

**Discuss the unique position of corporate lawyers in reporting and keeping tabs on criminal activity, especially in light of the Financial Transactions Reporting Act and the Terrorism (Bombings and Financing) Bill**

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Anti-money laundering legislation renders the conduct of legitimate business more dangerous and corporate lawyers, both in-house and external, are being called upon to protect companies from regulatory scrutiny.

Corporate lawyers have an instrumental role to play in developing educational and compliance programmes, as well as monitoring criminal activity. They are in a unique position as they serve a single client who is also the counsel's employer, and this may mean that such lawyers are vulnerable to pressure from their client. They can also become part of the corporation's management team, exposing them to even wider liabilities.

These lawyers must, however, maintain their independence, as they are just as exposed to obligations under anti-money laundering legislation as lawyers in independent practice. Some recent New Zealand cases illustrate that the courts will not hesitate to enforce lawyers' obligations under these provisions.

**The New Zealand position**

In an international context, New Zealand has engaged itself in the worldwide battle against money laundering. It is a signatory to the 1988 UN Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, and in 1991 it became a member of the Financial Action Task Force (FATF).

In accordance with these international measures, the Crimes Amendment Act 1995 was enacted which makes money laundering, and the intention to launder money, criminal offences in New Zealand.<sup>1</sup>

The Financial Transactions Act 1996 goes one step further by implementing measures for preventing and detecting money laundering through financial institutions. Central to the Act is a recognition that the financial institutions who deal with funds on a daily basis have a primary role in the war on money laundering and organised crime.<sup>2</sup>

The Act imposes obligations on financial institutions to verify the identity of persons conducting transactions, to report suspicious transactions, and to keep records. The term "financial institution" is defined widely so as to include not only banks, but anyone whose principal business is to provide financial services that involve the transfer or exchange of funds.<sup>3</sup>

The Act also applies to lawyers, but only to the extent that the lawyer receives funds in the course of the lawyer's business for the purpose of deposit or investment, or for the purpose of deposit or investment, or for the purpose of settling real estate transactions.

Although the Act does not apply to in-house counsel in this way, they could still be prosecuted as individuals under the Act for breach of the verification, record keeping, and reporting requirements.<sup>4</sup> Furthermore, in-house counsel are often considered to be part of the corporation's management team, and this exposes them to even wider liabilities.

Under s54 of the Act, where any body corporate is convicted of an offence under the Act, every director or officer concerned in the management of the body corporate shall be guilty of

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<sup>1</sup> Section 257A

<sup>2</sup> NZPD Vol 547, 4 April 1995, 6683

<sup>3</sup> Section 2

<sup>4</sup> Individuals can be fined up to \$20 000

an offence where it is proved that the act or omission that constituted the offence took place with that person's knowledge, authority, permission or consent.

The requirement to identify customers and keep certain records was enacted for the purpose of generating a paper trail that the police can trace in order to identify money launderers. The verification requirements are contained in Part II of the Act, sections 6 to 12.

The main objective is to prevent the keeping of anonymous accounts, or accounts in obviously fictitious names. Where a financial institution is obliged to verify identity, the institution is also required to keep such records as are reasonably necessary to enable the evidence to be retained.<sup>5</sup> These records must enable the transaction to be readily reconstructed at any time by the Commissioner.

Where the charge is brought under Part II of the Act, the defendant has a defence if he or she can prove that all reasonable steps were taken to secure compliance with that part of the Act; and that in those particular circumstances compliance could not have reasonably been expected.<sup>6</sup>

The reporting by financial institutions of suspicious activity is one of the key areas of the FATF recommendations. It observes that by far the majority of investigated or prosecuted money laundering cases are related in some way to suspicious transaction reports, comprising between 90% and 100% of the source of money laundering investigations.<sup>7</sup>

Section 15 of the Act provides that where any person conducts or seeks to conduct any transaction through a financial institution and the financial institution has reasonable grounds to suspect that the transaction is or may be relevant to the investigation or prosecution of any person for a money laundering offence or to the enforcement of the Proceeds of Crime Act 1991, the institution must, as soon as practicable after forming that suspicion, report that transaction or proposed transaction to the Commissioner.

This obligation, therefore, has both objective and subjective tests. It must be emphasised that the financial institution need not suspect or know that a money laundering transaction is taking place. It is enough that there is a reasonable suspicion that the transaction may be relevant to a money laundering investigation.

Owing to the changeable nature of laundering techniques it is impractical and ineffective to define a suspicious transaction in legislation. However this is conducive to uncertainty. For guidance to practitioners on the identification of suspicious transactions, section 3 of the Police Guidance Notes contains the suspicious transaction guidelines established in compliance with section 24 of the Act.

Examples of a suspicious transaction may include: exceptionally large deposits being made by a person or company whose business activities would normally be generated by cheques or other instruments; clients wishing to conduct one-off cash transactions who are reluctant to provide identification; clients insisting on using an institution's services for transactions not within that institution's normal business and for which there are other firms with publicly acknowledged expertise.<sup>8</sup>

It appears that lawyers are a common channel for laundering money, yet they rarely comply with their legal obligation to report suspicious transactions. This fact is reflected in the low number of suspicious transaction reports submitted by this group.

Although FATF acknowledges that this reluctance may arise from confidentiality or fear of losing clients, it concludes that their unwillingness to co-operate may have much to do with a

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<sup>5</sup> Section 21(2) FTRA

<sup>6</sup> Section 14

<sup>7</sup> Report on Money Laundering Typologies 2001-2002, paragraph 72

<sup>8</sup> At 53-56

lack of public pressure to do so.<sup>9</sup> Two recent prosecutions of solicitors for failure to comply with the reporting requirements of the Financial Transactions Reporting Act are indicative of a level of unawareness or neglect of practitioner's obligations under the Act.<sup>10</sup>

In *Police v Devereux*, Heath J at the High Court concluded that the charges: "[C]ould not properly be described as of a "technical nature" given that the whole purpose of the Act is to ensure that criminal activity is detected early in the piece by the reporting of suspicious transactions. Failure by "financial institutions" to comply with their obligations under the Act undermines the ability of law enforcement agencies to investigate and prosecute serious criminal offending in a timely fashion."<sup>11</sup>

The effect of this decision is that members of the legal profession, whether they are in-house counsel or independent practitioners, can no longer plead lack of knowledge of the obligations cast upon them by the Act, or the consequences of failing to report a suspicious transaction.

Specific reference is now made to the Financial Transactions Reporting Act in the NZLS Rules of Professional Conduct (rr1.10(1) and 3.03 (1)). The two recent prosecutions have both dealt with the failure to report suspicious transactions. However, practitioners should also be mindful of their obligations to verify identity and to retain records.

Corporate counsel are subject to the same obligations as independent practitioners under these provisions, and must therefore protect themselves from possible criminal penalties for failure to fulfil the three obligations. They must also resist any temptation to mislead or obfuscate, as this may lead to charges of aiding and abetting.

When acting in relation to a transaction, in-house counsel must exercise caution in balancing legal risk with the desire to facilitate the transaction.<sup>12</sup> For example, an issue might be the possible criminal consequences of setting up devices or mechanisms of concealment for their client where the scheme is subsequently found to be a laundry.

The question came before the High Court in New Zealand in the Equiticorp proceedings.<sup>13</sup> The structure was referred to as the "Yeoman Loop". It was argued by the Crown that the solicitor's knowledge of the establishment and use of the Yeoman Loop was such as to render him liable at law for the same offences as the principal offenders.

A money laundering charge might have been laid against the former Equiticorp chief if such an offence existed. Instead he was charged with conspiracy to defraud. Justice Tompkins, in a favourable decision,<sup>14</sup> held that it had not been proved that the solicitor has been aware of the dishonest purpose of the Loop.

It was obvious to him that the structure he was setting up was one that would enable payments to be made that would be difficult to detect, but the judge was not prepared to draw the necessary inferences.

The decision is a warning for lawyers who find themselves directly and knowingly involved in an arrangement that will result in a client obtaining money illegally. Although the case involved a partner of a firm, the principles are just as applicable to corporate counsel.

### **Terrorism (Bombings and Financing) Suppression Bill**

Money laundering aids and abets terrorism. FATF has recognised that there is in fact little difference between terrorist and other criminal methods in the use of the financial system.

<sup>9</sup> Report on Money Laundering Typologies 2001-2002

<sup>10</sup> *Police v Patel*, unreported, Callander DCJ, 16 May 2002, Auckland DC; *Police v Devereux*, unreported, Heath J, 27 June 2002, Auckland High Court, A03/02

<sup>11</sup> At paragraph 60

<sup>12</sup> See "Ethics for In-House Counsel" at [www.clanz.org](http://www.clanz.org).

<sup>13</sup> *R v Adams*, unreported, Tompkins J, December 18, 1992, Auckland High Court, T240-91

<sup>14</sup> *R v Gunthorp*, unreported, June 9 1993, CA46-93

As outlined above, New Zealand already complies with obligations to identify, monitor, and report suspect transactions. This bill represents the third and final stage of the domestic processes that have to be completed before New Zealand becomes party to the bombings and financing conventions.

The bill, as it is currently drafted, will impose a number of obligations on corporate lawyers and their corporations that are onerous. In particular, a number of clauses provide for an offence where a person is deemed to have been “reckless”, for example:

- ? Clause 9(1)(b) - Financing of terrorism
- ? Clause 10A(1)(b) - Prohibition on dealing with property of, or derived or generated from property of, terrorist and associated entities
- ? Clause 10B(1)(b) - Prohibition on making property, or financial or related services, available to terrorist and associated entities

There will be uncertainty regarding the range of circumstances over which these standards will apply, and this in turn will lead to costs being incurred by persons and institutions to protect them from its uncertain scope.

It will, therefore, be difficult for in-house counsel to implement compliance procedures in accordance with the legislation in its current form. This is of particular concern in light of the penalties for “reckless” breach (imprisonment for up to seven years).

Under clause 10A the burden rests on any person dealing with property to discover what acts have been carried out or facilitated by the direct or indirect owner or controller of the property with which they are dealing, and then to ascertain whether these acts might fall within the definition of a ‘terrorist act’. Property is broadly defined in clause 4 and dealing includes a range of transactions.

The provision therefore imposes criminal liability on a range of professional people who buy or sell a piece of property or act on behalf of another person.<sup>15</sup> It is noted that liability for recklessness is limited to entities that have been formally designated, however the reference to indirect ownership makes this potentially onerous<sup>16</sup>.

Clause 10B covers services provided directly or indirectly to people where the provider is reckless as to whether the ultimate beneficiary of the service has carried out, participated in or facilitated terrorist acts.

The wide scope of the definition of terrorist act places an unreasonable burden on anyone who provides property, financial or other services.<sup>17</sup> If this Bill is enacted it will become increasingly difficult for corporate counsel to protect companies from regulatory scrutiny.

## **Conclusion**

Lawyers are placed in a difficult position under anti-money laundering legislation, as they are being required to assume responsibility for the integrity of transactions.

To date, the majority of money laundering cases have involved money obtained through illegal drugs trafficking. This remains the area of great concern but money laundering is not confined to drug offences.

It also occurs in cases of serious fraud. Aware of the severe criminal penalties available for money laundering, prosecutors now seek money-laundering charges in fraud prosecutions and other white-collar crime cases.

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<sup>15</sup> Jane Kelsey’s submission on the Terrorism Suppression Bill to the Foreign Affairs, Defence and Trade Select Committee, November 2001. See <http://www.converge.org.nz>

<sup>16</sup> Ibid

In this climate, it is essential that corporate lawyers and government lawyers ensure that their clients introduce, and carefully implement, a comprehensive anti-money laundering programme.

It is also important that they do not shy away from their role as a monitor of criminal activity, as neglect of this obligation may lead to criminal penalties for failure to report, retain records, or verify identity, or even aiding and abetting under anti-money laundering legislation.

<sup>1</sup> Section 257A

<sup>2</sup> NZPD Vol 547, 4 April 1995, 6683

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<sup>8</sup> At 53-56

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<sup>10</sup> *Police v Patel*, unreported, Callander DCJ, 16 May 2002, Auckland DC; *Police v Devereux*, unreported, Heath J, 27 June 2002, Auckland High Court, A03/02

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<sup>16</sup> *Ibid*

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