Advocates and Other Legal Practitioners

Sector Specific AML/CFT Guidance Notes

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1. **Foreword**

The “legal sector” is the collective term used to describe the businesses detailed in (g) of Schedule 4 to the Proceeds of Crime Act 2008 (“POCA”) as detailed below:

(g) any activity which is specified in sub-paragraph (h) that is undertaken by:

(i) an advocate within the meaning of the *Advocates Act 1976*;
(ii) a registered legal practitioner within the meaning of the *Legal Practitioners Registration Act 1986*;
(iii) a notary public within the meaning of the *Advocates Act 1995 and the Notaries Regulations 20003*; or
(iv) any other legal professional who by way of business provides legal services to third parties,

except for any such persons who are employed by public authorities or undertakings which do not by way of business provide legal services to third parties.

The activities specified in sub-paragraph (h) include:

(h) when undertaken by a person referred to in sub-paragraph (g) —

(i) managing any assets belonging to a client;
(ii) the provision of legal services which involves participation in a financial or real property transaction (whether by assisting in the planning or execution of any such transaction or otherwise) by acting for, or on behalf of, a client in respect of —
   (A) the sale or purchase of land;
   (B) managing bank, savings or security accounts;
   (C) organising contributions for the promotion, formation, operation or management of bodies corporate;
   (D) the sale or purchase of a business; or
   (E) the creation, operation or management of a legal person or legal arrangement;

By virtue of being included in Schedule 4 to POCA (when engaging in the activities specified in sub-paragraph h) this sector is subject to the requirements of the Anti-Money Laundering and Countering the Financing of Terrorism Code 2015 (“the Code”).

It should be noted that as stated in Schedule 4 to POCA, paragraph 2, a business is not in the regulated sector by reason of the provisions of subparagraph (1)(h)(i) in relation to managing any assets belonging to a client where those assets only represent advance payment of fees.

Also, this sector is included in the Designated Businesses (Registration and Oversight) Act 2015 (“DBRO”) which came into force in October 2015. The Financial Supervision Authority now has the power to oversee this sector for Anti-Money Laundering and Countering the Financing of Terrorism (“AML/CFT”) purposes.
Furthermore, any firm which anticipates holding money in a client account or undertaking any of the activities listed above in the future may wish to register as a Designated Business even if the activities are not being undertaken at present.

The Authority wishes to thank the Isle of Man Law Society for their assistance in developing this sector specific guidance.

2. Introduction

The purpose of this document is to provide some guidance specifically for the legal sector. This sector specific guidance should be read in conjunction with the main body of the AML/CFT Handbook. It should be noted that guidance is not law, however it is persuasive. Where a person follows guidance this would tend to indicate compliance with the legislative provisions, and vice versa.

This document will cover unique money laundering and financing of terrorism (“ML/FT”) risks that may be faced by the legal sector and will provide further guidance in respect of customer due diligence (“CDD”) measures where a once size fits all approach may not work. Also, some case studies are included to provide context to these unique risks. The information included in this document may be useful to relevant persons to assist with their risk assessment obligations under the Code.

This document is based on the FATF Report on Money Laundering and Terrorist Financing Vulnerabilities of Legal Professionals\(^1\) and also includes some key warning signs from the Law Society for England and Wales\(^2\). The Authority recommends that relevant persons familiarise themselves with these documents, and other typology reports concerning the legal sector.

3. Risk Guidance

Guidance in relation to conducting risk assessments is provided under Part 3 of the AML/CFT Handbook. This section aims to provide further guidance to the risks generally unique to the legal sector. The services of the legal sector may be used by money launderers to provide an additional layer of legitimacy to the criminal’s financial arrangements, especially where the sums involved may be larger.

3.1. Client accounts

Client accounts are often used by the legal sector. The use of client accounts has been identified by the FATF as a potential vulnerability, as it may enable criminals to either place money within the financial system and / or use the money as part of their layering activity, with fewer questions being asked by financial institutions because of the perceived respectability and legitimacy added by the involvement of the legal professional.

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\(^1\) [http://www.fatf-gafi.org/media/fatf/documents/reports/RBA%20Legal%20professions.pdf](http://www.fatf-gafi.org/media/fatf/documents/reports/RBA%20Legal%20professions.pdf)

\(^2\) [https://www.lawsociety.org.uk/support-services/risk-compliance/anti-money-laundering](https://www.lawsociety.org.uk/support-services/risk-compliance/anti-money-laundering)
While the use of the client account is part of many legitimate transactions undertaken by the legal sector, it may be attractive to criminals as it can:

- be used as part of the first step in converting the cash proceeds of crime into other less suspicious assets;
- permit access to the financial system when the criminal may be otherwise suspicious or undesirable to a financial institution as a customer;
- serve to help hide ownership of criminally derived funds or other assets; and / or;
- can be used as an essential link between different money laundering techniques, such as purchasing real estate, setting up shell companies and transferring the proceeds of crime.

The following situations could give cause for concern:

- a client deposits funds in an advocate’s client account, but then ends the transaction for no apparent reason;
- a client advises that funds are coming from one source and at the last minute the source changes for no proper reason;
- a client requests to use a client account but does not require any underlying legal services; and / or;
- a client unexpectedly (and for no proper reason) requests that money received into a firm’s client account be sent back to its source, to the client or third party.

Where a client account is being utilised the rationale should be obtained and this should be monitored on an ongoing basis. The legal sector should think carefully before disclosing client account details as this allows money to be deposited into a client account without the firm’s knowledge. The firm should ask the client where the funds will be coming from. Will it be an account in the client’s name, from the Island or another jurisdiction?

Circulation of client account details should be kept to a minimum. Clients should be discouraged from passing the details on to third parties and should be asked to use the account details only for previously agreed purposes. Letters of Engagement should include reference to areas such as this.

### 3.2. Administration of estates

A deceased person’s estate is very unlikely to be actively utilised by criminals as a means for laundering their funds; however, there is still a low risk of money laundering for those working in this area.

When winding up an estate, whilst there is no blanket requirement that should be satisfied about the history and sources of funds which make up the estate under administration, the firm should try to ensure they have a high level knowledge of the general source of wealth of the estate and that they know the deceased. The firm should be aware of the factors which can increase ML risks and consider the following:
• where estate assets have been earned in a foreign jurisdiction, firms should be aware of the wide definition of criminal conduct in POCA; and/or

• where estate assets have been earned or are located in a higher risk territory, firms may need to make further checks about the source of those funds.

Firms should also bear in mind that an estate may include criminal property. An extreme example would be where the firm knows or suspects that the deceased person was accused or convicted of acquisitive criminal conduct during their lifetime. Firms, in particular those who regularly engage in criminal work, which also act under Power of Attorney and provide will services should also be aware.

If firm’s know, or suspect, that the deceased person improperly claimed welfare benefits/allowances or had evaded the due payment of tax during their lifetime, criminal property may have already been disposed of and may be included in the estate and so a STR may be required.

Relevant local laws will apply before assets can be released. For example, a grant of probate will normally be required before UK assets can be released. Firms should remain alert to warning signs, for example if the deceased or their business interests are based in a higher risk jurisdiction.

If the deceased person is from another jurisdiction and a law agent is dealing with the matter in the home country, firms may find it helpful to ask that person for information about the deceased to gain some assurances that there are no suspicious circumstances surrounding the estate. The issue of the tax payable on the estate may depend on the jurisdiction concerned.

Firms should be alert from the outset, and monitor throughout, so that any disclosure can be considered as soon as knowledge or suspicion is formed and problems of delayed consent are avoided.

3.3. Charities

The legal sector may have involvement in setting up charities or other non-profit organisations. While the majority of charities are used for legitimate reasons, they can be used as ML/FT vehicles. A charity should be risk assessed and treated the same as any other client. Firms acting for charities should consider its purpose and the organisations it is aligned with. If money is being received on the charity’s behalf from an individual or a company donor, or a bequest from an estate, firms should be alert to unusual circumstances, including large sums of money.

3.4. The use of trusts

The legal sector is often involved in the creation of trusts. Trusts are also at risk of being used as a ML vehicle. Trusts can be vulnerable to ML at any point of their life time. Even if the funds are clean at the establishment they may become proceeds of crime if used by trustees for criminal purposes.
When setting up a trust, be aware of ML/FT high risk indicators (see section 1.4 of this guidance) and ensure the nature / purpose of the business relationship is known to the firm.

Whether you act as a trustee yourself, or for trustees, the nature of the risk may already require information to be gathered which will help you in assessing ML risks, such as the location of assets and the identity of trustees. Involvement of a jurisdiction that has strict banking secrecy laws and confidentiality rules or those without equivalent ML laws may increase the profile of the retainer.

3.5. Property purchases

Criminal conduct generates huge amounts of illicit capital and these criminal proceeds need to be integrated into personal lifestyles and business operations. Property purchases are one of the most frequently identified methods of ML. In many countries a legal professional is either required by law to undertake the transfer of property or their involvement is a matter of custom and practice.

Property can be used either as a vehicle for ML or as a means of investing laundered funds. Criminals may buy property both for their own use, e.g. as principal residencies or second homes, or as business or warehouse premises, or as investment opportunities to provide additional income.

The purchase of real estate is commonly used as part of the last stage of ML. Such a purchase offers the criminal an investment which gives the appearance of financial stability. The purchase of a restaurant or hotel, for example, offers particular advantages, as it is often a cash-intensive business, which is the preferred currency of the criminals. Retail businesses provide a good front for criminal funds where legitimate earnings can be used as a front for the proceeds of crime.

There are several factors to consider in relation to property purchases including purchasing with a false name, purchasing through intermediaries, purchasing through a company / trust and mortgage fraud. Quick back to back sales are also important to consider as the frequent changes in ownership may make it more difficult for law enforcement to follow the funds and link the assets back to the predicate offence.

3.6. Conveyancing services / mortgage fraud

Research suggests that of all the services offered by the legal sector, conveyancing is the most utilised function by criminal groups. Conveyancing is a comparatively easy and efficient means to launder money with relatively large amounts of criminal monies ‘cleaned’ in one transaction.

In a stable or rising property market, the launderer will incur no financial loss except fees. Conveyancing transactions can also be attractive to money launderers who are attempting to disguise the audit trail of the proceeds of their crimes. As the property itself can be “criminal property”, the legal sector can still be involved in ML even if no money changes hands.
Conveyancing staff should be alert to instructions which are a deliberate attempt to avoid assets being dealt with in the way intended by the court or through the usual legal process. For example, staff may sometimes suspect that instructions are being given to avoid the property forming part of a bankruptcy, or forming part of assets subject to confiscation.

Specific risk indicators to consider in this area include:

- properties owned by nominee companies or multiple owners which could be used to disguise the true owners. The legal sector should be alert to sudden or unexplained changes in ownership;
- where a third party is providing the funding for a purchase but the property is being registered in someone else’s name. The firm should ensure they know the nature of the relationship between the parties. Appropriate CDD should be undertaken on the person providing the funding;
- considering how the property is funded, and any funding changes during the transaction. The legal sector should be alert for large payments from private funds, especially if receiving payments from a number of different individuals/ sources;
- an unusual sale price may indicate money laundering. If a firm becomes aware of a significant discrepancy in relation to the sale price this should be appropriately investigated;
- clients who attempt to mislead a lender to improperly inflate a mortgage advance (mortgage fraud) for example by misrepresentation the borrower’s income, or because the seller and buyer are conspiring to overstate the sale price. The firm should be aware of the potential of this occurring; and / or
- the possibility of larger scale mortgage fraud which will involve several properties / parties to the transactions. Vigilance in this area is key, and appropriate action should be taken by the firm. This may include making a disclosure as an improperly obtained mortgage could be criminal property as it is a benefit derived from a fraudulent application.

If a client has made a deliberate misrepresentation on their mortgage application, it is likely that the crime/fraud exemption to legal professional privilege will apply. This means that no waiver of confidentiality will be needed before a disclosure is made. However, such matters will need to be dealt with on a case-by-case basis.

3.7. Company and commercial work

The legal sector is often involved in the creation of companies. The nature of company structures can make them attractive to money launderers because it is possible to obscure true ownership and protect assets for relatively little expense. For this reason, firms working with companies and in commercial transactions should remain alert throughout their retainers with existing, as well as new, clients. It is a requirement of the Code that business relationships are subject to ongoing monitoring.

A common operating method amongst serious organised criminals is the use of front companies. These are often used to disguise criminal proceeds as representing the legitimate profits of fictitious business activities. They can also help to make the transportation of suspicious cargoes appear as genuine goods being traded. More often than not, they are used
to mask the identity of the true beneficial owners and the source of criminally obtained assets.

Corporate vehicles are also frequently used to help commit tax fraud, facilitate bribery/corruption, shield assets from creditors, facilitate fraud generally or circumvent disclosure requirements. The lack of transparency concerning the ownership and control of corporate vehicles has proved to be a consistent problem for money laundering investigations. Corporations serving as directors and nominee directors can be used to conceal the identity of the natural persons who manage and control a corporate vehicle.

Several international reports have highlighted the extent to which private limited companies, shell companies, bearer shares, nominees, front companies and special purpose vehicles have been used in laundering operations. Case studies submitted to the FATF have indicated the following common elements in the misuse of corporate vehicles:

- multi-jurisdictional and/or complex structures of corporate entities and trusts;
- foreign payments without a clear connection to the actual activities of the corporate entity;
- use of offshore bank accounts without clear economic necessity;
- use of nominees and use of shell companies; and/or
- tax, financial and legal advisers were generally involved in developing and establishing the structure. In some of these international case studies legal agents were involved and specialised in providing illicit services for clients.

### 3.8. Shell corporations

A shell company can be used for legitimate purposes, however it is also a tool that can be widely used by criminals. They are often purchased “off-the-shelf”, it remains a convenient vehicle for laundering money and for concealing the identity of the beneficial owner of the funds. The company records are often more difficult for law enforcement to access because they are held behind a veil of professional privilege or the professionals who run the company act on instructions remotely and anonymously.

Shell companies are often used to receive deposits of cash which are then transferred to another jurisdiction, to facilitate false invoicing or to purchase real estate and other assets. They have also been used as the vehicle for the actual predicate offence of bankruptcy fraud on many occasions. Where a shell company is being used adequate rationale should be provided for the use of this entity. If appropriate information is not provided this should be appropriately investigated by the firm.

### 3.9. Private Equity

The legal sector could be involved in any of the following circumstances:

- the start-up phase of a private equity business where individuals or companies seek to establish a private equity practice (and in certain cases, become authorised to conduct investment business);
• the formation of a private equity fund; ongoing legal issues relating to a private equity fund; and / or;
• execution of transactions on behalf of a member of a private equity practice's group of companies (a private equity sponsor that will normally involve a vehicle company acting on its behalf).

Generally private equity work will be considered to be low risk for ML and FT for the following reasons:

• private equity is also covered by the Code and similar legislation in equivalent jurisdictions;
• investors are generally large institutions, some of which will also be regulated for ML purposes;
• there are generally detailed CDD processes followed prior to investors being accepted;
• the investment is generally illiquid and the return of capital is unpredictable; and / or;
• the terms of the investment in the fund generally strictly control the transfer of interests and the return of funds to investors.

Specific risk factors in relation to this may be as follows:

• where the private equity vehicle, fund manager or an investor is located in a jurisdiction which is not regulated for money laundering to a standard which is equivalent to the FATF recommendations;
• where the investor is either an individual or an investment vehicle itself (a private equity fund of funds); and / or;
• where the private equity vehicle is seeking to raise funds for the first time or is approaching a large investor base.

3.10. Holding of Funds

Firms that choose to hold funds as stakeholder or escrow agent in commercial transactions should consider the checks to be made about the funds they intend to hold before the funds are received. CDD measures should be conducted on all those on whose behalf the funds are being held as per the Code requirements.

Particular consideration should be given to any proposal that funds are collected from a number of individuals whether for investment purposes or otherwise. This could lead to wide circulation of client account details and payments being received from unknown sources.

4. High Risk Indicators

As with the basic elements of a risk assessment discussed under Part 3 of the AML/CFT Handbook, the following list provides examples of factors or activities that are likely to indicate a higher risk of ML/FT and should warrant further attention or scrutiny by the firm (just because a feature is listed below it does not automatically make the relationship high risk, provided suitable controls are in place.)
As with all types of risk assessment, a holistic approach should be taken and the indicators below should be taken into consideration along with a wide range of other factors:

1. The client is overly secretive or evasive about:
   - their identity;
   - who the beneficial owner is (if applicable);
   - the source of funds; and / or;
   - the nature and intended purpose of the business relationship.

2. The client:
   - is a PEP;
   - does not seem to have an appropriate rationale for the services being sought;
   - is using complex structures without providing, or inadequately providing, appropriate rationale;
   - is using an agent or intermediary with no apparent legitimate reason;
   - delegates authority without appropriate rationale (for example power of attorney, mixed boards etc);
   - is actively avoiding personal contact with no apparent legitimate reason;
   - is reluctant to provide or refuses to provide information, data and documents usually required in order to enable the transaction’s execution;
   - provides false or counterfeited documentation;
   - is a business entity which cannot be found on the internet and/or uses an email address with an unusual domain part such as Hotmail, Gmail, Yahoo etc. especially if the client is otherwise secretive or avoids direct contact;
   - is known to have convictions for acquisitive crime (meaning a crime that generates proceeds), known to be currently under investigation for acquisitive crime or have known connections with criminals;
   - is conducting activities which are prohibited if carried on in certain countries, is engaged in higher risk trading activities, or engaged in a business which involves handling significant amounts of cash;
   - has connections to a higher risk country including those that the FATF has asked members to apply counter measures in relation to; those with ML/FT strategic deficient; those identified as major illicit drug producers; those that have strong links with terrorist financing; sanctioned countries etc;
   - is or is related to or is a known associate of a person known as being involved or suspected of involvement with ML/FT activities;
   - is involved with the use of bearer shares;
   - is involved in transactions which do not correspond to his normal professional or business activities;
   - frequently changes legal structures and/or; managers of legal persons; and / or;
   - asks for short-cuts or unexplained speed in completing a transaction.

3. The parties:
   - the parties to the transaction are connected without an apparent business reason;
   - the ties between the parties of family, employment, corporate or any other nature generate doubts as to the real nature or reason for the transaction;
   - there are multiple appearances of the same parties in transactions over a short period of time;
the age of the executing parties is unusual for the transaction, especially if they are under legal age, or the executing parties are incapacitated, and there is no logical explanation for their involvement;
• there are attempts to disguise the real owner or parties to the transaction;
• the person actually directing the operation is not one of the formal parties to the transaction or their representative; and / or
• the natural person acting as a director or representative does not appear to be a suitable representative.

4. The source of funds:
• the transaction involves a disproportional amount of private funding, bearer cheques or cash, especially if it is inconsistent with the socio-economic profile of the individual or the company’s economic profile;
• the client or third party is contributing a significant sum in cash as collateral for funding provided by the borrower/debtor rather than simply using those funds directly, without logical explanation;
• third party funding either for the transaction or for fees/taxes involved with no apparent connection or legitimate explanation;
• the transaction is aborted for no legitimate reason after receipt of funds and there is a request to send the funds to a third party;
• funds are received from or sent to a foreign country when there is no apparent connection between the country and the client;
• funds received from or sent to high-risk countries; and / or;
• the client is using multiple bank accounts or foreign accounts without good reason.

5. The choice of lawyer:
• instruction of a legal professional without experience in a particular specialty or without experience in providing services in complicated or especially large transactions;
• the client is prepared to pay substantially higher fees than usual, without legitimate reason;
• the client has changed advisor a number of times in a short space of time or engaged multiple legal advisers without legitimate reason; and / or;
• the required service was refused by another professional or the relationship with another legal professional was terminated.

5 Legal Privilege

Section 21 of the DBRO provides that:-

"A person is not under an obligation under this Act to disclose any information subject to legal privilege within the meaning of section 13 (meaning of "items subject to legal privilege") of the Police Powers and Procedures Act 1998."

Having regard to Section 21 of the DBRO, lawyers should be aware that in such circumstances they are not required to provide unauthorised disclosure of items subject to legal privilege to the Authority, or to the Law Society acting under the Authority’s delegated
authority. Indeed lawyers owe a duty to their clients not to disclose items subject to legal privilege under any circumstances without the express consent of their client.

Items subject to legal privilege are defined by reference to Section 13 of the Police Powers and Procedures Act 1998 ("the PPP Act") as follows:

**Meaning of "items subject to legal privilege"

(1) Subject to subsection (2), in this Act "items subject to legal privilege" means —

(a) communications between a professional legal adviser and his client or any person representing his client made in connection with the giving of legal advice to the client;

(b) communications between a professional legal adviser and his client or any person representing his client or between such an adviser or his client or any such representative and any other person made in connection with or in contemplation of legal proceedings and for the purposes of such proceedings; and

(c) items enclosed with or referred to in such communications and made —

(i) in connection with the giving of legal advice; or

(ii) in connection with or in contemplation of legal proceedings and for the purposes of such proceedings,

when they are in the possession of a person who is entitled to possession of them.

(2) Items held with the intention of furthering a criminal purpose are not items subject to legal privilege.

The statutory definition of legal privilege above identifies that there are two heads of legal privilege. One applies whether or not litigation is contemplated or pending, but covers a narrower range of communications (commonly referred to as advice privilege). The other applies only where litigation is contemplated or pending, but extends over a wider range of communications (commonly referred to as litigation privilege).

The right to legal privilege is that the client and not the lawyer of the client, and is not lost by the death of the client but continues to exist for the benefit of the client's successor in title. The importance of legal privilege cannot be overstated. It is a substantive legal principle such that there is nothing improper in a client standing on his privilege where it is made out, and if the client wishes to maintain privilege, this cannot be taken against the person doing so. Equally, it is the client's right to waive privilege either entirely, or where appropriately documented, under a limited waiver, and if the client is happy to waive privilege, lawyers cannot object.

Litigation privilege covers confidential communications made, after litigation is commenced or even contemplated, between:-
(a) a lawyer and his client;
(b) a lawyer and his non-professional agent, or
(c) a lawyer and a third party,

for the sole or dominant purpose of such litigation (whether for seeking or giving advice in relation to it, or for obtaining evidence to be used in it, or for obtaining information leading to such obtaining). In common with legal advice privilege, it is necessary that a communication in question is confidential in order to attract privilege.

Litigation privilege is based on the idea that legal proceedings take the form of a contest in which each of the opposing parties assemble his own body of evidence and uses it to try to defeat the other, with the judge or jury determining the winner. In such a system each party should be free to prepare his case as fully as possible without the risk that his opponent (or any other third party) will be able to recover the material generated by his preparations.

Legal advice privilege may be properly claimed in respect of communications between a lawyer in his professional capacity and his client for the purpose of seeking or giving legal advice for the client. It has been established by case law that legal advice is not confined to telling the client the law, and includes advice as to what should prudently and sensibly be done in the relevant legal context. It is important that there is a relevant legal context in order for communications to attract legal professional privilege.

It would be too far to extend legal advice privilege without limit to all advocate and client communications within the ordinary business of an advocate. However, where there is a relevant legal context to the instruction of the advocate, legal advice privilege will attract to all communications between the client and the advocate in connection with the giving of legal advice (Section 13 of the PPP Act).

Section 13 of the PPP Act defines legal privilege in terms entirely consistent with the common law principles which govern legal privilege. So far as legal advice privilege is concerned, it refers to communications made "in connection with the giving of legal advice to the client". Sections 13(2) of the PPP Act excludes communications in furtherance of any criminal purpose.

5.1. LPP and how it relates to Due Diligence

Accepting that neither the Authority, nor the Law Society as its agent, can have access to items subject to legal privilege, to what extent do communications made for the direct purpose of compliance with the Code attract legal professional privilege, and if so, to what extent?

Due diligence under the Code requires the client and the advocate to focus upon:

(1) the identity of the client;
(2) the identity of the beneficial ownership of the client;
(3) the nature of the contemplated transaction or instruction; and
(4) the source of any funds employed.
In most cases some, if not all, of the source of the information in relation to the above matters will be the client. In relation to the verification of such information, it may be difficult to disentangle information from the client from confirmations received from third parties.

Lawyers should note that the definition of "items subject to legal privilege" within Section 13 of the PPP Act refer to "communications made in connection with legal advice", and not simply communications for the purpose of giving legal advice. A communication designed to facilitate the obtaining of legal advice from an advocate, for instance by ensuring compliance with the Code, is likely to be a communication connected with providing and obtaining advice, even if the communication in question does not contain the legal advice itself.

Lord Carswell, in *Three Rivers District Council and Others v Governor and Company of the Bank of England* (No 5) (HL) 2005 1 AC 610 approved the principle affirmed in *Minter v Priest* [1929] 1 KB 655 that “all communications between a solicitor and his client relating to a transaction in which the solicitor has been instructed for the purpose of obtaining legal advice will be privileged, notwithstanding that they do not contain advice on matters of law and construction, provided that they are directly related to the performance by the solicitor of his professional duty as legal advisor of his client.” There is no reason to think that an Isle of Man Court would take a different approach to legal advice privilege in the Isle of Man.

As stated, that is not to say that all communications between a client and a lawyer are privileged. Case law supports the view that privilege does not extend to all information which a lawyer knows about his client. For example, it has been stated that legal advice privilege does not protect the conveyancing documents by which land is transferred from one person to another, or the client account ledger which a solicitor maintains in relation to his client’s money, or any appointment diary or record of time on an attendance note, time sheet or fee record, relating to the client. Nor does it extend to all information which a lawyer knows about his client (in one case it was said that “the privilege does not extend to matters of fact which the attorney knows by any other means than confidential communication with his client, even though if he had not been employed as attorney, he probably would not have known them”).

5.2. How Can an Advocate demonstrate compliance with the AML/CFT Legislation, whilst respecting legal privilege?

Although each engagement with a client should be considered within its own context and on its own merits, information relating to the name of the client, nationality, date of birth and gender of the client, the standard identification documents such as passport, driving licence, utility bills or local tax documents, and possibly verification material from third parties, are unlikely to be items subject to legal privilege.

Advocates will undoubtedly be asked to demonstrate compliance with the Code (and other AML/CFT legislation) by producing evidence that they obtain and retain information on the identity of their clients and any beneficial owner, verify the identity of their clients and any beneficial owner and undertake a client risk assessment and ongoing monitoring. Advocates should endeavour to be as open and transparent with the Authority (or its agents) in demonstrating their compliance in respect of these matters, whilst respecting any right to legal privilege which the client is entitled to claim.
Information, and the verification documentation, which evidences the identity of a client should rarely cause a problem. More detailed information relating to the nature and purpose of the relationship with the client, where such information is also confidential, may, and usually will, attract legal privilege, if the communication attracts litigation privilege and/or is made in connection with seeking advice as to what should prudently and sensibly be done in a relevant legal context.

Lawyers should ensure the due diligence materials in respect to which a client is entitled to claim legal privilege is kept separate to any due diligence materials which are open to inspection under the DBRO. In a similar vein, the procedural paperwork used by advocate firms to record the nature and purpose of an instruction, or to record the client’s risk assessment, should not contain information which discloses items subject to legal privilege. This does not mean that it is impossible to demonstrate that the nature and purpose of instructions or the client risk assessment is recorded, for example it may be possible to summarise such matters in a separate record using generic information which does not disclose confidential privilege communications. In this way it may be possible to indicate the nature and purpose of an instruction in general terms, without disclosing confidentially privileged information, but each case will need to be considered on its own merits.

The approach taken on site visits by the Authority, and accordingly by the Law Society as its agent, is likely to become clearer once such visits commence. The Authority understands that lawyers are compelled to respect the right of their clients to assert legal privilege in appropriate circumstances. In the unlikely event that the Authority was to challenge a decision taken by an advocate (on behalf of the client) to withhold access to certain due diligence information or documentation on the grounds of legal privilege, lawyers should raise the issue promptly with their client. The privilege belongs to the client and not to the advocate. It may be possible that the client, properly advised, may be prepared to provide a limited waiver to allow inspection, but in such circumstances steps may need to be taken to ensure that the waiver is properly worded and subject to appropriate safeguards. However, the client should be under no compulsion to waive legal privilege if he does not wish to do so, and as stated above, no adverse inference can be drawn from a client exercising his right to maintain a proper claim to privilege.

It is important to ensure that clients understand the proper boundaries to communications that can and cannot attract legal privilege. Ultimately if there was a challenge to the non-disclosure of information or documentation under the DBRO on the grounds of legal privilege, any proceedings to enforce disclosure would need to involve the client whose right to privilege was being challenged. For this reason it is important that lawyers properly advise clients as to what information and documents provided as part of the client due diligence procedures under the Code are likely to be disclosed and to consider what can properly attract a claim to legal privilege and will not be disclosed without the consent from the client. If the advocate is in doubt as to whether or not communications are subject to legal privilege, and disclosure under the DBRO is requested, the client may need to be advised to take separate legal advice.
6. Case Studies

The typologies below are real life examples of risks that have crystallised causing losses and/or sanctions (civil and criminal) against the legal professional:

6.1. Misuse of client account I

An employee working in a very small law firm in Australia received an email from a web-based account referring to a previous telephone conversation confirming that the law firm would act on the person’s behalf. The ‘client’ asked the employee to accept a deposit of AUD 260 000 for the purchase of machinery in London. The ‘client’ requested details of the firm’s account, provided the surname of two clients of a bank in London, and confirmed the costs could be deducted from the deposit amount. The details were provided, the funds arrived and the ‘client’ asked that the money be transferred as soon as possible to the London bank account (details provided) after costs and transfer fees were deducted. The funds were transferred, but no actual legal work was undertaken in relation to the purchase of the machinery.

The transfer of the funds to the law firm was an unauthorised withdrawal from a third party’s account. This specific case was brought to the attention of the Office of the Legal Services Commissioner (OLSC) in Australia, which took the view that the law firm had failed to ensure that the identity and contact details of the individual were adequately established. This was particularly important given the individual was not a previous client of the law firm. The employee – proceeding on the basis of instructions received solely via email and telephone without this further verification of identity – was criticised. The OLSC also found that the law firm failed to take reasonable steps to establish the purpose of the transaction and failed to enquire into the basis for the use of the client account.

The high risk indicators from this case include:

- the client avoiding personal contact without good reason,
- the client is willing to pay fees without the requirement for legal work to be taken; and,
- client asks for unexplained speed.

6.2. Misuse of client account II

A Quebec lawyer received approximately USD 3 million in American currency from a Montreal businessman, which he deposited into the bank account of his law practice.

The lawyer then had the bank transfer the funds to accounts in Switzerland, the United States, and Panama. In Switzerland, another lawyer, who was used as part of the laundering process, transferred on one occasion USD 1 760 000 to an account in Panama on the same day he received it from the Canadian lawyer. When depositing the funds in Canada, the Quebec lawyer completed the large transaction reports as required by the bank, fraudulently indicating that that the funds came from the sale of real estate.
A police investigation into the Quebec lawyer established that these funds were transferred to a reputed Colombian drug trafficker linked to the Cali Cartel. In their attempts to gather further information about the suspicious transactions, bank officials contacted the lawyer about the funds. The lawyer refused to provide any further information, claiming solicitor-client confidentiality. The bank subsequently informed the lawyer that it could no longer accept his business.

The high risk indicators from this case include:

- use of a disproportionate amount of cash;
- use of client account with no underlying legal work;
- funds sent to one or more countries with high levels of secrecy; and;
- client known to have connections with criminals.

6.3. Mortgage fraud

An individual in his early 20’s who worked as a gardener approached a legal professional to purchase several real estate properties. The client advised that he was funding the purchases from previous sales of other properties and provided a bank cheque to pay the purchase price.

The client then instructed a different set of legal professionals to re-sell the properties at a higher price very quickly after the first purchase. The properties were sold to other people that the client knew who were also in their early 20’s and had similar low paying jobs.

The client had in fact obtained mortgages using false documents for these properties, generating the proceeds of crime. The multiple sales helped to launder those funds.

The high risk indicators from this case include:

- disproportionate amount of private funding which is inconsistent with the socio-economic profile of the individual;
- transactions are unusual because they are inconsistent with the age and profile of the parties;
- multiple appearances of the same parties in transactions over a short period of time;
- back to back property transaction, with rapidly increasing value;
- client changes legal advisor a number of times in a short space of time without legitimate reason; and;
- client provides false documentation.

6.4. Purchase through intermediaries

A Canadian career criminal, with a record including drug trafficking, fraud, auto theft, and telecommunications theft, deposited cash into a bank account in his parents’ name. The accused purchased a home with the assistance of a lawyer, the title of which was registered to his parents. He financed the home through a mortgage, also registered to his parents. The CAD 320 000 mortgage was paid off in less than six months.
The high risk indicators from this case include:

- disproportionate amount of private funding/cash which is inconsistent with the known legitimate income of the individual;
- associates of the client is known to have convictions for acquisitive crime; and;
- there are attempts to disguise the real owner or parties to the transaction.

6.5. Multiple purchase same bank

In 2008 a law firm employee was approached by three individuals who were accompanied by a friend to seek a quote to purchase three separate properties. They returned later that day with passports and utility bills and instructed the law firm to act for them in the purchases.

The clients asked for the purchases to be processed quickly and did not want the normal searches undertaken. They did not provide any money to the solicitors for expenses (such funds would normally be provided) but said the seller’s solicitors would be covering all fees and expenses. The clients said they had paid the deposit directly to the seller. The mortgages were paid to the law firm, which retained their fees and then sent the funds to a bank account which the law firm employee thought belonged to solicitors acting for the sellers. No due diligence was undertaken.

In fact the actual owners of the property were not selling the properties and had no knowledge of the transaction or the mortgages taken out over their properties. The mortgage funds were paid away to the fraudsters, not to another solicitors firm.

In 2010, the supervising solicitor was fined GBP 10 000 for not properly supervising the employee who allowed the fraud to take place and the proceeds of the funds to be laundered. The solicitor’s advanced age was taken into account as a mitigating factor in deciding the penalty.

The high risk indicators from this case include:

- transaction was unusual in terms of all three purchasers attending together with an intermediary to undertake separate transactions;
- failure to provide any funds for expense in accordance with normal processes; and part of the funds being sent directly between the parties;
- client showed an unusual familiarity with respect to the ordinary standards provided for by the law in the matter of satisfactory client identification; and;
- client asked for short-cuts and unexplained speed in completing a transaction.

6.6. Use of companies / trusts I

A criminal involved in smuggling into the United Kingdom set up a Trust in order to launder the proceeds of his crime, with the assistance of a collusive Independent Financial Adviser (IFA) and a Solicitor, who also appeared to be acting in the knowledge that the individual was a criminal. The Trust was discretionary and therefore power over the management of the fund was vested in the Trustees, namely the criminal, his wife and the IFA.
The criminal purchased a garage, which he transferred directly to his daughter (who also happened to be a beneficiary of the Trust). She in turn leased the garage to a company. The garage was eventually sold to this company, with the purchase funded by a loan provided by the Trust. The company subsequently made repayments of several thousand pounds a month, ostensibly to the Trust, but in practice to the criminal. Thus the criminal who had originally owned the garage probably maintained control despite his daughter’s ownership. Through controlling the Trust he was able to funnel funds back to himself through loaning funds from the Trust and receive payments on that loan.

The high risk indicators from this case include:

- creation of a complicated ownership structure when there is no legitimate or economic reason;
- the ties between the parties of a family nature generate doubt as to the real nature or reason for the transaction; and;
- the client is known to be currently under investigation for acquisitive crimes.

6.7. Use of companies / trusts II

From 2000 to 2008, Jennifer Douglas, a U.S. citizen and the fourth wife of Atiku Abubakar, former Vice President and former candidate for President of Nigeria, helped her husband bring over USD 40 million in suspect funds into the United States through wire transfers sent by offshore corporations to U.S. bank accounts. In a 2008 civil complaint, the U.S. Securities and Exchange Commission alleged that Ms. Douglas received over USD 2 million in bribe payments in 2001 and 2002 from Siemens AG, a major German corporation.

While Ms. Douglas denies wrongdoing, Siemens has already pled guilty to U.S. criminal charges and settled civil charges related to bribery. Siemens told the Senate Permanent Subcommittee on Investigations that it sent the payments to one of Ms. Douglas’ U.S. accounts. In 2007, Mr. Abubakar was the subject of corruption allegations in Nigeria related to the Petroleum Technology Development Fund. Of the USD 40 million in suspect funds, USD 25 million was wire transferred by offshore corporations into more than 30 U.S. bank accounts opened by Ms. Douglas, primarily by Guernsey Trust Company Nigeria Ltd., LetsGo Ltd. Inc. and Sima Holding Ltd.

The U.S. banks maintaining those accounts were, at times, unaware of her Politically Exposed Person (PEP) status, and they allowed multiple, large offshore wire transfers into her accounts. As each bank began to question the offshore wire transfers, Ms. Douglas indicated that all of the funds came from her husband and professed little familiarity with the offshore corporations actually sending her money. When one bank closed her account due to the offshore wire transfers, her lawyer helped convince other banks to provide a new account.

The high risk indicators from this case include:

- client requires introduction to financial institutions to help secure banking facilities;
- client has family ties to an individual who held a public position and is engaged in unusual private business given the frequency or characteristics involved;
• involvement of structures with multiple countries where there is no apparent link to the client or transaction or no other legitimate or economic reason; and;
• private expenditure is being funded by a company, business or government.

6.8. Powers of attorney

A legal professional was asked to prepare a power of attorney for a client to give control of all of his assets to his girlfriend, including power to dispose of those assets. The legal professional then prepared a deed of conveyance under which the girlfriend transferred all of the property to the client’s brother and sister. The legal professional had just secured bail for the client in relation to a drug trafficking charge.

The high risk indicators from this case include:

• a power of attorney is sought for the disposal of assets under conditions which are unusual and where there is no logical explanation – it would have to be very exceptional circumstances for it to be in the client’s best interests to allow them to make themselves impecunious;
• unexplained speed and complexity in the transaction; and;
• client is known to be under investigation for acquisitive crime.

Based on case studies taken from the FATF Report on Money Laundering and Terrorist Financing Vulnerabilities of Legal Professionals (June 2013).