AMERICAN BAR ASSOCIATION TASK FORCE ON GATEKEEPER REGULATIONS AND THE LEGAL PROFESSION
COMMENTS ON GATEKEEPER PROVISIONS OF FATF CONSULTATION PAPER
April 9, 2003

We are grateful for the opportunity to participate in this second meeting of the Working Group on Gatekeepers (WGG) of the Financial Action Task Force (FATF) to review the FATF Consultation Paper as it relates to lawyers and independent legal professionals. The ABA Task Force has signed and endorses the joint statement by the international legal profession on the fight against money laundering. The nine signatory bar associations submitted the joint statement to the WGG on April 3, 2003.

1. THE PROCESS OF THE CONSULTATION PAPER

At the outset, we applaud FATF for its providing an opportunity to lawyers to participate in the FATF consultation process. At the same time, we are compelled to advocate the urgent need for enhanced due process prior to finalizing the Consultation Paper.

The context of the Consultation Paper is important. FATF, an intergovernmental body of 29 countries and two international organizations, is proposing recommendations that will lead national governments to make laws and regulations that will transform significantly the relationships between attorneys and clients, and affect the role of the attorney that has evolved over centuries and is enshrined in constitutional and national laws.

We believe lawyers should have an opportunity to participate fully in the identification and assessment of alleged problems that give rise to the proposed Recommendations. In the FATF process, identification of the problem B the typologies= exercise B has consisted only of anecdotal information. The affected persons, members of the legal profession, did not have an opportunity to participate in the identification or assessment of the problem.

Furthermore, the legal processionals= opportunity to help shape proposed law and rule making has come only after FATF has proposed the rules and is limited to commenting on two or more alternatives.

The need for additional process in formulating new Recommendations affecting the legal profession around the world is underscored by the fact that the FATF decision-makers are composed primarily of government regulatory and law enforcement officials, not private lawyers working in law firms on international business transactions. While well intentioned, the focus of FATF representatives is limited to anti-money laundering (AML) activities. Their goals are important. However, proper AML rule-making must include detailed knowledge of the roles and work of the legal profession and the

importance of access by all members of the public to justice. It must take full account of the trade-offs that fulfilling AML goals will have. Any informal group of government officials whose sole task is AML rules cannot properly undertake balanced rule-making unless the affected persons are involved at the outset and throughout the process. In this regard, we are seriously concerned that, in the effort to combat and prevent money-laundering, the WWG and FATF have not given adequate consideration to the values recognized in national and constitutional laws of professional confidentiality and trust and independence of the bar.

Our ABA Task Force has had more ample dialogue about the Gatekeeper Initiative and FATF proposals with a United States Government inter-agency group, chaired by members of the U.S. Department of Justice. We have appreciated the opportunity extended to our Task Force by the U.S. government, and have found these discussions more robust and useful. However, these discussions cannot substitute for direct interaction with FATF, especially after the drafts on which our discussions have occurred have changed. Indeed, the ABA Task Force believes that the type of extensive dialogue it has had with U.S. government officials provides a good model for continuing the dialogue with FATF, enabling FATF to have direct input from affected legal professionals around the world. We also note the recent decision of the Government of Canada to withdraw Gatekeeper regulation vis-à-vis the legal profession in Canada, and to engage in a renewed dialogue with the profession. This is another indication of the value and need for continuing the consultation exercise that FATF has initiated with bar association representatives.

We recognize that FATF is working within a time schedule and deadlines it has established. However, the timing for our most recent participation in this exercise illustrates the point. We had approximately less than one week to review the latest revised Consultation Paper and five days to provide written comments after the meeting. Taking account of the time required for transatlantic travel, the timing does not afford the members of our Task Force or other interested persons in the ABA to participate fully in the process. We believe that the rather unique confidentiality issues pertaining to the legal profession, and the special role of the legal profession as an instrument for legal compliance within society, provide compelling reasons for FATF to reconsider its own self-imposed deadlines and schedule.

As a result of the above, we urge FATF to extend the time for issuing a Recommendation covering the legal profession (and perhaps other professionals) and continue the valuable dialogue it has initiated with representatives of the bar. An improved due process will provide better legitimacy for the proposed rules, better ensure their legality at the international and national levels, and better secure a fruitful cooperation between FATF and both legal professionals and interested parties. We believe more cooperation between FATF and the organized bars will lead to effective rules that take into account the special characteristics of the legal profession. The ABA Task Force will devote the resources and make the commitment to pursue a mutually beneficial resolution of this issue within an acceptable time frame.

2. COMMENTS ON THE GATEKEEPERS= PROVISIONS

Notwithstanding our comments on the alternatives below, we continue to object to the FATF Consultation Paper's premise that lawyers are systematically contributing to money laundering and the lawyer's profession should be subject to suspicious transaction reporting (STR) requirements.

We believe the WGG and FATF should start the discussion of lawyers in the Consultation Paper by expressly recognizing the positive role of lawyers in helping assure compliance with law and deterring violations of AML regulations. The future work of the WGG and FATF should strive to continue the positive role played by lawyers in AML regulation and enforcement. This positive role will be furthered by enhancing rather than compromising the independence lawyers and the ability of clients to consult lawyers to ensure legal compliance.

1. Coverage of Lawyers

The potential societal harm from compromising the client-lawyer relationship outweighs any potential gain of the regulation, especially in the U.S. since already lawyers are subject to a wide range of AML controls that do not exist in most of the world. For instance, AML regulations include the requirement to make currency transaction reports (IRS Form 8300). Any transaction other than a currency transaction must utilize a bank or financial institution. Since they are already subject to AML due diligence, imposing the same requirements on lawyers and other gatekeepers is redundant. These prosecutions come with penal and forfeiture sanctions quite disproportionate to those of other countries. Hence, already U.S. lawyers in practice are subject to strong AML regulation. In addition, in the aftermath of the enactment of the USA PATRIOT Act and Executives Orders President George W. Bush issued concerning counter-terrorism in the aftermath of the terrorist attacks of September 11, 2001, U.S. attorneys and legal professionals and persons utilizing lawyers have experienced substantially weakened privacy rights.

Practically speaking, U.S. lawyers lack the ability and resources to undertake the same AML due diligence that financial institutions undertake. Financial institutions receive advisories from bank regulators, are able to exchange information with other financial institutions under Sec. 314(b) of the USA PATRIOT Act, are able to implement filers in payment areas through the application of sophisticated and expensive software customized to the practice of a financial institution, employ third parties to verify customer identification, and take other due diligence measures that are not available to most lawyers, many of whom practice alone or with one or few other lawyers.

With respect to coverage of lawyers, we strongly believe that Alternative 2 in Recommendations 13 and 14 is clearly preferable, namely that lawyers and independent legal professionals should be covered, but only when they are acting as financial intermediaries on behalf of or for the benefit of the client. This is based on our understanding that this alternative is intended to steer

clear of the fundamental attributes of the attorney-client relationship. However, because the proposed recommendation risks compromising the essence of the lawyer-client relationship even in this alternative, the definitions of financial intermediaries and financial transaction must be limited to circumstances in which lawyers and legal professionals are actually transferring, moving and/or holding money or funds of their clients through their accounts.

Although we believe Alternative 2 clearly preferable, we provide suggestions on Alternative 1 if the WGG and FATF decide to use Alternative 1.

The formation of entities clearly involves legal advice, such as complying with federal and state corporate law, determining which of various entities best fulfills business purposes, advising on tax matters, advising on internal corporate law matters, and how the corporate formation may fulfill other business and legal issues. This is clearly within the core elements of giving legal advice. Similarly, the provision of advice on the potential structures of estate, business and tax planning and the implementation of the same involves the core of a lawyers= work, except when lawyers and legal professionals are actually transferring, moving and/or holding money or funds of their clients through their accounts. Innumerable activities of lawyers involve advice about all types of legal matters, such as family matters, participation in natural resource, investment, and commercial activities may in some way touch on financial activities. Yet, these same activities involve the core of a lawyer's services and the notions of legal professional privilege, professional secrecy, and confidentiality (which the joint statement collectively called professional confidentiality and trust). In sum, the scope of Alternative 1 needs to be limited to those narrow situations where lawyers actually transfer, move, and/or hold money or funds of clients through their accounts.

The definition of lawyers and legal professionals requires clarification. As we read the history, FATF appears to use the terms interchangeably but includes "legal professional" as an inclusive term to recognize differences in the way lawyers may be licensed in different jurisdictions. The 2002 Consultation Paper at paragraph 280 states that "legal professionals...is intended to cover lawyers and legal professionals that are licensed or admitted to practice and who work in law firms or are self-employed; it does not cover lawyers who have the status of employees in a legal undertaking that is not in the business of providing legal advice to third parties."

We believe FATF has taken a measured approach by not extending AML requirements to in-house counsel. Such rules may be unnecessary and raise an impossible conflict between the lawyer and his client. For instance, the STR requirement should apply, if at all, to the firm or business; the in-house lawyer has an ethical duty to advise the client to comply with the law. Imposing a separate duty to report on the in-house lawyer would not be productive and would create an inherent conflict between the lawyer and his employer. Moreover, in many non-U.S. jurisdictions the attorney-client privilege does not extend to in-house counsel, so the protections contained in the recommendations for privileged communications would not work. Finally,

to impose obligations on in-house counsel, but not the business entity itself, would indirectly extend the requirements beyond the industries that were intended to be covered.

2. Exemption for Privileged Communications

An important element of the scope of coverage is the scope of the exemption for privileged communications. As mentioned above, the core of a lawyers= services are the principles of legal professional privilege, professional secrecy, and confidentiality (which the joint statement collectively called Aprofessional confidentiality and trust@). The Interpretive Note to Recommendations 13 and 14, pertaining to the scope of the exemption from the SAR requirement, is too narrow. It does not clarify that a reporting obligation does not exist for information obtained in the course of providing legal advice or legal assistance with a transaction, nor does it cover all the types of proceedings (other than judicial) where confidential communications occur. Therefore, it should be revised to clarify that information obtained in the context of providing a client Alegal advice or assistance@, as well as information obtained in connection with Aany type of proceeding, whether judicial, administrative, arbitral or otherwise@ is exempt.

3. Anti-Money Laundering Due Diligence

Recommendations 13 & 14 (as now numbered in the text) delineate the due diligence, including STR requirements for lawyers, notaries and independent legal professionals. Recommendations 13 and 14 refer back -- at least in terms of an option/bracketed text -- to the due diligence requirements of Recommendations 6 - 12, and the reporting and compliance requirements of Recommendations 15-20. Features of the due diligence recommendations (e.g. Recommendations 6- 7) include requirements to identify and "verify" identities, identify the business purpose of the transaction, identify and "verify" beneficial owners, and in some instances, continuing due diligence on the source of the funds (see Recommendation 6(d)). We continue to be concerned about the application to law firms and solo practitioners of due diligence requirements normally applied to "financial institutions" -- the practical and operational ability for lawyers to do the same due diligence as large financial institutions is questionable.

Further dialogue should be encouraged regarding due diligence requirements for lawyers. Therefore, we believe that recommendation 13 should delete references to the due diligence requirements for “financial institutions” (i.e., Recommendations 6-12). Instead, Recommendation 13 should include language to the effect that “lawyers should increase_ adequate due diligence to minimize the risk that unscrupulous clients abuse legal services for many laundering purposes” and “that national regulatory authorities should engage in a dialogue with organized bars in formulating any specific due diligence requirements and/or guidance for lawyers.”

Likewise, the reporting obligations that would be applied to lawyers, subject to the caveat in Recommendation 14, appear to be extremely broad. For example, Recommendation 15 adopts an "objective standard" for "suspicious" (i.e., "reasonable grounds to suspect or suspects") and also applies

to attempted transactions. Inclusion of an objective standard and attempted transactions would prevent the ability of much of the public to consult lawyers on financial transactions, including AML, because both clients and lawyers will fear potential adverse consequences for seeking or receiving advice on the law surrounding financial transactions, including AML requirements. The combination of terms such as "suspicious", "reasonable grounds" and "attempted" create an unworkable degree of uncertainty for the legal profession and clients, particularly in light of criminal sanctions for, infractions and thereby will have an unacceptable "chilling effect" on the attorney-client relationship. Only financial transactions that are completed should trigger a reporting obligation, and a subjective standard of suspicion should be adopted given the vast array of differing circumstances and lawyers that will be involved in any AML regime for the legal profession.

Below as an appendix is suggested wording for Recommendations 13 and 14.

4. Protection from Liabilities for Terminating Client Relationship

Recommendation 16 does not give full legal protection for liabilities arising from a lawyer terminating a client relationship due to the filing of a suspicious transaction report (STR). One way to help remedy this would be to delete the words "for breach of any restriction on" in the second line of Recommendation 16, and substitute "arising from". The protection from liability contained in Recommendation 16 appears to apply to confidentiality obligations imposed by contract, legislation, regulation or administrative requirement. It is not clear that an "ethics rule" or obligation would be covered by the safe haven. This should be explicitly covered in the language of Recommendation 16.

5. Tipping Off

Recommendation 17 contains the "no-tipping off" rule. The Interpretive Note for Recommendation 17 does not provide sufficient comfort for lawyers on the application of the no-tipping off rule. It merely states that lawyers are permitted to "seek to dissuade" the client from engaging in an illegal activity. That does not address the concern of no-tipping off
and conflicts of interest for lawyers. First, the interpretive note assumes the client is engaged in "illegal" activity, not "suspicious activity" that might be permissible but nonetheless be reportable. In such circumstances, a lawyer may not need to dissuade the client of anything illegal. Second, the notion of dissuading the client from activity does not indicate whether you can tell the client that a report will be filed. Third, there is nothing in the interpretive note about withdrawing from the representation and how this is managed in the context of no tipping off rule.

6. Other Matters

1. Enhanced Due Diligence

Recommendation 10 B Enhanced Due Diligence (EDD). EDD for high-risk transactions, such

as Politically Exposed Persons, should not be applied to lawyers because the nature of the definition requires an enormous and disproportionate expenditure of resources.

2. Compliance with AML Due Diligence

A self-regulatory organization (SRO) should supervise lawyers and notaries in the implementation of the WGG provisions [Recommendation 27(b)]. Only supervision by a SRO will ensure adequate protection to the values recognized in national and constitutional laws of professional confidentiality and trust and independence of the bar.

Appendix

Recommendation 13 --

e) Lawyers, notaries and independent legal professionals when they:

Alternative 1

[(i) Participate in the execution of financial transactions for their client concerning the

* buying and selling of real property or business entities;
* holding, transferring or moving of client money, securities or other assets;
* holding, transferring, or moving of assets in bank, savings or securities accounts;
* handling financial contributions for the creation, operation or management of companies;
* funding of trusts, companies or similar structures;

(ii) or when acting on behalf of and for their client in transferring financial assets in a financial or real estate transaction.] or Alternative 2 [when they carry out financial transactions for a client.]

Recommendation 14 --

Alternative 1

14. [The requirements set out in Recommendations [15 to 20] apply to designated non-financial businesses and professions in the same manner as for financial institutions, subject to the following qualifications:

a) [Lawyers, notaries and independent legal professionals should be required to report only when they:

i. Participate in the execution of financial transactions for their customer concerning the

* buying and selling of real property or business entities;
* holding, transferring or moving of client money, securities or other assets;
* holding, transferring or moving of assets in bank, savings or securities accounts;
* handling of financial contributions for the creation, operation or management of companies;

* funding of trusts, companies or similar structures; or

ii. Act on behalf of and for their customer in transfering financial assets in a financial or real estate transaction.

Alternative 2
[14. The requirements set out in Recommendations [15 to 20] apply to designated non-financial businesses and professions when they carry out "financial transactions for a client.]

Lawyers, notaries, independent legal professionals, and accountants acting as independent legal professionals, are not required to report suspicious [transactions] if the relevant information was obtained in circumstances where they are subject to rules of confidentiality, professional secrecy and/or legal professional privilege.

For purposes of Alternatives 1 and 2, participating in the execution or carrying out of financial transactions should be interpreted or defined to mean "transferring money or financial assets".

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