IN THE MATTER OF

THE INTELLECTUAL PROPERTY REGLATION BOARD ("IPReg")

AND IN THE MATTER OF

THE MONEY LAUNDERING REGULATIONS 2007

NOTE OF ADVICE

IN ADVANCE OF A WEBINAR ON 23rd SEPTEMBER 2014

Introduction

1. I am asked to advise IPReg on the application of the Money Laundering Regulations 2007 ("the 2007 Regulations") and Proceeds of Crime Act 2002 ("POCA") and its amending legislation, the Serious Organised Crime and Police Act 2005 ("SOCPA").

2. My advice is sought by way of an updating commentary and explanation on the application of the legislation in light of revisions to the IPReg Rules of Conduct for Patent Attorneys, Trade Mark Attorneys and Other Regulated Persons ("the New Code of Conduct") which is presently in draft and which will come into force on 1st January 2015.

3. This advice and the content and feedback from the Webinar scheduled for 23rd September 2014 will constitute renewed and updated guidance to the profession under the auspices of IPReg and the New Code of Conduct.

4. IPReg has issued guidance on two previous occasions, in May 2009 and in September 2010 when it issued Business Practice Guidance. Both sets of guidance were shaped by an informal indication from HM Treasury that it did not regard the 2007 Regulations as applying to Patent and Trade Mark Attorneys because they "...*were not regarded as dealing with assets which were likely to be utilised in money laundering...*". As a consequence the guidance was aimed at increasing awareness in the profession of the general application of the legislation and the resulting risks.

5. In the first instance, I am asked to review whether that approach to the 2007 Regulation is correct.

6. Much has changed since that guidance was issued; HMRC, not just HM Treasury, has now assumed responsibility for guidance and enforcement relevant to the 2007 Regulations. SOCA has been replaced with the National Crime Agency ("NCA") and the FSA has been replaced with the FCA

7. I anticipate that, after the Webinar scheduled for 23rd September 2014, I will formulate a comprehensive practice note to be read with the New Code of Conduct. This advice will therefore discharge two functions; it will address the fundamental question of whether the 2007 Regulations apply to Patent and Trade Mark Attorneys and it will set out the framework for practice advice to the profession to be read with the New Code of Conduct.

Application of the 2007 Regulations

8. In deference to the guidance issued to the profession in May 2009 and in September 2010, it quite properly contained the caveat that HM Treasury's opinion was itself qualified. The Treasury had made clear that only a court could give a definitive decision on application of the 2007 Regulations to Patent & Trade Mark Attorneys.

9. The problem with any reliance on that advice is two-fold; Firstly, it is informal guidance with no statutory or other ultimate authority. The only argument open to an IP professional in reliance upon it and in the event that they were to be prosecuted is that

such a prosecution would be an abuse of process given the existence of that advice. In my view such a challenge would be tenuous at best given the overriding qualification to the Treasury's advice.

10. Secondly and much more importantly, the guidance is in my view wrong. As recited in the May 2009 note to the profession its rationale was that "...*patent and trade mark attorneys were not regarded as dealing with assets which were likely to be utilised in money laundering...*". There are two problems with this; IP rights, whether genuine or whether bogus and contrived could very well be used as a vehicle for laundering the proceeds of crime[1]. Secondly, "dealing with assets" is not confined to direct dealing in the sense of immediate control but can arise merely by becoming "concerned in an arrangement" which facilitates the acquisition, retention, use or control of criminal property under S.328 of POCA.

11. In my experience the most common reason for misinterpretation of the 2007 Regulations is a failure to recognise and apply the substantive criminal offences that overlay them.

12. S.328 POCA is the widest of the relevant substantive criminal offences. Becoming "concerned in an arrangement" under S.328 could include becoming concerned in an arrangement whereby knowing infringement of another's IP rights takes place or where there is any conspiratorial or dishonest acquisition, retention, use or control of IP rights.

13. As organised criminals look for more and different ways to launder money, the use of IP rights is an obvious risk and potentially difficult to police.

14. As has been the case in bogus litigation, criminals can appear on both sides of a transaction or dispute creating a fictitious or tenuous "right" which is then purchased or bought-off by the criminal counter-party. It is in the nature of IP rights that such a ruse would be difficult to detect and challenge.

[1] Any purported asset or right with claimed value is a potential risk. For example, bogus rights asserted in litigation have been used to launder money.

15. Having reached the view that the guidance from the Treasury was founded on an erroneous rationale it does not necessarily follow that the conclusion expressed was wrong. It is therefore necessary to look at the 2007 Regulations.

The 2007 Regulations

16. Regulation 3(1)(d) expressly includes "independent legal professionals" amongst the regulated entitles to which the Regulations apply.

17. The relevant parts of Regulation 3(9) defines an "independent legal professional" as:

> *"...a firm or sole practitioner who by way of business provides legal or notarial services to other persons, when participating in financial or real property transactions concerning-*
>
> *(a) The buying and selling of real property or business entities;*
> *(b) The managing of client money, securities or other assets;*
> *(c) .....*
>
> *and, for this purpose, a person participates in a transaction by assisting in the planning or execution of the transaction or otherwise acting for or on behalf of a client in a transaction."*

18. In light of Regulations 3(1)(d) and 3(9) it is difficult in my view to see how the 2007 Regulations could not apply to Patent and Trade Mark Attorneys.

19. They provide legal services.

20. They are concerned in transactions involving the management of "client assets". In my view patents and trademarks are clearly assets. That much appears to have been conceded in the May 2009 guidance to the profession. In my view that concession was correct. The guidance issued by the NCA[2] defines criminal property as including "all real, personal, heritable or "movable property", "intangible and incorporeal property" and

[2] NCA Guidance issued in January 2014

"things in action". Client "assets" may themselves be criminal property or may be used to launder criminal property.

21. Importantly, Patent & Trade Mark Attorneys participate in such a transaction merely by "assisting in the planning or execution of it or otherwise by acting for or on behalf of a client in a transaction".

22. In my view Patent & Trade Mark Attorneys are caught by the 2007 Regulations where they might play a relatively minor role in a wider commercial transaction. The "*acquisition, retention, control and use*" of IP rights might form a small and relatively inconsequential part of the transaction but if the wider transaction is one involving criminal property within the meaning of S.328 POCA then the Patent & Trade Mark Attorney is caught by the Regulations for having "*assisted in the planning or execution*" of it.

23. Circumstances in which the 2007 Regulations are engaged are myriad, but a small number of obvious examples suffice to make the point:

    (1) The most obvious example is that a Patent & Trade Mark Attorney may "assist" a client to purchase IP rights with money that is criminal property within the meaning of S.328 POCA. Regulation 3(9)(b) is clearly engaged;

    (2) A Patent & Trade Mark Attorney may be engaged in advice on a much wider transaction, such as a share purchase agreement, which includes acquisition of IP rights. If that share purchase is made with criminal property within the meaning of S.328 POCA, the Patent & Trade Mark Attorney will have assisted in that transaction, even if such assistance was peripheral. Neither POCA nor the 2007 Regulations define "assisting in the planning or execution" to mean substantial or even material. Criminal money is frequently laundered through the entertainment and hospitality industry. Acquisition of a chain of clubs, wine bars or restaurants with criminal property may well involve the acquisition, retention, use and control of associated IP rights. If they have been paid for, even to a minor or marginal degree using criminal property, the Regulations are engaged by virtue of Regulation 3(9)(a) & (b);

(3) A Patent & Trade Mark Attorney may "assist" in registration of IP rights that have themselves been stolen. Regulation 3(9)(b) is clearly engaged;

(4) A Patent & Trade Mark Attorney may receive client money on account of disbursements or (less likely fees) which is criminal property. Once again Regulation 3(9)(b) is expressly engaged.

24. In my view the flaw in the analysis that led to the view that Patent & Trade Mark Attorneys were not caught by the 2007 Regulations was to confine that analysis to the notion that criminals would use patents and trademarks either as criminal property or as a means of laundering criminal property. As the 2007 Regulations make clear, their application is much wider than that.

25. Regulation 3(9) and the remainder of the 2007 Regulations should also be read with the substantive criminal offences which its mechanisms are intended to detect and prevent. When this is done, it is apparent that S.328 of POCA and the language of Regulation 3(9) have close similarities. That is no coincidence. If one adds to the extract from Regulation 3(9) in paragraph 17 above, the words from S.328 of POCA "*...intended to facilitate the acquisition, retention, use or control of criminal property*" one can see how POCA and the 2007 Regulations work together in a way that is clear, explicable and coherent.

26. In my view the guidance from the Treasury was wrong and Patent & Trade Mark Attorneys should not rely upon it. In my view they are caught by the 2007 Regulations and the New Code of Conduct should reflect this.

<u>The Practical Consequences for Patent & Trade Mark Attorneys</u>

27. Much of the guidance to the profession from September 2010 survives this review. Consistent with the 2007 Regulations the new focus of compliance is on assessment of risk and "outcomes".

28. The 2007 Regulations require procedures to be in place to detect and prevent money laundering. At the heart of those procedures is knowledge of your client's identity,

including beneficial ownership and knowledge of the transaction in which they are involved and the source of their funds.

29. The five key obligations placed on the regulated sector are:

- Providing staff training
- Customer due diligence, which involves knowing the customer/business (including client identification)
- Record keeping
- Having systems and controls in place to prevent money laundering/terrorist financing, which include the internal reporting of suspicions or knowledge of money laundering
- Identifying a 'Nominated Officer' to oversee the submission of a Suspicious Activity Report ("SAR") to the NCA and the implementation of the Regulations and appropriate guidance

30. Patent & Trade Mark Attorneys caught by the 2007 Regulations may face criminal sanction for breach of the Regulations or breach of SS.330 and 331 of POCA for failing to report a reasonable suspicion of money laundering. That liability is distinct from liability for the substantive money laundering offences under SS.327-329 of POCA.

Reporting obligations under POCA

31. The reporting obligations in POCA are applicable to anyone in the UK that may interact with an individual or business in a way that they may commit a money laundering offence.

32. Those working in the 'regulated sector' commit an offence if they do not submit a SAR to the NCA if they know or suspect, or have reasonable grounds to know or suspect, that another individual or person is engaged in money laundering; and the information came to them in the course of their business in the regulated sector.

33. It is an offence for an individual working in the regulated sector not to report to their 'Nominated Officer' or the NCA if the conditions for reporting have been met. POCA

also makes it an offence for a nominated officer not to disclose to the NCA if the conditions for reporting have been met.

34. Those reporting to the NCA need to be aware of the "tipping off provisions" (Section 333A-E) which make it an offence, having submitted a SAR, to reveal information which is likely to prejudice any resulting law enforcement investigation.

Defence against Money Laundering under POCA

35. POCA provides to reporters a defence against a money laundering offence by seeking the consent of the NCA to undertake an activity which the reporter believes may constitute one of the three money laundering offences under S.327 (concealing criminal property), S.328 (becoming concerned in an arrangement for acquiring, retaining, using or controlling criminal property) and S.329 (acquiring, using or possessing criminal property).

Consent

36. An authorised disclosure under S. 338 of POCA is made:

- before a person carries out the act prohibited by Sections 327-329
- while a person is carrying out the act prohibited by Sections 327-329, the act having begun at a point when the discloser did not know or suspect that the property is the proceeds of crime and the disclosure is made on the discloser's own initiative as soon as is practicable after s/he first knew or suspected that the property is the proceeds of crime, or
- after the act prohibited by Sections 327-329 and is made on the discloser's own initiative as soon as practicable after the act, and there is good reason for failure to make the disclosure before the act.

37. In response to a SAR decisions are made by the Consent Team of the UK Financial Intelligence Unit ("UKFIU") on behalf of the NCA.

38. Where consent is granted the reporter may proceed with the specified transaction. If they choose to do so they will have a defence against the three principal money laundering offences under SS.327-329 of POCA.

39. Consent for the purposes of Part 7 of POCA does not:

- oblige or mandate a reporter to undertake the proposed act
- imply NCA approval of the proposed act
- provide a criminal defence against other criminal offences pertaining to the proposed act
- provide derogation from professional duties of conduct or regulatory requirements
- override the private law rights or any person who may be entitled to the property specified in the disclosure.

Timeframe

The '*notice period*' (7 working days)

40. The law specifies consent decisions must be made within seven working days (the 'notice period') from the day after receipt of the consent request (excluding Bank Holidays and weekends). The purpose of the seven days is to allow the NCA time to risk assess, analyse, research and undertake further enquiries relating to the disclosed information in order to determine the best response to the consent request. The reporter runs the risk of committing a money laundering offence if they proceed prior to receiving a decision from the NCA.

41. If nothing is heard on the expiry of the "notice period" the reporter may proceed with the specified transaction or activity and will have a defence to any potential money laundering offences relating to that activity.

The '*moratorium period*' (31 calendar days)

42. If consent is refused within the seven working days, the NCA or a law enforcement agency designated by it has a further 31 calendar days (the 'moratorium period') – from the day of refusal – to further the investigation into the reported matter and take further action. That may include a restraint order The 31 days includes weekends and public

holidays. The reporter runs the risk of committing a money laundering offence if they proceed during the moratorium period whilst consent is still refused.

43. If no restraint or seizure action occurs after the end of the 31 day period, the reporter can proceed with the transaction or activity and will have a defence to any potential money laundering offences relating to that activity. Consent does not extend to any acts or dealings in or arrangement concerning criminal property not detailed in the initial disclosure or otherwise agreed with the NCA.

44. In the first instance, a consent decision will usually be communicated to the reporter by telephone in order to provide a quick response. The NCA will also send a letter by post recording the decision but there is no requirement to wait for this letter to proceed with the prohibited act if consent has been granted verbally.

Making a request for consent

45. Reporters are encouraged to make consent requests using SAR Online, which is promoted by the NCA as a "free, secure and efficient means of submitting SARs". The online media contains useful information on making a disclosure and has links to relevant legislation. A reporter will receive an automatic acknowledgment of its SAR and the NCA financial database reference number for the report. The NCA also claims that the Consent Team will also be able to start processing SAR Online submissions quicker than those submitted manually.

Guidance

46. When deciding whether an offence has been committed, the court must consider whether the defendant followed any relevant guidance issued by an appropriate body and approved by the Treasury.

47. By far the best guidance is in the Joint Money Laundering Steering Group (JMLSG) Guidance Notes for the UK Financial Sector which has been approved by HM Treasury and the Money Laundering Advisory Committee (MLAC) for the regulated sector.

Key Aspects of Compliance for Patent and Trade Mark Attorneys

48. In practice the key substantive Regulations for Patent and Trade Mark Attorneys are likely to be Regulations 7, 13 & 17.

49. Regulation 7 requires a "risk-sensitive" assessment of due diligence measures required in the case of each client. Regulation 7 speaks for itself but it is important to recognise that the degree of subjectivity it imports is both a benefit and a burden to the regulated professional. The key, in practice, is to follow the relevant guidance referred to in paragraphs 46 & 47 above.

50. In my view Regulation 7 is likely in many, if not most cases, to lead to an entitlement on the part of Patent and Trade Mark Attorneys to rely upon Regulation 13 (simplified due diligence) or Regulation 17 (reliance on another regulated professional).

51. Specifically Regulation 17 would apply in instances I have identified where a Patent and Trade Mark Attorney is involved in a wider transaction involving corporate or transactional lawyers where IP rights fall to be acquired or disposed of as part of a wider corporate transaction or acquisition.

52. The principal administrative burden rests in Regulations 19-21; record keeping, policies, procedures and training. These requirements once again speak for themselves but in my practical experience of acting for both large regulated entities and sole practitioners, the NCA will take a pragmatic and proportionate view in relation to record keeping, policies, procedures and training depending on the size, complexity and regulatory risk represented by the regulated professional. For a sole practitioner, the existence of a money laundering and anti-terrorist financing compliance file and a basic awareness of the JMLSG Guidance Notes for the UK Financial Sector will ordinarily suffice.

53. In my view there is no requirement for Patent and Trade Mark Attorneys to register under Regulation 22.

54. If there remains a reason to be cheerful this is probably its extent.

The Way Forward

55. As observed in the introduction to this Note of Advice, I have set out a framework in relation to compliance in light of the New Code of Conduct which can be refined in more detail after the Webinar on 23rd September 2014. I have in mind specific reference to compliance with the 2007 Regulations in Sections 5, 9 & 11 of the draft New Code of Conduct.

56. I consider that a meeting prior to the Webinar would be very helpful to focus on the particular concerns of IPReg and the profession it regulates. If, in the meantime, I can be of any further assistance or if any aspect of this Advice is unclear, please do not hesitate to contact me by phone or e-mail.

James Ramsden

20th August 2014.

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