Solicitors Regulation Authority

Anti Money Laundering Report

May 2016

Contents

Foreword

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Chief Executive

The proceeds of corruption and crime have no place in our economy and markets. As our report says, law firms are attractive to criminals because they are seen as adding legitimacy and credibility to transactions, and they do of course handle significant finance.

As the regulator of some 10,300 law firms and 170,000 solicitors in England and Wales, we are a supervisory authority with a key role in making sure law firms and their staff are meeting their anti money laundering obligations under our Code of Conduct and in legislation. We do that through raising awareness, through monitoring and through taking robust action when we identify a concern. As part of that, this report sets out the results of an intensive review of solicitors' anti money laundering compliance.

We share examples of both best and poor practice in our report in order to help firms – and I am pleased that the overall picture is positive. But neither we, nor the firms we regulate, can be complacent. It is important that public confidence is well placed and that solicitors are meeting the high professional standards we expect. Those standards have to be set independently in the public interest.

Against the backdrop of Government proposals to separate out regulation and representation in the legal sector, it is timely to remind ourselves that any perception of a conflict of interest will undermine public confidence. Although we operate independently, our status as part of the Law Society, which represents solicitors and their interests, is thrown into sharp relief in this difficult area. Truly independent regulation is all the more necessary as the need to fight corruption and money laundering becomes ever more important.

For us, preventing money laundering, with its connections to crime, corruption and terrorism, is a priority. The public, Government and the vast majority of the profession clearly agree with us.

Introduction

In September 2014, we announced our plan to undertake a thematic review of anti money laundering (AML) compliance by solicitors.[1] The principal aim was to gain knowledge and understanding of the AML compliance policies, procedures and controls implemented by a wide range of law firms, and determine how effectively firms were managing risks in this area. We also wanted to ensure that solicitors and their firms were fully aware of their statutory and regulatory obligations in relation to AML, and were up to date on forthcoming changes, such as the 4th Money Laundering Directive.

This report outlines what we found and also includes several examples of the good and poor practices that we encountered.

The AML thematic review builds on our previous work in this area. This report should be read together with our earlier publications (see here). Money laundering remains one of our priority risks for 2016[2], and this is not likely to change. We have produced a detailed overview of the risk which money laundering poses,[3] two warning notices,[4] and case studies illustrating practice risks.[5]

The aim of this report is to highlight the requirements of the Money Laundering Regulations 2007 (MLR), the Proceeds of Crime Act 2002 (PoCA), the Terrorism Act 2000 and the internal practices and procedures that can help solicitors and their staff to comply. This, in turn, will ensure that the legal profession plays its part in protecting itself, the public and society in general from the laundering of the proceeds of crime.

The key areas we discussed with firms were:

- Money Laundering Reporting Officers (MLROs)
- AML policies
- Client due diligence (CDD)
- AML training and awareness
- Reporting
- Suspicious Activity Reports (SARs)
- Record keeping

These areas are covered in this report.

Why have we done this?

Money laundering is an essential tool of serious and organised crime and terrorism. Solicitors are respected professionals who regularly handle large numbers of financial and other transactions. Criminals wish to take advantage of this and in particular the credibility and legitimacy given by lawyer participation in transactions. Solicitors' firms are an attractive target for those wishing to launder the proceeds of crime, as has been highlighted by the Financial Action Task Force (FATF).[6]

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1. SRA steps up anti money laundering work, 8 September 2014
2. SRA Risk Outlook 2015/16
3. Cleaning Up: Law Firms and the Risk of Money Laundering, November 2014
4. Warning notice: Money laundering and terrorist financing 8 December 2014 and Money Laundering and terrorist financing-suspicious activity reports 8 December 2014
5. Case studies: Money laundering - inadequate systems and controls over the transfer of money
6. Money Laundering and Terrorist Financing Vulnerabilities of Legal Professionals, June 2013

Solicitors have obligations under the MLR and PoCA which are directed at minimising the laundering of the proceeds of crime. Aspects of this regime are technical and complex.

In addition, the SRA Code of Conduct 2011, specifically requires compliance with money laundering legislation.[7]

Finally, the 4th Anti Money Laundering Directive[8] has been adopted and must be brought into force in European Union member states by 26 June 2017. It requires a number of changes to national AML regimes. These will impose greater demands on those in the legal profession in England & Wales who conduct business covered by the directive.

Internal Drivers

As a regulator and supervisory authority, we have a statutory duty under the MLR to effectively monitor legal professionals and their activities that fall under the regulations. We must take necessary measures to secure their compliance with them.[9]

We continue to receive a high number of reports regarding suspected money laundering and related activity. These reports are received from a wide variety of sources including the public, law firms, other regulators, law enforcement agencies and our own supervision and investigation of the profession. Each allegation is assessed on its facts before any further action is taken, which may include forensic investigation.

Money laundering is a serious crime and participation can result in severe penalties. Additionally, The Solicitors Disciplinary Tribunal (SDT) views it particularly seriously, even where the solicitor's participation was naïve and involved no personal gain. Cases that reach the SDT can result in suspension or strike-off.[10]

Reports to the SRA relating to money laundering 2012-2015

Nature of report	2012	2013	2014	2015	Total
Breach of Money Laundering Regulations or Proceeds of Crime	78	74	101	85	338
Money laundering (perpetrator or facilitator)	24	68	82	63	237
Providing banking facilities through client account	5	22	16	22	65

7. Outcome 7.5 of the Solicitors Code of Conduct 2011
8. DIRECTIVE (EU) 2015/849 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL
9. ML Reg 24
10. For example, SRA v Olayemi Daniel (2015) 11343-2015; SRA v Tidd (2013) 11178-2013

External Drivers

There was, and remains, a high level of external focus and increased activity on AML compliance from HM Government and law enforcement agencies. There is a genuine expectation that regulators should do more and this message was reinforced during the course of the consultation for the National Risk Assessment (NRA) on AML compliance.

The Government's Serious and Organised Crime Strategy[11]

This highlighted that a small number of complicit or negligent professional enablers, such as bankers, lawyers and accountants, can act as gatekeepers between organised criminals and the legitimate economy. To tackle this threat, the Home Office, wider government and law enforcement agencies, worked together with us and the Law Society to develop and deliver a communications campaign between October 2014 and February 2015 in order to:

- increase law firms' ability to recognise emerging money-laundering threats
- promote existing good practice
- encourage the legal sector to submit high-quality SARs.

The campaign received strong support from the legal sector, with influential professionals from a range of legal firms joining with representatives from the regulatory bodies, law enforcement and government, to promote key messages. This was achieved through:

- existing forums
- conferences and newsletters
- the legal sector press
- dedicated events such as round-tables and webinars.

During the campaign, an increase in law firms accessing the AML Guidance provided by the Law Society was identified. There was also an increase in SARs reporting to the National Crime Agency's UK Financial Intelligence Unit (NCA) in comparison to the previous year. The campaign period also coincided with our thematic review. Therefore it is likely both of these initiatives improved overall AML awareness and in turn led to an increase in SARs from the legal sector.

From November 2015, a second phase of the communications activity began and was delivered jointly with the legal and accountancy sectors. It aimed to promote and reinforce best AML compliance practice.

The Serious Crime Bill

The Serious Crime Bill had been progressing through Parliament during 2014 and received Royal Assent on 3 March 2015. Part of the Act is designed to "discourage corrupt and complicit professionals who support or facilitate organised crime". The Act contains a new offence of participation in the criminal activities of an organised crime group which carries a maximum custodial sentence of five years.

11. Serious-organised-crime-strategy, Gov.uk publication October 2013

The 4th Anti Money Laundering Directive

In December 2014, following a substantial period of negotiation, the European Union agreed the final text of the 4th Anti Money Laundering Directive. It was formally adopted on the 5 June 2015. EU member states have two years to transpose the new standards into their national legislation. Some key requirements of the directive, that are of relevance to the legal sector, include:

- an increase in the emphasis on a risk based approach in which law firms will be required to have written AML/CFT (Counter Financing of Terrorism) risk assessments, policies, procedures and controls in place proportionate to the nature and size of the firm

- a widening of the definition of Politically Exposed Persons (PEPs) to include both domestic and foreign PEPs

- changes in the application of simplified due diligence (SDD). Firms will need to provide justification for SDD after conducting a risk analysis to determine that a business relationship or risk presents a lower degree of risk

- an increase in transparency around beneficial ownership of companies and trusts and the maintenance of a central beneficial owner registry.

The Financial Action Task Force Mutual Evaluation Review (FATF MER)

In December 2006, the United Kingdom was the subject of a FATF MER which reported in June 2007. The next FATF MER of the United Kingdom was originally scheduled for spring 2016, but is now due to take place in spring 2017. It was anticipated that HM Treasury and the Home Office in preparation for the review, would (as has now happened) set up a series of engagements with regulators, including us.

The National Risk Assessment (NRA)

This was to be published late in 2015 and would have an aligned UK Action Plan to drive activity forward in anticipation of the scheduled FATF MER in Spring 2016.

Our Approach

Our thematic review was undertaken over a period of eight months (from 1 October 2014 to 31 May 2015) and we engaged with 252 firms in total.[12]

We specifically did not select a representative sample of firms but instead adopted a risk based approach, focussing our review on those firms identified as being either high impact and or higher risk. Historically, firms which have a potentially high impact owing to their size, turnover and volume of client base have been included in the Regulatory Management programme. Although, the fact that these firms are potentially high impact does not necessarily mean that they pose a high AML risk. The sample also included all firms that were then subject to a Forensic Investigation in the review period. Such investigations often involve alleged serious breaches of the SRA Handbook and thus, these firms already represented a higher risk.

12. This equates to just over 2% of our total regulated community

The sample firms comprised:

- 128 firms within our Regulatory Management (RM) portfolio at the time of the review period. This engagement was carried out by our Regulatory Managers.
- 124 firms which were subject to a Forensic Investigation during the review period. This engagement was carried out by our Investigation Officers.

The firms visited varied in size and structure from sole practitioners to City and international firms. A breakdown of the types of firms we visited is shown on the next page.

These firms provide a wide range of legal services. Some were involved in high-risk services and transactions on a frequent basis, whereas others only occasionally did work in which there was a risk of money laundering. It should be noted that the MLR do not apply to all legal services which may be conducted by law firms.[13]

Under the Proceeds of Crime Act 2002 (PoCA) the primary money laundering and terrorism financing offences apply to everyone. However, different reporting obligations apply depending upon whether the activity is regulated under the MLR or not. Since the case of Bowman v Fels,[14] we have noted that some firms have assumed that litigation, in particular personal injury work, is exempt from AML compliance. During our visits, firms were made aware that they were still at risk of committing money laundering offences under PoCA if, for example, they become involved in facilitating sham litigation such as staged road accident claims or dealing with bogus clients.

The scope of the review was to:

- gain a good understanding of the policies, procedures and controls put in place by firms to identify and prevent potential money laundering
- evaluate the level of knowledge, training and awareness in relation to AML compliance.

Our visits were designed to involve constructive engagement with the firms and to provide them with examples of best practice where appropriate that might improve their systems and controls.

We did not specifically review client files, or attempt to proactively uncover incidents of money laundering or breaches of MLR or PoCA. We did, however, reserve the right to investigate any conduct issues that came to light during the evaluation, including those related to money laundering.

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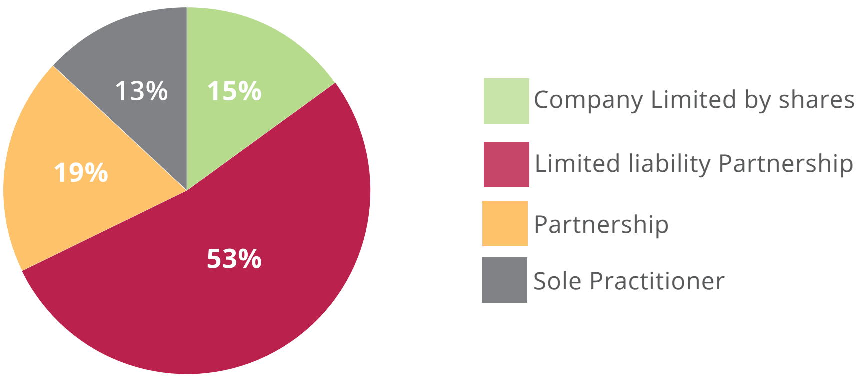
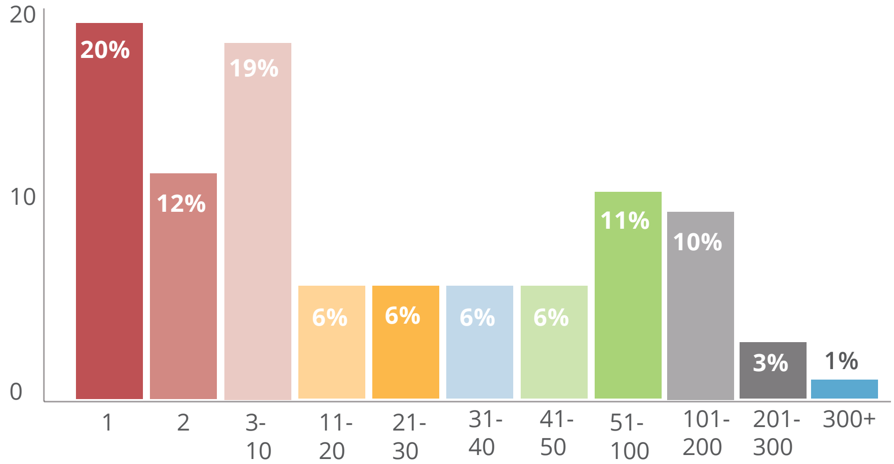
13. Only that which falls within the definition in MLR regulation 3
14. [2005] EWCA Civ 2006

A breakdown of the types of firms visited

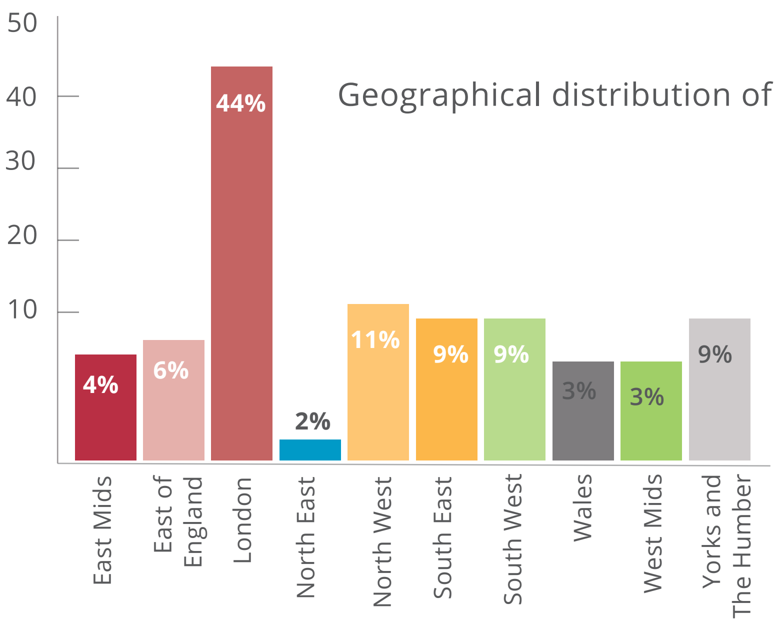
Composition of sample firms by structure



Composition of sample firms by no. of partners (or equivalent)



Geographical distribution of sample firms



Summary of our findings

All firms visited had a designated MLRO.

We found that most of firms we visited had effective AML compliance frameworks in place.

AML policies and procedures are only one element of an AML framework and their effectiveness is dependent on having a healthy compliance culture embedded within a firm. In general, we found that firms and their staff displayed a positive attitude towards AML compliance and were trying hard to meet all of their duties and obligations under MLR and PoCA.

We found there was an adequate application of Client Due Diligence (CDD). As we expected, each firms' processes and procedures in relation to CDD varied according to:

- the size of the firm
- types of legal services offered
- available resources.

Most large firms had dedicated client inception teams which undertook a large part of the CDD activity. By contrast, in smaller firms, the individual fee earner was responsible for carrying out due diligence on each of their clients.

All but a few firms that we visited had good controls in place to restrict work being conducted on a client matter prior to CDD being completed in accordance with the MLR.

Most firms had a good understanding of their recording and reporting obligations under both PoCA and the MLR.

Almost all of firms had suitable processes and procedures in place to enable staff to report suspicions of money laundering.

We did however find weaknesses in some areas. These are highlighted on page 11.

Action taken and next steps

As a result of our thematic review, our general conclusion was that whilst the legal sector is viewed as a high risk for being used by criminals for money laundering, the profession itself and the way it manages AML compliance is mitigating this risk.

The very fact of our proposed engagement with firms, particularly those within RM, often prompted a review and updating of policies. It also led to a refresh and more thorough roll out of training in advance of our visit. This moved the AML issue up the risk agenda of many firms.

In many instances, at the outset of our meetings, we met with the managing partners of firms in addition to MLROs, Compliance Officer Legal Practice (COLPs) and Compliance Officer for Finance and Administration (COFAs). This ensured that our interest in the firm's work in relation to AML and the drivers behind our thematic engagement were explained and discussed with representatives of senior management.

As part of the structured AML engagement by RM, we provided the firms we visited with examples of best practice, where necessary, to enable them to improve their AML processes and procedures. Often this feedback session was attended by managing partners (in addition to the MLRO, COLP or other risk personnel) who were instrumental in demonstrating a firm's commitment to minimising the risk of money laundering.

As part of their ongoing engagement with firms, the RM team will, where appropriate, continue to share best practice.

In a limited number of instances we are actively investigating evidence of potential money laundering in firms.

We have shared, anonymously, a number of our findings and conversations with firms with law enforcement agencies and the NCA, particularly with regard to some challenges in relation to firms making SARs.

We are aware that some aspects of the MLR prove more challenging for smaller firms, for example, MLRO succession planning or providing relevant training for staff. However, both of these are mandatory under the MLR. Despite these challenges, we have seen many instances of good practice among small firms. We encourage firms with limited resources to participate in peer groups where information on AML issues and best practice can be obtained, and to access the online resources available to the profession. We will continue to support small firms via the Small Firms Portal.

Ultimately, AML compliance should be appropriate to a firm's needs and based upon a thorough assessment of the risks presented by, but not necessarily limited to:

- individual clients
- the type of legal services offered
- the method of service delivery (eg where the client is not met face to face)
- jurisdiction risk.

Different clients, legal services, delivery methods and jurisdictions (and combinations of these factors) pose varying levels of risk. These should be identified and managed in a firm's policies and in the implementation of appropriate controls. The higher the level of risk, the greater the rigour needed in CDD, ongoing monitoring and control to mitigate any risk.

A risk-based approach enables firms to have flexibility in choosing the areas to concentrate their resources and how best to apply AML controls. There is no reason why AML procedures such as CDD should not be cost effective, and we saw many good examples of this on our visits.

We are committed to working with firms in this area and in preparation for the FATF MER. We hope that solicitors and firms will use this report as a spur and guide to continue to improve their AML processes and procedures.

Weaknesses found in some areas

- We identified that the responsibilities, visibility of, and support provided to, the MLRO varied amongst the firms. Many of the smaller firms, and also a number of the larger firms, did not have a deputy MLRO or a contingency plan in place to provide cover in the MLRO's absence.
- Most MLROs displayed a good understanding of AML, despite not having any formal qualification. However, we did find that, in several cases, an inexperienced or inadequately trained MLRO had a detrimental effect on the overall adequacy of their firm's AML compliance.
- We identified some weaknesses in relation to the low frequency with which firms reviewed their AML policies in order to ensure that they were up to date, relevant and fit for purpose.
- Additionally, a number of firms had either no or inadequate processes in place to test and measure the effectiveness of their systems and controls.
- In some firms, there was a lack of understanding and weaknesses in applying enhanced due diligence, identifying and dealing with Politically Exposed Persons (PEPs) establishing source of funds and source of wealth, ongoing monitoring and the requirements under the sanctions regime.
- Most firms we visited treated AML training as a priority and this training was usually mandatory with staff attendance monitored, recorded and action taken if not completed. However, in some instances the MLRO did not have sight of the level of attendance at AML training or the identity of non-attendees as this was managed by the HR or training function. We also identified a general lack of appropriate training for finance staff who are also a key line of defence in mitigating the risk of money laundering.

Money Laundering Reporting Officer

Regulatory and Legislative Framework

- Solicitors' firms that conduct work under the MLR (in the regulated sector) are required to have a 'nominated officer' to receive and make disclosures to the National Crime Agency (NCA).[15]
- Nominated officers are commonly referred to as The Money Laundering Reporting Officer (MLRO).
- The MLRO is central to a firm's AML risk control framework.

The extensive role and responsibilities of an MLRO, when carried out effectively, will assist firms in maintaining compliance with statutory and regulatory AML obligation and minimise participation in the laundering of the proceeds of crime.

MLRO key responsibilities

- Implement AML compliance policies, procedures and controls
- Monitor and assess the effectiveness of a firm's AML policies, procedures and controls
- Receive and evaluate internal SARs
- Maintain a confidential register of internal SARs including complete and thorough records of all enquiries made and document decision-making / the rationale and the method of closure (i.e. disclosure made to the NCA or no further action required)
- Make external SARs to NCA, as necessary
- Maintain a confidential register of external SARs to NCA
- Advise solicitors and staff of their obligations pending the outcome of consent SARs and following receipt of the outcome of consent SARs
- Act as a main point of contact for law enforcement agencies when dealing with formal and informal requests for information
- Ensure all staff are appropriately trained in AML and maintain staff awareness
- Keep fully up to date with developments in AML, for example, changes in legislation, current fraud typologies and emerging risks.

15. Regulation 20 (2)(d) MLR; Part 3 TA; Part 7 PoCA

Key findings from visits

Each firm we visited had AML policies and processes in place which included the appointment of an MLRO. We identified however that the role, responsibilities, visibility of and support provided to the MLRO varied amongst firms.

The majority of MLROs combined their role with other posts held at their firm, in particular that of COLP or COFA and in some cases both. This is not necessarily a problem in principle, but might become a potential issue if the MLRO is overburdened. If the MLRO is carrying out several roles, he or she might be unable to give sufficient time and consideration to AML duties, which carry a heavy personal liability.

Additionally, there were MLROs who held other posts which could present a conflict of interest, such as heads of business divisions in which there was a higher risk of money laundering. This may adversely impact their ability to carry out AML duties effectively and impartially. Several firms mentioned that they actively minimised this risk by appointing an MLRO who was independent of their transactional property work, which was acknowledged as their highest risk for money laundering.

The MLRO acts as the single point of contact for all AML related activity within a firm. A single point of contact however is also arguably a single point of weakness.

We found that a number of firms had not appointed deputy MLROs. This is a particular risk. The NCA has cited significant challenges in relation to MLROs at law firms, including inaccurate or out of date contact details, the unavailability of MLROs during working hours and no alternative point of contact when the MLRO is on leave or otherwise unavailable during the consent SAR notice period. It is essential that there is always an individual available at firms to carry out the MLRO functions. In particular, firms should consider how they could mitigate the risks posed by the sudden and/or prolonged absence of a sole MLRO.

Some firms had appointed deputy MLROs. Such firms and MLROs believed that a deputy provided useful support, oversight and cover. Deputy MLROs were also considered to be an opportunity to develop and train potential future MLROs.

We also visited some firms, who had deputy MLROs in place, but with low visibility in the firm. Some fee earning staff stated to us that they were not aware of the post of deputy MLRO or who they should contact in the MLRO's absence or unavailability.

Most MLROs displayed a good understanding of AML matters. We found that in several cases, a weak MLRO with little or no previous AML experience or training had a detrimental effect on the overall adequacy of their firm's AML policies, systems and controls.

Unsurprisingly, we often found that firms which had more robust processes and procedures and compliance monitoring in place were those in which the MLROs had AML training and attended relevant professional development courses. These MLROs generally also had a genuine practical interest in AML compliance, and were strong supporters of what the legislation and regulatory requirements were aiming to achieve.

Good practice

At one large firm which conducted more than 90% property work, the MLRO was a senior manager without the responsibility of managing a client base in order to have the time capacity to deal with AML issues. The MLRO spent approximately five hours per week on AML matters and had attended numerous courses (at least biannually) run by The Law Society and other external training providers. The firm regularly measured the effectiveness of its controls and AML issues were reported at monthly management meetings where AML was a standing item on the agenda.

At one smaller firm, the MLRO was a senior equity partner who attended training courses on a regular basis throughout the year and regarded their MLRO duties as an, “essential part of good business management”. It was for this reason that the MLRO stated he was not a fee earner so as to ensure, “that good practice and procedure is fully embedded across the firm”.

At one large city firm we identified that improvements had been made by appointing a deputy MLRO to assist the MLRO. Closer monitoring was put in place to ensure that the MLRO was not overburdened or compromised between fee earning and MLRO duties. Generally the firm had good systems and controls in place.

Poor practice

We visited a sole practitioner’s firm which had three fee earners and conducted residential conveyancing work. The sole practitioner, who was also the MLRO, had no previous AML experience and was not a member of any AML network or professional forum. The firm had AML policies in place, but we identified weaknesses in the firm’s implementation and controls in relation to

- recording CDD
- continuing to act in a transaction before full CDD had been carried out
- insufficient CDD checks on companies.

The MLRO had provided staff with basic AML training, but their understanding of the content was not tested by the MLRO.

There were also some concerns in relation to MLROs who lacked regular, specific training and were also generally not members of any professional groups or forums where AML issues could be considered. Such networks are a good source of support for MLROs, in particular for sole practitioners, and are a cost-effective way of keeping up to date and sharing best practice.

Inevitably, we found that MRLOs' AML knowledge and understanding varied. Key areas where some MLROs needed to improve their knowledge were as follows:

- The threshold for reporting
- Understanding the difference between 'source of funds' and 'source of wealth' and the extent to which enquiries ought to be carried out to verify each
- Appropriate levels of CDD
- The scope of the sanctions regime
- The need for, and extent of, ongoing monitoring.

✓ Good practice	✗ Poor practice
• The MLRO is independent, of sufficient seniority to influence management and access relevant information, able to devote sufficient time to the role and has a deputy MLRO to assist. • The MLRO is visible, approachable and resilient. • The MLRO is an AML expert and can provide clear advice and training. • The role and responsibilities of the MLRO and Deputy MLRO (and any other AML support staff) were recognised in performance appraisals.	• The MLRO lacks credibility and authority due to inexperience, insufficient knowledge or lack of seniority or respect within the firm. • The MLRO does not have the relevant autonomy and is not given any practical or senior management support. • The MLRO does not keep their technical AML knowledge up to date. • There is no Deputy MLRO or contingency plan in place to provide cover in the MLRO's absence.

Policies

Regulatory and Legislative Framework

Firms that conduct work in the regulated sector must establish and maintain appropriate and risk sensitive AML policies and procedures in relation to the following areas:[16]

- Customer due diligence measures and ongoing monitoring
- Reporting
- Record keeping
- Internal control
- Risk assessment and management
- Monitoring and management of compliance with, and the internal communication of, such policies and procedures.

AML systems and controls should be proportionate to risk, and do not need to be expensive.

Key findings

A positive consequence of our thematic review was that it prompted several firms to review and where necessary, update their policies in advance of our visit.

We found firms differed in their views about what constituted 'high-risk' work. The definition of high-risk work will depend to some extent on each firm's particular circumstances. Firms who carry out a high percentage of transactional or property work should consider the risk of their workload overall, even if they do not act for international, high net-worth clients or PEPs.

A number of larger firms had produced specific guidance for a wide range of areas of work, including conveyancing, corporate work and litigation. This guidance identified the particular AML issues and risks that were practice area specific and so better-equipped fee-earners to spot potential issues in their practice area.

Some international firms created policies for different jurisdictions to reflect the circumstances and risks of each jurisdiction. Others developed a universal AML policy based on the highest available requirements (often described as a 'gold standard') that they implemented across all of their offices irrespective of whether the local requirements were less demanding.

16. Regulation 20 MLR 2007

We found a small number of firms provided their client account details on their website or in their initial client care letter. This practice raises a number of risks. It increases the opportunity for money to be transferred prior to the completion of CDD. In addition, it could be used by criminals as a mechanism to launder money by sending money to a firm and then reclaiming the funds on the purported basis that the transfer had occurred in error, thus creating a veneer of legitimacy for those funds, which could now be shown to have come from a regulated professional.

Most firms had appropriate policies in place and also reviewed their policies annually. A small number reviewed policies more frequently, every six months. Some firms stated that they would review on an ad hoc basis or when events occurred which prompted a review, for example after submitting a SAR. During our visits, we found a few firms still referred to the Serious Organised Crime Agency (SOCA) rather than the NCA, which replaced SOCA in 2013. This suggested a failure to review and amend policies regularly, and raised questions about their use and effectiveness and the firm's commitment to AML generally.

We identified that some firms did not have any formal processes in place to test and measure the effectiveness of their AML policies and procedures. Several MLROs stated that the fact that their firm had not had any money laundering or terrorist finance issues was sufficient evidence to show that the firm's procedures were understood and being positively applied by staff. Equally, this could be that policies and staff understanding was inadequate to identify even common concerns or suspicious activity. Some firms had quality assurance processes and were actively testing their systems, notably CDD procedures. We consider a failure to do this as a risk and firms should ensure that they maintain, review and test the effectiveness of their policies and procedures on a regular basis.

The policies and procedures also need to be supported by senior management. This was the case in the majority of firms we visited. Having the policies agreed and endorsed by senior management is important, but there also needs to be a commitment to ensure that they are followed. Those firms that managed the risks well also ensured that staff were aware of potential disciplinary consequences if they failed to follow the firm's policies, in addition to any criminal or regulatory consequences.

Good practice

At one small firm we visited we observed that the AML policies were reviewed by the MLRO every six months. The effectiveness of the policies and procedures were also monitored every time a concern was raised by a fee earner about transactions they were working on. The MLRO cascaded a firm wide email on AML updates including any changes made to policies and procedures.

One large firm had comprehensive AML policies. Each policy was clear and well written. The policies were designed specifically for each local audience and contained both references to the law but also featured summaries of the key risks to fee earners and partners. The policies were available in an electronic format, clearly indexed and regularly reviewed. These were produced by the MLRO, the AML Committee and ultimately signed off by the Professional Practice and Risk Committee. The firm did not rely on mechanistic processes. The mitigation of risk involved both qualitative and quantitative measures. The firm had a mature system of controls in place. The system and policies were interconnected with no reliance on a single control or person.

Poor practice

One large firm we visited, that had undergone a merger, had not updated its AML systems and processes to ensure that consistent policies, systems and processes were being applied across the merged firm.

✓ Good practice	✗ Poor practice
• Policies are up to date, easily accessible, user friendly and easily understood by a wide audience. • Systems and processes are subject to regular quality assurance and independent testing and review to ensure they remain up to date and are effective (for example, dip sampling and exception reporting). • Policies ensure consistency in the reporting of concerns to the MLRO. • Regular and flexible approach to the review of policies to ensure they remain relevant, valid and effective. For example, reflect any changes to legislation or regulations, firm structure changes, changes in type of legal services offered, following the filing of a SAR to the NCA and emerging risks. • Senior management sets the right tone by demonstrating their own AML compliance to the rest of the firm and clearly communicating and enforcing the firm's commitment to minimising money laundering.	• Policies and procedures are out of date, inaccurate or generic. • Over reliance on external parties to design and implement policies and procedures with minimal input from the MLRO. • The firm does not conduct adequate risk assessments of their work in order to tailor appropriate and effective policies, systems and controls. • A mechanistic approach to compliance resulting in a poor firm culture of compliance. • Disinterest from senior management and poor role modelling.

Client Due Diligence

Regulatory and Legislative Framework

- Firms undertaking work in the regulated sector must establish and maintain appropriate and risk-sensitive policies and procedures relating to CDD measures.[17]
- Generally, a firm must apply CDD on a risk sensitive basis when they establish a "business relationship" with a client, carry out an occasional transaction, suspect money laundering or terrorist financing, or doubt the veracity of identification documents previously supplied.[18]
- Firms must apply Enhanced Due Diligence (EDD) and ongoing monitoring in all matters that present a higher risk of money laundering or terrorist financing, where the client has not been physically present for identification purposes or the client is a PEP.[19]

Key findings

The firms we visited were generally aware of the importance of CDD and many applied their CDD procedures across both regulated and unregulated work.[20] One benefit of this was that it mitigated the risk of unregulated work developing into regulated work without appropriate CDD and other enquires being undertaken. It also gave firms confidence regarding their entire client and transaction base.

It is important to highlight that individual experience, number of years in practice, size of firm, demographics of clients and a good reputation will not in themselves deter criminals from trying to launder money through a law firm.

Many firms have adopted a centralised client take on process and sometimes separate departments. Such processes can be efficient and promote consistency. However, there is a risk that fee earners may become detached from the CDD process and lack a detailed knowledge of their client and the transaction. This in turn may have an impact on the ability of the firm to conduct ongoing monitoring appropriately.

We encountered some conflicting views about what constitutes a business relationship. Many firms did not conduct any work prior to completion of CDD and larger firms often had automated systems designed to minimise the risk of fee earners working where CDD was not satisfactorily completed.[21] CDD should be completed before work is started for a client.[22]

17. Regulation 7 MLR 2007
18. Regulation 7(1)(a) MLR 2007
19. Regulation 14 MLR 2007
20. Regulation 3 specifies when the MLR applies. It applies to "independent legal professionals" who participate in financial or real property transactions (- Regulation 3 (9) MLR 2007) and also to tax advisers, insolvency practitioners, trust or company service providers and estate agents. All of which may be business activities conducted by firms.
21. Regulation 11 MLR 2007 sets out the requirement to cease a transaction where CDD is not completed
22. Regulation 9(2) MLR

However, the MLR permit CDD to be completed during the establishment of a business relationship in some circumstances but not if the work is an occasional transaction. Even so, it is permitted only if the specified conditions are met.[23] Therefore, firms should take care to ensure that they understand how these provisions work, what is permitted and that they are compliant.

However, some firms permitted fee earners to work up to 14 days before completion of CDD.[24] We recognise that in transactions where speed is important, it may be necessary to conduct some preliminary work that is not of a business nature, so as not to interrupt the normal course of business, as permitted by the MLRs if the other conditions are met. This could include things like preparing documentation. It is not appropriate, however, to take any money from the client, progress the transaction or bill the client for any services rendered, prior to the completion of CDD. Clients should be informed of any limitations that prevent the firm from working prior to the completion of CDD. In all cases, CDD should be completed as soon as practical. If CDD cannot be completed, work must cease except in the limited circumstances provided in the MLRs.[25]

Often where a matter file was opened pending completion of CDD, within the finance function a block or flag appeared on its system to ensure that no funds were processed on that matter until CDD was completed. However, in at least one instance we identified the absence of any such restrictions in the finance system exposing the firm to the risk of processing funds before successful completion of CDD.

Some MLROs and their firms had a lack of knowledge and understanding of when and how to establish a client's source of funds and source of wealth, with some firms failing to distinguish between the two. This is a concern given that this is a requirement under the MLRs in respect of PEPs and best practice for all other high risk clients or matters. We identified that in most cases fee earners were making enquiries of clients in respect of their source of funds and source of wealth. However, the client's response was often taken at face value with no request for any supporting documentation or corroborating information. This is of relevance to small firms as the definition of a PEP is broad (and will be wider following implementation of the 4th Money Laundering Directive) and will trigger these requirements.

On a number of our visits we noted that some firms were charging their clients the cost of undertaking CDD. In relation to regulated activity and in accordance with the MLRs, law firms are legally required to undertake CDD. It is our view that the cost of undertaking CDD cannot therefore be treated as a disbursement, since it is not a cost incurred on behalf of the client. Firms will be at risk under Outcome (8.1) if CDD payments are described in their bills to clients as disbursements. As a general rule, we would expect such charges to form part of a firm's overheads. There may on occasion be circumstances in which the cost of the CDD is particularly high (for example, when you have to carry out an overseas company search) and firms may wish to seek agreement with their client that the cost will be payable by the client.

23. Regulation 9 MLR deals with the timing of verification of identity.
24. In one case a firm allowed up to a month for the completion of CDD.
25. Regulation 11(2) MLR

In order to comply with Outcomes (1.12) and (1.13) firms should explain the likely cost with their client and obtain their client's informed consent at the outset of the retainer. If the client agrees to meet the cost of the CDD then firms should record it in their bill as part of profit costs. Some firms undertake CDD for all clients as a matter of course, irrespective of the nature of the retainer and whether it is a requirement of the MLRs. Whilst there may be good reasons for doing this, it is questionable as to whether there would ever be justification for passing the cost on to the client where such checks are not a requirement, even if the client agrees.

There are clients for whom firms should not act regardless of the level of risk that is assessed and applied. These clients are those subject to sanctions. The sanctions regime is absolute and stands outside any risk based approach. HM Treasury issues a consolidated list[26] of all individuals and entities that are subject to sanctions effective in the UK. Firms can only act for a client who is on the list with a licence from the HM Treasury Asset Freezing Unit.

During our visits we identified that some MLROs had a lack of knowledge and understanding of the sanctions regime and the requirements for sanctions screening both at the outset of engaging with a client and throughout the course of a retainer. When we asked the MLROs working in smaller firms whether their firm checks clients against the relevant sanctions lists, just over a third stated that they screened clients and of these most applied a risk based approach. In contrast the larger City firms evidenced a far better understanding of the sanctions regime and had often implemented automatic and ongoing sanction screening processes.

Several MLROs held the view that it was not necessary to screen locally based clients or that they simply did not deal with clients from high risk overseas jurisdictions. We drew these firms' attention to the fact that there are UK nationals and UK residents on the consolidated list.

Similarly, MLROs in firms which conducted predominantly non-regulated work for the purpose of MLR, for example personal injury work, believed wrongly that the sanctions regime did not apply to them. The regime applies to all payments received and made by a firm regardless of the nature of the transaction and there is no de minimis financial limit. For example, settlement payments for damages, legal aid payments, payments to beneficiaries of a will or payment of proceeds from a property transaction to a third party could fall within the regime. If these are paid to persons on the sanctions list, and the firm does not have a licence to act, it will be an offence.

Firms must conduct ongoing monitoring on a risk sensitive basis throughout the life cycle of a client matter. Ongoing monitoring means scrutinising transactions to ensure that they are consistent with:

- the firm's knowledge of their client
- the expected nature of the retainer
- the appropriate risk assessment remaining valid.

26. Financial-sanctions-consolidated-list-of-targets Gov uk publication

Inevitably, practices varied across firms. Some firms left the obligation for ongoing monitoring to the discretion of the matter partner. Other firms had automated processes requiring the lawyer responsible for a relevant matter to review it and report formally on a three or six monthly basis.

Similarly, where firms had identified high risk matters or clients there was a difference in how firms communicated that conclusion to fee earners. Sometimes it was reported only to the matter partner but it was rarely formally communicated to other team members who might in some instances be better placed to spot potential money laundering concerns during a transaction.

We identified that most firms had a time limit on the validity of CDD, and conducted checks again after a defined period or when taking a new instruction. There were a few firms, however, that did not conduct any ongoing monitoring. Some criminal organisations may target existing clients of firms to launder money on their behalf and a person may undertake both legitimate and non-legitimate transactions at the same firm. The requirements of ongoing monitoring can mitigate this risk.

Poor practice
At one large firm we identified that CDD recording was inconsistent amongst departments. The firm had a good standard template CDD form which could be made compulsory across the firm. We identified that the department with highest risk, residential conveyancing, did not use the form at all.
At one large firm, it was the partner's responsibility for ensuring CDD evidence had been obtained. However, there were no checks made to ensure that fee earners had obtained the appropriate CDD. The fee earners could open a file number before all CDD was in place, and therefore it was possible to work on the file with no limitations. The MLRO only reviewed the list of files where CDD was not in place on a quarterly basis. There was no system of file audits. Partners were not appraised on their attitudes to compliance.
In one city firm, CDD checks were only carried out in respect of new clients and there was no internal expiration date on the proof of identify obtained. Set expiration dates should be given to proof of identity used for repeat clients where that proof is held on file. The firm were over reliant on their reputation to protect them from approaches from clients who may want to use the firm to launder money.

Good practice

At one small firm, the CDD requirements were set out in the firm's manual and related to the level of risk of the matter as identified through the firm's risk matrix spreadsheet. The risk score determined the level of CDD to be applied to an individual client. The firm did not solely rely upon an electronic CDD check. Fee earners were also encouraged to review the risk score throughout the duration of the transaction.

One large firm we visited had a procedure that if a client was dormant for two years, when they returned to instruct the firm, they were treated as a new client. High risk clients were subject to renewed CDD on every new or change of instruction. A monthly review and mid transaction review of high risk clients and matters was carried out. The firm would not "grandfather in" any clients if they came with lateral hires or from other firms.

One large firm had procedures in place requiring that all prospective new clients had to be authorised by a partner and subject to CDD. UK requirements were applied worldwide subject to local additional requirements with the exception of the US. Each international office had its own MLRO. All high/medium risk matters were flagged and batch screened against a compliance database. A six monthly review was automatically run by the central team and if there were any ownership changes, for example, the central team would contact the fee earner.

At one large firm that we visited if a high risk client was approved and taken on, it would be flagged on the system that they were only approved for that one matter. The firm regularly interrogated the system and carried out bulk matter closures. They looked for periods of inactivity and closed matters down. The firm had a general policy not to act as escrow agents.

✓ Good practice	✗ Poor practice
• A centralised, accessible and user-friendly database for CDD. • Systems in place to bar matter progression, time recording and receipt of monies until CDD has been completed appropriately. • A coordinated and active engagement between fee earning and finance staff to prevent monies being received on client account prior to CDD being completed • Policies to escalate concerns to management, to cease relationships where appropriate, and to recognise and value CDD activity. • Appropriate procedures to enable effective ongoing monitoring of business relationships to be conducted and for concerns to be escalated. • Terminate the client relationship when an action of a client exceeds the firm's risk appetite or is subject to sanctions. • Staff performance and appraisal processes that recognise and rewards effective CDD activity.	• A superficial and mechanistic tick box approach to CDD. • A tendency to view CDD as a one-off exercise, and consequent failure to keep it up to date. • A failure to ensure that CDD is completed before the commencement of a 'business relationship', an occasional transaction is carried out and/or receipt of money on account. • An ineffective or hands-off MLRO who fails to assess and authorise high-risk clients. • A failure to distinguish between clients' source of funds and clients' source of wealth or obtain verifying evidence. • A failure to properly assess clients' risk, PEP(s) status or check the sanctions list. • Detachment of fee earners from the process that affects ability to adequately conduct ongoing monitoring.

Training and Awareness

Regulatory and Legislative Framework

- Firms undertaking work in the regulated sector must ensure that all relevant employees receive appropriate training. Employees must be aware of the law relating to money laundering and terrorist financing. They must also be given regular training on how to recognise and deal with transactions and other activities that may be related to money laundering or terrorist financing.[27]
- The upcoming EU 4th Directive stresses the importance of training. Both MLROs and other staff will need to be updated on the legislative changes including those relating to risk assessment and beneficial owner registers.

Key findings

We found that most firms had provided appropriate and relevant training to staff. Another positive consequence of our thematic review was that it prompted a number of firms to undertake refresher AML training of their staff in advance of our visit.

Training methods and materials varied from firm to firm and included one or more of face-to-face training, e learning, case studies and department or practice area specific training. Some employees commented that where possible, having both face-to-face and online training was valuable as different people had different learning styles.

We noted that the frequency of training varied between firms. Firms should regularly review their AML training requirements and take account of developing experience, changes in firms' work mix or changes in circumstances. For example, following mergers, we noted that some firms had failed to refresh and review the new firm's AML training. Consequently, staff had varying degrees of knowledge and understanding about the new firm's policies and procedures.

During visits, we inspected training records. Training records allow firms to review and determine who requires training and potential areas for future training. It is important that firms take steps to ensure all staff receive training and non-attendees are offered alternative training.

During our visits to larger firms, we also met with finance staff and employees. Most staff were satisfied with the level and frequency of training and demonstrated a good understanding of their firm's AML policies and procedures. We did note, however, that generic training might not be appropriate to enable finance staff to spot warning signs of money laundering in a finance context.

27. Regulation 21 MLR 2007

Good practice

At one large firm we visited, the MLROs delivered ad hoc sessions and department by department training on an annual basis. There was also an annual risk lecture which was well attended and combined a number of compliance issues including AML. The MLRO relied on a variety of different methods to ensure that staff were aware of AML issues via bulletins, lectures and e learning. Members of the compliance team took the International Compliance Association's qualification which included AML and a range of other topics. This was funded by the firm. Compliance/risk management was part of expected fee earner competency. The compliance team reported to the risk committee every quarter on its observations. A relationship of trust existed between the MLRO/compliance team and the fee earner community. The MLROs had also drafted very good, practice-specific scenarios highlighting AML risks

At one small firm, which undertook mostly foreign property and immigration work, we observed that the managers had organised specialist training for staff by the police in relation to false passports and other red flags in relation to money laundering.

Poor practice

In one large firm we identified that training records indicated that some staff had not undertaken AML training since 2008. This included staff within a high risk commercial sector. Staff interviewed also confirmed they could not recall when they had last undertaken AML training.

One large firm stated that they provide both online and face to face training at regular intervals. The firm's training records however suggested that a number of individuals had not received training for some time; in particular several partners and associates who undertook transactional work had not received AML training for up to seven years.

✓ Good practice	✗ Poor practice
• The MLRO delivers bespoke training including practical and practice specific examples and case studies. • AML training is mandatory, monitored, recorded and reviewed with mop-up training sessions being provided. • AML training is repeated on a regular cycle for staff. • AML training attendance and compliance is referred to in staff KPIs and appraisals. • The MLRO maintains awareness of issues through regular staff updates through a range of information streams.	• Training is not appropriate to the staff involved. • Training is not mandatory and the firm keeps no or inadequate training records. • The firm does not carry out testing to ensure that training is understood.

Reporting

Regulatory and Legislative Framework

- If you undertake regulated work, you must disclose any suspicions of money laundering.[28] Suspicions should be reported initially to the MLRO who will then decide whether a SAR is required to be made to the NCA.
- If you work in the unregulated sector, although the disclosure regime is different, you will also need to consider whether they are required to make a disclosure.[29]
- You are also required to make disclosures to the NCA of suspected terrorist financing,[30] regardless of whether you work in the regulated or unregulated sector.
- If you suspect that a transaction may involve money laundering or terrorist financing, you must apply to the NCA for consent to proceed with the transaction. This is called a "consent SAR" and requires the regulated person to provide information about the transaction and those involved.

Key findings

In general, we found that the firms we visited complied with the reporting requirements. Firms had procedures in place to enable staff to report suspicious transactions, and MLROs ensured that staff had the knowledge to make reports to them and did so. Most of the firms we visited had designed and implemented internal suspicious activity reporting template forms. The MLROs tended to occupy senior positions within the firms and were visible and known to staff. Feedback from staff emphasised that it was important that the MLRO was both authoritative and above all accessible and approachable to staff at all levels.

It was also important that staff understood how to deal with client enquiries once a report had been made and ensure that procedures were in place to prevent 'tipping off'.[31]

28. ss.330-332 PoCA 2002
29. s.337-339 PoCA 2002
30. ss.19-20 TA 2000
31. s.333A PoCA 2002

Good practice

One large firm had clear reporting lines in place. It was clear from the interviews that each individual knew the identity of the MLRO/deputy and the relevant procedure on how to report an issue. The MLRO was considered to be very approachable. One of the interviewees commented that the firm welcomed an inquisitorial and cautious approach to understanding clients and instructions and there was never any pressure to take short cuts on AML to achieve a commercial result. The finance staff commented that AML processes were not an add-on, “its part of our everyday role to do it”. The MLRO and the deputies moved around the offices and were regularly approached to discuss matters.

Poor practice

At one large firm, the MLRO stated that queries regarding AML issues were infrequent. This may reflect the fact that the partners would raise issues with the MLRO, the fee earners, however, were more likely to speak to the compliance manager. When we spoke to the fee earners and asked who they would approach if they had any AML concerns, they said that they would speak to their supervising partner and then the head of department.

Suspicious Activity Reports

It is the legal responsibility of law firms to submit SARs to the NCA in accordance with legislation contained within PoCA.

The NCA publishes figures in its SARs Annual Report each October. In its report for 2014, it identified that SARs submitted by law firms had reduced that year by 8% (from 3,615 in 2012/13 to 3,328 in 2013/14), against a backdrop of SARs increasing nationally. SARs submitted by law firms now represent less than 1% of all SARs nationally, and equate to only 0.3 SARs per firm, per year.

The 2013/14 figures are not an exception, as SARs submitted by law firms have reduced year-on-year from 6,460 in 2007/08 to 3,328 in 2013/14. Although the reduction is not exclusive to the legal sector,[32] the reduction in the number of SARs submitted by law firms is a concern.

During our visits we asked MLROs whether they were aware that SARs in law firms have been decreasing and what they considered might be the reasons for the decline. The responses are summarised as follows:

- General settling down in the AML environment since the MLRs were introduced in 2007, which has resulted in a better understanding in law firms of what is required under the SARs regime and a move away from reporting simply as a precaution.
- An overall reduction in transactional work post the financial crisis of 2008/9 has meant fewer SARs, particularly in relation to property transactions, a high-risk money laundering area of work.
- Firms increasingly refusing to act in particular matters in which there is a suspicion of money laundering or where clients or transactions are assessed as 'high risk' at the outset. This may have led to a reduction in consent SARs.
- A better understanding of the application of legal professional privilege (LPP).
- A better understanding of MLRs and PoCA.

A significant number of firms stated that in their view SARs had reduced because when the MLR were first implemented, law firms had been over-reporting in a defensive or precautionary manner. These firms stated that in time they had learned from experience which matters to report to the NCA and which were not appropriate to report. Some firms, on the other hand, stated that they were still submitting a similar number of SARs compared to those they were making when the regulations were introduced.

Some firms stated that they were more confident in assessing risk, identifying red flags and were refusing to act (or continue to act) for clients in matters in which there is a suspicion of money laundering or evidence of high risk. This may to some extent explain a reduction in consent SARs.

Several MLROs stated that the number of SARs had reduced due to improved controls when clients first came to the firm. MLROs should, however, consider submitting an intelligence SAR where the firm has refused to act. Refusing to act is effective in disrupting crime, but it could also displace criminal activity and criminals may seek to target another law firm.

32. For example, accountants' SARs have reduced from 7,354 in the period 2007/08 to 4,834 in the period 2013/14

Good practice

One firm had a clear and standardised process for dealing with and recording AML enquiries and reports regarding suspicions of money laundering. The firm ensures that staff file internal reports separately to client files, and keep a central database of money laundering reports. These include a complete internal record of each report, even if they do not ultimately lead to a SAR being made. This firm also provides fee earners with an anonymised annual overview of reports made to the NCA, to illustrate what they need to look out for.

Poor practice

One firm we visited had an inconsistent approach to reporting. Some reports and enquiries were routed to the MLRO, some to the internal risk team. Both keep separate records. Like its other policies, the firm's reporting policy was not kept updated. This approach meant that staff did not know how to make a report and may not have complied with their legal obligations. Staff did not feel that their suspicions would be taken seriously, and were under pressure to retain valuable clients. As a result, suspicious transactions were not appropriately considered, recorded or reported to the NCA. The MLRO will not be able to justify his internal AML decisions, if criminal or regulatory allegations arise.

If appropriate evidence is available to support a suspicion then an intelligence SAR should be submitted to the NCA in accordance with PoCA and in order to assist law enforcement agencies with intelligence analysis, trends and tracking criminal activity.

Several firms commented that the profession now has a better understanding of LPP and the privileged circumstances defence under PoCA S.330 and this may have impacted on the level of SAR reporting. We also identified a lack of understanding when speaking to MLROs at a small number of firms around the appropriate use of the crime/fraud exception.

Some firms stated they had not experienced a decline in their own submission of SARs and some had in fact seen an increase in their reporting. Other firms mentioned very specific factors relating to a change in their own SAR trends such as specific tax reforms and changing client bases.

In addition to the reduction in the number of SARs, in February 2014, the NCA produced a report in which concern was raised about the quality of some consent SARs submitted by the legal sector. The poor quality in some cases meant that the NCA was not able to make a judgement as to whether or not consent should be given. A common problem was insufficient detail being provided, particularly in relation to SARs concerning conveyancing transactions.

According to the NCA, approximately 75% of all SARs from the legal sector were consent SARs. The NCA's analysis of SARs from the legal sector found that 42% of these SARs required follow up with firms because the initial report was incomplete. At times, the poor quality of SARs indicated a lack of understanding or compliance with the MLR and PoCA by the solicitor or firm submitting the SAR.

The situation did not significantly improve after 1 October 2014, following the publication of a guidance note outlining the minimum level of information required to enable consent to be considered and given. As a result the NCA has been returning consent SARs that do not contain sufficient information to enable them to decide whether or not to grant consent. This, of course, means additional work for the NCA and in turn presents a dilemma for solicitors and firms in whether to resubmit a returned consent SAR. This inevitably means additional work for firms and could hold up business. Or it could lead to an individual taking the risk of not resubmitting the consent SAR and potential subsequent criminal and disciplinary consequences.

The Law Society and others have produced guidelines which provide law firms with advice on how to complete an NCA consent SAR request.

Good practice

- The firm has an effective procedure of which staff are well informed which enables them to report suspicious transactions to the MLRO.
- Records of reports are accessible by the MLRO and others as appropriate, yet secure and backed up.
- The MLRO is visible and approachable, reports regularly to management and is well supported.
- Confidentiality of reports is maintained with appropriate safeguards in place to prevent tipping off.
- Reporting to NCA is timely.
- SARs are sufficiently detailed to enable the NCA to determine whether to grant consent or not.
- MLRO acts as a main point of contact in liaison with Legal Enforcement Agencies when dealing with formal and informal requests for information.

Poor practice

- A hands-off or poorly-qualified MLRO.
- Staff are unclear about reporting procedures and obligations, and do not feel confident to use them.
- The MLRO keeps inaccessible, incomplete or inaccurate records.
- A poor AML compliance culture, with no policy framework.
- No policies or procedures in place to prevent tipping-off.

Record Keeping

Regulatory and Legislative Framework

- Record keeping is a fundamental element of an effective AML framework. Firms undertaking work in the regulated sector must keep comprehensive records of CDD, EDD and the supporting records (original documents or copies) about business relationships or occasional transactions that are the subject of CDD or ongoing monitoring.[33]
- To ensure that the requirements specified in Regulation 19 MLR are met, these records should be maintained in a format that is easily accessible. The records should be backed up securely.
- CDD records should be retained for five years beginning on a specified start date, generally the date an occasional transaction completed or the business relationship ended.[34] Accurate records are also important in order to defend any criminal charges of money laundering, terrorist financing or acting in breach of the MLR.

Key Findings

Firms had adapted their retention of records policies to ensure that they complied with their obligations under the MLR, Data Protection Act 1998 and SRA Handbook 2011.[35]

The firms we visited varied in their processes and procedures on recording CDD. The majority of firms maintained a centralised record of CDD in which records were quickly and easily retrievable to appropriate staff including the MLRO. Others kept CDD on individual client files with an electronic copy held on their case management systems.

We found that the standard of records in relation to internal suspicious activity reports that were held and maintained by MLROs varied. We noted that often verbal advice provided to fee earners, and discussions relating to money laundering issues, were not recorded in a written format. This applied particularly when no further action was taken in regard to the enquiry. In other instances, exchanges of emails relating to internal Suspicious activity reports were stored in a specific email folder.

It is imperative that detailed records are kept by the MLRO when an employee submits an internal Suspicious Activity Report. These should include:

- the circumstances on which the suspicion is held
- the further enquires undertaken
- the information obtained
- the rationale behind clearly documented decision-making.

33. Regulation 19(2) MLR 2007

34. Regulation 19 (3) (a) and (b) MLR 2007

35. Outcome 7.5 of the Solicitors Code of Conduct 2011

Good practice

One firm ensured that CDD information is recorded centrally and securely. The firm also ensured that the information is backed up. Staff who need to access information were able to do so, and use the system to ensure that CDD is up to date and accurate.

The MLRO used CDD records to ensure that staff training was relevant and targeted to the firm's needs.

Poor practice

The CDD records of one firm were not easily accessible and were incomplete. Staff were unable to accurately say what CDD had been collected. Staff could not easily access the system to check and update CDD.

This firm could not show compliance with the MLR. Its CDD records were incomplete.

✓ Good practice

- Records are in a format that is secure but accessible.
- Records are backed up securely.
- CDD is recorded in a central location.
- MLRO maintains a register of internal SARs and external disclosures to the NCA including complete and thorough records of all enquiries made documenting key decision-making, rationale and action taken.

✗ Poor practice

- Records are inaccessible or hard to find.
- Records are incomplete or inaccurate.
- MLRO does not maintain any records in relation to internal SARs and external disclosures.

Conclusion

Honesty, independence and sound judgment are at the heart of the legal profession and it is therefore a fundamental requirement that it continues to demonstrate a rigorous approach to the prevention of money laundering.

Effective AML measures are essential to maintain the profession's global reputation as an open and competitive but safe market. Solicitors are often in the front line for providing this protection.

Overall, the results of our engagement are encouraging. The profession showed a good grasp of its obligations and regulatory requirements. However, this is not a reason for complacency. The methods used by criminals to launder money are constantly evolving and being refined. Firms will need to keep themselves updated about new developments and, with the impending enactment of the 4th Anti Money Laundering Directive, new regulatory requirements. Firms need to guard against seeing AML as a tick-box exercise rather than a continuing duty needing constant vigilance, active engagement and judgement. The reputational risk to firms, their principals and staff if they are found to have been used to launder criminal proceeds is obvious. The presence of an informed, engaged and approachable MLRO, an effective CDD policy, and regular staff training are essential requirements to safeguard firms.

We are aware that some aspects of the MLR prove more challenging for smaller firms, for example, MLRO succession planning or providing relevant training for staff which is mandatory under the MLR. Despite these challenges we have seen many instances of good practice among small firms. We will continue to support small firms via the Small Firms Portal.

The risks faced by solicitors need to be minimised by ensuring they comply with the measures outlined in the legislation and the SRA Handbook 2011.

The profession needs to be alert to the risks of money laundering. Through constant vigilance, and embedding good AML practice at every level, firms can minimise the risks faced by the profession and the public. We will continue to work with the profession to promote good practice and compliance.

Ultimately, good AML practice will protect you, your firm, and the profession.