/15.

> I think this is why it`s useful that someone like me who`s relatively older in age and experience to do this sort of job because you develop a sort of second sense about things.[54]

Similarly for a number of transactional partners, the value of experience was highlighted, whereby a sensibility in terms of being suspicious `just comes with experience and awareness.`[55] As one partner reflected:

> I think the one thing you hope is over the years you kind of build up an innate sense of what`s right and wrong.[56]

(d) The Implications of the Meaning of Suspicion

What then are the implications of a concept of suspicion which is guided for the majority of participants by a blend of instinct, specific fact patterns and experience? One implication is that the judicial guidance from *Da Silva* can be seen as an over-definition of the concept of suspicion by the courts. Prior to *Da Silva,* subjective suspicion was reportable. Following the decision however, a subjective suspicion may be reportable or not depending on whether that suspicion is more than a vague feeling of unease. Given that there is no requirement for any objective grounds for forming a suspicion, it then becomes difficult to distinguish between a sense of unease and subjective suspicion. This over-definition by the courts may well serve no practical purpose however, given that the majority of participants determine whether they are suspicious or not according to instinct and experience, with the exception of a number of compliance participants familiar with the guidance in *Da Silva* attributable to their day to day practice. As will be explored later in this Chapter, the prevailing response from participants when faced with any money laundering concerns was to contact the firm`s MLRO rather than explore the semantic parameters of the term `suspicion`.

[54] Compliance Interview 17 dated 08/04/16.
[55] Transactional Interview 16 dated 08/12/15.
[56] Transactional Interview 20 dated 11/03/16.

The link between the specific fact pattern of a transaction and market norms when arousing suspicion also has ramifications, on the basis that an MLRO in receipt of an internal SAR may not have a nuanced level of knowledge with respect to a transaction. This opens up the potential for MLROs to make unnecessary SARs, or fail to make external SARs which ought to be made.

Responses from participants serve to highlight the impact that experience has in terms of raising or dismissing suspicions of money laundering. Much of that experience will be gained over many years whilst undertaking transactions on behalf of clients. However, that instinct may also be refined through a blend of AML training and raising awareness. The way in which the instinctive response to potential money laundering may be refined was set out by the compliance participant who explained:

> What I just want to do is hone the instinct by reminding people about practical everyday examples, which are relevant to their practice, of money laundering, so that they can spot it, so that the little antenna goes up.[57]

(iii) The Crucial Role of the MLRO

Following the formation of a suspicion in the minds of participants, it became evident from the interview data that MLROs assumed a crucial role within the SARs regime, and it is this feature of the regime that will now be explored.

(a) Wholesale Transference of Money Laundering Concerns to the MLRO

As commented upon in the preceding paragraphs, interview responses suggest that many lawyers` automatic response to any money laundering concerns was simply to contact the MLRO or compliance team rather than analyse the semantic parameters of the term `suspicion` and whether or not they met the threshold for a reportable suspicion under POCA 2002. As one transactional participant reflected:

[57] Compliance Interview 9 dated 15/12/15.

> I think you can look at it technically but I think if it doesn`t feel right, it`s worth talking to compliance about it.[58]

Many participants echoed this wholesale transference of the analysis of money laundering concerns to the MLRO at the internal report stage, a process illustrated by the transactional partner who commented `in some ways that makes life easy for me the practitioner because I don`t have to exercise any discretion.`[59]

For their part, this wholesale transference of analysis with regard to internal reporting by transactional lawyers is one which is encouraged by many MLROs and compliance personnel. As one Head of Compliance commented, `we discourage people from analysing their concerns in any legalistic way`, and this sentiment was echoed by several MLROs, one of whose succinct message to transactional lawyers was simply `don`t make the judgement call yourself, whatever you do`.[60]

This transfer of the analysis of money laundering concerns is understandable from the perspectives of transactional lawyers and MLROs alike and it reflects the statutory pathway of internal/external SARs set out in POCA 2002, albeit whilst widening out the concept of suspicion and, where relevant, whether the criteria under s 330 are actually met. From a law firm`s perspective it is highly desirable to identify any actual or potential instances of money laundering and thus avoid reputational damage to the business. From the lawyer`s perspective, making an internal report will discharge their responsibilities under POCA 2002. This was raised by several participants, one of whom commented in relation to internal reports `you know once you do that you avoid the personal liability, you`re off the hook, so why would you want to take the risk?`[61]

Such transference may also be the result of pure pragmatism, particularly in large commercial law firms operating a well-established compliance function, such that AML decisions are simply transferred to those best placed to make decisions

[58] Transactional Interview 8 dated 26/11/15.
[59] Transactional Interview 9 dated 26/11/15.
[60] Compliance Interviews 5 dated 07/12/15; Compliance Interview 12 dated 26/02/16.
[61] Compliance Interview 12 dated 26/02/16.

surrounding reportable suspicions. One transactional partner expressed their rationale in the following terms:

> . . . bring it up to the top of the water and let everyone, you know, discuss it or people who`ve got more experience in it, let them make the decision whether it`s an issue or whether it`s not an issue.[62]

This rationale was echoed by another participant who questioned:

> do you want to lose sleep over it . . . or do you want to speak to the person who actually understands the legislation?[63]

Regardless of the rationale behind it, such transference may be summarised by the participant who noted ` it kind of gets dealt with by the central AML officer – they just take it off and you`re just told what to do – they deal with it`.[64]

The final decision whether to make an external SAR is made by the MLRO - this much is stipulated by POCA 2002 itself and unsurprisingly is widely reflected amongst participants. Thus the MLRO `makes the call on whether it`s fine or not`, such that MLROs are variously referred to in terms of them operating as a `line of defence`, an `escalation point` or a `gatekeeper` by participants. [65]

None of the interview participants expressed any disquiet over the quality of their MLROs and it was clear that they had no reservations about transferring responsibility for reporting AML suspicions to their MLROs. Yet what the interviews do illustrate is that the role of MLRO is far more nuanced than merely acting as a conduit through which internal reports are simply channelled upstream to the NCA. As the following paragraphs demonstrate, the MLRO can actively shape and inform internal suspicions from an objective position, or alternatively dismiss suspicions in their entirety, such that no external report is ever made to the NCA. As participant

[62] Transactional Interview 16 dated 08/12/15.
[63] Compliance Interview 14 dated 10/03/16.
[64] Transactional Interview 20 dated 11/03/16.
[65] Compliance Interviews 17 dated 08/04/16, 1 dated 17/11/15, 10 dated 15/12/15 and 11 dated 19/02/16.

responses suggest a wholesale transference of money laundering concerns to the MLRO, it becomes clear that MLROs hold significant AML power in their hands.

(b) Wrestling with Disclosable Suspicions – the Evolving Conversation

Participants commonly represented the internal report stage in terms of it being an evolving conversation between themselves and the MLRO, some of which involved `quite complex, sometimes detailed debates`, an opportunity to `bat it between sort of MLRO and deputy MLRO and me` or, quite simply, `a bit of a fight!` [66] As one Compliance Officer observed, `I`ve sat with so many people struggling to find out . . . "can you tell me if that`s suspicious?" `.[67] Thus the MLRO may take an active role in forming the boundaries of a reportable suspicion at the internal report stage, with several participants acknowledging that MLROs and compliance officers view AML risks through a distinct lens such that, in the words of one MLRO `we would probably flag many more things than perhaps those in practice would`.[68]

Some transactional participants also reported seeking out the counsel of the MLRO purely as a sounding board, either to validate their instincts or to `feel comfortable that there is nothing there`.[69] The objectivity of the MLRO was highly prized by a number of participants and central to this objectivity was that it transcended client loyalty. This is best illustrated by the MLRO who said:

> I think that our function in a firm like this is to be able to be objective. So we haven`t got an interest in the client, we don`t know the client, we haven`t got an interest in whether or not we take that client on, but we *have* got an interest in making sure we comply with the regulations so therefore we`ve got an objective approach.[70]

[66] Compliance Interviews 10 dated 15/12/15 and 1 dated 17/11/15.
[67] Compliance Interview 2 dated 24/11/15.
[68] Compliance Interview 1 dated 17/11/15.
[69] Compliance Interview 7 dated 08/12/15.
[70] Compliance Interview 19 dated 24/05/16 (emphasis added).

(c) Dismissing Internal SARs

A further crucial aspect of the MLRO`s role is determining that an external report should *not* be made. Dismissing internal suspicions of money laundering was also highlighted as an integral part of the MLRO`s role by some participants, and several MLROs spoke of dismissing internal reports from lawyers that were insufficient to constitute a reportable suspicion. As one participant observed:

> you will have people come to you and say `oh I`m suspicious` then you look at it and go `well, you know, no - there`s not enough there`.[71]

Deciding not to submit an external SAR is a brave decision on the part of an MLRO, given that one of the requirements under POCA 2002 is to report subjective suspicion, where no objective grounds are required. The over definition of the term `suspicion` by the Court of Appeal in *Da Silva* has further complicated the position, requiring MLROs to distinguish between a suspicion which is reportable on the basis that it is more than a feeling of unease, and one which is not.[72]

(d) The Implications of Wholesale Transference of Money Laundering Concerns

The interview data suggests that in practice a remarkable degree of reliance is placed upon the skill and judgement of the MLRO by participants in relation to the reporting or dismissal of their AML concerns. This aligns with the way that POCA 2002 is structured and is therefore an unsurprising finding.

The potential impact of each MLRO`s decisions is highly significant however, both at a firm level and in a wider societal context, given the sheer volume of deals transacted by Top 50 law firms alone.[73] It is crucial therefore that each MLRO makes appropriate AML decisions. Whilst none of the participants expressed any disquiet over the quality of their respective MLROs, some quality issues have been identified across the sector as a whole. The SRA AML review, for example,

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[71] Compliance Interview 12 dated 26/02/16.
[72] *R v Da Silva* [2006] EWCA Crim 1654, [2006] 4 All ER 900 [16].
[73] Top 50 law firms alone recorded deal volumes of £1,021billion in the first half of 2016. See The Law Society, *City Legal Index* (2016) 4.

commented that those MLROs who were either inexperienced or inadequately trained were found to have a `detrimental effect` on the firm`s AML provision.[74] MLROs may therefore constitute `a single point of weakness`.[75] Concerns have also been raised over the decline in number and poor quality of legal sector SARs, both issues which were discussed earlier in this Chapter.

Appointing MLROs to act as a `filter` in the SARs regime is the mechanism provided for in POCA 2002. Yet it opens up a potential vulnerability in the system should the skill of an MLRO prove to be insufficient for the role. The effectiveness or desirability of the wholesale transference of AML decisions to the MLRO is predicated on the skill of that MLRO. The question then becomes one of balance: is the enhanced, but potentially flawed, skill of a single MLRO preferable to the NCA receiving SARS, albeit many of them potentially groundless, from multiple legal professions?

Given the existing reporting structure under POCA 2002, it is imperative that more is done to support and optimise the operation of the MLRO role in practice because of the crucial role they play. A number of potential measures to support this role will be considered later in this Chapter, comprising (i) a bespoke legal sector reporting form, and (ii) improved information sharing between the NCA and legal profession, which could be used to enhance AML training and raise awareness across the sector.

(iv) Defensive Reporting within the SARs Regime

Defensive reporting was not a prominent theme in the interview data, in contrast to the sustained focus it has received for many years, both within academia and at government level. In 2006, an overarching review of the SARs regime by Lander identified defensive reporting as a specific weakness of the regime.[76] A `significant level` of defensive reporting was identified once more as an issue from the

[74] ibid 12 and 14.
[75] SRA, *Anti Money Laundering Report* (2016) 14.
[76] Stephen Lander, *Review of the Suspicious Activity Reports Regime* (SOCA, 2006) paras 35, 52.

responses to the government`s 2015 Call for Information on the SARs Regime.[77] The issue has also attracted the attention of a series of academics including, inter alia, Arora, Stokes, Ryder and Yeoh.[78] As Goldby observes, the reporting requirements under POCA 2002 `encourages the reporting of any and every suspicion no matter how small and insignificant.`[79] The Law Society acknowledge that:

> In many cases, consent requests are made where there is no evidence or knowledge, to ensure protection against the severe consequences set out in POCA.[80]

Defensive reporting was raised specifically as an issue with regard to the `technical` SARs discussed in Chapter 4. However, only a small number of participants went on to refer to it in the more general context of the regime as a whole, such as the MLRO who observed that, `there may be a certain amount now of sort of protectionism.`[81] Even fewer participants referred to defensive reporting within their own practices, one notable exception being the MLRO who acknowledged that, `we are over scrupulous . . . maybe that means we lob in too many [SARs].`[82]

One MLRO was of the view that the maturity of the UK AML regime has resulted in a reduction in defensive reporting by the sector, stating:

> In the early reporting days, there were probably tens if not hundreds more reports being made because everybody was covering backsides and we've

[77] Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* (2016) Annex B.
[78] Robert Stokes and Anu Arora, `The duty to report under the money laundering legislation within the United Kingdom` [2004] JBL 332; Nicholas Ryder, *Financial Crime in the 21st Century* (Edward Elgar 2011) 46; Peter Yeoh, `Enhancing effectiveness of anti-money laundering laws through whistleblowing` (2014) 17(3) JMLC 327.
[79] Miriam Goldby, `Anti-money laundering reporting requirements imposed by English law: measuring effectiveness and gauging the need for reform` [2013] JBL 367.
[80] The Law Society, *Response of the Law Society of England and Wales to the consultation issued by the Home Office and HM Treasury on the Action Plan for anti-money laundering and counter-terrorist finance – legislative proposals* (2016) para 15.
[81] Compliance Interview 3 dated 25/11/15.
[82] Compliance Interview 15 dated 10/03/16 (word in brackets added).

got to report this, and we've got to report that, and I think now it's really settled.[83]

This reduction in defensive reporting attributable to the maturity of the regime is also alighted upon in the SRA AML thematic review of the legal profession, and may comprise one of the factors driving the decline in number of legal sector SARs.[84] This reduction will only constitute a positive development within the regime however, if the decline is in respect of SARs which are not, in fact, reportable. The maturity of the UK AML regime is also a theme that many participants raised in a number of contexts during the course of the interviews, and will be explored in Chapter 7.

(v) The Lack of Intelligence Value of SARs

One of the interconnected potential consequences of a suspicions based reporting regime combined with an `all crimes approach` to AML relates to the intelligence value of the SARs submitted. Thus, according to Stokes, `there must be doubts as to the actual quality of such disclosures for intelligence purposes where the threshold is placed so low.`[85] This issue was pinpointed in stark terms by one participant who stated, `defensive reporting . . . that`s why they`re getting a lot of gibberish.`[86] This issue was highlighted in the responses to the government`s Call for Information on the SARs Regime in 2015, noting that `the use of an all crimes approach, with no de minimus [*sic*], obliges reporters to raise SARs that are of little value.` [87]

The questionable intelligence value of SARs was raised specifically in relation to the `technical` SARs discussed in Chapter 4. A small number of participants revisited this theme in a more general context, with one such participant concluding that `most of the SARs we submit are of absolutely no intelligence value.`[88] The same

[83] Compliance Interview 20 dated 16/06/16.
[84] SRA, *Anti Money Laundering Report* (2016) 33.
[85] Robert Stokes and Anu Arora, `The duty to report under the money laundering legislation within the United Kingdom` [2004] JBL 332, 355.
[86] Compliance Interview dated 24/11/15.
[87] Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* (2016) Annex B, 39.
[88] Compliance Interview 18 dated 08/04/16.

participant however, also acknowledged what Stokes has referred to as the `leave no stone unturned` approach to AML that the UK has adopted under the aegis of POCA 2002, noting that:

> I think the whole idea was better report everything and the intelligence agencies can decide what's of use, and what's not of use.[89]

As the NRA 2015 identified intelligence gaps as an issue with regard to the `high end` laundering effected via the legal profession, any measures that would seek to raise the reporting threshold in an attempt to improve the intelligence value of SARs submitted, are likely to prove politically unpalatable.[90] Indeed, the Action Plan 2016 states that `the private sector holds much of the data needed to develop the intelligence picture.`[91] From a government perspective therefore, whilst there is a considerable appetite to improve the quality of SARs and overall effectiveness of the SARs regime, there is no appetite whatsoever to lose any potentially useful intelligence streams. While this remains the position, the interwoven issues of defensive reporting and the questionable intelligence value of SARs will abide.

(vi) Legal Professional Privilege and Privileged Circumstances

One effect of the SARs regime is that it erodes the duty of confidentiality that exists between a client and their professional advisors across a number of sectors.[92] The duty of confidentiality may be preserved however in relation to the legal sector where common law Legal Professional Privilege (LPP) applies so as to block disclosure.[93] In addition, bespoke provisions within the failure to report offence under s 330/1 POCA 2002 expressly carve out the requirement to disclose

[89] ibid; see also Robert Stokes and Anu Arora, `The duty to report under the money laundering legislation within the United Kingdom` [2004] JBL 332, 355.
[90] HM Treasury and Home Office, *UK national risk assessment of money laundering and terrorist financing* (2015) para 6.96.
[91] Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* (2016) para 2.22.
[92] In the banking sector for example, the case of Tournier held that disclosure by compulsion of law is one of the permitted exceptions to the duty of confidentiality owed by a bank to its customer. *Tournier v National Provincial and Union Bank of England* [1924] 1 KB 461, All ER Rep 550.
[93] For a detailed explanation of LPP see Chapter 2.

information received by legal professionals under `privileged circumstances` unless such information is supplied intending to further criminality.[94] A number of participants noted that privilege was a factor to be considered when determining whether or not to make a SAR, but no further issues with privilege were evident from the interview data. As one participant noted:

> . . . you have to absolutely have focus on privilege, as to when you have lost privilege, because up until that point . . . your duty entirely is to your client.[95]

Some participants expressed disquiet about making SARs in respect of their clients, a view articulated by the MLRO who said:

> . . . it`s kind of contrary to the whole sort of ethos of trust and understanding between solicitor and client which is at the heart of . . . the English legal profession.[96]

(vii) Improved Information Sharing - Lack of Analysis and Feedback on SARs

One of the issues that participants raised with regard to the SARs regime was the lack of sufficiently relevant, detailed, or indeed any feedback on the SARs submitted to the NCA, both at an individual level and across the sector as a whole. This results in an unfortunate position where, according to one participant, `there is no direct line between law enforcement and a report of suspicion.`[97] The need for improved information sharing, together with a desire for `clear operational outcomes, such as arrests and asset recovery`, were highlighted as key themes in the government`s Call for Information on the SARs Regime in 2015.[98]

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[94] POCA 2002, s 330(10). The exemption from disclosure in provided for in s 330(6)(b). See s 330(11) for provisions relating to loss of privileged circumstances where there is an intention to further a crime.
[95] Compliance Interview 20 dated 16/06/16.
[96] Compliance Interview 17 dated 08/04/16.
[97] Compliance Interview 9 dated 15/12/15.
[98] Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* (2016) Annex B.

Whilst some analysis of SARs is provided by the NCA in its annual report on the regime, this tends to be cast in general terms, and provides little by way of detailed analysis of the SARs submitted by each sector. [99] This generalised and limited feedback by the NCA limits the utility of such reports to the legal profession, a position which was pinpointed by the MLRO who commented in relation to his practice, `it`s not relevant, hardly any of the examples I've seen were relevant to an international commercial practice.`[100] This position prompted Owen to comment that the NCA annual SARs report made `for an excellent quarry of anecdotal success stories`, but went on to comment that, `In the absence of an overall quantitative strategic picture, I see them as a bit of a smokescreen.`[101]

This issue was expanded on by the compliance officer who articulated his frustration with the lack of analysis and information sharing as follows:

> There is a dearth of analysis in relation to what is actually being provided by law enforcement, and [it] shouldn't take a lot to help that, all it needs is `here are the number of SARs from City law firms that either helped or supported existing cases` and the key element there being where the case was not already known to law enforcement, and that's weak, there's no analysis on that, which should be an easy win.[102]

This desire for meaningful and relevant feedback on legal sector SARs from the NCA was echoed by the Deputy MLRO who reflected:

> I mean it would be fascinating to know what . . . actually happens with all of this data that`s flowing in because . . . the less that actually gets to law enforcement that they do anything about, the more the regime is fundamentally devalued. [103]

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[99] See for example NCA, *Suspicious Activity Reports (SARs) Annual Report 2015* (2016); see also the NCA`s bi-annual report, NCA, *SARs Reporter Booklet* (2017).
[100] Compliance Interview 8 dated 14/12/15.
[101] Martin Owen, `SOCA – getting serious?` [2008] 154 Money Laundering Bulletin 13,14.
[102] Compliance Interview 17 dated 08/04/16 (word in brackets added).
[103] Compliance Interview 9 dated 15/12/15.

A note of caution must be sounded at this juncture. As Goldby observes:

> it is not true to say that a SAR can only be deemed useful if it triggers an investigation, followed by a prosecution and conviction.[104]

Fleming also observes that SARs may have multiple uses in practice.[105] Some SARs may indeed be `noise` in that they are submitted defensively or report unfounded suspicions.[106] Nevertheless, as outlined by Fleming, SARs may also assist in building a cumulative intelligence picture, develop that intelligence picture, trigger or assist investigations, or provide sufficient intelligence in isolation.[107] Given this nuanced contribution that SARs make to the intelligence landscape, it may not be possible in all cases to draw direct links between SARs submitted and specific actions taken. From Fleming`s perspective then, the position is more complex than `simply "running the numbers."`[108] Rather, a `holistic, networked view of SARs data` is required.[109] What this indicates, is that it may not be possible to provide the direct connections between SARs and actions that some participants desired.

Despite this caveat, an increase in the analysis of SARs and information sharing by the NCA would do much to address the concerns raised by participants. Better analysis of SARs was one of the proposals put forward in the Action Plan 2016, alongside the stated intention to `provide assessments of these to the private sector`.[110] The need for improvements in information sharing is also addressed in the Action Plan 2016, which stated, `we need radically more information to be shared between law enforcement agencies, supervisors, and the private sector.`[111]

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[104] Miriam Goldby, `Anti-money laundering reporting requirements imposed by English law: measuring effectiveness and gauging the need for reform` [2013] JBL 367,381.
[105] Matthew Fleming, `UK Law Enforcement Agency Use and Management of Suspicious Activity Reports: Towards determining the value of the regime` (UCL 2005) para 22 ff.
[106] ibid.
[107] ibid.
[108] Matthew Fleming, `Issues in measuring the efficacy of a suspicious activity reports (SARs) regime`, [2007] 70 Amicus Curiae 9,9.
[109] ibid.
[110] Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* (2016) para 2.10.
[111] ibid 3. Exploring improved information sharing legislation between law enforcement and the private sector was listed as Action 4 and `Prevent` campaigns to raise awareness within the regulated sector was listed as Action 5, 5.

The Action Plan 2016, in setting out its four AML priority areas, emphasised a `stronger partnership with the private sector.` via `new means of information sharing` to enhance the UK`s risk-based approach to AML. [112] As Goldby notes, `Meaningful feedback is crucial to the implementation of a risk-based approach to anti-money laundering.`[113]

There have been a number of developments under the Criminal Finances Act 2017 in terms of greater information sharing. New provisions have been inserted into POCA 2002 permitting disclosures between members of the regulated sector and joint disclosures to the NCA with regard to money laundering concerns.[114] The information flow to the NCA will also be enhanced by way of `further information orders` provided for under the Act whereby the NCA may seek further information from those reporting to it.[115] Furthermore, Regulation 47 MLR 2017 requires supervisory authorities such as the Law Society to provide up to date information on money laundering risks and typologies relevant to the population they supervise.

Far more needs to be done, however, to address the lack of information sharing as between the NCA and the legal profession, a point made strenuously by the Law Society in the following terms:

> We strongly believe that the principal dialogue should be between law enforcement and the private sector and that information sharing across sectors merely supplements that dialogue.[116]

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[112] ibid, para 1.8.
[113] Miriam Goldby, `Anti-money laundering reporting requirements imposed by English law: measuring effectiveness and gauging the need for reform` [2013] JBL 367, 390.
[114] POCA 2002, s 339ZB – ZG inserted by Criminal Finances Act 2017, s 11.
[115] POCA 2002, s 339ZH inserted by Criminal Finances Act 2017, s 12.
[116] The Law Society, *Response of the Law Society of England and Wales to the consultation issued by the Home Office and HM Treasury on the Action Plan for anti-money laundering and counter-terrorist finance – legislative proposals* (2016) 10. See also Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* (2016) Annex B where respondents to the government`s Call for information on the SARs Regime articulated a desire for increased `outputs` to the reporting sectors comprising, inter alia, `trend and threat data`.

The operation of the Joint Money Laundering Intelligence Taskforce (JMLIT) within the banking sector models how such information sharing can work in practice. Piloted in February 2015, and paced on a permanent footing in May 2016, JMLIT showcases the way in which:

> . . . the NCA and other law enforcement officers are working side by side with staff from some of the major UK banks and financial institutions to tackle the highest priority risks.[117]

The shared expertise exemplified by JMLIT has resulted in a number of direct interventions, but also `more informed prioritisation` and `an improved collective understanding` with regard to money laundering risks in the sector.[118] Such an approach could be rolled out across the legal sector.[119] Alternatively, improved information sharing could be achieved by extending and expanding on the information comprised in the NCA biannual reporter booklets, which currently constitute `sanitised versions` of those reports available to end users with direct access to the SARs database. [120] Finally, information could be disseminated to the profession by granting the SRA, subject to confidentiality constraints, direct access to the SARs database. A note of caution should be sounded with regard to granting direct access, however, as the NCA report that the

> . . . majority of regulators indicated that they wanted better information from the SARs regime but did not wish to have direct access.[121]

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[117] NCA, *Suspicious Activity Reports (SARs) Annual Report 2015* (2016) 20. See also NCA, `Joint Money Laundering Intelligence Taskforce (JMLIT)` <http://www.nationalcrimeagency.gov.uk/about-us/what-we-do/economic-crime/joint-money-laundering-intelligence-taskforce-jmlit> accessed 4 July 2017.
[118] NCA, `Joint Money Laundering Intelligence Taskforce (JMLIT)` <http://www.nationalcrimeagency.gov.uk/about-us/what-we-do/economic-crime/joint-money-laundering-intelligence-taskforce-jmlit> accessed 4 July 2017.
[119] Action 2 of the Action Plan 2016 includes the proposal to `Consider how the taskforce approach could be developed in other reporting sectors.` Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* (2016)16. Findings from the Call for Information on the SARs Regime state that `Some non-bank contributors asked for an equivalent structure.` ibid, Annex B.
[120] NCA, *Suspicious Activity Reports (SARs) Annual Report 2015* (2016) 20.
[121] ibid 21.

Improved information sharing between the NCA and the legal profession would better support practitioners generally, and MLROs in particular, as it would provide clearer parameters within which to operate. The benefits of such information sharing would also cascade down to the profession more widely as more detailed and relevant typologies affecting the sector could be disseminated across the profession as a whole. Such examples could be interwoven into AML training offered at the firm level, thus improving awareness across the sector. The desire for relevant examples to be used in AML training was an issue that was raised by participants and was explored in Chapter 5.

(viii) A Bespoke SARs Form for the Legal Profession

As outlined at earlier in this Chapter, both the SRA and NCA have voiced concerns over the poor quality of the SARs submitted to them. Many participants, however, reported numerous difficulties when using the generic SARs form itself, an issue that could be addressed by the creation of a bespoke SARs form for the legal profession.

Currently, the banking sector constitutes the largest reporting sector in the UK, submitting 83.39% of all SARs in the period 2014/5.[122] Historically, the sector was also the initial focus of UK legislation when EU AML measures were transposed into UK law.[123] This historical and current dominance of the banks within the AML regime in general, and the SARs regime in particular, is clearly evident when filing a SAR. The form itself is cast in transactional terms tailored to financial institutions in that it requests, inter alia, details of the currency, bank account, debit or credit in respect of which the report is being made.

Given the `all crimes` approach of POCA 2002, it is frequently the case that none of the transactional details requested by the NCA may be relevant to a legal professional when reporting a notional saving or benefit identified in respect of the

[122] ibid.
[123] Money Laundering Regulations 1993, SI 1993/1933 and in particular the definition of `relevant financial business` in reg 4.

breach of an environmental licence for example. Legal professionals must navigate through the form to a free text section in order to make a disclosure.

Many compliance participants raised difficulties surrounding the submission of the SARs form itself as an issue with the reporting regime. Over 99% of all SARs are now submitted electronically, with the SARs Online portal constituting the NCA`s stated preferred method of submission.[124] However, participants reported encountering practical difficulties using the SARs Online system, with one commenting that, `the technology needs to improve, it needs to be easier to add information.`[125] This need for an upgraded IT system for SARs was recognised and designated as one of the issues listed for action in the Action Plan 2016.[126] In their responses to the Call for Information on the SARs Regime, all sectors `viewed the technical infrastructure . . . as inadequate.` [127]

Some participants found that `the online portal`s a bit clunky` and `immensely difficult to navigate`.[128] Still other MLROs were far more critical of the difficulties encountered when using the online filing system, stating that the NCA website was, quite simply, `appalling`.[129] Whilst the NCA acknowledge the challenges users face when using SARs Online, ongoing improvements to the IT system are `focussed on addressing back end resilience issues rather than user interface design changes.`[130]

The main difficulty participants experienced when using SARs Online stemmed from the fact that the forms themselves are `very much tailored to financial institutions` and therefore `don`t really lend themselves to law firms`.[131] Hence MLROs filing reports online must navigate their way through a series of questions

[124] NCA, *Suspicious Activity Reports (SARs) Annual Report 2015* (2016)12; NCA, *Suspicious Activity Reports (SARs) Annual Report 2013* (2014) 6 which states that 99.25% of all SARs are submitted electronically.
[125] Compliance Interview 6 dated 08/12/15.
[126] Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* (2016) para 2.9.
[127] ibid Annex B.
[128] Compliance Interview 11 dated 19/02/16; Compliance Interview 3 dated 25/11/15.
[129] Compliance Interview 16 dated 14/03/16; Compliance Interview 3 dated 25/11/15.
[130] NCA, *Suspicious Activity Reports (SARs) Annual Report 2015* (2016)22.
[131] Compliance Interview 1 dated 17/11/15.

relating to transactions of the type effected via the banking sector before being able to enter narrative comments with regard to the notional savings and benefits likely to be encountered by legal sector reporters. As one MLRO said of the online questions pertaining to the transfer of funds via a bank account prior to adding their narrative disclosure, ` I just ignore those which I think are completely irrelevant to, you know, to our sector.`[132] This challenge is pinpointed by the participant who stated:

> . . . the problem with the online form is the terminology that they use. They talk about suspect and then money transaction and sometimes none of these things apply at all. [133]

The frustration engendered by this lack of tailoring with respect to the SARs Online form was vocalised by the MLRO who commented:

> The difficulty with the forms is I think they're geared up to financial institutions such as banks and things and about 80 or 90% of the questions just don't relate to what we're doing.[134]

A number of participants felt that the SARs form was drafted purely with the financial sector in mind and that the legal sector had been clumsily bolted on to the same reporting system. This view is typified by the participant who concluded:

> . . . the form`s never been fit for purpose, certainly not fit for lawyers, it's designed for banks.[135]

This feature of the regime can be easily addressed by the provision of a bespoke legal sector reporting form, which is tailored to the needs of the profession. This solution was suggested by a number of participants, including the MLRO who proffered the view that, ` I think there could be a different set of templates for lawyers`.[136] The Law Society have also pressed this issue, arguing for the form to

[132] Compliance Interview 10 dated 15/12/15.
[133] Compliance Interview 7 dated 08/12/15.
[134] Compliance Interview 16 dated 14/03/16.
[135] Compliance Interview 12 dated 26/02/16.
[136] Compliance Interview 3 dated 25/11/15.

be `redesigned` in a manner which is `fit for purpose for all types of reporters.`[137] This issue is also reflected in the responses to the government`s Call for Information on the SARs Regime in 2015, which noted that `non-bank respondents felt that any new technical solution needs industry-specific templates.` [138]

A bespoke legal sector SAR would focus on those aspects of a transaction most likely to give rise to a report from a legal professional in practice: namely the nature of any underlying offences, and any notional savings and benefits potentially constituting criminal property. It is these features which are far more likely to form the basis of any report under POCA 2002 from the legal sector, as opposed to filing a SAR in relation to the debits and credits flowing through a bank account. A bespoke form would therefore address the difficulties encountered by the profession when submitting SARs, without impacting upon the statistical data harvested from SARs across all sectors.

Having outlined the issues that participants raised with regard to the SARs regime overall, consideration must now be given to the operation of the consent regime in particular.

3. The Consent Regime

As noted earlier in this Chapter, the consent regime provides a disclosure route affording legal professionals a complete defence to the substantive money laundering offences set out in ss 327-9 POCA 2002. In 2015, consent requests comprised 75.52% of SARs submitted by the sector, representing 17.8% of all consent requests overall.[139] Thus, as the majority of legal sector SARs are `consent` SARs, the consent regime is the aspect of the SARs regime most frequently encountered by the sector. The issue that arises in practice is that a legal professional may not perform any acts prohibited under ss 327-9 POCA 2002 prior

[137] The Law Society, *Response of the Law Society of England and Wales to the consultation issued by the Home Office and HM Treasury on the Action Plan for anti-money laundering and counter-terrorist finance – legislative proposals* (2016) 11.
[138] Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist financ*e (2016) Annex B.
[139] NCA, *Suspicious Activity Reports (SARs) Annual Report 2015* (2016) 11.

to receiving the relevant consent sought from the NCA. In addition, notifying a client that a SAR has been made may well constitute `tipping off` in certain circumstances.[140]

One of the measures considered in the government`s 2016 Action Plan was the removal of the consent regime on the basis that it was `inefficient`.[141] The regime, it was suggested, would be refocused on entities rather than transactions, and the `consent` defence removed, with the corollary being that `reporters who fulfil their legal and regulatory obligations would not be criminalised`.[142] This proposal was vigorously contested by the Law Society, who argued that the `protection offered by the consent regime works to offer balance and to avoid over-criminalisation.`[143] The balance referred to is a reference to the combined effects of an `all crimes` approach and suspicions based reporting regime.[144] As a potential alternative to the consent regime, the Law Society put forward embryonic suggestions for a `tiered` reporting scheme, referred to in Chapter 4, whereby reporters would `grade the importance of the SARs they submit.`[145] As the consent regime has been retained in its existing form following the transposition of 4MLD, such alternative proposals surrounding the consent regime have not been refined further.

It is set against this background that participants were asked to consider the consent regime. A small majority of participants overall, including a number of compliance respondents, had no issues with the consent regime. However, this finding must be treated with extreme caution as the majority of those participants who said they had no issues with the consent regime were transactional participants who had never used the consent regime in practice. Similarly, whilst a small majority of participants offered no suggestions for improvements to the

[140] POCA 2002, s 333.
[141] Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* (2016) para 2.8.
[142] ibid.
[143] The Law Society, *Response of the Law Society of England and Wales to the consultation issued by the Home Office and HM Treasury on the Action Plan for anti-money laundering and counter-terrorist finance – legislative proposals* (2016) para 14.
[144] ibid.
[145] ibid para 18.

consent regime, the majority of these responses also came from transactional participants with no experience of using the consent regime in practice.

(i) Dealings with the NCA Consent Team

Participants were fairly evenly split between those who had a positive or negative experience with the NCA consent team. With regard to those participants reporting negative experiences, a small number of participants pinpointed very specific issues they had encountered: they were of the view that the NCA were under-resourced, took a box-ticking approach, that it was difficult to expedite consent, and that there was no single point of contact at the NCA consent desk.

A number of participants raised two, more general, negative issues: namely that, (i) consent took too long to obtain and/or that response time was getting longer, and (ii) the NCA misunderstood the transactions participants were effecting. The first of these general issues, that NCA consent `takes too long` and that the NCA are `getting slower and slower to come back` to reporters is self-explanatory, and its impact in practice will be explored subsequently in this Chapter.[146]

The NCA`s perceived lack of understanding of the transactions effected by participants was attributed by a number of such participants to the fact that the NCA were more accustomed to dealing with banking sector SARs. This was highlighted by the compliance participant who said of the NCA:

> . . . because the majority of what they see is about a financial transaction and movement of money by a bank, when it comes to the legal profession they really struggle with "well how does a transaction work?" [147]

In addition to this lack of understanding of transactions effected by the legal sector in a general sense, a number of participants reported that the `technical` SARs discussed in Chapter 4 were poorly understood on the part of the NCA. This is best illustrated by the MLRO who explained:

[146] Compliance Interviews 1 and 16 dated 17/11/15 and 14/03/16.
[147] Compliance Interview 14 dated 10/03/16.

> If you`ve got a regulatory offence you can be on the phone to the consent desk trying to explain to them why it is actually reportable – they`re like "well I don`t understand what the problem is here".[148]

This lack of understanding of the transactions effected by the legal sector was put forward as an explanation for the poor quality legal sector SARs complained of by the NCA. As one compliance participant said of the NCA:

> . . . their statistics on "well we have to keep calling lawyers in relation to consents" is not because the consent is filled out poorly, it's because they don't understand the transaction, or don't understand how transactions work.[149]

Improvements in this area may well be forthcoming on the basis that the Law Society are working closely with the NCA with regard to consent requests from the sector.[150] A sector specific SAR form would also assist in ameliorating this position as it would be tailored to deal with notional savings and benefits as opposed to credits and debits through an account.

A fairly equal number of participants recounted positive experiences when obtaining consent from the NCA. Some participants reported establishing a good rapport with the NCA, as demonstrated by the MLRO who stated:

> I do quite like the fact there are people on the end of the phone who are now entering into a dialogue.[151]

Furthermore, in contrast to those participants who raised concerns over the response time from the NCA, a number of participants were of the view that obtaining consent was either quick and/or getting quicker. This view is typified by the participant who stated in relation to consent requests, `they`re turned round

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[148] Compliance Interview 13 dated 10/03/16.
[149] Compliance Interview 6 dated 08/12/15.
[150] Compliance Interview 12 dated 26/02/16. See The Law Society, `AML Policy Update - January 2017` (*The Law Society*, 27 January 2017) < http://www.lawsociety.org.uk/news/stories/aml-policy-update-january-2017> accessed 27 June 2017.
[151] Compliance Interview 10 dated 15/12/15.

very fast`. [152] A small number of participants observed a recent development on the part of the NCA whereby the NCA exercise their discretion not to make any decision on a SAR, a development deemed `seriously unhelpful`.[153]

Inevitably, the response time and interaction between the NCA and those reporting to it have an impact on dealings between legal professionals and their clients, and it is this aspect of the consent regime that forms the focus of the following paragraphs.

(ii) Deal Pressure and The Consent Regime

A number of participants highlighted the `challenge` that arises where consent has been sought from the NCA and a transaction cannot be completed prior to receipt of the relevant consent.[154] As one participant reflected, `it can be stressful . . . when you`ve got a looming completion date, trying to get that [consent] back.`[155] The issue is remarkably stark in that any failure to obtain consent `can hold up transactions.`[156]

This tension that exists for lawyers waiting for NCA consent to complete a transaction is best articulated by the transactional partner who said:

> . . . there is a bit of a collision between quite fast moving transactional environments and what is effectively a public body that moves at its own pace, that always feels quite stressful as an engagement point . . . it is somewhat unrealistic in a way for us to down tools whilst we wait for them to respond in an environment where we are moving fast through a process.[157]

Set in this context then, even receiving consent within 48 to 72 hours was deemed to be `a massive amount of time . . . that can delay a closing` according to one

[152] Compliance Interview 17 dated 08/04/16.
[153] Compliance Interview 17 dated 08/04/16.
[154] Compliance Interview 11 dated 19/02/16.
[155] Compliance Interview 1 dated 17/11/15 (word in bracket added).
[156] Compliance Interview 16 dated 14/03/16.
[157] Transactional Interview 2 dated 18/11/15.

Deputy MLRO.[158] This particular challenge is likely to become more of an issue for participants going forward, given that the moratorium period may now be extended by court order by up to a total of 186 days, following the enactment of the Criminal Finances Act 2017.[159] This extension of the moratorium period, in tandem with the pre-existing `all crimes` approach of POCA 2002 and a suspicions based reporting regime, may result in an increased burden on the legal profession, particularly where that extension is not accompanied by additional resourcing of the NCA.

(iii) The Client Relationship and Tipping Off

The transactional hiatus where `you have to prevaricate with your client` whilst waiting for consent from the NCA may have the effect of damaging that client relationship.[160] This concern was raised by a number of participants, including the transactional partner who commented on the consent regime as follows:

> . . . if it means you have to back off a transaction for seven days and it turns out there`s absolutely nothing wrong, you could have ended up seriously damaging the transaction, seriously damaging your relationship with the client.[161]

Seriously damaging a client relationship is one potential consequence of the operation of the consent regime. In addition, a number of participants were acutely mindful of their potential criminal liability for `tipping off` should they disclose the fact that a SAR has been made to their clients.[162] This prompted one transactional partner to comment that, `the thing we struggle with is not being able to tell the client.`[163] Some participants spoke of effectively `going under the radar ` once a SAR has been made to avoid any potential tipping off. [164] This places the lawyer in an invidious position with their clients, particularly where, as one

[158] Compliance Interview 9 dated 15/12/15.
[159] POCA 2002, s 335(6A), inserted by the Criminal Finances Act 2017, s 10.
[160] Compliance Interview 17 dated 08/04/16.
[161] Transactional Interview 11 dated 26/11/15.
[162] In certain circumstances, such as a company acquisition for example, a technical offence may have been revealed as part of the due diligence process. In those circumstances, a joint SAR may be made by the client and the law firm.
[163] Transactional Interview 8 dated 26/11/15.
[164] Transactional Interview 6 dated 25/11/15.

participant recounted, `the client`s screaming and tearing their hair out because they don't know what you're doing.`[165] Sophisticated clients may also challenge their legal advisors, as highlighted by the participant who noted:

> You have this ludicrous situation where often the client will say "well you've done this, I suspect you've done a SAR" and you can't say you have or you haven`t you know, the client`s not stupid.[166]

This interplay between deal pressure, the client relationship and tipping off are crystallised effectively in the comments made by the transactional partner who summarised:

> . . . if you're actually working to. . . a serious commercial deadline and the law firm has to stop acting . . . obviously it causes severe issues, not least with your client who wonders why you've done that, because you can't tell them because of tipping off.[167]

It is this dynamic that was also reflected in responses to the government`s Call for Information on the SARs Regime, prompting respondents to request `a form of words, agreed with the NCA, to use with customers who question the delay of their transactions.`[168]

4. Concluding Comments on the SARs Regime

Despite the numerous reports and consultations on the SARs regime, the majority of participants had no issues with, and no views on improvements to either the non-consent or consent regime. Caution must be exercised with regard to these findings however, given the large number of responses from transactional participants who had never used the SARs regime in practice.

It may also be recalled from Chapter 4 however, that the majority of participants expressed the clear view that minor offences and regulatory breaches attracting

[165] Transactional Interview 20 dated 11/03/16.
[166] Compliance Interview 17 dated 08/04/16.
[167] Transactional Interview 7 dated 25/11/15.
[168] Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* (2016) Annex B.

criminal sanctions should be excluded altogether from the ambit of the Act, with virtually all participants performing a compliance role holding this view. Removing such `technical` offences from the ambit of the Act would have the effect of streamlining the SARs regime insofar as it relates to the legal profession.

As the UK SARs regime is a suspicions based regime, a low reporting threshold is imposed upon the legal profession. For the majority of participants, the concept of suspicion was determined according to a blend of instinct, specific fact patterns and experience, as opposed to the judicial guidance set out in the *Da Silva* judgment. Moreover, the guidance in *Da Silva* may be seen as an over-definition by the courts. Following the decision, a subjective suspicion may be reportable or not depending on whether that suspicion is more than a vague feeling of unease. Given that there is no requirement for any objective grounds for forming a suspicion, it then becomes difficult to distinguish between a sense of unease and subjective suspicion. Such considerations may be entirely academic in practice, however, as participants` responses to any money laundering concerns was to contact the firm`s MLRO rather than explore the semantic parameters of the term `suspicion` and whether or not their suspicions were reportable or not.

The importance of the MLRO was evident from the data. Responses from participants illustrated the wholesale transference of money laundering concerns to the MLRO, who actively shaped or dismissed suspicions, and determined whether or not to make an external SAR. The potential impact of each MLRO`s decisions is highly significant both at a firm level and in a wider societal context given the sheer volume of deals transacted via the sector. The wholesale transference of money laundering concerns to the MLRO is only effective if the MLRO has the requisite skill to make appropriate determinations with regard to external SARs. Instances have been highlighted across the sector, although not by participants, where MLROs lack that requisite skill. This highlights the potential vulnerability of a system which places considerable AML responsibility in the hands of one person, as opposed to requiring lawyers themselves to make reports directly to the NCA.

Two collateral effects of a suspicions based reporting regime coupled with an `all crimes` approach are the interconnected issues of defensive reporting and the poor intelligence value of some SARs. Defensive reporting was raised specifically as an issue with regard to the `technical` SARs discussed in Chapter 4. However, only a small number of participants went on to refer to it in the more general context of the regime as a whole, and even fewer participants referred to defensive reporting in their own practices. Similarly, the poor intelligence value of SARs was also raised with regard to `technical` SARs, but only revisited by a small number of participants in a more general context.

As the NRA 2015 reported intelligence gaps with regard to the high end laundering effected via the sector, any measures that would seek to raise the low reporting threshold, by whatever means, are likely to prove unpalatable in a political context.[169] From a government perspective, whilst there is a desire to improve the quality of SARs and the overall effectiveness of the SARs regime, there is no desire to lose any potentially useful intelligence streams. While this is the case, both defensive reporting and the poor intelligence value of SARs are likely to remain live issues.

With the low reporting threshold and `all crimes` approach intact in the UK following the transposition of 4MLD, consideration must be given as to what other measures could assist in improving the SARs regime. One such measure is purely practical: the development of a bespoke legal sector SARs form would ease the online reporting process. The other is also practical in nature, namely an increase in analysis and information sharing with regard to SARs between the NCA and legal profession, as showcased by JMLIT. Such information sharing would then track through to AML training and act to promote awareness within the sector, both for MLROs and those reporting to them.

[169] HM Treasury and Home Office, *UK national risk assessment of money laundering and terrorist financing* (2015) para 6.96.

The consent regime also remains intact following the transposition of 4MLD, a retention welcomed by the Law Society. Of the alternatives considered, the entities based reporting regime consulted on by the government in 2016 did more to reflect the concerns of the banking sector, which deals with multiple transactions for each customer, but as a concept would have been insufficient with regard to law firms, who may only deal with individual transactions for a client. Thus, according to the Law Society, `Solely focusing on an entity will not adequately deal with the very real issues faced by those outside the banking sector.` [170] Therefore, an element of transactions based reporting would always need to be retained for the legal sector, reflecting the way legal services operate in practice. As the decision was made by government to retain the consent regime, very little further detail was provided on the proposed entities based reporting route, and therefore it is not possible to assess fully the relative strengths and weaknesses of this proposal. The tiered reporting system suggested, inter alia, by the Law Society, where reporters grade the importance of their SARs could be developed further in practice, but only, in the words of the Society, `if accompanied by robust guidance from government.`[171] As with the entities based reporting proposal, this suggested reporting route has not been developed further, so it is not possible to assess with any certainty the merits or otherwise of this route.

Participants were fairly evenly divided between those who had a positive experience of obtaining consent from the NCA, and those who recounted a negative experience. The issue surrounding the consent regime for the legal professional relates to deal pressure when seeking consent, and managing the client relationship so as avoid liability for `tipping off.` This latter aspect of the regime is set to become even more challenging given the power brought in by the Criminal Finances Act 2017 to extend the moratorium period by court order by up

[170] The Law Society, *Response of the Law Society of England and Wales to the consultation issued by the Home Office and HM Treasury on the Action Plan for anti-money laundering and counter-terrorist finance – legislative proposals* (2016) para 23.
[171] ibid para 18; see also Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* (2016) Annex B.

to a total of 186 days.[172]That challenge will be exacerbated if it is not accompanied by sufficient resourcing of the NCA. There exists, therefore, an inevitable tension between transactional efficacy and the competing requirements of the NCA and law enforcement. Refinements may be made to the SARs regime by way of improved information sharing, a bespoke SARs form, or the removal of technical offences from the scope of POCA 2002. Whilst the consent regime remains, the tension between a legal profession whose purpose is to effect transactions, and the NCA whose remit is to halt the flow of illicit funds, is a tension set to continue.

This Chapter has focussed on the key aspect of the AML regime that is the SARs regime, thus drawing to a close the examination of the mechanical aspects of the regime. The subsequent data chapter shifts its focus to consider participants` perceptions of and reflections on the regime, and their role within it.

[172] POCA 2002, s 335(6A).

Chapter 7 - Participants` Perceptions of the UK AML Regime

The previous data chapters of this thesis considered the practical issues that participants encountered when seeking to effect compliance with the mechanical aspects of the UK AML regime. This Chapter moves away from the mechanics of day to day practice and explores participants` perceptions of the regime overall, and their role within in. Accordingly, this chapter will consider participants` perceptions of the following: (1) the role of the legal profession within the UK AML regime, (2) the costs and benefits of AML compliance, (3) SRA regulation and enforcement of the regime, (4) identification of money laundering risk, and (5) UK law firms in a global context. As this Chapter deals with a number of discrete and disparate topics, concluding remarks will be provided at the end of each section.

1. The Role of the Legal Profession within the UK AML Regime

As stated in Chapter 2, AML obligations were initially imposed upon the legal profession in response to FATF`s `gatekeeper` initiative, which sought to include within an AML framework those professions deemed to be vulnerable to money laundering.[1] At the time, many objections were raised by the profession, most notably in relation to the erosion of lawyer-client confidentiality, and multiple challenges launched globally.[2] Historically then, and in much academic literature, lawyers have frequently been referred to as `gatekeepers` in terms of their AML role.[3] There has also been an evolving discourse in recent years in respect of the

[1] See, for example, Kevin Shepherd, `Guardians at the Gate: The Gatekeeper Initiative and the Risk-Based Approach for Transactional Lawyers` (2009) 43 (4) Real Prop. Tr. & Est. L.J. 607.
[2] Letter from ABA & Others to FATF (3 April 2003); Colin Tyre, `Anti-Money Laundering Legislation: Implementation of the FATF Forty Recommendations in the European Union`, 2010 J. Prof. Law. 69,72; Ronald J. MacDonald, `Money Laundering Regulation-What Can Be Learned from the Canadian Experience` 2010 J.Prof.Law. 143, 144.
[3] Kevin Shepherd, `Guardians at the Gate: The Gatekeeper Initiative and the Risk-Based Approach for Transactional Lawyers` (2009) 43 (4) Real Prop. Tr. & Est. L.J. 607.

`high-end` laundering effected via the legal sector, whereby legal professionals are cast as `professional enablers` or `facilitators` of money laundering.[4]

(i) General Comments on the AML Role of the Legal Profession

Participants were therefore asked to consider their role within the UK AML regime in the context of their CDD and reporting obligations. Responses from participants must be read with caution however, as they are likely to be weighted against any form of self-incrimination. Prior to considering the detailed and specific comments explored in subsequent paragraphs, a number of general points were raised.

Rather than objecting to the additional workload created by the regime, many participants expressed an active willingness to comply with their AML obligations. Nor were such responses restricted to compliance participants with a vested interest in the regime due to their role. As one transactional partner reflected, `we are professionals and we need to do things correctly`.[5] Put simply, `we just want to get it right`.[6]

Furthermore, a number of participants reported declining to act for clients, either in the absence of satisfactory CDD information, or in the presence of any money laundering concerns. For example, one compliance participant recounted a number of instances where, `we've just not got that level of comfort and therefore we`ve said no.`[7] This stance was also mirrored amongst a number of transactional partners, one of whom stated `no way at all would I get tempted to take on something I wasn't sure of, or carry on with something I'm not sure of.` [8] This finding aligns with the SRA Anti Money Laundering Report 2016, which states that

[4] The NCA defines high end money laundering as `the laundering of funds, wittingly or unwittingly, through the UK financial sector and related professional services.` NCA, *High End Money Laundering Strategy and Action Plan* (2014) para 3; see also comments in the NRA 2015 with regard to complicit legal professionals, HM Treasury and Home Office, *UK national risk assessment of money laundering and terrorist financing* (2015). With regard to professional enablers, Serious Crime Act 2015, s 45 criminalises participation in organised crime and is targeted at professionals such as lawyers and accountants.
[5] Transactional Interview 6 dated 25/11/15.
[6] Transactional Interview 8 dated 26/11/15.
[7] Compliance Interview 14 dated 10/03/16.
[8] Transactional Interview 17 dated 16/12/15.

declining to act for clients deemed to be high risk, or where there are money laundering concerns, was identified by MLROs as one of the factors driving a decline in consent SARs from the legal sector.[9] It is within this general context that specific aspects of the AML role of participants will now be examined.

(ii) The Role of the Legal Profession is Appropriate

The majority of participants felt their AML role was appropriate or that `the balance is right`.[10] This view was expanded upon by the transactional partner who said:

> I think we have a duty to maintain the good standing of the profession and to understand money laundering and to behave properly – does that then mean we have a role? then yes, of course it does. You know, we`re at the centre, or towards the centre, of deal activity.[11]

Many participants viewed their AML role as appropriate precisely because of their close involvement in the deal activity referred to in the quotation above. Such involvement at a `particular point in the cycle` means that, in terms of identifying potential money laundering on a transaction, lawyers are `in a unique position to actually come across some of these issues`.[12] Due to the nature of transactional work, lawyers are more likely to have an in depth knowledge of their client`s affairs than a bank, whose only visibility on a transaction may well be the transfer of funds through a bank account. For one transactional partner then:

> . . . because of our unusual situation in the transaction process . . . we`re the only ones that probably can get near it occasionally.[13]

A number of participants referred explicitly to their role as `gatekeepers`, such as the compliance participant who reflected:

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[9] SRA, *Anti Money Laundering Report* (2016).
[10] Compliance Interview 15 dated 10/03/16.
[11] Transactional Interview 14 dated 01/12/15.
[12] Compliance Interviews 9 and 18 dated 15/12/15 and 08/04/16.
[13] Transactional Interview 20 dated 11/03/16.

> You have a gatekeeper responsibility . . . there was a lot of discussion about that sort of 10 years ago about, you know . . . this is not our role, but actually I think the way the world's gone, I think it's wrong to not accept that you've got responsibility in that sphere.[14]

This evolution of the lawyer`s role to encompass AML measures was also highlighted by a number of interviewees, such as the partner who recalled:

> When I started out in this career, this, I suppose for all of us, this wasn't really part of the plan, this wasn't . . . supposed to be, you know, part of our job.[15]

(iii) Lawyers as Unpaid Investigators

A small number of participants felt that the effect of the AML regime was that the legal profession were overburdened, or that they performed the role of unpaid detectives. Indeed, this perception of lawyers as policemen is one which can be found in academic literature in the area. Levi, for example, states that lawyers have been, `involuntarily co-opted into becoming unpaid agents of the state`, a crime control approach which Garland describes as a `responsibilization strategy`.[16]

This view of lawyers as policemen can be illustrated by the compliance participant who stated, `we are providing a significant body of intelligence as unpaid investigators for law enforcement.`[17] This position was reiterated by the transactional participant who said in relation to money laundering, `I think we`re being made to police it rather than the police`[18] This position even prompted one transactional partner to pose the question, `is it *really* my role to be the

[14] Compliance Interview 18 dated 08/04/16.
[15] Transactional Interview 15 dated 08/12/15.
[16] Michael Levi, `Pecunia Non Olet? The Control of Money-laundering Revisited` in Frank Bovenkerk and Michael Levi (eds), *The Organized Crime Community: essays in Honour of Alan. A. Block* (Springer 2007) 162; David Garland, `The Limits of the Sovereign State: Strategies of Crime Control in Contemporary Society` (1996) 36(4) Brit. J. Criminol 445,452.
[17] Compliance Interview 6 dated 08/12/15.
[18] Transactional Interview 20 dated 11/03/16.

policeman? I don`t actually think it is`.[19] To summarise then, the effect that a lawyer`s AML role has on the client retainer in practice was set out by the partner who stated:

> . . . you're being asked to police something, when really your function is not to act as policemen but to act as a facilitator of a transaction, and they don't really go hand-in-hand.[20]

(iv) The Maturity of the AML Regime

One factor which has had an impact on participants` roles within the AML regime is the maturation of that regime. This was an aspect of practice that was referred to by many participants, despite the initial `pushback` from both lawyers and clients alike when the regime was first introduced.[21] The effect of the maturation of the regime was raised specifically with regard to identifying beneficial ownership in Chapter 5, and with regard to defensive reporting under the SARs regime in Chapter 6. It was also raised in a far more general context, both with regard to law firms themselves, and in respect of the clients they serve. This general move towards maturity was highlighted by the compliance participant who said of the regime:

> We are going through a period now where actually I think we've come through the first wave where we were, particularly for the legal profession, just trying to get to compliance right, and trying to do what is expected of us – and then there's a sort of maturity that comes with that after a while, and you, you`re wanting to focus, you want the regime to work and you want to focus on the things that really help.[22]

This view was reiterated by the MLRO who noted:

[19] Transactional Interview 15 dated 08/12/15 (emphasis added).
[20] Transactional Interview 20 dated 11/03/16.
[21] Transactional Interview 1 dated 18/11/15.
[22] Compliance Interview 2 dated 24/11/15.

> I think we've now got much more accustomed to it, we've got a much better understanding of what the legislation actually means.[23]

A number of participants were of the view, expressed by one partner, that `the level of knowledge has improved dramatically over the last 5-10 years`.[24]

Some participants noted that clients too were now `very attuned` and `very used` to complying with the regulations such that:

> All clients on a UK/European basis know that if they instruct a law firm they have to front up with certain information about who they are and what they do.[25]

This maturity was highlighted by the transactional partner who noted:

> . . . 5 to 10 years ago it was actually quite hard to get . . . the information that you needed. Now it tends to be more readily provided and people understand why you are asking for it.[26]

The extracts above, together with the comments made in Chapters 5 and 6, suggest that the maturity of the regime has brought with it improvements in the level of awareness that practitioners and clients have of the regime, leading to a streamlining of CDD processes and a potential decline in defensive reporting. Such refinements may in turn have the effect of improving the efficiency of the UK AML regime overall.

(v) Poor Evidence of Money Laundering via the Legal Profession

Having considered the appropriateness or otherwise of their AML role, participants then raised a number of additional themes, namely the lack of evidence of laundering via the sector, and the pragmatic view that skilled and determined launderers will never be caught.

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[23] Compliance Interview 3 dated 25/11/15.
[24] Transactional interview 1 dated 18/11/15.
[25] Transactional Interviews 6 and 1 dated 25/11/15 and 18/11/15.
[26] Transactional Interview 19 dated 10/03/16.

A number of participants were of the view that the legal profession`s involvement in money laundering was misunderstood. In particular, several participants strongly objected to the labelling of the sector as professional enablers, such as the compliance participant who said:

> I've taken significant objection to the professional enablers point with the National Crime Agency . . . I think the concern I've had is there has been a worrying blurring between those who try and get it wrong, and those who are willingly complicit.[27]

Similarly, several participants objected to the `high risk` rating given to the profession in the NRA 2015. This rating prompted one participant to summarise the NRA 2015 findings in the following terms:

> The key point in it is `we don't know` – that's the key point about the profession – `we don't know and we don't understand – therefore we`ve rated it as high risk.`[28]

Such objections align with those raised by the Law Society on publication of the NRA in 2015. The Society`s response to the report was that it `lacks balance` and `by its own admission, is not backed up by robust intelligence.`[29] The Law Society president at the time went on to state that the report was `misleading`.[30]

This lack of evidence in relation to money laundering by legal professionals, considered in Chapter 1, was raised by a number of participants, one of whom expressed concern that there were `no proper statistics or understanding of exactly how lawyers are involved apart from the corrupt ones`.[31] This view was also expressed by the compliance participant who reflected:

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[27] Compliance Interview 6 dated 08/12/15.
[28] Compliance Interview 2 dated 24/11/15.
[29] The Law Society, `Intelligence shortcomings render anti-money laundering report findings misleading, warns legal sector` (*The Law Society*, 15 October 2015)< http://www.lawsociety.org.uk/news/press-releases/intelligence-shortcomings-render-anti-money-laundering-report-findings-misleading-warns-legal-sector/> accessed 26 July 2017.
[30] ibid.
[31] Compliance Interview 2 dated 24/11/15.

> There isn`t really any evidence that lawyers have been used to money launder, the ones that are is because they are actually corrupt.[32]

This concern is one which is shared by the Law Society, whose president stated, again in the context of the publication of the NRA 2015, that the involvement of lawyers in money laundering was `overstated` and that `professional enabler` involvement was `not supported by arrest or prosecution statistics.` [33] Whilst a detailed examination of the enforcement of the UK AML regime is outside the scope of this thesis, nevertheless it may be recalled from Chapter 2 that prosecutions of lawyers for money laundering offences are relatively rare, and typically involve complicit professionals.

(vi) The Pragmatic View - `Good` launderers will never be caught

The comments made by participants with regard to their AML obligations were also contextualised by reference to one overarching caveat: that lawyers, despite all best efforts and diligence, will be unable to identify `increasingly sophisticated` launderers.[34] This was an issue raised specifically in Chapter 5 with regard to the potential for launderers to obscure their beneficial ownership of entities, or make false declarations on the PSC Register. It was also an issue raised by participants in a more general context. Participants concluded that, `if you`re a good launderer we won`t spot you` and that `the real fraudster will always find a way`[35]. This pragmatic view was expanded upon by the partner who said:

> I think you`ve got to accept that your fence will never be perfect to stop the very, to say `better` money launderers is a bad word . . . the people who understand the system.[36]

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[32] Compliance Interview 7 dated 08/12/15.
[33] The Law Society, `Intelligence shortcomings render anti-money laundering report findings misleading, warns legal sector` (*The Law Society*, 15 October 2015) <http://www.lawsociety.org.uk/news/press-releases/intelligence-shortcomings-render-anti-money-laundering-report-findings-misleading-warns-legal-sector/> accessed 26 July 2017.
[34] Transactional Interview 8 dated 26/11/15.
[35] Compliance Interview 12 dated 26/02/16 and Compliance Interview 15 dated 10/03/16.
[36] Transactional Interview 5 dated 25/11/15.

That skilled launderers will avoid detection is not an issue unique to the legal sector. Rather, it is a reality which pervades the entire legitimate economy. However this reality did not prompt any participants to argue for deregulation based on the potential futility of AML measures in respect of committed launderers.

(vii) Concluding Comments On the Role of the Legal Profession

Responses from participants when discussing their role within the UK AML regime must be read in light of an overarching caveat: that those responses will be weighted against any form of self-incrimination. Nevertheless, many participants expressed an active willingness to comply with their AML obligations rather than objecting to the additional workload created by the regime. Furthermore, a number of participants reported declining to act for clients where they were unable to satisfy their CDD requirements, or where money laundering concerns were present.

The majority of participants felt that their role in the AML regime was appropriate, a view that was largely attributable to the unique role lawyers play when effecting a transaction. A number of participants even self-identified as `gatekeepers`. In contrast, only a small number of participants felt that their role was inappropriate to the extent that they felt overburdened, or that they were being asked to act as unpaid investigators. These findings suggest a considerable shift in the perception that lawyers have of their AML role since AML obligations were initially imposed upon the profession amidst widespread consternation.

This shift in perception may well be driven by a general maturation of the regime, and indeed a number of participants stated that their role as a lawyer had evolved over the years to include AML. Many participants referred positively to the maturation of the regime, in that both law firms and clients had become more familiar with the regime. More specifically, this maturation offered specific benefits such as the streamlining of CDD processes, and a potential reduction in defensive reporting. Both these refinements may have the effect of improving the efficiency of the AML regime overall.

Two further themes were evident from participants` responses when discussing their AML role. A number of interviewees felt that the profession`s involvement in money laundering was both misunderstood and overstated, particularly as presented in the NRA 2015, which is a view shared by the Law Society. The low number of prosecutions of lawyers for money laundering offences, and limited academic scrutiny of the area, however, means that it is not possible to paint an accurate picture of lawyer involvement in money laundering.[37] It also means that it is not possible to determine whether this particular perception of participants` is accurate or not.

Reflections on their role within the AML regime were also accompanied by a pragmatic acknowledgment from some participants that `good` launderers will never be caught. However, this acknowledgment was simply made as a statement of fact, rather than being used as a springboard to call for more deregulation.

Complying with the extensive AML obligations imposed upon the legal profession in the UK comes at a cost, and it is this aspect of the regime that will now be considered, together with any perceived benefits of such compliance.

2. The Costs and Benefits of AML Compliance

(i) The Cost of AML Compliance

(a) Background

The cost burden of AML compliance across the regulated sector was highlighted in the government`s Action Plan 2016, with the British Bankers` Association estimating compliance costs within their sector to be £5bn per annum.[38] Whilst there is no recent `headline` figure available in respect of the legal sector, a survey of 125 firms on CDD costs by the Law Society in 2016 revealed the following: that over 30% of those firms expended over £100,000 annually in CDD related staffing

[37] See Chapter 1 of the thesis.
[38] Home Office and HM Treasury, *Action Plan for anti-money laundering and counter-terrorist finance* (2016) 12.

costs, whilst 22% expended over £200,000 per annum.[39] Spend on internal systems for nearly a quarter of firms ranged between £5-25,000 per annum.[40] Of those firms that reported using external databases (61%), some reported spending over £200,000 per annum on such services.[41] Furthermore, 84% of firms felt that CDD costs would rise following the transposition of 4MLD.[42] A small scale survey of 21 top 100 firms by the Law Society in 2009 indicated combined `easily quantifiable` AML costs across participant firms of £6.5 million.[43]

The term `easily quantifiable` costs hints at the difficulties inherent in accurately calculating AML costs, with a number of participants of the view that AML costs were `very hard to quantify`.[44] Firms may be able to calculate those `hard` costs attributable to compliance staff, training providers and third party database providers. In contrast, the `soft` costs attributable to the time a fee earner spends on AML compliance and ongoing monitoring are much harder to quantify. This distinction was explained by the MLRO who said in relation to their centralised compliance team costs:

> It doesn`t capture the full cost, because it doesn`t capture the fee earner`s involvement if we have to get information from them.[45]

For some participant firms, even the hard costs may be difficult to quantify. Their dedicated compliance teams were typically tasked with dealing with a whole range of compliance issues such as sanctions screening or conflicts checking, meaning that an assessment of AML costs in isolation is not always feasible.

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[39] The Law Society, *HM Treasury consultation on the transposition of the Fourth Money Laundering Directive – The Law Society Response* (2016) 4.
[40] ibid 5.
[41] ibid.
[42] ibid.
[43] The Law Society, *The costs and benefits of anti-money laundering compliance for solicitors - Response by the Law Society of England and Wales to the call for evidence in the Review of the Money Laundering Regulations 2007*(2009) *27; s*ee also an earlier study by the Law Society in 2008 where 20 firms revealed AML costs ranging from `thousands of pounds to millions of pounds`, ibid 48.
[44] Compliance Interview 2 dated 24/11/15.
[45] Compliance Interview 20 dated 16/06/16.

Participants were not asked to quantify their AML compliance costs for the reasons set out above. Rather, they were asked for their views on those costs, with their responses explored below.

(b) Participants` Views on Compliance Costs

Participants were fairly evenly split between those who felt that compliance costs were high or too high, and those who either did not perceive compliance costs as overly burdensome, or had no view on such costs. Those participants who perceived AML compliance costs as high or too high referred to them variously as `enormous`, `massive`, `significant` and `huge`.[46] Several participants observed that the aspects of legal practice relating to compliance were `significantly increasing` to a point where `risk is a great big growth industry`.[47]

In purely practical terms, many participant firms operated a dedicated compliance team. For many participants, AML compliance costs were either aggregated with other compliance costs and/or absorbed into the firm`s overhead costs. For a large majority of participants, no or only very limited AML costs were ever passed on directly to the client, although it was unclear from responses whether this was a reference to costs such as company searches or PEP searches, or a reference to a fee earner`s time.

(ii) The Benefits of AML Compliance

Participants identified multiple benefits stemming from compliance with the AML regime, notwithstanding such compliance is compulsory. The benefits explored below are in addition to the obvious and compelling benefit of avoiding imprisonment for non-compliance.

(a) Reputational Risk

A majority of participants identified brand protection of their firms as being a key benefit of AML compliance. At its most basic level, such protection arose from

[46] Compliance Interviews 12 and 2 dated 26/02/16 and 24/11/15, Transactional Interview 10 dated 26/11/15 and Compliance Interview 7 dated 08/12/15.
[47] Transactional Interviews 12 and 3 dated 01/12/15 and 18/11/15.

forestalling or spotting potential money laundering `because to be criminally implicated is . . . terrible for our reputation.`[48] As one partner added, `I think reputational risk is as high as the potential criminal risk`.[49]

On the basis that `pure money laundering risk is a subset of franchise risk`, responses from participants then tended to move away from considerations focussed simply on avoiding criminality. Participants discussed a number of aspects pertaining to reputational risk. As one compliance participant stated:

> . . . it`s slightly more complicated than just sort of saying it`s `brand` - there`s a lot of things that that make up that statement about brand.[50]

Adverse press was identified as one such aspect of `brand` on the basis that, `nobody wants it out there in the legal press that you got involved in a criminal transaction of some sort.`[51] In addition, a number of law firms provide compliance advice to other institutions as part of their legal practice, and therefore:

> . . . we have to make sure that we are getting these things right so that we can continue to bring in that work.[52]

Participants felt that the detailed CDD information required on client inception enabled law firms to make informed judgments as to whether to continue with the retainer in the context of reputational risk. As one participant explained:

> . . . sometimes there`s nothing `wrong` with that particular client, they're fully ID`d, they`re, you know, everything passes muster but they've been dealing in a way in a particular jurisdiction that you find might be difficult for you and for your clients and your reputation – I'd say for firms such as ours that that's where the main risk for us comes through.[53]

[48] Transactional Interview 7 dated 25/11/15.
[49] Transactional Interview 8 dated 26/11/15.
[50] Compliance Interview 14 dated 10/03/16.
[51] Transactional Interview 8 dated 26/11/15.
[52] Compliance Interview 14 dated 10/03/16.
[53] Compliance Interview 2 dated 24/11/15.

It is on this footing that `the company we keep` in terms of a firm`s client base was identified as having the potential to damage the reputation of the firm.[54]

Brand protection was also cast in such terms as having implications within the law firm itself, both for existing and potential future staff. This was reflected by the partner who stated `I want to be part of an organisation that is seen as slick and very professional`.[55] Maintaining a good reputation was also seen to be of benefit in terms of attracting future staff, an aspect highlighted by the MLRO who said:

> . . . through our reputation we attract good partners, new partners, lateral hires and good people coming out of the universities who want to be lawyers, so attracting new associates and trainees.[56]

In summary and in terms of AML non-compliance, the view of one MLRO was `never mind the kind of regulatory consequences, the brand consequences are profound.`[57] For one Deputy MLRO then, such brand protection was seen as a `fantastic knock-on benefit` of AML compliance.[58]

(b) Identifying and Understanding the Client Risk Profile

A number of participants were of the view that compliance with CDD requirements assisted in properly identifying the client and `who is behind our clients`.[59] Whilst identifying the client may seem a straightforward exercise, this is not always the case where sophisticated group company structures are in place across multiple jurisdictions. Thus, according to one MLRO, `the great thing about AML is it does focus people on working out who their client is`.[60]

The collection of CDD information means that law firms can make an informed decision as to whether to continue with the retainer, both from a risk perspective and, as highlighted in the previous section of this Chapter, from an interconnected

[54] Compliance Interview 13 dated 10/03/16.
[55] Transactional Interview 20 dated 11/03/16.
[56] Compliance Interview 15 dated 10/03/16.
[57] Compliance Interview 13 dated 10/03/16.
[58] Compliance Interview 9 dated 15/12/15.
[59] Compliance Interview 3 dated 25/11/15.
[60] Compliance Interview 17 dated 08/04/16.

reputational perspective. CDD therefore `enables us to get information on clients we would have liked to have got anyway`.[61] Law firms must then determine whether they are `comfortable with acting for that client.`[62] One compliance interviewee expanded on this benefit in the following terms:

> What CDD's about is just part and parcel of knowing who your client is and making a sensible decision as to whether you want to act for them, and ongoing monitoring is part and parcel of you keeping that relationship live and understanding where the risks are . . .[63]

(c) Collateral Benefits of CDD

Participants stated that obtaining detailed information in respect of a client also assisted with a host of other compliance matters such as sanctions compliance, conflicts checking, credit control, and establishing whether any disqualified directors are involved in the retainer. It is in this context that one participant deemed CDD checks to be:

> . . . simply necessary to understand the risks we are exposed to, manage them, and control a lot of other unrelated, or largely unrelated risk.[64]

For several participants, CDD information was also used to market more effectively to their clients. This collateral benefit of AML compliance was outlined by the Deputy MLRO who said:

> . . . so marketing – you know the group, you know the business, you know . . . what people are connected to, who the ultimate owners are, you know, and you can put that into your interaction database and you can market more effectively actually.[65]

[61] Transactional Interview 8 dated 26/11/15.
[62] Compliance Interview 17 dated 08/04/16.
[63] Compliance Interview 18 dated 08/04/16.
[64] Compliance Interview 5 dated 07/12/15.
[65] Compliance Interview 9 dated 15/12/15.

(d) Creating a `Clean` Corporate Culture

For some participants, AML compliance was valued on the basis that it fostered high ethical standards. This concept of `good corporate citizenship` was promoted by participants at an individual, firm, professional and societal level.[66] For example, with regard to individual lawyers, one MLRO`s focus was on the fact that `everybody has a personal responsibility and duty` to try and prevent money laundering. At a firm level, stalwart AML compliance was viewed as `a huge internal benefit which is part of our culture and values`.[67] AML compliance was perceived as being more than a purely practical exercise in `good housekeeping and good discipline`.[68] Rather, such compliance was seen as assisting the firm as a whole, whereby:

> . . . there are benefits to the firm in maintaining its professional good standards and that would include a clean, unblemished record for regulatory and compliance matters, including money laundering.[69]

Considering the legal sector as a whole, one transactional partner commented `we`re keen to make sure that we exude an ethical, responsible persona.`[70] The wider societal benefits of AML compliance were also considered by several participants, such as the partner who reflected:

> There is a whole moral element about ensuring best practice and ensuring business is done in the in the correct, ethical way.[71]

(iii) Concluding Comments on the Cost and Benefits of AML Compliance

Participants were fairly evenly split between those who felt that compliance costs were high or too high, and those who either did not perceive compliance costs as overly burdensome, or had no view on such costs. Quantifying such costs is particularly challenging as they comprise both those `hard` costs attributable to

[66] Compliance Interview 6 dated 08/12/15.
[67] Compliance Interview 19 dated 24/05/16.
[68] Transactional Interview 12 dated 01/12/15.
[69] Transactional Interview 14 dated 01/12/15.
[70] Transactional Interview 1 dated 18/11/15.
[71] Transactional Interview 19 dated 10/03/16.

training and compliance systems for example, in addition to those `soft` costs attributable to fee earner time expended on AML matters. For many participant firms, AML costs were aggregated with general compliance costs rather than segregated, making it more difficult to isolate, and therefore calculate, AML costs.

Regardless of their views on the costs of AML compliance, participants still identified many benefits attributable to effective AML compliance. The identification of those benefits may in turn have the effect of enhancing compliance with the regime. The most basic benefit, in addition to avoiding imprisonment, was that firms would be in a position to frustrate potential money laundering via their firms, thus avoiding criminality. Thereafter, brand protection was the most frequently cited benefit of AML compliance. The concept of brand protection was itself multi-faceted, encompassing fears surrounding adverse press, professional embarrassment for those firms providing external legal advice on AML, and difficulties surrounding attracting staff.

CDD was seen as beneficial, both in the mechanical sense of actually identifying the client, and in the broader sense of using such information to assess the risks attached to a particular client, both in reputational terms and in a broader commercial sense. A crossover with other compliance obligations was also identified, such as conflicts checking and sanctions compliance. Moreover, additional opportunities for cross-selling were identified, by mining effectively CDD information collected for AML purposes.

Such benefits were also set in a wider context: that of operating with personal and professional integrity in a manner which fostered an ethical environment at every level, ranging from the individual lawyer to society at large. In conclusion, the issues explored above can be summarised by the MLRO who said of AML compliance:

> First of all it`s the right thing to do. Secondly, we`ve got to do it, and thirdly if we don't do it there's a liability for the firm, there's a liability for individuals.[72]

[72] Compliance Interview 19 dated 24/05/16.

Having considered their role within the AML regime, and the attendant costs and benefits attributable to that role, participants were asked to consider the way in which the regime was regulated by the SRA and enforced. Their responses are explored below.

3. SRA Regulation and Enforcement of the UK AML Regime

As stated in Chapter 2, a detailed examination of SRA regulation, or enforcement of the UK AML regime within the legal profession is outside the scope of this thesis. Nevertheless, participants were asked for their views on these aspects of the regime in order to provide a holistic consideration of the regime.

(i) SRA AML Regulation of the Legal Profession

Many participants expressed a variety of negative views with regard to the SRA as an AML regulator. A number of those participants, the vast majority of whom were compliance participants, felt that the SRA were a weak and `ineffectual` AML regulator.[73] This view can be summarised by the MLRO who stated simply, `as an AML regulator, frankly, I don`t think they do a great deal.`[74] Several participants felt that the SRA should have `more teeth` as an AML regulator, such as the compliance participant who stated, `proactive regulation I think is something that they could do more often . . . a regulator needs to be on your shoulder a bit.`[75]

A small number of participants felt that the SRA were under-resourced, such as the MLRO who stated:

> I suspect they`re under-resourced in terms of the number of people they can deploy - of course the flipside of the coin is they`re stretched because of the large number of firms that there are in the . . . country.[76]

The comments on under-resourcing were not restricted to numbers of employees either, with several participants perceiving a lack of `breadth or depth` in terms of

[73] Compliance Interview 5 dated 07/12/15.
[74] Compliance Interview 19 dated 24/05/16.
[75] Compliance Interview 10 dated 15/12/15.
[76] Compliance Interview 15 dated 10/03/16.

AML expertise within the organisation.[77]

Criticisms were also levelled by a number of participants at the SRA Anti Money Laundering Report published in 2016.[78] Visits by the SRA to participant firms to gather information for the thematic review were deemed to be superficial by several participants. In addition, it was felt that the SRA did not `raise any sort of insightful questioning at all` or `ask difficult questions.`[79] As one MLRO commented, `I can`t say it was a grilling.`[80]

Fewer participants expressed positive views with regard to SRA regulation, with such positive comments largely focussing on the thematic review referred to in the previous paragraph. According to one Deputy MLRO whose firm was visited by the SRA, `that did more for raising the profile of money laundering issues than I think anything to date.`[81] Several participants were reassured by the SRA visit as providing a `bit of comfort` that their firm`s AML systems were appropriate. In a more general context, a few participants were of the view that the SRA were improving with regard to their AML awareness within the sector.

A large number of participants, the vast majority of whom were transactional participants, had no view on the SRA as an AML regulator. It is important to note, however, that this lack of any view was typically on the basis that, as explained by one partner, `I don`t deal with the SRA, our compliance team would`.[82] Therefore many participants did not feel sufficiently exposed to the SRA to form a meaningful view.

(ii) Enforcement of the AML Regime

It may be recalled from Chapter 2 that enforcement action may comprise regulatory action by the SRA and SDT or prosecution by the CPS. Participants were

[77] Compliance Interview 5 dated 07/12/15.
[78] SRA, *Anti Money Laundering Report* (2016).
[79] Compliance Interviews 18 and 1 dated 08/04/16 and 17/11/15.
[80] Compliance Interview 15 dated 10/03/16.
[81] Compliance Interview 9 dated 15/12/15.
[82] Transactional Interview 7 dated 25/11/15.

not asked to comment on each aspect of the enforcement regime, but rather to reflect on the enforcement regime overall.

A small majority of participants, including a number of compliance participants, either had no view on the enforcement of the AML regime, or felt that they had insufficient exposure to or involvement in enforcement matters, making it `difficult to comment`.[83] Many interviewees, most of whom were compliance participants, were of the view that the regime was poorly enforced, such as the MLRO who commented that `the enforcement I think is lax`.[84] It was this laxity which prompted one MLRO to state:

> I don't know of a firm that has been told off for not having a proper regime in place . . . they should be enforcing more I think.[85]

This view was echoed by the MLRO who reflected, `I'm not aware of a case where the criminal sanctions under the MLR have been deployed.`[86]

A small number of participants felt that there was some enforcement in respect of serious breaches, such as the participant who recollected:

> . . . people aren't hauled up before the courts as I understand it for sort of technical breaches of things that have gone wrong, the cases I've read about have been, to me, seemed quite serious.[87]

The dearth of prosecutions within the sector for the failure to report offences set out in s 330-1 POCA 2002 was attributed by one participant to the fact that `there aren`t that many where they can show that the person wasn`t in on it`.[88] The consequence of this failure to prosecute lawyers then means that:

[83] Compliance Interview 8 dated 14/12/15.
[84] Compliance Interview 15 dated 10/03/16.
[85] Compliance Interview 16 dated 14/03/16.
[86] Compliance Interview 15 dated 10/03/16.
[87] Compliance Interview 17 dated 08/04/16.
[88] Compliance Interview 6 dated 08/12/15.

> . . . your evidential basis on which to keep complaining that there is concern from a professional enablers perspective is weak.[89]

It is this lack of evidence with regard to the involvement of the profession in money laundering activities, raised both in Chapter 1 and earlier in this Chapter, which has caused particular concern amongst participants and the sector at large. Such poor enforcement can be seen as leading to much broader consequences. For one Deputy MLRO, poor enforcement resulted in a regime which is `fundamentally devalued` and `flawed.`[90]

A number of participants felt that the SRA should be far more robust and proactive in their enforcement of the regime, such as the MLRO who stated `they should be enforcing more I think.`[91] The value of SRA enforcement cases then being publicised was drawn out by one MLRO on the basis that:

> . . . it`s a useful way of educating people within the firm if you`ve got a range of examples of what`s happened when AML has gone wrong. [92]

For the reasons set out earlier in this thesis, the way in which information is collated in relation to AML enforcement within the sector means that it is extremely difficult to construct a meaningful picture of enforcement. This drawback was recognised by Transparency International UK in their 2015 report on UK AML supervisors, stating in respect of the legal sector:

> . . . as a result of the limits in information on specific enforcement outcomes, there is a lack of public understanding relating to the nature of AML enforcement and the specific details of enforcement cases.[93]

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[89] Compliance Interview 6 dated 08/12/15.
[90] Compliance Interview 9 dated 15/12/15.
[91] Compliance Interview 16 dated 14/03/16.
[92] Compliance Interview 19 dated 24/05/16.
[93] Transparency International UK, `Don`t Look, Won`t Find Weaknesses in the Supervision of the UK`s Anti-Money Laundering Rules`, (*Transparency International UK*, November 2015) 39 < http://www.transparency.org.uk/publications/dont-look-wont-find-weaknesses-in-the-supervision-of-the-uks-anti-money-laundering-rules/>accessed 3 August 2017.

It is this lack of visibility surrounding enforcement that prompted one Deputy MLRO to state:

> There isn't any enforcement you know, and actually if I'm going to invest £X million in a compliance program, I like to know that the people who aren`t investing £X million in their compliance program . . . are exposed to enforcement risk.[94]

(iii) Concluding Comments on SRA AML Regulation and Enforcement

Whilst many participants had no views on the SRA as an AML regulator, typically attributable to their status as transactional participants, a number of participants felt that the SRA were a weak AML regulator, with several expressing a desire for more proactive regulation. The challenges surrounding AML regulation were acknowledged however, and several participants expressed the view that the SRA were under-resourced, both in terms of staff and level of expertise.

The SRA Anti Money Laundering Report 2016 attracted criticism on the basis that the SRA visits to participant firms providing AML information were superficial and did not ask challenging questions. In contrast, and whilst fewer positive comments were made in relation to SRA AML regulation overall, a number of positive comments focussed on the SRA visits as part of their thematic review of AML. For a number of participant firms, the SRA visits had the effect of raising awareness of AML within their firms, and provided some level of validation with regard to their AML systems, policies and procedures. A few participants felt that the SRA were improving their levels of awareness of AML within the sector.

A small majority of participants either had no view on the enforcement of the regime, or felt insufficiently exposed to it to comment. This may not be too surprising given that enforcement action, by whatever means, is not an ordinary feature of day of day practice, even for those fulfilling a compliance role. Many participants were of the view that the regime is poorly enforced in respect of all

[94] Compliance Interview 9 dated 15/12/15 (`X` added for anonymity).

but the most serious of breaches. It was also noted that a lack of visibility over enforcement cases deprives the sector of a useful AML education tool.

Perceptions of a weak, ineffectual and under-resourced regulator overseeing a regime that is poorly enforced may have a collateral detrimental effect on AML compliance however, although it may also be the case that the many benefits identified by participants serve to outweigh this effect. In the alternative, it is possible that the regime is appropriately enforced and that the brouhaha surrounding lawyers as professional enablers and facilitators is unjustified.

4. Assessment of Money Laundering Risk

A further prominent theme evident from the interview data was the way in which participants assessed and classified money laundering risks to their practices. Within 4MLD, and thereafter MLR 2017, there is a significant focus on the assessment of money laundering risks at all levels. Hence the MLR 2017 require risk assessments to be conducted at a national level, by supervisory authorities, and by the regulated sector.[95] Law firms must assess risks according to the `size and nature` of their business, and by reference to a range of risk factors including client identity, jurisdiction and the nature of transactions undertaken or services offered.[96] Participants were therefore asked what they considered to be the money laundering risks to their firms overall. Thereafter, participants were asked to categorise the level of risk that money might be successfully laundered through their firms as low, medium or high. In addition to identifying those specific risks referred to below, a number of participants reiterated the significance of the reputational risk to their firms in respect of any potential involvement in laundering.

[95] MLR 2017, regs 16-18.
[96] MLR 2017, reg 18(3) and 18(2)(b).

(i) Firm Level Money Laundering Risks

(a) Jurisdictional Risks

For a majority of participants, jurisdictional risk was identified as a key money laundering risk to their firms overall, and was the risk most frequently cited. Many participant firms operated internationally and therefore jurisdictional risk was frequently considered in a global context. Particular emphasis was placed upon those risks inherent in dealing with jurisdictions where, put diplomatically, `there`s perhaps not as much focus on bribery and corruption`.[97] The challenge that this then presented for many participant firms was articulated by the MLRO who said:

> We are an international firm, so the threats that we see come from countries which you would classify as being particularly high risk, where the likelihood for there to be money laundering where people in positions of responsibility are more likely to be corrupt – that's the area we look at particularly carefully.[98]

Dealing in jurisdictions deemed to have a `sorry reputation for lack of integrity` are a particular risk for law firms on the basis that the firm may become inadvertently involved in laundering funds during the course of a retainer.[99] This risk may arise, for example, where a law firm acts for a client acquiring a target company in a high-risk jurisdiction with a `badge of shame` attached to it in terms of its AML standards.[100] This risk is particularly acute, according to one partner:

> . . . where you are making acquisitions in what I would call `frontier` jurisdictions, so a lot of the African jurisdictions, a lot of the south-east Asian jurisdictions, where in order to get things done people have, you know, in the past greased some palms.[101]

[97] Compliance Interview 14 dated 10/03/16.
[98] Compliance Interview 3 dated 25/11/15.
[99] Compliance Interview 15 dated 10/03/16.
[100] Compliance Interview 15 dated 10/03/16.
[101] Transactional Interview 9 dated 26/11/15.

It was also acknowledged that dealing in jurisdictions such as offshore centres, where `secrecy is paramount . . . for legitimate *and* illegitimate reasons` posed a particular challenge for law firms in terms of the opacity of beneficial ownership information.[102] In addition to offshore jurisdictions, such as BVI and the Cayman Islands, referred to by one participant as `the usual suspects` in terms of the AML challenges they present, participants pinpointed a number of jurisdictions which they considered as high risk in the context of their firms. [103] Such jurisdictions included Africa, central and eastern Europe, the former Soviet republics, the Middle and Far East, emerging markets, Asia, Russia and Ukraine.

At a practice area level, jurisdictional risk was also the most commonly cited money laundering risk. Hence overseas investors, `offshore ownership` or those corporate transactions involving an `overseas wrapper`, were identified as posing a potential money laundering risk.[104]

There are many subcategories of risk falling within the umbrella category of `jurisdictional` risk however. For participant firms for example, money laundering risks relating to the source of funds or wealth, counterparty risks and PEPs will frequently involve an international element. It is to these risks that this Chapter now turns.

(b) Risks Relating to Particular Clients – New Clients, PEPs and Wealthy Individuals

Several participants felt that new clients posed a particular money laundering risk to their firms at the point of inception, such that:

> . . . one clearly needs to have a level of scrutiny about who they are, what they do, and what their context and financial backing is . . . that is ever more complex and challenging` [105]

One participant outlined their concern as follows:

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[102] Compliance Interview 2 dated 24/11/15 (emphasis added).
[103] Compliance Interview 7 dated 08/12/15.
[104] Transactional Interviews 11, 15 and 12 dated 26/11/15, 08/12/15 and 01/12/15.
[105] Transactional Interview 2 dated 18/11/15.

> The risk is new clients where you're on heightened alert . . . maybe they're in a difficult jurisdiction and . . . you know, if the relationship hasn't been a long one, the trust hasn't built up.[106]

Specific client types were also identified as a money laundering risk by a number of participants, such that overall, for one MLRO, `the key risks for a firm of this size relate to its client base`.[107] High risk clients included foreign PEPs (domestic PEPs were not included within the definition of `PEP` at the time of the interviews), which is unsurprising given that under MLR 2007 PEPs were deemed to be high risk and EDD automatically applied to them. High net worth individuals, private equity investors, and Russian oligarchs in particular, were also considered to be a money laundering risk for a number of participants, as was also the case at the practice area level. As one MLRO commented:

> We have acted in the past and continue to act for Russian oligarchs . . . when they are taken onto our client base they throw up all sorts of issues – identification, CDD but most of all the provenance of the monies.[108]

Several participants were alive to the risk posed by such wealthy individuals, including the Deputy MLRO who stated:

> . . . where we`re dealing with their personal assets, you know, I think there is potentially a risk of money laundering there in its kind of strictest sense.[109]

(c) Source of Funds or Wealth Risk

The illicit source of funds or `provenance of the monies` relating to a transaction was raised as a money laundering risk by a number of participants.[110] The issues that arose for participants relating to establishing a client`s source of funds and source of wealth were considered in Chapter 5. For some participants, this risk was

[106] Transactional Interview 8 dated 26/11/15.
[107] Compliance Interview 15 dated 10/03/16.
[108] Compliance Interview 15 dated 10/03/16.
[109] Compliance Interview 9 dated 15/12/15.
[110] Compliance Interview 15 dated 10/03/16.

partly attributable to their international client base. In this context, the risk was identified by one compliance participant as:

> . . . funds coming in from all sorts of jurisdictions really, and actually identifying the *true* source of those funds and the source of wealth of clients.[111]

Similarly, at a practice area level, the `identification of funds which are used to fund transactions, and understanding where those funds come from` were perceived as being key areas of concern for a number of participants.[112]

For other participants, the funding risk arose in a far narrower context. A few participants referred to last minute changes to the source of funds on a transaction as a potential risk, which is considered as one of the classical indicia of money laundering.[113] This risk was identified by the partner who reflected:

> . . . all you need is money coming in from a different source on a closing and . . . not noticing that actually this wasn't the recognised source.[114]

Another participant recounted their transaction experience such that:

> . . . sometimes you see `oh, I'm sending the funds from this entity` and then two minutes before the completion they come from a totally different entity.[115]

Such last minute changes to funding may well be entirely benign, particularly with regard to complex group company structures, but can result in delaying a transaction whilst the law firm in question satisfies itself with regard to the revised funding arrangements.

[111] Compliance Interview 1 dated 17/11/15 (emphasis added).
[112] Transactional Interview 9 dated 26/11/15.
[113] See The Law Society, *Anti-money laundering Practice note* (2013) *para 11.2.2.*
[114] Transactional Interview 17 dated 16/12/15.
[115] Compliance Interview 7 dated 08/12/15.

(d) Deal Risk

A number of participants stated that the money laundering risks to their firms arose due to the nature of their business: namely undertaking high value, fast paced, complex, cross-border transactions. This view is illustrated by the participant who identified inherent money laundering risks relating to:

> . . . the sheer scale of our business and the nature of the deals we`re doing and the geographical spread of our business.[116]

A few participants perceived those risks as increasing as their firms expanded, both geographically and in terms of practice area.

Participants identified one further aspect of deal risk which was also raised by several participants in relation to their practice areas: that of counterparty risk, ie in respect of the other party to a client`s transaction. This risk was outlined by the compliance participant who said in respect of counterparties to a transaction:

> . . . it`s probably a slightly higher risk from other parties that might be involved in a transaction because it is more difficult to carry out due diligence on those parties.[117]

As mentioned previously in this Chapter, the issue may arise in the context of acting for a client on the acquisition of a target company whose activities may give rise to criminal property under the provisions in POCA 2002, and therefore implicate the law firm itself.

(e) The Breadth of POCA 2002

Several participants were acutely mindful of the fact that their firms could be targeted by money launderers. This was highlighted by the MLRO who said:

> . . . we are clearly well aware that law firms can be targeted, and indeed have been targeted and used by criminals to launder the proceeds of crime.[118]

[116] Compliance Interview 5 dated 07/12/15.
[117] Compliance Interview 1 dated 17/11/15.

For one partner then, `the concern would be that you inadvertently become tied up in a transaction that is in fact being used for an improper purpose`.[119]

For a greater number of participants however, those `technical` breaches which were discussed in Chapter 4 were considered to be a money laundering risk to their firms. It may be recalled that a technical breach causing property to become criminal for the purposes of POCA 2002 will require a SAR to be made by the law firm to the NCA, and consent obtained to continue with the transaction on behalf of their client. Failure to submit a SAR and obtain consent may trigger liability within the law firm under the substantive money laundering offences. An example of this risk in respect of such `technical` breaches was provided by the compliance participant who explained the way in which this issue affected law firms as follows:

> . . . like your share acquisitions where there's been a . . . strict liability offence like asbestos where we are looking to buy the shares in a company, and strictly speaking if they haven't complied with it then it's a criminal offence, and theoretically we're laundering, or could be laundering unless we get consent.[120]

Whilst this risk of money laundering linked to technical breaches was raised by a number of participants, it was also cast as a risk `at the lower end of the spectrum in terms of seriousness of crimes.`[121] This led one MLRO to conclude with regard to technical breaches, ` that sort of risk we live with all the time. It's a risk - is it a real one? No not really.`[122]

(f) Practice Area Risks

Specific practice areas were identified as presenting a heightened risk of money laundering. These practice areas included corporate, finance, and, most prominently, real estate. Acting for high net worth individuals such as PEPs and

[118] Compliance Interview 17 dated 08/04/16.
[119] Transactional Interview 1 dated 18/11/15.
[120] Compliance Interview 11 dated 19/02/16.
[121] Compliance Interview 14 dated 10/03/16.
[122] Compliance Interview 8 dated 14/12/15.

oligarchs or private equity funds was also considered as a money laundering risk by a number of participants within their practice areas.

The particular focus on real estate as a high risk practice area is unsurprising. First, buying and selling property, as outlined in Chapter 1, is one of the more `traditional` money laundering typologies via the legal profession.[123] Secondly, widespread money laundering concerns have been raised with regard to the purchase of UK property by foreign investors.[124] Frequently, those concerns relate to the purchase of properties in London by Russian oligarchs.[125] Typically therefore, it was acknowledged that `it`s often an easy way to launder money by buying real estate, usually using . . . corporate vehicles.`[126] Participants were extremely aware of the elevated money laundering risk surrounding this particular practice area, such as the partner who stated, `I would say that the risk is potentially quite high in relation to the area that I work.`[127]

The money laundering risks identified within practice areas broadly reflected those identified as a firm level risk. Accordingly, jurisdictional risk was the most frequently cited risk. Similar concerns were also raised with regard to identifying the source of funds/wealth on a transaction, and the potential risk that counterparties posed. Each of these aspects of risk is considered in the previous paragraphs of this Chapter.

A number of participants, including a very small number of real estate practitioners, were of the view that the nature of their client base had the effect of mitigating their money laundering risk to a certain extent. Thus, for one transactional participant:

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[123] *FATF, Money Laundering and Terrorist Financing Vulnerabilities of Legal Professionals* (2013) *44-53.*

[124] Transparency International UK, `Faulty Towers: Understanding the Impact of Overseas Corruption on the London Property Market` (*Transparency International UK*, March 2017) < http://www.transparency.org.uk/publications/faulty-towers-understanding-the-impact-of-overseas-corruption-on-the-london-property-market/> accessed 30 July 2017.

[125] Olga Smirnova, `Just who owns what in central London?` (*BBC News*, 21 March 2016) < http://www.bbc.co.uk/news/business-35757265> accessed 30 July 2017.

[126] Transactional Interview 17 dated 16/12/15.

[127] Transactional Interview 19 dated 10/03/16.

> A lot of our clients will either be major corporates, or will be major UK corporates or major overseas corporates, a lot of them will be listed companies, so I think from that perspective that probably reduces risk.[128]

For those participants with a `lender led` or funder led client base, such as those acting for `well-known mainstream banks` for example, the money laundering risk was also perceived as lower due to the nature of those clients.[129]

(ii) Classification of Money Laundering Risk at a Firm Level

A large majority of participants classified the risk that money would be *successfully* laundered through their firms as low, with few participants rating the risk as medium or high. Two clear factors influenced the classification of risk as low: (i) the robust AML procedures implemented by participant firms, and (ii) the client base of such firms.

A number of participants were of the view that `strong or stringent` AML procedures within their firms mitigated the money laundering risks posed.[130] This analysis can be illustrated by the transactional partner who commented:

> I think that like most firms of our size, our processes and procedures are such that minimise the chances of us being inadvertently involved in that kind of thing, so . . . I don't have any particular concerns that the firm is likely to be used in that way.[131]

This view was endorsed by the MLRO who said of their firm`s AML procedures:

> The systems are strong, they`re constant, they`re known, they`re respected, they are not . . . automated.[132]

The second factor which influenced participants in their classification of successful money laundering through their firms as a low risk was the nature of their firms`

[128] Transactional Interview 11 dated 26/11/15.
[129] Transactional Interview 19 dated 10/03/16.
[130] Transactional Interview 16 dated 08/12/15.
[131] Transactional Interview 1 dated 18/11/15.
[132] Compliance Interview 15 dated 10/03/16.

client base, both in terms of their clients` identity and the length of those client relationships. This was also a feature in respect of the practice area risks identified earlier in the Chapter. For firms acting for `blue-chip or institutional` clients, for example, `they`re more of a known quantity and the risk is lower because of the identity of the client.`[133] Similar considerations were applied in respect of listed or regulated entities, a position set out by the compliance participant who said:

> The vast majority of our clients are regulated institutions or listed companies . . . who would already be looking at their systems and have done for many, many years.[134]

The length and depth of that client relationship was another factor taken into consideration by participants when categorising risk. A lower risk was assigned where, in the words of one partner, `we . . . understand and know our clients really well.`[135] Of key importance then, as articulated by one compliance participant, is the `client selection piece` which entails:

> . . . making sure that we are acting for the right clients, and we do quite a substantial amount upfront in terms of . . . money laundering risk analysis.[136]

Quite simply, for one participant `we are *very very* careful in who we take on as a client.`[137]

A number of participants placed a strong emphasis on the fact that a low classification of risk did not equate to any relaxation of their AML vigilance. Such participants stated that they were still very much aware of the potential risk of money laundering and remained on `high alert`.[138] For one MLRO, a low risk

[133] Compliance Interview 11 dated 19/02/16.
[134] Compliance Interview 18 dated 0/04/16.
[135] Transactional Interview 20 dated 11/03/16.
[136] Compliance Interview 14 dated 10/03/16.
[137] Transactional Interview 7 dated 25/11/15 (emphasis added).
[138] Transactional Interview 8 dated 26/11/15.

classification was `not to say we are in any way cavalier or relaxed about the risks`.[139] This dynamic was expanded upon by the MLRO who said:

> I actually think the risk is probably relatively low, but . . . that is not to say it doesn't exist, and it doesn't mean that I approach my job and my responsibilities on the basis that the risk is low, because however high or low the risk is, if it exists it`s my job and the job of those who work with me to ensure that we deal with that risk in an appropriate . . . way.[140]

(iii) Concluding Comments on Firm Level Risk

For a majority of participants, jurisdictional risk was identified as a key money laundering risk for their firms. At a `headline` level, issues arose in respect of jurisdictions where opacity is commonplace, such as offshore jurisdictions, but also in respect of those jurisdictions at a higher risk of corruption. The example provided by several participants is that they potentially become inadvertently participative in money laundering where their client is acquiring a target company in respect of which criminal property arises for the purposes of POCA 2002. In the absence of NCA consent, potential liability for a substantive money laundering offence arises. Jurisdictional risk has many facets to it, and it pervades several other categories of risk identified by participants. For example, the difficulties surrounding identifying the true source of funds or wealth on a transaction are often made more challenging when placed in an international context. Deal risk can also be viewed as a subset of jurisdictional risk where the sheer size, complexity and cross-border nature of many transactions with counterparties from `racy` jurisdictions elevates the money laundering risk on a given transactions.[141]

Particular client groups were identified as posing an elevated money laundering risk. New clients, about whom less information is known, were identified as a risk at the point of inception. Inevitably foreign PEPs were deemed to be high risk given that the MLR 2007 assigned them a high risk rating where EDD automatically

[139] Compliance Interview 13 dated 10/03/16.
[140] Compliance Interview 17 dated 08/04/16.
[141] Transactional Interview 17 dated 16/12/15.

applied.[142] High net worth individuals, and Russian oligarchs in particular, together with private equity investors were also perceived as presenting a heightened risk of money laundering.

The sheer breadth of POCA 2002 was identified as presenting a firm level risk of money laundering. This is on the basis that failure to obtain NCA consent in respect of those `technical` breaches discussed in Chapter 4 have the potential to trigger a substantive money laundering offence within law firms.

Specific practice area risks were also identified. Corporate, finance and real estate practice areas were viewed as presenting particular money laundering risks, although that risk was perceived as being mitigated to a certain extent where the client base consisted of high profile listed or institutional clients. One very specific threat was also highlighted: namely where there are last minute changes to the source of funding on a transaction, which is traditionally seen as a classic hallmark of money laundering. Such changes may well be benign in the context of complex group company structures, but they do have the effect of halting a transaction whilst further enquiries are made.

A large majority of participants classified the risk of money being successfully laundered through their firms as low. The rationale behind this classification drew upon two distinct strands. Participants felt that the strength of their firm`s AML policies and procedures was sufficient to forestall such attempts. Furthermore, and as for practice area risks, a client base comprising regulated or listed entities or institutional investors was perceived as mitigating the money laundering risk to a certain extent. This was also the case where those clients were well known to the firm.

By its very nature money laundering is a clandestine pursuit and therefore it is not possible to determine with any accuracy whether participants` perceptions and classification of risk align with the reality of those risks for their firms. Law firms must therefore be guided by the risk categories set out in the MLR 2017 together with sector specific guidance from the Law Society.

[142] MLR 2007, reg 14.

Just as jurisdictional considerations were a prominent theme when assessing money laundering risks, the positioning of UK law firms serving an international client base in a global market also attracted significant comment from participants. Those comments are explored below.

5. UK Law Firms in a Global Context

(i) Are UK law Firms at a Competitive Disadvantage Internationally?

Many participant firms operated on a global basis and therefore were required to comply with differing AML regimes across multiple jurisdictions, with a number of firms electing to apply a global AML standard. Within that global context, the UK has a more stringent AML regime than many jurisdictions, both within the EU itself and internationally, such as the US for example.

Participants were therefore asked whether they felt the level of AML regulation in the UK put UK law firms at a competitive disadvantage on an international playing field, a consideration that has become ever more relevant as the UK now contemplates a post-Brexit future. A small majority of participants stated that UK law firms were not at a competitive disadvantage due to the high level of regulation in the UK. Furthermore, rather than being a disadvantage, a number of those participants highlighted the positive advantages of operating in a highly regulated environment. First, several participants stated that English law was attractive as a choice of law in an international context, such as the transactional participant who said:

> . . . people don`t choose UK law firms because of . . . the level of regulation they`re under, they chose them because of English law.[143]

Secondly, a number of participants felt that it was an advantage for clients to transact business in the `safer` environment provided by the UK.[144] On this basis, for one MLRO, `being regulated is an attraction because clients can come to us with

[143] Transactional Interview 10 dated 26/11/15.
[144] Compliance Interview 4 dated 03/12/15.

confidence.`[145] This advantage was expanded on further by the transactional partner who said:

> I think actually our rigour around regulation is to some extent why, you know, London and the UK have historically been seen as a good market to operate in because we do police it, we do actually have rigour around our regulation.[146]

Finally, a number of participants were of the view that the level of regulation in the UK served to discourage prospective launderers, or those `people who are doing wrong` from transacting via the UK.[147] Of clients reluctant to comply with the UK AML regime for example, one partner reasoned that:

> . . . if you want to go somewhere because it's so important to you that you don't have to comply with this information, I almost think probably that's not a client we want.[148]

Ultimately, this led one compliance participant to conclude that:

> I'd rather be commercially disadvantaged and not end up dealing with criminals and money launderers than take on work that we shouldn't be doing.[149]

Far fewer participants felt that the UK AML regulatory regime did put UK law firms at a competitive disadvantage. This disadvantage was felt in comparison to other EU countries on the basis that `there`s a much higher bar for UK law firms than there is for many of our European competitors.`[150] Other participants reported feeling competitively disadvantaged on an international stage, particularly when compared to the less stringent AML requirements in the US. It is this disparity

[145] Compliance Interview 8 dated 14/12/15.
[146] Transactional Interview 20 dated 11/03/16.
[147] Transactional Interview 12 dated 01/121/5 (emphasis added).
[148] Transactional Interview 8 dated 26/11/15.
[149] Compliance Interview 5 dated 07/12/15.
[150] Compliance Interview 1 dated 17/11/15.

which prompted one compliance participant to recount, `The US look at us like we`re crazy people when we ask them for CDD stuff.`[151]

(ii) Concluding Comments on Competitive Disadvantage

A majority of participants concluded that UK law firms were not at a competitive disadvantage in an international context due to the high level of AML regulation in the UK. Indeed, a number of key advantages stemming from such stringent AML requirements were identified. Participants stated that clients were more likely to be attracted to a properly regulated market subject to English law, and money launderers potentially diverted to other jurisdictions with lower levels of regulation. Far fewer participants felt UK law firms were at a competitive disadvantage, but those that did felt disadvantaged both within the EU and internationally, particularly in comparison to the US.

Perhaps the correct question is not whether UK law firms are competitively disadvantaged or not, but rather `whether that competitive disadvantage is one that is right to have`.[152] With regard to a highly regulated AML environment the reframed question then becomes, in the words of one partner:

> . . . do I think that the competitive disadvantage it puts us against somewhere that doesn't have that, is that worth it? I would say that it was because I think that it's important.[153]

The question for the UK therefore is whether having an ornate and costly regulated environment is worth it. It is a question that the UK, in response to the inestimable economic and human cost of money laundering, has answered in the affirmative.

6. Chapter Summary

This Chapter has explored the perceptions that participants have of the AML regime, and their role within it. That the majority of participants felt their AML role was appropriate suggests a real shift in perception over the last decade, given the

[151] Compliance Interview 6 dated 08/12/15.
[152] Transactional Interview 5 dated 25/11/15.
[153] Transactional Interview 5 dated 25/11/15.

objections that were raised when the sector first became subject to AML obligations. This shift may well form part of a more general maturation of the regime, and responses from participants also suggested a streamlining in CDD processes and a potential reduction in defensive reporting. Far fewer participants felt that they were being cast as unpaid policemen, although there was a perception that legal professional involvement in money laundering was both misunderstood and overstated, and that truly skilled launderers would never be caught.

Many benefits of AML compliance were identified, the most prominent of which was brand protection of the law firm. Thereafter AML compliance was perceived as assisting with client identification, cross-selling to clients, and other compliance activities such as sanctions compliance. It was also reported that AML compliance fostered a clean corporate environment.

Many participants had no views on the SRA as an AML regulator, whilst a number of participants felt that the SRA were a weak AML regulator. Enforcement of the regime was also considered to be weak. The concern that this raises is that a regulator perceived of as being weak, in tandem with a regime that is perceived to be poorly enforced is not a compelling driver of AML compliance, although the benefits outlined above might counteract this potential negative effect. The alternative is that the regime is being appropriately enforced, but that the extent to which lawyers are involved in money laundering has been widely exaggerated by multiple organisations including FATF and the NCA.

Money laundering risks were identified as: (i) jurisdictional risks, (ii) risks from particular client groups such as new clients, high net worth individuals, PEPs and private equity investors, (iii) the `all crimes` approach of POCA 2002, (iv) practice area risks such as corporate, finance and real estate, and (v) last minute changes to funding on a transaction. Most participants classified the risk that money would be successfully laundered through their firms as low on the basis that their firm`s AML compliance systems were robust, and that their client base was typically composed of regulated or listed entities.

A majority of participants concluded that UK law firms were not at a competitive disadvantage in an international context due to its highly regulated environment. Rather, the UK offered the benefit of English law and a properly regulated market that could potentially drive launderers to other jurisdictions. A highly regulated market was deemed to be an appropriate response in order to forestall money laundering.

This Chapter concludes the data section of the thesis. The subsequent and final chapter will draw together and explore the research findings, make recommendations for policy change and consider potential avenues for further research.

Chapter 8 – Conclusion

This thesis is situated in an era of unprecedented scrutiny of legal profession involvement in money laundering. Such scrutiny is set to continue unabated as the UK Government have committed to publishing second National Risk Assessment at the end of 2017, and the UK awaits a further mutual evaluation by FATF in 2018. Accompanying this focus is an evolving discourse surrounding the profession`s involvement in laundering, shifting from that of `gatekeeper` to `professional enabler` and `facilitator`. The UK response to the abiding money laundering threat has been to implement a range of AML measures which the legal profession must comply with. It is the challenges surrounding compliance with such obligations that are the subject of this thesis.

Existing research which focusses on money laundering and the legal profession tends to be quantitative in nature, or addresses the facilitation aspect of money laundering via the sector. This research takes a different approach by exploring the issue from a compliance perspective, and situates the study within a qualitative paradigm. The study also focusses on Top 50 UK headquartered law firms, a section of the legal population that recorded deal volumes of £1,021billion in the first half of 2016 alone, a figure which dwarfs other tiers of the sector.[1] This is also a section of the profession that is extremely hard to access for research purposes, with the result that the responses analysed in this thesis are seldom heard in an academic context. The significance of the research therefore, is that it offers a further dimension to existing research in the field.

The research question is deceptively simple: what compliance issues do participants from Top 50 UK headquartered law firms in England and Wales encounter when operating within the UK AML regime? The answer to that question, however, is both complex and multi-dimensional, as the previous chapters of this thesis demonstrate. This Chapter draws together the conclusions made in the body of the thesis, together with any recommendations that flow from

[1] See The Law Society, *City Legal Index* (2016) 4.

those conclusions. Accordingly, this Chapter will follow the structure of the thesis and consider: (1) the AML legislative regime, (2) the mechanical aspects of the regime, (3) the SARs regime, and (4) participants` perceptions of the regime. The Chapter will then discuss the unifying strand of the thesis: Top 50 law firms in a global context. The Chapter will close by considering the limitations of the research and any implications for future research.

When reviewing the findings of the study, it must be borne in mind throughout that this research was conducted by an `insider`, with the attendant impact that has with regard to data generation and analysis. It also offers perspectives on the regime through a distinctive and restricted lens: that of a legal professional within a Top 50 UK law firm, who may also have a potential vested interest in the regime.

1. The UK AML Legislative Regime

Responses from participants on the UK AML legislative regime centred around two key areas: (i) the exclusion of minor offences and regulatory breaches from the ambit of POCA 2002, and (ii) the inclusion of an intent element in the substantive money laundering offences set out in ss 327-9 of the Act. Both these measures support a common aim: a desire to add proportionality to the regime insofar as it relates to the legal profession. This lack of proportionality can be viewed as the inevitable consequence of the `all-crimes` approach under POCA 2002 in tandem with the potential liability imposed on legal professionals for inadvertent laundering under ss 327-9 of the Act.

The `all crimes` approach of POCA 2002 means that law firms are obliged to make `technical` SARs in respect of nominally criminal offences. This creates an excessive administrative burden and disproportionate transactional interruption for law firms, whilst diverting resources away from those real areas of money laundering risk. Any diversion of resources away from real areas of risk essentially militates against the operation of a truly risk-based regime, which is the central tenet of the UK`s AML response. Treating serious criminal offences and `technical` breaches in the same way has led to a number of interviewees perceiving the regime to be broken or discredited. That participants may perceive money laundering as either

`real` or `technical` may also give rise to a potential failure to identify and report matters which are technically reportable under the Act. Each of these factors may have the effect of hampering the effectiveness of the regime. Minor offences and regulatory breaches could and should be excluded from the ambit of POCA 2002. Furthermore, the legislative opportunity afforded by the transposition of 4MLD provided the perfect opportunity to have done so.

The desire that participants expressed for the inclusion of an intent element in the substantive money laundering offences would also address the disproportionate effect of the Act, which currently captures both inadvertent and complicit laundering within the same offences. Such inclusion would have the effect of streamlining the number of SARs made under the consent regime as lawyers would only be seeking consent for intentional laundering in the rarest of cases.

It may be surprising therefore, given the preceding findings, that many participants expressed strong support for the retention of criminal sanctions under MLR 2007 (with the same principles applicable to MLR 2017). This contrasts with the position of the Law Society, which has lobbied for the exclusion of criminal sanctions from the regulations for many years. The reasons behind such strong support are varied, but the dominant view was that criminal sanctions constitute a stronger driver of AML compliance than weaker penalties. Several participants were of the view that the deployment of criminal sanctions was a measure commensurate with the seriousness of the ill that is money laundering. Furthermore, it was felt that compliant legal professionals would remain untouched by criminal sanctions in any event.

It is noteworthy that excluding minor offences from POCA 2002, including an intent element within the substantive offences, and even removing criminal sanctions from MLR 2007/2017 could all be effected whilst being fully compliant with 3MLD, 4MLD and the overarching FATF Recommendations 2012 which sit behind them. Yet given the current AML zeitgeist, the UK is highly unlikely to relax its AML regime in the ways considered above. The `high` risk rating of the legal profession in the UK`s first National Risk Assessment in 2015, whilst disputed by the profession, may

well have extinguished any political will to be seen to relax the AML regime in relation to the sector. The Brexit negotiations compound this position further as the UK cannot afford to be seen by prospective trading partners to relax its AML requirements given the widely held perception that London is the money laundering capital of the world. For the time being then, the legal profession remains overburdened by a regime which is disproportionate in the context of the money laundering risks it is trying to combat.

2. The Mechanical Aspects of the Regime

As this research explores the AML compliance issues faced by participants, a significant proportion of the thesis is dedicated to the mechanical aspects of the regime relating to CDD, AML training and client account provisions. Concluding comments with regard to such provisions are set out below.

(i) Beneficial Ownership

Establishing the beneficial ownership of clients was one, if not the, most prominent CDD issue raised by participants. The process is undoubtedly challenging and resource intensive, both in terms of time and cost. Those challenges are exacerbated with regard to non-EU jurisdictions that do not have robust disclosure obligations in place, or in relation to specific client groups such as trusts and private equity clients.

The majority of participants had no view, were ambivalent, or satisfied with the 25% beneficial ownership threshold currently in place in the UK. This finding may be partially attributable to the fact, raised by a number of participants, that identifying a percentage of share ownership or voting rights in a company may still not reveal definitively who is actually controlling an entity. A truly dedicated launderer will both be able to phish under whatever percentage disclosure threshold is specified and/or fail to declare their beneficial ownership interests on the PSC Register. The proposed Directive amending 4MLD, which considers lowering the beneficial ownership threshold to 10% in relation to high risk entities, such as holding company structures, may therefore be limited in its utility.

In any event, any beneficial ownership register will almost immediately be out of date given the constant ownership changes that take place within the legitimate economy. This is an unavoidable effect of genuine commercial dealings, and a workable balance must be struck in this respect. The requirement when the PSC Register was first introduced was to update beneficial ownership information on an annual basis. This requirement has now been reduced to a 14 day time period in order to align with Article 30 of 4MLD.

Despite these limitations, there are a number of avenues that should be explored in order to enhance further the transparency of beneficial ownership. One potential measure is to dispense with nominee shareholdings, with the limited exception of those trading in listed securities or other narrowly defined categories determined by legislation. This would assist in preventing nominee shareholders achieving opacity with ease and shift the balance of transparency towards the legitimate economy.

The other response required is a move towards greater transparency in non-EU jurisdictions on a global basis. Currently, incorporating a holding company or setting up an elaborate group company structure in an opaque jurisdiction may have the effect of defeating beneficial ownership transparency. At a UK and European level several measures have been, and are currently being, taken which model enhanced transparency measures. In the UK, although its precise requirements are yet to be determined as at September 2017, an Overseas Entity Beneficial Ownership Register will be implemented. The Register is designed to capture information on beneficial owners of overseas entities owning UK property or involved in UK government procurement contracts. At an EU level, the transposition of 4MLD required the implementation of central beneficial ownership registers across member states. In addition, the proposed Directive amending 4MLD seeks to make those registers interconnected across the EU.

Such registers showcase a potential way forward in years to come: namely the implementation of a global register of beneficial ownership interests applicable to those nations implementing FATF recommendations. Any register will never be

able to capture real time beneficial ownership interests due to the constant changes characterised by the legitimate economy, not will they ever be able to deter the truly committed launderer. They will, however, serve to improve beneficial ownership transparency on a global basis.

(ii) Simplified Due Diligence, PEPs and Source of Funds/Wealth

Whilst the beneficial ownership challenges outlined above were identified as the most prominent AML compliance issue faced by participants, a number of discrete areas of the regime were discussed, and are considered in turn in this and subsequent sections of this Chapter.

In relation to simplified due diligence (SDD), the permitted categories of clients where SDD automatically applied under MLR 2007 have been swept away by MLR 2017, and each law firm must now make its own determination as to whether to apply SDD to its clients. Several entities to which SDD may potentially be applied must be assessed with regard to their listing on `equivalent` markets, and in the absence of any definitive list, law firms must conduct their own in house due diligence to establish equivalence.

The SDD changes brought in by MLR 2017 may also mean that particularly risk-averse law firms will simply opt to apply standard CDD on all clients as a matter of course. This is a development which would effectively increase the CDD burden on law firms further, and defeat the whole purpose of the SDD provisions. Whether this development comes to fruition remains to be seen.

The inclusion of domestic PEPs within the scope of MLR 2017 was of little consequence to participants, although there are inevitable costs implications attributable to the inclusion of domestic PEPs within the regime. This reflects one of the features of law firms with an international practice: a domestic PEP for a firm`s London offices is a foreign PEP in relation to its Hong Kong offices for example. Therefore domestic PEPs were already being treated in the same way as foreign PEPs prior to MLR 2017 by many participant firms.

Under MLR 2007, the PEP status of a client automatically triggered the requirement for law firms to apply enhanced due diligence (EDD), which some participants felt was inappropriate, and detracted from more pressing areas of money laundering risk. The implementation of MLR 2017 provides that EDD will be applied to PEPs using a risk-based approach. This deals only partially with the concerns of those participants who felt that the blanket application of EDD to PEPs was a disproportionate effect of the regime.

Practical difficulties abound with regard to the delicate and sensitive issues of source of wealth and source of funds, difficulties exacerbated by a lack of rigid parameters in MLR 2007 and limited sector specific guidance. Participants recounted that decisions on source of funds/wealth can be, in essence, a judgement call on the part of each law firm. One key issue raised by participants is that of prior criminality: whether funds which originate from `questionable` sources are forever tainted. The potential issue this raises is that under POCA 2002, a lawyer is required to submit a SAR to the NCA in respect of any dealings with criminal property. It is the author`s view that the wording in MLR 2007 and related Law Society guidance do not require law firms to undertake exhaustive investigations as to the prior criminality of their clients. This does not mean that law firms can be cavalier in their attitude to the provenance of funds or wealth, however. Rather, it is submitted that sufficient safeguards are in place by way of potential liability under the substantive money laundering offences or failure to report offences set out in POCA 2002, in tandem with the reputational risks to the law firm of dealing with illicit funds.

For `standard` risk clients, source of funds information is an ongoing monitoring requirement, as opposed to a requirement at the client inception stage. This does rather put legal professionals on the back foot in terms of obtaining such information once the retainer has already started. Whilst source of funds information is not an explicit requirement at the point of client inception under MLR 2007, a lawyer will still be required to determine the source of funding

connected to a retainer as a matter of professional conduct in order to be able to properly advise the client.

There is no absolute obligation in MLR 2007 to apply CDD to third party funders on a transaction, although law firms do have an obligation to understand that source of funding. Nevertheless, some participants perceived this to be an area of money laundering risk, and voluntarily elected to conduct CDD on such third party funders, notwithstanding the lack of any strict requirement to do so, particularly when funds were being received into the client account. Ultimately, whether to conduct CDD on a third party or not will be dictated by the risk appetite of a particular firm.

(iii) Reliance and Ongoing Monitoring

Both MLR 2007 and MLR 2017 contain provisions which enable law firms to rely on specified third parties such as banks or other law firms to conduct client due diligence on their behalf. Law firms may also be relied upon to conduct CDD on behalf of third parties. However, these provisions contain considerable drawbacks in that a law firm relying on a third party still retains criminal liability for any CDD breaches. In the reverse scenario, a law firm being relied upon may attract civil liability in tort for CDD breaches, and is also under an obligation to update the CDD information it provides to third parties. It is entirely unsurprising therefore that the reliance provisions in MLR 2007 (and comparable provisions in MLR 2017) are rarely used by the profession in practice. Civil and criminal liability issues aside, it is submitted that each law firm will have its own risk appetite and parameters, and therefore reliance is not a provision which should be utilised routinely in any event.

Ongoing monitoring was highlighted simultaneously as the most important and the hardest aspect of the regime, the challenge being the retention of money laundering risks at the forefront of a lawyer`s mind during the course of transactions. This is a potential vulnerability which could be addressed in part by raising awareness through AML training.

(iv) AML Training

The value of AML training was appreciated by many participants and a preference for face-to face, bespoke training was expressed. One of the issues raised by participants was a general lack of money laundering case studies and examples relevant to large commercial law firms which could be used in AML training. Such lack is one aspect of the regime which can be addressed with relative ease by improved information sharing between the NCA, law enforcement agencies and the regulated sector. Indeed, there are already movements in this direction within the banking sector as demonstrated by the establishment of JMLIT. Improved information sharing would provide relevant examples which could be utilised in raising awareness and in AML training. This could have the effect of refining the judgement both of MLROs and those reporting to them. Improved information sharing is discussed subsequently in this Chapter.

(v) Client Account

Whilst participants were extremely aware of the money laundering risks relating to the client account, and a majority of them had experienced clients trying unsuccessfully to use the account as a banking facility, only a tiny minority perceived such attempts as potential money laundering. Rather, attempts to use the client account in this way were framed as attempts at commercial efficacy, which may or may not be the case.

There has been much debate over recent years proposing that law firms should no longer hold client accounts. It is the author`s view, however, that the client account should be retained for the reasons explored below. The lack of a client account would make transactions more complicated and costly to effect via third-party escrow providers. It would also mean that solicitors would no longer provide undertakings to transfer funds on completion in respect of accounts which were held by third parties, which is frequently the case on commercial transactions currently. The lack of a client account also has wider implications. Funds would be flowing via entities with far less oversight on transactions, namely banks and third

party escrow providers. Conceivably then, the lack of client account could actually increase the money laundering risk within other sectors. Neither banks nor third-party escrow providers are able to view transactions holistically, in contrast to law firms, and therefore may be less able to forestall potential laundering. It is for these reasons that the author holds the view that the client account should be retained.

The implementation of MLR 2017 has introduced one key change with regard to law firms` pooled client accounts. As the pre-ordained categories of customer attracting SDD have been dispensed with, banks must now make their own determination as to whether SDD applies to each of its law firm customers using a risk-based approach. This opens up the potential risk that banks will de-risk by declining to operate pooled client accounts on behalf of law firms, the administrative effect of which would be significant. A precedent for such de-risking is evident from the charity sector, where banks have declined to operate bank accounts for those charities operating in high risk jurisdictions. Whether this becomes a reality or not remains to be seen.

3. The SARs Regime

The majority of participants had no issues with, and no views on improvements to any aspect of the SARs regime. However, these findings should be considered with caution given the large number of responses from transactional participants who had never personally used the SARs regime. As highlighted earlier in this conclusion, the majority of participants felt that minor offences and regulatory breaches should be excluded from POCA 2002, the effect of which would be a streamlining of the SARs regime insofar as it relates to the `technical` reports made by the legal profession.

The UK operates a `suspicions` based AML reporting regime, a concept which for the majority of participants is interpreted by reference to a blend of instinct, the particular fact pattern of a transaction, and experience as opposed to the judicial guidance in the leading case of *Da Silva*. Such guidance, it may be recalled, provides that suspicion is `a possibility, which is more than fanciful, that the relevant facts

exist. A vague feeling of unease would not suffice.`[2] One implication of this is that the judicial guidance from *Da Silva* can be seen as an over-definition of the concept by the courts. Prior to *Da Silva* it was clear that subjective suspicion was reportable. Following the decision however, a subjective suspicion may only be reportable if that suspicion is more than a vague feeling of unease. It then becomes challenging to make a distinction between a sense of unease and subjective suspicion. In the alternative, the guidance in *Da Silva* may serve to filter out more fanciful suspicions. Such nuances may be purely academic however, given that the majority of participants determine whether they are suspicious or not according to instinct, the fact pattern on any particular transaction, and experience. Whilst experience will accrue over the course of multiple transactions, instinct can also be refined through a blend of AML training and raising awareness.

The MLRO`s role is pivotal within the SARs regime, and the interview data suggests a wholesale transference of money laundering concerns to them by participants. The potential impact of each MLRO`s decision to make a SAR to the NCA or not is significant, both for their respective firms and for society in a much broader sense, due to the size of the deals transacted via the sector, and within Top 50 law firms in particular. Such wholesale transference is unsurprising as this is the way in which the SARs regime is structured within POCA 2002. It does, however, highlight the vulnerability of a system which sees AML decisions placed in the hands of a single individual within an organisation.

Whilst none of the participants expressed any concerns as to the quality of their MLROs, this may not be the case across the sector as a whole. Rather than acting as an AML fortress, a poor MLRO may in fact be a law firm`s AML fault line. The SRA in their thematic review, for example, have reported poor practice on the part of some MLROs, and concerns have been expressed by both the NCA and the SRA over a reduction in quantity and the poor quality of legal sector SARs. The question remains therefore whether the use of a skilled, but potentially flawed MLRO acting

[2] *R v Da Silva* [2006] EWCA Crim 1654, [2006] 4 All ER 900 [16].

as a filter in respect of external SARs is preferable to the NCA receiving more, potentially groundless, SARs directly from legal professionals.

Given the reluctance of the UK government to relax the reporting thresholds in any manner in the light of the NRA 2015 and the political climate created by Brexit, other ways of improving the regime, and supporting MLROs in practice must be considered. This could be achieved in part by the creation of a bespoke legal sector SAR form in response to the difficulties participants reported when submitting SARs which were created for, and are tailored to, the banking sector. A bespoke form would cater for the underlying offences, notional savings and benefits constituting criminal property that law firms are likely to encounter and report on a transaction, as opposed to the debits and credits which are a feature of banking sector SARs. Nor would the creation of a bespoke legal sector SAR form impact upon other sections of the regulated community. Rather, it would streamline the consent process when dealing with the NCA.

Further improvements to the regime could be implemented by way of enhanced analysis of SARs and better information sharing between the NCA, law enforcement agencies and the legal sector. The Joint Money Laundering Intelligence Taskforce showcases how such information sharing can work in practice within the banking sector, and could be rolled out across the legal sector. Alternatively, the NCA biannual reporter booklet could be expanded significantly, or the SRA granted direct access to the SARs database in order to cascade information down to the profession. Improved information sharing would provide clearer AML parameters within which the legal profession operates and better support MLROs in practice. It would also provide those relevant money laundering examples which participants expressed a desire to encounter in their AML training.

The issues that arise for the legal professional when using the consent regime relate to deal pressure during the consent process, and managing the client relationship in such a way as to avoid liability for `tipping off.` This particular challenge is set to become even harder to manage given that the Criminal Finances Act 2017 brought in new powers to extend the moratorium period up to a total of

186 days. It will be interesting to see how law firms manage the client relationship during a protracted moratorium period. It is inevitable, given the consent regime in its current form, that a tension will always exist between a legal profession tasked with the completion of a transaction, and an NCA tasked with halting the flow of illicit funds.

4. Perceptions of the Regime

Questions relating to participants` perceptions of the regime were sometimes asked directly, but were often interwoven in the responses to questions on other aspects of the regime. One of the limitations of this thesis, as detailed in Chapter 3 and later in this Chapter, is that it explores AML compliance issues through a distinct lens ie from the perspective of legal professionals within Top 50 law firms, some of whom have a vested interest in the regime. Nowhere is this limitation more evident than when considering the comments made in relation to participants` perceptions of the AML regime. Such responses will inevitably be weighted against any form of self-incrimination. Participants` responses should therefore be read in light of this overarching caveat.

(i) The Role of the Legal Profession within the AML Regime

Many objections were raised by the profession when lawyers first became subject to AML obligations. The interview data suggests a notable shift in this area however, as a majority of participants felt their AML role was appropriate, with some even self-identifying as `gate-keepers`. Few felt they were being used as unpaid detectives, for example, which had been one of the objections raised when the regime was first introduced. This shift may form part of a general maturation of the regime, a shift which has seen the lawyer`s role evolve to encompass AML as a matter of course. Participants reported an increase in market sophistication accompanying this maturation, which meant that CDD processes have become streamlined where clients are familiar with, and more willing to produce, beneficial ownership information. A few participants noted that an improved familiarity with the regime also fostered a decline in defensive reporting. In addition, there were a number of reports of declining to act for clients who raised money laundering

concerns, which accords with one of the findings from the SRA thematic review of AML in 2016. Each of these aspects of maturation has the potential to enhance the effectiveness of the overarching AML regime.

Rather than raising objections to the additional workload created by the regime, which one might ordinarily expect to see, many participants expressed an active desire to comply with their AML obligations. Nor was such willingness restricted to compliance participants, who might be expected to have a vested interest in the regime due to their roles.

The profession`s involvement with money laundering was perceived as being both misunderstood and overstated by a number of interviewees, particularly as presented in the National Risk Assessment 2015. Whilst this perception may seem self-serving on first inspection, it must be recalled from Chapter 1 that it is a view echoed by a number of commentators, both by the Law Society and within the academic community.

(ii) Benefits of Compliance, SRA AML Regulation, and Enforcement

Avoiding criminality was the baseline benefit of AML compliance identified by participants together with the creation of a `clean` corporate culture. Thereafter, the multi-faceted concept of brand protection was perceived as the paramount benefit of compliance. Damage to a firm`s reputation could occur as a result of any hint of involvement in money laundering, leading to negative press coverage, professional embarrassment for firms offering AML legal advice, and challenges in recruiting staff. Brand protection aside, a number of practical benefits of CDD were pinpointed. Clients could be properly identified and appropriately risk assessed, and the CDD process assisted with conflicts checking, sanctions compliance and cross-selling.

Whilst many, typically transactional, participants had no views on the SRA as an AML regulator, a number of participants felt that the SRA were a weak AML regulator, with several advocating more robust regulation. Similarly, a small majority of interviewees either had no view on the enforcement of the regime, or

felt unable to provide any meaningful commentary. Whilst an assessment of the effectiveness of the SRA as an AML regulator, and the enforcement of the AML regime are outside the scope of this thesis, these perceptions do raise concerns. At its most benign, a lack of SDT and enforcement cases deprives the sector of a useful AML education tool. More troubling still is the fact that a regime that is poorly regulated and rarely enforced may mean that there is scant opportunity for small battles against money laundering to be won, let alone the entire war. In addition, a combination of ineffectual regulation and lax enforcement can hardly be said to constitute effective drivers of AML compliance, although the benefits of AML compliance which participants identified may counter this. The alternative possibility is that a low level of enforcement actually signals a low level of lawyer involvement in money laundering.

(iii) Assessment of Money Laundering Risks

Jurisdictional risk was identified as a key money laundering risk by a majority of interviewees and is multi-faceted in nature. It refers both to those risks inherent in dealing with jurisdictions where corruption is more prevalent, often on complex large-scale transactions, as well as increased difficulties in establishing the source of funds or wealth on a transaction.

A number of more specific risks were identified. Particular types of client, for example, were perceived as posing a heightened risk of money laundering. These included new clients at the point of on-boarding, foreign PEPs, high net worth individuals such as Russian oligarchs and private equity investors. Particular practice areas, namely corporate, finance and real estate were also perceived as presenting a heightened level of risk. Failure to obtain NCA consent in respect of `technical` breaches on the part of clients also presented a risk that participant firms would then become inadvertently participative in a money laundering offence. Finally, last minute changes to funding on a transaction were pinpointed as a risk.

Most participants classified the risk of money being successfully laundered through their firms as low. One reason for this categorisation was that participants felt their

firm`s AML policies and procedures were sufficiently robust to thwart money laundering attempts. The other reason is that participants felt a client base made up of predominantly listed, regulated and/or entities with whom there was a longstanding business relationship mitigated the money laundering risk to a certain extent. It is not possible to discern with any accuracy the extent to which those perceptions of risk and the reality of those risks intersect, given the clandestine nature of money laundering coupled with the dearth of enforcement cases in the field.

(iv) Top 50 Law Firms in a Global Context

For a majority of participants, the highly regulated AML environment in place in the UK did not put UK law firms at a competitive disadvantage internationally. Rather, a highly regulated market subject to English law was lauded as a feature that was attractive to clients, potentially diverting launderers to less regulated jurisdictions. Even if UK law firms *are* competitively disadvantaged as a result of a higher level of regulation in this jurisdiction, the debate then becomes this: is it worth it if it means that money laundering is successfully thwarted in this jurisdiction? It is submitted that, given the human and economic cost of laundering, the answer to that question is a resounding `yes`.

5. Limitations of the Research

The limitations of the research are that it does not explore AML compliance issues from the perspective of the SRA, NCA, CPS or law enforcement agencies. Therefore, the research explores AML compliance issues through a very specific lens: that of a solicitor or compliance professional within a Top 50 UK headquartered law firm. For compliance participants, that perspective may be narrowed further on the basis that their roles may be partially attributable to the sophisticated compliance requirements in place in the UK. Furthermore, the research was conducted by an `insider` former practitioner. Whilst that position was beneficial in terms of securing access to participants, and for establishing credibility and rapport during the interviews, it also means that, despite constant researcher reflexivity, the research cannot be said to be entirely value free.

Nevertheless, the 40 in depth interviews provide multiple different perspectives on the regime, both from lawyers at the `coalface` of legal practice drawn from varied transactional practice areas in different sized firms, and from compliance professionals able to offer a different perspective. Participants from Top 50 firms can be difficult to access due to the constraints on their time. In addition, the research design, data collection and data analysis techniques deployed in this thesis were both rigorous and meticulous.

6. Implications for Future Research

Future research will seek to address the limitations of this thesis identified in the preceding paragraphs by seeking the perspectives of the SRA, NCA, CPS and law enforcement agencies on AML compliance in Top 50 law firms.

This thesis focusses on Top 50 UK headquartered law firms for the reasons explored in the Methodology Chapter. However, the legal services market has shifted significantly over the last few decades and there are a number of non-UK headquartered law firms with a strong UK presence via their London offices. Whilst such firms are required to comply with the UK AML regime, there may be differences, which further research could reveal, in how those firms apply CDD standards or perceive money laundering risks. US law firms, for example, operate within a notably different regime in the US and may therefore face different issues when complying with the UK AML regime.

Jurisdictional issues are a key theme interwoven throughout this entire thesis. This is unsurprising given the vast majority of participants were drawn from firms with an international presence. Future research could therefore explore the compliance issues faced by smaller national or regional firms, on the basis that such firms operate with entirely different client demographics and resources.

Brexit presents a key opportunity for the UK to reassess its AML provision. It may be recalled that historically, the standards promulgated by FATF have been adopted via a series of EU directives. As the UK will remain a member of FATF post -Brexit, it remains committed to complying with those standards. Nevertheless, the UK has gone further that the requirements recommended by FATF and the various EU AML directives in a number of ways. It has implemented an `all-crimes` approach in POCA 2002, and has not incorporated an intent element in the substantive money laundering offences. The research findings suggest that the effect of this AML structure is that it imposes a disproportionate burden upon the legal profession. The legislative sea swell provided by Brexit could furnish the UK with the perfect opportunity to address this lack of proportionality.

It may be politically unpalatable to relax the AML regime in respect of a profession which is said to pose a high risk of money laundering, particularly when the UK is commonly perceived as being awash with illicit funds. However, what will be even more politically unpalatable is if the UK fails to attract business to its shores in a post-Brexit world due to its highly regulated environment when compared to other jurisdictions. It is this concern that has prompted some commentators to suggest that the UK may be compelled to relax its regime in the manner indicated above, and it remains to be seen whether this pathway will evolve into a reality.

One of the key CDD issues that participants reported was establishing the beneficial ownership of their clients. Those difficulties were exacerbated in non-EU jurisdictions with less stringent disclosure obligations. The position in Europe is currently assisted by the requirements under 4MLD to maintain centralised registers of beneficial ownership. The proposed directive amending 4MLD envisages that these centralised registers should be interconnected across all member states, a benefit that the UK will no longer automatically have access to post-Brexit.

A majority of participants were drawn from firms with an international, if not global, practice. The jurisdictional challenges that this then presents are interwoven throughout the entire thesis, with such challenges likely to increase as law firms continue to expand their businesses globally. First, establishing the beneficial ownership of a client, their true source of wealth and source of funds can be more challenging when a cross-border element is present, particularly in those jurisdictions where opacity is prized. Secondly, law firms may become inadvertently involved in money laundering offences when acting for clients in more corrupt jurisdictions. Finally, jurisdictional risk was identified as the most significant risk of money laundering by participants.

That a global response is required to global money laundering threats is not a new concept. Indeed, FATF was formed as long ago as 1989 as a *global* AML standard setting body. What is required is far more global interconnectedness in that response across multiple jurisdictions, and this is a key aim of the UK`s AML Action Plan 2016. We have already seen central beneficial ownership registers implemented across the EU as part of the transposition of 4MLD. Global registers of beneficial ownership interests may therefore be a possibility in years to come. Whilst these may be unlikely to represent the real time beneficial ownership position, nor will they deter the truly dedicated launderer, they will go some way to addressing the current position whereby non-EU opacity hampers transparency. Greater moves towards transparency are also required in respect of those jurisdictions which currently bask in a sea of opacity, where the siren calls of nominee shareholdings ring out.

Annex 1 – Participant Schedule

No.	COMPLIANCE PARTICIPANTS – DATE OF INTERVIEW	NUMERICAL RANK OF FIRM IN TOP 50
C1	17/11/15	21-30
C2	24/11/15	1-10
C3	25/11/15	1-10
C4	03/12/15	31-40
C5	07/12/15	1-10
C6	08/12/15	11-20
C7	08/12/15	31-40
C8	14/12/15	11-20
C9	15/12/15	1-10
C10	15/12/15	1-10
C11	19/02/16	41-50
C12	26/02/16	41-50
C13	10/03/16	1-10
C14	10/03/16	1-10
C15	10/03/16	21-30
C16	14/03/16	41-50
C17	08/04/16	11-20
C18	08/04/16	1-10
C19	24/05/16	21-30
C20	16/06/16	11-20
No.	**TRANSACTIONAL PARTICIPANTS – DATE OF INTERVIEW**	
T1	18/11/15	1-10
T2	18/11/15	21-30
T3	18/11/15	21-30
T4	20/11/15	1-10
T5	25/11/15	1-10
T6	25/11/15	1-10
T7	25/11/15	11-20
T8	26/11/15	31-40
T9	26/11/15	1-10
T10	26/11/15	1-10
T11	26/11/15	11-20
T12	01/12/15	31-40
T13	01/12/15	31-40
T14	01/12/15	31-40
T15	08/12/15	11-20
T16	08/12/15	11-20
T17	16/12/15	21-30
T18	16/12/15	21-30
T19	10/03/16	21-30
T20	11/03/16	11-20
	PILOT INTERVIEW 15/11/15	41-50

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