By Janis M. Meyer Published: Jun 10, 2016

The Panama Papers—An Incentive for 'Spring Cleaning'

The release by the International Consortium of Investigative Journalists (ICIJ) in early April of documents from the files of the Panamanian law firm Mossack Fonseca and additional releases of details of offshore transactions involving well-known public figures, corporations and law firms (the Panama Papers) have shone a light on the use of offshore accounts and shell entities to shield the identities of the real parties to a variety of transactions. https://panamapapers.icij.org. The names of individuals and entities as diverse as the Prime Minister of Iceland, soccer's world governing body, FIFA, and Pablo Picasso's granddaughter have appeared in connection with the releases. The releases have resulted in a flurry of articles concerning tax avoidance, U.S. and non-U.S. tax loopholes, and the role of the legal profession in these transactions. The commentary and speculation will in all likelihood continue as more information is released.

An additional, and perhaps as important, concern raised by the release of the Panama Papers is the manner in which the information was obtained. The ICIJ (along with the German newspaper Suddeutsche Zeitung) received the documents, numbering in the millions, through a cyber-leak at Mossack Fonseca. Regardless of whether the leak originated inside the firm or was the work of an outside hacker, it focuses attention on the vulnerability of law firms that are responsible for maintaining the confidentiality of their clients' files.

A number of articles discussing the Panama Papers have included the allegation that the legal profession has been complicit—and even supportive—in assisting the wealthy in hiding their gains, ill-gotten or otherwise, in secrecy jurisdictions. Similar concerns have been raised about the use of offshore vehicles to hide the proceeds of money laundering and to finance terrorism.

The issue was highlighted earlier this year when Global Witness, an international investigative group, released videos of its meetings with a number of U.S. lawyers purportedly seeking advice and representation for a West African minister of mining who wanted to use what were clearly ill-gotten funds for a number of extravagant investments in the United States. Whether out of ignorance of the law, an overly active business development gene, or a lawyer's inbred courtesy to any potential client, the lawyers, with one exception, appeared eager to assist in suggesting ways the transaction could be structured. Many of the suggestions involved use of offshore accounts or entities. https://youtube.com/globalwitness.

None of the law firms whose names have been mentioned in the Panama Papers or those who were featured in the Global Witness videos have been accused of wrongdoing. As many, including President Barack Obama, have pointed out, "a lot of this stuff is legal." Rupert Neate and David Smith, "Obama Calls for International Tax Reform Amid Panama Papers Revelations," The Guardian, April 5, 2016. Thus, an initial inquiry may be whether there should be reform of the tax laws that permit these types of transactions. Whether the laws should be reformed is an issue for Congress and the Executive Branch to grapple with in the coming months and years.

Meanwhile, it is questionable whether lawyers should be criticized for advising their clients concerning tax strategies that are legal. Even if a lawyer may find a particular tax strategy distasteful, it is not difficult to foresee a malpractice suit against a lawyer who fails to advise her client of that strategy simply because she does not like it. See ABA Model Rule of Professional Conduct 1.2(a) (adopted in most states in varying forms) ("a lawyer shall abide by a client's decisions concerning the objectives of representation and…shall consult with the client as to the means by which they are to be pursued."). The lawyer can recommend against it or, in certain circumstances, resign, but, provided the conduct is legal, it is up to the client to decide whether to pursue it.

The vast majority of lawyers abide by applicable law and by ABA Model Rule 1.2(d) that "[a] lawyer shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is criminal or fraudulent….," and, as noted above, the fact that the name of a lawyer or law firm appeared in the Panama Papers does not mean it has broken the law.

Nevertheless, there will in all likelihood be a continued discussion of whether the United States should adopt a lawyer regulatory scheme that could mandate "know your customer" procedures similar to those used in the United Kingdom and a number of other non-U.S. jurisdictions. Such procedures could include mandatory due diligence at the outset of engagements and on a continuing basis requiring lawyers to have a reasonable belief as to the true identity of the client, the nature or origin of any funds being used for a transaction, and the true nature of the matter they are being asked to undertake.

Although a number of U.S. law firms, particularly those with offices outside the United States, conduct some form of such due diligence as part of their client intake procedures, it is not mandatory here. It is likely, however, that the legal profession will be under increased scrutiny as the Panama Papers revelations continue.

Accordingly, lawyers and law firms should view the Panama Papers as an opportunity to do some internal review to (1) determine whether they have procedures in place to avoid running afoul of the law and the applicable ethical rules, and (2) develop or enhance those procedures where needed to ensure that they are protected against a Panama Papers or Global Witness-type incident.

1. Review Client/Matter Intake Procedures. Firms should review their client intake and screening procedures to ensure that they know who their clients are. Most large firms, particularly those with offices outside the United States, utilize software to check not only for those individuals and entities in embargoed jurisdictions but also for those that may raise questions about the origin of the funds involved or the purpose of the transactions.

The same screening should be done on the type of matter proposed. Is this a transaction that will involve work in a jurisdiction known for having weak controls, financial or otherwise? Is this a client the firm should take on? The best way to deal with a problem client is not to take on the representation in the first place.

Ideally, the procedures should include a periodic review of current clients as well. To conserve resources, firms may choose to limit this review to those practice areas that are particularly vulnerable to the potential for abuse, such as real estate, tax, estate planning, representation of public figures, and any other areas where concealing one's identity may be appealing. This is not intended to suggest that clients in those areas are law-breakers but rather that these matters should receive additional scrutiny.

As noted above, the use of offshore accounts and shell entities is relevant not only to tax avoidance but also to money laundering and terrorist financing as well. In 2010, the American Bar Association issued a paper entitled "Voluntary Good Practices Guidance for Lawyers to Detect and Combat Money Laundering and Terrorist Financing." The Guidance sets forth suggested, not mandatory, procedures, but it provides a road map for lawyers to determine what procedures may be right for their firm. See also ABA Formal Op. No. 463 (2013) (Client Due Diligence, Money Laundering, and Terrorist Financing). Some firms have also looked to the anti-money laundering regimes in the United Kingdom and other non-U.S. jurisdictions for guidance.

2. Know Your Local Counsel. To state the obvious, most, if not all, offshore transactions need the involvement of local counsel. Lawyers should establish a policy of "knowing their local counsel." Firms should take pains to ensure that the local counsel they hire for their clients adhere to the same standards they do. This should be true for all local counsel, not just those outside the United States. Developing a

list of dependable and trustworthy local counsel, standardized procedures for retaining local counsel, and a standard retention letter will help in this effort.

3. Plug Those Leaks. Every law firm is struggling with cybersecurity issues. The release of the Panama Papers illustrates with clarity how client confidences can be breached when there is a leak. Although some may argue that the leak in this instance performed a public service, the fact remains that the majority of lawyers have been charged with safekeeping records of clients who have sought legal services for legitimate purposes and have a right to expect that their confidences will be preserved.

There is no 100 percent foolproof way to avoid leaking or hacking, but firms need to have procedures in place to minimize such events and any damage that may be caused. An increasing number of clients are requiring their outside counsel to have robust security systems in place. Firms may wish to review their policies and procedures with respect to whether all lawyers in the firm should be allowed access to all client information or just that of the clients they are working for, how much access to the firm's systems outside vendors should have, how lawyers and staff access the firm's systems from remote sites, and whether and how lawyers and staff should be allowed to use flash drives, to name just a few areas of concern. The release of the Panama Papers underscores the importance of this effort.

The same is true for local counsel. Law firms should require local counsel to certify that their systems are up to the standards the firms establish for themselves and reserve the right to audit local counsel's procedures.

4. Train Your Lawyers—and Staff. The firm's lawyers, and its staff, need to understand the significance of the issues raised by the Panama Papers. If they do not already have them, firms should develop training programs, for both lawyers and non-lawyers, on proper client intake procedures, local counsel selection, and, of course, cybersecurity. Members of staff are often on the front line, and training may enable them to spot something that "does not look right." The "if you see something, say something" approach may prevent a potential problem the lawyers missed. Some firms have commenced training programs or have enhanced those already in place to cover these points.

This is not an exhaustive list of measures firms can or should take, but a little "spring cleaning" provides a good starting place for firms to avoid, at the least, an embarrassing incident or prevent a more serious charge of wrongdoing.