

# Sectoral Risk Assessment 2019



## INTRODUCTION

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As an AML supervisor, CILEx Regulation is required to set out information on money laundering and terrorist financing risk that we consider is relevant to those we supervise. This is our first annual update to the sectoral risk assessment we published in March 2018.

We have identified and assessed the international and domestic risks of money laundering and terrorist financing to which you are subject. Alongside the National Risk Assessment, the information in this sectoral risk assessment is designed to assist our firms in carrying out their own money laundering and terrorist financing risk assessment. It reflects changes to the risks to which firms may be exposed based upon intelligence gathered from a variety of sources.

### Money Laundering

Money laundering is the generic term used to describe the process by which criminals disguise the original ownership and control of the proceeds of criminal conduct by making such proceeds appear to have derived from a legitimate source. Money laundering also includes money that is used to fund terrorism.

Every business covered by the money laundering regulations must be supervised by a supervisory authority.

The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (“the money laundering regulations”) set the administrative requirements for the anti-money laundering regime within the regulated sector and outline the scope of customer due diligence. The regulations aim to limit the use of professional services for money laundering by requiring professionals to know their clients and monitor the use of their services by clients.

### Our responsibilities

CILEx Regulation is fully supportive of the government’s intention to strengthen the supervisory regime, taking our responsibilities seriously to help implement a coherent and effective risk-based approach. This means both CILEx Regulation and our supervised firms focusing efforts where risks are highest.

We will work to build trust in the legal system, tackling professional enablers of money laundering, and helping to support our members and firms to raise standards and reduce money laundering. We want our firms to ensure that their clients and the legal system are protected and not just adopt a tick box approach to compliance with rules.



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We will ask to see your firms' written risk assessment as part of our routine supervision, but this must remain confidential and should not be disclosed to customers, or third parties.

In carrying out this sectoral risk assessment we are required to consider:

- a) reports published by the Commission under Article 6.1 of the fourth money laundering directive;
- b) guidelines issued by the European Supervisory Authorities under Articles 17, 18.4 and 48.10 of the fourth money laundering directive; and
- c) the National Risk Assessment 2017.

## Who do the regulations apply to?

The money laundering regulations place obligations on firms offering services that are most likely to be targeted by those wishing to launder money. These include independent legal professionals, and trust or company service providers.

You must consider whether the activities you carry out mean that you are subject to these regulations. For example, carrying out estate administrations' and holding client money or providing company formation services.

All firms, both regulated and unregulated, that are within scope of the money laundering regulations must take appropriate steps to identify and assess their risk of being used for money laundering or terrorist financing.

## Your own risk assessment

The money laundering regulations require that you must identify and assess the risks of money laundering and terrorist financing to which your own business is subject.

In carrying out the risk assessment this will help you understand the risks you face and mean that you should be better prepared to counter them if you were to be targeted.

You must take into account:

- a) information made available to you by CILEx Regulation, including this risk assessment; and
- b) risk factors including factors relating to:
  - (i) your products and services;
  - (ii) your consumers and clients;
  - (iii) your transactions;
  - (iv) your delivery channels; and
  - (v) the countries or geographic areas in which you operate.



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Your firm's risk assessment must be kept up to date and in writing. In deciding what actions are then necessary following the assessment, you should consider the size and nature of your business.

## National Risk Assessment

The 2017 National Risk Assessment highlighted that legal services remain attractive to criminals due to the credibility and respectability they can convey, helping to distance funds from their illicit source and integrate them into the legitimate economy.

While some proportion of those legal service providers involved in money laundering cases are complicit, the majority of these cases are likely to involve those who are either wilfully blind or negligent.

Although legal services are at a high risk of exploitation for money laundering, they are not judged to be attractive for terrorist financing, so the risk associated with the sector is assessed to be low.

The services at highest risk of exploitation are trust and company formation, conveyancing and client account services. Whilst legal executives are assessed to be exposed to lower risks, as they can now offer all these services they should be aware of the risks connected to them.

National Crime Agency investigations have also highlighted that criminals may use a combination of legal services to add layers of complexity to a transaction and hamper effective due diligence. This is a future risk for our regulated firms.

## Financial Action Task Force Review of UK Anti-money laundering and counter-terrorist financing measures

The review, published in December 2018, highlighted an inconsistent level of AML compliance across the professional bodies, including the relatively low level of suspicious activity reports (SARs) outside of the financial sector.

Demonstrating your understanding of the risks you might face is key in helping us develop a robust regime in the legal sector and ensuring that you understand when any suspicions you have must be reported to law enforcement.

CILEx Regulation will be working with the other AML supervisors to address issues raised in the review.



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## Risk factors

In the table that follows we have set out the updated risk factors that we consider to be significant for our firms. In looking at these risk factors, we are considering the inherent level of risk before any mitigation that you put in place.

## Future updates and further support

CILEx Regulation will continue to update this sectoral risk assessment with new information from government, law enforcement and our own regulatory regime. Any changes should prompt a review of your own written risk assessment, which should be carried out at least annually to reflect any changes in your firm and the work it carries out.

CILEx Regulation publishes [further information](#) on preventing money laundering and terrorist financing.



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## RISK FACTORS

In looking at these risk factors, we are considering the inherent level of risk before any mitigation that you put in place. These are the ones we consider to be significant for our firms.

### 1. Product and services risk

Criminals will look at the services that you offer to assess whether you may be targeted for money laundering. The 2017 National Risk Assessment identified the following products and services as posing the highest risk of being used for money laundering:

<p><b>Trust and company formation</b></p> <p>The creation of trusts and companies on behalf of clients is assessed to be the legal service at greatest risk of exploitation.</p> <p>Law enforcement investigations often highlight trusts and companies being used to</p> <ul style="list-style-type: none"> <li>• hide beneficial ownership,</li> <li>• undermine due diligence checks, and</li> <li>• frustrate law enforcement investigations.</li> </ul>	<p><b>Conveyancing</b></p> <p>Property provides the opportunity to launder large amounts of money in a single transaction, as well as often being a store of growing value.</p> <p>Over 50% of SARs related to the legal sector in 2016 were linked to the property market.</p> <p>Often overseas companies linked to the proceeds of crime are involved in property purchases.</p> <p>Overseas property investment is now moving into smaller cities and towns, so the potential risk is spreading.</p>	<p><b>Client accounts</b></p> <p>Accessing a client account can make funds appear to have a genuine source for criminals and may not attract the attention of law enforcement agencies.</p> <p>A client account must never be used:</p> <ul style="list-style-type: none"> <li>• as a banking facility, or</li> <li>• to pass funds through it without a legitimate underlying legal transaction.</li> </ul> <p>Firms should be aware of any attempt:</p> <ul style="list-style-type: none"> <li>• to pay funds into a client account without a genuine reason;</li> <li>• to get a refund of funds from a client account (particularly to a different account from which the original funds were paid);</li> <li>• to access your client account bank details; or</li> <li>• to access the client account prior to client due diligence being completed.</li> </ul>
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## 2. Consumer and client risk

Whilst smaller practices often have a deep knowledge of their clients, long-standing relationships, and/or a primarily local focus, this may mean they sometimes do not document risks faced by their practice.

Each client should be considered separately, as each will have their own individual risk-profile.

### Concealing identity

For some clients, there may be good reasons why they cannot produce identification documents, for example elderly people or illegal immigrants.

But for money launderers the warning signs may include:

- seeking anonymity on behalf of themselves, a third party or beneficial owner;
- being evasive about proving their identity;
- producing non-standard documentation; or
- acting outside their usual pattern of transactions.

The risk posed by your client also extends to the risk posed by the beneficial owner, if applicable.

### Politically exposed persons (PEPs)

For those firms that are involved with PEPS and associates, the money laundering regulations require:

- the PEP to be clearly identified; and
- for firms to undertake enhanced due diligence on them.

The definition of PEPs now includes individuals from the UK, rather than just restricted to overseas individuals. So the identification of domestic PEPS now affects all firms.

PEPs will often have access to public funds, so extra checks to mitigate the risks of corruption are required.

### Cash-intensive or high-risk sectors

Those that present a greater risk to you may include those:

- handling large volumes of cash may;
- linked to a higher risk of corruption or being used for money laundering i.e. arms trade or casinos.

You should have a policy on what amount of cash, if any, you will accept, and in what circumstances.



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### 3. Transaction risk

Identifying the risks involved in a transaction is helped by being alert for unusual activity or requests that don't make commercial sense.

#### Size and value of the transaction

Criminals will want to see how much money they can launder. Sometimes a small seemingly innocent transaction can be followed by a much larger or high-value one.

You should be investigating:

- unusually large transactions;
- those that are not consistent with your client (i.e. suddenly buying a high value property when previously only associated with low value properties); or
- why a client is seeking to make several linked transactions, as this may present a higher risk.

#### Payment type

Whilst there may be legitimate reasons for a client's choice, anonymity and money laundering can be made easier by using:

- cash as it may not have passed through the banking system and is often untraceable or
- some electronic currencies.

You should have a policy on what amount of cash, if any, you will accept, and in what circumstances.

#### New products or technologies

Criminals are always seeking new ways to launder funds as old ways become too risky and loopholes are closed. They may also seek out firms unexperienced in new areas.

Think about new or previously identified risks, if your firm:

- moves in to a new business area;
- provides a new delivery channel for services;
- starts a brand-new pattern of transactions; or
- is using a new innovative technology.

#### Complex transactions or products that facilitate anonymity

Increased simplicity and transparency reduces the risk of money laundering, so criminals can use complexity as a way of obscuring the source of funds or their ownership.

Make sure that:

- you do not proceed with a transaction until you fully understand the purpose and nature of the transaction you are being asked to undertake;
- you make further enquiries or seek expertise if unsure;
- the complexity of a transaction or corporate structure is not hiding the beneficial owners.

#### Transactions that don't fit with your firm or client's normal pattern

Consider the risks of being asked for:

- transactions or services that you don't offer;
- an unconnected transaction or service for no reason;
- a service out of line with the original customer due diligence; or
- a service out of the normal pattern of transactions, without a good reason.

When doing your initial client due diligence consider what services your client might want in the future.



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## 4. Delivery channel risk

The way that services are delivered can increase or reduce risk to the firm. Whilst complexity can increase risk, by maintaining strong transparency can help to reduce risk.

Newly qualified members may lack understanding and experience, and may not identify higher risk situations, though in some instances this risk is managed when members are required to undertake substantial training and work experience prior to providing services.

Remote clients	Combining services	Payments to or from third parties
<p>Whilst you firm might be delivering services countrywide, you need to be mindful of the risks of remote clients and how you may mitigate these risks.</p> <p>Consider:</p> <ul style="list-style-type: none"> <li>• Sometimes not meeting a client face-to-face may make sense, so then adopting other ways to identify that client protects you and your firm.</li> <li>• Clients who are not keen on meeting in person might be a cause for concern and you need to recognise this increases the risk of identity fraud.</li> </ul>	<p>You should always remain alert to:</p> <ul style="list-style-type: none"> <li>• how a client is making use of the services that your firm offers;</li> <li>• whether what appear unconnected services are being used to conceal a transaction that is risky;</li> <li>• a company formed for one purpose some time ago is now being used with you for another;</li> <li>• separate firms being used for various parts of what appears a connected transaction.</li> </ul>	<p>The involvement of third parties in a transaction is often a reason for suspicion. Consider:</p> <ul style="list-style-type: none"> <li>• Why a third party or associate is required in a transaction;</li> <li>• Whether they disguise where funds and assets are coming from or going to;</li> <li>• Unexpected transactions including payments in error;</li> <li>• By returning the funds without query, this can effectively launder criminal money;</li> <li>• Why you are being required to make any third-party payment, rather than the client;</li> <li>• Litigation settlements out to a client are in scope.</li> </ul> <p>You should always make sure you identify the source of funds and source of wealth. Consider how far back you should go on identifying sources to be certain of where the money comes from.</p>



## 5. Geographical risk

You should consider the geographical risk at all stages of a transaction:

- which services are required;
- where the client is based;
- where the beneficial owners are based; and
- the source and destination of funds.

For those working primarily with local clients, consider the reasons for distant clients deciding to make use of your services.

### Dealing with overseas jurisdictions

Countries with anti-money laundering and counter-terrorist financing regimes which are equivalent to the UK may be considered lower risk. However, for some overseas jurisdictions, the risks of money laundering are more common and therefore a higher risk.

Firms are required to have in place enhanced due diligence measures in dealing with countries that have not implemented FATF recommendations, or have significant levels of corruption or other criminal activity, such as terrorism.

A list of high risk jurisdictions is available on the Financial Action Task Force [website](#).

Transparency International produces an annual corruption index available [here](#).

Similarly enhanced due diligence measures are required when dealing with countries subject to sanctions, embargos or similar measures. We are required to collect information on sanctions breaches, so care must be exercised in dealing with overseas countries and individuals. A list of all those countries subject to financial sanctions is available [here](#).



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