Law Society of Scotland

Report Stage Briefing

Criminal Finances Bill - Report Stage Briefing

23 November 2016

Introduction

The Law Society of Scotland is the professional body for over 11,000 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 rule 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 Treasury-designated AML supervisory authority for solicitors in Scotland, our engagement with the topics of anti-money laundering and counter terrorist financing serves the public interest by assessing compliance with requirements and encouraging continuous improvement within the profession. Our activities include:

- Our regulatory regime requires all firms holding client money to certify compliance with the money laundering regulations on a six monthly basis. The accuracy of these certifications is subsequently verified through our extensive inspection programme which covers 25% of firms annually.
- We also undertake proactive, intelligence-led inspections of specific firms where suspicious activity has been detected
- Working with firms to promote improved AML compliance where necessary and dealing with non-compliance.
- We perform AML risk assessment of large member firms, who will be subject to AML audit starting in 2017
- Holding educational events featuring contributions from cross-sectoral AML subject matter experts.
- Providing helpline services for solicitors in practice, including AML queries.
- Active membership of the Anti-Money Laundering Supervisors Forum and Legal Affinity Group.
- Regular engagement with the UK government to contribute to AML/CTF developments.

This briefing is provided in advance of the Report Stage of the Criminal Finances Bill. We have commented on specific parts of the Bill where we feel we can usefully contribute.

Summary

In respect of anti-money laundering, the Society has made significant efforts to ensure that Scottish solicitors fully comply with their Anti-Money Laundering obligations under the Money Laundering Regulations 2007, Proceeds of Crime Act 2002 and Terrorism Act 2000. These requirements are now embedded within the Scottish profession but subject to continuous monitoring.

By way of background, in June 2016 the Society responded to the consultation issued by Home Office/HM Treasury: Action Plan for anti-money laundering and counter-terrorist finance[1]. At that time the Society liaised with the Law Society of England and Wales (LSEW), and the Law Society of Northern Ireland regarding the commissioning of the Counsel Opinion which underpinned the consultation response produced by the LSEW[2]. The Society endorsed the LSEW response and provided some additional comments contained in a supplemental paper. We have also provided a full response to the recent government consultation on the 4th Money Laundering Directive

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Clause 10: Sharing of Information within the regulated sector

The Society is supportive of measures which allow better information sharing between persons undertaking regulated undertakings within the regulated sector. If a framework is intended to be voluntary, we would be supportive of measures which do not seek to impose any additional compulsory reporting obligations upon solicitors.

The current drafting of Clause 10 (insert new section 339ZB to the Proceeds of Crime act 2002) allows disclosure within the regulated sector provided that Conditions 1 to 4 are met. Conditions 1 to 4 are cumulative and each of the Conditions must be satisfied before the disclosure can be made. A disclosure can be either requested by the NCA, or requested by another person carrying out a regulated undertaking within the regulated sector. In both of those circumstances, a disclosure may only take place after a notification has been made to the NCA[3].

We previously noted that the principal dialogue should be between law enforcement and the private sector and that clear assurances are required regarding the legality of information sharing within the private sector. Law enforcement should consider an increased role in alerting other parts of the private sector in response to information it receives. This would minimise any remaining risks arising from increased data sharing within the private sector such as those of data protection breaches, defamation and risks to the personal safety of reporters.

In addition, matters relating to professional privilege will need to be considered. Professional privilege typically arises in connection with information obtained by a professional legal adviser, otherwise than for

[1] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/517993/6-2118-Action_Plan_for_Anti-Money_Laundering__print_.pdf
[2] http://www.lawsociety.org.uk/policy-campaigns/consultation-responses/home-office-and-hm-treasury-consultation-on-the-action-plan-for-aml-and-cft-legislative-proposals/
[3] Clause 10 of the Criminal Finances Bill, insert new section 339ZB to the Proceeds of Crime Act 2002 at section 339ZB(4).

the purposes of committing a crime, from a client in connection with the provision of legal advice by the adviser to that person. It is suggested that any attempt to legislate against privilege should be opposed by a government which values the rule of law.

Obligation to Report Serious Organised Crime: Section 31 of the Criminal Justice and Licensing (Scotland) Act 2010 ("the 2010 Act")

In Scotland the obligation to report to the National Crime Agency (NCA) through the Suspicious Activity Report (SAR) regime exists alongside the obligation under the 2010 Act for solicitors (and a wide array of other persons) to report knowledge or suspicion that another person is involved in serious organised crime. Under the 2010 Act, the offence of involvement in serious organised crime is committed where a person knows suspects or ought reasonably have known or suspected that an action would enable or further the commission of serious organised crime.

Reports under the 2010 Act are not made to the NCA and in certain circumstances (e.g. where a Scottish solicitor knows or suspects the laundering of the proceeds of crime), Scottish solicitors would be required to make two separate disclosures one to the NCA under the SAR regime and one to a "constable" as required under this legislation. However Section 31 does not apply where the information is received by the solicitor in "privileged circumstances" such as when legal advice is being given to a client.

The Society is committed to aiding efforts to reduce money laundering and serious organised crime. However, given the dual reporting requirement in Scotland, the Society would be supportive of any amendment to the SAR regime which alleviated the demands placed on Scottish solicitors while not undermining efforts to tackle money laundering and terrorist financing.

Proposed Amendments – Scottish Limited Partnerships (SLPs)

Introduction

The Law Society of Scotland has been advised that an amendment (NC1) to the Criminal Finances Bill is to be proposed to require the Secretary of State to review the extent of financial criminal activity associated with SLPs and to set out what steps the Government intends to take to prevent SLPs being used for criminal purposes.

SLPs are commonly used for a wide range of legitimate purposes and are an important and useful business entity. However, we recognise that in some recent well-publicised cases it has been suggested that SLPs have been set up to be used for money laundering purposes.

We are willing to work with the Government to find a way to resolve this issue and to ensure that SLPs can continue to be used for legitimate purposes.

Below, we set out some background on the nature and use of SLPs, in order to inform discussion on this subject.

Nature of Scottish limited partnerships & public disclosure

Limited partnerships are a sub-category of partnerships. All partnerships are formed under the Partnership Act 1890, with some special rules applying to limited partnerships under the Limited Partnerships Act 1907. These Acts apply to both Scottish and English partnerships and Scottish and English limited partnerships are accordingly the same, except that Scottish partnerships and limited partnerships have separate legal personality from their partners whereas English partnerships and limited partnerships do not have such separate legal personality.

All partners in a partnership are normally liable for all of the debts of the partnership (whether as a separate Scottish legal person or as the partners collectively in an English partnership). In a limited partnership the liability of the limited partners is limited to the amount of the capital they have agreed to contribute, similar to the liability of shareholders in a company. Limited partners are not permitted to be involved in managing the partnership in which they have invested on pain of losing their limited liability and the limited partnership must have at least one general partner who carries out that management and is liable for all partnership debts.

Partnerships are formed by agreement among partners and can be formed as limited partnerships by registration at the UK Companies Office of details of all partners, capital contributions of limited partners, the name of the partnership, its principal place of business, the general nature of its business and the intended duration of the partnership. A fee of £20 is payable to make this registration and once registered a certificate of registration is issued by the Companies Office. A limited partnership will be Scottish or English by virtue of its principal place of business on formation. Changes to registered details of a limited partnership, such as changes to its partners, must also be registered at the Companies Office. This publicity is intended to ensure that those dealing with a limited partnership will not be misled as to its partners and their liability for partnership debts.

Current uses of Scottish Limited Partnerships

Partnerships and limited partnerships are very common business entities used for many legitimate purposes. Their operational flexibility and their tax transparency (i.e. partners rather than the partnership itself are taxable on partnership activity) are their principal advantages as business entities. In addition, the

separate legal personality of Scottish partnerships and limited partnerships can provide extra clarity when operating a business using a partnership.

Limited partnerships are a favoured business entity in many types of businesses and sectors, particularly where passive involvement of some participants in the business is important to that business. Both Scottish and English limited partnerships accordingly play a central role in the multi-billion pound funds industry both in the UK and worldwide, providing means to connect UK and foreign investors to businesses, shares, property and other assets in which they may wish to invest in the UK and elsewhere. The separate personality of SLPs means that they are particularly useful in this sector as they enable investments to be structured and grouped efficiently. Many jurisdictions worldwide (for example Luxembourg) seek to promote investment vehicles designed specifically to compete with Scottish and English partnerships; this is a critical and valuable market and policy makers should be conscious of the impact any changes might have on the UK's position in that market.

Another sector in which policy makers should be aware of the common use of Scottish limited partnerships is agriculture, where a great many Scottish farms are owned and operated using such partnerships. Again the possible unintended effects on this sector of changes that might be made to partnerships should be borne in mind.

Criminal use of Scottish Limited Partnerships

It is, of course, recognised that in some recent well-publicised cases, it has been suggested that SLPs have been set up to be used for money laundering purposes and these cases have presumably influenced the amendment proposed to the Bill. It may be that the issues pertinent to these cases are more to do with the way in which the SLPs were used by the criminals, rather than the fact that SLPs were used (as opposed to an alternative UK or foreign entity). We are keen to ensure that SLPs can continue to be used for legitimate purposes as discussed above and therefore would be happy to engage with the Government to identify the issues behind any criminal use of SLPs and find a way to resolve these issues. We suggest that any review should not focus solely on SLPs, but on how other relevant legal entities might be used for criminal purposes.

List of bodies to be consulted

The amendment requires the Secretary of State in conducting the review to consult with the Scottish Government, the National Crime Agency, the Serious Fraud Office, the Financial Conduct Authority, HMRC, interested third sector organisations and any other persons he deems relevant. However, it does not specifically require the Secretary of State to consult with industry bodies or the Department for Business, Energy and Industrial Strategy (BEIS); neither would be automatically caught under either 'interested third sector organisations' or 'any other person he deems relevant'.

Although ‘interested third sector organisations’ is not defined in the Bill or amendment, its meaning could be restricted to charities, community groups and similar organisations. Therefore, in addition to the bodies already listed in the amendment, the Secretary of State should be under an express obligation to consult with:

1. Industry bodies of relevant industries or sectors; and
2. The Department for Business, Energy and Industrial Strategy.

This would ensure that industry bodies such as the British Private Equity and Venture Capital Association (BVCA) and the Alternative Investment Management Association (AIMA) would be involved in the review. Further, BEIS should be consulted to ensure that the impact on businesses is fully considered and that policy is joined-up across departments.

Further discussion

The Law Society of Scotland would be happy to facilitate further discussion of the issues discussed in this briefing.

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