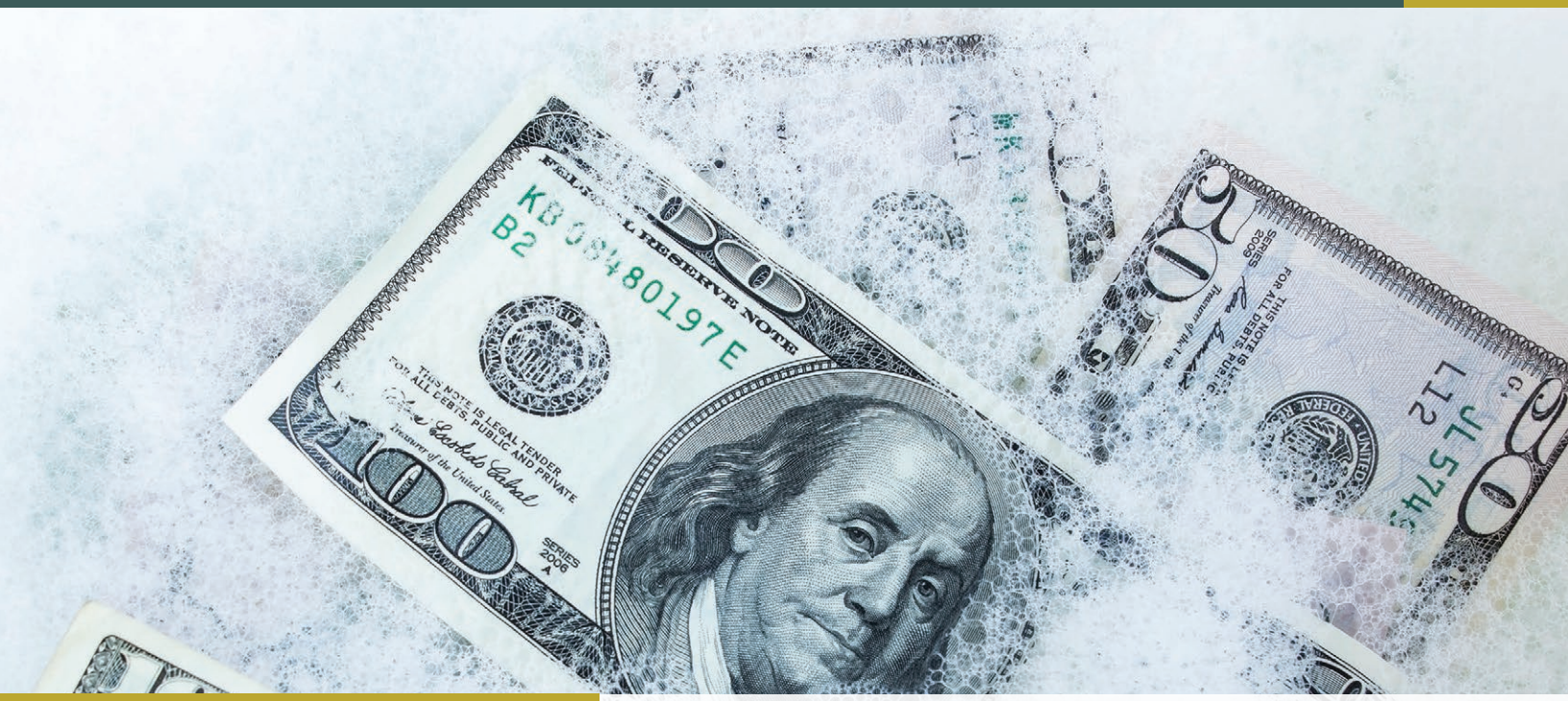

AML for law firms: The risk is real

Client intake
The importance of quality over quantity

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Is ALSP outsourcing right for your firm?

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AML for law firms: The risk is real

In 2016, the U.S. Department of Justice alleged that the perpetrators who embezzled billions of dollars from the Malaysian government laundered some of those funds through the client accounts of some major U.S. law firms. The firms weren't prosecuted, but the case illustrates one of the ways law firms can unwittingly fall prey to money launderers. A risk-based approach may help them reduce the odds.

RISKS FOR ATTORNEYS

The American Bar Association (ABA) has long opposed anti-money laundering (AML) legislation that targets attorneys. It argues such laws would be burdensome and undermine confidentiality and attorney-client privilege. But the ABA has supported the guidelines developed by the Financial Action Task Force (FATF), an inter-governmental body whose recommendations are recognized as the international AML and counter-terrorist financing standard.

The FATF has identified several legal activities that are particularly susceptible to money laundering, including:

- Buying and selling real estate or business entities,
- Managing client money, securities or other assets,
- Managing bank, savings or securities accounts,
- Organizing contributions for the creation, operation or management of companies, and
- Creating, operating or managing legal persons or arrangements.

The vulnerability may be intensified when these activities are conducted across borders.

3 TYPES OF RISK

According to the FATF, the cited activities should be subject to a comprehensive risk assessment. The assessment typically considers three types of risks:

1. Country or geographic risk. This type of risk relates to the location(s) of the client, the transaction, and the source of the wealth or funds. A higher risk generally is associated with certain kinds of countries, including those that provide funding or support for terrorist activities, are rife with organized crime or corruption, or are subject to sanctions imposed by organizations such as the United Nations.

2. Client risk factors. The FATF has developed a lengthy list of the characteristics of clients whose activities might pose a higher risk, including if they're politically exposed persons (PEPs), conduct the client relationship in an unusual way, have a

A FRAMEWORK FOR SMALL FIRMS AND SOLOS

The Financial Action Task Force (see main article) has outlined a "practical" approach to identifying and assessing money laundering risk for smaller firms and solo practitioners. It includes the following recommendations:

Adopt client acceptance and know-your-client policies. Identify the client, its beneficial owners, the true "beneficiaries" of the transaction, the source of funds and the transaction's purpose.

Adopt engagement acceptance policies. Understand the exact nature of the work and how it could facilitate the movement or hiding of criminal proceeds. Don't accept work if you lack the requisite experience.

Understand the rationale for the work. You should be reasonably satisfied that a commercial or personal rationale exists. But you aren't required to objectively assess that rationale.

Exercise vigilance for red flags. Identify and carefully review aspects of the transaction where you have reasonable grounds to suspect that funds are criminal proceeds. Such circumstances may trigger reporting obligations.

Consider appropriate action. Determine what, if any, actions must be taken.

Document. Adequately document and record the previous steps.

structure that makes it difficult to determine the controlling interest or true beneficial owner, or are cash-intensive businesses.

3. Service risk factors. The list of service risk factors is similarly long. It includes services where an attorney may effectively vouch for the client's standing, reputation and credibility, without an appropriate knowledge of the client's affairs. Other examples are services that could conceal beneficial ownership from relevant authorities, services where the attorney lacks expertise and real estate transfers in unusually short periods of time.

RECOMMENDED PROCEDURES

A collaboration among the ABA, the International Bar Association, and the Council of Bars and Law Societies of Europe developed a multi-step procedure for attorneys concerned about money laundering activities, sometimes referred to as client due diligence (CDD). It begins at the client intake process.

An attorney should identify and verify the identity of the client and the beneficial owner. The attorney also must understand the client's circumstances and business, based on information obtained during the normal course of the client's instructions.

From there, the attorney should evaluate whether assisting the client would risk committing money laundering. This can be done by conducting a risk assessment of any red flags and clarifications from the client. If the attorney decides to proceed with the engagement, he or she should continue to monitor the client's profile for signs of money laundering, especially if the client is a PEP or from a higher-risk country.

When an attorney has grounds for suspecting criminal proceeds are being used in a transaction

or in engaging the attorney, he or she should, where required or permitted, make a suspicious transaction report (STR) to the appropriate authority. The attorney must avoid tipping off the client about the filing of an STR.

STAY VIGILANT

Effective CDD isn't an isolated activity. Attorneys should engage in ongoing CDD to ensure the information collected remains current and relevant, especially for higher-risk clients. •

CLIENT INTAKE

The importance of quality over quantity

Want to improve profitability, reduce stress, and preempt malpractice lawsuits and billing-related disputes? Drop uncooperative or slow-paying clients and use a formal client selection process to avoid taking on new ones.

HOW DO EXISTING CLIENTS RATE?

Begin refocusing on client quality, not quantity, by reviewing all existing clients to determine whether any of them are weighing you down. First apply the 80/20 rule to identify the 20% or so of clients that likely account for 80% of your revenues. Research has shown that these clients often require only 20% to 40% of your time — making them even more appealing.

Next, assign your clients letter grades of A, B, C or D. Clients in the A category are the cream of the crop: They pay their bills on time, provide interesting work and send you valuable referrals. B clients have some minor flaws (perhaps they occasionally operate in "crisis" mode) but are otherwise desirable clients. C clients can be uncooperative or less lucrative or they may harbor unreasonable expectations. And D clients are demanding and difficult to work with; they complain regularly and quibble over every line item on an invoice.

Now comes the hard part: Drop your D clients and any C clients that can't be brought up to the B level with a little work. Be sure to review your local rules for the proper procedures before you end any engagements.

It may seem like you're tossing away good money by "firing" clients. But these clients are likely costing you time, stress — and possibly your reputation. How many hours, for example, does your managing partner or billing department devote to collections related to these clients?

DO YOU HAVE A CLIENT INTAKE FORM?

The best way to avoid awkward dismissals of C and D clients is to avoid establishing relationships with such clients in the first place. An effective client intake form can help your firm ensure a consistent intake process, avoid risky clients and document new representations.

The form should solicit, at the very least, the following information about a prospective client:

- Industry and entity type,
- Income and available assets,

- Nature and value of the matter,
- Necessary legal expertise (practice area),
- Fee arrangement, and
- Referral source.

The form should also include space for background research on the prospect. Finally, investigate criminal records, credit reports, bankruptcies, legal malpractice lawsuits and other litigation.

Of course, the client intake process begins *before* you formally meet face-to-face with a potential client. Client intake begins with the first phone call — and attorneys and staff should take advantage of this opportunity to perform some initial screening. Train employees who answer these calls to ask some basic questions that could disqualify prospective clients from making an appointment with an attorney. For example: What is the matter concerning? Have you sought counsel on this matter from any other attorneys? Who referred you to our firm?

ARE THERE CONFLICTS OF INTEREST?

The client intake form also should explore conflicts of interest. To accomplish that, determine the existence of adverse parties and potentially adverse parties; nonadverse third parties (for example, witnesses); known and potential conflicts; and whether any of your firm's attorneys (or their family members) have an ownership interest in the client or sit on the client's board of directors.

To make conflict-related data easy to access and evaluate, enter intake form information into a database. Your database should contain details about current and former clients and adverse parties. Investigate any positive hits to determine whether an actual conflict of interest exists.

Consider circulating conflict memoranda regularly to help reduce the odds of conflicts. Attorneys and other relevant staff should be required to review proposed representations in the memos for potential conflicts.

FOCUS ON QUALITY

It's important for attorneys in your firm to prioritize client intake as part of law firm management. And don't be afraid to end engagements that demand more time than they're worth. •

Save money by shifting credit card fees

The acceptance of digital forms of payment, including credit cards, has become ubiquitous across industries. But some law firms have yet to get on board — even though electronic payments often improve collections. The hesitation usually is due to a resistance to shouldering the processing costs that typically range from 2% to 5% of every transaction.

In many states, though, law firms can have the best of both worlds: higher collections and minimal processing costs. The secret? Putting the responsibility for the fees on clients.

SHIFTING STRATEGIES

Several techniques are available. The easiest method is to provide discounts to cash-paying customers and charge more for those clients who pay by credit or debit card. Cash discounts generally are permissible in all states.

Alternatively, you could add a surcharge to transactions. This approach can be complicated, though, because payment processors have varying fee structures and rules for merchants that surcharge. If you go this route, it's wise to work

with a payment processor that will compute the surcharge and automatically add it, so that your firm doesn't have to manually perform the calculation.

A few firms that accept credit card payments with a surcharge also allow payment by debit card without any extra fee — so clients feel like they have a "free" option. Other firms that apply a surcharge also accept payment by electronic check with no fee to the client (the processing fees for e-checks are typically lower than those for credit cards). But some firms simply accept only credit card payments, with the fees shifted, and enjoy a corresponding bump in revenues.

UNDERSTANDING RULES AND REGULATIONS

Several states have laws prohibiting or restricting the shifting of processing fees for credit cards. No states permit such fee-shifting for debit cards.

> *If you add a surcharge to transactions, work with a payment processor that will compute the surcharge and automatically add it.*

Attorneys must also take into account limits imposed by rules of professional conduct. Rules regarding the reasonableness of fees, trust accounts and confidentiality can come into play when imposing surcharges.

For a fee to qualify as "reasonable," you likely can't add a surcharge that exceeds your actual costs. Processing fees must be paid out of the operating account, not a client's account — but not every processor will permit this. And you must take care to use general language like "services rendered" to describe charges, rather than "Smith divorce" or "Jones termination case."

In addition, several states have ethics opinions addressing the issue. It's worth noting, though, that some of these opinions came out before a class action settlement of an anti-trust case brought against credit card processors. Under the settlement, U.S. merchants could begin adding surcharges to specific transactions starting in January 2013. The settlement raises questions about how binding the earlier opinions are, especially in states without laws explicitly banning surcharges.

Finally, the payment processors have rules merchants must satisfy to shift the fees to clients. For example, you generally must notify the processor at least 30 days before you begin the practice. The amount shifted is typically limited to your merchant discount rate for the applicable card. You also must notify clients. That means disclosing the surcharge dollar amount on every receipt.

WEIGHING OPTIONS

Shifting processing fees to clients isn't right for every attorney or firm. Some clients might resent such charges and feel nickel-and-dimed. If you determine that your clients won't rebel, though, you can see a positive financial impact. •

Is ALSP outsourcing right for your firm?

To the chagrin of some law firms, alternative legal service providers (ALSPs) aren't going anywhere. According to a recent report, the overall market for ALSPs grew by about $5 billion between 2015 and 2019, reaching almost $14 billion. Nearly 80% of law firms and 71% of corporate legal departments have used ALSPs at one time or another, a strong sign they're becoming a mainstream legal option.

If your firm still views ALSPs as competitors, it may be time to reframe your perspective. When law firms collaborate with ALSPs, rather than compete, it can pay off for all involved, including clients.

ADVANTAGES OVERRIDE CONCERNS

Thomson Reuters' report *Alternative Legal Service Providers 2021: Strong Growth, Mainstream Acceptance, and No Longer an "Alternative"* predicts that the ALSP market might have reached its tipping point. Widespread acceptance of the business model and benefits that are well-suited for current conditions, it says, position ALSPs to quickly expand market share.

You're not alone if you're skeptical, though. The report finds that about half of law firms continue to harbor some doubts about the quality and security of ALSPs. But the negative perceptions seem to be giving way as firms increasingly embrace ALSPs for tasks such as e-discovery, legal research, document review, and regulatory risk and compliance matters.

Several reasons are driving the shift in attitudes. For example, ALSPs can give firms access to specialized expertise and proprietary tech-driven solutions. They also can function as consultants on legal technology for firms. This access is particularly valuable for smaller firms, helping to even the playing field when they're competing against larger, better-resourced firms. Regardless of firm size, an openness to ALSPs also demonstrates to current and potential clients an openness to innovation and new, more cost-efficient ways of doing business.

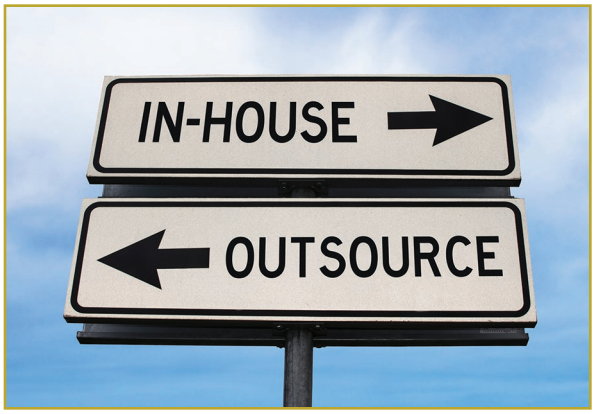
Outsourcing to ALSPs can lead to greater client satisfaction, too. Pressure to cut costs has only intensified in recent years, and outsourcing can do just that, to the benefit of both the law firm and its clients.

At the same time, taking tasks like research and document review off of the plates of attorneys lets them focus more of their time on higher-priority work with higher profit margins. Odds are, they prefer such work, so outsourcing also boosts their satisfaction and engagement, in turn enhancing retention.

Finally, outsourcing to ALSPs brings the same perks to a law firm that any type of outsourcing does, starting with lower costs. The firm can shrink its payroll and reduce its investments in training, overhead and other nonbillable employee expenses.

PROCEED WITH CAUTION

Outsourcing to ALSPs comes with numerous advantages, but it's important to remember that law firms still own the transferred processes. You can't afford to take an entirely hands-off approach — it truly must be a collaboration with the provider. •



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