



The Law Society

Anti-money laundering compliance by the legal profession in England and Wales

A review of compliance by a number of firms one year after implementation of the third money laundering directive in the UK

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supporting
solicitors

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2008 Law Society anti-money laundering survey

Introduction by MLTF Chair

The Law Society, through its Money Laundering Task Force, has been vigorously lobbying government at all levels for many years to design an anti-money laundering regime in the UK which is clear, workable and proportionate.

We have been providing extensive support to our members and actively monitoring the practical implications for firms in meeting the challenges posed by compliance with their anti-money laundering obligations.

This survey is an important element of our many monitoring activities in this area. The results confirm the messages that those on the Money Laundering Task Force and within the Law Society have been receiving from across the profession, in day to day discussions and specific networking groups.

We see these results as a useful starting point to generate discussions about how we can work together with the profession, law enforcement and government to develop a more proportionate and effective anti-money laundering regime for the UK.

I extend the thanks of the Law Society and the Money Laundering Task Force to those members of the profession who volunteered their time and took part in this important survey.

Alison Matthews
Associate Director - Compliance, Irwin Mitchell

Chair of the Money Laundering Task Force

Background

In August 2008, 115 solicitor's firms in England and Wales volunteered to take part in a detailed survey considering the processes adopted by solicitors to comply with the Money Laundering Regulations 2007 and the associated costs.

The survey was conducted in September 2008, with print copies of the surveys sent to participants. We received 55 responses, some of which were only partially completed.

Headline results

- AML compliance pervades the whole firm. Half of the respondents were training 88% or more of their staff, with 36% of respondents training all of their staff.
- The 2007 regulations have required significant changes in existing systems; although that does not mean that there is the same level of sophistication in firms' systems. There was a general trend towards an increase in the complexity of the system and the amount of data it can capture. There was also an indication of increased staffing.
- The UK is exporting AML compliance for lawyers world-wide, with 62% of respondents with international offices advising that they are applying the UK standard to all of their offices.
- Documentation and audit of compliance activities remains an area for development:
 - 76% of firms had conducted a risk assessment on their firm as a whole, but only 72% had formally documented these risks.
 - 54% of respondents rely on fee earners' normal file notes to provide evidence of ongoing monitoring, only 23% have set deadlines for these notes to be made to ensure they are done.
 - 65% are auditing compliance through file checks undertaken internally. This suggests auditing of compliance on individual matters, rather than the auditing or review of the compliance system as a whole. While this is understandable given that the regulations have only been in place for 12 months, it is an area for future development.
- Greatest reported challenges include:
 - Time constraints are the greatest challenge in implementing the risk based approach
 - The lack of publicly available data is the greatest challenge in identifying and verifying beneficial owners.
- The reliance provisions, which were meant to reduce the compliance burden, are not widely used.
 - In the UK, only:
 - 57% of respondents have relied on other solicitors

- 41% have relied on a financial institution
 - 27% have relied on an external accountant.
- Respondents are less willing to rely on other regulated professionals
- Outside of the UK, the level of reliance drops even further.
- 64% of respondents said that the criminal sanctions attaching to them, if the other person made an error, were the greatest deterrent in not using the reliance provisions.
- 64% of respondents had been asked by others if they could be relied upon, but only 48% agreed to the request. The risk of civil action against them if they made an error was a key reason for not agreeing to be relied upon.
- 33% of respondents had turned down a retainer from a politically exposed person, due to the perceived risks of that client.
- While there was a general perception that costs have increased since the 2007 regulations, 77% of respondents do not record specifically the costs of complying with anti-money laundering obligations.
- From the very small sample who provided costs information
 - Costs of compliance range from thousands of pounds to millions of pounds.
 - Most of this is spent on undertaking due diligence and training
 - 50% of firms which responded on the issue of costs indicated an increase in gross expenditure since the new regulations of 10% or more
 - 90% of firms which responded on costs do not pass on the full cost of compliance to their clients.
- 67% of respondents felt that the Law Society had been supportive or very supportive of them in meeting their AML obligations.

Key demographic information

The respondents to the survey came from the following geographical areas:

Region	Percent
City of London	38
Rest of London	11
North West	11
South East	11
Yorkshire	7
Eastern	7
South West	6
West Midlands	5
North East	4

There were no respondents from the East Midlands or Wales

The respondents came from the following sized firms:

Firm size	Percent
Sole practice	9
2-4 partners	24
5-10 partners	13
11 – 25 partners	16
26 -80 partners	14
81 or more partners	24

As such the majority of respondents are from either the very large firms or the very small firms, which may give a significant spread to the data.

Systems results

Policies

- 100% of respondents had updated their policies
- 87% updated their policies in-house

Staff involved in AML compliance

- the top 25% had 9 staff or more
- 50% of respondents had 5 staff or fewer
- the bottom 25% had 3 staff or fewer
- Range: 1 to 1,306 staff involved in AML compliance

The types of compliance staff included:

- MLROs' and their deputies
- Risk and compliance
- Finance
- Senior management

- Administration
- Client acceptance
- Legal staff – some had specialist AML lawyers

Types of systems changes

Some of the key changes which have been made to implement the 2007 regulations, included:

- all forms, manuals and policies being re-written
- building in risk assessment at every stage
- changes to file opening systems to take into account enhanced due diligence and beneficial owners
- new training had to be developed

What systems do we now have in the legal sector?

- For some it was the formalisation of a paper system where there had been no systems before
- For others – they have moved to electronic systems
- For others – they have significantly enhanced their electronic systems, with alerts for ongoing monitoring and integrating CRM databases with e-verification
- For a number there appears to have been an increase in resources, with 3 specifically mentioning the hiring of new staff

Overseas offices

- 62% of respondents with overseas offices are applying the UK standard as a global standard in all offices.

Reviewing compliance with the system

- 29% used supervision meetings
- 29% used file audits or reviews by the MLRO
- 47% used file audits or reviews by internal audit
- 5% used file audits or reviews by external audit
- 6% used their quality management system accreditation process
- 11% had no formal review process

Reviewing appropriateness and effectiveness of systems

- 65% relied upon internal audit of files
- 5% relied upon external audit
- 23% relied upon Lexcel or some other quality management system
- 23% said they had no formal review process

The risk based approach (RBA)

Satisfaction that they had implemented the RBA

- 89% were either satisfied or very satisfied that they had implemented the RBA
- 11% were neutral
- No one was dissatisfied or very dissatisfied

Risk assessment of the whole firm

- 76% has risk assessed the firm as a whole and 97% of those did so in-house.
- Of the 24% who had not conducted a firm wide risk assessment, 56% of those planned to do so in the next 12 months.
- 72% claimed to have formally documented their AML risks, but 79% believed they had a formal strategic response in place to deal with their AML risks.

Assessing risks of retainers

- 95% said they assessed the risk for each retainer, but only 64% said they had a standardised risk assessment tool to enable them to do so.
- When asked about how they assessed risk without a standardised tool, the response was that they:
Trained staff regarding the new regulations and the fee earners looked at each case on its merits and decided the risk level.
- Risk assessment for individual retainers are conducted by:
 - Fee earners alone in 36% of firms
 - Fee earners with some overview from either management or a compliance team in 49% of firms
 - A centralised compliance team or management only in 15% of firms.

Benefits from the risk based approach

- 37% had already seen some benefits or expected to see them
- 17% did not know if there were benefits
- 46% have either seen no benefits as yet or do not expect to see any.

Greatest challenge in implementing a risk based approach

- 41% thought it was time constraints
- 21% thought it was a lack of guidance
- Lack of resources and difficulties in changing existing processes also featured as challenges

Undertaking Client Due Diligence (CDD)

How is CDD undertaken?

- 85% of respondents said they apply a standard set of verification requirements to clients of the same risk level.
- All are keeping some form of record of the client due diligence
 - 65% keep a paper copy with the main paper file
 - 38% keep a paper copy on a separate client file
 - 2% keep only a reference to the identity material considered
 - 50% keep an electronic copy
 - 61% keep the information in a centralised database

Timing of CDD

- 41% do not allow a file to be opened until CDD is completed
- 39% allow fee earners to open a file but have an alert to close the file down if CDD is not completed within a short set time frame
- 62% make use of the timing exemption in regulation 9 – allowing them to proceed with the transaction before CDD is undertaken if the matter is low risk and it is necessary not to interrupt the normal course of business.
- 28% make use of the timing exemption in regulation 11(2) which allows them to proceed with the provision of legal advice before CDD is undertaken.

Verification of individuals

- 70% use passport or identity card
- 80% use passport or identity card and another document
- 19% use electronic verification only
- 48% use passport and electronic verification

There was also a willingness to consider other documents where a passport was not available, as set out in the practice note.

Verification of companies

- 60% used the listing on a regulated market
- 93% used the companies registry
- 89% used the certificate of incorporation
- 61% used audited accounts
- 56% used e-verification.

Client base which qualified for simplified due diligence

- 14% said none qualified
- 12 % said 90% or more qualified
- For the majority of respondents it was less than 50% of their work

Usefulness of simplified due diligence

- 71% found it useful or very useful
- 28% were not sure when it applies
- 43% found it difficult to get information to allow them to decide that simplified due diligence applies
- 23% found it difficult to get information specifically on equivalence.

Beneficial owners of companies – how do you identify

- 89% from the client
- 55% from other regulated persons
- 92% from the relevant company registry
- 56% from e-verification

The process used depended on the type of company and where they are located.

Greatest challenge in identifying beneficial owners of companies

- 42% said it was the lack of publicly available information
- 31% said it was clients being unwilling to provide information
- 21% said it was that information on registries or e-verification was not reliable

Beneficial ownership of trusts – how do you identify

- 88% from the trustees
- 46% from other regulated persons
- 45% review the trust deed
- 24% use e-verification

Practicality of applying the definition of beneficial ownership for a trust

- 24% find it practical or very practical
- 33% are neutral
- 43% find it either impractical or very impractical

Verification of beneficial owners beyond information used for identity

- 44% said that they sought further information to verify beneficial owners occasionally
- 33% said they did so rarely.

Use of Enhanced due diligence for non face-to-face clients

- For a majority of respondents, non face-to-face work accounted for 25% or less of their client base.
- 43% will ask for extra documents
- 40% said they would use e-verification
- 17% would use payment through a UK bank's account
- Only 51% found that banks are generally providing the wire transfer information which would assist them with CDD.

Politically Exposed Persons

- 67% said that they had no PEPs as clients
- The highest level of PEPs in any client base was 10% (that was from 2 respondents)
- Of those who had PEPs
 - 30% were primary clients
 - 45% were beneficial owners of primary clients
- PEPs came from the following areas of practice
 - 48% from corporate
 - 16% from property
 - 16% from trust work
 - 12% from commercial
 - 8% from litigation
 - 4% from tax
 - 12% from other areas
- PEPs were identified by:
 - 43% by asking them
 - 43% by general internet query
 - 60% by e-verification

PEPs – enhanced due diligence

- Senior management approval by:
 - 13% partner on file
 - 4% practice area partner
 - 75% MLRO
 - 4% client acceptance committee
 - 4% by risk committee
 - 28% by managing partner
 - 12% by other
- 70% undertook further verification of the PEP's identity
- Source of funds are established by:
 - 68% ask the client
 - 52% use the internet or public documents
 - 36% use a intelligence provider
 - 36% will contact the relevant bank or other regulated persons
- Enhanced ongoing monitoring is undertake by:
 - 32% through file notes by the fee earner
 - 27% through reports to the supervising partner
 - 40% through reports to the MLRO
 - 38% through reports on the actual funds by the accounts department
 - 38% simply tell the partner / fee earner to monitor more closely
- Respondents reported a very small amount of work being lost due to the enhanced due diligence requirements, but some have said they received negative comparisons by their clients with firms operating in other jurisdictions which do not require it.

- 33% of respondents had turned down work because of the perceived risk posed by PEPs.

Sanctions lists

- 48% do not check their clients against the Treasury consolidated list
- 26% check all of their clients against the Treasury consolidated list
- Of those who do check their clients
 - 69% use an e-verification provider to conduct the check
 - 31% re-check their client base at intervals against the list

Existing clients

- 30% of respondents had all of their clients identified under the previous regulations
- 62% of respondents had half or more of their client base who had not been identified prior to the 2007 regulations.
- One year on, of those respondents who had un-identified clients
 - 26% have not identified any of their previously exempted clients
 - 20% have identified all of their previously exempt clients.
- Verification processes undertaken for existing clients:
 - 65% use standard identification requirements
 - 29% use e-verification
 - 35% review existing files for relevant information
 - 35% get a certificate from the relevant fee earner
- A very small amount of work has been lost as a result of the need to undertake CDD on existing clients.

Reliance

Firms who have relied on others in the UK

- 41% have relied on a financial institution
- 4% have relied on an auditor
- 2% have relied on an insolvency practitioner
- 28% have relied on an external accountant
- 10% have relied on a tax adviser
- 57% have relied on another solicitor
- 4% have relied on a barrister

Firms who have relied on others outside of the UK

- 25% have relied on a financial institution
- 4% have relied on an auditor
- 10% have relied on an external accountant
- 2% have relied on a tax advisor
- 40% have relied upon another independent legal professional

Why do firms not want to rely?

- 64% cite criminal sanctions if the person they relied upon makes an error
- 48% are not happy with the CDD standards others apply
- 18% find that others are not prepared to provide the material relied upon
- 34% find it difficult to assess equivalence in order to rely

Are others relying on solicitors?

- 64% said they had been asked if they could be relied upon
- They had been asked by the following regulated persons
 - 18% by financial institutions
 - 12% by auditors
 - 21% by external accountants
 - 6% by tax advisors
 - 81% by other solicitors
 - 51% by barristers
 - 3% by conveyancers
 - 9% by estate agents
 - 6% by trust and company service providers
 - No requests had been received from insolvency practitioners, high value dealers or casinos
- Only 48% said that they actually allowed others to rely on them
- The reasons for not allowing reliance included:
 - Risk of civil claims for errors
 - Client confidentiality
 - Too costly or time intensive to provide

Ongoing monitoring

How is it recorded?

- 23% have set times for a form to be completed or a file note to be made.
- 54% rely on routine notes by the fee earner
- 20% rely on notes during supervision meetings
- 56% rely on file audits and reviews

MLRO queries

How are these recorded?

- 27% are kept on the main client file
- 9% on a separate client specific file
- 90% on a central file held by the MLRO
- No one kept them on a practice area file

Training

What staff do they have and who do they train?

- 83% train compliance staff
- 94% train their partners
- 98% train their fee earners
- 90% train their accounts staff
- 68% train their legal secretaries
- 35% train reception staff

Number of staff trained in the last 12 months

- Range: 0 to 3000
- Top 25% are training 310 or more
- 50% are training 70 or fewer
- Bottom 25% are training 5 or fewer

Percentage of your staff being trained

- 36% of respondents were training all their staff
- The bottom 25% were training up to 63% of their staff
- 50% of respondents were training 88% of their staff

How do they train?

- 80% upon induction
 - 71% through AML manual
 - 36% through updates on the intranet
 - 18% through subscriptions to AML news resources
 - 31% through staff meetings
 - 56% through in-house seminars
 - 45% through on-line training
 - 45% through external seminars.
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- In relation to in-house seminars and on-line training – 30% use both, but 27% of respondents use neither.

How regularly do they train through formal seminar or on-line training?

- 51% every 12 months
- 29% every 2 years.

Costs of compliance

We only received a very small response rate, around 20 firms, to these questions. As such the results are not necessarily indicative of the profession as a whole, but provide a basis for starting a discussion about the level of anti-money laundering costs borne by the private sector.

Recording of costs

- 80% of firms do not specifically record time on AML compliance
- 77% do not specifically record costs on AML

Time estimates – per week

- Meeting CDD obligations
 - Top 25% spend 75 hours or more
 - 50% of respondents spend 20 hours or less
- Disclosure discussion and making disclosures
 - Around 2 hours each activity per week
- Keeping records
 - Top 25% spend 9 hours or more
 - 50% of respondents spend 2 hours or less

Time estimates - per year

- AML systems development
 - Top 25% spend 100 hours or more
 - 50% of respondents spend 50 hours or less
- Training
 - Top 25% spend 200 hours or more
 - 50% of respondents spend 40 hours or less

Costs – per annum

- AML systems development
 - 50% are spending up to £4,000
 - top 25% are spending £25,000 or more
 - Range – £4,000 to £1.5 million
- Compliance with CDD
 - 50% are spending up to £5,00
 - top 25% are spending £42,000 or more
 - range - £0 to £1.5 million
- Maintaining records
 - 50% are spending up to £2,500
 - top 25% are spending £10,500 or more
 - range - £0 to £100,000

- Auditing compliance
 - 50% are spending up to £2,250
 - top 25% are spending £13,750 or more
 - range – £0 to £775,000
- Training
 - 50% are spending up to £4,000
 - top 50% are spending £12,250 or more
 - range - £0 to £2.5million
- Communication with MLRO
 - 50% are spending up to £3,000
 - top 25% are spending £13,000 or more
 - range - £0 to £100,000
- Making disclosures
 - 50% are spending up to £500
 - top 25% are spending £7,500 or more
 - range 0 to £164,000

Increase to compliance costs

- Increase in gross expenditure from AML compliance
 - 50 % up to a 10% increase
 - top 25% and increase of 75% or more

Passing on costs to clients

- 90% do not pass on the full cost
- Of those who do
 - 31% passed on 10% of costs
 - 13% passed on 25% of costs
 - 6.5% passed on 50% of costs
- 5% passed on the full cost of compliance

Budgets for 2008 / 09

- 93% said that they were happy that their budget for 2008/09 was sufficient.

Law Society products and services

Professional Update addendum survey

A further survey on the questions relating to services used was conducted in the hope of obtaining a larger sample size and assessing the scalability of the responses. The survey ran for two weeks in December. We received responses from a further 116 firms.

TLS support

- 67% thought that TLS was supportive or very supportive
- 24% were neutral
- 9% thought that TLS was unsupportive or very unsupportive

Lexcel

- 14% had used Lexcel
- 85% of those thought it helped them with AML compliance
- 35% would be interested in obtaining Lexcel if it would assist with compliance

Use of existing services

Service	Survey response	PU response
practice note	96%	91%
practice advice service	42%	29%
AML directory	14%	10%
AML e-alerts	84%	54%
MLRO e-forum	34%	15%
TLS training	54%	47%
AML client brochure	16%	18%