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Take note, absolutely everyone

New rules governing money laundering come into effect in 14 weeks' time. No one is immune

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This week solicitors will receive the Law Society's Money Laundering Practice Note – its guidance to law firms on coping with the new money-laundering regulations 2007 that take effect in mid-December.

Mind you, “note” may be a little misleading. Running to more than 100 pages, this guidance represents an important development in the way law firms deal with money-laundering issues. It will affect every member of staff from senior partner to back office secretary and the repercussions of getting it wrong would be very serious in terms of both reputation and exposure to prosecution.

The buck clearly stops at the top of the firm and a serious breach could lead to two years in jail. As Des Hudson, chief executive of the Law Society of England and Wales, has commented: “The consequences of noncompliance on money-laundering obligations are significant and we urge any solicitor with anti-money-laundering responsibility to study the new practice note.”

Law firms must now move quickly to ensure that all their people understand their obligations under the Act (introduced to satisfy the European Commission's third Money-Laundering Directive). Significantly, John Redwood took pot shots at Euro-inspired money-laundering “red tape” a few weeks ago in his “competitiveness” recommendations to the Conservative Party, and undoubtedly law firms do find the obligations onerous, together with the consequent need to train people. “It's a tremendous burden,” Ian Hargreaves, of Addleshaw Goddard, says. “We have about 1,300 employees who will now need to be trained. It requires a big investment of time and money.”

Faced by the legal obligation to train, the top law firms have set up an informal network called the Online Compliance Consortium (now representing 70 per cent of the country's leading law firms) to provide a forum for discussion of how to do this to greatest effect. After the publication yesterday of the new guidance, work started immediately on developing electronic learning materials to gear staff up for their new responsibilities.

The reality is that money-laundering regulation of one kind or another is now unavoidable across the Western industrialised world. “In general, the principle of

stopping money laundering is not in dispute and sophisticated clients understand the need for this approach,” Mark Humphries, of Linklaters, says. Nonetheless, there are continuing doubts about the proportionality of the paperwork in relation to the system’s effectiveness as a first-line filter. Rod Fletcher, of Russell Jones & Walker, says: “While the leading firms will comply consistently because of fear for their reputation, there are some firms out there with less rigid standards and they will be the ones targeted by the money launderers.”

Perhaps most important among all the changes will be a shift towards what is called a “risk-based approach”. Under the present rules there is a one-size suits all, “tick box” requirement that draws no distinction between different types of client. As a result, law firms were put in the invidious position of having to report to the authorities a wide range of minor misdemeanours that they had discovered in their clients’ records (such as, for example, a late environmental audit). This has no relevance to the War on Terror and, as Roger Butterworth, of Bird & Bird, put it: “Exactly what the Serious Organised Crime Agency does with these reports is not clear.”

The new approach by contrast will give law firms discretion to apply their energies to checking up in greater depth on those people or organisations that look more likely to be involved in money laundering. “The new regulations are a mix of carrot and stick,” Hargreaves says. “The advantage is that the burden is eased when the risk is lowest and it also allows us to rely more on other professionals. But when there is greater risk then we will have much more to do.”

In particular, law firms will have to drill down a further level to establish who is the beneficial owner of a business (rather than just the person who is fronting it up, as in the past) and if the individuals concerned are members of governments or senior figures in the Civil Service – “politically exposed persons” in the jargon – they will come under even greater scrutiny.

The issue of beneficial ownership has been particularly contentious with City law firms working with the Law Society to persuade the Government to clarify who exactly it is looking for. The initial fear was that the regulations would be “the UK’s equivalent of Sarbanes-Oxley” and merely succeed in driving business away from London because it was so heavy-handed. In the event though, the Government took on the concerns of the Law Society and responded positively. As a result the rules announced yesterday seem broadly to be acceptable to the legal profession.

Ironically, perhaps, it was alleged that the private equity industry in particular would take flight from London if a broad interpretation of the rules was imposed. As an example of the law of unintended consequences maybe that would not have been quite such an unpopular outcome after all.