An Overview of the Legislative Package on Anti Money Laundering

A tectonic shift is on the way in Europe's AML strategy. By the end of this year, the Anti Money Laundering and Combating the Financing of Terrorism Legislative Package presented by the Commission in July 2021 is expected to be adopted by the European Union.

This comes as Belgium, next in line for the 5th round of FATF Mutual Evaluations, takes the presidency of the Council of the European Union; and as several high-profile cases of alleged money laundering have tarnished the reputation of major European Financial Institutions, and of the readiness of the European AML/CFT framework.

While the European Union Member States are, from a technical standpoint, largely compliant with AML regulations and FATF recommendations, there is a clear need for improvement. On average, FATF rated the European Union as having moderate levels of effectiveness for all 11 "Immediate Outcomes" used to evaluate AML/CFT measures.

Faced with the reality of a fragmented regulatory landscape (the Commission identified such problem drivers as unclear and inconsistent rules, inadequate supervision, lack of coordination among FIUs), the European Commission considers that further harmonisation of legal frameworks across the Union is the only way forward. European lawmakers have therefore proposed a momentous package, revolutionary in many respects:

- It sets out to introduce a new European institution, the Authority for Anti-Money Laundering and Countering the Financing of Terrorism (or AMLA, for Anti-Money Laundering Authority)
    - This Authority would have binding powers in its oversight of the European FIUs and FIs
- It purports to address issues of legislative fragmentation across Europe by improving standards through a so-called "single rulebook" of AML policies;

    - This rulebook is particular in that this is the first time AML rules are proposed by the Commission as a directly applicable regulation rather than a directive
- It intends to plug gaps in AML prevention by expanding the scope of Money Laundering activity and providing a response to new financial technologies such as crypto assets.
    - This is the role the 6th AML directive, amending and replacing the 4th and 5th Directives, before full evaluation of either of their impact could be fully conducted (the Commission points to delays due to opening infringement procedures against Member States for non- or incomplete notifications of transposition)
    - The revised Transfer of Funds Regulation lines up with a broader response by EU legislators to new technology – Though part of the legislative package, it has already been adopted on 16 May 2023, and will apply from 30 December 2024.

What can we expect the AML Package to change for Financial Institutions? Are stricter standards and an expanded scope for oversight going to benefit banks and other obliged entities, or will the added workload due to broader requirements for customer due diligence cause further backlogs to the compliance processes?

With provisional agreements and deals reached by MEPs and the Council on most aspects of the AML Package, it is now only a matter of time until the updates are adopted. The entry into force is therefore expected within the next two years at the latest, and obliged entities must be prepared to comply with rules both updated and completely new. This article aims to give a detailed overview of the upcoming legislative package on the prevention of money laundering and terrorism financing in the European Union. While each proposal requires separate analysis, the effects can be expected in bulk. Let's start by taking a look inside the package.

The 2024 outlook for AML in Europe: What's new and what's important about it?

The single rulebook – poster child for harmony?

The operative word for European action on AML in 2024 is "one-stop-shop". While we'll discuss centralised oversight later with the AMLA, it's clear from the idea of a "single rulebook" on AML/CFT that the name of the game is not just harmonisation but standardisation. The previous regulatory efforts on AML in Europe took the form of directives. Directives allowed Member States to adapt the top-down rules to the specificity of national contexts. However, such an approach, caused uneven application of the rules across the bloc.

The solution found by the Commission is essentially to brute-force the problem away: through regulation rather than directive, there are no chances that either the intent or the spirit of the law can be subverted at the Member State level.

But what's being standardised exactly? A lot of already broken ground is included in the Regulation, and this is because it contains a lot of subjects previously included in AMLD4 and AMLD5, which are being repealed by AMLD6.

To be clear: the Regulation does not bring many deep changes to existing AML obligations, but instead creates a standardized approach to provisions formerly part of AMLD4 and AMLD5; while the AML Directive of the Package handles the administrative and supervisory provisions of the prior framework. This is done so existing national legal AML frameworks continue to operate as before from a practical

standpoint (as the set up and upkeep of FIUs, NCAs and so on is left to each Member State to decide as fits the situation), only they will apply the same rules.

Major differences and additions brought by the Regulation, as such, are to do with: An expansion of the "obliged entity" status to a larger array of Crypto assets Service Providers (CASPS) and actors like crowdfunding platforms or migration operators; reinforced requirements for beneficial ownership identification; prohibition of anonymous crypto wallets; and limits to cash or bearer instruments use. Additionally, the Regulation clarifies pre-existing provisions on internal policies and controls, customer due diligence, and data protection.

KEY CHANGES

Entities in scope

The list of obliged entities is **expanded** to include a larger array of **Crypto assets Service Providers** (CASPs) and actors of sectors such as **crowdfunding platforms and migration operators**. As pertains to groups where not all entities would be obliged by AML regulations and directives, Regulatory Technical Standards are expected to delineate the conditions under which the Single Rulebook will apply at group level, though the regulation does come with the intent that **group entities in third countries will have to abide by the European level rules** (or that groups will have to ensure the next best level of compliance by putting relevant measures in place in case direct compliance by third country entities is not possible).

Beneficial Ownership

The Regulation comes with some updates to identifying beneficial owners: It **confirms that the threshold for qualification is at 25%** (there was an initial idea to lower the threshold of ownership to 15% or 5% in certain high-risk sectors, but it seems to have been abandoned) and that **listed companies are exempt** from such measures. It also outlines the situations by which control 'by other means' apply, and mandates Member States to maintain lists of entity types that are concerned by beneficial ownership identification.

The wealth of information required to identify beneficial owners is increasing, with the **addition to Member States' central registers of data such as national ID numbers, TINs, place of birth, description of the ownership structure of the held entity**. On top of broader requirements, the Regulation **makes annual updates to beneficial ownership registers mandatory** and any change outside of annual reporting must be transmitted no later than 14 calendar days thereafter.

More importantly**, third country entities incorporated outside the Union will have to submit beneficial ownership information to the register of the Member State they operate in** (either through entering into business relationships with obliged entities, such as setting up a bank account; or through acquisition of real estate).

Payment limits

Thresholds for certain types of payments are changing, and some reporting responsibilities are shifting: **For crypto assets, any transaction over 1.000€ will need to be subject to CDD measures. For payments in cash, the absolute limit is confirmed at 10.000€** (subject to further limitations by Member States), in addition to a shift in controlling such transactions, now **only the responsibility of financial actors**, whereas before traders in goods had a responsibility to do so (they are now excluded from the AML/CFT scope of obliged entities).

As a reminder, these payment restrictions would not apply in case of person-to-person transfers outside of professional relationships (between family members, for instance).

Bearer Instruments

Bearer shares and cash payments are further restricted, and **anonymous accounts or methods of payment are forbidden** from operating through all obliged entities (this is particularly important for crypto wallets).

Within two years of adoption, bearer shares will be completely prohibited, to the exception of those from companies with securities listed on a regulated market or whose shares are issued as intermediated securities.

CLARIFICATIONS

Due diligence

The Regulation **frames the application of CDD**, the steps to follow in initial client identification, **and the situations where SDD and EDD should apply.**

Outsourcing

It outlines the practicalities of outsourcing, with a particular highlight to **where responsibility lies** (No surprise here, the financial institution that is outsourcing functions to third parties is ultimately responsible for ensuring compliance by those third parties)

Reporting

The Regulation provides **the standard for suspicious activity reporting**: it must deal with the **full spectrum of activity** of a customer subject to transactional analysis, from the transactional pattern to the activity and risk profile. Reporting **must be done on transactions and attempted transactions**, and **no pending operation subject to reporting may be authorised until an FIU is notified and consents**, unless such blockage could be detrimental to an investigation.

Data Protection

The conditions by which personal data may be processed in accordance with the GDPR framework are clarified.

IN SHORT

The Regulation is **not expected to be particularly difficult to comply with for obliged entities**, as many of the delineated practices are already in place, albeit with lesser thresholds in some cases. The key issues here will likely be of an operational nature, as the Regulation does streamlines processes, and many obliged entities which previously had recourse to in-house specific procedures will have to amend them.

Overall, the greatest potential hurdle is from the point of view of smaller entities, or prospective obliged entities (for instance those seeking a banking license), for which the threshold for access to such a status may become that much steeper at the entry point.

As previously mentioned, the new Directive on AML/CFT picks up the slack left by the AML Regulation's replacing of all provisions on the obligations of private sector actors at the European level. AMLD6 instead **focuses on administrative and organisational measures** that are best designed with flexibility in mind: Member States already have oversight structures in place which vary from country to country, which it would not be useful to replace top-down.

The Directive picks up previous provisions from the Fourth and Fifth Directives it repeals and adds on to them: it **clarifies the role and duties of FIUs and national supervisors**, puts forward **a framework for cooperation and joint analysis**, proposes **rules to streamline avenues of communication between obliged entities and FIUs**, and adds **clarifications on the various Member State level central registers** (for beneficial ownership, bank account ownership, and real estate ownership).

Administrative cooperation

In line with the streamlining objectives of the Package, the Directive sets out the **need for rolling risk assessment processes** by the Commission and Member States respectively, to further prevent fragmentation. Data coming out of those assessments as well as performance analysis of Member States' AML frameworks **will be aggregated by the AML Authority** for guidance purposes.

Beneficial ownership registers

Earlier, we saw that the Regulation intended to solidify the requirements for identification of beneficial ownership. The Directive adds on, or rather prefaces this solidification by **setting out the rules that must be followed in the creation, management and upkeep of Member State registers**. In particular, provisions for **ease of access by authorised institutions** (Financial Investigation Units, Self-Regulatory Businesses, obliged entities), **relative loosening of rules relative to public access to registers** (information must be available, but may be conditioned on a fee; exemptions to public identification may not be set for entire registers but only specific entities), or for **setting up interconnection between all central registers of Member States**, aim at creating a **more transparent and practical environment** for AML compliance.

Tangential to beneficial ownership of entities, **ownership of bank accounts and real estate property is also included in the scope of creation of centrally operated registers of information**. Interconnectedness at the supervisory level is expected, and these would only be accessible to FIUs or competent authorities within the boundaries of their investigations and duties.

Financial Investigation Units and Supervision of Obliged Entities

The Directive clarifies the obligations by Member States concerning **oversight of obliged entities**, and the establishment of FIUs. Public national supervisory authorities are further defined in the text, their duties, powers, and scope broadened.

It lists the role and powers that should be granted such FIUs as part of the European AML Framework. **FIUs are expected to work as part of a greater system of financial intelligence** to promote cooperation across the Union and ensure among other things a **harmonised response to reports by obliged entities**, and a **capacity for cross-border analysis**. In that regard, the Directive **opens the door**

for joint oversight efforts through joint analysis of suspicious transactions, notably cross border activity.

Of all four pieces of legislation included in the AML package for 2024, the 6th AML Directive is **the least focused on the obligations of financial institutions and other obliged entities**; but the increased scrutiny on information submitted to central registries, especially for beneficial ownership (foreign entities in particular would now have to provide almost the same level of granularity as domestic ones, as explained above), does come with a **high likelihood that the standards and expectations for KYC will also gravitate towards more precision and wealth of detail**, and therefore continue to foster the need for a competent, efficient workforce (or, failing that, by-the-numbers solutions that will undoubtedly put some strain on the resources of financial institutions).

The AMLA – De-centralised yet centralising

Indubitably, the core pillar of this year's AML legislative package will be the creation of a new European institution: **The Anti Money Laundering Authority**. The political agreement for it has already been reached in December 2023, and **Frankfurt** has been selected as **the host city** for the institution in late February 2024.

Though **a decentralised body** (that is, an agency distinct from EU institutions with a distinct legal personality), in practice the role of the AML Authority for the Union will be one of undeniable **centralisation of practices, knowledge, and cooperation initiatives**. It is intended as a **direct supervisor of certain specific entities active in Europe**, those active in more than 6 distinct Member States, and an indirect supervisor of all the obliged entities under the European AML framework.

The AMLA is not necessarily something that will require much adapting from FIs in general, because it **essentially takes over or adds on to pre-existing oversight**. It does largely the **same things as an FIU** (audit, investigate, inspect on site, mandate changes), but **strictly for the riskiest entities** of the Union - primarily, these will be selected via criteria like transborder or multinational presence, see below for the specificities of selection; it does largely the **same thing as an NCA**, in that it **provides guidance through regulatory and implementation technical standards, as well as recommendations.**

In clearer terms: The Authority will **directly supervise certain entities** that are deemed among the riskiest operating in the Union, and **indirectly supervise** (that is, guide, recommend, assist in coordinating investigations) **all entities otherwise obliged** under the existing EU framework on AML/CFT.

SELECTED ENTITIES

The process of selecting those entities falling under direct supervision is thus: Upon assessment of various criteria such as **size, risk, typical customer profiles, products, or existing third country activity**, those entities with either **high risk in at least four Member States** (if previously investigated for AML breaches); **six Member States** (and high risk in at least one); **seven Member States or more**; will become "**selected obliged entities**" and receive **direct oversight**.

This direct oversight will be multifaceted: The Authority will have **power to directly investigate entities**, request information from the entity (or natural and legal persons belonging to them, third

parties mandated with outsourcing, etc.), conduct **on-site inspections**; and can request assistance in doing so from any National Competent Authority. If an entity is found lacking or in breach of EU law, the Authority will **decide on appropriate measures** to be followed by it, from changes to internal processes to **revoking of their license**. The AMLA will also have the **power to fine entities in breach of their obligations**, through administrative pecuniary sanctions or penalty payments.

To ensure that the fines imposed by the Authority are legitimate and in line with its powers and duties, any such decision may be **subject to review by the Court of Justice of the European Union**.

INDIRECT SUPERVISION

As far as **non-selected entities** are concerned, the AML Authority will not be as much of a felt presence because it will typically position itself as **a support institution** for existing financial supervisors, through **periodic reviews of their readiness and through the coordination of AML colleges**, which are instruments for **cooperation and consultation among supervisors**.

We won't spend too much time detailing the intricacies of setting up the institution in and of itself (though it is important to note that part of the Authority's budget will come from levies paid by the directly supervised obliged entities), **for any entity otherwise obliged under AML/CFT frameworks**, but not selected as directly supervised by the Authority, **nothing really changes**. The overarching guidelines will just come from somewhere different but the FIUs and NCAs will still be the direct points of contact with regulatory bodies.

The Regulation does **leave the door open for circumstances whereby the Authority may direct investigations or sanctions towards a non-selected entity**, sometimes to the point of taking over supervision if the entity is non-compliant.

COORDINATION OF THE FINANCIAL SECTOR

The Authority will be equipped to **coordinate the efforts of FIUs**, particularly by being a fulcrum for so-called joint analyses: Should a Member State's FIU identify a need to request the assistance of other Member States' FIUs, the Authority (after due notification of that fact) will aid in that request.

Additionally, the Authority will **guarantee the effectiveness of the joint analysis procedures** and methods, notably through periodic reviews and updates. Outside of analyses, and further to its role as a supporting institution to national level investigators, it will also **provide for the creation of trainings, personnel, and practice exchanges**; and will be responsible for the upkeep of the supervisory network FIU.net.

Lastly the Authority will become a **primary deliverer of regulatory and implementing technical standards** (whenever the Parliament and Council delegate such tasks to the Commission, and subject to final say by the Commission); regularly publish **guidelines and recommendations on best practices**; and is intended to become a dedicated repository of opinion and technical analysis for all issues related to its area of competence.

This concludes the brief overview of the most relevant provisions of all the components of the upcoming AML package. This analysis does not include a more in-depth look at the intricacies of the internal organisation of the AML Authority, the selection of its board members and staffing, as well as other administrative provisions, on the basis that how the Authority works from within has ultimately little effect on the application of its powers and the scope of its duties.

As a final note, attention should however be paid to the provisions outlining the high degree of cooperation with other EU and non-EU, and AML and non-AML, institutions expected from the Authority; insofar as such cooperation efforts are in line with the objectives of the Regulation. That is, the links created between the Authority and other supervisory bodies aren't likely to push obliged entities to comply with unnecessary or out-of-scope regulations, but the circulation of information across borders and institution is nonetheless worth mentioning, if only because it could create more fault lines for GDPR compliance at the institutional level.

Looking ahead

We've described to some extent the changes and updates coming with the Package. These, per the Commission's own claims, ought to be a benefit to, rather than an imposition, on obliged entities: since rules will be streamlined by the AML Regulation; recommendations and guidance will be centralized; and FIUs will be incentivized to coordinate and further standardise their procedures and responses across the Union ; there is an expectation that the regulatory burden, especially when it comes to setting up internal policy and dedicated response, tailored to the specificities of national frameworks, will be all the lesser.

With the same rules applying in the same way throughout the Union, one size could indeed fit all situations. This is particularly beneficial to financial actors that have cross-border activities or multinational presence in any capacity (subsidiaries, outsourcing, correspondent banking situations, etc.). Smaller institutions aren't likely to feel much of a difference (though it is also expected that AML compliance will become cheaper as a result also): if active in only one jurisdiction already, the only possible effect will be that some of the technicalities in applying AML obligations will shift towards the standard set by the Authority.

As such, preparing for the entry into force of the AML package is unlikely to be a tall order, at least with the currently available information: For one, the texts aren't finalised yet, so there is always the possibility that the final version of the provisions is slightly different from the current one (for instance, there was an initial MEP agreement in March 2023 to set the threshold for beneficial ownership to 15% rather than 25%, but the current text of the Regulation has discarded that proposal) ; for another the actual technical and implementing standards for each piece of legislation are also pending, so the exact application of each provision is also up in the air.

Ahead of the package becoming binding throughout the European Union, the best strategy for financial institutions should nonetheless not be a passive one. It is still possible at this stage to assess, internally, whether procedures already in place will need to be adapted or whether the already applicable national legislation is sufficiently similar to what it will be within the Package's framework update to not merit any broad modifications. This is especially important in areas such as customer due diligence and beneficial ownership identification, which are in particular focus in the Package.

As always, proper compliance starts with people: proper staffing, and proper training of staff ahead of the application will ensure the smoothest transitions.

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