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This paper sets out the comments and overall counter-proposals by the Chamber of Advocates (the “Chamber”) on the consultative document issued by the Malta Financial Services Authority (MFSA) entitled “Raising the Bar for CSPs”¹.

The Chamber is making these responses as part of the consultative process launched by the MFSA. This paper provides high level responses to the conceptual framework and high-level proposals made by the MFSA in the consultative paper. Accordingly, these responses inevitably lack the level of detail that will ultimately be required for the purpose of putting in place the proper regulatory infrastructure. The Chamber will be in a position, over the course of the next couple of weeks, to establish even the detailed infrastructure and rules for its counter-proposals set out in this paper.

1. Introduction

- 1.1. The proposals by the MFSA in the consultative document are a reaction to the Moneyval report on Malta (the “Report”) that has identified, amongst others, the legal profession and corporate service providers as a high risk with respect to the implementation and enforcement of the regulatory infrastructure to combat financial crime and money laundering. It is therefore with respect to the attainment of the proper standards in this area that the *bar needs to be raised*.
- 1.2. The Chamber believes that in this area Malta, as a nation, needs to make a robust and prompt response to the criticism levelled at it in the Report and indeed, to deal with this effectively. However, it is our view that with respect to the legal profession, the Report levels criticism that goes well beyond the provision of certain company services identified in the consultation document. Indeed, the Report identifies as a matter of significant risk, the lack of overall regulation of the profession. In this respect, the Chamber believes that the proposals made in the consultative document, if implemented, would not suffice to deal with the issues raised in the Report with respect to the legal profession.
- 1.3. The Chamber takes this opportunity, apart from answering the questions raised in the proposals, of making its own recommendations on the matter.

2. Executive Summary

- 2.1. The Chamber disagrees, in principle, with the proposals being suggested in the consultative paper. That disagreement is indeed principle based:
 - (a) firstly, it strongly disagrees that company services provision is, or should be, considered as an industry, sector, or worse, a profession in its own right, or that one can simply place all providers of the same services, independently of the profession they hail from, in the same pot. Conversely, the Chamber believes that these are services which can be provided by different professions and non-professionals, such as persons or entities registered or

¹ Ref. 17-2019 dated 22 October 2019

authorised as CSPs. This is an area of overlap between different practitioners, most notably lawyers, accountants and registered CSPs.

- (b) secondly, each profession that is active in the provision of company services has its own rules and regulations to abide by. The legal profession is subject to AML/CFT regulation in all aspects where it conducts “relevant activity”. The provision of company services is only one such area, in some instances an ancillary area to the provision of other services by lawyers and should therefore remain the subject of regulations made for the profession as a whole, rather than have the profession regulated, in some instances, by another regulator.
- 2.2. It is clear that the Report has levelled criticism at the lack of overall regulation of the legal profession and not just with respect to lawyers acting as company service providers. To meet the expectations of another peer review on this matter, it is unlikely that simply regulating lawyers in the provision of company services will attain any level of success. It is clear that only a more comprehensive regulatory framework, supported by effective supervisory measures for the profession in all its aspects, and in dealing with all areas of “relevant activity” under AML/CFT regulation, can stand some prospect of success.
- 2.3. It would make no sense for the provision of company services by lawyers to be removed from the scope of the current definition of “relevant activity” for the profession and have them regulated separately as a CSP when, in effect, there is already a whole structure of regulation that covers lawyers in the provision of other services, including these.
- 2.4. Accordingly, lawyers should remain subject to the general AML/CFT law, even where these services are concerned, indeed as an integral part of the exercise of the profession, and they should constitute a “relevant activity” like all other instances that constitute a “relevant activity”.
- 2.5. The solution therefore lies in enhancing the regulation of the profession across the board, through the adoption of the Bill that will endow the Chamber with the appropriate tools to exercise rule-making, supervisory and enforcement powers over the profession that will, as part of its overall function, also have the function to regulate legal professionals in this area.
- 2.6. The Chamber believes that there should be the creation of a “National Co-ordination Committee” (NCC) composed of the regulators of the professions and MFSA as regulator of incorporated CSPs, together with the FIAU, as a useful tool that can co-ordinate the efforts of each regulator and ensure, as far as practicably possible, that professional regulations in the matter of AML/CFT reflect equivalent policies; and that there is co-operation in the field of supervision and enforcement. The establishment of an NCC in this area would contribute towards a forum that would not only discuss issues in the area of AML/CFT in the different professions and CSPs but also of being able to identify potential problems going forward at an early stage that would allow regulators to devise reactions to such matters in a more comprehensive manner.

3. The Conceptual Basis for a better regulatory architecture

- 3.1. In the first place, it is fundamental to analyse the service providers and the activities that give rise to the concerns in the Report and therefore, to identify with some precision where the bar needs to be raised. The consultative paper identifies, as does the Report, designated non-financial businesses and professions as a main source of the concern, and that it is therefore these DNFBPs that are really a primary target of improved and enhanced systems going forward.
- 3.2. The Report however also identifies other general shortcomings with respect to the legal profession, including that:
- 3.2.1. There is no specific law regulating lawyers other than ethical standards issued by and subject to monitoring by the Commission for the Administration of Justice.
- 3.2.2. While the authorities have the legal authority to disqualify an advocate upon conviction of a crime, there are no proactive on-going fitness and properness checks for lawyers.
- 3.2.3. Therefore, it is assessed that the market entry measures in Malta for sole practitioners, partners or employed professionals in law firms are not adequate. This is a significant ML/FT risk for Malta, which is recognised by Malta in its NRA, as the legal profession often handles many international customers and faces challenges with identification of non-face-to-face clients.
- 3.3. It is submitted that these concerns need to be addressed just as fully if a comprehensive response is to be made and any response that does not deal with these aspects in the same robust manner is likely to fail.
- 3.4. The activities that give rise to the concern seem to be best described in the following extract from the consultative paper² defining DNFBPs:

As part of the definition of DNFBPs, the FATF Trust and Company Service Providers refers to all persons or businesses that are not covered elsewhere under these Recommendations, and which as a business, provide any of the following services to third parties: [i] acting as a formation agent of legal persons; [ii] acting as (or arranging for another person to act as) a director or secretary of a company, a partner of a partnership, or a similar position in relation to other legal persons; [iii] providing a registered office; business address or accommodation, correspondence or administrative address for a company, a partnership or any other legal person or arrangement; [iv] acting as (or arranging for another person to act as) a trustee of an express trust or performing the equivalent function for another form of legal arrangement; [v] acting as (or arranging for another person to act as) a nominee shareholder for another person.

- 3.5. This is also in line with the requirements of EU AML legislation.

² See Section 2.1.1

- 3.6. Historically, a number of the activities mentioned have been the domain of legal professionals and accountancy professionals, who by virtue of their training and qualifications are deemed to have the proper prerequisites to provide these services.
- 3.7. In 2013, through the enactment of the Company Service Providers Act³ (the “CSP Act”) other persons/entities were allowed to provide certain services, provided that they are registered with the MFSA. Legal and accountancy professionals were exempt from registration and therefore continued to enjoy the same ability to provide these services as had hitherto been the case. Each of those professions remained to be regulated by their respective professional regulators.
- 3.8. The services that can be provided by legal professionals, accounting/auditing professionals and CSPs are the following:
- ❖ formation of companies or other legal entities;
 - ❖ acting as, or arranging for another person to act as, director or secretary of a company, a partner in a partnership, or in a similar position in relation to other legal entities;
 - ❖ provision of a registered office, a business correspondence or administrative address and other related services for a company, a partnership or any other legal entity;
- 3.9. It is unfortunate, but a reality that the introduction of the CSP Act seems to have created, in our view artificially, a new industry sector of CSP services. In fact, we all seem to have even coined this as new term. Whilst it is somewhat convenient to use this term to denote clearly identified services, it has also led to distort the real nature of some of these services. The formation of companies and legal entities, for instance, remains strictly a contractual matter that remains fundamentally a legal service and therefore, the domain of legal professionals in the ordinary course of the practice of their profession.

4. Reactions to the main proposals put forward

Q1. *The Chamber’s views on the extension of the role of CSPs*

- 4.1. The Chamber disagrees with such extension, in principle. The guidance of, and advice to, clients in the submission of applications for licensing and guiding them through that process, is intrinsically a legal service which should not be provided by persons who do not have the necessary legal training and qualifications.
- 4.2. CSPs do not qualify as such as they are not warranted lawyers, nor do they belong to a kindred profession such as accountants, who have the required training to be able to handle such guidance and advice. This is a matter which the proposed Legal Profession (Advocates)

³ Chapter 529 of the Laws of Malta

Regulation Bill (the “Bill”) deals with extensively, based on the distinction of reserved legal services and restricted legal services.

- 4.3. The Chamber also notes that there is absolutely no advantage to gain through such an extension in addressing the concerns that need to be addressed in the Report, which is ultimately the main issue at stake here. The guidance and advice to applicants for authorisations does not fall within the scope of AML legislation at all.
- 4.4. The Chamber has sought further clarification on this point from the Authority during a meeting held with MFSA and it transpires that, in effect, this proposed extension is intended to ensure that only practitioners who have the necessary resources, technical know-how and experience should be able to undertake this service.
- 4.5. The Chamber acknowledges that there may well be different levels of practitioners, both in the legal and accountancy profession, that may have different skill sets and competences, and that when practitioners who do not have the necessary background, technical knowledge and resources embark on guiding applicants for authorisation, this may mean the submission of applications and documentation which is not up to the required level by the MFSA. Indeed, all professionals, properly so called, ought not to engage in activities that require specialised knowledge, unless they have the necessary level of know-how and competence to properly guide their clients. In our view, this is the very essence of being a professional. The Chamber therefore agrees with the principle that such guidance should only be provided by those who can properly and professionally provide such guidance. However, it is our view that whilst there is merit in this position, the manner in which the Authority is proposing to address it is somewhat disproportionate.
- 4.6. This matter needs to be handled through some form of accreditation by the MFSA itself, rather than a requirement to be or become a CSP. In fact, it has no relationship whatsoever to CSPs. Any lawyer should be eligible to provide the service in question by virtue of being a warranted lawyer, but the MFSA, as the licensing authority of regulated business, may impose additional requirements to allow such lawyer to act in respect of providing guidance to others in such matters, if that person submits himself/herself to being tested and assessed for enhanced competence levels, knowledge of the area and its available resources.
- 4.7. In this context, the Chamber trusts that the proposed extension for CSPs to provide guidance and advice to applicants for licensing is relinquished completely. This is certainly not a CSP activity, but rather an activity that ought to be conducted exclusively by those who are qualified to and therefore, can and are authorised to provide legal services.
- 4.8. There are other means in which the MFSA may deal with members of the professions whose work delivered to MFSA may not always be up to the desired standards. This includes the issuance of proper guidance notes which, if not complied with, will entail that such work will be rejected. Another alternative may be that the MFSA, as the issuer of various licences for regulated business, introduces a system of guidance notes supported by a system of accreditation based on competence assessments.

4.9. We believe that this would serve the purpose that is intended to be achieved in a more efficient manner and without the requirement of any disproportionate requirements for competent legal professionals who have the necessary experience, technical competence and resources to have to set up CSPs in order to be able to continue to provide this service to clients.

Q2 Categorisation of CSPs

4.10. The Chamber, in line with its position on Q1 above, disagrees that there is any need for the categorisation of CSPs. First of all, with the removal of the proposal that CSPs can provide guidance and advice to applicants for regulated business, there remains very little purpose in categorising the other two services.

Q3. Removal of exemptions

4.11. The Chamber is in complete disagreement with this proposal.

4.12. It seems that what is being proposed here is really turning the whole principle on its head. The MFSA argues in para. 3.5.1 of the consultative paper that *“the CSP Act exempts a number of persons from the registration requirement thereunder. Experience and engagement with the industry and competent authorities have shown that this has resulted in a large number of persons providing CSP services falling outside the sui generis framework which has, in turn, led to unequal market entry requirements. In this light it is being proposed that the authorisation requirement under the CSP Act is widened by removing: [i] the exemption from registration for advocates, notaries, legal procurators and accountants; and [ii] the notification requirement for persons having a licence or registration to provide company services in an approved jurisdiction and converting it to a full authorisation requirement. The Authority is also considering revisiting the de minimis rule to address the concerns raised by Moneyval and to eliminate any existing supervisory gaps.*

4.13. We reiterate that the provisions of what, since 2013, have been considered as CSP services, had up to then been services which have been provided predominantly by lawyers and accountants. This was indeed the basis why lawyers and accountants benefitted from an exemption under the CSP Act. In actual fact, it was not an exemption at all, but simply the recognition that these were services already provided by those professions that remained regulated by their own professional bodies, the introduction of a new figure that was also able to provide those services within a legal framework that applied only to this new figure – the CSP. The argument now seems to be that lawyers and accountants are considered to be persons providing CSP services falling outside the *sui generis* framework which has, in turn, led to unequal market entry requirements. It is argued that the contrary ought to be the case; lawyers and accountants, by virtue of their own warrant, ought to be able to continue providing the services they provide and which they provided well before the introduction of the CSP framework – not by virtue of an exemption, but rather because they are still subject to AML/CFT regulation, in the course of the exercise of their profession anyway.

- 4.14. The Chamber cannot agree that *“any person providing the services of a CSP would require authorisation thereby ensuring that all CSPs are being subjected to harmonised market entry measures and more rigorous fitness and properness assessments prior to operating.”* This fails to recognise that lawyers and accountants provide and should continue to provide these services as an integral part of their own professional practice and as professionals regulated within their own profession. Indeed, they should not become or turn themselves into CSPs to provide such services.
- 4.15. The solution therefore is certainly not the removal of an exemption under the CSP Act, but rather the recognition that lawyers (and accountants) ought to be able to perform these services as an integral part of their professions; to be subject to regulation and supervision by their respective regulator and, if necessary, to enhance the robustness of the regulation of each profession, a matter which is currently being undertaken in the legal profession through the proposed Bill to regulate the legal profession.
- 4.16. The Chamber believes that some of the services identified as CSP services remain intrinsically a legal service, such as the formation of companies and other legal entities which, as stated, is really a matter of contract. In this context, lawyers should require no licence or authorisation over and above the fact that they are duly admitted as advocates to provide such service. It is also just as crucial to determine with some precision what is meant by the *formation of a legal person*.
- 4.17. Also importantly, we express the view that the practice whereby lawyers sit as company secretaries in Maltese companies, ought to be encouraged. The presence of a qualified lawyer as a company secretary during meetings of directors, who can guide and assist the board in processes and governance issues, is a practice that can certainly enhance the quality of the board of directors.
- 4.18. It is therefore our view that lawyers ought to be able to provide these services in their capacity as lawyers and in the ordinary exercise and conduct of their profession, without any other requirement from any other authority – indeed they should be able to perform these activities on the basis of their warrant as duly admitted lawyers. They should remain regulated in the exercise of these activities by the regulator of the profession.
- 4.19. A pertinent issue that may need further debate in this area relates to lawyers or law firms that, rather than providing company services as lawyers or as law firms, decide to do so as a separate company. We see two alternatives that can be adopted here:
- (a) The first is that as long as the equity base of the company and the law firm are identical, then that firm should have the option of being regulated by the profession but would therefore have to be subject to all the ethical rules of the profession, even in the exercise of company services, notwithstanding that they are provided by a satellite company – indeed the law firm would have to remain accountable for the activities undertaken by the company, in practice the Chamber would for all purposes of professional regulation, look through the corporate veil of such company;

- (b) Alternatively, and in all cases not falling in (a) above, the company through which such services are provided should be required to comply with all other CSP regulation and be subject to regulation by the MFSA, rather than the professional regulator.

Q4. *CSPs to be legal persons*

- 4.20. Subject to the above the Chamber agrees that those who do not provide CSP services by virtue of their professional warrants, ought to set up a legal person through which such services are to be provided.

Q5. *Designated Persons*

- 4.21. Overall, we are in agreement with this principle. Each designated person would, of course, be the person against whose competence and experience the entity will be assessed and who would therefore have to take responsibility for any persons working within that entity.

Q6. *Competence Assessments*

- 4.22. The Chamber has already expressed its view that it is generally in agreement with the introduction of competence assessments. However, we believe that this should be adopted differently to the manner in which it is being proposed in the consultative paper. See Q1 above.

Q7. *Client on-boarding processes*

- 4.23. We agree that the regulator of each profession ought to assess the client on-boarding processes and procedures of applicants. In the case of lawyers, this would fall to be undertaken by the Chamber as regulator of the profession under Bill. Through the NCC, a proposal being made below in this response, the different regulatory bodies would coordinate to establish a level of standardisation and uniformity in the requirements in each profession.

Q8. *Capital Requirements*

- 4.24. Capital Requirements in this respect are, in our view, a misnomer.
- 4.25. CSPs, in all instances, act in an advisory capacity where minimum capital requirements are not and indeed should not be a regulatory requirement. Their intrinsic business does not require them to use their capital for any particular purpose and the worst case for lawyers, accountants and/or other providers in the area would be proper and effective PI cover for negligent or wrong advice.
- 4.26. Introducing capital requirements in advisory business is to place this on the same level as regulated business which is intrinsically capital hungry, such as banking and insurance, but which is misplaced in the case of advisory business.

5. The Chamber's proposed Institutional Architecture

- 5.1. The Chamber's overall reaction to the proposals is that it is in disagreement with the proposed structures and revisions contemplated by the consultative paper. However, the Chamber is aware and indeed highly sensitive to the importance of reacting to the Report, in as robust and prompt a manner as possible. In this context, rather than simply being critical of the proposals, the Chamber believes that it can make constructive proposals on how to address the matter.
- 5.2. The legal profession is subject to AML/CFT requirements under the 4th EU AML Directive as transposed locally in a number of aspects of the exercise of their profession. This includes, but is not limited to, any company services that they provide which brings lawyers, like anyone else within the scope of 'relevant activity', as 'subject persons'.
- 5.3. It would make no sense for the provision of company services by lawyers to be removed from the scope of the current definition of "relevant activity" for the profession generally and have them regulated separately as a CSP when, in effect, there is already a whole structure of regulation that covers lawyers in the provision of other services, including these.
- 5.4. Accordingly, lawyers should remain subject to the general AML/CFT law, even where these services are concerned, indeed as an integral part of the exercise of the profession, and they should constitute a "relevant activity" like the rest.
- 5.5. The Chamber is of the firm view that the current proposals will not address the deficiencies highlighted in the Report with respect to the legal profession and that it is only a more comprehensive system of regulation of the profession generally that will address those deficiencies.
- 5.6. The proposal cannot possibly address in a comprehensive manner the criticism levelled in the Report, simply by addressing the provision of certain company services. The full text of the assessment in that report⁴ goes well beyond the provision of company services. It reads as follows:

When prospective law graduates apply for their advocate warrant exam, they have to submit a police conduct certificate. The warrant is approved by two judges. However, there is no specific law regulating lawyers other than ethical standards issued by and subject to monitoring by the Commission for the Administration of Justice. The same process applies to foreigners wishing to practice law in Malta (however, the police certificates are not verified). While the authorities have the legal authority to disqualify an advocate upon conviction of a crime, there are no proactive on-going fitness and propriety checks for lawyers. Therefore, it is assessed that the market entry measures in Malta for sole practitioners, partners or employed professionals in law firms are not

⁴ See para. 421 of the full report

adequate. This is a significant ML/FT risk for Malta, which is recognised by Malta in its NRA, as the legal profession often handles many international customers and faces challenges with identification of non-face-to-face client.

- 5.7. That criticism cannot be addressed simply by the change in regulatory structure dealing with what is just one (minor) aspect of the services provided by the legal profession. The answer lies in a more comprehensive regulatory infrastructure of the legal profession, and the enactment of the Bill that provides the basis for a modernised regulatory infrastructure for the profession generally and as a whole. Indeed, there is a compelling reason for the Bill to become a priority in addressing the issue, the Report raises as one of the main findings, and classifying it as a matter of significant risk, that there is no law to regulate the legal profession in Malta and that we lack any pro-active on-going fitness and properness checks – with the conclusion that the market entry requirements for lawyers in Malta is not adequate.
- 5.8. It would be short-sighted to think that the CSP proposals can actually deal effectively with the findings in the Report on the legal profession. In any event, it would also make little, if any, sense to have the legal profession subjected to separate regulation or regulators and which simply addresses one area of when lawyers have to deal with AML/CFT matters, rather than to put in place a cohesive and homogenous regulatory infrastructure that deals with AML/CFT matters in the profession’s practice across the board.
- 5.9. The solution therefore lies in enhancing the regulation of the profession across the board, through the adoption of the Bill that will endow the Chamber with the appropriate tools to exercise rule making, supervisory and enforcement powers over the profession that will, as part of its overall function, also have the function to regulate legal professionals in this area.
- 5.10. In this context, the Chamber recommends that the legal profession ought to remain regulated as a profession in all its aspects and areas of practice, including in the areas of company service provision. That the legal profession should be subject to a cohesive and homogenous regulatory regime that extends to all areas of legal practice and which will effectively address the matters raised by the Report. The basis for this solution are already available through the enactment of the Bill – as this will provide the statutory basis for the Chamber to be able to regulate the profession, including with respect to AML/CFT matters, and to do so not only with respect to company services, but across the board in all other areas where lawyers can be undertaking ‘relevant activity’.
- 5.11. We are not privy to the position being taken by the accountancy profession on this matter, however we do see an architecture that would see three regulators, with the legal profession being regulated by the Chamber; the accountancy profession regulated by the accountancy regulator; and *ad hoc* CSPs regulated by the MFSA.
- 5.12. In the context of this proposal, the Chamber believes that a “National Co-ordination Committee” (NCC) composed of the three regulators and the FIAU, would be a useful tool that can co-ordinate the efforts of each regulator and ensure, as far as practicably possible, that professional regulations in the matter of AML/CFT reflect equivalent policies; and that

there is co-operation in the field of supervision and enforcement. The establishment of an NCC in this area would contribute towards a forum that would not only discuss issues in the area of AML/CFT in the different professions and CSPs, but also of being able to identify potential problems going forward at an early stage, that would allow regulators to devise reactions to such matters in a more comprehensive manner.

- 5.13. The Chamber is highly sensitised to the importance of addressing the Report's findings and is committed to work closely with the MFSA, the FIAU and other bodies with a view to put in place, in the shortest possible time, an institutional architecture that will effectively address the Report's criticism. In this context, the Chamber is committed to work on a detailed plan of the manner in which it intends to address the regulation of the profession in this respect by the end of 2019, including setting out timelines and milestones that it targets to attain in this sector by Q1 2020.
- 5.14. Accordingly, the Chamber would welcome further discussion with all stakeholders involved with a view to put together a plan and detailed regulatory infrastructure that would meet the expectations and demands set out in the Report.