



Law Society
of Scotland

Call for Evidence Response

Call for Evidence: Review of the UK's AML/CFT
regulatory and supervisory regime

October 2021



Introduction

The Law Society of Scotland is the professional body for over 12,000 Scottish solicitors. With our overarching objective of leading legal excellence, we strive to excel and to be a world-class professional body, understanding and serving the needs of our members and the public. We set and uphold standards to ensure the provision of excellent legal services and ensure the public can have confidence in Scotland's solicitor profession.

We have a statutory duty to work in the public interest, a duty which we are strongly committed to achieving through our work to promote a strong, varied, and effective solicitor profession working in the interests of the public and protecting and promoting the Regulation of law. We seek to influence the creation of a fairer and more just society through our active engagement with the Scottish and United Kingdom Governments, Parliaments, wider stakeholders, and our membership.

As the AML supervisor for Scottish solicitors, supervising over 800 firms in Scotland, we welcome the opportunity to consider and respond to the HM Treasury Call for Evidence: *Review of the UK's AML/CFT regulatory and supervisory regime*¹ and we have the following comments and responses to put forward.

Specific Comments

Recent improvements to the regulatory and supervisory regimes

1.What do you agree and disagree with in our approach to assessing effectiveness?

Response: We agree with the approach to assessing effectiveness as described, although we note that, for the framework to really achieve effectiveness, information should be shared, where appropriate, on a reciprocal basis between the regulated sector and law enforcement. Currently the stated approach does not appear to reflect this, as set out within the Call for Evidence; *"The regulated sector work in partnership with supervisors and the government to improve collective understanding of the ML/TF threat, which in turn ensures compliance activity is focussed on the highest risks and the regulated sector provides valuable information to law enforcement"*.²

2.What particular areas, either in industry or supervision, should be focused on for this section?

Response: We believe that the approach could be further enhanced by the amendment of the first Primary Objective, that is; *"The regulated sector act to identify, prevent and report suspicious transactions"*³

¹ Call for Evidence: Review of the UK's AML/CFT regulatory and supervisory regime. See: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1004602/210720_MLRs_Review_Call_for_Evidence_final.pdf

² Call for Evidence, page 7, para 2.9

³ Ibid

To focus on the requirement to compel the regulated sector to implement risk-based controls to prevent money laundering, which is a fundamental constituent of the framework, emphasis should be given to:

- creating the gateways and environment to encourage proactive collaboration and reciprocal information and intelligence sharing across all anti-money laundering (AML) regime stakeholders - the regulated sector, supervisors, government, and law enforcement, both nationally and internationally,
- ensuring industry and supervisory work is not only risk-based but intelligence-led, and outcomes driven, rather than focusing on a “defensive” AML process designed to limit negative consequences. Such an approach is resource intensive, may drive negative behaviours and may not enhance or contribute to the overall objectives of the regime, and
- supervisors and the regulated sector should be further encouraged to take a risk-based approach to narrow and focus resource and efforts on those elements of their business which truly are of a higher AML risk.

3.Are the objectives set out above the correct ones for the MLRs?

Response: Yes, we agree, subject to the caveats and amendments as above in Q1 and Q2. We think the secondary objective regarding partnerships is equally as important as the primary objectives and should be labelled accordingly.

4.Do you have any evidence of where the current MLRs have contributed or prevented the achievement of these objectives?

Response: See our response to Question 8 below and regarding low impact activity.

High-impact activity

5.What activity required by the MLRs should be considered high impact?

Response: We believe that the requirement as set out in Regulation 18⁴ is high impact as it requires regulated persons to consider, assess and document the risks inherent to their own individual backgrounds and circumstances, in turn providing the initial means, information and focus to drive and implement a risk-based approach.

⁴ Unless otherwise stated, all references to ‘Regulation’ throughout this response means the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017. See: <https://www.legislation.gov.uk/uksi/2017/692/contents>

We believe that clarity regarding (and the compulsion to undertake), source of funds/source of wealth (SoF/SoW) investigation by regulated persons is extremely high impact and lies at the very heart of strong risk-based, AML controls. These requirements should be coupled with more pronounced requirements to understand and document the background and circumstances of the client/customer. This is arguably as important, if not more so, than verification of identification in the context of client due diligence (CDD).

- The meanings of source of funds and source of wealth should be included in the general interpretation section of the Regulations, in line with recognised Financial Action Task Force (FATF) and ‘Wolfsberg’ definitions.⁵
- Undertaking and documenting appropriate, risk-based SoF/SoW enquiries should be stated as a required CDD measure (the extent a regulated entity should go to should be risk-based and a higher standard of evidence required in enhanced due diligence (EDD) situations). These requirements are currently only stated as a “must-do” under Regulation 35 EDD: PEPs
- We suggest that undertaking and evidencing SoF/SoW should be a stated requirement of EDD under Regulation 33.
- Under Regulation 28 (11a) we suggest an amendment of wording regarding source of funds, to ensure it is central to the concept of ongoing monitoring of a relationship/ transaction.
- It is a general suggestion to reframe Regulation 28 (11a). This is to ensure ongoing monitoring of the source of funds is at the heart of this regulation. It is unclear to us what “*where necessary*” (as stated in Regulation 28) means, and it is further unclear as to why this requirement stands apart in parentheses, apparently subordinate to other requirements?

6. What examples can you share of how those high impact activities have contributed to the overarching objectives for the system?

Response: Our supervisory work has provided several examples where the risk of money laundering would have been reduced if source of wealth/source of funds requirements had been more clearly stated.

7. Are there any high impact activities not currently required by the MLRs that should be?

Response: We believe the government should formally embed and establish a Money Laundering Reporting Officer (MLRO) position and define MLRO responsibilities in the regulations. This role currently appears only in financial services via the Financial Services & Markets Act 2000 (FSMA 2000) and within the Financial Conduct Authority handbook. These do not apply to all regulated professions captured by the 2017 Regulations.

⁵ Wolfsberg Group Frequently Asked Questions – Source of Wealth/Source of Funds. See: https://www.wolfsberg-principles.com/sites/default/files/wb/Wolfsberg%20SoW%20and%20SoF%20FAQs%20August%202020%20%28FFP%29_1.pdf

We suggest that the Regulations should be amended so that compliance with them may only be achieved in writing, and a presumption is introduced that if controls and measures to satisfy compliance with the regulations is not written, compliance has not been achieved. For example, there should be a stated requirement to undertake written client / matter risk assessments as well as ongoing monitoring during a transaction

8.What activity required by the MLRs should be considered low impact and why?

Response: Whilst we understand, accept, and agree with the Financial Action Task Force (FATF) Recommendation (28) and the need to prevent “bad actors” from being in positions of influence/authority in the regulated sector, we believe the current requirements of Regulation 26 (Prohibitions & Approvals), are low impact, due to the:

- established controls/checks undertaken by the legal sector upon entry to the profession,
- ease of circumvention due to self-declaration of Beneficial Owner, Officer and Manager (BOOM), and
- limited and narrow scope of Schedule 3 offences.

National Strategic Priorities

9.Would it improve effectiveness, by helping increase high impact, and reduce low impact, activity if the government published Strategic National Priorities AML/CTF priorities for the AML/CTF system?

Response: We are unclear of the value of the publication of strategic national priorities in terms of increasing high impact/decreasing low impact activity in the context of the legal sector.

We consider the National Risk Assessment (NRA) /Sectoral RA framework already highlights areas of highest ML/TF risk for the legal sector. Terrorist financing is already considered in the NRA as being of lower risk for the legal sector

10.What benefits would Strategic National Priorities offer above and beyond the existing National

Response: We understand that the publication of Strategic National Priorities (NSPs) may be of use for other regulated sectors, in particular banking/financial services, who are exposed to a much broader, diverse range of anti-money laundering /counter terrorist financing threats than the legal sector. In considering this, it may help these firms develop and sustain a more focused risk-based approach in line with our response to Q2 above.

Risk Assessment of ML/TF?

11. What are the potential risks or downsides respondents see to publishing national priorities?

How might firms and supervisors be required to respond to these priorities?

Response: We would be concerned that any such publication may prioritise certain areas such as high value or “top-end” money laundering risks, and as such may direct regulated persons away from controlling the equally as important lower-end, lower value money laundering threats which blights local communities and in turn harms society more generally.

Extent of the regulated sector

12. What evidence should we consider as we evaluate whether the sectors or subsectors listed above should be considered for inclusion or exclusion from the regulated sector?

Response: Evidence and feedback regarding current and future trends from all AML stakeholders including regulated persons (particularly banks/financial services) supervisors and national and international law enforcement bodies is critical in informing which sectors should be considered for inclusion.

13. Are there any sectors or sub-sectors not listed above that should be considered for inclusion or exclusion from the regulated sector?

Response: We believe that some litigation, likely commercial and above a certain value, should be included in the activities which render someone an independent legal professional and so subject to the regulations. We include this because bogus litigation appears so often as a headline grabbing money laundering technique (e.g, Moldovan Laundromat). It was also mentioned in the recent UK Government Intelligence Committee Report on Russia - s.51.⁶ It therefore occurs to us that the fact that litigation is outwith the scope of the Money Laundering Regulations (MLRs) may be a weakness in the UK’s AML defences.

14. What are the key factors that should be considered when amending the scope of the regulated sector?

Response: The potential for use of the sector/sub sector to transfer or conceal/obscure value or ownership of assets, or the potential to add a veneer of respectability to transactions or underlying parties to a transaction. We believe that the key factors are;

- the complexity and speed of such transmission,

⁶ Intelligence and Security Committee of Parliament ‘Russia’ HC 632. See; https://isc.independent.gov.uk/wp-content/uploads/2021/03/CCS207_CCS0221966010-001_Russia-Report-v02-Web_Accessible.pdf

- the potential for the sector/subsector being considered to move value (particularly large amounts) cross-border/internationally, and
- change/advances in technology and the use of technology to transfer value, ownership of assets, or undertake (or potentially circumvent) key AML controls.

Enforcement

15.Are the current powers of enforcement provided by the MLRs sufficient? If not, why?

Response: Any discussion about whether the current powers of enforcement under the MLRs are sufficient, we suggest, ignores the point that those powers are almost exclusively reserved to the FCA and HMRC. The 2017 Regulations identifies 22 AML supervisors and imposes certain obligations on those supervisors. But the same Regulations do not provide those supervisors with additional powers of necessary for enforcement. As well as placing those powers in the hands of the 22 supervisors, consideration will need to be given to furnishing any independent discipline tribunal with the necessary and appropriate powers. It will also be necessary to ensure relevant provisions dovetail with other legislation.

The current powers of enforcement under the MLRs are sufficient, however they are hampered as they do not in all cases tie in with other legislation which inhibits or undermines the powers conferred to us as a supervisor.

We do not think that the ability to work with the statutory supervisors to increase access to more significant enforcement powers offers a workable solution.

During 2021/2022 we intend to work with Scottish Government to develop a solution for this issue

16.Is the current application of enforcement powers proportionate to the breaches they are used against? If not, why?

Response: As a supervisor, we believe we use our full range of powers (prescribed both through the MLRs, the Solicitors (Scotland) Act 1980 and resultant Practice Regulations⁷) proportionately and dissuasively.

17.Is the current application of enforcement powers sufficiently dissuasive? If not, why?

Response: As above – fining powers conferred by the MLRs are reserved to the FCA and HMRC and limited by other legislation by which we are bound. From a wider perspective across the regulated sector, it is not clear to us (in some cases) that enforcement of MLRs by way of fines, is sufficiently dissuasive, and may still be seen as a “cost of doing business”. For example, the income generated from undertaking business in a non-compliant manner is higher than the potential fine levied.

⁷ Law Society of Scotland Practice Rules <https://www.lawscot.org.uk/members/rules-and-guidance/rules-and-guidance/>

18. Are the relatively low number of criminal prosecutions a challenge to an effective enforcement regime? What would the impact of more prosecutions be? What are the barriers to pursuing criminal prosecutions?

Response: Yes, we believe the low number of criminal prosecutions does hamper the effectiveness of the regime, as the perception may develop that prosecution services and law enforcement do not perceive serious technical breaches as being suitable for prosecution and that they may be unwilling to devote resources to these investigations. Therefore, the effectiveness of the regulations as a deterrent may be reduced. It is possible that these agencies may perceive that where professional bodies have pursued disciplinary action that further action is not necessary. It may be that further work by government is necessary to ensure that there is a common understanding of the importance of pursuing criminal prosecutions in appropriate cases and to ensure that the relevant agencies have an appetite for running these cases.

Regarding barriers to criminal prosecution, the relative complexity of the process may play a part. In addition, because of that complexity and the existence of professional bodies, law enforcement and prosecution services may consider their role diluted. Also, it is suggested that AML failings may be failings of omission, for example; they did not have in place relevant procedures, they did not conduct all required checks or enquires etc. To prosecute such failings would require the prosecution services to prove a negative. This itself is a complex process, though defining such 'sins of omission' specifically as criminal offences might assist, for example; legislation is used to shift the burden of proof, meaning the supervised must now demonstrate compliance rather than the supervisor demonstrate non-compliance. It is accepted this would be quite a departure from the maxim 'innocent until proven guilty'.

Barriers to the risk-based approach

19. What are the principal barriers to relevant persons in pursuing a risk-based approach?

Response: We believe and suggest that there may be a concern across relevant persons that supervisors and other AML authorities may take an overly prescriptive approach to assurance against the regulations, rather than an outcome-focused one. This may lead to a focus on "defensive" AML processes designed to "appease" supervisors and limit negative consequences. Such an approach is by its nature not risk-based, may be resource intensive, may drive negative behaviours and may not enhance or contribute to the overall objectives of the AML regime.

It is also the case that in the legal sector, firms often apply a "standard" CDD criteria (rather than taking a risk-based approach) across different matter types, to avoid the requirement to re-apply or undertake

further CDD on a client that returns to the firm to undertake further legal work, which may be of higher inherent AML risk

20.What activity or reform could HMG undertaken to better facilitate a risk-based approach? Would National Strategic Priorities (discussed above) support this?

Response: We suggest that further efforts are undertaken by UK Government to provide clarity to supervisors on their expectations regarding a risk-based approach, which in turn may improve AML understanding, consistency and focus of supervision, and in turn give relevant persons the confidence to focus on areas of highest risk and impact.

It is not clear to us, in the context of the legal sector, that National Strategic Priorities (NSPs) would enhance or add significant value to the existing information framework, although we do see benefit for other sectors, particularly where the national perspective is set out in the NRA which cascades to individual sectoral risk assessments issued by (Professional Body Supervisors (PBSs).

21.Are there any elements of the MLRs that ought to be prescriptive?

Response: We believe that undertaking and documenting appropriate, risk-based SoF/SoW enquiries of clients should be prescribed as a required CDD measure (albeit the extent a regulated entity should go to should be risk-based and a higher standard of evidence required in EDD situations). This would provide useful clarity to our supervised population. To support this, the meanings of SoF/SoW should be included in the general interpretation section of the Regulations, in line with recognised FATF and 'Wolfsberg' definitions.⁸

We also suggest that the MLRs should be amended so that compliance with them may only be achieved in writing, and a presumption is introduced that if controls and measures to satisfy compliance with the Regulations is not written, compliance has not been achieved.

Understanding of risk

22.Do relevant persons have an adequate understanding of ML/TF risk to pursue a risk-based approach? If not, why?

Response: AML/TF risk is a specialised and specific risk discipline, requiring requisite knowledge, experience, and expertise. It occurs to us that there is a divide between large, regulated businesses, which may be able to afford/hire specialist resource to manage risk in this area, and far smaller relevant persons

⁸ See footnote 5 above.

without this specialist resource/expertise to whom AML is but one of a multitude of risks/responsibilities which they are obliged to tackle.

These smaller entities may therefore, and understandably, lack an understanding or appreciation of ML/TF risks to deploy a risk-based approach adequately and effectively.

23.What are the primary barriers to understanding of ML/TF risk?

Response: As per our response to Q22 above, a lack of specialist knowledge and expertise in a complex area of risk, particularly in the wider regulated sector out with banking/financial services, along with time and resource constraints as set against a backdrop of increasing regulatory burden across the board, and a challenging business environment.

24.What are the most effective actions that the government can take to improve understanding of ML/TF risk?

Response: UK Government could seek to communicate and provide real-world examples of the underlying/predicate crimes which drive money laundering – reinforcing the imperative for the MLRs and the need to understand AML risks as it effects individual regulated businesses.

The UK Government should continue work to ensure the quality, consistency, and clarity of guidance of AML guidance available across the regulated sector.

Expectations of supervisors to the risk-based approach

25.How do supervisors allow for businesses to demonstrate their risk-based approach and take account of the discretion allowed by the MLRs in this regard?

Response: We have recently published a “Supervisory Risk Appetite” statement,⁹ which outlines our position regarding the implementation of a Risk Based Approach (RBA) within firms we supervise, and what that means to them in practice. This statement outlines the measures we take to ensure that the discharge our duties under the MLRs are in proportion to the risks inherent across our supervised population.

Further, we have implemented a set of key factors we must consider when making decisions regarding supervisory assurance outcomes. These help to ensure consistency and form the basis on which our supervisory assurance work will be undertaken and fair, risk-based outcomes, are determined.

⁹ See <https://www.lawscot.org.uk/media/370492/law-society-of-scotland-aml-risk-appetite-statement-february-2021.pdf>

26. Do you have examples of supervisory authorities not taking account of the discretion allowed to relevant persons in the MLRs?

Response: We are not in a position to answer this question.

27. What more could supervisors do to take a more effective risk-based approach to their supervisory work?

Response: External feedback received from HMT, Office for Professional Body Anti-Money Laundering Supervision (OPBAS) and other external stakeholders indicates that the methodology and data driven approach we have implemented to understand the risk profile our supervised population is a best-practice example.¹⁰ It is important that such risk-profiling is based on those areas identified by recognised sources such as FATF, UK Government, Law Enforcement) as being of the highest AML risk, through NRAs and other such publications.

On a more granular level, we believe it is important for supervisors to concentrate resource and assurance efforts on the highest risk areas of the relevant persons they supervise – deploying a full range of supervisory tools and varying the nature, intensity, frequency and focus of supervision, based on the established risk profile of the supervisee.

To this end, we further believe that supervisors should devise an appropriate risk appetite and supervisory strategy and be clear regarding the outcomes to be driven from their supervisory efforts, which again should be in line with stated UK Government strategy and outcomes.

28. Would it improve effectiveness and outcomes for the government and / or supervisors to publish a definition of AML/CTF compliance programme effectiveness? What would the key elements of such a definition include? Specifically, should it include the provision of high value intelligence to law enforcement as an explicit goal?

Response: Yes. Such a definition should closely reflect the definition published in the FATF RBA) for Supervisor's document (March 2021) Section 1.4 "*Characteristics of an effective risk-based supervisory framework*"¹¹

¹⁰ We would be happy to share details of this with other supervisors to (if and where necessary) improve quality and consistency in this important area.

¹¹ FATF Guidance for a Risk-Based Approach Supervisors. See: <https://www.fatf-gafi.org/media/fatf/documents/Risk-Based-Approach-Supervisors.pdf>

The provision of high value intelligence to law enforcement could be used as one measure of supervisory effectiveness, but we are unclear that this should be an explicit goal in terms of effective supervision, as this is ultimately outwith a supervisor's gift to control.

29. What benefits would a definition of compliance programme effectiveness provide in terms of improved outcomes?

Response: Such a definition may:

- provide specific benchmarks for AML supervisors to measure and review supervisory strategy compliance programme effectiveness against,
- clearly articulate UK Government expectations and goals across all supervisors, and
- increase and improve consistency in supervision.

Application of enhanced due diligence, simplified due diligence and reliance

30. Are the requirements for applying enhanced due diligence appropriate and proportionate? If not, why?

Response: Generally, we believe they are both appropriate and proportionate although we note that the requirement, in Regulation 33, to apply EDD "*in any case where the relevant person discovers that a customer has provided false or stolen identification documentation or information and the relevant person proposes to continue to deal with that customer*" could be misleading and in potential conflict with requirements under Regulation 31 "*requirement to cease transactions*" in such situations as CDD cannot be adequately applied.

We believe that Regulation 33 (1a) should be extended to include an express requirement to apply EDD in any case identified as high risk under Regulation 28 (12a) ii – that is "an assessment of the level of risk arising in any particular case"

Further, and in our experience, the prescriptive requirement to apply EDD where "a business relationship is established with a person established in a high-risk country" may be misinterpreted by regulated persons insofar as they then mistakenly believe that EDD is not required when geographical risks are high, but where the jurisdiction concerned is not on the UK list of High Risk Third Countries (HRTCs).¹² Recognising this may run contrary to the opinions expressed in s 3.17 of the Call for Evidence, we believe an amendment to include a more prescriptive requirement to undertake EDD when geographic risks are

¹² HM Treasury Advisory Notice: High-Risk Third Countries. See: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1001025/HM_Treasury_Advisory_Note_High_Risk_Third_Countries-2.pdf

assessed as high based on other established/recognised literature (e.g., FATF Mutual Evaluation Review (MER) assessments, Basel Index, US International Narcotics Control Reports¹³ reports)

31. Are the measures required for enhanced due diligence appropriate and sufficient to counter higher risk of ML/TF? If not, why?

Response: In addition to current requirements, which we believe to be appropriate, we suggest that undertaking enquiries into and obtaining documentary evidence of SoF and where appropriate SoW, should be a stated requirement of EDD under Regulation 33.

32. Are the requirements for choosing to apply simplified due diligence appropriate and proportionate? If not, why?

Response: Yes, we believe the requirements are proportionate and appropriate. We would extend Regulation 37 (1) to include a provision to allow simplified due diligence (SDD) in any case identified as lower risk under Regulation 28 (12a) ii – that is “*an assessment of the level of risk arising in any particular case*”.

33. Are relevant persons able to apply simplified due diligence where appropriate? If not, why? Can you provide examples?

Response: As supervisors we see the majority of SDD applications in specific situations where clients are either a recognised financial/credit institution or the ultimate client/beneficial owner is listed on a regulated stock exchange. We do not see many examples where SDD has been applied where the regulated person assesses AML risk to be lower. Generally, in such lower risk situations, the regulated person chooses to apply the requirements of Regulation 28.

34. Are the requirements for choosing to utilise reliance appropriate and proportionate? If not, why?

Response: In alignment with the joint Legal Sector Affinity Group (LSAG) response to this current Call for Evidence, we agree that a restriction of liability on relying parties is required (e.g., those culpable for ensuring the information meets the needs of your checks, but not of its accuracy) to encourage its use more broadly.

We also propose that reliance be expanded to allow entities to rely on digital identity technology providers who meet a minimum standard set in the regulations. Possible standards could include the good practice guide 45 set out by the Department for Digital Culture, Media, and Sport (DCMS) or the safe harbour

¹³ See; <https://www.state.gov/2021-international-narcotics-control-strategy-report/>

standard set by HM Land Registry (HMLR). This will help to reduce low value repetitive checks on the same client or company by multiple parties e.g., during the residential conveyancing process.

We also note potential contractual restrictions on the provision of CDD information to 3rd parties, where that CDD has been undertaken or supplied by a technology provider/partner to those being relied upon

35.Are relevant persons able to utilise reliance where appropriate? If not, what are the principal barriers and what sort of activities or arrangements is this preventing? Can you provide examples?

Response: As per our response to Q34 above.

36.Are there any changes to the MLRs which could mitigate derisking behaviours?

Response: We are not in a position to answer this question.

How the regulations affect the uptake of new technologies

37.As currently drafted, do you believe that the MLRs in any way inhibit the adoption of new technologies to tackle economic crime? If yes, what regulations do you think need amending and in what way?

Response: Not as far as we are aware.

38.Do you think the MLRs adequately make provision for the safe and effective use of digital identity technology? If not, what regulations need amending and in what way?

Response: See our response to Q34 above. In addition, we also propose that reliance be expanded to allow entities to rely on digital identity technology providers who meet a minimum standard set in the regulations. Possible standards could include the good practice guide 45 set out by the DCMS or the safe harbour standard set by HMLR. This will help to reduce low value repetitive checks on the same client or company by multiple parties e.g., during the residential conveyancing process.

39.More broadly, and potentially beyond the MLRs, what action do you believe the government and industry should each be taking to widen the adoption of new technologies to tackle economic crime?

Response: We suggest that current data privacy laws be reviewed to ensure consistency and compatibility with the MLRs and other financial crime compliance related legislation.

SARs reporting

40.Do you think the MLRs support efficient engagement by the regulated sector in the SARs regime, and effective reporting to law enforcement authorities? If no, why?

Response: Yes. Regulation 19 already requires that relevant persons must have policies, controls and procedures which require any person within the organisation to comply with the relevant sections of Proceeds of Crime Act 2002 (POCA) and Terrorism Act 2000 (TACT).

41. What impact would there be from enhancing the role of supervisors to bring the consideration of SARs and assessment of their quality within the supervisor regime?

Response: We believe that this would be a positive step. As supervisors we welcome further powers to review Suspicious Activity Report (SAR) quality. In terms of specific impacts, there may be some cost associated with providing the means to/ensuring the secure transmission, storage, and deletion of such sensitive data. However, it would be envisaged that such secure transmission and storage platforms are already being used by supervisors for the collection of other sensitive information from their supervised populations.

Additionally, policies and procedures would need to be put in place within supervisory bodies (and self-regulatory organisations) to ensure access and use of such information is strictly controlled. There also may be cost and resource implications for supervisors associated with undertaking additional assurance across SARs within their supervised population.

Finally, there could be a short to medium-term negative impact in terms of risk-based supervision, where supervisory resources are diverted away from high-risk/high impact areas, towards potentially lower risk/lower impact areas where SARs have been submitted erroneously/without basis or defensively by relevant persons, which supervisors are then compelled to undertake assurance/assessment across.

42. If you have concerns about enhancing this role, what limitations and mitigations should be put in place?

Response: As above, there must be robust protections in place to ensure secure transmission, storage, and deletion of such sensitive data, along with policies and procedures that would need put in place within supervisory bodies, and self-regulatory organisations, to ensure access and use of such information is strictly controlled.

Additionally, if AML supervisors have access to SARs an expectation may develop that such supervisors should play an increased roll in law enforcement, or at least more closely link the supervisor and law enforcement. A clear distinction must be maintained between the upholding of professional standards and breaches of the criminal law.

43. What else could be done to improve the quality of SARs submitted by reporters?

Response: The ongoing work to modernise the SAR reporting online form, portal and IT infrastructure is welcomed. The design of the online form (financial sector focused) and technical issues have undoubtedly contributed to frustration amongst reporters and may have impacted on the quality of submissions.

While there have been significant efforts already, further guidance, workshops, and outreach from both UKFIU and supervisors should take place. Communication specialists may be able to contribute innovative new approaches in these areas to avoid simply repeating previous efforts which it seems has not brought about sufficient levels of quality.

44. Should the provision of high value intelligence to law enforcement be made an explicit objective of the regulatory regime and a requirement on firms that they are supervised against? If so, how might this be done in practice?

Response: It should be made an explicit objective of the regulatory regime. However, it cannot be made a requirement on firms on which they are supervised “against”. If there is no intelligence to be provided, there is no intelligence to be provided. That said, supervisors should test that this is the case, along with testing the quality of any reporting that has been made, when undertaking assurance on their supervised population.

Concurring with the LSAG response (to this current Call for Evidence), we also note that the framework for submitting SARs is undertaking significant transformation at present with a new consultation on POCA due to be published in late 2021 and the new SARs IT system set to go live in early 2022. We would therefore suggest that it would be best to allow the already significant changes in this area to bed in, and benefits to be realised before any further changes are made to the role of supervisors.

45. To what extent should supervisors effectively monitor their supervised populations on an on-going basis for meeting the requirements for continued participation in the profession?

Response: We believe this ongoing monitoring of SARs quality should be a requirement of supervisors – albeit we do not believe that this would, on a stand-alone basis, merit any suspension or strike-off from the legal profession. It should however be one consideration in an overall assessment of AML compliance. We, and many other supervisors, already conduct extensive on-going monitoring in the form of reviews, inspections etc and which provide evidence to support members continued participation in the profession (or otherwise).

Gatekeeping tests

46. Is it effective to have both Regulation 26 and Regulation 58 in place to support supervisors in their gatekeeper function, or would a single test support more effective gatekeeping?

Response: It would appear that, for the sake of consistency and clarity, that the two tests could be amalgamated. Additionally, the terms of Regulation 58 (4) should be applied across the regulated sector, and not be confined to those supervised by the Financial Conduct Authority/Commissioners.

47.Are the current requirements for information an effective basis from which to draw gatekeeper judgment, or should different or additional requirements, for all or some sectors, be considered?

Response: In terms of Regulation 26, we believe that the offences as listed under Schedule 3 are too narrow to effectively test if someone is “fit and proper” to hold such a position. We also consider that there should be a requirement to reapply such tests on an ongoing basis.

48.Do the current obligations and powers, for supervisors, and the current set of penalties for non-compliance support an effective gatekeeping system? If no, why?

Response: Along with the lack of requirement to reapply the test on an ongoing basis (therefore a beneficial owner, officer, or manager could commit an offence under schedule 3 of the 2017 Regulations and would not need to declare this to a supervisor) we consider that the value provided by Regulation 26 as a check is also easy for any relevant person to circumvent. Supervisors become aware of the individuals that need approval under regulation 26 through self-declaration. If an entity wished to hide a beneficial owner, officer, or manager from the Regulation 26 check, they could simply choose to not declare them, meaning they would not be checked.

Guidance

49.In your view does the current guidance regime support relevant persons in meeting their obligations under the MLRs? If not, why?

Response: Yes, we believe the current guidance regime does support relevant persons in this regard, albeit HMT should take further steps to ensure consistency in the quality, scope and, detail guidance available across the different areas of the regulated sector.

50.What barriers are there to guidance being an effective tool for relevant persons?

Response: We suggest that Regulation 76 (6) (b) (ii) of the 2017 AML Regulations should be amended. It is currently drafted as follows: -

(6) In deciding whether P has contravened a relevant requirement, the designated supervisory authority must consider whether at the time P followed [...] (b) any relevant guidance which was at the time [...] (ii) issued by any other supervisory authority or appropriate body and approved by the Treasury. For the purposes of this regulation ‘designated supervisory authority’ is defined later in Regulation 76 (8b) as HMRC or the FCA.

We believe and suggest that the effectiveness of approved AML guidance would be improved if Regulation 76 (8b) was widened to include all supervisory authorities as listed in Schedule 1 of the MLRs

Thought should be given to the re-organisation of guidance to better account for often very wide diversity and differences in the purposes and nature of business undertaken, even within the same sector. For example - in the legal sector, there are significant differences in both the work undertaken by (and therefore the inherent risks faced by) solicitors, as compared to barristers/advocates, or notaries. It may therefore be more appropriate that different guidance is written, specifically for these legal sub-sectors, as opposed to the current LSAG approach (requested by HMT) where accounting for these disparities may weaken the guidance, introduce potential confusion, or make it more difficult for relevant persons to follow. These were issues discussed with HMT during the last LSAG guidance drafting process.

51. What alternatives or ideas would you suggest to improve the guidance drafting and approval processes?

Response: We suggest that HMT should issue further information to supervisors and others involved in guidance drafting, regarding what they consider to be the key constituents and areas to be covered by guidance, and potentially high-level information relating to suitable format of guidance. This would promote consistency.

We further suggest that a representative from HMT should be assigned to each group drafting guidance, to be involved and give input during the drafting process. This early and ongoing dialogue may then help support and expedite the final sign-off process.

Structure of the supervisory regime

52. What are the strengths and weaknesses of the UK supervisory regime, in particular those offered by the structure of statutory and professional body supervisors?

Response: We strongly believe that the current supervisory structure continues to be of significant benefit to the UK AML regime.

Given the diverse and often specialist nature of AML-regulated activities (even within the same “sector”), and the specific and complex inherent AML risks associated with these activities, we believe it is imperative to ensure that supervision of these activities is undertaken by those with the appropriate and necessary levels of knowledge, skills, and expertise in those fields.

Clearly, given the diversity of the current structure, there is a potential for inconsistencies in supervisory approach and enforcement. Any such inconsistencies could weaken the UK's AML defences and create opportunities for criminal exploitation, including through regulatory arbitrage. However, OPBAS have been tasked with eradicating such inconsistencies and this may mean that this risk is now balanced by an effective control.

53.Are there any sectors or business areas which are subject to lower standards of supervision for equivalent risk?

Response: Considerable resource has been focused on ensuring that PBS supervision is performed to acceptable standards. Generally, a similar independent oversight of the work of the statutory supervisors would improve transparency and provide assurance that consistent standards were being applied across the whole supervisory regime.

It appears to us that certain sections of the trust & company service provision industry (particularly company formation agents) continue to be central to significant criminal abuse and have featured centrally in large scale laundromat cases in recent years. It appears to us that these businesses may continue to subject to a different level of supervisory oversight.

54.Which of the models highlighted, including maintaining the status quo, should the UK consider or discount?

Response: To ensure consistency, consideration may be made to consolidation of the overall supervisory framework, whilst ensuring that those involved in supervision have the “critical mass” to supervise effectively, and extremely importantly appropriate and necessary levels of knowledge, skills, and expertise in the areas under their supervision are retained. A potentially better alternative which may improve consistency without losing the benefits of the current regime, may be to expand the scope and remit of OPBAS subject to the caveats and conditions as set out in our responses to Q56-59 below.

We strongly oppose the consolidation of the regime down to “very few” or a single supervisor, as suggested at paragraph 4.11 of the Call for Evidence.

55.What in your view would be the arguments for and against the consolidation of supervision into fewer supervisor bodies? What factors should be considered in analysing the optimum number of bodies?

Response: In addition to our contentions above regarding the potential loss of knowledge skills and expertise to supervise effectively, we believe that there could be significant and unnecessary costs

associated with the consolidation of the regime down to “very few” or a single supervisor. Other factors to be closely considered should be:

- retention of skills, knowledge, and experience,
- the geographic location and proximity of both supervisor supervisees,
- devolved powers and different legal structures/frameworks across the UK,
- existing effective matches of PBSs and single police forces in the devolved nations enabling more effective relationships and information sharing, and
- relationships of supervisor to both the supervised population and other local and national bodies AML stakeholders which may enhance supervision.

Effectiveness of OPBAS

56.What are the key factors that should be considered in assessing the extent to which OPBAS has met its objective of ensuring consistently high standards of AML supervision by the PBSs?

Response: Overall, we believe the creation and work of OPBAS has made an extremely positive contribution to our work, and the effectiveness and development of the overarching UK AML supervisory regime. OPBAS should be suitably and sustainably resourced to ensure it retains the skills, knowledge and experience it has built up from its inception.

We would welcome the publication of a performance assessment framework for OPBAS. We would expect a performance assessment framework to tie into a published strategy which would show key milestones to be achieved over the strategy period culminating in a desired final position.

Overall, a general and significant increase in the standards of AML supervision by PBS's should at some point be reflected in the NRA. While the inherent sectoral risks will remain, HMT/Home Office/law enforcement should at some point be able to report that the level of supervision by PBS's (reflecting improvements facilitated by OPBAS) has had a clear impact on reducing the risk of money laundering through the legal sector.

In more detail we consider that the following factors would feature prominently in a performance assessment framework which measures the extent to which OPBAS has meet its objectives: .

Evidence of;

- increased sharing of supervisory best practice and appropriate guidance across the PBS community,
- the widespread (or total) adoption of effective risk-based approaches to supervision across PBSs, in line with the recently released FATF guidance on this subject,
- appropriate senior management engagement and governance arrangements within PBSs,

- that PBS AML supervisory functions are adequately resourced with staff at the necessary levels of skill and are supported with appropriate tools and technology.
- the effective implementation and deployment of the broad range of supervisory tools and powers available to PBSs, and
- increased volumes of tactical intelligence sharing from law enforcement to PBSs, and
- success in the removal of barriers to information sharing between PBSs and to/from law enforcement.

57. What are the key factors that should be considered in assessing the extent to which OPBAS has met its objective of facilitating collaboration and information and intelligence sharing?

Response: Overall the impact of OPBAS on this area should be reflected in clear evidence that barriers to effective information sharing have been removed which will be reflected in greatly increased levels of tactical intelligence by law enforcement.

Factors which should be considered would be:

- evidence of the creation and use of appropriate MOUs/gateways internally between PBSs, and externally between PBSs and LEAs,
- the volume of appropriate intelligence-led supervisory assurance/investigations undertaken by PBSs, particularly where intelligence has been provided by LEAs,
- greater numbers and examples of cross-sector collaboration, and/or intelligence-led investigation activity between LEAs and PBSs,
- whether activity within public-private partnership work has been (where appropriate) redesigned to be less focused on financial services and to produce collaboration and outputs which add value to the supervisory activities of PBSs, and
- where appropriate, a more visible presence of the national and regional information sharing expert working groups, including appropriate and proactive intelligence alerts/materials/publications available to supervised populations.

Remit of OPBAS

58. What if any further powers would assist OPBAS in meeting its objectives?

Response: We believe that the current powers OPBAS has at its disposal should be sufficient to meet its objectives.

59. Would extending OPBAS's remit to include driving consistency across the boundary between PBSs and statutory supervisors (in addition to between PBSs) be proportionate or beneficial to the supervisory regime?

Response: The statutory supervisors have very significant responsibilities, and it is likely that the supervisory regime as whole would benefit from the application of the specialist skills of OPBAS to drive consistency as described. This would be particularly relevant where some services offered by the legal sector straddle the supervision of HMRC and legal sector PBSs. Where appropriate, this would need to be backed by necessary amendments to (and a balancing of) the powers and responsibilities of PBSs and statutory supervisors currently embedded in the MLRs

Supervisory gaps

60.Are you aware of specific types of businesses who may offer regulated services under the MLRs that do not have a designated supervisor?

Response: We are aware of limited instances in the Scottish legal sector where individuals undertake work which may fall within Regulation 12 (1) of the MLRs, but who are not supervised by us as they do not hold a practicing certificate and as such are not on the Roll of Scottish Solicitors.

61.Would the legal sector benefit from a ‘default supervisor’, in the same way HMRC acts as the default supervisor for the accountancy sector?

Response: We would suggest that the legal sector would benefit from a set of default supervisors, depending on the individuals/business geographical location and business activities. This should be based around the current legal sector PBS model.

62.How should the government best ensure businesses cannot conduct regulated activity without supervision?

Response: Appropriate legal basis would be required, along with provisions to prevent businesses operating in such circumstances under threat of criminal sanction and could be based on the current HMRC model as cited in the Call for Evidence. This could be best undertaken by ensuring a central resource is available to conjoin, cross-refer and analyse data and intelligence held by government and other stakeholders/agencies such as law enforcement, HMRC and other supervisors to identify instances where individuals or businesses appear to be undertaking regulated work without requisite supervision.



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