



The Law Society

**Select Committee on the European Union - Sub-
Committee F (Home Affairs) Inquiry into Money
Laundering and the Financing of Terrorism
Response from the Society of England and Wales**

February 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 welcomes the opportunity to provide evidence to the Sub-Committee on UK's anti-money laundering regime, and in particular, the opportunity to address the interplay with the anti-money laundering regimes across European and the rest of the world.
- 1.4. The European anti-money laundering Directives impose quite burdensome obligations on certain parts of the private sector. The strict implementation of the Directives by the UK Government and its decision to impose criminal sanctions for all breaches of the Directive is negatively affecting the competitiveness of UK solicitors, particularly in comparison to other legal practitioners in the EU and around the world.
- 1.5. The Society encourages the UK Government, the European Commission and the Financial Action Taskforce (FATF) to comprehensively examine whether the benefits of the anti-money laundering and asset recovery regimes they have each instigated actually outweigh the burdens imposed. The Society would like them to consider practical ways to help reduce the burdens placed upon the private sector and to provide more detailed information of methodology to help the private sector be more effective in their compliance.

2. Background

- 2.1. International action to tackle money laundering began with the UN treaties on trafficking of illicit substances in 1988 and confiscating the proceeds of crime in 1990.
- 2.2. Following the G7 summit in Paris in 1989, FATF was formed to develop international policies to combat money laundering. FATF published the 40 Recommendations on Money Laundering in 1990 (the FATF recommendations).
- 2.3. The European Commission incorporated the FATF recommendations into its First Money Laundering Directive in 1991. That Directive was implemented into UK law via the Criminal Justice Act 1993 and the Money Laundering Regulations 1993. The Regulations applied to financial institutions and to those engaged in investment business under the Financial Services Act 1986 e.g. solicitors undertaking private client and corporate work.
- 2.4. In 2001, the European Commission responded to amendments to the FATF recommendations, by passing the Second Money Laundering Directive (the

Second Directive). The Second Directive extended anti-money laundering obligations to a number of 'service' professionals, such as accountants, auditors, tax advisors, estate agents and independent legal professionals. The individuals and entities covered by these obligations are referred to as 'the regulated sector' throughout this evidence. The Second Directive was incorporated into UK law via the Proceeds of Crime Act 2002 and the Money Laundering Regulations 2003.

- 2.5. In 2005, the European Commission decided to adopt a Third Money Laundering Directive (the Third Directive). Key changes within the Third Directive were the extension of client due diligence checks to beneficial owners, the recognition of the need for checks to be applied on a risk-based approach, and the requirement for enhanced client due diligence to be undertaken in certain circumstances.
- 2.6. The Third Directive was implemented in the UK via the Money Laundering Regulations 2007, and further amendments to the Proceeds of Crime Act 2002. Implementation was completed on 15 December 2007.
- 2.7. The Society has had many years experience of the UK's legislation and the Money Laundering Regulations and has been actively involved in lobbying on the Directives and the Regulations, both in Europe and in the UK. The majority of the Society's members undertake work which is within the regulated sector and are therefore familiar with the primary legislation as well as having to comply with the regulations.

Response to Questions

3. Cooperation with and between Financial Intelligence Units (FIUs)

3.1. How effective is cooperation among FIUs, and between FIUs and other authorities? What are the practical results of this cooperation?

- 3.1.1. The Society's representative arm is not generally involved in making suspicious activity reports (SARs) to the Serious Organised Crime Agency (SOCA), the UK's FIU. As such, the Society does not have direct experience of the effectiveness of cooperation between FIUs.
- 3.1.2. However, a number of the Society's members have been required to submit SARs in relation to suspected cross-jurisdictional money laundering activities. They advise us that SOCA generally takes the lead in sharing the SARs with other FIUs through the EGMONT Group (an international group of FIUs) and keeps the Society's members informed of the progress of the SAR and the granting of consent in different jurisdictions. Solicitors advise the Society that on this practical level, there appears to be a good level of cooperation between FIUs at an international level.

3.2. How does the private sector feed into this cooperation? To what extent is satisfactory feedback to the private sector required by international standards, and what happens in practice?

Private sector's involvement

- 3.2.1. Through the submission of SARs, in accordance with the requirements under the Proceeds of Crime Act 2002, the private sector provides the FIUs with raw intelligence on money laundering and other crimes. Where those SARs contain information on cross-jurisdictional criminal activity, they may form the basis for intelligence reports to be disseminated by SOCA to other FIUs.

International standards on feedback

- 3.2.2. The provision of feedback to the private sector from FIUs is required by a number of international standards, issued both by FATF and the European Commission.
- 3.2.3. FATF recommendation 25 provides: *The competent authorities should establish guidelines, and provide feedback which will assist financial institutions and designated non-financial businesses and professions in applying national measures to combat money laundering and terrorist financing, and in particular, in detecting and reporting suspicious transactions.*
- 3.2.4. FATF recommendation 32 provides: *Countries should ensure that their competent authorities can review the effectiveness of their systems to combat money laundering and terrorist financing systems by maintaining comprehensive statistics on matters relevant to the effectiveness and efficiency of such systems. This should include statistics on the STRs (suspicious transaction reports) received and disseminated; on money laundering and terrorist financing investigations; prosecutions and convictions, on property frozen, seized and confiscated; and on mutual legal assistance or other international requests for cooperation.*
- 3.2.5. The Third Directive contains the following articles:

Article 33

- i. *Member States shall ensure that they are able to review the effectiveness of their systems to combat money laundering or terrorist financing by maintaining comprehensive statistics on matters relevant to the effectiveness of such systems.*
- ii. *Such statistics shall as a minimum cover the number of suspicious transaction reports made to the FIU, the follow-up given to these reports and indicate on an annual basis the number of persons prosecuted, the number of persons convicted for money laundering or terrorist financing offences and how much property has been frozen, seized or confiscated.*
- iii. *Member States shall ensure that a consolidated review of these statistical reports is published.*

Article 35 (sub parts 2 and 3)

- ii. *Member States shall ensure that the institutions and persons covered by this Directive have access to up-to-date information on the practices of money launderers and terrorist financiers and on indications leading to the recognition of suspicious transactions.*
- iii. *Member States shall ensure that, wherever practicable, timely feedback on the effectiveness of and follow-up to reports of suspected money laundering or terrorist financing is provided.*

Feedback from FATF

- 3.2.6. FATF provides a number of detailed typology reports on their website each year. In 2008 these reports began to focus in greater detail on terrorist financing methodologies and to cover how these methodologies apply in non-financial sectors also covered by the FATF Recommendations. These reports are of interest in identifying global money laundering and terrorist financing trends and methodologies, but

can be of less relevance for smaller firms wanting to understand the money laundering risks they face in their local communities.

- 3.2.7. While mutual evaluations are undertaken in relation to different FATF jurisdictions each year, there is no consolidated report produced by FATF which outlines the size of the criminal economy in each jurisdiction and how effective the anti-money laundering regimes have been in disrupting and preventing the criminal activity and the laundering of the proceeds of that criminal activity. At present there is no agreed methodology for making such assessments, and academic research questions the capacity of agencies to undertake such assessments on the basis of existing information.

Feedback from the European Commission

- 3.2.8. The European Commission does not provide any information on methodologies or an annual report on the effectiveness of the money laundering regimes within each of its jurisdictions.

Feedback within the UK

- 3.2.9. SOCA issues an annual threat assessment which outlines the estimated size of the criminal economy and provides a general overview of the criminal activities prevalent across the UK, as well as an indication of where certain criminal activities are concentrated.
- 3.2.10. SOCA has recently started producing a range of 'alert products' which highlight detailed methodologies being utilised within the UK to launder funds. Some information is also provided as to where in the UK these particular methodologies are being employed. Currently these alert products are provided to law enforcement bodies and anti-money laundering regulators and supervisors. Due to the nature of the protective marking and confidentiality disclaimers on these products, permission needs to be obtained from SOCA on a case by case basis when disseminating this information publicly to one's members.
- 3.2.11. In relation to individual SARs, the private sector will only receive feedback on the usefulness of their SAR and what action law enforcement is taking if they have sought consent, or if law enforcement requires further information from the reporter during an investigation. However, the level of feedback will be very limited or non-existent in most cases. Many of the Society's members still report a perception that their SARs are simply going into a black hole and they are not sure that they are actually making any difference in the fight against crime generally or money laundering more specifically.
- 3.2.12. SOCA is now producing an annual SARs report. This provides an overview of:
- the number of SARs received,
 - who is making those SARs and,
 - where they are able to obtain information from other law enforcement agencies: information on the amount of money seized or recovered, arrests made, and convictions obtained.
- 3.2.13. This report goes some way to helping demonstrate to those covered by the UK's anti-money laundering regime that their SARs are actually being used. However, the report does not make clear how

many of the SARs made by the non-financial sector provide information which adds value to that provided by the financial sector. Nor does the report provide a comprehensive review of the whole UK criminal asset recovery regime. Responsibility for asset recovery sits across 43 police forces; a number of government departments, including HM Revenue and Customs and the Department of Work and Pensions; as well as the CPS. The information held by all of these separate agencies on asset recovery is not collated into a single report.

3.2.14. The Society welcomes the efforts by SOCA to provide greater levels of feedback to the private sector and greater transparency in its processes. The Society also welcomes the consistent support from FATF to the regulated sector through the public dissemination of emerging methodologies.

3.2.15. The Society would encourage the UK government to look at how they can provide a more comprehensive review of the effectiveness of the anti-money laundering and asset recovery regimes within the UK on a regular basis. The Society would be interested in seeing both the European Commission and FATF produce a regular review on the effectiveness of the activities being undertaken across their member jurisdictions to prevent and disrupt money laundering. The Society appreciates that at this time, there is no internationally agreed methodology for collecting and assessing this information. The creation of such a methodology should be the first step in this process.

3.2.16. The Society would also be interested in more information being provided about methodologies which will assist those regulated persons in the non-financial sector to identify warning signs of money laundering within their sector and particularly to help identify suspected terrorist financing.

3.3. What is the extent of the feedback and input on terrorist financing issues from intelligence and security services?

3.3.1. The Society appreciates that the provision of information about terrorist methodologies can be particularly sensitive and has the potential to jeopardise existing investigations or provide inspiration for new terrorists cells in their planning. However, there is a legal obligation on solicitors to be alert to warning signs of terrorist financing and to report cases of known or suspected terrorist financing. Failure to discharge those legal obligations effectively may lead to a jail term.

3.3.2. For this reason the Society is concerned about the lack of information, particularly for those in the non-financial sector, in relation to warning signs of terrorist financing. The Society appreciate the work being done by FATF to incorporate more terrorist financing methodologies within their typology reports, and encourages both the UK Government and the European Commission to look at ways to develop greater information on terrorist financing methodologies for those outside of the financial sector.

3.3.3. The Society would be happy to work with governments and law enforcement agencies on ways to disseminate this information to its members for the purpose of terrorist financing prevention, without it being disseminated more widely to the public.

3.4. To what extent are alternative remittance systems appropriately covered by obligations of cooperation in this context? What will be the impact of the implementation by Member States of the relevant provisions of Directive 2007/54/EC in this regard?

3.4.1. The Society has no comment to make on this question.

4. EU internal architecture

4.1. To what extent is the EU internal architecture adequate to counter current and future challenges?

4.1.1. The European Union's internal architecture in this field is a complex structure of inter-governmental cooperation under the third pillar in relation to policy and judicial cooperation mechanisms and first pillar Community law. Because the anti-money laundering obligations originate from FATF, an international body, there is no obligation on the Commission to undertake any impact assessment to consider whether the obligations imposed are proportionate to the perceived ill within Europe or that they are fit for purpose.

4.1.2. The competence relating to anti-money laundering matters is split between the Directorate General for Internal Market and the Directorate General for Freedom, Security and Justice.

4.1.3. This results in a myriad of decision-making procedures, including:

- co-decision;
- consultation;
- implementation measures adopted under the comitology procedure, and;
- adoption by parliament in the form of a directive.

4.1.4. Implementation into national law is left to Member States, who may face internal pressures during implementation processes that are different to those taken into account during negotiations for the passing of the Directive through Commission processes. This may mean that Member States significantly delay implementation, only partially implement or implement on a basis that is different to its represented intentions during the negotiations in relation to a Directive.

4.1.5. While the Commission has the power to commence infringement proceedings against those Member States which fail to implement a Directive, this procedure is costly and time consuming. The Commission cannot act to remove either gold-plating or under-implementation in national law which acts as a competition barrier.

4.1.6. The Society has found that the current approach has not provided the best model for coherence and clarity. The Society appreciates that in the area of money laundering there is a delicate balancing act in developing legislation that will give sufficient powers to law enforcement, but not overburden private sector participants, all within the confines of the FATF recommendations.

4.1.7. During the drafting of the Third Directive, the Society proposed a number of amendments which were tabled by a Member of the European Parliament. These amendments were proposed on the basis of the Society's detailed understanding of how various legal entities are formed and conduct their business, and how different transactions

proceed to completion. The Society recommended amendments which were designed to reduce unnecessary burdens on the regulated sector while ensuring that the right information about ownership and transactions were obtained at the time where it was most likely to uncover money laundering. The Society also made a number of recommendations which were designed to ensure a more level playing field across the European Union.

4.1.8. During the committee stages many of the Society's proposed amendments were adopted and formed part of the draft plenary session report. However most of these amendments were withdrawn seemingly as part of the wide political negotiations with the Council of Ministers and the rush to secure agreement on the text. Many of the issues on which the Society sought amendments are the same issues which are still causing the solicitors profession much difficulty and great expense.

4.1.9. In terms of national implementation, many of the other Member States have not extended their anti-money laundering regime to legal professionals and seven Member States have failed to implement the Third Directive a year after the deadline for implementation.

4.1.10. The UK, on the other hand, has strictly implemented the directive. The Society found the implementation of the concept of beneficial owners in relation to trusts particularly challenging. During negotiations in Europe, the Society were advised that steps would be taken during implementation into national law to make sure the definition actually worked for common law jurisdictions. Unfortunately when it came to drafting the regulations, HM Treasury advised that they were unable to make amendments because they were bound by the wording of the Third Directive.

4.1.11. The Society did not accept this as the correct position on UK implementation and received support from the Commission for its view. This meant that the Society had to undertake extensive lobbying work and obtain legal opinion which demonstrated that the proposed drafting was so lacking in meaning in English law that it was unconstitutional and unlawful. Compromise drafting was eventually agreed upon, although the application of the civil concept of beneficial ownership to common law trust is still an area which causes difficulty to many solicitors and others within the regulated sector. The repeated need to re-lobby on particular issues uses up valuable resources of professional and supervisory bodies, limiting the time available to be devoted to preparing guidance and advice for their members to help them comply with their obligations.

4.2. What are the respective roles of Europol and Eurojust in countering money laundering and terrorist financing?

4.2.1. Europol is the organisation that aims to improve the effectiveness and co-operation of competent authorities in the Member States in preventing and combating terrorism, unlawful drug trafficking and other serious forms of international organised crime. Under this remit, they have competence to deal with anti-money laundering and examine activity in relation to terrorist financing. However, the Society understands that Europol has little direct impact in the UK and that investigations will instead be led by UK agencies, such as SOCA.

4.2.2. Eurojust is a permanent network of judges and prosecutors, with a remit to enhance the effectiveness of the competent authorities within Member States when they are dealing with the investigation and prosecution of serious cross-border and organised crime. In the Council Decision establishing Eurojust, the competence to act in relation to the laundering of the proceeds of crime is clearly set out. The Society understands that co-ordination meetings between national authorities have taken place in relation to money laundering offences, but that the cases considered at these meetings have not had terrorist financing as their core issue. Eurojust has a coordinating function rather than a prosecutorial or investigative role as such. The Treaty of Lisbon would provide Eurojust with a mandate to initiate criminal investigations which it does not have under the current legal basis.

5. International Cooperation

5.1. What have been the results of the third round of mutual evaluations of EU Member States to date carried out by the FATF and MONEYVAL, with particular reference to the effectiveness of international cooperation (including as between FIUs)?

5.1.1. Full details of the mutual evaluations can be found on the FATF website. A short summary of the key international cooperation indicators for the mutual evaluations published in 2007 and 2008 is attached at Annex A of this paper.

5.2. To what extent has the formal framework for criminal justice cooperation in this area been effective?

5.2.1. The mutual evaluation reports appear to suggest that criminal justice cooperation in the area of anti-money laundering and counter terrorist financing works well at times but could be improved.

5.3. To what extent are these systems used to enforce compliance with national tax obligations?

5.3.1. While the Society is aware that information on suspected breaches of taxation obligations, both nationally and internationally, forms the basis for SARs made in the UK, the Society is not aware of the extent to which this information is being shared with other FIUs.

6. EU-UN cooperation

6.1. What is the extent of EU-UN cooperation on financing of terrorism? What are the longer-term implications of the *Kadi* judgment?

Background to Kadi's case

6.1.1. The United Nations Sanctions Committee designated Mr Kadi and the Al Barakaat International Foundation as associated with Usama bin Laden, Al-Qaeda or the Taliban. In accordance with resolutions of the Security Council, UN Member States must freeze the funds and other financial resources of such persons or entities. To give effect to the resolutions, the Council amended Regulation 881/2002, ordering the freezing of funds and economic resources of the persons and entities listed, in order to include the claimants. The Court of First Instance (CFI) rejected Mr Kadi's and Al Barakaat's action for annulment of the Regulation. It ruled that in principle the Community courts have no jurisdiction, except concerning *jus cogens*, to review the validity of the Regulation as Member States are bound to comply with Security Council

resolutions according to the Charter of the United Nations, an international treaty which prevails over Community law.

Judgment

6.1.2. While the ECJ confirmed that the Council was competent to adopt the Regulation, it set aside the CFI judgment. It found that Community courts must ensure the review of the lawfulness of all Community acts in the light of the fundamental rights which form an integral part of the general principles of Community law. This includes the review of Community measures which are designed to give effect to resolutions adopted by the Security Council. It annulled the Regulation in so far as it froze Mr Kadi's and Al Barakaat's funds as their rights of defence, including the right to be heard, and the right to an effective legal remedy had not been respected. Indeed, the Regulation had no procedure for communicating the evidence justifying the inclusion of the names of the persons concerned in the list. Moreover, the lack of guarantee, enabling the case to be put in the circumstances, constituted an unjustified restriction on the right to property. The Court maintained the effects of the Regulation for a period of three months in order to allow the Council to remedy the infringements.

Implications from the judgement

6.1.3. The Society appreciates and accepts that there is a public interest in the protection of society as a whole from terrorism and terrorist financing, and accept that at times law enforcement and international bodies will have to act quickly on preventative measures. However the Society firmly believe that due regard must be had for the individual's human rights at all times. These rights must particularly be respected once the initial threat of the financing has been curtailed through the imposition of sanctions and freezing orders.

6.1.4. In terms of the relationship with the UN/EU for future counter terrorist financing cooperation, the Society believes that this judgement will promote a greater transparency and accountability in the relationship. This will allow the European Union, through its legislative body to act as a responsible check and balance on the UN's use of what is an extremely draconian power.

6.1.5. The Society hopes that the Kadi judgement will produce a greater awareness within all international and legislative bodies of the need to balance carefully the public interest with the fundamental human rights of individuals when exercising powers.

7. Monitoring implementation

7.1. What EU mechanisms exist for monitoring implementation of the relevant legislative measures, and what results in terms of formal compliance and effective implementation have so far emerged from the use of those measures?

7.1.1. The Directorate General for Internal Market publishes a log of the transposition measures for the Financial Services Action Plan Directives. As of January 8 2008 this includes the Third Directive.¹ This table

¹http://ec.europa.eu/internal_market/finances/docs/actionplan/index/transposition_en.pdf

identifies where Member States have completed that notification process on the implementation of the Third Directive - or not.

7.1.2. At present there are seven Member States who have not communicated this information and infringement proceedings have been commenced.

7.1.3. Where a Member State notifies the Commission of their implementation measures the file is closed. To date no examination of the substance of the provisions contained in the Member State's legislation has been undertaken to determine infringement of specific articles. As such there is extensive variation in the level of implementation between Member States.

7.1.4. While the infringement procedure may be helpful in the long term as regards effective compliance with the EU Directive this is a lengthy and time consuming process.

7.1.5. As regards third pillar measures, the Council instigates a system of peer review. The European Commission publishes implementation reports. While these have the persuasive "name and shame" capability, there are no infringement powers under the third pillar.

7.1.6. The FATF mutual evaluations have a similar persuasive "name and shame" capability. However the fact that these reviews are conducted as a peer review and adoption of the final report is subject to a vote by the FATF membership. The Society is concerned that there may be pressure to soften criticism of fellow jurisdictions for political reasons rather than a strict application of the evaluation methodology. This may in turn reduce the effect of such mutual evaluation reports in shaping governmental action by the individual Member States.

7.1.7. FATF also has the power to list a jurisdiction as being non-compliant. The review of 47 jurisdictions commenced in 1998, with 23 jurisdictions listed as non-compliant in 2000 and 2001. FATF can not prohibit individuals or entities undertaking business with other individuals or entities within the non-compliant jurisdictions. However, it can issue warnings about those jurisdictions and recommend that Member States imposed high levels of due diligence for transactions and business relationships with individuals and entities from those jurisdictions. In 2006 the last two jurisdictions were removed from the non-compliant list. It should be noted that removal from the FATF non-compliant list does not mean that a jurisdiction has an anti-money laundering or counter terrorist financing regime which is fully compliant with the FATF recommendations or equivalent to the Third Directive.

7.2. What are the implications of those results for cooperation within the EU, and more broadly?

7.2.1. Where there are differing levels of implementation across different jurisdictions there is the risk of businesses within more regulated jurisdictions suffering a competitive disadvantage to those in less regulated jurisdictions.

7.2.2. The Society is aware that in certain jurisdictions where legal professionals are not covered by the Third Directive, their complete exemption from reporting suspicious activities is being used as a selling point. Even where direct competition is not affected, the costs of the extra burden of compliance with stringent anti-money laundering

obligations decreases the ability of those firms to price their services competitively.

- 7.2.3. There is a risk that regulated businesses within strictly compliant jurisdictions will be subsidising law enforcement and crime reduction in other jurisdictions, where their greater compliance and higher levels of quality reporting result in relevant intelligence being disseminated abroad. This is of greater significance if the other jurisdictions are failing to provide timely and relevant intelligence to the FIUs in the strictly compliant jurisdictions.

7.3. Has consideration been given within the EU or by the FATF to whether the overall results derived from the present system justify the burdens placed on the private sector?

- 7.3.1. The mutual evaluations conducted by FATF do not consider the costs actually borne by the private sector in meeting their compliance obligations. The mutual evaluations also do not quantify the scale of the criminal economy in the relevant jurisdiction or the actual overall results in disturbing or preventing criminal activity achieved through the anti-money laundering regime in that jurisdiction.
- 7.3.2. The European Commission did not undertake an impact assessment of the FATF obligations before passing any of the European Directives on anti-money laundering. The Second Directive contained a requirement to conduct a review of the extension of anti-money laundering obligations to legal professionals. This review did not occur until after the adoption of the Third Directive. Due to the number of Member States which had either not extended their anti-money laundering regime to cover legal professionals at all or who had significantly delayed in doing so, the report was unable to draw any significant conclusions as to the appropriateness of their inclusion.
- 7.3.3. The Society is of the view that it would be appropriate for both FATF and the European Commission to consider in detail whether the overall benefits from anti-money laundering regimes justify the burden placed on the private sector. As stated earlier in this evidence, a starting point for such a review would be the difficult task of formulating an agreed methodology by which to collect information and assess the extent of the criminal economy and the effectiveness of the anti-money laundering regime.
- 7.3.4. In the UK the Society understands that there are approximately 150,000 private sector entities regulated for anti-money laundering. In 2007/08 they made 210,000 SARs. In that period, the UK government actually recovered approximately £135.7 million in criminal property. Even if all of the criminal property recovered in the UK was as a result of the anti-money laundering regime and the receipt of SARs, which it is not, the highest average return per SAR would be approximately £646. While government may point to the prevention value of the anti-money laundering regime, it is very difficult to calculate the monetary value of crime that is disrupted and prevented. However, it is interesting to note that there has been no change to estimated economic and social cost of serious organised crime in the UK of around £20 billion, according to the UK threat assessments in both 2006/07 and 2008/09.

7.3.5. Estimating the cost of compliance with anti-money laundering obligations for the regulated sector is also not an easy task. Firms may be able to quantify:

- the number of staff employed to undertake client due diligence checks and make SARs;
- the cost of subscriptions for e-verification services;
- the cost of new case management systems to record due diligence and ongoing monitoring, and;
- fees incurred for training programmes or the cost of providing internal training.

7.3.6. Many firms will not however be able to quantify the amount of time spent by individual staff members across the firm:

- assessing the risks of clients;
- chasing up due diligence material;
- monitoring clients and transactions for warning signs, and;
- discussing suspicions and internal reports with MLROs and deciding whether or not a SAR is required to be made.

7.3.7. These hidden costs are felt more keenly by those parts of the regulated sector where transactions are not mere numbers and ongoing monitoring is not susceptible to automated processes. What is clear is that the private sector is investing more in the UK's anti-money laundering regime than the UK government is recovering because of it.

7.3.8. The Society conducted a survey in late 2008 to assess how solicitors were implementing the Money Laundering Regulations 2007. While the responses in relation to costs of compliance were very small in number, by comparison to the profession as a whole, they do provide illustrative examples of what some firms are spending on compliance. The results suggest that even small firms are spending thousands of pounds a year in compliance, while large international firms are spending millions.

7.3.9. The results of the survey are at Annex B of this response.

7.4. Are there plans to review the existing EU legislation or international standards in a manner which would be more sensitive to the position of the private sector?

7.4.1. The Society is aware that the European Commission is set to review certain aspects of the implementation of the Third Directive during 2009 and 2010. The Society is already in discussion with the Commission about the issues which the review may legitimately cover.

7.4.2. From December 2007, FATF engaged in more open dialogue with the non-financial parts of the private sector which are covered by the FATF Recommendations. The Society was pleased to be involved, in conjunction with the CCBE and the IBA, in these productive discussions with FATF. These discussions lead to the development of useful guidance on applying the risk based approach to the legal sector.

7.4.3. The Society welcomes increased dialogue with legislators and policy setters in the area of anti-money laundering and counter terrorist financing. The Society is particularly keen to enhance understanding of legislators as to how non-financial sections of the regulated sector

operate, so that greater proportionality can be built into anti-money laundering obligations.

8. Compliance and equivalence

8.1. What are the powers and procedures with respect to those third countries which fail properly to implement international standards in these areas? Are these adequate?

8.1.1. As outlined in section 7.1 above, FATF undertakes mutual evaluations and regular reviews of their non-compliant list. Where a jurisdiction is listed as non-compliant, FATF can recommend that Member States impose higher due diligence and require extra precautions be taken when dealing with individuals and entities from those third jurisdictions. FATF cannot take any direct action against the non-compliant jurisdictions.

8.1.2. The Commission's infringement powers do not extend to non-EU jurisdictions.

8.1.3. Individuals and firms in strictly regulated Member States which undertake business with those from under-regulated third jurisdictions face a higher risk of being involved in money laundering. This risk may act as a deterrent for some in conducting business within those third jurisdictions, but it is not clear that this restriction on business is sufficient to bring about changes in the anti-money laundering regimes of third jurisdictions. Instead, the higher the sanctions for those in the strictly regulated Member States, the greater the risk to undertake business in these third jurisdictions and the greater restriction is placed on their competitiveness and ability to operate freely across jurisdictions.

8.2. Does the 2005 Directive adequately encourage non-EU States which have introduced equivalent systems to counter money laundering and the financing of terrorism?

8.2.1. The Third Directive allows for client due diligence burdens to be reduced in certain cases where a regulated individual or entity is undertaking business with an individual or entity in a jurisdiction with equivalent anti-money laundering obligations. The Third Directive also requires that enhanced due diligence is undertaken in circumstances where there is a higher risk of money laundering; although what amounts to enhanced due diligence in such cases is undefined.

8.2.2. There are two key areas where equivalence can reduce burdens, these are through reliance and simplified due diligence.

8.2.3. In the Society's recent survey (at Annex B), only 40% of respondents had relied on regulated persons outside the UK and this was generally only other legal professionals. 64% of respondents advised that they chose not to use the reliance provisions because they remained criminally liable for any failures by the person relied upon, while 48% were not happy with the due diligence undertaken by others, even where the standards were supposed to be equivalent.

8.2.4. In relation to simplified due diligence, 71% found these provisions useful when they could use them; but for the majority of respondents, these provisions applied to less than 50% of their clients. Also, 43% found it difficult to obtain information which would allow them to decide that simplified due diligence actually could be applied.

- 8.2.5. Respondents reported a very small amount of work being lost due to enhanced due diligence, although some had received negative comments from clients about the extra requirements.
- 8.2.6. As such the barriers to non-equivalent jurisdictions are not insurmountable and the reductions in burdens for those which are equivalent are minimal.
- 8.2.7. The greatest incentive for other non-EU jurisdictions to develop equivalent systems to counter money laundering and terrorist financing would be clear evidence that the benefits to their economy and society as a whole outweigh the burdens imposed on the private sector. Unfortunately, to date this analysis has not been undertaken, nor this evidence provided.

8.3. How does the system for determining equivalence operate in practice?

- 8.3.1. There is currently no transparent system which provides an individual or entity in the regulated sector in the UK with any certainty that they are dealing with an equivalent jurisdiction or regulated market.
- 8.3.2. Regulated individuals or entities are required to make the assessment of equivalence themselves. Under the Money Laundering Regulations 2007 there is no single definition of an equivalent non-EU jurisdiction.
- 8.3.3. For reliance provisions to apply in relation to persons within a non-EU jurisdiction, the person must be:
- A credit or financial institution (or equivalent institution), auditor, insolvency practitioner, external accountant, tax adviser or independent legal professional;
 - Subject to mandatory professional registration recognised by law;
 - Subject to requirements equivalent to those laid down in the money laundering directive, and;
 - Supervised for compliance with those requirements in a manner equivalent to section 2 of Chapter V of the money laundering directive.
- 8.3.4. Simplified due diligence will apply where the client is a company whose securities are listed on a regulated market subject to specified disclosure obligations. These are disclosure obligations which are consistent with:
- Article 6(1) to (4) of Directive 2003/6/EC of the European Parliament and the Council of 28 January 2003 on insider dealing and market manipulation;
 - Articles 3, 5, 7, 8 10, 14 and 16 of Directive 2003/71/EC of the European Parliament and of the Council of 4th November 2003 on the prospectuses to be published when securities are offered to the public or admitted to trading;
 - Articles 4 to 6, 14, 16 to 19 and 30 of the Directive 2004/109/EC of the European Parliament and of the Council of 15th December 2004 relating to the harmonisation of transparency requirements in relation to information about insurers whose securities are admitted to trading on a regulated market, or;

- Community legislation made under the provisions mentioned above.
- 8.3.5. Neither the Third Directive nor the Money Laundering Regulations 2007 specify whether it is sufficient that the other jurisdiction simply has legislation in place or whether practical compliance and enforcement is actually required. It is also not clear whether it is sufficient that the majority of the requirements set out are met or if all must be met.
- 8.3.6. Simply obtaining information, in one's own language, on the legislative frameworks existing in other countries, let alone information on their practical application is very difficult, time consuming and costly for those within the private sector.
- 8.3.7. HM Treasury has agreed a list of countries outside of the EU which are considered to have equivalent money laundering legislation. However this list is voluntary, non-binding and does not have the force of law.
- 8.3.8. The countries included on that list are:
- Argentina
 - Australia
 - Brazil
 - Canada
 - Hong Kong
 - Japan
 - Mexico
 - New Zealand
 - Russian Federation
 - Singapore
 - Switzerland
 - South Africa
 - United States
- 8.3.9. However, in the case of Argentina, Australia, Brazil, Canada, Mexico, and the United States, the anti-money laundering legislation does not apply to legal professionals, which is a requirement under the Third Directive. Other countries on the list have been reviewed by FATF which has deemed aspects of their compliance only partial or in some cases there are aspects which are non-compliant. As such, it is not clear that reliance on the list issued by HM Treasury would satisfy the requirements set out in the Money Laundering Regulations 2007 for assessing equivalence.
- 8.3.10. The Society and its members appreciate the flexibility that the current regulations provide in allowing firms to take a risk based approach in assessing equivalence in emerging markets. However the Society is of the view there needs to be greater transparency in the law, not just guidance or government statements, to make it easier and more cost effective for regulated individuals and entities to actually assess equivalence, particularly in well established jurisdictions and markets.