EU AML/CFT authority: key success factors

1. An ambivalent level of efficiency in a fragmented, though single, market stresses the need for current EU regulatory efforts

The Chair introduced another important discussion on the key success factors for an effective EU anti money laundering (AML)/combating the financing of terrorism (CFT) Authority (AMLA). In summer 2021, the European Commission presented its ambitious package of legislative proposals to strengthen the EU's AML and CFT rules, including the creation of a new EU authority to fight money laundering.

There is surely agreement on the need for a single EU rulebook on AML and CFT, and that we can all benefit from the AMLA. At the same time, there is a question around how to make AMLA operational. The Chair asked what the success factors for effective operation of the AMLA are and what missing elements might lead to a protective AML/CFT framework.

The Chair asked if the current AML/CFT framework is effective and how successful the EU is in fighting AML/CFT as a member of the international community.

An official stated that there is an ambivalent picture of how successful the European Union is. On one hand, the Commission and member states are very ambitious when it comes to regulation. This is also observed at the Financial Action Task Force (FATF). In some important pillars of AML, the European Union even provides the model that other regions strive for.

There is certainly a problem with regulation fragmentation. There is even more of a problem of implementation in Europe as an area in which there is a common market without borders. We must definitely improve in financial intelligence and detect cases much earlier than we currently do. We have fragmentation in both regulation and the application of the rules in the common market, creating loopholes and offering room for regulatory arbitrage. We have no focus point at the supranational level; building this with the new AML package is desirable.

We have a comparatively weak sanctions regime, and we sometimes have weak law enforcement in member states. Last but not least, our companies are struggling with considerable legal uncertainty when it comes to the interaction of AML with other areas of law like privacy.

The points of focus of the EU are welcome

An industry speaker stated that Western Union supports the AML package and the move from a directive to regulation and a rulebook type format. It also supports the establishment of the AMLA. Regarding the main challenges in the current framework in Europe, a positive approach is to give the top five parts of the package that we like. Implicit in each of these are areas with opportunities.

Improved cooperation and information sharing, particularly among national Financial Intelligence Units (FIUs), is addressed by the package and would be helpful. Western Union's investigators have seen instances in which national FIUs and law enforcement in Europe have clearly not been speaking to one another.

The second item that the package addresses is a common Suspicious Transaction Report (STR) template. This will help European law enforcement and those in the private sector to provide information more quickly and efficiently to governments.

The third item is privacy constraints and the occasional conflicts between the General Data Protection Regulation (GDPR) and AML regulatory obligations. When financial institutions encounter this conflict, they necessarily tend to err on the side of privacy rather than providing information to law enforcement.

The fourth item is de risking. This is a big issue for Western Union and other money transmitters, and particularly for agents. However, more needs to be done. Something like the European Banking Authority (EBA) opinion of January 2021 would be helpful.

The fifth item is a review of Electronic Identification (EID). It would mean that digital transactions tended to be less costly, and it would flow through a better experience for the customer.

Implicit in these areas are challenges. There are certainly areas in which the US is behind on beneficial ownership. Work on beneficial ownership was underway eight years previously, and it is only just starting to make progress. Europeans have been far ahead of the US on this.

2. Anticipated points for attention for an efficient AMLA

The Chair asked what the main coordination challenges for the AMLA are and how closely it should cooperate with the national competent authorities (NCAs). A regulator stated that supervising money laundering activities and combatting terrorist financing is a difficult job. The European Central Bank (ECB) has just asked for all of its institutions to be taken away and responsibility for them given to others.

It is necessary to consider some coordination issues. Given the AMLA's history, it would also be possible to

say that the AMLA should take everything. However, there are issues.

2.1 One essential challenge is to figure out how to reap the benefits of the enormous efforts made

We did not do well enough in the early teens, but the current efforts from the biggest financial institutions and supervisors reflect that nobody wants to be caught with a money laundering or terrorist financing scandal. We do not have a problem on the authority or big institution side in terms of a lack of effort. Danske was in a deplorable state and still has work to do. It has dedicated 15% of its staff to preventing money laundering and terrorist financing. This is not a lack of effort.

A regulator stated that he is a supervisor who has many questions to ask banks, but it is necessary to determine how to complete these tasks more smartly and avoid duplicating efforts. This is where the AMLA could make the most of its progress. It is necessary to be much better at using technology while cooperating on its use and sharing data between financial institutions and between the public sector and financial institutions.

2.2 Fully learning on the SSM arrangements and experience should help to address the AMLA coordination issues

A regulator stated that much of what a prudential supervisor does consists of the same items that an AML supervisor looks at. There are questions of compliance, culture, risk management and potentially whether people are fit and proper. On a good day, there is a coordination problem; on a bad day, there is a turf problem.

The Chair asked if it is possible to draw similarities between what was achieved for the Single Supervisory Mechanism (SSM) and what is currently proposed in the AMLA regulation in terms of the organisation and articulation of onsite supervision. A regulator stated that there are a number of similarities between the AML package's intended achievements and the SSM. The global financial crisis showed that divergence in the implementation of supervisory practices was detrimental to the stability of Europe's banking sector. An integrated system of supervisory authorities with a strong centre is necessary.

Similar dynamics are at play around AML/CFT supervision and the integration of the European financial system. It was natural for the AMLA proposal to draw on the SSM model from an operational point of view. The most striking similarity relates to the fact that AMLA will use joint supervisory teams (JST) to supervise the financial obliged entities that will be directly supervised by AMLA. Those JSTs, with staff both from AMLA and national authorities working together, will be at least as important in the AMLA context.

Within the SSM, the JSTs have been key for the development of a genuine common supervisory approach for the supervision of significant and less significant institutions. It is possible that the way the AMLA will supervise the institutions it will be in charge of will percolate down to the way supervision of other entities is performed. In that way, it will level up the whole supervisory framework.

There are a few differences between the JSTs currently in place in the SSM and those envisaged in the AMLA proposal. Only one of them is somewhat technical, but it is crucial. In the Commission's proposal, the JSTs will be responsible for offsite and onsite supervision. Within the SSM, onsite and offsite supervisory tasks are performed by different dedicated teams. The combination of JSTs for day to day offsite supervision and dedicated onsite teams for performing those in depth reviews has proved to be highly beneficial. Having dedicated onsite inspection teams gives the supervisory toolkit more teeth.

Although the AMLA proposal rightly draws on the SSM experience, when it comes to the operationalisation of AMLA's direct supervision, there is still room for drawing to a larger extent on the successful SSM experience.

3. AMLA must build up an agile and prospective risk-based approach

Efficient links within the network of FIUs and supervisors and technology should help.

The Chair stated that AMLA borrows a large amount from the SSM. There is still some room. He asked if AMLA needs to embrace an intelligence based approach.

A regulator stated that this is a complex proposition for AMLA and a key opportunity to support those in Europe to be very effective in transnational crime. When considering the complex moving parts of its responsibilities, it will have to select the firms that pose the most significant risk for money laundering accurately. The debates around whether all countries should be included in order to engender a good money laundering supervisory culture are reasonable. However, there is also a proposition whereby they need to work with the NCAs that will eventually do the vast majority of frontline money laundering supervision to ensure an effective, integrated system. There is an overwhelmingly strategic challenge to supervise Designated Non Financial Business and Professions (DNFBP), of which there are more than 2 million. There is going to be a very targeted, strategic approach.

There is a unique opportunity to drive up the effectiveness of transnational coordination with respect to FIUs and the effectiveness of suspicious transaction and order reports (STOR). This must be done in a risk based way, but it must also be dynamic because the typologies will change. People will be better able to identify crimes and be responsive in a timely way only where they are intelligence led. That is a complex proposition. All regulators will coalesce around the ideas of being risk based and targeted to spend rare supervisory resources on the issues of most concern. This would presumably be risk-focused.

However, money laundering is secretive and designed to evade detection. Typologies change over time and with success. Information sharing is at the heart of this, but it is possible to have much information, necessitating a rigorous, structured, systematised risk assessment and targeted deployment of resources. However, it is necessary be dynamic enough to take relevant

information from the front line and the participant firms themselves. It is also necessary to work effectively with the FIUs whose core raison d'être is to detect the crime and pass that on to law enforcement, and that must be disseminated well across Europe to raise standards with FIUs. It must be disseminated well with NCAs and the ECB because the SSM is a core supervisor for some of the most important entities in Europe that might pose threats to money-laundering.

A regulator added that it is extremely important to recognise that supervisors play a large role and are supporting actors to a large extent because the real key in terms of the value chain is the link between the financial institution, prosecutors, and the police. It is necessary to support it.

As public authorities and supervisors, it is necessary to monitor the banks well enough, supervise them and contribute to improving this. It comes back to making KYC processes easier. There is currently an explosion in suspicious activity reports because it is the easiest thing to do. There is very little feedback between FIUs, the police, prosecutors and institutions that work on reporting to them. That is the key part of the value chain that supervisors and public authorities need to support.

3.1 Further reinforcing cooperation duties of FIUs should be envisaged

The Chair asked how cooperation could be fostered among national FIUs and if there should be a European FIU. A public representative stated that his view on supervising is similar to those of his colleagues in many ways. On FIUs, the current proposal is not sufficiently ambitious and does not go far enough. There are concerns from the national FIUs along the lines of them saying that they need to control the information and be responsible for inviting others. They believe that politicians and others might find out that they are suspicious about them if information leaks.

While the aforementioned position is respectable, the current proposal does not go far enough. While joint actions are taken by different FIUs, it is very easy for someone to say they do not want to participate in the joint analysis. They do not really have to give more of an explanation. If one FIU asks for a joint analysis, the centre passes it on and does not do anything. It is just process management. Not much value is added by sending out invitations.

The FIU cooperation should not just be voluntary because the AMLA is only adding red tape. It is already possible to simply ask for help via email. The joint analysis should be much more ambitious. The Parliament has asked for the creation of a European FIU in the past, and we should at least move towards the germ of a European FIU. This is difficult because different member states have different resources, but a European FIU would be vital, particularly because this does not have to be about criminal law. Some people understandably say that this is criminal law and Europe has nothing to do with it. However, there is great scope for administrative action, and it is advisable to move forward with this.

3.2 AML requires setting the scope of AMLA supervision appropriately in order to also address non-financial obliged entities, crypto assets and crypto currencies

The Chair highlighted the issue of the optimum scope of the AMLA's supervision. He asked if the so called 'geographical approach' is sufficient and if the non financial sector could also be involved.

3.2.1 Non-financial obliged entities require attention

An official stated that the geographical approach is the concept for selecting entities. If one entity is only active within one member state, or even only regionally within one member state, then it should remain under the supervision of the corresponding national supervisor. The AMLA should support and take care of convergence. If this is becoming a high risk institution then the AMLA can step in as provided for emergence, cases. If an entity has major cross border activities that can lead to blurred responsibility and coordination is hardly managed, the AMLA should be the competent authority.

In terms of the right scope, the AMLA needs a deep understanding and experience of supervision in each member state so that the AMLA has comprehensive coverage of the internal market. For that reason, at least one institution in each member state should be supervised by the AMLA.

It is positive that the AMLA will be involved in the non financial sector at some stage, but this is a completely different story: There are 2 million obliged entities. Many notaries, lawyers, casinos and car dealers can hardly conceive of being supervised on a supranational level. Nevertheless, the AMLA should also start to look at this in a phased approach. However, ensuring that the financial sector is properly supervised first, should be the priority.

3.2.2 Defining priorities is difficult since assessing the risk posed by an entity is challenging

The Chair asked about the selection criteria for direct AMLA supervision. A regulator stated that this is a simple question but a complex issue. Engaging in an entity's AML/CFT risk exposure is less straightforward than measuring the size of its balance sheet. AML/CFT risk exposure is not always commensurate with an entity's volume of clients or activities. Selection criteria for the financial obliged entities that will be directly supervised by the AMLA should be broad enough in terms of activities and geographical extent.

With respect to the type of activities, there should be a single set of criteria for all financial institutions. There is probably no valid reason for differentiated criteria for banks and other financial institutions. Activities performed by means of direct provision of services can also be as exposed as AML/CFT exposure and activities performed through branches, networks of agents or distributors. There should be a single way of treating the free provision of services under free establishment. Selection criteria should clearly address the riskiness and cross border activities in a more neutral way when it comes to the types of entities and the modalities of the cross border activities.

3.2.3 AMLA geographical coverage: pragmatism and consistency

A regulator stated that the AMLA's direct supervision should cover the whole internal market with respect to the geographical coverage. One indirect way to go in that direction would happen if, once an entity had been selected, all the financial obliged entities that belong to the same group would be under the supervision of the AMLA. The JST would supervise the group on an individual and consolidated basis. Another step forward would be that, if a selected entity has a non EU parent company, all the EU based entities sharing the same non EU parent company should also be directly supervised.

There would be a more direct way to ensure the coverage of the whole internal market. The ACPR and the Banque de France believe there would be merit in adding at least one entity in each member state for supervision by the AMLA. This should foster a common supervisory approach and ensure that direct and indirect supervision are not completely separate areas. A close link between the two will also be crucial.

4. Appropriate AMLA governance is essential

A public representative stated that the AMLA governance structure is very important. On the EBA failure, we would not be present without the report of the Court of Auditors on Danske Bank that essentially said the EBA had 'messed up'. The EBA failure was a question of governments. The state voted to stop that sanction. It is known that the EBA even involved the state. Governance is crucial, and the governance in front of us is a positive step forward.

5. Digital innovation raises varied AML challenges

The Chair asked whether crypto asset providers should comply with regulation. A regulator stated that the European Securities and Markets Authority (ESMA) talks about crypto from the perspective of investor protection and Markets in Crypto Assets (MiCA) regulation. It knows that there are concerns from every angle. However, the technological innovations underneath crypto could also bring huge benefits for financial inclusion. The potential for smart contracts is astonishing. Nobody wants to obstruct innovation.

However, when considering the purpose of regulation, macro, micro and investor protection, ESMA only brings regulation forward where we believe that the offering requires some kind of parameter or safety to work well. Looking at crypto, the meaning is unclear because there are so many different types of asset reference tokens. There is no inherent value. The regulator is very comfortable with the proposition that any means of transfer of value should have the same types of requirements as the traditional financial means.

Crypto has been used to facilitate crime and is the payment method of choice for ransomware attacks. It is very high risk from an AML perspective. Truly applying the conventions that necessitate knowing the client, the source of funds and where the money is going seems more like a level playing field, which makes sense.

5.1 Technology should help progress on ID verification, onboarding and information sharing and improve banks' customer experience regarding AML procedures

The Chair stated that AML/CFT risk management is not possible without accurate data and technology that allows for use of the data and drawing all the benefits from it. The Chair asked how to ensure effective private/public sector data sharing and how big an issue GDPR is.

A regulator offered to present his vision, where it could hit a wall and why. His vision would be a setup in which banks using national electronic IDs could verify customers' identities. There are different stages of national IDs and sensitivities, but they should have security and safety around them so that they can be used to verify customers in all but high risk cases.

The regulator receives many emails and letters from 30 year customers of a bank asking why they need to go there to show their passport. There is a gap between the public's demand for a tough fight against money laundering and terrorist financing and its willingness to do it; this needs to be overcome. The regulator's second aim is for banks to be able to call government lines to ask if a person with a particular ID, is a "politically exposed person" (PEP) or a PEP relation.

An industry speaker endorsed the proposal in the package encouraging technological innovation. He welcomes the European Commission's proposal on EID. It would create a much better customer experience if there were a harmonised, EU wide identity framework. It would also be much less expensive. Those costs are passed on to the customer. We support that. However, we would like to retain the option of a traditional in person KYC for populations like migrants.

A regulator stated that the third element of his vision is that it is advisable to build registers of beneficial ownership that could be used for identification by the banks that on board customers. If these types of actions were taken, it would also work out the issue of de risking.

The regulator would also like banks to share information on risk flags and would like authorities to share more data. If these issues can be addressed smartly across the EU, it will make a substantial difference in fighting money laundering and terrorist financing. The AMLA will have a huge role.

5.2 Facilitating information sharing and interlinking AML entities should be beneficial and would reduce the risk of only focusing on some entities

The Chair asked about the technology part. An industry speaker stated that there are always ideas around beneficial new technology. However, an opt in regime for the AMLA would be more efficient and would place Europe ahead of the US. At present, we register with the

Financial Crimes Enforcement Network (FinCEN) as a money transmitter, but we have 49 states that examine us. Europe would leapfrog the US if we could do that.

If only a small number of financial institutions are designated as high risk, then they could also be named and shamed. We are still trying to determine what will mark someone as high risk. Western Union hopefully does not fall into the new category of super high risk, but it would certainly be classed as high risk, so it would not want to be one of only two or three entities that could be in the category.

The Chair stated that it would be difficult to conclude the discussion. Simple questions received very complex answers. Building an EU wide AML/CFT framework with AMLA at its centre will be a very difficult task.

Lithuania has experienced huge success in technology sector expansion, but all of this success comes at a cost and creates understanding of the risks. In the financial sector a few decades ago, there were extensive discussions about credit risk, liquidity risk and related matters. However, AML/CFT risk management and cyber security are connected top priorities. There is no other way to succeed in the project ahead.

5.3 Leveraging technology to make KYC processes further effective raises GDPR challenges

A regulator stated that the real problem is not lack of effort or supervision; it is the need to work together to provide information for know your customer (KYC) processes and transaction monitoring. The AMLA could make a difference here because many of these items also relate to European legislation. GDPR is a considerable issue. This is where it is advisable to move and cooperate if it is really desirable to make a difference.

Another regulator stated that the entities will have to adopt technology and be network types of organisations in a structured way. If there is a serious money laundering threat, the revocations of licences will happen to entities and other institutions. Two way feedback loops are important. New, anonymised technology can assist that in being more effective. However, there will be a debate about the effectiveness of disclosures for the purposes of advancing money laundering investigations and the undoubtable importance of privacy. More work in this space is necessary.

The regulator stated that she recognises that the Commission is going to do more work in terms of clarification, but this area might prove to be an impediment without further work. We must become an intelligence led organisation.

A regulator stated that privacy issues surround these items along with GDPR. It is necessary to have a public discussion about how far to go in relation to these matters. There is a trade off between fighting money laundering and terrorist financing and privacy. An enlightened discussion would avoid hitting the wall and determine how to prioritise these items.

A public representative stated that it is difficult to envisage a consensus between Parliament, legislators, and countries on the trade off between data protection and intelligence. There is objective alliance between the good and the bad here. The people who support privacy are objectively protecting the people who want to commit crimes; this is the truth of how data protection works. The public representative wants privacy protection, but he agrees that banks should be able to share flags and authorities should be able to share more information. This is the biggest struggle.