

Risk Update • November 2022

Anti-money laundering (AML)



The Solicitors Regulation Authority (SRA) has published its [AML annual report](#). The report identifies several common areas of weakness which accord with our experience from conducting law firm audits, including failures in relation to client due diligence, firmwide risk assessments (FWRA) and policies, controls and procedures. In particular, the SRA said firms need to do more work on source of funds. Misuse of client

account as a banking facility where there is no underlying transaction has been a key theme in matters which the SRA reported to the National Crime Agency; the SRA's [updated guidance on Integrity](#) mentions the case of a solicitor struck off for being reckless, but not dishonest, in making improper transfers from client account.

29 firms or individuals have been fined for a variety of AML breaches and eight referred to the Solicitors Disciplinary Tribunal which has imposed five fines and three suspensions.

The report notes that '[in] some of the best examples the SRA saw it was clear the person undertaking the FWRA had worked closely with various teams and partners across the business to assess the risks'. This is something we have always done when assisting firms in preparing their FWRAs. The report also noted the need to update FWRAs regularly – and that some firms had not done this.

Note that the Legal Sector Affinity Group (LSAG) guidance states that the FWRA must be a distinct written document, rather than part of a general overall risk assessment. As mentioned in our September 2022 Risk Update, it needs to cover proliferation financing, on which LSAG guidance is expected soon, and we have been assisting firms with this when reviewing and updating their risk assessments.

Perhaps surprisingly the number of firms regulated by the SRA within the scope of The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 is only 6,408 out of 9,770 (April 2020 figures). We query whether there may be some which have not recognised, and hence not declared, that they are doing work within the scope of the regulations. Tax advice is a risk area, as it can creep into many areas of practice such as employment, personal injury and family, particularly following the changes introduced by The Money Laundering and Terrorist Financing (Amendment) Regulations 2019.

There are constant changes to assessment and treatment of country risk and high risk jurisdictions. Links are provided on www.legalrisk.co.uk/News. Myanmar is added to the Financial Action Task Force (FATF) black list, Democratic Republic of Congo, Tanzania and Mozambique added to the grey list, and Pakistan and Nicaragua removed from the grey list. Many firms rely solely on the Transparency International Corruption Perceptions Index but other sources should also be considered; see for example the Basel AML Index 2022. We use a weighted compilation of these and a number of other sources for our assessment.

A proposed amendment to section 1 of the Legal Services Act 2007 in the Economic Crime and Corporate Transparency Bill will, if passed, add 'promoting the prevention and detection of economic crime' to the regulatory objectives.

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Note

This newsletter is a general guide. It is not a substitute for professional advice which takes account of your specific circumstances and any changes in the law and practice.

Subjects covered change constantly and develop.

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Professional indemnity insurance (PII) - and Solicitors Indemnity Fund (SIF)

Over the years we have acted for solicitors against insurers for cover against claims for reimbursement of fees received which have been hotly contested. In the recent case of *Royal & Sun Alliance Insurance Ltd* [2022] EWHC 2589 (Comm), Northern Irish solicitors succeeded in a claim for indemnity from insurers in respect of such a claim; the judge concluded that a claim for damages against the firm in the amount of its fee to which it had acquired a contractual right under a subsisting contract constitutes a loss to the firm for which they are entitled, if the other pre-requisites to cover are established, to an indemnity under the policy. (See www.legalrisk.co.uk/News for a link.)



At a recent conference in the USA, two underwriters indicated that they expect that in 2024-5 we shall see claims attributable to home working during the Covid lockdowns attributable to the loss of learning by osmosis and junior lawyers not asking questions because they do not know what to ask and making decisions they should not be making. These are gaps which persist with hybrid working.

The SRA has issued a further consultation paper, [Consumer protection for post six-year negligence](#), in its long-running campaign to replace SIF, which provides indemnity to solicitors and their staff after expiry of the compulsory six years' runoff under the Minimum Terms and Conditions.

The good news is that the SRA now accept that the appropriate solution is an indemnity fund rather than a discretionary compensation fund; previous proposals for the latter would not have provided protection for solicitors and their staff, and would have provided inadequate protection for claimants. The SRA's acceptance of this fundamental principle is welcome.

However, the SRA's proposal is predicated on savings of £300,000 - £400,000 to be made by taking the arrangements in-house. The SRA decided to do this at its September 2022 board meeting. We believe the underlying analysis is flawed and those savings are unlikely to be achieved. We explain why in more detail in an [article](#) on our website.

The deadline for submission of responses is 3 January 2023. For the reasons explained above, responses should not in our view be confined to the two questions posed by the SRA, but the more fundamental question of whether the decision to bring the indemnity fund in-house is warranted to avoid post-transaction remorse, a concept well known to those experienced in defending professional liability claims.

Fiduciary duties and retainers

[Belsner v CAM Legal Services Ltd](#) [2022] EWCA Civ 1387 has attracted much publicity in relation to costs, particularly success fees in low value road traffic claims. We mention it here because the Court of Appeal reversed the decision of the judge at first instance holding that solicitors owed a fiduciary duty when nego-

tiating the terms of their retainer with a potential client. Note however that the decision does not preclude a duty being owed when negotiating a subsequent change to the retainer, including revision of charging rates.

Data protection and information security

The Information Commissioner's Office has [fined Interserve](#) £4.4m following a data breach. Of interest to law firms, the breaches included outdated systems, inadequate endpoint security, and failure to train staff in relation to phishing emails.

Meanwhile, in the United States, the Securities and Exchange Commission has [fined Morgan Stanley](#) \$35m for exposing customers' data by disposing of unencrypted back up drives and tapes through an intermediary which auctioned them online without first erasing them.

Sometimes while checking open source internet sites for client due diligence purposes, it is possible to come across sites of uncertain provenance; do you proceed to check it out, or fear criticism for not doing so? A free resource for checking websites is now available: <https://www.getsafeonline.org/checkawebsite/>.