

## Cooperation, Co-option or Coercion? The FATF Lawyer Guidance and Regulation of the Legal Profession

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Threats to the independence of the legal profession have become a preoccupation for bar leaders, regulators and academics, driven by the dual pressures of globalization and the changing business structure of the profession. The Preliminary Issues Outline of the American Bar Association Commission on Ethics 20/20, released in November 2009, noted that an “increase in globalized law practice raise[s] serious questions about whether existing ethical rules and regulatory structures adequately address the realities and challenges of 21st Century law practice.”<sup>1</sup> A Law Society of Upper Canada task force report in December 2009 noted that the “profession’s ability to maintain self-regulation has been eroded,” pointing specifically to changes in both England and Australia as especially ominous for lawyers elsewhere in the common law world.<sup>2</sup> The adoption of the *Legal Services Act 2007* in England signaled the fundamental transformation in objectives for and governance of the legal profession; one result was the effective end of self-regulation, replaced by a front-line regulator with closer ties to government.<sup>3</sup> In Australia, increasing public distrust of the legal profession and a concomitant interest in consumer protection led to reforms that have replaced self-regulation with a co-regulatory system that separates regulatory from representative functions

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1. Am. Bar Ass’n, Commission on Ethics 20/20, Preliminary Issues Outline 1 (2009).

2. The Law Soc’y of Upper Can., Governance Task Force, Final Report to Convocation 74-75 (2009), available at [http://www.lsuc.on.ca/media/convdec098\\_governance.pdf](http://www.lsuc.on.ca/media/convdec098_governance.pdf).

3. Legal Services Act, 2007, c. 29 (U.K.); for a detailed discussion of the events leading up to the adoption of the 2007 legislation, see Paul D. Paton, *Between a Rock and a Hard Place: The Future of Self-Regulation—Canada Between the United States and the English/Australian Experience*, 2008 J. PROF. LAW 87, 96-104 [hereafter Paton, Rock and Hard Place]; also Judith L. Maute, *Revolutionary Changes to the English Legal Profession or Much Ado About Nothing?*, PROF. LAW 2006, at 1; John Flood, *Future Directions in the UK Legal Profession: Life After the Legal Services Act 2007* (Apr. 17-18, 2008) (unpublished paper), available at <http://www.law.georgetown.edu/LegalProfession/documents/FloodWebsitePaper.doc>.

and that relies on the integrated involvement of government, the legal profession and the courts.<sup>4</sup> Even in the United States, the encroachment of the Securities and Exchange Commission into direct regulation of conduct for those lawyers “appearing and practicing before the Commission” following the adoption by the United States Congress of Section 307 of the Sarbanes-Oxley Act of 2002 in the aftermath of Enron and other corporate scandals has meant a recalibration of the fundamental understanding about the appropriate distance between government and regulation of lawyer activities.<sup>5</sup>

The October 2008 *Lawyer Guidance* issued by the Financial Action Task Force [FATF]—a supranational, intergovernmental body charged with responsibility for developing standards and measures for combating money laundering and terrorist financing—can thus be viewed as the latest talisman for gauging the balance being struck between government actions to protect the public interest and the traditional conception of lawyer self-regulation and independence.<sup>6</sup> While the narrow focus in the FATF context is the juxtaposition of safety and security in an age of terrorism against the sanctity of privilege and confidentiality between lawyer and client, what the FATF documents and debate signal about the relationship between government and the bar has much greater ramifications for the future regulation of the legal profession as a whole, domestically and internationally.

In that respect, situating the FATF initiative in the broader array of recent legislative and regulatory responses positioning lawyers as “gatekeepers”<sup>7</sup> confirms that

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4. Law Council of Australia, Submission to the Standing Committee of the Attorneys-General: Towards National Practice 4 (October 2001); see also Paton, Rock and Hard Place, *supra* note 3, at 104-107; Ted Schneyer, *Thoughts on the Compatibility of Recent U.K. and Australian Reforms with U.S. Traditions in Regulating Law Practice*, 2009 J. PROF. LAW 13; Steve Mark, *Views from an Australian Regulator*, 2009 J. PROF. LAW 45.

5. Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204; Securities and Exchange Commission, “Final Rule: Implementation of Standards of Professional Conduct for Attorneys” (5 August 2003), available at <http://www.sec.gov/rules/final/33-8185.htm>. I have argued this point in Paul D. Paton, *Corporate Counsel as Corporate Conscience*, 84 CAN. BAR REV. (2005) 533 at 546-552. For an extended analysis of the history of Section 307 and the firestorm over proposals by the SEC to implement mandatory “noisy withdrawal” and reporting on client misconduct by counsel to the Commission, see Stephen M. Bainbridge and Christina L. Johnson, *Managerialism, Legal Ethics and Sarbanes-Oxley Section 307*, 2 MICH ST. L. REV. 299 (2004); Deborah L. Rhode and Paul D. Paton, *Lawyers, Ethics and Enron*, 8 STAN J. L. BUS. FIN 9 (2002); Roger C. Cramton, George M. Cohen and Susan P. Koniak, *Legal and Ethical Duties of Lawyers After Sarbanes-Oxley*, 49 VILL. L. REV. 725 (2004).

6. Financial Action Task Force, RBA Guidance for Legal Professionals (2008) [hereafter “FATF Lawyer Guidance”], available at <http://www.fatf-gafi.org/dataoecd/5/58/41584211.pdf>.

7. See, Reiner Kraakman, *Gatekeepers: Anatomy of a Third-Party Enforcement Strategy*, 2 J.L. ECON. & ORG. 53 (1985); Reiner Kraakman, *Corporate Liability Strategies and the Costs of Legal Controls* 93(5), YALE L.J. 857 (1984); John C. Coffee, Jr., *Understanding Enron: It’s About the Gatekeepers*, *Stupid* 57 BUS. LAW 1403 (2002); Valerie Breslin and Jeff Dooley, *Whistle Blowing v. Confidentiality: Can Circumstances Mandate Attorneys to Expose their Clients?*, 15 GEO. J. LEGAL ETHICS 719 (2001); Rebecca Gregory, *The Lawyers Role: Will Uncle Sam Want You in the Fight*

the FATF Recommendations and Lawyer Guidance are both important for how they potentially change lawyer practices day to day, as well as for how they signal the shifting direction of lawyer obligations to clients and to the public interest. Moving beyond traditional expectations of lawyers as advisors guiding clients to act with integrity, elected officials—and in turn the regulators—have probed or tested assumptions of a singular loyalty to clients by introducing expectations of duties or obligations by lawyers to the broader public interest that conflict with or supersede the lawyer-client compact. The situation is still evolving, but it is clear that elected officials are no longer willing to accept as an article of faith that the lawyer-client relationship is impenetrable; the challenge for the legal profession is to recognize that in an era when expectations of lawyers as gatekeepers have been fundamentally altered, the profession needs to be proactive in assessing where its rules might better serve the public interest, and in making better arguments to protect those values it articulates as fundamental.

Where that debate takes place is also shifting: as Laurel Terry has rightly noted, the forum for discussion about the proper role of a lawyer in the United States has moved from its traditional venues—the American Bar Association, state Bars and Supreme Courts—to international forums.<sup>8</sup> The potential impact of the FATF on U.S. lawyer regulation may therefore in part be assessed by reference to what has happened elsewhere. The Canadian experience, in particular, offers a cautionary tale. Federal legislation in Canada designed to implement FATF initiatives set the stage for a direct confrontation between government and the bar. An uneasy truce—the adjournment of constitutional challenges by the Canadian legal profession to the new laws and the eventual adoption by the profession itself of money laundering rules along the lines proposed by the FATF—were powerful illustrations of the shifting expectations about lawyer self-regulation and signals of the willingness of both courts and governments to override assertions of the need for lawyer independence when a broader public interest was at stake.

Following a brief overview and introduction to the work of the FATF and the 2008 Lawyer Guidance, the balance of this article focuses on the Canadian experience, as well as signals emerging from Australia, to discern where the line is now being drawn between competing conceptions of legal and ethical obliga-

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*Against Money Laundering and Terrorism?*, UMKC L. REV. 23 (2003); William H. Simon, *Introduction: The Post-Enron Identity Crisis of the Business Lawyer*, 74 FORDHAM L. REV. 947 (2005); Sung Hui Kim, *The Banality of Fraud: Re-situating the Inside Counsel as Gatekeeper*, 74 FORDHAM L. REV. 983 (2005); K.R. Fisher, *The Higher Calling: Regulation of Lawyers Post-Enron*, 37 U. MICH. J.L. REF. 1017 (2004); Geoffrey Miller, *From Club to Market: The Evolving Role of Business Lawyers* 74 FORDHAM L. REV. 1105 (2005); Robert W. Gordon, *A New Role for Lawyers? The Corporate Counselor After Enron*, 35 CONN. L. REV. 1185 (2003); Susan P. Koniak, *Corporate Fraud: See, Lawyers*, 26 HARV. J.L. & PUB. POL'Y 195 (2003); Sung Hui Kim, *Lawyer Exceptionalism in the Gatekeeping Wars*, 63 SMU L. REV. 73 (2010).

8. Laurel S. Terry, *An Introduction to the Financial Action Task Force and Its 2008 Lawyer Guidance*, 2010 J. PROF. LAW 3 (2010).

tions between lawyer and client. Changes to lawyer regulation in Australia and England noted above have been seen as indicators of governments becoming “less inclined to bow to lawyers’ traditional role as governors of their own profession.”<sup>9</sup> As Colin Tyre has described in his article elsewhere in this volume, authorities in the United Kingdom have implemented a more stringent anti-money laundering regime and obligations for lawyers beyond what was required by FATF guidance.<sup>10</sup> Further, the March 2009 Smedley Report (“Review of the Regulation of Corporate Legal Work”)<sup>11</sup> may signal intentions for future regulation of corporate practice in England into which money laundering initiatives more directly fall. In assessing regulatory risk particular to corporate legal practice, the Smedley Report’s suggestion that there ought not to be a unitary approach to regulating the profession in its entirety has gained traction, which may have ramifications for commercial lawyers in the United States and elsewhere.<sup>12</sup>

While the FATF key documents—the “40+9 Recommendations”<sup>13</sup> and the 2008 FATF Lawyer Guidance described briefly below and elsewhere in this volume—both implicate the lawyer-client relationship in many important ways, it is the broader signals that are being sent from governments about the place and role of the legal profession and of lawyers as “gatekeepers” that may be most important in assessing their “transformative” impact.

### **Overview: The FATF 40+9 Recommendations and 2008 Lawyer Guidance**

The FATF is a supra-national organization currently comprised of 34 member states and two regional organizations representing most major financial centers

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9. Janice Mucalov, *Walking the tightrope*, 13(6) CBA NATIONAL (October 2004) 16 at 17; Judith L. Maute, *Bar Associations, Self-Regulation and Consumer Protection: Whither Thou Goest?*, J. PROF. LAW. 53 (2008).

10. See also the comprehensive discussion of the anti-money laundering rules of the United Kingdom, going beyond FATF Recommendations, in Colin Tyre, QC, *Anti-Money Laundering Legislation: Implementation of the FATF Forty Recommendations in the European Union*, 2010 J. PROF. LAW. 69 (2010).

11. Nick Smedley, *Review of the Regulation of Corporate Legal Work*, 31 March 2009, available at [http://www.legalregulationreview.org.uk/files/report\\_smedleyfinal.pdf](http://www.legalregulationreview.org.uk/files/report_smedleyfinal.pdf); the question of the contours of privilege in corporate contexts is a related matter, see Paton, *Corporate Counsel as Corporate Conscience*, *supra* note 5 at 558-559; see also Adam M. Dodek, *Reconceiving Solicitor-Client Privilege*, 35 QUEEN’S L.J. 493 (2010).

12. How applicable international models might be for U.S. purposes is open to debate given the nature of lawyer regulation in the U.S.: Schneyer, *supra* note 4. Whether the U.S. profession is itself self-regulating is also a matter for continuing debate: see Fred C. Zacharias, *The Myth of Self-Regulation*, 93 MINN. L. REV. 1147 (2009).

13. The Financial Action Task Force [FATF], *The Forty Recommendations*, available at <http://www.fatf-gafi.org/dataoecd/7/40/34849567.PDF>; Financial Action Task Force, 9 Special Recommendations (SR) On Terrorist Financing (TF), available at <http://www.fatf-gafi.org/dataoecd/8/17/34849466.pdf> (Oct. 22, 2004). Together these two sets of recommendations are referred to as the FATF 40+9 Recommendations.

around the world.<sup>14</sup> Formed in 1989, the FATF was originally tasked with examining money laundering techniques and trends, reviewing national and international practices, and making recommendations needed to effectively combat money laundering. In October 2001, the FATF Mandate was expanded to incorporate measures against terrorist financing. The four key objectives of its current mandate (2004-2012) are to:

- revise and clarify global standards and measures for combating money laundering and terrorist financing;
- promote global implementation of the standards;
- identify and respond to new money laundering and terrorist financing threats; and
- engage with stakeholders and partners throughout the world.<sup>15</sup>

The FATF developed and published its first articulation of standards in 1990 as a “complete set of counter-measures against money laundering, covering the criminal justice system and law enforcement, the financial system and its regulation, and international co-operation.”<sup>16</sup> The impetus was the desire to “combat the misuse of financial systems by persons laundering drug money.”<sup>17</sup> The original Forty Recommendations were revised in 1996 to reflect evolving money laundering practices and techniques, and then reviewed and updated again in 2003. Though not an international convention in the formal sense, the Recommendations have been endorsed by more than 130 countries and “are the international anti-money laundering standard.”<sup>18</sup> A complementary set of Eight Special Recommendations on Terrorist Financing aimed at combating the funding of terrorist acts and terrorist organizations was released in October 2001; a ninth was added in 2004.<sup>19</sup>

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14. A current listing of FATF Members, Associate Members, and Observers is available at [http://www.fatf-gafi.org/document/52/0,3343,en\\_32250379\\_32236869\\_34027188\\_1\\_1\\_1\\_1,00.html](http://www.fatf-gafi.org/document/52/0,3343,en_32250379_32236869_34027188_1_1_1_1,00.html). See also Financial Action Task Force, “FATF Membership Policy,” 29 February 2008, available at [http://www.fatf-gafi.org/document/25/0,3343,en\\_32250379\\_32236963\\_43649561\\_1\\_1\\_1\\_1,00.html](http://www.fatf-gafi.org/document/25/0,3343,en_32250379_32236963_43649561_1_1_1_1,00.html). Amongst the criteria for membership, the jurisdiction “should be strategically important”.

15. These objectives were confirmed at a Ministerial meeting in Washington DC in April 2008. See Financial Action Task Force, FATF Annual Report 2008-2009 at 6 and Annex 1: FATF Mandate at 24-27, available at <http://www.fatf-gafi.org/dataoecd/11/58/43384540.pdf>; see also Financial Action Task Force, “An Introduction to the FATF and Its Work,” available at <http://www.fatf-gafi.org/dataoecd/48/11/45139480.pdf>.

16. Financial Action Task Force, “The 40 Recommendations”, available at <http://www.fatf-gafi.org/dataoecd/11/58/43384540.pdf>.

17. Financial Action Task Force, “FATF 40 Recommendations, 20 June 2003” Introduction, p. 2, available at <http://www.fatf-gafi.org/dataoecd/7/40/34849567.PDF>. [hereafter “FATF 40 Recommendations”].

18. *Id.* See also Kevin L. Shepherd, *Guardians at the Gate: The Gatekeeper Initiative and the Risk-Based Approach for Transactional Lawyers*, 43 REAL PROPERTY, TRUST & ESTATE L.J. 607 (2009).

19. Financial Action Task Force, “FATF IX Special Recommendations,” available at <http://www.fatf-gafi.org/dataoecd/8/17/34849466.pdf>.

Together, the so-called “40+9 Recommendations” together with their respective Interpretative Notes, represent a “comprehensive framework for combating money laundering and anti-terrorist financing.”<sup>20</sup>

Key to the success of the FATF measures is their voluntary adoption and rigorous implementation worldwide. Recognizing that countries have diverse legal and financial systems, the Recommendations attempt to set “minimum standards for action for countries to implement the detail according to their particular circumstances and constitutional frameworks.” Monitoring and evaluation of national actions against these international standards is identified as a “key element” in the fight against money laundering and terrorist financing, and assessments are conducted by the International Monetary Fund and the World Bank, as well as by the FATF and regional bodies, in accordance with evaluation principles articulated by the FATF most recently in June 2010.<sup>21</sup>

The question of regulatory compliance is therefore a national question asked of states, and any issues dealing with regulation of professionals consequently invite (at a minimum) a dialogue between national authorities and those bodies responsible for regulating professional conduct (if indeed the two are separated). This becomes particularly important in light of the conflict over the inclusion of legal professionals in the Recommendations, and the subsequent determination that lawyers should be subject to separate guidance in implementing a “risk-based approach” to combating money laundering and anti-terrorist financing measures.

The October 2008 FATF Lawyer Guidance<sup>22</sup> came about as a result of a strong response from international bar associations, including the ABA, the IBA and the Council of Bars and Law Societies of Europe (CCBE) to the inclusion of requirements in Recommendation 12 that would have subjected lawyers in particular situations to the application of customer due diligence and recordkeeping requirements, and more crucially in Recommendation 16 that would have required lawyers to disclose confidential client information as part of “suspicious transaction reporting” obligations.<sup>23</sup> Both place demands that interfere with the traditional

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20. “FATF 40 Recommendations”, *supra* note 17 at 2.

21. Financial Action Task Force, “Key Principles for Mutual Evaluations and Assessments,” June 2010, *available at* [http://www.fatf-gafi.org/document/34/0,3343,en\\_32250379\\_32236963\\_45572898\\_1\\_1\\_1\\_1,00.html](http://www.fatf-gafi.org/document/34/0,3343,en_32250379_32236963_45572898_1_1_1_1,00.html). Published assessments of FATF Members are available at [http://www.fatf-gafi.org/document/25/0,3343,en\\_32250379\\_32236963\\_43649561\\_1\\_1\\_1\\_1,00.html](http://www.fatf-gafi.org/document/25/0,3343,en_32250379_32236963_43649561_1_1_1_1,00.html).

22. FATF Lawyer Guidance, *supra* note 6.

23. FATF 40 Recommendations, *supra* note 17. See in particular Recommendation 12 [record-keeping and due diligence], and Recommendation 16: “Lawyers, notaries, other independent legal professionals and accountants should be required to report suspicious transactions when, on behalf of or for a client, they engage in a financial transaction in relation to the activities described in Recommendation 12(d).” For a further discussion of the events leading up to the adoption of the Lawyer Guidance, see Terry, *supra* note 8 and Shepherd, *supra* note 18. See also International Bar

self-regulating approach and independence of the legal profession; the second in particular posed the threat that lawyers would become delegated agents of the state required to report on the activities of their clients, something anathema to both the independence of the profession and the sanctity of the lawyer-client relationship.

An important caveat at the end of Recommendation 16 relates to the protection of privilege and confidentiality: “Lawyers, notaries, other independent legal professionals, and accountants acting as independent legal professionals, are not required to report their suspicions if the relevant information was obtained in circumstances where they are subject to professional secrecy or legal professional privilege.”<sup>24</sup> The Lawyer Guidance reiterates this: “The provisions contained in this Guidance, when applied by each country, are subject to professional secrecy and legal professional privilege. As is recognized by the Interpretative Note to FATF Recommendation 16, the matters that would fall under legal professional privilege or professional secrecy and that may affect any obligations with regard to money laundering and terrorist financing are determined by each country.”<sup>25</sup> The question then becomes the extent to which each country will extend this protection, or balance the public interest in preventing or deterring money laundering and terrorist financing as against client confidentiality. The conception of the role of the lawyer as “gatekeeper” is thrown into stark relief, tied closely to the conception of the role of government in determining the parameters of professional responsibility and regulation of the legal profession.

It is on all of these levels that the Canadian experience is illustrative. As detailed below, federal legislation designed to implement FATF initiatives set the stage for a direct confrontation between the public interest in anti-terrorist initiatives and the Canadian legal profession’s protection of what it considered to be its core values. A constitutional challenge by the profession to the legislation was ultimately left unresolved. The profession voluntarily adopted client identification and recordkeeping requirements, as well as other regulatory requirements in respect of cash transactions, which in the end effectively implemented the FATF initiatives while neatly sidestepping the creation of a positive duty to report.

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Association, “IBA Anti-Moneylaundering Forum,” *available at* <http://www.anti-moneylaundering.org/AboutAML.aspx#overview>; American Bar Association, Task Force on Gatekeeper Regulation and the Profession, Task Force Actions and Related Documents, *available at* <http://www.abanet.org/crimjust/taskforce/actions.html>; American Bar Association, Task Force on Gatekeeper Regulation, Report to the House of Delegates, February 2003, *available at* <http://www.abanet.org/leadership/recommendations03/104.pdf>; American Bar Association, House of Delegates, Resolution August 11-12, 2003, *available at* <http://www.abanet.org/leadership/2003/journal/119a.pdf>.

24. FATF 40 Recommendations, *supra* note 17, Recommendation 16, para (c).

25. FATF Lawyer Guidance, *supra* note 6. The Lawyer Guidance has been rightly criticized for failing to include in-house counsel in the definition of legal professionals to whom these protections will apply, and for taking a patchwork approach by permitting each country to determine the level of privilege protection: *see* Louise L. Hill, *The Financial Action Task Force Guidance for Legal Professionals: Missed Opportunities to Level the Playing Field*, 2010 J. PROF. LAW. 151 (2010).

## The Canadian Experience: An Uncomfortable Truce

### Introduction/Overview

The Canadian *Proceeds of Crime (Money Laundering) Act*,<sup>26</sup> enacted by the federal government in 2000 in response to the original FATF 40 Recommendations, would have required lawyers and others such as accountants, insurance companies, banks, and other institutions taking deposits, to report any transactions exceeding \$10,000 in cash, any international transfers exceeding \$10,000, as well as “suspicious transactions” to the new Financial Transactions and Reports Analysis Centre of Canada (FINTRAC), a new Crown corporation to be established pursuant to the legislation. However, only parts of the Act came into force, with proclamation of the balance and new regulations deferred. The Canadian legal profession viewed the provisions of the legislation and proposed regulations affecting legal counsel as infringing on solicitor-client confidentiality and the fundamental independence of Canadian lawyers.<sup>27</sup> In a submission to Parliament about the legislation, the Canadian Bar Association argued that the “social cost of conscripting the legal profession into the role of state investigators against their own clients is profound.”<sup>28</sup>

Subsequent legal challenges by the Federation of Law Societies, the umbrella group of regulators responsible for regulation of the legal profession in each province,<sup>29</sup> against the federal government lasted for four years before being adjourned without a decision on the merits of the constitutionality of the impugned provisions.<sup>30</sup> A series of interlocutory judgments in the related cases all

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26. *Proceeds of Crime (Money-Laundering) and Terrorist Financing Act* S.C 2000, c. 17 [hereafter “PCMLTFA”].

27. Federation of Law Societies of Canada, “Money-Laundering Chronology of Events,” available at [http://www.flsc.ca/en/pdf/ml\\_chronology.pdf](http://www.flsc.ca/en/pdf/ml_chronology.pdf).

28. Canadian Bar Association, Submission to the House of Commons Standing Committee on Finance, April 2000, cited in *id*; see also the related press release at [http://www.cba.org/CBA/news/2000\\_releases/00-04-11\\_money\\_laundering.aspx](http://www.cba.org/CBA/news/2000_releases/00-04-11_money_laundering.aspx).

29. Federation of Law Societies of Canada, “About Us”, available at <http://www.flsc.ca/en/about/about.asp>. It provides the following description: “The Federation of Law Societies of Canada (FLSC) is the national coordinating body of the Canada’s 14 law societies mandated to regulate Canada’s 95,000 lawyers and Quebec’s 3,500 notaries. Law societies are independent bodies established by provincial or territorial legislation to regulate members of the legal profession in the public interest. They are charged with ensuring that people in Canada are served by legal professionals who meet high standards of education, competence and professional conduct. To fulfill this role, law societies set standards for admission to the profession and the conduct of members; they investigate complaints and discipline members of the profession who breach the established standards of conduct; to provide further protection for the public, they also maintain plans to provide compensation to clients when a member of the profession is negligent or misuses client funds. The Federation is the voice of Canada’s law societies on a wide range of issues critical to the protection of the public and the role of law, including solicitor-client privilege, the importance of an independent and impartial judiciary, and the role of the legal profession in the administration of justice.”

30. Federation of Law Societies of Canada v. Canada (Attorney General), [2001] B.C.J. No. 2420 (November 20, 2001) (BCSC); Federation of Law Societies of Canada v. Canada (Attorney

framed the question of the balancing of public and private interests in a similar way, without resolving where the balance should lie. One judge noted that the challenge was “not a prosaic legal debate about the potential differences between lawyers as a profession and other forms of trades or professions or occupations, but is a matter which of considerable importance to the social order of [the nation] and also, though, to [the country’s] obligations as a nation on the planet.”<sup>31</sup> The public interest in controlling money laundering and participation in the international effort to prevent terrorist activity, a concern heightened by recent events, was held to be “overwhelming and obvious”.<sup>32</sup> Another judge concluded that “[i]rrespective of the ultimate decision on the constitutionality of the legislation, there is no doubt at all that the responsibilities it will place on lawyers in their dealings with their clients will be onerous and will pose difficult questions with respect to the boundary line between conflicting legal and continuing ethical obligations.”<sup>33</sup>

The question of where that line should be drawn—and by whom—remains the continuing challenge for the legal profession internationally and is perhaps the most important lesson to be drawn from the Canadian experience with FATF implementation insofar as it concerns the legal profession. Despite the profession’s fierce resistance to the government’s proposed approach, in the end the Federation of Law Societies of Canada adopted a model “know your client” rule for the legal profession in 2008,<sup>34</sup> stating in a news release that it was doing so to ensure that Canadian lawyers were “at the forefront of the fight against money laundering.”<sup>35</sup> This built upon a 2004 Federation model rule restricting lawyers from accepting

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General), [2001] A.J. No. 1697 (December 12, 2001) (Alta. Q.B.); Federation of Law Societies of Canada v. Canada (Attorney General) (2002) 57 O.R. 3d(383), [2002] O.J. No. 17, (S.C.J.) (January 9, 2002); Federation of Law Societies of Canada v. Canada (Attorney General), [2002] S.J. No. 200 (April 15, 2002) (Sask. Q.B.); Federation of Law Societies of Canada v. Canada (Attorney General) [2002] N.S.J. No. 199 (April 17, 2002) (N.S.S.C.); For more discussion see Paul Waller and Katrin Roth von Szepesbela, *Silence is Golden—Or Is It? FINTRAC and The Suspicious Transaction Reporting Requirements for Lawyers*, ASPER REV. OF INTL. BUS. & TRADE L. 85(2004); see also Ronan Reinart, *Laundering Around the World: Legislative Responses to Money Laundering in Canada, the United States and Bermuda*, ASPER REV. OF INTL. BUS. & TRADE L. 131(2004).

31. Federation of Law Societies v. Canada (Attorney General), [2001] A.J. No 1697 (Alta Q.B.) at paras 2-5.

32. Federation of Law Societies of Canada v. Canada (Attorney General) [2002] N.S.J. No. 199 (N.S.S.C.) at para 67.

33. Federation of Law Societies v. Canada (Attorney General), [2002] O.J. No. 17 at para 42.

34. Federation of Law Societies of Canada, “Model Rule on Client Identification and Verification Requirements,” adopted on March 20, 2008 and modified December 12, 2008, available at [http://www.flsc.ca/en/pdf/Federation\\_Model\\_Rule\\_081212.pdf](http://www.flsc.ca/en/pdf/Federation_Model_Rule_081212.pdf).

35. Federation of Law Societies of Canada, “Federation fights money laundering with new “know-your-client” model rule,” Press Release, March 31, 2008, available at <http://www.flsc.ca/en/whatsnew/whatsnew.asp#ml>.

cash in amounts more than \$7500 from clients or third parties.<sup>36</sup> Whether the truce on the constitutional challenge was a pyrrhic victory for the profession, or represented a triumph for self-regulation, is an open question. Legal regulators claimed that the Federation of Law Societies had launched its own initiatives to fight money laundering and terrorist financing “[i]ndependently of the litigation.”<sup>37</sup> The end result was a significant—and very Canadian—compromise.<sup>38</sup>

### Legislation and Litigation

The *Proceeds of Crime (Money-Laundering) Act*,<sup>39</sup> introduced and often referred to as Bill C-22, was designed to update and replace the 1991 *Money Laundering Act* and its regulations.<sup>40</sup> “Regulated persons and entities” were required to report suspicious transactions and certain other financial transactions, later prescribed in regulations as those involving \$10,000 or more in cash, to FINTRAC, a federal agency set up to receive and analyze financial reports and disclose that information to the police. In addition, reporting persons were prohibited from “tipping off” their client that a report had been made. Bill C-22 was given Royal Assent in June 2000, but only parts of the new legislation were in force, with proclamation of the balance and new regulations under it deferred to the fall of 2001. It was the November 2001 regulations making the provisions of the Act applicable to lawyers that caused a firestorm. Both the Federation of Law Societies and the Canadian Bar Association contended that the proposals unacceptably infringed on solicitor-client confidentiality and the professional independence of Canadian lawyers. The Federation, in particular, argued that the legislation made lawyers “secret agents of the state”, collecting information about clients against their interests and reporting to a government agency; this threatened not only the sanctity of the solicitor-client relationship but also fundamental Canadian constitutional principles and the integrity of the administration of justice.<sup>41</sup>

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36. See the history behind the earlier Federation Model Rule set out in Law Society of Upper Canada, Professional Regulation Committee, Report to Convocation, January 27, 2005, paras 1-5, available at <http://www.lsuc.on.ca/media/convjan05prereport.pdf>.

37. Law Society of Upper Canada, Professional Regulation Committee, Report to Convocation, April 24, 2008, para 16, available at [http://www.lsuc.on.ca/media/convapr08\\_prc.pdf](http://www.lsuc.on.ca/media/convapr08_prc.pdf) [hereafter “Law Society of Upper Canada April 2008 Report”].

38. Portions of this section have been drawn and updated from an earlier research paper on “Lawyers as Whistleblowers” I was commissioned to write in 2005-06 for the Law Society of Upper Canada Task Force on the Rule of Law and the Independence of the Bar; it was later published as Paul D. Paton, *The Independence of the Bar and the Public Interest Imperative: Lawyers as Gatekeepers, Whistleblowers or Instruments of State Enforcement?*, IN THE PUBLIC INTEREST: THE REPORT AND RESEARCH PAPERS OF THE LAW SOCIETY OF UPPER CANADA’S TASK FORCE ON THE RULE OF LAW AND THE INDEPENDENCE OF THE BAR 175-207 (Lorne Sossin, ed., Toronto: Irwin Law, 2007).

39. PCMLTFA, *supra* note 26.

40. *Proceeds of Crime (Money-Laundering) Act*, S.C. 1991, c. C-26 [repealed].

41. Law Society of Upper Canada, April 2008 Report, *supra* note 37, at paras 9-11.

In particular, if a transaction were subject to the reporting requirements of the legislation, a lawyer would be required to report a client's name, address and occupation and the source of the client's funds. Further, the lawyer would be prohibited from disclosing to the client that such a report had been made, and would be subject to serious criminal penalties for violating the new rules. The legislation also included powers to search a lawyer's office without a warrant and to copy records.

The legal profession's response to the proposals and, in turn, the legislation and regulations was a vigorous assertion of an orthodox view about the paramountcy of solicitor-client privilege and confidentiality. The recognition that there is a public interest imperative driving the legislation was sublimated to the profession's perception of the appropriate balance to be maintained. A Working Group of the Law Society of British Columbia established in response to concerns about the legislation, was of the view that

“such a statutory requirement for disclosure will substantially and unreasonably infringe on the confidentiality of the solicitor-client relationship and the independence of legal counsel, will put the interests of lawyers in conflict with those of their clients and will place them in breach of long-established legal, professional and ethical duties owed to the client. The potential benefit of disclosure is substantially outweighed by the benefits of fully protecting solicitor-client confidentiality.”<sup>42</sup>

The question of the appropriate balance—between disclosure in the public interest and the broader protections of full protection of solicitor-client privilege—was placed squarely at the heart of the parliamentary debate and later before the courts. The consequential impact on the role and place of lawyer as gatekeeper, and the balance between lawyer as advocate of individual interest and as protector of the broader public in the face of terrorism and other threats, remained important themes throughout.

Concerns about money laundering legislation and the potential impact on lawyers in fact had predated the enactment of the legislation in 2000. In 1998, the Canadian Bar Association had responded to requests from the Solicitor General of Canada for input on proposals to create a Suspicious Transaction and Cross-Border Currency Reporting regime by urging consultations with the legal profession, and noting that the inclusion of lawyers and law firms in the category of persons or institutions required to report was “likely inconsistent with the duty of confidentiality which lawyers owe to their clients.” Through 1999 the CBA framed its concerns in the context of the potential damage to the confidential relationship between solicitor and client by requiring lawyers to report their clients based on a

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42. Law Society of British Columbia, *Proceeds of Crime Working Group calls for changes to money laundering legislation*, BENCHERS BULLETIN, (May-June 2001), available at [http://www.law.society.bc.ca/publications\\_forms/bulletin/2000-01/01-06-01\\_BillC22.html](http://www.law.society.bc.ca/publications_forms/bulletin/2000-01/01-06-01_BillC22.html).

“suspicion” of money laundering, and argued that such an obligation would “have a chilling effect on legitimate commercial transactions.”<sup>43</sup> The arguments of then-CBA President Eugene Meehan are worth noting for the manner in which they asserted the orthodox view:

“The requirements of the Bill would fundamentally alter the very foundation of the solicitor-client relationship. This relationship is premised upon the protection of both privilege and confidentiality. Clients must be able to seek the assistance of a lawyer knowing that the information that they pass to the lawyer will remain with the lawyer and go no further. Uncertainty in the integrity of the privilege or confidentiality will create uncertainty in and undermine the solicitor-client relationship ...”<sup>44</sup>

The CBA’s April 2000 submission to the House of Commons Standing Committee on Finance on the proposed legislation reiterated portions of Meehan’s statement quoted above, but also interjected the undercurrent concern about conscripting lawyers as instruments of state enforcement. Before the Senate Committee on Banking Trade & Commerce, Meehan acknowledged that there was a balancing to be done, but was clear that the “possible beneficial effects of the bill are outweighed by its predictable deleterious effects.”

The strength of the Canadian legal profession’s arguments were undercut by the absence of empirical data or studies about the effect of privilege (or the absence thereof) on the solicitor-client relationship in the Canadian context. This gap is in contrast to the available U.S. literature, though even here there is room for additional investigation and substantiation by the bar of the need for privilege protection. Professor William Simon of Columbia University, for one, has concluded that in dealing with questions of confidentiality and corporate clients, the argument that “as a general matter, clients will not consult lawyers without confidentiality safeguards, and that, since legal advice promotes compliance with the law, this will be socially costly” is “implausible”.<sup>45</sup> A 1989 empirical study of corporate attorney-client privilege, analyzing the responses of corporate attorneys and business executives in New York City, as well as judges and magistrates of the United States District Courts for the Southern and Eastern Districts of New York, noted that the “factual premise upon which the privilege is based... is largely a matter of faith that is supported only by a minimal amount of empirical evidence.”<sup>46</sup> The study concluded that “corporate attorney-client privilege,

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43. Federation of Law Societies of Canada, “Money-Laundering Chronology of Events,” *supra* note 27.

44. Quoted in *id.*

45. See William H. Simon, *Introduction: The Post-Enron Identity Crisis of the Business Lawyer*, 74 *FORDHAM L. REV.* 947 (2005); Robert Eli Rosen, *Problem-Setting and Serving the Organizational Client: Legal Diagnosis and Professional Independence*, 56 *U. MIAMI L. REV.* 179 (2001).

46. Vincent C. Alexander, *The Corporate Attorney-Client Privilege: A Study of the Participants*, 63 *ST. JOHN’S L. REV.* 191, 194 (1989).

despite lingering doubts, may perform a useful function by enhancing candid disclosure between attorneys and corporate management”, there was “questionable value of the privilege as an inducement to candor in particular types of legal counseling”. Others have cast doubt on the need for strict rules of confidentiality to promote trust and loyalty in the lawyer-client relationship, including one set of studies suggesting that many individuals and lawyers in fact misunderstand the lawyer’s obligation to maintain the client’s secrets.<sup>47</sup> Notwithstanding the legal profession’s continued assertions, the benefit of privilege and confidentiality protections in inducing candor is open for debate. The need for empirical data and studies to underpin the assertions of the impact of the instrumental benefits of privilege and confidentiality is thus critical for a dialogue with legislators and regulators concerned about the balance to be struck. Assertions by the profession alone are not enough.

The litigation that ensued over the legislation in Canada did not resolve the question of what evidence would be required to substantiate the profession’s assertions about the impact of the new rules on client behavior or relationships. The Federation of Law Societies of Canada, on behalf of provincial and territorial law societies, brought applications in courts across the country for a declaration that certain provisions of the PCMLTFA were unconstitutional and of no force or effect to the extent that they applied to legal counsel.<sup>48</sup> In a November 2001 decision, the British Columbia Supreme Court granted an interlocutory injunction relieving lawyers of the reporting requirements set out in the Act and regulations; courts in Alberta, Ontario, Saskatchewan and Nova Scotia followed suit. In May 2002, the Attorney General reached an agreement with the Federation to exempt all Canadian lawyers and Quebec notaries from Part 1 of the PCMLTFA until the constitutional challenge was heard in BC Supreme Court and the Court had decided the case on the merits. On April 15, 2003, the BC Supreme Court ordered the adjournment of

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47. George H. Brown, *Financial Institution Lawyers as Quasi-Public Enforcers*, 7 GEO. J. LEGAL ETHICS 637, 646 (1994): “the public policies underlying the historical and present day statutes governing financial institutions, the critical importance of our banking system to a well-functioning and efficient economy, the existence of federal deposit insurance, the need to protect innocent depositors, and the lawyers’ important role in advising and consummating financial transactions all combine to outweigh the traditional objections to a lawyer’s disclosure of information learned in the course of a client representation;” see also Fred C. Zacharias, *Rethinking Confidentiality*, 74 IOWA L. REV 351 (1989).

48. Federation of Law Societies of Canada v. Canada (Attorney General), [2001] B.C.J. No. 2420 (November 20, 2001) (BCSC); Federation of Law Societies of Canada v. Canada (Attorney General), [2001] A.J. No. 1697 (December 12, 2001) (Alta. Q.B.); Federation of Law Societies of Canada v. Canada (Attorney General) (2002) 57 O.R. 3d(383), [2002] O.J. No. 17, (S.C.J.) (January 9, 2002); Federation of Law Societies of Canada v. Canada (Attorney General), [2002] S.J. No. 200 (April 15, 2002) (Sask. Q.B.); Federation of Law Societies of Canada v. Canada (Attorney General) [2002] N.S.J. No. 199 (April 17, 2002) (N.S.S.C.).

the constitutional challenge on consent until November 1, 2004.<sup>49</sup> The adjournment followed the decision by the federal government on March 20, 2003 to repeal several regulations subjecting Canadian lawyers to the recording and reporting requirements of Part 1<sup>50</sup>. In June 2004, the hearing set for November 1, 2004 was adjourned to October 31, 2005. Finally, on May 13, 2005, the BC Supreme Court adjourned the matter sine die on the following conditions:

1. That if a new set of regulations affecting legal counsel is enacted pursuant to the Proceeds of Crime Act by the Federal Government without the consent of the Federation, that the coming into force of those regulations would be deferred in accordance with the May 2002 Agreement between the Federation and the Attorney General of Canada;
2. That the Attorney General of Canada agree to interlocutory injunctions exempting legal counsel and legal firms from the application of the Act and its Regulations should it become necessary to maintain the status quo at any stage of the proceedings: and
3. That the Federation and the Attorney General have an unrestricted right to re-set the petition for hearing.<sup>51</sup>

Accordingly, the substantive question of the constitutionality of the provisions was never conclusively decided. The manner in which all of the cases frame the question of balancing to be decided is instructive and important. As Justice Watson of the Alberta Court of Queen's Bench noted, "manifestly important and even definitive social values in Canada" were engaged by the court case, and that the challenge was "not a prosaic legal debate." As Justice Watson also noted, Parliament through the Attorney General was prepared to argue "in effect, in vindication of the legal choices that it made in service of what it determined to be the public interest. As mentioned before, that public interest as perceived by Parliament apparently touches not merely on what is in the best interests of Canadians and members of the polity of which we all belong, but also Canada's relationship with the rest of the international community."<sup>52</sup> The public interest in controlling money laundering

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49. See Federation of Law Societies of Canada, "Money-Laundering Chronology of Events," (May 2005) available at < [http://www.flsc.ca/en/pdf/ml\\_chronology.pdf](http://www.flsc.ca/en/pdf/ml_chronology.pdf)>. For more discussion see Paul Waller and Katrin Roth von Szepesbela, *Silence is Golden—Or Is It? FINTRAC and The Suspicious Transaction Reporting Requirements for Lawyers*, ASPER REV. OF INTL. BUS. & TRADE L. 85 (2004); see also Ronan Reinart, *Laundering Around the World: Legislative Responses to Money Laundering in Canada, the United States and Bermuda*, ASPER REV. OF INTL. BUS. & TRADE L. 131 (2004).

50. See Canada Gazette, Vol. 137, No. 2, March 25, 2003, available at [http://www.flsc.ca/en/pdf/ml\\_SDR2003-102.pdf](http://www.flsc.ca/en/pdf/ml_SDR2003-102.pdf).

51. *Id.* The Order of the Supreme Court of British Columbia is found online: [http://www.flsc.ca/en/pdf/ml\\_13May05.pdf](http://www.flsc.ca/en/pdf/ml_13May05.pdf).

52. Federation of Law Societies v. Canada (Attorney General), [2001] A.J. No 1697 (Alta Q.B.) at paras 2-5.

and for Canada to participate in the international effort to prevent terrorist activity was held to be “overwhelming and obvious.”<sup>53</sup>

The important role of the legal profession and the duty of loyalty and confidentiality were balanced against this public interest, though at times these concerns were framed as contiguous or synonymous with the public interest rather than juxtaposed against it. In the British Columbia court challenge, Justice Allan accepted that the “solicitor-client relationship is a unique one, not comparable to the other professions and entities covered by the Act and Regulations.”<sup>54</sup> In the Nova Scotia litigation, Chief Justice Kennedy noted

“The functions of legal counsel are at the heart of the constitutionally protected principles of fundamental justice. The rule of law, the right to counsel, the right to remain silent, the privilege against self-incrimination and the right to a fair trial. That’s why, these are the reasons why, these are the principles that the applicants say they are trying to protect. That is the public interest. That is the broad public interest that they say they represent. The proper functions of legal counsel sustain and allow for the constitutionality, the entrenched principles that are so significant to the maintenance of the rule of law.”<sup>55</sup>

Chief Justice Kennedy also seemed influenced by the fact that lawyers would “continue to be governed by the Criminal Code and will not aid or abet money laundering crimes with impunity”, whether or not the PCMLTFA applied to them.<sup>56</sup> Justice Allan in B.C. found that the proclamation of the impugned section of the Regulations constituted “an unprecedented intrusion into the traditional solicitor-client relationship.”<sup>57</sup> Justice Cullity in Ontario agreed, neatly summarizing the potential consequences of the legislative reforms:

“In imposing a duty on legal practitioners to give secret reports of their clients’ transactions to a government agency, the legislation clearly impinges on, and alters, the traditional relationship between solicitors, or counsel, and their clients. It does not merely override a lawyer’s ethical duty of confidentiality—something that has always been possible in legal proceedings with respect to matters not subject to solicitor-client privilege—it strikes at the lawyer’s duty of loyalty and the client’s

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53. *Federation of Law Societies of Canada v. Canada (Attorney General)* [2002] N.S.J. No. 199 (N.S.S.C.) at para 67.

54. *Federation of Law Societies of Canada v. Canada (Attorney General)* [2001] B.C.J. No 2420 (B.C.S.C.) at para 77.

55. *Federation of Law Societies of Canada v. Canada (Attorney General)* [2002] N.S.J. No. 199 (N.S.S.C.) at paras 76-77.

56. *Id.*, at para 73.

57. *Federation of Law Societies of Canada v. Canada (Attorney General)* [2001] B.C.J. No 2420 (B.C.S.C.) at para 108.

privilege against self-incrimination as well as the principle that lawyers should be independent of government. The duty of loyalty is affected not only by the obligation to make secret reports to government about a client's transactions and personal details but, also, because of the inevitable involvement of the lawyer's personal interests and potential liability to severe penalties when decisions whether to report are to be made."<sup>58</sup>

Justice Cullity did not reject the possibility that the state could impose obligations that interfered with the independence of the bar, as it had done previously,<sup>59</sup> but was uncomfortable with the imposition of "obligations inconsistent with those owed by lawyers to their clients" which interfered with the solicitor-client relationship.<sup>60</sup> He concluded that "[i]rrespective of the ultimate decision on the constitutionality of the legislation, there is no doubt at all that the responsibilities it will place on lawyers in their dealings with their clients will be onerous and will pose difficult questions with respect to the boundary line between conflicting legal and continuing ethical obligations."<sup>61</sup>

In the end, even without a definitive answer to the constitutional challenge and the question of where the balance is to be struck, the Canadian money laundering litigation offers an important series of signals from judges about their obvious discomfort with the transformation of the traditional role of lawyer as client advocate and representative into potential informant, and the consequent transformation of the relationship between lawyer and client itself. Yet there is also a very strong sense in the decisions that broader public interest concerns in an age of terrorism and Canada's international obligations at least render the debate far from open and shut. The decisions both juxtapose the orthodoxies advanced by the legal profession against the public interest, and position them as synonymous with it. The legislation and the willingness of the Attorney General of Canada to defend a public interest concern it found "obvious and overwhelming" ahead of concerns about the sanctity of the solicitor-client relationship was profound.

### **Regulatory Change**

Steps taken by Canadian legal regulators in 2005 and 2008 to adopt rules and regulations addressing both client identification and verification concerns, and handling of cash, respond substantively to the issues raised by the FATF 40+9 Recommendations as well as to a lesser degree the Lawyer Guidance. The new rules have transformed lawyer office management practices in a significant way. More

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58. *Federation of Law Societies v. Canada (Attorney General)*, [2002] O.J. No. 17 at para 42.

59. *Wilder v. Ontario Securities Commission* (2000) 47 O.R. (3d) 361, *aff'd*, (2001) 53 O.R. (3d) 519 (C.A.) (upholding the jurisdiction of the OSC to reprimand a lawyer, despite objections from the Law Society of Upper Canada that such an action was an unacceptable intrusion by a government regulatory body on the authority of the self-regulatory body for lawyers in the province).

60. *Federation of Law Societies v. Canada (Attorney General)*, [2002] O.J. No. 17 at para 48.

61. *Id.*, at para 18.

important, however, are the symbolic messages the regulators have attempted to send through the adoption of the new rules: the legal profession is attuned to the concerns expressed in the international and national discussions and debates; the profession itself is positioned to respond to these concerns without being directed to do so by government; and protection of core values like privilege and confidentiality is both essential and consistent with the Lawyer Guidance.

There were two sets of reforms: the first in 2004/2005 to adopt a “No-Cash” Model Rule, and the subsequent adoption in 2008 of a “Know Your Client” rule and protocols.

1) *The “No-Cash” Rule*

In October 2004 the Federation of Law Societies proposed a “No Cash” Model Rule restricting lawyers from receiving cash in amounts over \$7500; this was subsequently adopted in some form by all Canadian legal regulators. As an illustration of the adoption of the model rule on a provincial level, in January 2005 the Law Society of Upper Canada in January 2005 amended Rule 2.02(5) of the Rules of Professional Conduct to add commentary on lawyers’ responsibilities when their suspicions are raised about the legality of a transaction for which the lawyer receives instructions.<sup>62</sup> The Law Society of Upper Canada also adopted changes to what were then By-Laws 18 and 19 to institute new recordkeeping provisions with respect to receipt of cash<sup>63</sup> and a prohibition on receipt of cash in an aggregate amount of \$7500 or more in respect of any one-client file.<sup>64</sup>

The symbolic and substantive effects of this rule were both important. First, the “No Cash” rule effectively rendered unnecessary the proposed obligation under the PCMLTFA requiring lawyers to report to FINTRAC all transactions involving \$10,000 or more in cash.<sup>65</sup> The Federation of Law Societies, further, positioned the adoption of the rule not as undermining the authority of the federal government to regulate in the area, but rather that its adoption demonstrated that “Canadian law societies take seriously their responsibility to regulate the profession in the public interest, based on a strong public interest in an independent Bar that provides confidential, loyal access to justice [sic] and a public interest in ensuring that lawyers do not participate in or facilitate money laundering or terrorist financing.”<sup>66</sup> The

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62. Law Society of Upper Canada, Rules of Professional Conduct, Rule 2.02(5) (Commentary), available at <http://www.lsuc.on.ca/regulation/a/profconduct/rule2/>; see also Law Society of Upper Canada, Professional Regulation Committee, Report to Convocation, January 27, 2005, available at <http://www.lsuc.on.ca/media/convjan05prereport.pdf>.

63. Law Society of Upper Canada, By-Law 18, Section 2 and Section 2.1; these provisions are now in By-Law 9 (Financial Transactions and Records), available at <http://www.lsuc.on.ca/media/bylaw09.pdf>.

64. Law Society of Upper Canada, By-Law 19, Section 1.1-1.4; these provisions are also now in By-Law 9, *id.*

65. Law Society of Upper Canada April 2008 Report, *supra* note 37 at paras 17-18.

66. *Id.*, at para 19.

federal government subsequently amended the PCMLTFA in December 2006 to exempt lawyers from the financial transaction reporting requirements of the original version of the Act.<sup>67</sup>

The Federal Government did so despite the grave concerns expressed by the Auditor General of Canada in her November 2004 Report to the House of Commons that “the removal of lawyers from the reporting requirements of the legislation in Canada means that our anti-money laundering system does not fully meet international standards.” Further, the Report noted, “[t]his exemption is widely regarded as a serious gap in the coverage of the anti-money-laundering legislation. It means that individuals can now do banking through a lawyer without having their identity revealed, bypassing a key component of the anti-money-laundering system.”<sup>68</sup>

## 2) *The “Know Your Client” Rules*

In mid-2005 the Federation of Law Societies laid the foundation for what later became its Model Rule on Client Identification and Verification Requirements.<sup>69</sup> The process continued through 2007, with the Federation consulting both with member Law Societies as well as with the federal Department of Finance. While there was some concern expressed about the imposition of new requirements, in the main changes were recognized as prudent and appropriate practices for lawyers.

In April 2008, the Law Society of Upper Canada announced a by-law change effective October 31, 2008 (implemented on December 31, 2008) requiring the lawyers and paralegals it licenses henceforth to take particular steps to verify the identity of new clients whenever they are retained by a client to provide legal services, engage others on behalf of a client or give instructions on behalf of a client in respect of activities set out in the by-law implementing the change.<sup>70</sup> Exceptions

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67. Though referred to as Bill C-25, officially it became *An Act to amend the Proceeds of Crime (Money Laundering) and Terrorist Financing Act and the Income Tax Act and to make a consequential amendment to another Act*, S.C. (Canada) 2006, C. 12, s 10.1 (Royal Assent—14 December 2006), available at <http://www2.parl.gc.ca/HousePublications/Publication.aspx?Docid=3294693&file=4>.

68. Office of the Auditor General of Canada, Report of the Auditor General of Canada to the House of Commons, November 2004, [Chapter 2—Implementation of the National Initiative to Combat Money Laundering], paras 2.30-2.33, available at [http://www.oag-bvg.gc.ca/internet/English/parl\\_oag\\_200411\\_02\\_e\\_14906.html#ch2hd3c](http://www.oag-bvg.gc.ca/internet/English/parl_oag_200411_02_e_14906.html#ch2hd3c).

69. Federation of Law Societies of Canada, “Model Rule on Client Identification and Verification Requirements, (Adopted by Council of the Federation of Law Societies of Canada as of March 20, 2008 and amended on December 12, 2008), available at [http://www.lsuc.on.ca/media/convjan09\\_prc.pdf](http://www.lsuc.on.ca/media/convjan09_prc.pdf), pp. 14-22.

70. Law Society of Upper Canada, By-Law 7.1 (Operational Obligations and Responsibilities), Parts III (Client Identification and Verification) and IV (Withdrawal of Services), available at [http://www.lsuc.on.ca/media/bylaw7\\_1.pdf](http://www.lsuc.on.ca/media/bylaw7_1.pdf); Law Society April 2008 Report, *supra* note 37 at paras 38-42; see also Law Society of Upper Canada, Professional Regulation Committee, Report to Convocation (January 29, 2009), available at [http://www.lsuc.on.ca/media/convjan09\\_prc.pdf](http://www.lsuc.on.ca/media/convjan09_prc.pdf). The April 2008

to this requirement included situations where a lawyer is acting as in-house counsel for an employer, or as an agent or referral from another lawyer who has already taken steps to verify the identity of the client.<sup>71</sup> The amendments also directed that licensees keep a record of the information and documents obtained to identify and verify the identity of clients.<sup>72</sup> The by-law requires the lawyer to obtain an individual client's full name, home address, telephone number and occupation; similar details are required for a business client, with the additional requirement that the lawyer obtain information about the "general nature of the business." For private and public companies, the lawyer has to make reasonable efforts to obtain and record the name and occupation of all directors, as well as individuals owning more than 25% of the shares.<sup>73</sup> Under the by-law, the lawyer has 60 days to verify the identity of a client where the client is not an individual.<sup>74</sup>

The By-Law speaks of both "identification" and "verification". The identification requirements apply whenever a lawyer provides professional services to a client.<sup>75</sup> Verification is the information needed to confirm that the client is who they say they are; the verification requirements are triggered when receiving, paying or transferring money to or on behalf of that client, or giving instructions to do so. There are exceptions to this verification requirement: for example, funds paid to a lawyer by a financial institution, public body, or a public company, or received from the trust account of another licensed lawyer, are exempt.<sup>76</sup>

In addition to imposing identification and verification requirements, the by-law changes reinforced an existing obligation under the Law Society's Rules of Professional Conduct not to "knowingly assist in or encourage any dishonesty, fraud, crime or illegal conduct."<sup>77</sup> Section 24 of the by-law requires a lawyer who in the course of complying with the client identification or verification requirements

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rule change was originally scheduled to come into force as of October 31, 2008 but implementation was delayed until December 31, 2008: Law Society of Upper Canada, "Law Society to launch 'know your client' requirement at year-end," Press Release, October 30, 2008, *available at* [http://www.lsuc.on.ca/media/oct3008\\_news\\_release.pdf](http://www.lsuc.on.ca/media/oct3008_news_release.pdf) [hereafter "Law Society Know Your Client Press Release"].

71. By-Law 7.1, *id.*, s. 22(2).

72. By-Law 7.1, *id.*, s. 23(14).

73. By-Law 7.1, *id.*, s. 23(2).

74. By-Law 7.1, *id.*, ss. 23(6).

75. By-Law 7.1, *id.*, s. 22(1)(a).

76. By-Law 7.1, *id.*, s. 23(3).

77. Law Society of Upper Canada Rules of Professional Conduct, Rule 2.02(5), *available at* <http://www.lsuc.on.ca/regulation/a/profconduct/rule2/>; the Commentary to the Rule notes that "A lawyer should be on guard against becoming the tool or dupe of an unscrupulous client or persons associated with such a client. A lawyer should be alert to and avoid unwittingly becoming involved with a client engaged in criminal activity such as mortgage fraud or money laundering. Vigilance is required because the means for these and other criminal activities may be transactions for which lawyers commonly provide services such as: establishing, purchasing or selling business entities; arranging financing for the purchase or sale or operation of business entities; arranging financing for the purchase or sale of business assets; and purchasing and selling real estate."

“knows or ought to know that he or she is or would be assisting a client in fraud or other illegal conduct” to immediately cease any such activities and if unable to comply with the identification and verification requirements, to withdraw.<sup>78</sup>

The terms of these client “due diligence” requirements are themselves not especially controversial except in so far as they impose additional research and recordkeeping requirements on lawyers. Indeed, the report recommending them for approval noted that in many respects, the rules “codif[y] the steps a prudent lawyer would take in the normal course to verify a client’s identity upon being retained to provide legal services.”<sup>79</sup> It is the symbolic effect that is most instructive, and made clear that the adoption of the rules was driven in part by political concerns about the relationship between government and the self-regulating profession. In announcing the launch of the “know your client” requirements, the Treasurer (President) of the Law Society stated that by codifying these procedures in a by-law, “we are ensuring that Ontario’s legal profession is at the forefront of the fight against money laundering and other criminal activities.”<sup>80</sup> The language in the report recommending the changes is even more overt, and stunning:

“Like the adoption of the No-Cash Rule, national implementation of the Model Rule on Client Identification and Verification *will demonstrate that responsible self-governance by the law societies makes federal regulation of the legal profession on this subject unnecessary.*”<sup>81</sup> [emphasis added]

Whether the result of coercion, co-option or clever cooperation, Canadian lawyers are left with two sets of Rules that in the main accord with FATF Recommendations 12 and 16 but that are imposed as part of professional self-regulation rather than by government legislation. Further, the question of the balancing between the public interest in disclosure and the profession’s interest in preserving privilege and confidentiality (and the role of lawyer as “gatekeeper”) at the heart of the constitutional challenges is left in abeyance, deferred for another day.

## Australia

As noted in the introduction, concerns about the effective end of self-regulation for the legal profession in both England and Australia make developments in those two jurisdictions important.<sup>82</sup> A brief review is provided here of Australian imple-

78. By-Law 7.1, *supra* note 70 at s. 24.

79. Law Society April 2008 Report, *supra* note 37 at para 30.

80. Law Society of Upper Canada, “Law Society’s new ‘know your client’ requirements enhance public protection,” Media Release, April 29, 2008, *available at* [http://www.lsuc.on.ca/media/apr2908\\_client\\_id.pdf](http://www.lsuc.on.ca/media/apr2908_client_id.pdf).

81. Law Society April 2008 Report, *supra* note 37, at para 33.

82. English developments are reviewed in Colin Tyre, QC, *Anti-Money Laundering Legislation: Implementation of the FATF Forty Recommendations in the European Union*, in this volume.

mentation of FATF-related requirements in order to assess how matters have unfolded where self-regulation has given way to “co-regulation”. In part, it is still early in the process, with legislation most directly affecting lawyers still under development. While the concerns expressed by the Australian legal profession mirror those arising in the Canadian experience—consistency of any new obligations with existing professional obligations, preservation of privilege and confidentiality, and resistance to any “suspicious transaction reporting” regime that would require lawyers to inform on their clients—the process of reform appears to have been quite different, with the Law Council of Australia focused on lobbying government to draft or amend legislation to take its concerns into account, rather than attempting to fend off government legislation and regulation by introducing its own rules and requirements.

The Australian Government’s anti-money laundering reform agenda has proceeded in two phases, or “tranches”. The first tranche was aimed at the financial sector but inadvertently captured some general legal services; the second tranche, currently under development, is directed at a range of other sectors, including lawyers. The *Anti-Money Laundering/Counter Terrorism Financing Act*<sup>83</sup> (the “AML/CTF”) was passed in 2006 specifically to implement FATF standards, and was directed towards financial services, gambling and bullion dealers.<sup>84</sup> It imposes a number of obligations on businesses when they provide particular “designated services”. The obligations include customer due diligence (including identification, verification of identity, and ongoing monitoring of transactions); reporting of suspicious matters, threshold transactions and international funds transfer instructions; recordkeeping requirements; and establishing and maintaining an AML/CTF program in accord with a risk-based approach to regulation. Under the Act, the Australian Transaction Reports and Analysis Centre (AUSTRAC) was given an expanded role as the national AML/CTF regulator with supervisory, monitoring and enforcement functions over a wide range of business sectors.<sup>85</sup>

The Law Council of Australia complained that because of the way in which the AML/CTF Act had been drafted, it captured ordinary trust account activities of legal practitioners. After making representations to AUSTRAC, the Law Council reported in August 2008 that AUSTRAC had finalized a rule exempting lawyers from “designated remittance services”.<sup>86</sup> An exemption for legal services from the

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83. *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (Aus.), No. 169, 2006, available at <http://www.comlaw.gov.au/comlaw/legislation/act1.nsf/asmade/bytitle/AD9D7C024DC9E300CA257244001003BF?OpenDocument>.

84. *Id.*; see the “Anti-money laundering” webpage of the Attorney-General’s Department of the Government of Australia, available at [http://www.ag.gov.au/www/agd/agd.nsf/Page/Anti-money\\_laundering\\_Anti-moneylaundering](http://www.ag.gov.au/www/agd/agd.nsf/Page/Anti-money_laundering_Anti-moneylaundering); see also Australian Government, Attorney-General’s Department, “AML/CTF legislation,” available at [http://www.ag.gov.au/www/agd/agd.nsf/Page/Anti-money\\_laundering\\_AMLCTFlegislation](http://www.ag.gov.au/www/agd/agd.nsf/Page/Anti-money_laundering_AMLCTFlegislation).

85. *Id.*

86. AML/CTF Rules Instrument 2007 (No 1), Chapter 23, (13 August 2008), available at <http://www.comlaw.gov.au/comlaw/management.nsf/lookupindexpagesbyid/IP200730563?OpenDocument>; see also the summary of Rules on the AUSTRAC website, available at <http://www.austrac.gov.au>

definition of providing a custodial or depository service was under consideration, with the Law Council advising that AUSTRAC's position was that legal practitioners whose activities fell within the definition "are legally required to report but it is not [AUSTRAC's] expectation that they will" and that lawyers had the option of applying for a "no action" letter from AUSTRAC if they were not satisfied with the Law Council's general assurance.<sup>87</sup>

The greater concern for the Australian legal profession is the prospect of the reforms in "tranche two". The Law Council noted that from the outset, it had "been proactively engaged in lobbying the Government to ensure that any obligations imposed on legal practitioners are consistent with existing professional obligations and not unduly onerous." Further, the Law Council emphasized, reforms should be precisely targeted and must not subject legal practitioners to a "suspicious transaction reporting obligation that would require them to inform on their clients to regulatory agencies." In a statement to the profession, the Law Council reported that it "has argued that a suspicious transaction reporting obligation would infringe upon client confidentiality and damage the important relationship of trust between lawyer and client."<sup>88</sup>

This question of the impact of any AML/CTF obligations on client confidentiality and legal professional privilege is identified as a "major issue for the legal profession" in a February 2009 Law Council publication, "Anti-Money Laundering Guide for Legal Practitioners."<sup>89</sup> Concerns are expressed that a section of the existing AML/CTF Act providing that the Act does not affect the law relating to legal professional privilege has a narrower application than client confidentiality obligations and that legal professional privilege "may not be as wide as many legal practitioners assume." The Guide goes on to caution that the rules on client confidentiality "may not, therefore, exempt practitioners from AML/CTF reporting obligations and practitioners will need to develop a good understanding of when information was provided in privileged circumstances, and when legal professional privilege applies."<sup>90</sup> It further provides this sobering note: "As with the United Kingdom and other jurisdictions, the application of privilege in relation

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aml\_ctf\_rules.html; *see also* Law Council of Australia, "Legal Practitioners Reporting Obligations under the Anti-Money Laundering/Counter Terrorism Financing Act," 21 August 2008, *available at* [http://www.lawcouncil.asn.au/shadomx/apps/fms/fmsdownload.cfm?file\\_uid=8FC574F9-1E4F-17FA-D2B8-F8C76A23CA8B&siteName=lca](http://www.lawcouncil.asn.au/shadomx/apps/fms/fmsdownload.cfm?file_uid=8FC574F9-1E4F-17FA-D2B8-F8C76A23CA8B&siteName=lca).

87. *Id.*; the "no action" letter guidelines are available at Australian Government, Australian Transaction Reports and Analysis Centre, Guidance Note 08/01, *available at* [http://www.austrac.gov.au/files/gn0801\\_no\\_action\\_letters.pdf](http://www.austrac.gov.au/files/gn0801_no_action_letters.pdf).

88. Law Council of Australia, "Anti-Money Laundering and Counter-Terrorism Financing Reforms," *available at* <http://lawcouncil.asn.au/initiatives/aml-ctf.cfm>.

89. Law Council of Australia, "Anti-Money Laundering Guide for Legal Practitioners," February 2009, p. 5, *available at* [http://www.lawcouncil.asn.au/shadomx/apps/fms/fmsdownload.cfm?file\\_uid=8FCE74BF-1E4F-17FA-D2A2-C549BD6656B4&siteName=lca](http://www.lawcouncil.asn.au/shadomx/apps/fms/fmsdownload.cfm?file_uid=8FCE74BF-1E4F-17FA-D2A2-C549BD6656B4&siteName=lca).

90. *Id.*

to AML/CTF legislation might be an issue which is only given greater clarity by subsequent court cases following the release of any legislation.”<sup>91</sup>

As in the Canadian context, the Law Council of Australia states that another issue for the profession is “who will regulate AML/CTF obligations for legal practitioners.” The Guide notes that the principal regulator is AUSTRAC, that State and Territory legal professional bodies are “currently neither pursuing nor expecting any additional AML/CTF regulatory role, and there are no plans to take an intermediary role in suspicious transaction reporting.”<sup>92</sup> Notably absent from the Law Council’s documents, however, are the rhetorical flourishes about the sanctity of the lawyer-client relationship and about the importance of the self-regulatory independence of the profession found in the Canadian materials. Rather, the emphasis is on active engagement with the Government in representing the interests of the legal profession in the development of Tranche Two of the AML/CTF legislation and a commitment to continuing to do so “vigorously.”<sup>93</sup> Indeed, in assessing the potential supervisory role of the legal professional bodies in respect of AML/CTF obligations, the Law Council notes that “there are also concerns about both the funding of regulatory resources and the potential conflict between adopting AML/CTF regulatory roles whilst also pursuing an advocacy role and lobbying for change in the legislation.”<sup>94</sup>

The Australian position on Tranche Two is still developing, but it is clear that the central concerns of the Australian legal profession—protection of privilege and confidentiality, and the regulation of lawyer conduct—are similar to those articulated by the profession and by legal regulators in Canada. What appears starkly different is the approach being adopted, with a conciliatory, consultative emphasis in the Law Council’s documents. Rather than being perceived as co-option, this may reflect the reality of the changed circumstances in respect to the regulation of the legal profession generally and the need to co-exist in a more consultative, co-operative relationship with the government charged with implementing FATF-related reforms. Without more information than what is publicly available, further comment about the apparent absence of confrontation would be purely speculative; however, approaches to key issues affecting the profession in Australia (including multidisciplinary practice, and incorporation of and public investment in law firms) have been radically different than elsewhere.<sup>95</sup>

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91. *Id.*, at 19.

92. *Id.*, at 5, 20; *see also* the discussion of Suspicious Transaction Reporting and Secrecy of Reporting at 11.

93. *Id.*, at 5, 20.

94. *Id.*, at 20. I found no such concern about a conflict in roles expressed by the Canadian legal professional regulators.

95. *See, e.g.*, Steven Mark, *Views from an Australian Regulator*, *supra* note 4; Paton, *Rock and Hard Place*, *supra* note 3; Paul D. Paton, *Multidisciplinary Practice Redux: Globalization, Core Values and Reviving the MDP Debate in America*, 78 *FORDHAM L. REV.* 2193 at 2240-2242 (noting a cooperative approach between government and the profession in Australia); Christine Parker, *Law*

## Concluding Note

The FATF initiatives to combat money laundering and terrorist financing thus present challenges for lawyers at two levels: in the way in which lawyers conduct business day-to-day, and in the way that governments conceive of the profession's role and independence in an age of terrorism. The client identification and verification rules, and related recordkeeping requirements, represent a potentially costly and cumbersome but ultimately sound set of due diligence practices. While implementing them creates a new treasure trove of records, challenges posed by state enforcement authorities' efforts to investigate and examine lawyer records aren't new. Suspicious transaction reporting requirements, however, more seriously threaten the sanctity of the lawyer-client relationship and the protections of privilege and confidentiality; deputizing lawyers as state agents is anathema to the legal profession's core conception of itself, but in keeping with the increasing willingness of government to treat lawyers as "gatekeepers" with responsibilities both to their clients and to the broader public interest. It is the fact that governments (and courts) are willing to balance those responsibilities that represents a profound shift that the legal profession must confront.

At a macro level, the FATF initiatives present an even more challenging question for the profession in North America: who should regulate lawyer conduct? The 2003 resolution proposed by the ABA Task Force on Gatekeeper Regulation and the Profession, and adopted by the ABA House of Delegates, captured all of these dimensions when it stated its opposition to "any law or regulation that, while taking action to combat money laundering or terrorist financing, would compel lawyers to disclose confidential information to government officials or otherwise compromise the lawyer-client relationship or the independence of the bar."<sup>96</sup> The Law Society of Upper Canada's frank admission that its response in implementing "know your client" rules was directed towards demonstrating that government did not need to regulate in this area signaled the Canadian profession's grave concerns about the potential for FATF implementation to interfere not only with the lawyer-client relationship but with self-regulation itself.<sup>97</sup>

In that respect, as well, the Canadian experience demonstrates a backing away from the ultimate confrontation between government and the profession on this question. The adjournment of the constitutional challenges to federal anti-money laundering legislation might be seen as both government and the profession staring over the precipice, with neither entirely prepared to bet on the eventual out-

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*Firms Incorporated: How Incorporation Could and Should Make Firms More Ethically Responsible*, 23 U. QUEENSL. L.L. (2004); Andrew Grech & Kirsten Morrison, *Slater & Gordon: The Listing Experience*, 22 GEO. J. LEGAL ETHICS 535 (2009).

96. American Bar Association Task Force on Gatekeeper Regulation, Report to the House of Delegates, Recommendation, February 2003, available at [http://www.abanet.org/crimjust/taskforce/gatekeeperresolution\\_v1.doc](http://www.abanet.org/crimjust/taskforce/gatekeeperresolution_v1.doc).

97. Law Society of Upper Canada April 2008 Report, *supra* note 37 at para 33.

come. The fact that the Federation of Law Societies of Canada implemented rules which—apart from mandatory, secret reports on client activities—effectively put into place the substance of the FATF Recommendations is a sign of both prescient compromise and the profession’s anticipatory self-defense in the face of a significant threat to both its core values and to its self-regulatory authority. The fact that government didn’t press the issue of reporting, despite the concern from the Auditor-General that failing to do so would leave Canada in non-compliance with FATF standards, was a sign that it, too, was prepared to compromise. Whether this represents co-option, coercion or cooperation depends in part upon how jaundiced a view one takes about whether the legal profession is acting in the public interest or its own.<sup>98</sup>

In that respect it will also be important to monitor the events unfolding in Australia as the Law Council engages with AUSTRAC and the Australian Government over the implementation of “Tranche Two” of AML/CTF reforms in that country. With self-regulation of the legal profession in that country already effectively replaced by a system of co-regulation, the signs are in place for a cooperative approach between the Law Council and the Australian government, or at least a sanguine recognition by the profession that constructive dialogue and an articulation of the values at stake—as already has been demonstrated with the reforms to existing legislation when unintended consequences were identified—can lead to an end result that reconciles the public interest with the profession’s key concerns.

Neither of these issues—the question of lawyer as “gatekeeper”, and role of government in regulating the legal profession—are likely to go away soon, in the FATF context or otherwise. As Colin Tyre has rightly put it, “this is a tide which is not going to go out again. When national governments get into the habit of having a new resource for obtaining information on criminal activity, they are not going to give it up again very lightly.”<sup>99</sup> In both Canada and Australia, vigilance and sustained engagement by the legal profession’s representatives have been essential in order to check government action. The challenge in both countries, and indeed universally for the legal profession, will be to convincingly articulate why lawyers merit special treatment, why privilege and confidentiality matter, and why self-regulation and the independence of the profession cannot and should not be sacrificed even in the face of a profound and global threat. Globalization of legal services and the increasing prevalence of cross-border practice mean that developments in one jurisdiction affect all. Seeking to serve as constructive contributors to a dialogue with governments about how best to preserve core values and yet serve the public interest will be important not only in addressing FATF implementation but the pressures on lawyers to become “gatekeepers” generally.

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98. See, e.g., DEBORAH L. RHODE, *IN THE INTERESTS OF JUSTICE: REFORMING THE LEGAL PROFESSION* (2000).

99. Remarks by Colin Tyre, QC, panelist, “The Transformative Effect of International Initiatives on Lawyer Practice and Regulation: A Case Study Focusing on FATF and its 2008 Lawyer Guidance,” New Orleans, LA, AALS Annual Meeting, January 2010.

