



Law Society  
of Scotland

# Anti-Money Laundering Supervisory Report 2021

February 2021



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## 1. Context to this report

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The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (MLRs) set administrative requirements for the anti-money laundering regime within the regulated sector.

Regulation 12 states that the regulations apply to 'independent legal professionals', that is:

*“a firm or sole practitioner who by way of business provides legal or notarial services to other persons, when participating in*

*financial or real property transactions concerning—*

*(a) the buying and selling of real property or business entities;*

*(b) the managing of client money, securities or other assets;*

*(c) the opening or management of bank, savings or securities accounts;*

*(d) the organisation of contributions necessary for the creation, operation or management of companies; or*

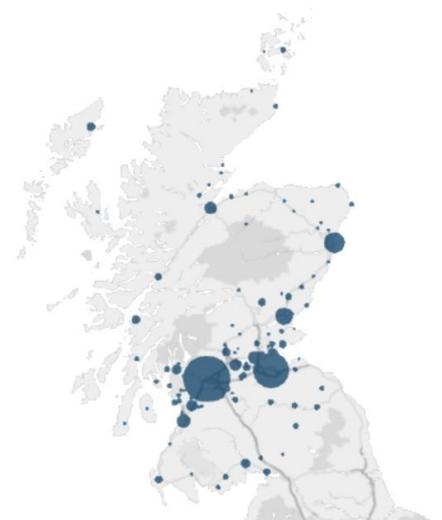
*(e) the creation, operation or management of trusts, companies, foundations or similar structures”*

The Law Society of Scotland is the Professional Body AML Supervisor for Scottish solicitors, with a remit across c. 750 firms spread throughout Scotland. AML supervisory authority status has been ratified by Her Majesty's Treasury through Schedule 1 of the MLRs and is discharged through the use of the Solicitors (Scotland) Act 1980.

### Our Regulatory Requirements

MLR r.46 set out the Society's primary duties and responsibilities in respect of AML supervision, including:

- Adopting a risk-based approach to the exercise of its supervisory functions,
- Basing the frequency and intensity of its on-site and off-site supervision on the risk profile of our supervised population
- Keeping a record in writing of the actions it has taken in the course of its supervision, and of its reasons for deciding not to act in a particular case;
- Taking effective measures to encourage its own sector to report breaches of the provisions of these Regulations to it



MLR r.49 sets out further duties upon the Society:

*“Self-regulatory organisations must make arrangements to ensure that:*

- *their supervisory functions are exercised independently of any of their other functions which do not relate to disciplinary matters;*
- *sensitive information relating to the supervisory functions is appropriately handled within the organisation;*
- *they employ only persons with appropriate qualifications, integrity, and professional skills to carry out the supervisory functions;*
- *contravention of a relevant requirement by a relevant person they are responsible for supervising renders that person liable to effective, proportionate, and dissuasive disciplinary measures under their rules”.*

*“Self-regulatory organisations must:*

- *provide adequate resources to carry out the supervisory functions;*
- *appoint a person to monitor and manage the organisation’s compliance with its duties under these Regulations”*

The Money Laundering and Terrorist Financing (Amendment) Regulations 2019 further prescribe that self-regulatory organisations such as the Society must also publish an annual report containing information regarding:

- measures taken by the self-regulatory organisation to encourage the reporting of actual or potential AML breaches
- the number of reports of actual or potential breaches received by that self-regulatory organisation
- the number and description of measures carried out by the self-regulatory organisation to monitor, and enforce, compliance by relevant persons with their obligations the MLRs, the Terrorism Act 2000 (TA) and the Proceeds of Crime Act 2002 (POCA)

This inaugural annual AML supervisory report has been produced as an interim step ahead of any future set reporting period agreed with Her Majesties Treasury (HMT) and the Office for Professional Body AML Supervision (OPBAS) and highlights the work we have undertaken in fulfilling our supervisory obligations under the regulations.

The Society also expects the report to develop further in the coming years as our supervisory approach develops and matures, and more substantive information becomes available.

### **The Office for Professional Body Supervisors (‘OPBAS’)**

In January 2018, new regulations gave rise to OPBAS with the aim of improving the consistency of AML supervision across the twenty-two Professional Body Supervisors. OPBAS sets out guidance and its expectations of PBSs in performance of their duties under the MLRs, in the form of the ‘OPBAS Sourcebook’ – which the Society must also adhere to.

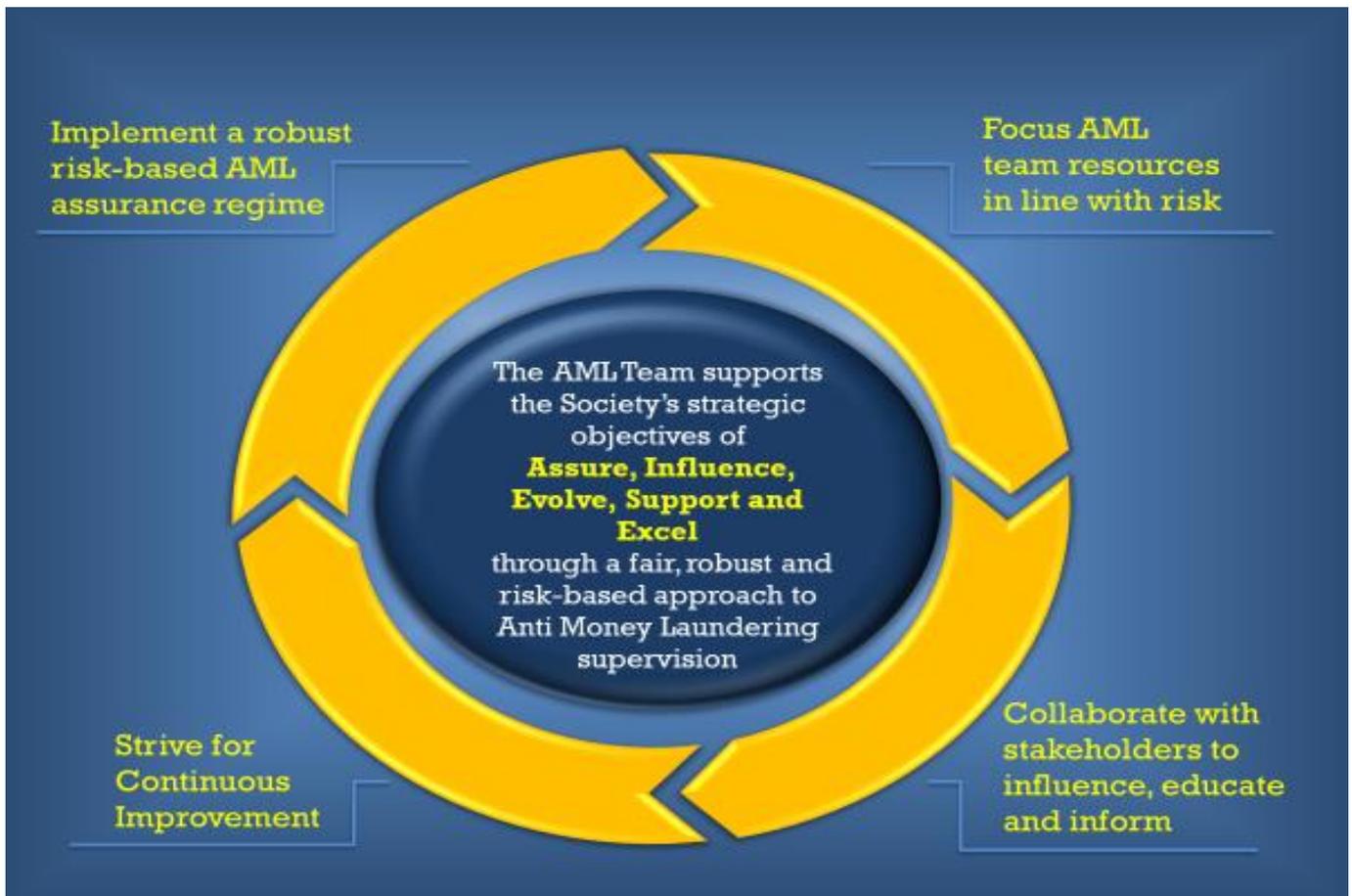
## 2. Our AML Supervisory work

### AML team - Structure

The Society currently has a dedicated team of 3 AML experts consisting of the Head of AML and two managers, responsible for AML Supervisory and assurance work across the profession. This team is embedded within (and supported by) the Society’s wider Financial Compliance and Regulatory functions and prioritises assurance and other supervisory activity on a risk-based approach – in line with responsibilities under r.46.



### AML Team Mission Statement & Objectives



**The AML Certificate & Our Risk Based Approach to Supervisory Assurance**

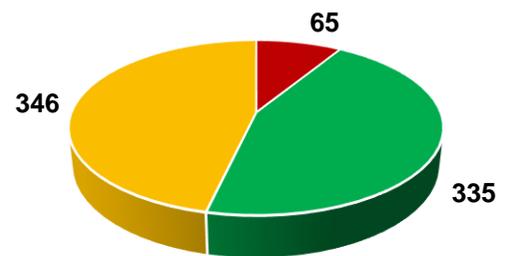
The Society AML Certificate is an annual compulsory questionnaire issued to in-scope firms, consisting of c. 50 questions relating to inherent AML risk factors. In line with the MLRs and the UK National Risk Assessment, it focuses on a firm’s inherent exposure to higher risk clients and areas of practice such as conveyancing, trust and company provision, along with geographic and delivery channel risk.

Once analysed, the data collected is used to build a risk profile of our supervised population, and can also allow us to understand specific risks, trends, or issues across individual firms.

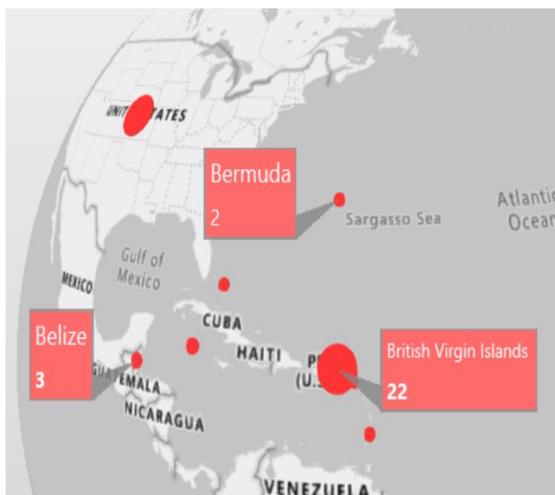
This profiling mechanism allows the Society to satisfy requirements of r.46 – i.e., to adopt a risk-based approach to the exercise of its supervisory functions, and to base the frequency and intensity of our supervision on the risk profile of our supervised population.

**The Scottish Legal Profession – Inherent Risks and Risk Profile**

Through the analysis of our 2019/20 AML Certificate returns, we have built a risk profile of our supervised population – we believe that 335 firms represent an inherently lower risk of handling the proceeds of crime, 346 are at medium inherent risk and 65 pose an inherently higher risk given the type of business activities they undertake, the types of clients they hold and their geographical reach



The analysis of AML certificate information also gives us the ability to identify specific risks within our supervised population.



The geographic pictorial (*left*), for example, shows beneficial ownership information linked to conveyances for corporate clients.

We can also identify information linked to Trust & Company Service Provision (TCSP) or Politically Exposed Person (PEP) risk, for example:

**>5000 Registered Offices provided including ownership in B.V.I, Nigeria, China, Estonia, Korea, Seychelles, Singapore and more.**

**>250 conveyances linked to Politically Exposed Persons**

## AML Assurance

### High Risk Reviews

(In accordance with the provisions of r.46) the AML team base the frequency and intensity of assurance work according to the risk profiles developed in the AML Certificate process.

Depending upon the circumstance and specific risks highlighted via the certificate, reviews can vary between full firm inspections or reviews focused on specific files or areas of a firm's business. We also perform ad-hoc reviews based on intelligence gathered from sources such as law enforcement our reporting concerns helpline.

Full firm inspections test both the adequacy of a firm's Policies, Controls and Procedures (PCPs) as set against fundamental regulatory requirements such as CDD, governance and internal controls, record keeping and training; and also, the effectiveness of such measures "on the ground", by testing adherence to PCPs through sample review of file matters.

AML Certificate data allows us to sample effectively and efficiently, focusing on high-risk or other matters of interest from an AML perspective. This data forms the basis of file selection

During the 2020 pandemic, all high-risk reviews have been successfully conducted remotely, using secure online tools and email encryption facilities

### Medium Risk Reviews

Those firms deemed of medium inherent AML risk are also inspected on a cyclical basis, although this can be varied as required. Inspections are undertaken by the members of the wider financial compliance team. These inspections focus predominately on file-level AML compliance in the context of wider client accounting matters. The AML team work with the Financial Compliance where issues are identified which may indicate higher AML risk. These can be reported to the AML team for further specialist investigation or input.

### Assurance Statistics

#### *High-risk:*

Since the initiation of our new risk-based approach to AML assurance in late 2018 we have conducted **27 high-risk assurance reviews** – seventeen full firm inspections and ten file reviews.

**27**

*High risk firm inspections  
and file reviews initiated  
since the first AML  
Certificate*

### Assurance Outcomes

Eight firms were referred to the interim AMLSC between January and July 2019. In the next 12 months to August 2020 a further eighteen firms were referred to the newly established, permanent AMLSC.

These reviews have led to a range of outcomes, from no further action required, to a tailored remediation plan being agreed with a follow-up re-inspection, through to escalation of the report to AML Sub Committee for review. Recommendations have included complaint referrals to the Scottish Legal Complaints Commission in the most serious/egregious circumstances.

In total, ten of the cases referred between January 2019 and August 2020 resulted in referrals to the Scottish Legal Complaints Commission (SLCC) and one to the Crown Prosecution Service. Eight firms were asked to remediate deficiencies and are subject to future re-inspection.

Under r.46(5) obligations we also submit an average of 10 Suspicious Activity Reports (SARs) a year to the National Crime Agency, based on information gathered and suspicions aroused through the course of our inspection work and other activities.

### Assurance – General Observations

Anti-money laundering is *not* a zero-failure regime. The wider intention of our supervisory work is to help build a Scottish legal sector which is engaged with the issues around AML, which understands its risks and obligations and which therefore organically applies itself to the suppression of financial crime through adequate, effective and compliant policies, controls and procedures.

Through our AML assurance work and frequent engagement with the profession, the AML team have made some recurring observations on areas which require improvement in understanding and underlying compliance. These include:

- The requirement to undertake appropriate and **ongoing due diligence on trust and company services** provided to clients
- A general misunderstanding of the additional measures required in higher-risk situations – i.e. what constitutes effective **“Enhanced Due Diligence”**.
- A lack of understanding around the definitions and the application of relevant **Source of Funds/Source of Wealth checks** – and in what circumstances these may be relevant.
- A misunderstanding regarding **Beneficial Ownership** (including definitions, dilution issues and what is meant by “ultimate beneficial ownership”) and associated CDD requirements
- Issues regarding contemporaneous, comprehensive and compliant AML-related **record-keeping and document management**

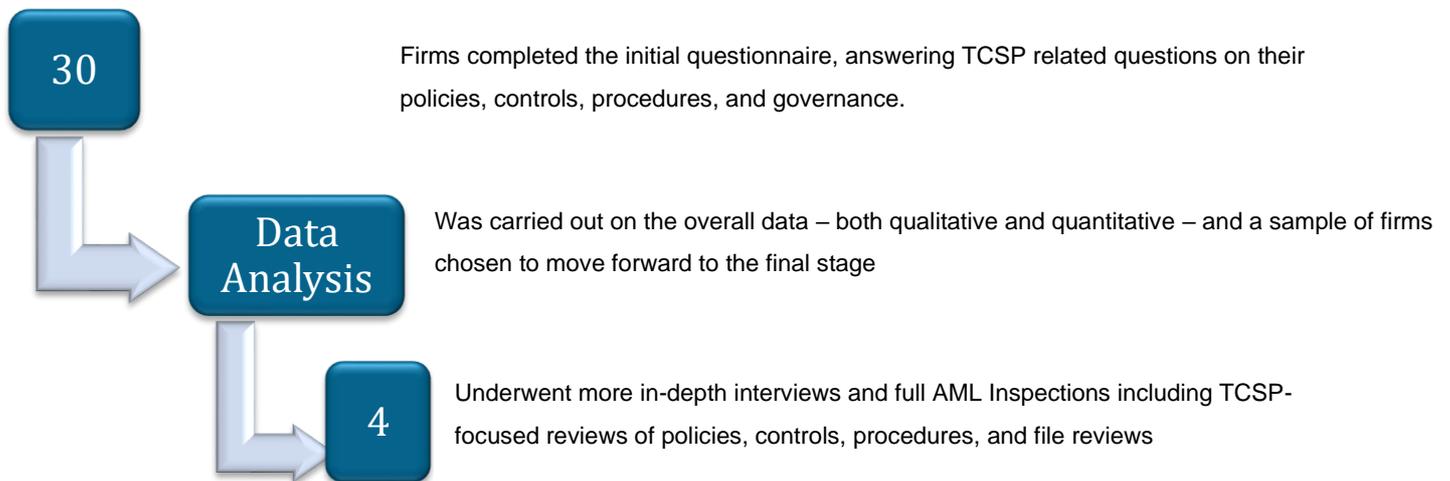
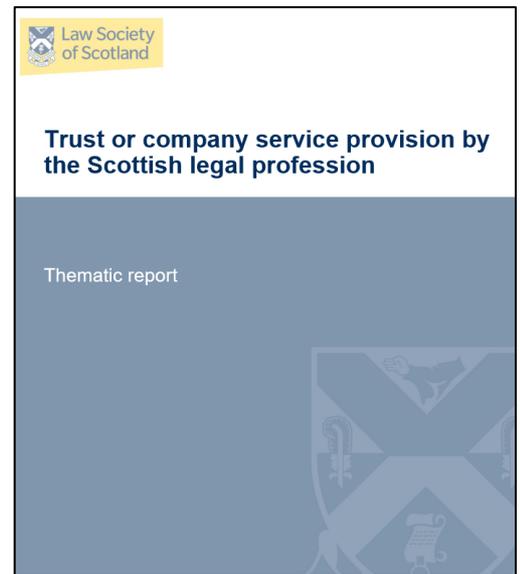
Thematic Review - Trust & Company Service Provision (TCSP)

The UK’s previous National Risk Assessment 2017 noted that Trust & Company Services Provision was a high AML risk area for the legal profession. It was against this background that the Society published our first AML thematic review, focused of TCSP work undertaken by the Scottish profession, in February 2020.

*(N.B. this review was then subsequently cited in s10.9 of the UK National Risk Assessment 2020)*

The objectives of the review were to –

- allow the Society to better understand the breadth of provision of trust or company services by the Scottish legal profession and enable us to better direct our resources in terms of supervision
- review compliance with the Regulations across the Stage 3 firms
- highlight the regulatory obligations placed on solicitors when providing trust or company services to their clients



As the above illustration highlights, four firms were eventually chosen to be taken forward to the final thematic stage – essentially an AML inspection of their practice, with a focus on their TCSP work.

We were encouraged by the data provided in the questionnaire submissions but identified several consistent themes from the review.

Key findings of the TCSP Thematic Review included:

- Firms not ensuring that the provision of trust or company services and the associated risks are properly reflected in firm level risk assessments
- Firms failing to address those services in their policies, controls and procedures (PCPs) to mitigate the risks
- Improvements required to AML file management and record keeping to evidence compliance with the Regulations and the Law Society of Scotland Practice Rules
- Failure to produce AML-specific files relating to client matters and relationships in a timely manner
- Failure to undertake ongoing monitoring of client relationships and documenting “Know Your Client (KYC)” information on an ongoing basis

### 3. AML Governance & Training

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Over the course of the last year, the Society has taken several significant steps to strengthen its governance framework in relation to our AML supervisory responsibilities, along with the ongoing competence of staff.

- A new internal AML Policy has been implemented, which clearly delineates internal supervisory and representative functions, governance, and decision-making responsibilities. As per the requirements of r.49, we have appointed Lorna Jack, Our Chief Executive as the “Board level” person, responsible for monitoring and managing the organisation’s compliance with its duties under these Regulations.
- Following a necessary underlying amendment to the Solicitors (Scotland) Act 1980, the Society also enacted new, AML specific practice rules in May 2019, which strengthened the Society’s AML supervisory basis and regime by cementing the specific AML inspection regime and annual AML certificate process into a solicitor’s core responsibilities and duties. The new rules also introduced a suspension power allowing the Society to suspend the practising certificate of a solicitor found to have failed to comply specifically with the AML Rules.
- The Society has set up a new AML sub-committee (AMLSC) – consisting of 7 lay members and 7 solicitors. We have attracted a depth and breadth of AML experience the committee, across a range of different firms and from a range of backgrounds, including financial services and law enforcement/prosecution. The Committee is responsible for independent review and decision-making regarding significant cases of non-compliance with the Money Laundering Regulations along with ensuring that our supervisory strategy and approach remains fit for purpose.

- To ensure the ongoing competence of the AML team, we have commissioned bespoke, specialist AML supervisory training via a 3<sup>rd</sup> party AML expert training provider. Further, we have invited other PBSs to participate in this training to share knowledge, expertise, and training, and play our part in ensuring consistency in professional body supervision across the legal sector.

#### Participation in national AML Supervisory Forums

The Society are active members of key national AML supervisory forums, including the AML Supervisors forum (AMLSF), the Legal Sector AML Affinity Group (LSAG) (which we previously chaired) and the Legal Sector Intelligence Sharing Working Group (ISEWG) (which we currently chair).

This allows the Society to monitor legal sector AML developments, issues and trends, help promote joint working, collaboration and consistency in supervisory efforts cross-sector, and ensure gateways/contacts with key stakeholders such as HM Treasury, OPBAS, the National Crime Agency, HMRC and other Schedule 1 Professional Body Supervisors.

The Legal Sector ISEWG works to improve information sharing (regarding both trends AML risk trends and specific threats ) between law enforcement and AML supervisors, so contributing to our risk-based approach.

We have recently led the efforts to develop and published fully revised and updated legal sector AML guidance, and are also active participants in relevant aspects of the Government's Economic Crime Strategy.



#### 4. Reporting Breaches & Concerns

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In response to our obligation under r.46 to take effective measures to encourage the sector to report breaches, the Society launched a new “reporting concerns” hotline in February 2019. This hotline allows anonymous concerns to be disclosed by any person (the public, solicitors or others working in the legal sector) via a phonenumber and/or a dedicated webpage contact form. These channels are monitored and managed by the Society’s public communications team with agreed escalation routes to the Director of Financial Compliance in respect of any potential AML-related matters. Further work will be undertaken this year to boost and renew awareness of the availability of the “reporting concerns line” to the public and profession.

##### Reporting Concerns – key numbers

22 – total number of reports

15 – passed to the Director of Financial Compliance

3 – deemed valid concerns of money laundering, SARs raised and investigated

2 – investigation reports subsequently passed to AML Sub-Committee

Of the **twenty-two reports** received to the year ending January 2020, **fifteen** concerns were passed to the Director of Financial Compliance.

Other official and unofficial channels for reporting breaches or concerns are also available and open to the profession.

We have, for example, included a specific section in the AML Certificate which asks respondents to share relevant information or intelligence which may help the Society mitigate AML risk within the sector.

## 5. Guiding the Profession

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The AML team also makes available relevant and appropriate support and guidance to help the profession achieve compliance with regulatory requirements.

To this end, the AML Team have undertaken a number of initiatives, including an extensive AML support section on our website.

The non-assurance work we undertake is important in the context of the wider support the Society offers its members and as illustrated here, can range from specific assistance to firms on AML matters, ad hoc queries, to webinars, conferences and national projects.

**The AML Team spent > 200 hours undertaking non-assurance related work in the year to August 2020**



#### Case Study: Collaboration with the NCA

The National Crime Agency have recently begun to implement a drive towards more digital engagement with external reporters and stakeholders. We were delighted to design and produce the inaugural NCA webinar on Suspicious Activity Reports; a first-of-its-kind webinar tutorial with the aim of improving the quality of SARs submitted by Scottish solicitors so that they provide the maximum possible value to law enforcement.

The NCA has welcomed this initiative and noted evidence of quality improvement since the webinar was launched. The webinar has been made available [on our website](#), and to other supervisors for their use

#### Case Study: COVID Non-F2F AML Guidance

We quickly formulated and released new guidance for solicitors to help ensure compliance with CDD requirements in light of COVID-19 lockdown restrictions, addressing a major concern/blocker for the profession. The guidance can be accessed [via this webpage](#)

## 6. Moving Forward

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Given the ongoing pandemic, 2021 will remain an incredibly challenging business environment for the legal sector.

As a responsible AML supervisor we will continue to be sensitive to this, while remaining resolute and resilient in discharging our statutory obligations. The pandemic continues to stretch resources within our member firms and (by extension as a professional membership body ) this will impact the scope of, and resource available for our AML supervision.

Central to balancing these challenges will be a continued, strong focus on our risk-based approach to supervisory assurance – using our resources wisely across areas of higher AML risk in our supervised population. To help achieve this objective (and to ensure the safety of our staff and those we work with) we will also continue to utilise secure technology to undertake fully remote inspections of firms and high risk transactions.

Other key pieces of work will include a refresh of our r.17 sectoral risk assessment and continued participation in the Government's Economic Crime reform agenda.

We look forward to working with the Scottish legal profession and our partners across the AML regulatory landscape to ensure the Scottish legal profession continues to be a hostile environment in which to launder the proceeds of crime.