



The Law Society

**Select Committee on the European Union - Sub-  
Committee F (Home Affairs) Inquiry into Money  
Laundering and the Financing of Terrorism**  
**Supplementary written evidence from the Law Society of  
England and Wales**  
March 2009

supporting  
solicitors

## 1. Summary

- 1.1. The Law Society ('The Society') is the professional body for solicitors in England and Wales representing over 115,000 solicitors. The Society represents the interests of the profession to decision makers within Parliament, Government and the wider stakeholder community, and has an established public interest role in law reform.
- 1.2. The Society is committed to ensuring that anti-money laundering measures are clear, proportionate, effective and workable in practice. Through lobbying, the Society is campaigning for the achievement of a level playing-field across the EU and the rest of the world, in order to ensure that UK legal practitioners and businesses are not at a disadvantage in relation to non UK legal practitioners and businesses.
- 1.3. The Society thanks the committee for the opportunity to give oral evidence to on 4 March 2009, and welcome the opportunity to provide supplementary evidence relating to the UK's anti-money laundering and counter terrorist financing regime.
- 1.4. The committee specifically requested access to:
  - The Society's advice to the profession on complying with its anti money laundering and counter terrorist financing obligations; and;
  - The Society's submission to the Home Office on the consent regime.
- 1.5. The Law Society's practice note is available at:  
<http://www.lawsociety.org.uk/productsandservices/practicenotes/aml.page>
- 1.6. The Law Society's submission to the Home Office is available at:  
[http://www.lawsociety.org.uk/documents/downloads/dynamic/lresp\\_consent\\_regime.pdf](http://www.lawsociety.org.uk/documents/downloads/dynamic/lresp_consent_regime.pdf)
- 1.7. The committee also asked for the Society's views on how the anti-money laundering and counter terrorist financing regime could be improved to address the concerns we had raised in our initial written evidence and our oral evidence.
- 1.8. We see that there are two key areas of improvements which could be made, namely:
  - Targeting the AML regime more effectively so that the regulated sector can focus their preventative activities on the criminal conduct which is the focus of the Government's anti-money laundering and counter terrorist financing strategy; and
  - Reducing the cost of client due diligence compliance on the regulated sector.
- 1.9. The Society has outlined in more detail below the specific changes to legislation and actions by government which we think would achieve these improvements.
- 1.10. The Society has also noticed with concern a number of suggestions in evidence before the committee that the problems with the legislation could be resolved through memorandums of understanding with law enforcement, prosecutorial discretion, Executive Government agreements, professional guidance and the like. We urge the committee to take care with respect to

such suggestions. The rule of law provides that the Executive Government cannot contract out of the normal and legal consequences of the legislation which Parliament has enacted. Where there is a problem with the legislation, it is only legislative intervention which will rectify the situation.

## **Targeting the AML regime**

### **2. Review the focus of the definition of criminal property**

2.1. The Society appreciates that this is a complex and difficult area of law, where unintended consequences can easily arise. This is particularly evident in the difficulties faced by the Home Office in achieving consensus on the way forward with respect to the consent regime.

2.2. As the Society advised in our oral evidence there are a number of issues with respect to the definition of criminal property as it applies in the UK. This is partially due to a departure from the FATF recommendations and the EU directives and partially due to the nature of our domestic law.

2.3. The FATF 40 recommendations provide a number of options for countries to define criminal property, through the way they define a predicate offence<sup>1</sup>.

2.4. FATF encourages countries to apply their anti money laundering laws to all serious predicate offences. It defines serious predicate offences as:

- a) all crimes; or
- b) a list of crimes with a penalty of at least one year's imprisonment; or
- c) or a list of crimes which at least covers the following:
  - participation in an organised criminal group and racketeering;
  - terrorism, including terrorist financing;
  - trafficking in human beings and migrant smuggling;
  - sexual exploitation, including sexual exploitation of children;
  - illicit trafficking in narcotic drugs and psychotropic substances;
  - illicit arms trafficking;
  - illicit trafficking in stolen and other goods;
  - corruption and bribery;
  - fraud;
  - counterfeiting currency;
  - counterfeiting and piracy of products;
  - environmental crime;
  - murder, grievous bodily injury;
  - kidnapping, illegal restraint and hostage-taking;
  - robbery or theft;
  - smuggling;
  - extortion;
  - forgery;
  - piracy; and
  - insider trading and market manipulation.

2.5. The UK has adopted the all crimes approach. As we advised in our oral evidence, this can create a stricter application of the law in the UK because

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<sup>1</sup> A predicate offence is the first criminal offence (i.e. theft) through which a person can receive criminal property, in order to then launder the criminal property.

of the very wide range of offences in the UK which are treated as criminal. In many parts of Europe many such offences are dealt with by way of administrative action and have administrative sanctions. This could mean that even in other European countries which adopt an all crimes approach, certain activities which are caught within the UK will not be caught in those countries.

- 2.6. Once one understands the definition of criminal conduct, the legislation goes on to define criminal property as: *“Property which is, or represents, a person’s benefit from criminal conduct, where the alleged offender knows or suspects that it is such”*.
- 2.7. Property is defined as: *“All property whether situated in the UK or abroad, including money, real and personal property, things in action, intangible property and an interest in land or a right in relation to any other property”*.
- 2.8. These definitions raise a number of other problems, which we outlined in our oral evidence, including issues of money laundering on the basis of monies saved, the need for repeated reports about old offences despite attempts to rectify past criminality and the need to obtain consent even where there is absolutely no intent to launder.
- 2.9. Consequently in practice you may have criminal property from a wide number of regulatory offences which, we do not believe, are intended to be within the key focus of the Government’s anti-money laundering and counter terrorist financing strategy, such as:
- Failure to register as a processor of personal data with the Information Commissioner;
  - Failure to obtain a waste disposal licence; or
  - Failure to obtain a fire and asbestos report for the sale of commercial premises.
- 2.10. There may also be anomalous results such as:
- The need to continually report old offences, such as the previous failure to pay the minimum wage, with respect to a business entity, despite efforts to rectify the criminal activity, because the assets of the business entity remain tainted by the criminal conduct of a previous owner; or
  - The potential need to seek consent to return criminal property to the victim of the crime.
- 2.11. The Society notes the Crown Prosecution Service’s evidence before the committee that it would exercise its discretion not to prosecute in relation to such minor regulatory matters or in cases where the law is clearly producing such anomalies. While the Law Society is in favour of prosecutorial discretion generally, the rule of law requires that law, particularly criminal law, is made as clear and as certain as it can be. It is not desirable that solicitors, who are Officers of the Court, are encouraged to knowingly break the law on the basis that the Executive did not really intend the law to operate as it does and avoid prosecution because of the discretion of the prosecutor.
- 2.12. The Society would like to work with the Home Office to review ways of re-focusing the definition of money laundering and the money laundering offences to ensure that they target the anti-money laundering and counter terrorist financing regime so that it is more effective in disrupting serious and organised crime which is at the heart of the Government’s strategy in this

area. We appreciate that this will be a detailed process which will require the involvement of a number of stakeholders.

### **3. Expanding the adequate consideration defence**

- 3.1. Under section 329 of the Proceeds of Crime Act 2002, it is a defence for someone to acquire or possess criminal property if they provided adequate consideration for the property, unless they know or suspect that the goods or services they provided may help another to carry out criminal conduct.
- 3.2. This defence applies where professional advisors receive money for or on account of costs. The fees charged must be reasonable and the value of work must equate with the fees received.
- 3.3. Unfortunately this defence does not apply to sections 327 and 328 of the Proceeds of Crime Act 2002. Where a solicitor enters into a retainer and is receiving funds for costs which they suspect may be tainted, they will be:
  - assisting a person to transfer criminal property in contravention of section 327 and
  - Entering into an arrangement which enables a person to use their criminal property in contravention of section 328.
- 3.4. To ensure that the legislative intention of the defence of adequate consideration is fully implemented, the Society would like to see the defence also applied to sections 327 and 328. This defence does not provide an open gate for criminals to siphon off criminal funds to their professional advisors. Instead it helps to guarantee the fundamental human right of access to justice and a fair and just legal system for people suspected, accused or even convicted of criminal activities.

### **4. Removal of criminal sanctions from the Regulations**

- 4.1. The Money Laundering Regulations 2007 (the Regulations) do not cover the offences of being involved with money laundering. They cover:
  - obtaining correct identity information
  - turning away business if you cannot obtain correct identity information
  - setting up systems to enable you to comply with your obligations and
  - Training your staff.
- 4.2 Within the supervisory regime for compliance with the Regulations, there is the power to discipline, fine, and remove from practice or remove licences of, those who fail to comply with the Regulations. This is consistent with the approach in many other European countries.
- 4.3 We believe that by going further to criminalise a breach of the Regulations; the UK is undermining the proper application of the risk based approach. Instead of the regulated sector in the UK looking first at their client and the transaction to assess the risk of money laundering, they tend instead to look at the risk of going to jail if they get the process wrong. This has tended to result in over-compliance with the Regulations in practice.
- 4.4 Rather than being of benefit to the fight against money laundering, this over-compliance means that a considerable amount of time and resources are spent on the process e.g. obtaining detailed client identification material in

4.5 The law enforcement agencies may take the view that these criminal sanctions exist only for the most serious of cases. However it is hard to imagine that a person in the regulated sector whose failings with respect to the regulations were so bad as to warrant criminal action would not also be able to be charged with a failure to report offence or even a principal money laundering offence. This added level of criminal sanction is neither warranted nor proportionate and is not beneficial to the effective operation of the Government's anti money laundering and counter-terrorist financing strategy.

## **5. Reducing the cost of compliance with the regulations**

5.1. During oral evidence before the committee, it became apparent that small firms in the regulated sector are spending thousands of pounds a year to comply with client due diligence, training and monitoring obligations. Larger firms are spending millions of pounds, while some of the banks are spending tens of millions of pounds in compliance.

5.2. Some of our firms have advised us that opening a new international corporate client matter can cost in the vicinity of £5,000 due to the lost time of fee earners or compliance staff in undertaking all of the checks required and the direct costs associated with obtaining documents or e-information to verify the information they have received. These costs are not directly passed on to the client and present a challenge to such firms as to whether they take on clients who may cost more to verify than the value of the retainer. Smaller firms are also concerned about the costs of client take-on.

5.3. The Society is concerned that much of the client due diligence information required under the Regulations is difficult, if not impossible, to obtain, costly and the requirements to obtain such information are not necessarily targeted at the right point or person to help detect possible money laundering.

5.4. The Society would like to see the UK government and other governments around the world, work together to increase the availability of client due diligence information to the regulated sector in an affordable way.

## **6. Obtaining beneficial ownership information**

6.1. Obtaining information on beneficial owners, particularly in complex structures can be extremely difficult. There are a number of jurisdictions where secrecy of beneficial ownership is protected by law or where the only information you will get is directly from your client.

6.2. The Regulations also require that beneficial owners are identified wherever they exist, and the risk based approach only applies to whether you verify them. This means that even in low risk transactions, you are still required to go through quite detailed beneficial ownership searches. Where the only information available is from the client, you are in effect verifying the information as best as possible, simply by obtaining it. Therefore the risk

based approach, as it currently stands, provides limited benefit in reducing the compliance burden.

- 6.3. The Society would like to see the Regulations amended so that beneficial owners only have to be identified on a risk based approach. This was one of our recommended amendments to the Third European Directive on Money Laundering, which was accepted during the committee stages but was abandoned during the Council of Ministers negotiations.
- 6.4. Also, the Society would ideally like to see all FATF countries prevent entities with obscure beneficial ownership structures from being established in their jurisdiction. However, as an interim measure, we think it would be of assistance if all FATF countries require entities formed within their jurisdiction to register beneficial ownership information on a register. We would like to see that information made available to the regulated sector either free of charge or at a minimal cost.
- 6.5. The Society would like to see the UK government take a lead in negotiations with other jurisdictions to facilitate the creation of such a register.

## **7. Equivalence**

- 7.1. The Society outlined in paragraphs 8.2 and 8.3 of its initial written evidence to this committee how equivalence is meant to reduce the burdens of compliance and how in practice this is not working.
- 7.2. The Society is of the view that the equivalence provisions would be more effective if:
  - a) There were an agreed list of equivalent jurisdictions and regulated markets at an EU or FATF level.
  - b) The Money Laundering Regulations 2007 were amended so that reliance on the government issued list was deemed to be compliance with the Regulations for the purposes of the legal question of equivalence.
  - c) The Money Laundering Regulations 2007 were amended to remove the extra requirements with respect to assessing equivalent markets.

## **8. Politically Exposed Persons and Sanctions**

- 8.1. Firms are spending large sums of money on commercial providers to help them assess whether a client is:
  - a) a politically exposed person (PEP), on whom they have to do enhanced client due diligence, or
  - b) On a sanctions lists, therefore requiring them not to do business with that client.
- 8.2. The definition of a PEP is very wide. It includes all persons who within the last year held one of the following positions with a Community Institution, International Body or a state (other than the UK):
  - a) heads of state, heads of government, ministers and deputy or assistant ministers
  - b) members of parliament

- c) members of supreme courts, or constitutional courts or of other high level judicial bodies whose decisions are not generally subject to further appeal
  - d) members of courts of auditors or of the boards of central banks
  - e) ambassadors, charges d'affairs and high-ranking officers in the armed forces
  - f) members of the administrative, management or supervisory bodies of state-owned enterprises
- 8.3. The definition also includes immediate family members of a PEP and their known close associates. For known close associates, it is sufficient that a regulated person only have regard to information in their possession or which is publicly known.
- 8.4. Where a solicitor is acting for a PEP, it is a criminal offence not to:
- a) have senior management approval to commence the business relationship,
  - b) take adequate measures to establish source of wealth and source of funds, and
  - c) Conduct enhanced ongoing monitoring of the transaction.
- 8.5. In terms of the sanctions list, it is a criminal offence to deal with financial resources of a person on the sanctions list. There are currently approximately 7,000 persons on HM Treasury's consolidated sanctions list. The list is available in HTML or PDF and runs to some 135 pages the way in which it is formatted means that it is not possible to search it electronically. The numbers of clients that firms take on daily makes it time consuming to search the list manually.
- 8.6. With so many people covered by the above definitions and the risks to a firm for dealing with either a PEP or a person on a sanctions lists being so high, it is understandable that many are seeking the assistance of commercial providers to create and search lists for them. However the costs for these services are high.
- 8.7. Within the solicitor's profession, approximately 87% of our member firms are small, with 4 partners or less. They do not have a person who can dedicate their full time to anti-money laundering compliance. Nor can they afford the £1,000 a year fee that is a general starting rate for access to these types of commercial providers. However, the Society is receiving increasing information that PEPs are starting to target smaller legal firms in the hope that they will go undetected.
- 8.8. The Society has long argued that governments are best placed to know who their own PEPs are and it is unfair to impose a requirement on the private sector to conduct enhanced due diligence on those people without providing a public list of who they are.
- 8.9. The Society would like to see:
- a) EU and FATF country governments provide free and easily searchable lists of their own PEPs for use by the regulated sector.
  - b) The UK government make its sanctions list more easily searchable.

## 9. Conclusion



- 9.1. The Society is happy to provide any further information to the committee as required.
- 9.2. We look forward to continuing to work with the UK government and other relevant bodies to ensure that the UK has an anti-money laundering and counter terrorist financing regime which is clear, effective, workable and proportionate and addresses the real risks.