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Draft Money Laundering Regulations 2017: What to look out for and where to start

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At the time of writing this article, the key UK draft response to the Fourth AML Directive; the Money Laundering, Terrorist Financing and Transfer of Funds (Information on Payer) Regulations 2017 ('the Regulations') have been available for a little over four weeks. They were finally published with an attendant consultation on 15 March 2017.

The UK is under an obligation to bring the requirements of the Directive into force by 26 June 2017, though, at the time of writing, a snap General election has been announced for 8 June 2017 and it is unclear, what, if any effect this will have on the timetable.

In light of the consultation, and the potentially hurried timeframe, it is difficult to say how much, if anything might be changed in the draft. However, firms need to be making preparations and so a round-up of the key issues, even though in draft for the time being should be helpful.

Those key issues start with the overall length and detail of the Regulations; 106 pages long and more than double the number of Regulations compared to the Money Laundering Regulations 2007 they are due to replace. Already, published responses to the consultation have spoken of gold-plating and duplication of regulation. Even the title is lengthy; The Money Laundering, Terrorist Financing and Transfer of Funds (Information on Payer) Regulations 2017. What then are the key headlines?

Risk Assessment

The requirement for relevant businesses to carry out a risk assessment has got to be the starting point. This is particularly crucial given that everything else you do to implement the requirements flow from your risk assessment of your firm and its operations, structure, clients and even staff.

Everyone in the regulatory chain, from HM Treasury and HMRC, to the supervisors, including the Solicitors Regulation Authority will have to undertake a similar process , but Regulation 18 requires that law firms 'must take appropriate steps to identify and assess the risks of money laundering and terrorist financing to which its business is subject.' What is more, not only must that assessment be provided to the SRA on request, but also the methodology and detail behind it; 'the information on which that risk assessment was based' unless notified it is not necessary. Firms really need to be getting under way with this process as soon as possible.

The next step is to establish and maintain policies, controls and procedures which address the risks you have identified in the risk assessment, in a risk-based and appropriate manner. In other words, having identified the risks, we need to show how what we do addresses and mitigates the risks identified.

Key roles

The policies, controls and procedures are much as you would expect and include the old Regulation 20 requirements to apply client due diligence measures, together with the monitoring and management of compliance and internal communication of policies.

The inclusion of the term 'controls' is important as there is an increased focus on the area of internal controls in Regulation 21. This fits with more control around who can be an owner or manager of a business conducting relevant business, nothing new to law firms of course, to a responsibility for assessing and screening those within our firm involved in compliance with the Regulations.

This appears to include a clear indication that businesses will have to provide a named, senior individual who has responsibility for compliance with the Regulations. Regulation 21(1)(a) requires the appointment of a board level or equivalent individual in this role. In addition, firms will have an apparently enhanced obligation to train employees and agents and to screen relevant employees and agents. Responses to the consultation are currently under consideration and points have been made, for example by the Law Society on this apparent widening to include agents. Nevertheless, it is clear that you will need to show you have assessed the skills and expertise of those involved in say, the CDD process as well as their conduct and integrity.

Given the already rigorous system of regulation surrounding law firms, it is hoped that some of these requirements might be fulfilled by the SRA processes already in place.

Audit

Regulation 21, Internal controls goes on to require the setting up of an independent audit function to monitor compliance and effectiveness of systems. The days of firms leaving their policies year on year without review and still containing references to SOCA may be about to come to an end.

'Super' Regulator

Much has been made of the large number of supervisors appointed in the UK and the perceived inconsistencies between the application and policing of different sectors within the regime. Transparency International, amongst others had been lobbying for a more effective regulatory regime (see their report; Don't Look, Won't Find Weaknesses in the Supervision of the UK's Anti -Money Laundering Rules). The Government has proposed the creation of the Office for Professional Body Anti-Money Laundering Supervision (OPBAS) to 'help improve the overall standards of supervision and ensure supervisors and law enforcement work together more effectively' as an over-arching regulatory body.

Training

Apart from the need to screen relevant employees by assessing the skills and expertise of those involved in compliance with the Regulations, the training requirement remains pretty much as it was, under the old Regulation 21. That meant firms had to ensure awareness of the law relating to both money laundering and terrorist financing as well as providing regular training in how to recognise and deal with transactions which may be related to them. There is an addition in the shape of a requirement to make them aware of the law relating to data protection. This is a new, though not altogether surprising development.

Data protection

There is a natural tension between the need to undertake extensive research into someone's background and for example, their right to privacy and for their data not to be retained for any longer than is necessary. The Regulations maintain the requirement to keep CDD material for five years from the end of the business relationship (Regulation 39), but Regulation 40 then covers data protection. This makes clear that CDD information must not be used for wider purposes.

Beneficial Ownership Information

An obligation on UK companies and trusts to provide those conducting due diligence under the Regulations with appropriate beneficial ownership information relating to the entity is a new inclusion. This requirement can be found in Part 5 of the Regulations. This could prove a useful addition for firms undertaking CDD, though from a practical perspective, the ability to sufficiently understand ownership and control most frequently arises in overseas entities. Nevertheless, it is not unhelpful, particularly relating to trusts.

Customer Due Diligence and Ongoing Monitoring

Unlike the rules they are designed to replace, the Regulations do not separate these obligations into two separate areas, but more appropriately combine them in Regulation 28. They are, of course, part of the same continuous process and this is made clearer by ensuring they appear together.

Group and International Implications

If a firm is part of a group or International practice, and a relevant parent undertaking(as per the Companies Act 2006, Section 1162 definition), Regulation 20 imposes an obligation to ensure that the policies, controls and procures required under Regulation 19(1), apply to all its subsidiary undertakings, including subsidiary undertakings located outside the United Kingdom, and to any branches it has established outside the United Kingdom.

Although firms have always had to be cognisant of the risk of passporting in clients and matters from other offices with less stringent controls, this could create a real challenge for firms.

As the greater number of Regulations suggest, there is a great deal more detail to get to grips with in the Regulations. The application of that detail should be dictated by the findings under the risk assessment. Accordingly, those tasked with implementation should get their 'to-do' lists ready:

- Appoint a board level (or equivalent(individual responsible for compliance
- Prepare a documented risk assessment
- Check that your system of risk profiling on client/matter engagement is working
- Review your policies and procedures in light of the risk assessment
- Refresh your training
- Check everyone understands how to report and who to report to
- Check your system for keeping an audit trail – if it's not written down, it didn't happen.

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