

Reflection paper on possible elements of a Roadmap for seamless cooperation between Anti Money Laundering and Prudential Supervisors in the European Union

Introduction

On 8 May 2018, First Vice President Timmermans, Vice President Dombrovskis and Commissioner Jourova have sent a letter to the ESAs and SSM Chairs with the purpose of initiating a collective reflection about how to improve the framework for cooperation between AML/CFT¹ and prudential supervisors².

The letter reflects the growing concerns felt by policymakers that, in the wake of recent money laundering scandals, there may be gaps in the EU's supervisory framework, in terms of the division of responsibilities and the sharing of critical information, which have contributed to the failure or serious difficulties of several European banks and presented challenges for the control of financial stability risks. A spotlight has been cast on the extent to which the current EU supervisory system fully and adequately covers the risks to stability associated with AML/CFT failings. In particular, these experiences have exposed shortcomings with respect to cooperation and information sharing, both at domestic level between different authorities and across borders in other EU member states.

The letter invited the ECB and the ESAs to take part in a joint working group with the relevant Commission services, tasked with identifying "specific actions to be taken by the respective authorities" to improve practical coordination of AML supervision, in the short term and beyond.

Composition and mandate of the Joint Working Group

The Joint Working Group started work in June 2018 and is chaired by the representatives of the Commission's Directorate-General for Justice and Consumers (DG JUST), and the Directorate-General for Financial Stability, Financial Services and Capital Markets Union (DG FISMA), and includes the representatives of the European Central Bank, and of the three European Supervisory Authorities, and the Chair of the ESAs Joint Committee Anti-Money Laundering sub-committee (AMLC).

In addition to the issues explicitly addressed in the letter of the Vice-Presidents Timmermans and Dombrovskis and Commissioner Jourova, the Joint Working Group has taken into consideration the relevant statements which were made more recently at high political level, specifically in the 19th June Franco-German Meseberg declaration

¹ AML supervision covers also countering financing of terrorism ("CFT").

² Prudential supervision is referring here to the activities of competent authorities that monitor and enforce compliance with prudential rules for regulated financial undertakings (i.e. credit institutions, investment firms, insurance and reinsurance companies, payment institutions etc)

roadmap³ and in the 25 June letter from Eurogroup Chair, Mario Centeno, to the President of the European Council Donald Tusk⁴.

The present document, drawn up by the Joint Working Group sets out the scope of possible actions that could be undertaken by the various relevant stakeholders (elaborated below in the Problem definition section).

This is a working document which does not represent the views of the institutions and bodies participating in the Joint Working Group. This reflection paper is being sent to Member States and the Chairs of the ECON, LIBE and TAX3 Committees of the European Parliament to seek views on possible next steps to enhance the cooperation between the prudential and the AML supervisors in the EU.

Problem Definition

The Joint Working Group recalls that combating money laundering and terrorist financing is a shared responsibility between Member States, national authorities and European institutions and bodies (within their respective mandates), which needs to be acknowledged as a priority and supported by adequate resources. Such shared responsibility implies that those responsible must ensure that all tools and measures available under the existing regulatory and institutional frameworks are fully utilized in a way which delivers optimal results. It is also important that the adequacy of the existing framework is constantly monitored.

Whereas the Anti-Money Laundering Directive (AMLD)⁵ has a wide scope, covering also entities outside the financial sector, this paper is limited to setting out issues concerning financial institutions that are subject to both prudential supervision and AML supervision. Acknowledging the substantial improvements brought to the AML framework by the recently adopted AMLD 5, the paper focuses on the interaction between the framework governing prudential supervision in the Union and the implementation of the AMLD.

The Joint Working Group has performed an initial stocktake of the situation and identified a number of shortcomings in the current arrangements:

1. Under the current framework (i.e. CRD, MiFID, Solvency II), **prudential supervisors** are obliged to consider ML/TF aspects with respect to a number of their prudential supervisory functions:
 - Authorisation of financial institutions;
 - Assessment of acquisitions of qualifying holdings;

³ "For anti-money laundering, we need a set of substantive core criteria which reliably measure the money-laundering-risks that exist in the banking sector. In addition, we need a robust monitoring process reporting on the effective implementation of these criteria. Both, criteria and monitoring process, should be developed by December 2018 by European Institutions, including SSM, and Member States, with France and Germany providing common input. It is essential that such process is not only of formal nature, but materially reduces risks stemming from AML-non-compliance.."

⁴ "Finally, there is agreement on the importance of enhancing the current monitoring of the implementation of Anti-Money Laundering measures. As a first step, the institutions will prepare a report in July. Based on this, and in close cooperation with the National Competent Authorities, there should be agreement on further measures by end 2018, possibly as part of an Action Plan".

⁵ DIRECTIVE (EU) 2015/849 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, amending Regulation (EU) No 648/2012 of the European Parliament and of the Council, and repealing Directive 2005/60/EC of the European Parliament and of the Council and Commission Directive 2006/70/EC

- Fit and proper assessment of the management body;
- On an ongoing basis, supervisors must assess all the risks to which an institution is or might be exposed
- Withdrawal of authorisation in case a financial institution is found liable for a serious breach of national AML provisions.

However in practice, prudential supervisors may often not sufficiently consider AML/CFT aspects, for a number of different reasons:

- EU prudential rules are not sufficiently precise, which leads to differing transposition and to divergent supervisory practices across Member States;
 - There is no detailed articulation of the interaction between prudential and AML supervisory frameworks, such as specification of the type of information to be exchanged, triggers, risk-based metrics, criteria for breaches under the AML/CFT framework or particular ML/TF risks that ought to be reflected in the prudential process;
 - In the EU legislation there are no detailed provisions on cooperation obligations between prudential and AML supervisors, that would facilitate timely and regular input of AML/CFT-related findings into the activity of prudential supervisors, nor any clear obligation in prudential or AML/CFT legislation for the prudential supervisor to notify AML/CFT supervisors of any AML/CFT issues which might be discovered, or ML/TF risks identified.
2. Within the Banking Union's **Single Supervisory Mechanism**, the ECB must integrate AML/CFT concerns systematically when performing its supervisory tasks towards significant institutions and when authorising and assessing acquisitions of qualifying holdings in the case of both significant and less significant institutions, in the same way as all other banking supervisors. That task is however made more challenging because:
- As a supervisor working across many different national jurisdictions, the ECB must apply differently transposed EU legislation, potentially resulting in differences as to what input the ECB is entitled to receive from the AML supervisors and how such input can be integrated into the prudential supervisory processes.
 - The ECB has the competence and responsibility to withdraw authorisation from credit institutions for serious breaches of AML/CFT rules, while remaining fully dependent on national AML supervisors for information relating to such breaches detected by national authorities.
3. With respect to **AML/CFT supervision**, the EU's AML framework is based on a minimum harmonisation Directive and host state supervision of establishments:
- The resulting divergences in national laws are not conducive to coherent AML supervisory practices.
 - Cooperation mechanisms under the AML/CFT framework are less developed than compared to the framework for prudential supervision,

and while the AMLD5⁶ seeks to remove obstacles and improves the exchange of information between AML and prudential supervisors, the framework leaves discretion as regards sharing of information between AML and prudential supervisors;

- There are no detailed procedures for cooperation in case of the need to withdraw an authorisation on the grounds of ML/TF concerns;
 - AML rules are not clear with respect to enhanced supervisory powers;
 - AML rules do not clarify how cooperation between AML authorities and prudential supervisors should take place in cross-border scenarios, e.g. where AML governance of a branch or a subsidiary could potentially impact the risk profile of the entire bank or group prudentially supervised in another jurisdiction;
 - At international level, coordination in relation to EU-specific AML/CFT issues remains fragmented.
4. **The ESAs** have a role to play with respect to AML supervision: as part of their broad objective of ensuring integrity, transparency and orderly functioning of financial markets, strengthening supervisory cooperation and preventing regulatory arbitrage, they must ensure that provisions of AML/CFT legislation are applied effectively and consistently. Under the AML Directive and Fund Transfers Regulation, they have been empowered to promote convergence in AML/CFT supervision, for example through the issuance of guidelines, preparation of draft regulatory technical standards and the investigation of specific cases of breaches of EU AML law. However, tight resources coupled with a lack of appropriate powers have an impact on the ESAs' ability to take on a more substantial role in the AML/CFT area. More specifically:
- Prioritisation, amongst multiple competing tasks have so far led to insufficient resources being directed towards the ESAs' role with respect to AML/CFT. Collectively, the ESAs have 2.2 full time staff working directly on AML issues, of which 1.8 are at the EBA;
 - In recent years, the focus of the ESAs and the Joint Committee's Anti-Money Laundering Committee has been on delivering upon a number of mandates delegated to them under the AMLD4. As a result, their capacity to undertake more extensive convergence work has been limited to the EBA providing on average two training sessions per year and sharing information in the Joint ESAs Anti Money Laundering Committee (AMLC), where possible in its quarterly meetings, which also have full policy agendas.
 - Although the EBA is the most proactive ESA in relation to AML/CFT, it does not have the necessary powers to act as the lead authority on AML/CFT;
 - Finally, the ESAs do not have the requisite powers to be adequately involved in cooperation with third countries on AML/CFT related issues.

⁶ It is noted that the AMLD5 has only very recently been adopted and Member States have until January 2020 to transpose it into their national legal order. Therefore, the substantial improvements of the AMLD5 have yet to be put into practice.

Possible Actions

In order to address the various identified problems, the Joint Working Group has identified the following possible actions for consideration. Section 1 focuses on actions which could be taken by prudential supervisors, section 2 on actions which could be taken by AML supervisors, Section 3 focuses on actions which could enhance the effectiveness, powers and governance of the ESAs, while Section 4 discusses a possible longer-term objective to address the identified problems.

1. *Better incorporation of AML/CFT considerations into prudential supervision*

1. Mapping of relevant ML/FT risks and best prudential supervisory practices to address them [possible timeframe by end H1 2019]

In light of divergent prudential supervisory practices, the EBA, in cooperation with EIOPA and ESMA as relevant, could undertake an evaluation with a view to identifying and mapping:

- the **different aspects of AML/CFT** that are of pertinence for prudential purposes: e.g. a bank being abused for ML/FT purposes; shareholders or members of the management board having links to ML/TF; deficiencies in banks' risk control and compliance function; features of business models that might be indicative of increased ML/TF risks;
- the **key areas** that need closer scrutiny by prudential supervisors in relation to ML/TF risks;
- **best practices** for integrating AML/CFT-related concerns into prudential supervision.

Such an exercise should be undertaken in cooperation with prudential supervisors and in consultation with AML supervisors.

2. Common guidance on how to factor AML/CFT related aspects into the prudential supervisory process [possible timeframe by end of 2019]

Even though prudential supervisors are not in charge of ensuring compliance with AML/CFT rules, given the implications for the financial soundness of supervised entities and more generally for financial stability, it is essential that all prudential supervisors appropriately account for ML/TF risks. To ensure that this is done consistently, prudential rules could better articulate how prudential supervisors should factor-in ML/TF risks. In this vein, the EBA, in cooperation with EIOPA and ESMA, could develop, as a follow-up to the mapping of best practices, guidelines under Article 16 of the ESAs Regulations or draft technical standards (where allowed under a specific mandate in sectoral legislation), specifying how prudential supervisors should:

- take into **account ML/TF risks in ongoing supervision**, potentially on the basis of commonly used or more specific indicators and associated appropriate warning thresholds: common guidance could be developed in sectoral supervisory guidelines, such as EBA's SREP Guidelines (particularly the

sections on business model analysis, governance and risk management assessment and conduct risk), as well as horizontally for all sectors;

- factor-in **ML/TF risks during the processes of authorisation**, particularly in terms of ensuring robust governance and internal control mechanisms, as well as suitability of shareholders: common guidance could be developed in sectoral supervisory guidelines or technical standards, such as the EBA's draft regulatory technical standards on authorisation and assessment of shareholders, as well as horizontally for all sectors;
 - integrate **ML/TF risks during the overall assessment of qualifying holdings and fit and proper tests of management**: common guidance could be developed horizontally to complement the existing ESAs guidelines for all sectors.
3. **Ensuring effective cooperation between prudential supervisors and AML supervisors and Financial Intelligence Units (FIUs) [possible time frame: by end-2019]**

Given that prudential supervisors rely on the relevant findings of AML supervisors and FIUs for their assessments of the prudential impact of ML/TF risks and that they may themselves uncover aspects relevant for those authorities, the cooperation between all relevant authorities could be further enhanced. In this context, it could be envisaged that:

- **prudential supervisors cooperate with AML/CFT supervisors** throughout the various phases of the supervisory processes, with a view to establishing adequate channels for information exchange and ensuring ongoing information flows in both directions (ensuring that prudential supervisors receive from AML/CFT supervisors and FIUs relevant quality information in a timely manner and equally obliging them to report to AML supervisors and/or FIUs their own findings of suspicious activities or AML/CFT failings);
- EBA, in cooperation with EIOPA and ESMA, and building on the provisions on distribution of competences in the AMLD and in the prudential frameworks, develops guidance with a view to helping prudential supervisors **identify relevant competent AML/CFT supervisors as counterparties in case of groups operating cross-border** (both intra-EU and in third countries), in relation to the supervision of individual entities (branches and subsidiaries), as well as of the overall group;
- the prudential framework is amended to provide for **binding mediation powers for the ESAs/EBA** in relation to potential disagreements between prudential and AML/CFT supervisors, particularly disagreements concerning the information to be exchanged. Such mediation powers are aimed at ensuring the adequate and consistent application of Union law;
- prudential supervisors send a clear **signal to the industry** that ML/TF risks are factored also into the prudential supervisory process and that they cooperate closely with AML supervisors for this purpose.

4. Clarification of aspects related to the withdrawal of authorisation [possible timeframe: *by mid-2019*]

To ensure that the withdrawal of authorisation for a serious breach of AML/CFT rules by the prudential supervisors is applied consistently and takes into account possible financial stability implications, several aspects could be clarified:

- the **degree of/criteria guiding discretion of prudential supervisors** in withdrawing the authorisation once a serious breach of AML/CFT rules is ascertained;
- the uniform interpretation of the **language referring to serious breaches of AML/CFT rules** in the Capital Requirements Directive⁷;
- the consistent consideration of **consequences of licence withdrawal**, particularly in terms of the need to preserve critical functions in the bank, the involvement of resolution authorities and the possibility to suspend payment of deposits by the deposit guarantee scheme;
- identification of **measures** available to prudential authorities to address prudential concerns stemming from ML/TF risks and breaches of AML/CFT rules.

5. Consistency throughout the prudential and AML frameworks [possible timeframe: *by 2023*]

To ensure consistent and clear interactions between the prudential and AML/CFT frameworks, EU legislation could be adjusted in the long run.

6. SSM- specific actions

Whilst the actions envisaged under the first five points are as relevant for the ECB as they are for all national prudential supervisors, there are certain specificities of the SSM that may require additional actions from the ECB:

1. The ECB should intensively continue preparations and **conclude a multilateral MoU with all relevant AML/CFT** authorities by 10 January 2019, in line with AMLD5. The MoU should be as broad as possible and should ensure that the ECB receives quality information from AML/CFT authorities in a timely manner and that the ECB reports to AML/CFT supervisors on its own possible findings of suspicious activities or AML/CFT failings.
2. By mid-2019, the ECB could ensure that **practical arrangements** are operational which allow the ECB to consistently factor-in AML/CFT concerns when performing its supervisory tasks. In particular, given that the ECB is in charge of authorisation, withdrawal of authorisation and assessment of acquisitions of qualifying holdings, also in relation to **less significant institutions**, the ECB could further enhance the cooperation framework with the national competent authorities to ensure:

⁷ Directive 2013/36/EU of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms (CRD IV) (as amended)

- effective and efficient interaction;
- timely exchange of quality information;
- specification in detail of the respective duties of the ECB and the national competent authorities.

The ECB could also issue instructions and guidance to national competent authorities, where relevant and subject to the conditions set out in the Council Regulation (EU) No 1024/2013.

2. Enhancing cooperation and exchange of information among AML supervisors and prudential authorities

1. Common guidance by the ESAs on improving AML supervision and exchange of information between the relevant authorities

The ESAs have the ability to:

- consistently and rigorously monitor the implementation of the Risk-Based Supervision Joint Guidelines issued by the ESAs in April 2017, and expand them to include guidance on best practices for the imposition of sanctions in cases of breach of AML/CFT rules, while taking into account the different practices and legal frameworks in Member States [**possible timeframe: by end-2019**];
- enhance the ESAs Risk Based Supervision Guidelines to be applied by the AML/CFT supervisors specifying common procedures and methodologies for the supervision and assessment of credit and financial institutions' compliance with anti-money laundering and terrorist financing rules [**possible timeframe: by mid-2019**];
- follow up on the recommendations addressed to them in the Commission's 2017 Supranational Risk Assessment, and provide an update report by January 2019;
- finalise the guidelines on the cooperation of, and information exchanges among, AML/CFT supervisors of credit and financial institutions and prudential supervisors, which will establish AML colleges, taking into account the need to ensure the broadest possible scope for such exchanges, by January 2019;
- finalize the joint opinion that needs to be delivered pursuant to Article 6(5) AMLD, looking in particular into strategic aspects of AML/CFT supervision, by January 2019.

2. Memorandum of Understanding between AML supervisors and the ECB

With the support of the ESAs, AML supervisors should press forward urgently with their work to support preparations and conclusion of a multilateral MoU with the European Central Bank by 10 January 2019. The scope of the MoU should be as broad as possible, covering exchange of all relevant information, and should also give non-exhaustive examples in order to ensure clarity and guidance as to the relevant information that should be exchanged.

3. Report on FIUs⁸

The Commission may examine the need for more centralised AML/CFT supervision in the context of its task to produce a report on FIUs' cooperation under Article 65(2) AMLD, as amended, by June 2019.

4. Twinning programmes to allow regular staff exchange and mentoring

AML supervisors, in collaboration with the EBA could present a final plan, by mid-2019, to establish exchange and mentoring (**twinning and secondee**) **programmes** that would allow regular exchange of staff and mentoring between supervisors and potentially with the ESAs, with a view to sharing best AML/CFT supervisory practices and finding ground for convergences whilst understanding national specificities in relation to AML/CFT.

⁸ FIUs mainly carry out analytical functions, in line with their tasks under the AMLD and in accordance with international rules. In some Member States the FIUs also carry out supervisory tasks in relation to all or some of the obliged entities under the AMLD (which include but are not limited to credit and financial institutions).

3. *Enhancing the effectiveness, powers and governance of the European Supervisory Authorities*

1. **Giving the ESAs the resource capacity to make better use of existing powers and tools to improve AML supervision and to devise strategies for further enhancing the supervisory framework**

Starting now, the EBA could be given the capacity to further prioritize its work on AML/CFT issues, in cooperation with EIOPA and ESMA as relevant. This could include:

- undertaking stringent reviews of the activities of supervisory authorities (AML and financial/prudential) to identify weaknesses and best practices. These reviews could lead to objective and concrete recommendations on how AML supervision must be improved, coupled with an effective follow-up mechanism to ensure compliance with the recommendations;
- building on the outcome of the reviews, increasing the number of AML focused trainings to both AML and financial/prudential supervisors, as well as providing thematic guidance to authorities;
- continued monitoring as to the need to investigate breaches of Union law in the field of AML/CFT;
- making greater use of the Anti-Money Laundering Committee (AMLC) as a forum for exchanging views on AML supervision and relevant risks; this would entail meeting more frequently, establishing additional channels for information sharing and extending time and scope for discussions to cover also specific case studies, exchanging best practices and elaborating common approaches to common problems; consideration could also be given to raising the level of participation to this committee to the heads of the national AML supervisors;
- promoting the use of existing prudential supervisory colleges to improve coordination and exchange of information on concrete AML/CFT issues and the links between prudential and AML colleges;
- using Article 33 of the EBA Regulation as a legal base to develop a strategy for third country AML/CFT authorities' interaction, including establishing a framework for such interaction (e.g. by preparing a framework MoU) and coordinating material EU-relevant contacts between Union and third country AML/CFT and prudential supervisors in relation to AML/CFT relevant findings in the sectors falling under EBA's remit. This coordination function would support and not replace the necessary and appropriate contacts that prudential and AML/CFT supervisors have or will have with their third country relevant counterparts;
- building on the work carried out in the AMLC, developing a plan for setting up and maintaining a Union-wide centre of expertise for information gathering and exchanges in relation to AML-relevant findings in the financial sectors falling under EBA's remit. This could include collecting relevant information and establishing a centralised database to facilitate assessment of ML/TF risks in the context of fit and proper assessments.

In order to allow the EBA, in cooperation with EIOPA and ESMA to deliver on this mandate, adequate resources need to be made available.

2. Ongoing legislative proposals could help strengthen the ESAs' toolbox for AML purposes

During autumn 2018, Council and Parliament could consider the significant benefits to the ESAs' AML/CFT-related work which the on-going ESAs review could bring about, and in particular that:

- Based on risk priorities and the findings of reviews, strategic supervisory priorities, could be set for AML supervisors which should be reflected in the Joint Opinion that the ESAs deliver for the purposes of the Commission's biannual supranational risk assessment report;
- more independent reviews of the AML-related activities of supervisory authorities (both financial/prudential and AML) to provide objective and transparent perspectives on supervisory practices, as well as to assess in what directions more AML/CFT work may be needed;
- In circumstances where a dispute has arisen between the competent authorities in respect of information sharing and exchange, the ESAs can carry out a binding mediation. Such mediation powers are aimed at ensuring the adequate and consistent application of Union law.

3. Strengthening the ESA framework and putting the EBA in the lead for AML/CFT supervisory issues

Consideration could be given to the following additional legislative changes, which could further strengthen the contribution that the ESAs could make to the fight against AML/CFT:

- centralising the AML mandate, which is currently shared among all three ESAs, within the EBA, in close cooperation with ESMA and EIOPA, as relevant. This would bring greater effectiveness and efficiency and capitalise on the AML work carried out by the EBA already today;
- On the basis of information from national risk assessments, reviews and other relevant sources, carrying out an annual risk assessment exercise to test strategies and resources in the context of the most important emerging ML/TF risks; the findings of the exercise should be reflected in the Joint Opinion that the ESAs are obliged to deliver under the AMLD for the purposes of the Commission's biannual supranational risk assessment report
- building on the AMLC, setting up a Union-wide centre of expertise within the EBA to gather findings from AML supervision and AML-relevant findings from prudential supervision and ensuring that the information is appropriately analysed and disseminated to competent authorities concerned, as well as shared amongst the ESAs;

- entrusting the EBA with the responsibility to cooperate and liaise with the relevant third country AML supervisors with a view to better coordinating action at EU level in material AML-related cases involving a cross-border and third country dimension. This coordination function should support and not replace the necessary and appropriate contacts that supervisory authorities in the EU already have or will have with their third country relevant counterparts.

4. Possible longer-term objectives leading to an enhanced AML/CFT supervisory framework

A range of further measures to improve the effectiveness and convergence of AML supervision could be considered, such as:

- introducing more empowerments in AML/CFT legislation to make use of tools that allow for greater convergence of AML/CFT supervision such as, for example, regulatory and implementing technical standards; and
- transforming the AML/CFT Directive into a Regulation in order to achieve greater consistency and convergence in the application of Union AML/CFT rules.

Moreover, with regard to the outcome of the ESA review and the report that the Commission has to produce under the AMLD5 on FIUs, also structural changes to enhance the supervisory framework could be considered. The following actions could be considered:

- establishing at EU level a mechanism to better coordinate the activities of AML/CFT supervisors for financial sector entities, notably in situations where the AML/CFT concerns are likely to have cross-border effects;
- a possible centralisation of AML supervision via an existing or a new Union body having the ability to enforce harmonised rules and practices.

Follow-up:

The present document provides the first mapping of possible actions to enhance the effectiveness of interaction between prudential and AML/CFT supervision of financial institutions in the EU.

The Commission would welcome views on these possible actions, in order to inform potential next steps by the European institutions and bodies.