



HM Treasury

**Consultation on: Reform of the Anti-Money Laundering
and Counter-Terrorism Financing Supervisory Regime**

A response by
CILEx Regulation

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Introduction

This response represents the views of CILEx Regulation (CRL), the regulatory body for Chartered Legal Executives, CILEX Practitioners and legal entities. Chartered Legal Executives (Fellows) are members of the Chartered Institute of Legal Executives (CILEX). CILEX Practitioners are authorised by CRL to provide reserved legal activities. CILEX is the professional body representing around 16,500 members and is an Approved Regulator under the Legal Services Act 2007 (LSA). Fellows and CILEX Practitioners are authorised persons under the LSA. CRL regulates all grades of CILEX members.

CRL is also a regulator of entities through which legal services are provided. It authorises entities based upon the reserved and regulated activities.

CRL and CILEX provide an alternative route to legal qualification and practice rights allowing members and practitioners, who do not come from the traditional legal route to qualify as lawyers and own their own legal practice.

CILEX became an approved supervisory authority for money laundering on 6 February 2015. Its authorised entities are supervised by CRL as the independent regulator of CILEX members, CILEX Practitioners and entities.

CRL is a member of the Legal Sector Affinity Group and the AML Supervisors forum and supports the aims of reinforcing a risk-based approach across all sections of the Anti-Money laundering and counter-terrorist finance regime.

Its authorised entities and a small number of individuals working as sole practitioners are supervised for money laundering compliance.

HM Treasury – Reform of the Anti-Money Laundering and Counter-Terrorism Financing Supervisory Regime Consultation

Specific Comments Objectives

1. Do you agree that increased supervisory effectiveness, improved system coordination, and feasibility are the correct objectives for this project? Do you agree with their relative priority? Should we amend or add to them?

CRL believes that these are the correct objectives for this project, and also agrees with their relative priority. It is also important that all unintended consequences of meeting these objectives are considered fully (impact on general regulation) and that there is appropriate oversight in place for the chosen model to ensure that the effectiveness.

OPBAS+

2. What would the impact be of OPBAS having the FCA's rule-making power? What rules might OPBAS create with a new rule-making power that would support its aim to improve PBS supervision?

This would mean that OPBAS would have an increase in its authority and potential effectiveness through these powers, leading them possibly to adopt a more constructive and risk-based approach to their use. The effectiveness of PBS supervision could improve by tailoring regulations to particular professions and sectors, as well as jurisdictions, and not just having an oversight role but setting the dialogue on changes to supervision alongside PBS. That may allow better focus on higher risk issues.

There would need to be appropriate transparency and oversight of the increase in OPBAS powers and how they were used and implemented. PBSs would expect to be consulted on any proposed changes.

3. Which, if any, of these powers should OPBAS be granted under this model? Are there any other powers that OPBAS could be granted under this model to aid OPBAS in increasing the effectiveness and consistency of PBS supervision?

CRL believes that of the additional powers suggested the most difficult to implement would be that to restrict or reduce supervisory populations as this could have a wider impact than just on AML supervision. These powers also only focus on sanctioning powers rather than being constructive in allowing OPBAS to actively develop the supervisory regime in areas such as information sharing, shaping how reliance can be used through new technologies, and improving liaison with law enforcement.

It is also difficult to envisage how this could be implemented quickly, easily and in a cost-effective way that actually would provide effective supervision. Presumably this would only be for a short time and therefore the impact on the supervised population would be disproportionate.

4. What new accountability mechanisms would be appropriate in order to ensure proportionate and effective use by OPBAS of any new powers?

CRL agrees with the proposed accountability mechanisms for OPBAS suggested in the consultation.

It is important that accountability and an ability to appeal a decision by OPBAS is in place to ensure fairness and transparency. It is vital that HM Treasury should take a more critical oversight of OPBAS, requiring them to publicly explain the use of its powers, including interventions, in its reporting to HM Treasury, and to communicate this to PBSs.

5. Do you have evidence of any specific types of regulated activity which are at high risk of being illegally carried out without supervision?

CRL has provided HM Treasury with examples of unregulated firms offering estate administration/probate work that may appear to require supervision. CRL does not have evidence of illegal activity but believe that if the legal sector is to present a consistent standard of AML supervision, then a 'default supervisor' should be investigating these firms.

6. Do you think a "default" legal sector supervisor is necessary? If so, do you think a PBS could be designated as default legal sector supervisor under the OPBAS+ option?

CRL believes that it is important that a "default" legal sector supervisor is put in place to detect unsupervised firms carrying out activity within the scope of the MLRs and ensure that the MLRs apply consistently across both the regulated and unregulated legal sector. CRL has shared examples with HM Treasury, and this has been raised by its supervised community as an issue.

CRL cannot comment on whether a "default supervisor" is required for the devolved administrations

7. Overall, what impact do you think the OPBAS+ model would have on supervisory effectiveness? Please explain your reasoning.

Depending on how OPBAS uses any new powers, and whether they are prepared to be creative in adapting to differences between the supervised communities, then there is an opportunity to improve supervisory effectiveness further. This would allow a truly risk based approach, focusing resources by supervisors, and support by OPBAS, on areas of higher risk.

8. Overall, what impact do you think the OPBAS+ model would have on system coordination? Please explain your reasoning.

The OPBAS+ model will not address the external concerns related to the current multi supervisor regime and the perception of inconsistencies, fragmentation, and supervisory gaps.

However, the additional powers under the OPBAS+ model could be utilised beneficially by OPBAS to enhance system coordination.

9. Overall, how significant do you think feasibility constraints would be for the OPBAS+ model? Please explain your reasoning.

The OPBAS+ model would be the easiest option to implement in a short space of time, with the least disruption across the regime, however against that needs to be consideration as to whether it meets all the required outcomes. CRL cannot really comment on whether the required legal and regulatory changes can be implemented in a timely manner, but it is assumed that there would be the necessary government impetus behind any proposed changes.

Of concern for the PBS would be an increase in the OPBAS levy where a few PBS do cover the majority of OPBAS costs. The current lack of transparency remains a frustration.

PBS Consolidation

10. Were we to proceed with the PBS consolidation model, what would the relative advantages be of (a) a UK-wide remit, (b) retaining separate PBSs in the Devolved Administrations? Which would best achieve the consultation objectives? Please answer with explicit reference to either the legal sector, the accountancy sector, or both.

The following comments of CRL relate solely to the legal sector. The two sectors are very different and operate under distinct legislative regimes. Consolidation of supervision of the two sectors is not considered a feasible option.

In answering questions 10 - 22, CRL believes that there should only be a devolved approach taken to PBS consolidation in the legal sector (i.e., 3 Consolidated PBS legal sector supervisors, one for each devolved administration) and that having separate divisions within a single supervisor would not work.

Increased supervisory effectiveness

CRL believes that by understanding the risks, challenges and make up of our supervised population through its general regulation has enabled it to have a suitable and effective supervisory regime in place. It has developed and expanded the information available to its supervised community and has a good working relationship with CILEX which aids their mutual effectiveness.

The move away from a local understanding of the risks that firms face may not actually increase supervisory effectiveness, as well as being seen as onerous to the supervised community. CRL currently has positive engagement with its supervised community, which enhances its supervisory effectiveness. CRL does not believe it is clear what residual responsibilities will sit with non-PBS supervisors nor the professional bodies such as CILEX. There is no evidence that smaller supervisors are not able to respond quickly to new risks or challenges.

There is a risk that expertise and knowledge may be lost from non-PBS with a move towards consolidation, as the perception will be that that is where all the knowledge and opportunities will reside in the future.

Improved system coordination

Whilst this model will reduce the number of PBS that need to be engaged with, looked at on risk-based approach there has to be consideration as to whether it will lead to more effective system coordination or just a smaller number of people at meetings.

The loss of specialist knowledge about the particular professions and the risk they pose may be the counter to adoption of this model.

Feasibility

CRL does not believe consolidation of PBSs across the devolved administrations could be achieved quickly or easier due primarily to the differing legislative regimes. However, if three devolved supervisors are retained then it would be easier and quicker.

CRL believes that AML compliance supervision (and financial sanctions supervision) logically fits with information gathered by the PBS as part of its general legal supervisory action. This information feeds into an understanding of the work of a firm and the risks posed to it. For example, if a firm moves into a new area of work that has AML compliance considerations currently the CRL recognises this and ensures that changes are made to the firms AML processes and procedures. Under the new model how would this information flow without creating a dual system of supervision?

The risk is that the consolidated legal sector PBS model creates more burden on business, is particularly onerous for small firms and sole practitioners, creates confusion around gatekeeping responsibilities, and has implications for data sharing/administrative issues, including GDPR, and costs between the respective consolidated PBS supervisor and the non-PBS supervisors.

As with all the following models, there are additional cost and resource implications to be considered for all parties because the consolidated PBS will be required to keep data and intelligence separate from its own general regulatory work. How and who would pay for this? CRL therefore does not believe this model will produce reduce costs and efficiency.

There is also the risk that this will cause firms to move all regulation to the consolidated PBS, were this is feasible, because it is perceived as easier to have one 'supervisor' rather than two to supply information to. This needs to be carefully considered.

CRL also wishes to mention that the consultation document states that this model will '*reduce inconsistency and complexity by ensuring only the highest performing supervisors remained*'. If in E & W there is one consolidated PBS, then the implication could be that all others are low performing.

Given the disparate sizes of the PBS, it is likely that only one will ever be able to take on the role of a consolidated PBS.

11. How could HM Treasury and/or OPBAS ensure effective oversight of consolidated PBSs under this model? Would it be appropriate to provide OPBAS with enhanced powers, such as those described in the OPBAS+ model description?

CRL agrees that enhanced powers such as those described under the OPBAS+ model may be appropriate for effective oversight of a consolidated PBS model.

12. Under the PBS consolidation model, do you think that HMRC should retain supervision of ASPs and TCSPs which are not currently supervised by PBSs? Why/why not?

CRL does not believe it should comment on changes directly impacting the accountancy sector.

13. What would the impact be of consolidated PBSs having a more formal role in identifying firms carrying out unsupervised activity in scope of the MLRs? What powers would they need to do this?

The consolidated PBS responsible for identifying firms carrying out unsupervised activity in scope of the MLRS would need to have similar legal powers in place to enable it to require information from such businesses, inspect them and to provide it with powers to require such businesses to cease their unsupervised activities. This may go beyond what a PBS would have for its own supervised population.

There would need to be consideration as to who would fund this activity by the consolidated PBS.

14. Under the PBS consolidation model, what would the advantages and disadvantages be of a consolidated accountancy or legal sector body supervising a range of different specialisms/professions for AML/CTF purposes?

CRL has covered this in the answer to Question 10.

15. What steps, if any, could HM Treasury take under this model to address any inconsistencies in the enforcement powers available to supervisors?

HM Treasury should ensure that the 'consolidated PBS' has retained or been given effective enforcement powers over the consolidated supervised population, so that there is no diminution in the powers available to them to take appropriate action.

There then needs to be a clear relationship between these and any disciplinary processes within the former PBSs who are no longer delivering AML supervision because effectively an individual would be subject to two disciplinary processes.

16. Which option, to the extent they are different, would be preferable for providing for supervision of non-members under the PBS consolidation model? Are there alternatives we should consider?

CRL believes that the first option is preferable.

17. What powers, if any, might be required to minimise disruption to ongoing enforcement action and to support cooperation between the PBSs retaining their AML/CTF supervisory role and the PBSs which are not?

It will depend on how the enforcement action is being carried out but as the numbers of enforcement actions are relatively low, these should be transferred to the relevant consolidated PBS as soon as possible. Otherwise, consideration will need to be given to transition arrangements under any legislative changes. CRL believes that OPBAS could have a role in coordinating this process.

18. Overall, what impact do you think the PBS consolidation model would have on supervisory effectiveness? Please explain your reasoning.

CRL does not believe that the PBS consolidation model would necessarily lead to increased supervisory effectiveness. It will depend on how the operational model is designed especially around collection and sharing of information from supervised entities. There has been no discussion regarding the residual responsibilities of PBS for supervisory effectiveness as they will presumably no longer be listed within the MLRs.

However, there does remain the risk that it will just create increased regulatory cost for all parties because of increased operational complexity, for example, who will pay for any separate IT system that the consolidated supervisor will need to maintain data related to supervised entities of other PBS.

19. Overall, what impact do you think the PBS consolidation model would have on system coordination? Please explain your reasoning.

If the number of PBS's are reduced, and one organisation is interpreting and setting standards then clearly that makes it easier for information and intelligence sharing between the consolidated PBS and law enforcement agencies. What that means for the responsibilities for non-PBS regulators needs to be made clear, especially in relation to general regulation of legal services, where presumably the consolidated PBS will need to co-ordinate actions with them.

Also, that will make it easier to engage with other stakeholders and parties.

20. What additional powers or tools, if any, could enable OPBAS to ensure the transition to a new model is smooth and supervision standards do not fall in the interim?

If the decision was made to adopt this model, then OPBAS would need to work with the nominated consolidated PBS to project manage the role and oversee transition arrangements, particularly with regard to communications to the supervised populations.

They would need to seek agreement on the operational basis of the model especially with regard to data sharing and residual activities for the non-PBS regulators. This all needs to be decided early to enable appropriate powers and resources to be made available to OPBAS to facilitate this.

21. How do you believe fees should be collected under the PBS consolidation model?

The cost of AML supervision is covered within the usual practice fee charged to a firm by CRL, rather than being a separate fee. The consolidated PBS supervisor will need to charge fees to cover the cost of carrying out supervision on behalf of other existing PBS in the sector (which could not be subsidised from other existing income). Any fee is likely to be passed directly to supervised entities, rather than absorbed by the previous PBS.

Presumably the consolidated PBS will need to adopt a similar fee structure for its own population, so there should be a discussion around the issuing of fee invoices directly to all supervised entities. It is unclear at present what residual role the non-PBS supervisors retain.

22. Overall, how significant do you think feasibility constraints would be for the PBS consolidation model? Please explain your reasoning.

The feasibility constraints would be less significant based on a devolved administration approach.

SPSS

23. Do you agree these would be the key structural design features to consider if creating a new public body (whether it was an SPSS or an SAS)? Should anything be added or amended?

CRL agrees that those suggested are the key structural design features to be considered. It is assumed that appropriate legislation and structures, including enforcement and resourcing, will be put in place to cover all authorities.

24. If an SPSS were to be created, which sectors do you think it should supervise?

CRL generally agrees with the analysis as set out in Appendix G.

25. Were an SPSS to be created, what powers should it have?

CRL is content with the powers suggested in the consultation but believes that further consideration will be required around the relationship of the SPSS with the professional bodies (in future presumably not listed in the MLRs) and other stakeholders including law enforcement.

For example, the basis on which information and intelligence can be shared between the parties and the use of technology to aid effectiveness in AML supervision.

26. How should enforcement responsibility be transferred should an SPSS be created?

CRL believes that a measured approach would be better to ensure consistent supervisory outcomes during the transition period.

27. What powers should HM Treasury have to oversee an SPSS?

CRL believes that the SPSS chosen must enable the continuing independence of the legal profession, without interference from Parliament. That needs to be preserved without the oversight structure that is put in place.

28. Overall, what impact do you think the SPSS model would have on supervisory effectiveness? Please explain your reasoning.

The current structure means that AML (and sanctions) supervision is now an inherent part of general professional regulation, certainly amongst the legal regulators. The challenge of the SPSS model is how does this operate effectively and add value when the existing structures for professional regulation will remain in place.

Therefore, the perceived benefits that might occur related to consistency of supervisory outcomes, interaction with law enforcement, use of technology and more effective “policing of the perimeter”, are countered by duplication of information required from supervised entities, issues related to data sharing, the same need to have relationships with the underlying professional bodies but the loss of live risk knowledge and experience from those bodies.

There is a question as to how the various individual professions would view this type of model being effectively a new supervisory body to which they would be reporting. It may impact on the current relationships with PBSs and the supervisory effectiveness and achievement of required outcomes.

29. How significant would the impact be on firms of splitting AML/CTF supervision from wider regulatory supervision in the sectors to be supervised by the SPSS?

CRL believes that this would create a significant impact and increased regulatory burden on firms, with potentially significant duplication of information and checks required on firms, with little perceived benefit to the vast majority. It would have most impact on smaller firms and sole practitioners.

CRL does not believe that these issues could simply be mitigated by “certificates of good standing”, without creating a shadow system of AML supervision by the PBS.

30. Overall, what impact do you think the SPSS model would have on supervisory effectiveness? Please explain your reasoning.

This question was answered at Question 28.

31. Overall, how significant do you think feasibility constraints would be for the SPSS? Please explain your reasoning.

CRL does not foresee the transfer to a SPSS as something that could be achieved quickly and given this, then wider considerations regarding future structures of regulation across the sectors might also need to be considered to gain any real benefits in supervisory effectiveness.

The complexity of the UK legal framework and regulatory mechanisms, including the devolved nations, also adds to the feasibility constraints for an SPSS.

CRL has highlighted the issues related to operations, the size, scale and diversity of the professional bodies and supervised populations, and that it may just move existing challenges to a different body without producing the benefits sought and losing valuable knowledge from the sectors.

SAS

32. Do you foresee any major challenges for effective gatekeeping, under either the SPSS or SAS model? If so, please explain what they are, and how you propose we could mitigate them?

If these are assumed as the preferred option, then they will need to set the standards and checks for any appropriate gatekeeping. A decision will have to be made as to whether these checks are part of membership of the associated stakeholders, or the SPSS & SAS are going to operate their own individual gatekeeping function. The standards will need to be agreed across all parties.

Then systems will need to be put in place to manage the data required, but this should be feasible.

33. Overall, what impact do you think the SAS model would have on supervisory effectiveness? Please explain your reasoning.

The issues raised in the answer to Question 28 would become even greater as the supervisory body becomes more remote from those they are supervising,

34. Does the separation of AML/CTF supervision from general regulatory activity present a major issue for those firms currently supervised by the statutory supervisors? Please explain your reasoning.

Please refer to the points raised in the answer to Question 29. Again, the issues raised would be even greater given the wider scope, size and nature of an SAS.

35. Overall, what impact do you think the SAS model would have on system coordination? Please explain your reasoning.

The impact on system coordination will be dependent on whether the underlying systems remain as they are or whether changes are also made to their structures. So, there could be benefits where there are a small number of stakeholders, for example between national and international organisations.

It really depends on where it is believed that the greatest impact on supervisory effectiveness can be made by the changes and the acknowledgement that the creation of a SAS might impact on effectiveness of relationships and thereby direct supervision between professional bodies and the SAS

36. Overall, how significant do you think feasibility constraints would be for the SAS? Please explain your reasoning.

Please refer to the points raised in the answer to Question 28. Again, the issues raised would be even greater given the wider scope, size and nature of an SAS.

Sanctions

37. Given the change in the sanctions context in the UK since Russia's invasion of Ukraine, have supervisors changed their approach to oversight of sanctions systems and controls amongst regulated populations? If so, what activity has this entailed?

CRL has provided HMT with details of its supervisory action related to sanctions in the latest supervisory annual return and this covers the actions CRL has undertaken to understand and assess our supervised population's exposure to sanctions regimes and individuals, specifically at the moment, Russia and Belarus.

Currently the legislation puts the supervisory responsibility with OFSI, so the work CRL has carried out is to ensure firms compliance with legislation as required under our Code of Conduct, rather than under direct powers CRL gains from that legislation.

CRL has questioned firms on their understanding of the sanctions regime, their appetite to engage with sanctioned individuals or entities, and the mitigations & controls that they have in place. This information gathering has now been embedded within its AML assessment and assurance work both when firms are first authorised and as part of their annual return.

CRL has added significant information on financial sanctions to our website and directly to firms.

38. Do supervisors need additional powers to monitor sanctions systems and controls effectively, or can this be done under existing powers? What would any new powers need to consist of?

CRL believes that additional powers, similar to those granted under the MLRs, are necessary to become a fully effective sanctions supervisor and define the difference with OFSI.

The sanctions regime applies to all firms, rather than just those whose work falls with the scope of the MLRs. Therefore, an extension to its powers to request and review information, share intelligence, review processes and procedures and enforce against would be sensible.

These need to be considered alongside the new regulatory objective related to economic crime and the expectation that this will pose on legal sector regulators.

39. Aside from legislative powers, do you foresee any other barriers to supervisors effectively monitoring sanctions systems and controls?

As CRL has stated for many small and medium sized supervisors, sanctions supervision is delivered as part of the wider supervisory activities alongside legal services regulation /supervision and AML supervision. With the new regulatory objective related to economic crime being added for the legal sector, there needs to be real consideration of what is the most effective model to work towards that benefits all stakeholders.

The knowledge that is required to carry out all these supervisory activities effectively is entwined and therefore the impact of differing bodies delivering this supervision needs to be carefully considered, as there is the risk of increasing regulatory cost to those being supervised. That ultimately could impact on consumer choice, so needs to be recognised and acknowledged.

Regarding staff, it may be that in depth knowledge of a firm is best for supervision rather than specific knowledge of sanctions but more arm's length in delivery and understanding.

40. *Should any new potential supervisory powers relating to sanctions broadly cover all types of UK sanctions?*

Yes, this would be sensible and would mean that any future type of sanctions could come under these supervisory powers.

Options Comparison

41. *How would you expect losing AML/CTF supervision to affect PBS' financial models, and the fees charged to supervised populations?*

CRL can only really comment on its own financial model, where the cost of AML supervision is covered within the usual practice fee charged to a firm. It is unlikely that there would be any substantial reduction, if at all, in fees if AML supervision was moved away from CRL.

It needs to be considered that any other supervisor will need to charge fees to cover the cost of carrying out supervision on behalf of other existing PBS in the sector (which could not be subsidised from other existing income). Under the current AML supervisory regime information is only collected once by each legal sector PBS; under the options presented there will be duplication of information and this will undoubtedly have a cost that will be passed on. Any fee is likely to be passed directly to supervised entities, rather than absorbed by the previous PBS.

It also needs to be considered whether the existing levy payable to OPBAS fee will continue, which will be dependent on whether OPBAS continues.

42. *Based on your experience and the considerations set out in this document, what is your analysis of the relative extent to which each of the four reform options would lead to (a) improved supervisory effectiveness and (b) improved system coordination.*

CRL believes that there are inherent challenges with each model, and it really depends on the strategic direction of supervision and regulation in the UK as to which is the most appropriate at this point.

The OPBAS+ model retains the simplicity of approach linking to ongoing legal regulation and can be seen as the most cost-effective. Of the others the cost requirements and regulatory burden will increase on supervised entities as there is greater consolidation. If PBS Consolidation is required to satisfy a reduction in PBSs, then it has to be on a devolved basis.

CRL has set out why SPSS and SAS are not considered options that can be easily adopted and cause greater tension with the underlying general legal regulation that is in place in this sector.

Public Sector Equality Duty

43. Are you able to provide evidence as to how the options set out in this document would help or harm individuals or households with protected characteristics?

No comment.

Any questions relating to this consultation response can be directed to David Pope, Director of Operations (david.pope@cilexregulation.org.uk).