Victorian Legal Services
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Reforming Australia's anti-money laundering and counter-terrorism financing regime

VLSB+C submission to the Attorney-General Department's second stage consultation on AML/CTF reforms

Introduction

The Victorian Legal Services Board (**Board**) and the Victorian Legal Services Commissioner (**Commissioner**) are the independent statutory authorities responsible for regulating the legal profession in Victoria under the Legal Profession Uniform Law (**Uniform Law**). The Board and the Commissioner effectively operate as one body, the VLSB+C. Further information about VLSB+C's history and authorising legislation, powers and functions can be found in our previous submission to the Attorney-General's Department (**AGD**) dated 16 June 2023.

VLSB+C welcomes the opportunity to respond to the AGD's second stage consultation on Australia's anti-money laundering and counter-terrorism financing (**AML/CTF**) regime.

As mentioned in our 16 June 2023 submission, we support the expansion of the AML/CTF regime to Tranche 2 entities, as well as efforts to simplify, modernise and improve the existing regime to ensure it is fit-for-purpose. Lawyers should be aware of the risk that their expertise may be exploited by criminals seeking to conceal and launder illegally obtained money, and we agree that the high risk services that lawyers offer should be subject to the AML/CTF regime.

We have reviewed the AGD's proposals for expanding the AML/CTF regime to include eight 'designated services' provided by professional service providers (**PSPs**) – including lawyers. We have also reviewed proposals for simplifying, clarifying and modernising the current AML/CTF regime. Our comments are directed to certain matters raised in Consultation Papers 2 and 5.

Consultation Questions

Proposed Designated Service 3 (Consultation Paper 2)

Of the eight proposed "designated services" provided by PSPs, we would like to comment on designated service 3, which captures PSPs who receive, hold, control, or disburse money, property and other assets on behalf of clients. We note that the scope of designated service 3 excludes "fees paid for professional services", "pre-payment for goods and services", "property management activity", and "prescribed disbursements".

While we support the intention of proposed designated service 3, our view is that transactions that pose a high risk of facilitating money laundering would most likely fall into the exceptions as currently defined.

In particular, the "fees paid for professional services" and "pre-payment for services" exclusions raise the risk that payments to lawyers will be mischaracterised to evade reporting obligations. We are aware that Consultation Paper 2 considers this issue and determines that "*fees for professional services, including as a retainer in advance, are excluded from this proposed designated service due to carrying a very low risk*". However, we wish to alert the AGD that our investigative staff have observed:

- apparent proceeds of crime being used to fund a criminal accused's legal defence, as well as non-criminal legal work undertaken on behalf of clients with criminal associations, and
- a lawyer accepting work for a client that involved nominal "commercial" advice about investments and purchasing overseas equipment. Money was deposited in the lawyer's trust account and contracts prepared, but the client's "instructions" were subsequently changed with a request for the funds to be

"refunded" into another account. The money was discovered to have been sourced from various online scams. Without the intervention of the Australian Federal Police, who were following other enquires, that money would have been washed through the trust account.

In neither of the situations above would AML/CTF obligations have arisen. In the former case, the payment would be considered "fees paid for professional services" and in the latter, a retainer in advance of legal services being provided.

In our experience the majority of legal work undertaken by lawyers (for which payment may or may not be held in trust) is for clients who would be classified as very low risk for potential money laundering. Higher-risk scenarios, where there is a greater risk of proceeds of crime being used to pay for legal services, or of the client 'washing' money through a lawyer's trust account in the manner described above, involve:

- clients seeking legal advice for defence of indictable charges arising from allegedly trafficking in commercial quantities of drugs (or similar), and giving rise to ready access to large amounts of untraced cash
- clients seeking legal advice for defence of indictable charges for accused individuals associated with outlaw motorcycle gangs or notable crime families
- legal services for a client who works in an area where there is both:
    - prominent reliance on cash/hard-to trace-funds, and
    - negative reputational risks stereotypically associated with the industry (e.g. wholesale fruit/vegetable markets and bookmaking or gaming), and
- the purchase/acquisition of businesses stereotypically associated with organised crime (e.g. gymnasiums, tattoo parlours, tobacco shops, strip clubs, and some types of car yards).

If it would be useful, we would be pleased to meet with AGD officers to provide further investigative insights relevant to this issue.

Other comments: Prescribed disbursements and escrow

We would appreciate further clarity as to whether the following matters will be a prescribed disbursement (and therefore exempted from designated service 3):

- payments made under court orders (noting that subjecting every large family law or property transaction to AML/CTF obligations would be administratively burdensome)
- dealings with property on behalf of executor clients, and
- fees for services related to the client's matter, such as for title searches, or expert witness or reports.

In relation to the AGD's question about whether escrow services should be excluded from the scope of designated service 3, our view is that these services should be subject to AML/CTF obligations. There is no practical difference between lawyers holding money in escrow or in a trust account. Lawyers providing only escrow services face increased risks of money laundering in the absence of providing any related legal services, as there is no solicitor-client relationship with the escrow customer. We note that the UK's Solicitor Regulation Authority has published a warning notice to law firms about using client accounts as banking facilities, highlighting the risk of money laundering in such schemes.

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Legal professional privilege and the duty of confidentiality (Consultation Paper 2)

Consultation Paper 2 notes that the AGD does not propose protections to exempt reporting entities (who are lawyers) from providing information or documentation on the basis that such information is confidential, in line with the existing exception to a lawyer's duty of confidentiality in which disclosure of confidential material is compelled by law.

Regarding the interaction between a lawyer's duty of confidentiality and the obligation to report suspicious matters, we further note that a lawyer's duty to the court and the administration of justice is paramount and prevails over any duty to the client.[1] Identifying clients and verifying the source of funds should already be best practice in the legal profession to avoid knowingly dealing with the proceeds of crime. Currently, where a lawyer has suspicions relating to a client's behaviour or source of funds, it is already incumbent upon them to make inquiries to understand and settle these suspicions or cease to act.

Implementing an AML/CTF program, including customer identity verification and transaction monitoring, helps lawyers recognise and mitigate money laundering or terrorism financing risks. Rather than forcing lawyers into an ethical dilemma, a suspicious matter report (**SMR**) obligation would instead shield lawyers by providing a clear process and legislative backing to make enquiries of their client.

Broader changes to the AML/CTF Scheme (Consultation Paper 5)

Leveraging pre-existing processes to comply with AML/CTF obligations

Consultation Paper 5 proposes a shift towards an outcomes-focused approach to implementing an AML/CTF program, and proposes that reporting entities including PSPs would be able to leverage existing measures to comply with their AML/CTF obligations.

We support the aim of using pre-existing measures to help lawyers meet AML/CTF obligations and reduce their regulatory burden. We also consider that some existing systems can be leveraged appropriately (e.g. the Verification of Identity Standard established by ARNECC). However, other pre-existing processes will not be suitable for this purpose.

For example, the trust account provisions in Part 4.2 of the Uniform Law seek to ensure law practices hold money on trust in a way that protects the interests of the persons for whom or on whose behalf it is held.[2] Trust account audits and external examinations of trust records are undertaken to make sure that trust money is distributed in accordance with client instructions and appropriate records are kept. It would be outside the expertise of auditors or examiners to assess a reporting entity's compliance with AML/CTF requirements.

We note that Consultation Paper 5 specifically suggests that it would be a requirement for reporting entities to certify to AUSTRAC that their AML/CTF Compliance Officer is a "fit and proper person". As AGD is aware, in order for legal practitioners to be issued with a practising certificate (or have their practising certificate renewed), they are required to be fit and proper persons. Though we appreciate that it would reduce the regulatory burden on reporting entities to appoint the holder of a practising certificate as their AML/CTF Compliance Officer, we wish to advise the AGD that being fit and proper to hold a practising certificate on its own cannot guarantee that a lawyer is suitable to perform the role of Compliance Officer.

When screening a lawyer prior to appointing them as a Compliance Officer, their fit and proper status can be a strong indicator but should not be relied upon in isolation to pass the screening. AUSTRAC's Guidance on employee due diligence suggests useful additional steps that could be undertaken before appointing a Compliance Officer, such as

[1] *Legal Profession Uniform Law Australian Solicitors' Conduct Rules 2015* r 3.
[2] *Legal Profession Uniform Law* (Victoria) ('Uniform Law') s 127.

character and background checks, identity verification, and an independent ML/TF risk assessment.[3] Any screening process should be risk-based and tailored to a practice's particular requirements.

We recommend that education and guidance be developed by the AGD or AUSTRAC to assist the legal profession to understand which pre-existing processes they can use to comply with AML/CTF requirements. We are happy to provide any assistance in the development of this advice that the AGD and AUSTRAC would consider useful.

Business Relationship

Consultation Paper 5 seeks feedback on what should be considered the conclusion of a business relationship. For lawyers, the appropriate conclusion of a business relationship should be the end of the retainer and finalisation of a file. Typically, a retainer ends when the matter is completed, or the client discharges the lawyer. It may also end if the lawyer terminates the engagement for just cause with reasonable notice, or if it ends by operation of law.[4]

Tipping Off offence

Consultation Paper 5 proposes reframing the existing tipping off offence in the AML/CTF Act so that if reporting entities submit, or are required to submit, a SMR, they must not disclose any information about the report, if doing so would prejudice an investigation or potential investigation. We understand that this reframing is intended to clarify that disclosing SMR information directly to a person of interest or their associate would constitute tipping off, whereas disclosure to another entity within a business group, or to a regulator, would not.

As noted in our 16 June 2023 submission, we have experienced authorised deposit-taking institutions (**ADIs**) failing to comply with their statutory obligations under section 154 of the Uniform Law to report irregularities in law practice trust accounts to us, on the basis that doing so may breach the current tipping off provision. This is not unique to Victoria. We understand the Law Society of New South Wales is experiencing similar issues with ADIs in their jurisdiction. It is an important component of our consumer protection regime that we receive early information about potential trust account irregularities.

There have been further frustrations where law practice trust accounts have been restricted by an ADI due to suspicious activity, or a failure to comply with "know your client" obligations, and the lawyer has not been notified of the reasons why due to concerns about breaches of the tipping off. This results in the lawyer attempting to continue to transact on the account.

We remained concerned about the way the operation of section 154 of the Uniform Law and section 123(9) of the AML/CTF Act is being interpreted by some of the ADIs. In particular, it is of concern to us that some ADIs have a different perspective on the operation of the tipping off offence and doubt their ability to share information with us as required under the Uniform Law. Given that reporting entities are likely to be anxious about potentially breaching the tipping off offence, our preference would be for the revised offence to include a clear statement to the effect that nothing in the offence affects an ADI's obligation to provide any information required or compelled by regulators.

Information Sharing

We wish to take this opportunity to reiterate our request for the introduction of formal information sharing arrangements under which we would be made aware when a reporting entity is knowingly or unwittingly involved in ML/TF activities.

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[3] AUSTRAC, 'Employee due diligence' (Web Page, 15 January 2024) <https://www.austrac.gov.au/business/core-guidance/amlctf-programs/employee-due-diligence>.
[4] Legal Profession Uniform Law Australian Solicitors' Conduct Rules 2015 r 13.1.

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As discussed in our 16 June 2023 submission, Part 9.4 of the Uniform Law permits us to make arrangements with Australian authorities for exchanging, obtaining or disclosing information relevant to any of our functions,[5] to request information in cooperation with, or with the assistance of, any agency, and to use the information to exercise said functions.[6] However, it does not require other authorities to enter into information sharing arrangements, or provide information to us upon our request. Accordingly, we have no way of identifying lawyers involved in money laundering, other than through our own trust account investigations.

AUSTRAC already shares and disseminates information with numerous Commonwealth, State and Territory government partners. Our role as the legal regulator is to ensure that the legal profession is held to the highest professional standards, for the protection of consumers and to support the rule of law. By having clear codified arrangements for information sharing with AUSTRAC, Uniform Law regulators can support AUSTRAC in its objective of detecting, deterring, and disrupting criminal abuse of the financial system.

We would welcome the opportunity to discuss with AGD amendments that may be required to the Uniform Law framework, and to discuss practical arrangements with AUSTRAC, to facilitate an effective partnership between AUSTRAC and Uniform Law legal regulators.

Conclusion

We thank the AGD for the opportunity to comment on the consultation paper and hope that our comments will be taken into consideration.

Yours faithfully

Kerri-anne Millard
Director, Policy & Outreach

[5] Uniform Law s 436.
[6] Uniform Law s 441.