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National Legal Profession Anti-Money Laundering & Counter-Terrorism Financing Guidance

Guidance Note No 8 – How Do I Undertake Client Due Diligence?

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How Do I Undertake Client Due Diligence?

The suggestions and recommendations in this Guidance Note do not reflect or express legally binding obligations. Their adoption is voluntary. They are to be applied at the discretion of the individual legal practice.

Aims

The specific aims of undertaking client due diligence in mitigation of your risk of involvement in money laundering and terrorism financing are to:

- know with whom you are dealing;
- better understand the client, the proposed instructions, the nature and purpose of your relationship with the client and the client's objectives and following;
- detect, and enable you to respond to, any red flags for money laundering and terrorism financing.

Knowing your client and understanding the nature and purpose of the intended relationship, including whether the client is acting as an intermediary for another person or entity, is fundamental to your ability to meet your professional obligations. Legal practitioners are obliged to deliver legal services competently and diligently,¹ which is only possible with a good understanding of the client and their needs. Practitioners are obliged to ensure that they avoid engaging in conduct that is likely to a material degree to bring the profession into disrepute.² Involvement in money laundering or terrorism financing, even where the involvement is unwitting, has the potential to have this effect and to diminish public confidence in the legal profession and the administration of justice.

If the client is an entity (for example, a company or a trust) rather than a natural person, you should take reasonable steps to understand who controls the client entity. This can be termed 'beneficial ownership information'. This knowledge is often important simply to provide the client with advice that is consistent with their overall profile and interests. The anti-money laundering and counter-terrorism financing rationale for the need to know who controls the client is to satisfy yourself that the source of wealth of the client is legitimate, makes sense and is consistent with your client's instructions to you.

To guard against unwitting involvement in money laundering or terrorism financing practitioners should also be alert to unusual circumstances including inconsistencies between the client's reported or legitimate sources of wealth and a given set of instructions. This is predicated upon knowing who your client really is, and being prepared to ask more questions than perhaps you might ordinarily be accustomed to asking. You should also be alert to 'red flags' in relation to the client's identity and more broadly, as the engagement progresses.

The nature of the questions you will ask of your client and the depth of your enquiries should be based on an assessment of risk as discussed below and in *Guidance Note No 6 – How Do I Identify and Assess My Risk?*



This steps in this Guidance Note are recommended rather than mandatory. It is up to the legal practice to determine what is appropriate for its particular circumstances.

Guiding Principles

This National Legal Profession Guidance draws on the standards and guidance that have been issued by the global anti-money laundering and counter-terrorism financing watchdog, the Financial Action Task Force (FATF). The FATF has issued standards (FATF Standards)³ that set out essential structural components of risk mitigation regimes.⁴

Accordingly, this Guidance takes a **risk-based approach** to preventing money laundering and terrorism financing. The risk-based approach encourages legal practices to concentrate resources in higher risk areas, and by extension, apply appropriately fewer resources (including staff time) where the risk is lower. Importantly, the risk-based approach also applies to client due diligence. This is why the FATF Standards provide for simplified, standard and enhanced client due diligence.⁵ Consistent with your professional obligations as a legal practitioner (and FATF Standards) there will be never be an occasion where it is not appropriate to perform client due diligence. Client due diligence is always necessary at least to a minimum standard, regardless of the level of risk.

The extent of the enquiries that your practice will make of a client (beyond a minimum standard) will be determined by a judgment about the level of risk involved and the level of risk that is tolerable (that is, the 'risk appetite' of a legal practice). Every client and transaction is unique, and each person in a legal practice engaging with client intake and the client will be exercising a degree of discretion to some extent, whether taking proactive or responsive steps. This requires alertness and engagement and, by implication, for staff to be trained to understand the fundamentals of what money laundering and terrorism financing can look like.⁶ In turn, the exercise of discretion by individuals within the practice will need to be informed by a good understanding of the client due diligence systems that the legal practice has in place and why they are there, as well as the risk appetite of the practice and how these measures work in practice.

Pitfalls to Avoid

The following situations have been identified as common occasions for a failure to properly identify clients:

- *First-time or 'walk-in'*
- *Knowing one party but not the other eg husband and wife*
- *Instructions via an agent with the solicitor having no direct contact with the client*
- *Identification (ID) documents provided without face to face contact*
- *ID documents that are unfamiliar, unusual, unavailable, have no photo, no signature, etc*
- *Discrepancies in ID*
- *ID by a third party*
- *Family members with the same or similar names.*⁷



Steps to Take

Your Intake Process – Consider Introducing a Client Risk Assessment for Money Laundering and Terrorism Financing Risk

Your practice should already have a client intake system in place that includes a process for checking for conflicts, and reflects your file opening and file management protocols.⁸ As each prospective client⁹ is brought in to the practice via the intake system, the practice will effectively be undertaking a multifaceted risk assessment in which prospects for costs recovery and legal prospects, among other matters, are being evaluated. It is good practice to integrate your risk assessment of the client for money laundering and terrorism financing risk into your existing intake process using the principles outlined below.

To assess the level of risk (if any) posed by the client to the practice, you will be taking into account your overall analysis of your practice risk drawing on the sources of information set out in Guidance Note 6. This includes the 11 transactional and commercial activities considered high risk by FATF (see Appendix 1). In addition, client or matter risk should be assessed using at least these risk factors:¹⁰

- What is the nature of the client / client type? (eg a publicly listed company may pose a lower risk)
- What are the geographic connections of the client, counter-party or any third party? (eg see discussion of high risk jurisdictions, below)
- How will you be delivering the service? (eg remotely, in person).

Assessing the risk to your practice of acting for your client will help you determine the extent of the due diligence that you will undertake. In turn, your due diligence enquiries will assist you to exercise your discretion whether to accept the client (or continue with the engagement).¹¹ Your existing familiarity with the client and knowledge of their affairs will be relevant to these decisions.

What Information Will You be Seeking?

While they are not binding, the FATF Standards set recommendations on client due diligence and record-keeping. These may help you to mitigate your money laundering and terrorism financing risk. Note that even in overseas jurisdictions where they are binding (because they have been transposed into domestic law) the FATF Standards for client due diligence almost invariably apply only where the legal practitioner is preparing or carrying out a transaction concerning one or more of the **11 activities** listed in Appendix 1. Where a practitioner is preparing for or carrying out such an activity, FATF recommends that the legal practice or legal practitioner not only identify the client (which is, in any event, required in Australia under legal practice file management rules¹²), but to:

- a. verify the client's identity using reliable, independent source documents, data or information;
- b. identify the beneficial owner, and take reasonable measures to verify the identity of the beneficial owner, such that the legal practice is satisfied that it knows who the beneficial owner is. For clients that are companies, partnerships, trusts or another type of legal person or legal arrangement, legal practices should as far as practicable understand the ownership and control structure of the client;



- c. understand and, as appropriate, obtain information on the purpose and nature of the intended business relationship (or engagement);¹³
- d. conduct ongoing due diligence on the business relationship or engagement, and undertake ongoing scrutiny of any transactions undertaken throughout the course of that relationship, to ensure that the transactions being conducted are consistent with the practice's knowledge of the client, their business and risk profile, including, where necessary, the source of the funds involved.

FATF recommends that legal practices should apply each of the measures under (a) to (d) above 'but should **determine the extent of such measures** using a risk-based approach'.¹⁴

This Guidance uses the terms 'standard', 'reduced' and 'increased' client due diligence to signify the varying extents to which your legal practice may choose to apply client due diligence measures depending on the outcomes of your risk assessments. These categories are not prescriptive. **Standard Client Due Diligence** should be taken to mean the measures in the basic client intake guidance set out in Appendix 2 to this Guidance Note. Where the information in the Appendix indicates areas of discretion for your legal practice, it may be prudent to strive to meet the benchmarks in (a) to (d), above.

Timing and Responding to Issues that Arise as You Undertake Client Due Diligence

It is best to undertake due diligence on your prospective client prior to the engagement, and then to repeat all or some of the steps undertaken at intake periodically. The extent of these enquiries and their frequency should be proportionate to the risks that you have identified in relation to that client or category of clients.

Over time, existing clients should be transitioned into your anti-money laundering and counter-terrorism financing risk mitigation framework. FATF recommends that client due diligence should be applied to existing clients 'on the basis of materiality and risk' at appropriate times.¹⁵

Once the work under the engagement is complete (for example, the property has been transferred in a simple conveyance), there is no legal obligation to repeat the client due diligence.





Reduced Client Due Diligence

Where your legal practice has robustly assessed the client's risk and found the risk to be low, due diligence may be adjusted in particular ways to take account of the lower risk. Examples of what reduced due diligence could look like include:

- verifying the identity of the client and the beneficial owner after rather than before engagement (and, for example, if the transactions involved subsequently exceed a certain value);
- reducing how frequently you undertake client identification updates as part of your ongoing risk monitoring; and/or
- refraining from carrying out specific measures you might consider you require for higher-risk clients to probe the client's financial position and sources of wealth (to understand the purpose and intended nature of the engagement) and instead, inferring the purpose and nature of the engagement from the instructions.

FATF emphasises that reduced measures are 'not acceptable whenever there is a suspicion of money laundering or terrorist financing, or where specific higher-risk scenarios apply.'¹⁶

Increased Client Due Diligence

The keys to dealing with higher-risk situations are due diligence and vigilance.

Higher-risk matters and clients call for increased monitoring and more concentrated due diligence.

In higher-risk situations, where the risk appetite of the practice and results of due diligence lead to a decision to keep the engagement on foot, you should still augment the degree to which you monitor the relationship so you can detect whether any transactions, instructions or activities have an unusual or suspicious appearance. Increased due diligence may include:

- obtaining additional information on the client (for example, their occupation, volume of assets, open-source information including through public databases), and updating more regularly the identification data of the client and any beneficial owner;
- obtaining additional information on the intended nature of the business relationship/engagement;
- obtaining information on the source of funds or source of wealth of the client (see *Guidance Note No 9 – How Do I Ascertain Source of Funds?*);
- obtaining information on the reasons for intended or previous transactions;
- if you are not a principal, obtaining the approval of senior management of your legal practice to commence or continue the engagement; and
- increasing monitoring of the matter/engagement and, where appropriate, the number and timing of



controls applied (such as requiring additional information).¹⁷

Companies and Trusts

Appendix 2 to this Guidance Note sets out information that you may consider obtaining if your client is a company, trust, partnership or other legal person or entity. This would not apply where the client is a publicly listed company or a majority-owned subsidiary of such a company, because they are already subject to enforceable disclosure requirements in Australia.

In the case of a client that is a trust, FATF Standards encourage countries to mandate that legal practitioners identify (and verify the identity) of:

- the settlor;
- the trustee/s;
- the beneficiaries (as individuals, or information obtained as to the class so as to be able to identify individuals); and
- any other natural person exercising ultimate effective control over the trust including through a chain of control or ownership.

The Interpretive Notes to the FATF Standards, while not binding upon Australian legal practitioners, advise that the type of information to obtain in relation to a company, trust or partnership would normally include:

- the powers that regulate and bind the legal person or arrangement (such as the memorandum and articles of association of a company); and
- the names of senior management personnel for the entity (for example, the senior managing directors of a company, trustee(s) of a trust).

The FATF Recommendations, which form part of the FATF Standards, again while not binding upon Australian legal practitioners, indicate that where the client is a company or trust, the beneficial owner should be identified and their identity verified. Again, the exception is where the client or holder of the controlling interest is a publicly listed company or a majority-owned subsidiary of such a company, in which case FATF does not consider it is necessary to identify or verify the identity of shareholders or beneficial owners because they are already subject to enforceable disclosure requirements.

FATF recommends that where you are attempting to identify beneficial owners but enquiries show that there is no natural person who is a beneficial owner, you should take reasonable measures to identify (and verify the identity) of the senior managing official of the entity.

To meet its verification standards, FATF indicates that identity data must be obtained through 'reliable means' which can include the client themselves (as relevant), and reliable third parties, including public registers.

High Risk Countries

Where it is apparent that a client or person or entity controlling the client is from a high-risk country, the practitioner's alertness to the risk of financial crime should be heightened. High-risk countries include those that FATF has determined have weak measures to combat money laundering and terrorist financing.



The association with a high-risk country is a good reason to ask more questions of the client than you might otherwise, until you are satisfied that the client's source of wealth is legitimate.

The FATF has published black and grey lists of countries that can be consulted at <https://www.fatf-gafi.org/en/countries/black-and-grey-lists.html>.

High-risk countries might also include:

- those that are subject to sanctions, embargoes, or other measures imposed by bodies that include, for example the United Nations;
- those identified as having significant levels of corruption or other criminal activity; and/or
- locations from which funds or support are known to be provided to terrorist organisations.

Politically Exposed Persons (PEPs)

It may be that your client due diligence reveals the involvement of a PEP. A PEP is an individual who is or has been entrusted with prominent public functions within a domestic or foreign government or international organisation.

A legal practitioner advising a client that is a PEP or corporate entity or trust that is beneficially owned by a PEP should exercise a higher level of client identification and due diligence. See *Guidance Note No 10 – How Do I Check Whether Someone is a PEP?*

Responsibility

Finally, the principal of a law practice is ultimately responsible for the conduct of the practice, including the conduct of all the law practice's staff members.

The principal must ensure that legal services are being delivered in a competent, diligent and timely manner, and that associates of the law practice are complying with their statutory and other professional obligations. Every legal practice would benefit from an effective compliance management system that incorporates:

- policies and procedures setting out protocols that all members of the legal practice must adhere to. This includes client engagement, file opening and client due diligence (including conflict checking), anti-money laundering and counter-terrorism financing client risk assessment, costs disclosure, protocols for client meetings, approval of letters of advice, briefing counsel, court appearances, undertakings and billing, and anti-money laundering and counter-terrorism financing risk monitoring; and
- appropriate training for staff members about the compliance obligations of the law practice.

Appendix 1



FATF Risk Areas – Recommendation 22(d) and (e)

FATF's risk-based approach calls for client due diligence and record-keeping measures (and ongoing monitoring of the effectiveness of these processes) to be instigated where a practice prepares for or carries out transactions for a client in connection with the activities listed below. This is because the listed activities have been identified by the FATF as posing high levels of risk that legal practitioners may become unwittingly involved in money laundering or terrorism financing (where these risks have not been adequately mitigated). These activities may be found in Recommendation 22, paragraphs (d) and (e) of the FATF Standards.

The activities are:

1. buying and selling real estate;
2. managing client money, securities or other assets (including operating a trust account);
3. managing bank, savings or securities accounts;
4. organising contributions for the creation, operation or management of companies;
5. creating, operating or managing companies, trusts or other types of legal persons or arrangements;
6. buying and selling businesses;
7. acting as a formation agent of companies or trusts or similar entities;
8. 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;
9. providing a registered office, business address or accommodation, correspondence or administrative address for a company, a partnership or any other legal person or arrangement;
10. 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; and
11. acting as (or arranging for another person to act as) a nominee shareholder for another person.

Recommendation 22 urges countries to ensure that money laundering and terrorism financing risk associated with these activities when undertaken by legal professionals (among other specified occupational groups and professions) are mitigated by legally enforceable measures in specified ways. While the Recommendations are not law, it is recommended that legal practices have careful regard to whether they carry out any of these activities, as a first step in the broader assessment of their potential exposure to risk.



Appendix 2

KYC – Basic Level for Transactional Matters¹⁸

This Appendix highlights some key, recommended steps for client intake. It is not a checklist for client intake for all circumstances and should not be mechanically applied.

Client Identity

It is important to sight source identification documentation where practical to better safeguard against the use of inauthentic (forged) documents.

Client is a Natural Person

In the case of an individual client, **depending upon the nature of the representation and level of risk** including any initial concern the legal practitioner may have as to the client's intentions or their background, the legal practitioner may need to obtain **some or all** of the following information, the client's:

- full name;
- employment history including current occupation/activities;
- date and place of birth;
- current and prior residential address/es
- business address/es;
- phone numbers;
- marital status;
- names of prior or current spouses and/or names of children, dates of birth of any such spouses and/or children;
- the name and contact information of any other legal practitioners with whom the client regularly deals;
- the name and contact information of the client's accountant;
- prior criminal convictions;
- pending lawsuits; and
- status of tax return lodgments.

Consider using the '100 points of identification' method as a rule of thumb when verifying identity information. In addition, the client could be asked to provide a summary of their personal and business history which will help with identification of source of wealth and source of funds for a transaction if needed.

Client is a Company, Trust or Other Entity

In the case of an entity that is not publicly listed in Australia, **depending upon the nature of the representation and level of risk** including any initial concern the legal practitioner may have as to the intentions of individual seeking the engagement, or their background, legal practitioners may seek to obtain the names of any subsidiary/parent/nominee entities, and any of the following:

- any Australian Business Number;
- any Australian Company Number;
- the address of the registered office and principal place of business if different; and/or



- the names and details of primary directors, officers, trustees, partners, managers, and/or people serving in any fiduciary capacity in connection with the entity.

The legal practitioner should consider verifying the client by (as applicable) searching the Australian Securities and Investments Commission databases, seeking a copy of the partnership agreement or deed of trust, or other documentation from a reliable independent source proving the name, form and current existence of the entity. Obtaining source identification documentation is often mandatory for practitioners undertaking a conveyance.

The legal practitioner should consider whether it is necessary to verify information on the fiduciaries of the entity as described in relation to natural persons, above. Depending on other risk factors, if not disclosed by partners, members or shareholders of the entity when the above information is provided, the legal practitioner should consider taking steps to determine beneficial ownership as discussed in the body of this Guidance Note.

Consider Seeking Letters of Introduction

In addition to the basic information discussed above, depending on risk factors and the information provided by the client in course of the processes just described, the legal practitioner may consider requesting letters of reference from other professionals that have had dealings with the client such as other solicitors, their accountant or bank.

Designated Persons or Entities

If there is any doubt, or if the client is a foreign person or there are international persons or entities disclosed in the process of identifying the client, the legal practitioner could check the list of persons designated under sanctions against the name of their client, their spouse, any beneficial owners and/or any other related persons or business entities:

<https://www.dfat.gov.au/international-relations/security/sanctions/consolidated-list>.

Open-Source (Internet) Searches

Internet search results are not reliable but are easy to conduct and may provide valuable information that can then be checked. For example, an internet search result might lead to an article that highlights a connection to a business that has not been disclosed – even one involved in a criminal proceeding. Court records can then be checked to verify the information. Searches could be conducted in relation to the client, spouse, beneficial owners and/or any other related persons or business entities.

Repeat and Review

The steps may be repeated on a periodic basis that is appropriate to the size and complexity of the practice, and the level of client risk, to check that the client information is current.



References

1. For solicitors, see Australian Solicitors Conduct Rules, rule 4.1.3.
2. For solicitors, see Australian Solicitors Conduct Rules, rule 5.1.2.
3. FATF (2012-2023), *International Standards on Combatting Money Laundering and the Financing of Terrorism & Proliferation*, FATF, Paris, France (FATF Standards).
4. The essential components (which the FATF urges countries to adopt) are the Recommendations, and additional criteria, parameters and considerations for their design and implementation domestically are set out in Interpretive Notes and a Glossary. Together these make up the FATF Standards, see n 3.
5. The FATF Standards are not binding upon legal practitioners directly. However, this Guidance draws inspiration from and encourages the application of FATF's risk-based approach to due diligence. In keeping with the FATF risk-based approach, in Australia, banks, casinos and other entities, whose client due diligence processes must comply with the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (Cth) and Anti-Money Laundering and Counter-Terrorism Financing Rules Instrument 2007 (No 1), are required to apply client due diligence measures to a certain standard, depending on the assessed level of risk.
6. See *Guidance Note 3 – What Does Money Laundering Look Like?* and *Guidance Note 4 – What Does Terrorism Financing Look Like?*.
7. Lawcover (2022) *Risk Management Workshops for Principals – Workshop 1, All About the Client*, Workbook, p 20.
8. See, for example, in Uniform Law jurisdictions, r 93(2)(a)-(d) of the Legal Profession Uniform General Rules 2015.
9. Henceforth the term 'client' will be used for convenience to include a prospective client.
10. These are also explained in *Guidance Note 6 – How Do I Identify and Assess My Risk?* pp 8-9 in the context of a practice-wide risk assessment, but the explanation holds for client risk assessments equally.
11. You may wish to refer to *Guidance Note No 11 – Ceasing or Declining to Act*.
12. For example, in Uniform Law jurisdictions, see Legal Practice Uniform General Rules 2015, rule 93(2)(a)-(d).
13. These provisions are drawn from Recommendation 10 ('Customer Due Diligence and Record-Keeping') of the FATF Standards, p 14. The original measures are directed to financial institutions and are intended to apply to legal practitioners by application of Recommendation 22. The concept of the business relationship may not be relevant in all circumstances to all legal practitioners. For example, in a family law context, where it is intended that funds from a property settlement may transition through a solicitor's trust account, the legal practitioner is not engaged in relation to 'business' activities. The words 'or engagement' have accordingly be added for relevance to the legal context.
14. FATF Standards, p 14. The FATF links the risk-based approach to the framework set by the Interpretive Notice. The relevant Interpretive Notes are to Recommendations 1 and 10 of the FATF Standards.
15. Recommendation 10, FATF Standards, p 15.
16. FATF Standards, Interpretive Note to Recommendation 10, p 71. This Interpretive Note may be consulted to



understand what factors FATF considers to point to low risk and higher risk scenarios.

17. See also FATF Standards p 70-71. FATF's term for increased due diligence is 'enhanced due diligence'.
18. Adapted from Appendix A to the American Bar Association (2010) *Voluntary Good Practices Guidance for Lawyers to Detect and Combat Money Laundering and Terrorist Financing*.

This Guidance Note was produced on 28 June 2024 and is current at the time of publication.