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Specialists in Professional Regulation

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law firm compliance advice and training

Coronavirus Crisis Compliance Clinic for Birmingham Law Society

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Summary of questions and answers from the recent Zoom session given by Jayne Willetts, Bronwen Still & Matt Moore

Question 1

I am the COLP of a medium sized firm with three offices. Approximately 90% of our staff are now home working. What are the compliance issues that I need to address?

In terms of home working, these are the two key issues which the SRA always considers paramount:

(i) Client confidentiality - Code of Conduct - standard 6.3 "you keep the affairs of current and former clients confidential…"

Things to consider

- reinforcing the importance of client confidentiality with risks to think about for all homeworkers and how they might deal with them e.g.
    - keeping laptops, papers etc secure at home, preferably in a room which can be locked but otherwise making sure laptops are locked when not in use and documents not left unattended
    - ensuring phone calls cannot be overheard

(ii) Supervision – Code of Conduct requirements to think about are these:

- Standard 2.2 “You keep and maintain records to demonstrate compliance”
- Standard 4.4 “you have effective systems for supervising clients’ matters”

Possible arrangements to make:

- having a plan in place with clear communication lines laid out for homeworking - probably a good idea to have one individual to coordinate
- ensuring that there are clear instructions for all staff about the structure that will operate whilst homeworking – who they report to, and when – who will be in touch with them and when – also sensible to have a nominated person or “buddy” assigned for those to contact who may be struggling with their work
- line managers/others need to keep an eye not just on work but more generally staff welfare and how they are coping – some may have particularly stressful homeworking conditions or finding isolation hard to cope with
- retaining social contact through weekly meetings/social platforms – keeping a team spirit going

Question 2

We are seeing very few new client enquiries but have a problem when we do in that we are not meeting them to inspect their documents for money laundering checking purposes. Do we have to turn the work away until we are able to open the office again?

The main point to take on board is that seeing an individual client face to face who is not known to you, or to someone else in the regulated sector who is willing to certify their identity, is clearly preferable for very obvious reasons, and this is the basis on which the great majority of firms operate in normal times. These are not, however, normal times and fortunately the professional guidelines do not lay down a mandatory requirement for a face-to-face meeting.

The best authority on this is para 4.9.1 of the Legal Sector Affinity Group AML Guidance which states that although “in most cases” face to face verification should enable most clients to meet the requirements it follows that for some it will not do so, nor is it essential to do so in most other cases. The same section also states that in some instances e-verification in its own right may be sufficient, though it does also acknowledge at para 4.3.3 that this is capable only of proving that someone of this identity exists, and not necessarily that you are dealing with that person.

Taking all of this into account you might therefore fairly modify your normal procedures in current circumstances with a three, or perhaps four, stage process.

1: You ask the client to send you a copy of their normal documents – ideally a photocopy but possibly a photo via their or a relative's phone. If this is legible you should print this off for your file. An alternative might be to ask them to hold up the documents during a Skype or Zoom call with their face also in vision which you would again note however possible.

2: You then commission an e-verification check on the client(s) which will mean that their documentary details such as their passport number may be checked electronically.

3: If that check produces no concerns you might also make a point of sending a letter to the client at their given address and require some form of acknowledgement to be sent to you by post. This would be on grounds that a fraudster would find it difficult to intercept such items via the postal system.

4: Finally, and as an optional fourth step, you could then request that the client follows this up by providing a sight of their documents in the normal way at a later stage of the transaction if you do meet with them, as long as other risk factors do not suggest otherwise. Many transactions may be completed before that will be possible, however.

An important rider to this, however, is that all that you do by way of CDD must always be subject to your risk assessment in accordance with the Money Laundering Regulations 2017. A good example of where risk considerations would be likely to make this alternative process inadvisable would be matters involving a sale of a vacant high value property as in the *Dreamvar (UK) Ltd v Mishcon de Reya* and other such related cases. There are also various situations where "enhanced due diligence" is required, as where the value of the transaction is one that you would deem to be "unusually high" for the firm or the client, in which case suitable additional measures would need to be taken.

Remember also that establishing the client's identity is only one of the aspects of the CDD process. You must also be satisfied that you understand the "purpose and intended nature" of the instructions and so you must always give careful thought as to whether anything illegal might be intended. See MLR 2017 r.28(2).

Finally, if deviating from your normal practice in this way while the current restrictions on movement apply, you might also request sign-off on a case by case basis by your MLRO, MLCO or perhaps Head of Department.

Question 3

We are worried about our firm's finances. We are putting in place cost cutting measures and furloughing staff. Do we need to report to the SRA?

The duty to inform the SRA of financial difficulty appears at Rule 3.6 Code for Firms – *"notify the SRA promptly of any indicators of serious financial difficulty"*

There is no definition of *"serious financial difficulty"* in the 2019 Standards & Regulations and as yet no guidance.

Under the 2011 Code *"serious financial difficulty"* was defined as *"an inability to pay PII insurance and or rent or salaries or breach of bank covenants"*

All firms will be suffering financial pressures but whether to report serious financial difficulty will be a matter of degree. By way of example - a firm which normally pays its PII insurance premium in a lump sum would not need to report if during the pandemic it needs to pay by credit instalments. However, if the firm could not obtain credit and had no other means of paying it would need to report. Similarly, if a firm reaches an agreement with its landlord for a deferral of rent this would not need to be reported but if the landlord refused and subsequently took possession proceedings then reporting would be necessary. There will be firms awaiting payment of government coronavirus grants which will mean that their finances are precarious for a very short time but once the grant is received things are on a better footing – again no need to report as a temporary difficulty averted by government help.

It is best to keep a log of the way in which your firm's finances develop – so, if the worst happens, and you have to report serious financial difficulty, you can justify why you did not do so earlier. Also bear in mind that any SRA investigation is unlikely to occur until the lockdown has ended so there will be a time to take stock once we are permitted to return to our offices and resume practice again.

Question 4

We're trying to use our spare time at the moment to get our manuals up to date. What are the main issues from the Fifth AML Directive that we should be looking out for?

The Amendment Regulations which took effect on the 10th January worked by making certain amendments to the MLR 2017 and were intended to address the Fifth EU AML Directive. The 10th January was the last date under EU law by which member states had had to address the new requirements but there was very little advance notice of them as a result of the December election and then Christmas and the New Year. The SRA made it clear at the time, however, that they would expect the new provisions to be addressed within a very short timescale. They should certainly feature in firms' policies by now.

The need for AML risk assessments under r.18 has received a good deal of attention from the SRA of late. There is now an additional requirement to AML risk assess "new products, new business practices … or new technology" at r.19(4)(c), as would be the case if opening up new offices or service areas. Remember that risk assessments must be written and open to inspection by the SRA as the supervisory body if required.

Other than this the impact of the new regulations will be greater in commercial firms than others. In simple terms the main new requirements are as follows, with references to the amended parts of the MLR 2017.

- There is a new specific duty when forming a business relationship with a company or other such entity to understand its ownership and control structure. This has long been regarded as best practice in any event and is one of the areas where firms may well have been compliant already (r.28(3)).

- The issue of beneficial ownership is also addressed. When first instructed by a company or limited liability partnership (forming a 'business relationship' with them) the firm must consult the PSC register and they will then be under an obligation to inform Companies House of any discrepancies that emerge in relation to the identities of the beneficial owners. In addition to undertaking its initial CDD check on such clients the wording at the new r.30A also extends this obligation to occasions when discrepancies also "otherwise become available.." in the course of carrying out (the firm's) duties under these Regulations", and so when undertaking ongoing monitoring as required by r.28(11). This new duty is stated to be subject to legal professional privilege, however, so pending definitive guidance on this the client's agreement to making such a report should be obtained.

- The other main area where there are developments of note is in relation to enhanced due diligence (EDD). There is an apparently minor but potentially significant change of wording here in that whereas the MLR 2017 required EDD where a transaction was 'complex *and* unusually large' this is now changed to 'complex *or* unusually large'. Quite what is required to trigger this requirement must inevitably be judged on a firm by firm basis, rather than on some form of objective basis for the profession as a whole: what amounts to a complex or unusually large transaction for a small commercial department operating in a general high street firm will inevitably be very different to what it would be for a major City practice. We would recommend that you amend your policy to state what level of consideration must be involved before EDD is required on this basis within your firm.

- Within the area of EDD there is also more emphasis on dealings with what are regarded as high-risk territories. For a list of all such territories see the Law Society practice note on this at https://www.lawsociety.org.uk/support-services/advice/articles/european-commission-list-of-high-risk-third-countries/. Since Pakistan, Sri Lanka and Trinidad and Tobago are included on this list this may be of greater relevance than might seem to be the case depending on the make-up of your client base. For the amount of involvement required of an individual or business involved with any of the listed states see the new r.33(3).

- In relation to EDD in general a revised r.33(3A) now sets out a list of the EDD measures that must be undertaken. This includes obtaining additional information on the client and any beneficial owners, the source of funds and the reasons for the transaction, and then the approval of 'senior management' will be required – the MLRO or MLCO, for example. In essence a wider degree of checking is required as to all of surrounding circumstances of the matter as well as more on the client and the source of funding.

Question 5

Do you have any advice on the use of social media by staff during the lockdown?

With more time on our hands, the use of social media has increased exponentially during the lockdown. No-one has the chance to express opinions at the water cooler or the coffee machine in the office or in the pub after work in a way that one might do normally with trusted colleagues.

Venting views on social media can be very risky. The national media has reported upon a law firm dismissing a left leaning paralegal who posted unpleasant comments about the Prime Minister *"deserving"* his recent illness.

Now may be the time to remind staff of your social media policy and the fact that the SRA can take action even if posting in a personal capacity. The relevant Principle is Principle 2 that you are required to act *"in a way that upholds public trust and confidence in the solicitors' and in legal services provided by authorised persons".* In shorthand, we must not damage the reputation of the profession. It is preferable to avoid disclosing the name of the firm and a professional qualification on a personal social media profile so as not to provide a link to the profession and the firm. But better still, staff need to be reminded that care and restraint are the watchwords when posting on social media platforms. If they can't say anything kind don't say anything.

Question 6

Our firm is taking on a new director. What do I need to tell the SRA and do I need to complete any forms?

If you are making certain changes to your firm, you need to notify the SRA in advance. Usually, this involves completing the relevant form. Go to "Firm based authorisation/existing firms" on the SRA's website.

Events which require notification and form filling:

- Changing the legal entity of your firm
- Applying for emergency approval of your firm or compliance officers
- Changing your compliance officer
- Adding a new manager and/or owner
- Electing to become a Licensed Body
- Your firm has succeeded another
- Your firm is providing financial services
- When to submit an accountant's report
- Applying for an Accountant Report Waiver
- Your firm is using a third-party managed account (TPMA)
- Making changes to your Anti Money Laundering (AML) authorisation

For a new deemed approved manager (solicitor, REL or RFL) you need to add their details in the firm's MySRA account.

For a deemed approved owner, you need to complete form FA4.

Not deemed approved manager or owner (other lawyer/non-lawyer), they would need to complete form FA2.

If the firm carries out work that is subject to the MLRs, then as a BOOM (Beneficial owner, officer or manager), they would also need to be approved as such, on form FA10b. Also need to acquire a basic DBS check as proof that they do not have any criminal convictions which would prevent them becoming a BOOM.

Question 7

Do you have any advice about Accounts Rules compliance during the lockdown?

Rule 8 of the SRA Accounts Rules contains the requirements for client accounting systems and controls and is prefaced by:

You keep and maintain accurate, contemporaneous, and chronological records

Firms must keep up to date with bookkeeping during the lockdown to avoid Accounts Rules breaches and to protect the financial future of the firm. It is now more essential than ever to have a day by day hour by hour picture of the firm's finances both client account and office account. Now may also be the time for the COFA to become better

acquainted with the workings of the accounting software. Also bear in mind that remote working could provide an ideal opportunity for employee fraud. Surprise checks often work better than regular pre-planned ones. Very regular reconciliations of both client and office account can provide a simple and effective method of checking. This aspect of coping during the lockdown is probably the most important one as the SRA is unlikely to treat leniently any shortfalls on client account even during the lockdown.

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