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John BERRIGAN, Director General, Directorate-General for
Financial Stability, Financial Services and Capital Markets Union (FISMA)

24 March 2022

Subject: AML/CFT legislative package – issues related to supervisory cooperation and the selection criteria for direct supervision

Dear Messrs Garicano, Radev, Moulin and Berrigan,

On 20 July 2021, the European Commission published an anti-money laundering and countering the financing of terrorism (AML/CFT) package¹ consisting of four legislative proposals that, once in force and implemented, will transform the EU's legal and institutional AML/CFT framework.

As you know, the EBA has a legal mandate to prevent the use of the EU's financial system for money laundering and terrorist financing (ML/TF) purposes. Over the past six years, we have worked to put in place a holistic approach to tackling the ML/TF risk across all areas of supervision and across all aspects of an institution's operations and life cycle.

The EBA works closely with 57 AML/CFT supervisors from all Member States that are members of our AML/CFT Standing Committee (AMLSC). In this context, AML/CFT experts participating in the AMLSC discussed the Commission's proposals and identified a number of technical points that relate to the future approach to AML/CFT regulation and supervision that I believe can be helpful to you when finalising this legislative package.

I am attaching to this letter their agreed views on some of the technical points in the package for your consideration.

From the EBA's perspective, I would like to highlight, in particular, the changes experts think may be

¹ https://ec.europa.eu/info/publications/210720-anti-money-laundering-countering-financing-terrorism_en

needed to ensure that the AMLA can exercise its powers effectively, and to ensure that it will supervise directly those cross-border groups that expose the EU single market to the highest levels of ML/TF risks.

I would also like to highlight the importance experts place on strengthening the cooperation provisions in the current drafts to ensure that the AMLA will be able to cooperate effectively also with those financial services supervisors that do not have a direct AML/CFT remit, and with the three ESAs so that rules that apply to financial institutions and their supervisors in the EU are consistent and workable. ML/TF cannot be fought effectively in isolation, and it will be important that we continue to build on the synergies that exist between the AML/CFT, prudential and conduct frameworks to safeguard a holistic approach to protect the European Union from financial crime.

I hope that you will find this contribution useful. My staff and I remain at your disposal, if you deem it of interest, for further discussions.

Yours sincerely,

[signed]

José Manuel Campa

CC: Irene Tinagli, Chair of the Committee on Economic and Monetary Affairs, European Parliament

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Eero HEINÄLUOMA, Member of European Parliament

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AML/CFT experts' views

on cooperation and on the selection criteria for direct supervision by the new Anti-Money Laundering Authority in the proposed AML/CFT package

Introduction

1. On 20 July 2021, the European Commission published an AML/CFT package² consisting of four legislative proposals that, once in force and implemented, will transform the Union's legal and institutional AML/CFT framework. This package comprises of:
 - a proposal for a Regulation of the European Parliament and of the Council on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing ('AMLR')³;
 - a proposal for a Regulation of the European Parliament and of the Council establishing the Authority for Anti-Money Laundering and Countering the Financing of Terrorism and amending Regulations (EU) No 1093/2010, (EU) 1094/2010, (EU) 1095/2010 ('AMLAR')⁴;
 - a proposal for a Directive of the European Parliament and of the Council on the mechanisms to be put in place by the Member States for the prevention of the use of the financial system for the purposes of money laundering or terrorist financing and repealing Directive (EU) 2015/849 ('AMLD6')⁵; and
 - a proposal for a recast Regulation of the European Parliament and of the Council on information accompanying transfers of funds and certain crypto-assets ('FTR')⁶.
2. This note sets out the view of AML/CFT experts from competent authorities in the European Union (EU) on those aspects of the package that relate to cooperation and the criteria to select institutions for direct AMLA supervision. It was adopted by the European Banking Authority's (EBA) AML/CFT Standing Committee, which brings together national competent authorities that are responsible for the AML/CFT supervision of credit and financial institutions.

² https://ec.europa.eu/info/publications/210720-anti-money-laundering-countering-financing-terrorism_en

³ COM/2021/420 final

⁴ COM/2021/421 final

⁵ COM/2021/423 final

⁶ COM/2021/422 final

3. AML/CFT experts welcome the European Commission's proposal to develop a single rulebook for the AML/CFT legal framework in the EU, and the associated establishment of an EU-wide AML/CFT supervisor (AMLA). Once established, AMLA will have direct and indirect supervisory powers over credit and financial institutions, as well as indirect supervisory powers over non-financial institutions.
4. These proposals are in line with the EBA's response to the Commission's Call for Advice on the future legal AML/CFT framework⁷ and with the EBA's response⁸ to the public consultation on the AML/CFT Action Plan. Once adopted and implemented, these proposals will transform the EU's legal and institutional AML/CFT framework.
5. AML/CFT experts identified points that the Commission and the co-legislators may wish to consider during their negotiations of the proposed AMLAR, AMLR and AMLD6 to strengthen cooperation between different stakeholders and to ensure a holistic, consistent and robust approach to tackling ML/TF risks across all areas of financial services supervision. Experts also considered the proposed criteria to select institutions for direct supervision by the AMLA and how these could be reviewed to ensure that the highest ML/TF risk cross-border financial institutions are identified.

Ensuring effective cooperation and information exchange to support a consistent approach to tackling ML/TF risk in the EU's financial sector

6. The Financial Action Task Force (FATF) sets global AML/CFT standards. Its standards are clear that cooperation between different stakeholders is one of the key components of an effective AML/CFT regime. In line with the FATF's standards, the proposed legislative package contains provisions that the Commission hopes will ensure the highest level of cooperation between the widest range of stakeholders.
7. AML/CFT experts support the Commission's objectives. Strengthening cooperation between different stakeholders in the fight against financial crime has been a key focus for competent authorities (CAs) and the European Supervisory Authorities (ESAs) in recent years, through for example, the conclusion of a multilateral cooperation agreement between the European Central Bank (ECB) and AML/CFT supervisors⁹, the establishment of an AML/CFT colleges framework¹⁰ and

⁷ EBA's Report (EBA/REP/2020/25) on the future AML/CFT framework in the EU in response to the European Commission's Call for Advice on defining the scope of application and the enacting terms of a regulation to be adopted in the field of preventing money laundering and terrorist financing

⁸ Response by the European Banking Authority to the European Commission's public consultation on an AML/CFT Action Plan and the establishment of an EU level AML/CFT supervisor, published 19 August 2020, available: https://www.eba.europa.eu/sites/default/documents/files/document_library/Publications/Other%20publications/2020/923773/EBA%20response%20to%20the%20consultation%20on%20the%20Commission%27s%20AML%20CFT%20action%20plan%20final%20for%20publication.pdf

⁹ The Multilateral Agreement on the practical modalities for exchange of information pursuant to Article 57a(2) of Directive (EU) 2015/849, concluded between the ECB and the competent authorities responsible for supervising compliance of credit and financial institutions with anti-money laundering and countering the financing of terrorism (AML/CFT) obligations under the fourth Anti-Money Laundering Directive (AMLD4); approved by ESAs on 10 January 2019, available here: <https://www.eba.europa.eu/esas-announce-multilateral-agreement-on-the-exchange-of-information-between-the-ecb-and-aml-cft-competent-authorities>

¹⁰ ESAs joint guidelines (JC 2019 81) on cooperation and information exchange for the purpose of Directive (EU) 2015/849 between competent authorities supervising credit and financial institutions (AML/CFT Colleges Guidelines)

the publication of guidelines¹¹, which set out practical modalities for cooperation between AML/CFT supervisors, prudential supervisors, and Financial Intelligence Units (FIUs). Drawing on the lessons learnt from the ESAs' work, and their own experience, AML/CFT experts consider that explicit requirements for cooperation in the legislative text are necessary to ensure that cooperation can take place and will be effective in practice. To this effect, the Commission and the co-legislators may wish to consider during their negotiations of the legislative proposals whether the current draft is sufficient to ensure that:

- the AMLA and other CAs that are responsible for the supervision of credit and financial institutions are able to cooperate and exchange information with each other, and with the widest scope of other stakeholders;
- the roles and responsibilities of home and host Member States' supervisors are clearly defined in situations where obliged entities operate in another Member State under the freedom to provide services or under the right of establishment;
- the AMLA and other EU standard setters, including the ESAs, cooperate continuously and effectively, at all stages of the policy-making process, so that their respective regulatory instruments are consistent and complementary, and that they can be implemented effectively by credit and financial institutions and their respective supervisors;
- the key terms are defined unequivocally and that they are used consistently across the AMLR, AMLAR and AMLD6.

A. Cooperation for the purposes of AML/CFT supervision

8. AML/CFT experts note that the new legislative package includes high-level requirements for cooperation between home and host supervisors, between EU and non-EU financial supervisors as well between financial supervisors and certain non-AML supervisors. The cooperation framework in the legislative proposal is based in part on existing arrangements, including AML/CFT colleges. AML/CFT experts have identified a number of points that, if not addressed, may hamper the effectiveness of cooperation and information exchange and therefore, effective supervision.

- **Cooperation between home and host Member States' supervisors**

9. Article 33 of AMLD6 provides for the AML/CFT supervision of obliged entities that operate across borders in different Member States under the freedom to provide services (FPS) or under the right of establishment (ROE). Article 34 provides for the cooperation in the context of group supervision. In the AML/CFT experts' view, it would be important to clarify the roles and responsibilities of home and host Member States' supervisors in this regard. Examples of areas where clarifications would be beneficial include:

¹¹ EBA Guidelines (EBA/GL/2021/15) on cooperation and information exchange between prudential supervisors, AML/CFT supervisors and financial intelligence units under Directive 2013/36/EU

- a) host Member States supervisors' roles and responsibilities. According to Articles 2(5) and 2(6) of the draft AMLR, host supervisors' powers in respect of establishments, like branches of foreign banks or other forms of establishment of foreign payment institutions, such as a network of independent agents, are broader than those in respect of credit and financial institutions that only provide services in the host Member State but are not established there. However, the current provisions in Article 33 of the AMLD6 do not appear to recognise these differences.
- b) host Member States supervisors' powers to take measures or impose administrative sanctions where breaches or weaknesses are identified. AML/CFT experts note that host supervisors' powers to impose certain measures on their own initiative or in agreement with the home Member State supervisor appear to be determined based on the type of institutions, instead of the type of operation that an institution has in the host Member State. For example, in respect of payment service providers, electronic money issuers and crypto-asset service providers (CASPs), host Member State supervisors appear to have exclusive powers to take certain measures¹² to address serious failings, regardless of whether they operate in the host Member State on a right of establishment (ROE) or free provision of services (FOS) basis, whereas for other types of credit and financial institutions, an agreement from the home supervisor seems to be required¹³. In the AML/CFT experts' view, such approach may hamper cooperation and should be re-assessed in a way that is consistent with supervisors' powers in the draft AMLD6.

- **Cooperation in AML/CFT supervisory colleges**

10. AML/CFT experts welcome the translation of the ESAs' AML/CFT Colleges Guidelines¹⁴ into the draft legislative package¹⁵. To minimise disruption and to ensure the continued functioning of more than two hundred AML/CFT colleges that have been set up so far, the experts consider that it would be important that the proposed provisions mirror those set out in the ESAs' AML/CFT Colleges Guidelines where possible. Based on AML/CFT experts' experience of establishing and operating AML/CFT colleges since 2020, adjustments in the new package may be necessary in respect of the following points:

- a) the scope¹⁶ of the AML/CFT colleges framework. The proposal limits the scope of the colleges framework to EU credit and financial institutions with establishments¹⁷. As it is the case for the AMLA selection criteria (refer to Section D below), other types of groups for which AML/CFT supervisory colleges currently exist are not included in the current draft of the AMLD6. In the experts' view, narrowing down the scope of the existing AML/CFT supervisory colleges framework in this way may risk lowering the current standards for

¹² Article 33(4) of the draft AMLD6

¹³ Article 33(5) of the draft AMLD6

¹⁴ Joint guidelines on cooperation and information exchange for the purpose of Directive (EU) 2015/849 between competent authorities supervising credit and financial institutions (The AML/CFT Colleges Guidelines).

¹⁵ Article 36 of the draft AMLD6 and Article 29 of the draft AMLAR

¹⁶ Articles 36(1) and (2) of the draft AMLD6

¹⁷ Article 36(1) of the draft AMLD6

cooperation and cross-border AML/CFT supervision that have been put in place in accordance with the ESAs' AML/CFT Colleges Guidelines.

- b) conditions for establishing and maintaining AML/CFT colleges¹⁸ are based on the geographical exposure of the group. This means that a college is required to be established and maintained regardless of the ML/TF risk presented by the institution. Consequently, the application of the risk-based approach to the establishment of colleges may lead to a breach of Union law. In the AML/CFT experts' view, it would be important to ensure that the establishment and maintenance of AML/CFT supervisory colleges remains proportionate to the level of ML/TF risk, in particular for lower ML/TF risk financial institutions, and to the significance of the cross-border activity, so that supervisors can agree to deprioritise the establishment or adjust the operation of existing lower risk AML/CFT supervisory colleges, including the frequency of meetings, on a risk-sensitive basis without breaching EU law.
- c) applicability of AML/CFT colleges framework. AML/CFT experts are concerned that the proposal appears to create an expectation that EU supervisors influence the setting up of AML/CFT supervisory colleges by their counterparts in third countries¹⁹ and that they could be held responsible for failing to do so successfully. In the experts' view, the setting up of AML/CFT supervisory colleges by non-EU authorities should flow from relevant FATF standards and not be set out in EU law.
- d) exemption of selected obliged entities from the AML/CFT supervisory colleges framework. The draft AMLAR²⁰ appears to suggest that no college is required to be set up for selected obliged entities that will be supervised by the AMLA, unless they have establishments in at least two third countries²¹, whereas the draft AMLD6²² reflects the current AML/CFT supervisory colleges framework and requires the establishment of AML/CFT supervisory colleges for all credit and financial institutions that meet the criteria under the draft AMLD6. This means that by the time the AMLA will assume direct supervision, AML/CFT supervisory colleges will already be set up also for all selected obliged entities and, from the draft legal text, it is not clear whether these colleges should be disbanded or paused. AML/CFT experts are concerned that disbanding of these AML/CFT supervisory colleges may create a significant resource burden for financial supervisors, as colleges would need to be re-established once the AMLA is no longer responsible for direct AML/CFT supervision of these institutions.
- e) the AMLA's oversight role of AML/CFT supervisory colleges. AML/CFT experts note that the AMLA does not have mediation powers, similar to the powers that the EBA has in accordance with the ESAs' AML/CFT Colleges Guidelines. Article 5(3)(g) of the draft AMLAR is limited only to *'disagreements on the measures to be taken in relation to an obliged*

¹⁸ Article 36(1) of the draft AMLD6

¹⁹ Article 36(3) of the draft AMLD6

²⁰ Article 29 of the draft AMLAR

²¹ Article 5.2.c of the draft AMLAR and 36.3 of the draft AMLD6

²² Article 36 of the draft AMLD6

entity’ and does not address other types of disagreements that may arise in supervisory colleges, including which observers should be invited to the college. In the absence of such provisions, it is not clear how conflicts between supervisors relating to colleges will be resolved.

- **Cooperation with supervisory authorities in third countries**

11. Article 37(1) of the AMLD6 governs the cooperation between the EU’s financial supervisors and their counterparts in third countries. AML/CFT experts note that Member States have discretion in respect of the cooperation agreements that could be put in place as the current wording stipulates that *‘Member States may authorise financial supervisors to conclude cooperation agreements [...]’*. The experts are unsure about the extent of the Member States’ discretion and whether they can choose *‘not to authorise’*, which would lead to divergent approaches between the Member States and potentially, hamper effective AML/CFT supervision.

12. One of the conditions that allows the conclusion of the cooperation agreement with a third country authority is the guarantee that professional secrecy and confidentiality requirements applicable to those authorities are equivalent to the standards applicable in the EU. The responsibility for assessing the equivalence rests with financial supervisors with *‘the AMLA lending such assistance as may be necessary’*²³. AML/CFT experts are unsure about the meaning of the provisions *‘may lend such assistance’* and about the AMLA’s overall role in this process. In the experts’ view, it would be useful to draw on a similar process in the prudential area where the assessment of equivalence is carried out by the EBA²⁴ and the outcomes of it are shared with relevant EU competent authorities. Such an approach ensures consistent outcomes from these assessments and avoids duplication of efforts by multiple supervisors assessing the same third country authority.

13. Finally, the experts note that the requirement for EU financial supervisors to conclude a cooperation agreement with authorities in third countries to exchange information²⁵ means that the attendance of those third countries’ supervisors in AML/CFT colleges will be subject to signing the cooperation agreement in accordance with Article 37(1) of the draft AMLD6. In the experts’ experience, negotiations of terms of such an agreement can be complex and may take time. This means that, in the absence of specific provisions relating to colleges, there is a risk that third country supervisors might not be able to attend AML/CFT supervisory colleges or that their attendance may be delayed significantly, which would have a detrimental effect on cooperation and robust AML/CFT supervision.

- **Cooperation with prudential supervisors**

14. Over the past six years, the ESAs have worked to put in place a holistic approach to tackling ML/TF risk across all areas of supervision and across all aspects of an institutions’ operations. This holistic approach is in line with the FATF’s standards and draws on the synergies that exist between the

²³ Article 37 of the draft AMLD6

²⁴ Article 33(2) of the Regulation (EU) No 1093/2010

²⁵ Article 37(1) of the draft AMLD6

different supervisory frameworks. It is important that the new AML/CFT framework recognises these synergies and safeguards the holistic approach. In this context, AML/CFT experts note that:

- a) Supervisory cooperation provisions in Article 48 of the draft AMLD6 are limited to interactions between the AML/CFT supervisors and prudential supervisors of credit institutions. There appears to be no cooperation foreseen between financial and non-financial supervisors and prudential supervisors responsible for other sectors, such as payment institutions, investment funds or life insurance. AML/CFT experts' experience shows that the absence of an explicit requirement on behalf of different supervisors to cooperate hampers cooperation and information exchange and may even be perceived as a legal obstacle to cooperation. As a result, the objective of improved supervision of obliged entities may not be met.
- b) Article 47 of the draft AMLD6 and Article 14 of the draft AMLAR impose obligations on supervisory authorities and FIUs to cooperate with the AMLA and provide information to it. There seems to be no similar obligation imposed on the AMLA to cooperate with other competent authorities and prudential supervisors, including the European Central Bank, which is necessary in situations where, for example, the AMLA has identified breaches or areas of increased ML/TF risks, which may have an impact on prudential supervision or the overall risk profile of institutions. This may lead to supervisors operating in silos with important ML/TF risks being missed or not being acted upon and raises questions about the AMLA's ability to fulfil some of its powers, which have an impact on prudential supervision, like the proposal of withdrawal of licence²⁶.

Proposal 1:

15. The co-legislators and the European Commission may wish to clarify and make further adjustments to the AML/CFT package in relation to:

- a) the roles, responsibilities and powers of home and host Member States' supervisors in respect of institutions that operate in other Member States via ROE and FOS to ensure adequate and effective supervisory coverage of all obliged entities. In particular, the powers to impose supervisory measures and sanctions should be consistent with the clearer delineation of the powers to supervise between the home and host supervisors;
- b) the cooperation mechanisms to ensure effective cooperation between the AMLA and other AML/CFT supervisors, non-AML supervisors and other prudential supervisors to ensure that they do not operate in silos and to ensure that the cooperation standards set out in the proposed AML/CFT legislative package are not lower than the standards currently enforced through the various ESAs guidelines and the multilateral cooperation agreement between the ECB and AML/CFT supervisors;

²⁶ Article 20(2)(i) of the draft AMLAR

- c) the framework for AML/CFT supervisory colleges to ensure that it is closely aligned with the framework established under the ESAs AML/CFT Colleges guidelines, while ensuring that the risk-based approach and proportionality principles are embedded in the framework;
- d) the process for cooperation between financial supervisors in the EU and their counterparts in third countries to ensure that it is streamlined and consistently applied in the EU by:
 - i. confirming the extent of Member States' discretion allowing or refusing such cooperation;
 - ii. clarifying the AMLA's role in fostering cooperation with authorities in third countries and, the possibility for the AMLA to assess the equivalence of the confidentiality and professional secrecy provisions applicable to those authorities with those applicable in the EU;
 - iii. ensuring the timely participation of third countries authorities in AML/CFT colleges, for example, by allowing the equivalent supervisors to participate where they have agreed to abide by the rule of the AML/CFT college;
 - iv. ensuring, on behalf of financial supervisors, the timely conclusion of the cooperation agreement in accordance with Article 37 of the AMLD6 by, for example, mandating the AMLA with the development of a template for this agreement.

B. Cooperation for the purposes of regulatory standard-setting

16. AML/CFT experts support the Commission's objective that the AMLA be a strong and independent body with competencies in AML/CFT, at the centre of the AML/CFT framework in the EU. Section 7 of Chapter 2 of the draft AMLAR empowers the AMLA to develop legal instruments such as RTS, ITS, guidelines, recommendations and opinions for obliged entities and supervisors. AML/CFT experts note that:

- a) limited consultation and cooperation is envisaged between the AMLA and experts from competent authorities and other EU bodies, such as the ESAs or the ECB, when developing these legal instruments. Under the current proposals, the AMLA is required to liaise with the ESAs on two occasions only, in respect of guidelines under Article 48(6) and under Article 52 of the draft AMLD6. The proposal does not set out how, at what stages and to what extent the ESAs would be involved in this process, or what would happen should the views of the AMLA and the ESAs diverge. The proposal does not envisage either that regulatory instruments would be developed jointly by the AMLA and the ESAs.
- b) there are many synergies between the requirements in the proposed AML/CFT package and different sectoral legislation. AML/CFT experts note that the EBA's current guidelines,

including for example core AML/CFT guidelines like the Risk Based Supervision Guidelines²⁷ and the Risk Factors Guidelines²⁸, contain numerous cross-references to guidelines and standards developed under sectoral legislation and vice versa. In the absence of a duty to cooperate between the AMLA and the ESAs, some of these synergies may be missed, or result in different or potentially contradicting standards being imposed on obliged entities in respect of the same issue. Examples include:

- i. proposed AMLA guidelines on obliged entities' internal policies, controls and procedures²⁹, which appear to touch on similar issues as those addressed by the EBA's Guidelines on internal governance under Directive 2013/36/EU³⁰. The current proposal does not envisage that the AMLA should cooperate or consult the EBA to ensure a consistent approach.
 - ii. the AMLR requirements on credit and financial institutions in respect of compliance functions³¹ and outsourcing³², which overlap with similar requirements applicable to them under sectoral legislation and are further elaborated in the EBA's Guidelines on the internal governance under Directive 2013/36/EU³³, EBA and ESMA's joint Guidelines on fitness and propriety³⁴ and the EBA's Guidelines on outsourcing arrangements³⁵. The AMLR makes no references to these provisions.
 - iii. the EBA is mandated by sectoral legislation to develop draft RTS³⁶ to further specify the mechanisms for cooperation and information exchange between competent authorities, FIUs and AML/CFT authorities that supervise third country branches in the context of identifying serious breaches of AML/CFT rules. There does not appear to be a similar mandate in respect of third country branches given to the AMLA in the new AML/CFT legislative package.
- c) AML/CFT and wider supervisory objectives may not always be aligned. For this reason, the ESAs, which together are responsible for setting regulatory standards across all areas of financial services supervision, have worked to ensure that any regulatory products developed by them benefit from the input of prudential, conduct and AML/CFT supervisors

²⁷ EBA's Guidelines (EBA/GL/2021/16) on the characteristics of a risk-based approach to anti-money laundering and terrorist financing supervision, and the steps to be taken when conducting supervision on a risk-sensitive basis under Article 48(10) of Directive (EU) 2015/849 (amending the Joint Guidelines ESAs 2016 72)

²⁸ EBA Guidelines (EBA/GL/2021/02) on customer due diligence and the factors credit and financial institutions should consider when assessing the money laundering and terrorist financing risk associated with individual business relationships and occasional transactions ('The ML/TF Risk Factors Guidelines') under Articles 17 and 18(4) of Directive (EU) 2015/849

²⁹ Article 7(4) of the draft AMLR

³⁰ EBA Guidelines (EBA/GL/2017/11) on internal governance under Directive 2013/36/EU

³¹ Article 9 of the draft AMLR

³² Article 40 of the draft AMLR

³³ EBA's Guidelines (EBA/GL/2017/11) on internal governance under Directive 2013/36/EU

³⁴ Joint ESMA and EBA Guidelines (EBA/GL/2017/12) on the assessment of the suitability of members of the management body and key function holders under Directive 2013/36/EU and Directive 2014/65/EU

³⁵ EBA's Guidelines (EBA/GL/2019/02) on outsourcing arrangements

³⁶ Article 48o (6b) of the Proposal for a Directive of the European Parliament and of the Council amending Directive 2013/36/EU as regards supervisory powers, sanctions, third country branches, and environmental, social and governance risks, and amending Directive 2014/59/EU (CRD VI)

to foster a joined-up and consistent approach, and the development of standards that can be implemented effectively. Going forward, the responsibility for developing AML/CFT standards will transfer from the EBA to the AMLA, thereby introducing an institutional split between AML/CFT and prudential or conduct standard-setters. In the absence of adequate arrangements that govern cooperation between the AMLA and the ESAs, including a mechanism for the resolution of potential conflicts, there is a risk of divergent approaches developing between different EU regulators going forward. This may hamper the effectiveness of prudential, conduct and AML/CFT supervisory approaches.

Proposal 2:

17. The co-legislators and the European Commission may wish to consider whether current provisions in the draft legal texts of the AML/CFT package are adequate to ensure consistent approaches to setting EU-wide AML/CFT standards in accordance with sectoral financial services legislation. Specifically:

- a) in the area of financial regulation, whether provisions are sufficient to ensure that the AMLA and the ESAs cooperate closely throughout their respective rule-making processes to ensure that, where synergies between the regulatory products delivered by the AMLA and those delivered by the ESAs exist, they are identified and addressed in good time. This could be achieved, for example, by:
 - i. amending Article 46(2) of the AMLAR to include the ESAs as a permanent non-voting member on the General Board of the AMLA, similar to the AMLA's role on the ESA's Board of Supervisors³⁷, with regard to topics that relate to credit and financial institutions that are subject to EU law within their remit.
 - ii. considering whether provisions similar to those set out in Article 9a(9) of the EBA's Regulation³⁸ should be included in the draft AMLAR in relation to the AMLA so that the ESAs have the right to be heard on issues that relate to their respective areas of competence by having an opportunity to submit written observations on any draft decision regarding regulatory products and issues that relate to obliged entities within their remit and at the same time requiring the AMLA to duly consider such observations before taking its final decision.
- b) in those areas where the ESAs have already issued guidelines addressed to financial supervisors, and such areas will fall under the AMLA's competence after the adoption of the AML/CFT draft proposal, ensure the continuation of these guidelines until they are replaced by the same or by similar instruments developed by the AMLA, according to AMLAR.

³⁷ Article 89(8), Article 90(2) and Article 91(2) of the draft AMLAR

³⁸ Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC

C. Ensuring the clear and consistent use of key terms

18. AML/CFT experts welcome the inclusion of definitions in the draft AMLR and AMLAR, which, in their view, will contribute towards the implementation of a more consistent approach to AML/CFT across all Member States. In AML/CFT experts' view, some definitions may benefit from further fine-tuning to guard against legal uncertainty and to foster common understanding of relevant terms in all EU Member States.

19. In the AML/CFT experts' view, areas where definition would benefit from further clarity include terms which are:

- a) defined in the draft AMLD6 but that could be defined in directly applicable Union law instead, as maintaining these definitions in the AMLD6 may lead to divergent approaches during the transposition process. This could hamper the effective implementation of the new AML/CFT framework.
- b) related to the same topic but defined in different legislative acts. For example, there are important synergies between the term '*financial supervisor*' in AMLD6 and other references to supervisors, such as the term '*non-financial supervisor*' in the draft AMLAR and the term '*supervisor*' in the draft AMLR. There is a risk that the use of different terms could lead to uncertainty over the role of each type of supervisor with regards to the enforcement of the new legislative package's provisions.
- c) not defined but used in key provisions in the proposed AML/CFT legislative package. AML/CFT experts are concerned that there is a risk that in the absence of clear definitions of those terms, divergent approaches and inconsistent interpretations may develop. For example, the draft AMLD6 includes references to '*immediate remedies*', '*serious failings*' and '*appropriate and proportionate measures*'³⁹ in the context of host supervisors' powers, but it does not define or explain these terms. AML/CFT experts note that some terms could be defined in the RTS⁴⁰ but consider that including a definition of those terms in the Level 1 text would be important to ensure a consistent approach from the start, bearing in mind also the time the AMLA will need to develop the RTS.
- d) defined in the draft AMLR in a high-level way that, in the experts' view, may not be conducive to a common understanding of the same terms. For example:
 - i. the definition of '*financial institution*'⁴¹ includes a cross-reference to the activities set out in Annex I of Directive 2013/36/EU⁴², as in the AML/CFT legal framework currently

³⁹ Article 33(4) of the draft AMLD6

⁴⁰ Article 39(7) of the draft AMLD6

⁴¹ Article 2(6)(a) of the draft AMLR

⁴² Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC

in force⁴³. AML/CFT experts' experience suggests that the scope and meaning of some of these activities such as lending, financial leasing, guarantees and commitments, central securities depositories and intra-group activities is not always clear, and that greater clarity concerning these activities in sectoral legislation would be important to ensure common approach across the EU as well as a level playing field.

- ii. the term '*non-AML authority*'⁴⁴ is limited to competent authorities responsible for the prudential supervision of the banking sector. There are no similar terms that would reference non-AML authorities responsible for the prudential or conduct supervision of other financial sectors, like life insurance, payment institutions or investment funds, that are also within the scope of the AML/CFT framework, but that do have a role to play to ensure a holistic and effective approach to tackling ML/TF risk through supervision.
- iii. the definition of the term '*competent authority*'⁴⁵ entails a range of public bodies and not just financial services supervisors, as is the case in other EU legal acts⁴⁶. Given the inter-connectedness between EU legislation in the financial services context and the ongoing role of prudential and other supervisors in the fight against financial crime, the inclusion of other public bodies in the definition of this term leads to uncertainty.

20. AML/CFT experts also note that the proposed approach to setting regulatory expectations for obliged entities is not always consistent. For example:

- a) the current AMLR proposal is explicit on the type of internal policies, controls and procedures⁴⁷ obliged entities are required to put in place. At the same time, the proposal does not refer to policies, controls and procedures in respect of politically exposed persons (PEPs) and suspicious transactions reporting (STRs).
- b) the current AMLR proposal envisages that the AMLA will set regulatory expectations on internal policies, controls and procedures through guidelines⁴⁸, which are non-binding legal instruments, whereas specific provisions in respect of 'group-wide policies', which is a subset of overall policies and procedures and form part of an obliged entity's internal controls framework, will be set out in Regulatory Technical Standards⁴⁹ which are legally binding instruments. As a result, the implementation of these provisions might be challenging for obliged entities and difficult for AML/CFT supervisors to enforce.

⁴³ 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

⁴⁴ Article 2(5) of the draft AMLR

⁴⁵ Article 2(31) of the draft AMLR

⁴⁶ Art 4(1)(40) of Regulation 575/2013 and Article 4(2) of Regulation (EU) 1093/2010

⁴⁷ Article 7(2) of the draft AMLR

⁴⁸ Article 7(4) of the draft AMLR

⁴⁹ Article 13(3) of the draft AMLR

- c) some obligations appear to be embedded in legally non-binding recitals instead of the binding legal text. This is the case, for example, for certain intra-group transactions, which, in accordance with recitals⁵⁰, are exempt from the application of AML/CFT measures. AML/CFT experts note that there is no legal basis for such exemption in the legally binding text of the draft AMLR. In the absence of an explicit legal basis, the expectations set out in the recitals cannot be applied.

Proposal 3:

21. The co-legislators and the European Commission may wish to consider during the negotiations whether:

- a) the definitions of terms set out in the draft AMLAR, AMLR and AMLD6 are used consistently throughout the legislative proposals and are sufficiently clear and unequivocal, particularly where they cross-refer to sectoral legislation, in order to ensure the effective application of the AML/CFT package's provisions, once adopted;
- b) any rights, obligations and exemptions applicable to obliged entities are set out consistently and sufficiently clearly in the enacting text of the legislative proposals. In particular, it would be helpful if the Commission and co-legislators would:
 - i. include an explicit reference in Article 7(2) of the draft AMLAR to internal policies, controls and procedures related to PEPs and STRs; and
 - ii. clarify in the legally binding text in the AMLR, which intra-group transactions would be eligible for the exemption from AML/CFT rules and how the exemption should be applied, either on a risk-sensitive basis or in circumstances where AML/CFT preventative measures in intra-group scenario are considered ineffective or inadequate.

Proposals for amended selection criteria under Articles 12 and 13 of the draft AMLAR

22. Articles 12 and 13 of the draft AMLAR set out the criteria that determine which credit and financial institutions ('institutions') that operate on a cross-border basis will be directly supervised by the AMLA. The supervisory powers in respect of those institutions will transfer from national competent authorities ('NCAs') to the AMLA.

23. Article 12 of the draft AMLAR sets out the criteria that determine which institutions are eligible to be considered for direct supervision by the AMLA ('eligibility criteria') and Article 13 provides additional criteria that determine which institutions are selected in accordance with Article 12 to qualify for direct supervision ('qualifying criteria'). The eligibility criteria are largely quantitative and

⁵⁰ Recital 8 of the draft AMLR

focus on the extent of the institutions' operations across the EU. The qualifying criteria include both quantitative and qualitative factors, including the institutions' risk exposure. Through these criteria, the Commission's proposal aims to ensure that institutions with the greatest cross-border activities and which are exposed to the highest ML/TF risks will be supervised by the AMLA. It also envisages that in those cases, the supervision by the AMLA will add value and strengthen the EU's AML/CFT defences.

24. AML/CFT experts support the Commission's objectives. To ensure that these objectives can be fulfilled, and drawing on the EBA's work in AML/CFT supervisory colleges⁵¹, the EBA's Opinion on ML/TF risks⁵², the EBA's staff-led implementation reviews of national competent authorities' approaches to AML/CFT supervision as well as information obtained in the context of the EBA's wider work to lead, coordinate and monitor the EU financial sector's AML/CFT efforts, the AML/CFT experts suggest that the Commission and the co-legislators consider the following points during their negotiations of the draft legislative proposals:

- the extent to which the selection criteria for credit and financial institutions, as well as for different types of groups, are adequate to ensure that those cross-border institutions and groups that, due to the nature of their business expose the internal market to the most significant ML/TF risk, are supervised by the AMLA, regardless of their size;
- whether the eligibility criteria should be extended to those entities that due to the nature of their business may expose the internal market to significant ML/TF risks but are currently excluded from direct supervision by the AMLA, like Crypto Asset Service Providers (CASPS);
- whether to align the competent authorities' obligations in respect of risk profiling of obliged entities and the supporting methodology in accordance with Articles 31(1)(c) and 31(2) of the draft AMLD6 with similar obligations set out in Articles 12(2) and 12(5) of the draft AMLAR for the purposes of direct supervision to avoid duplication of efforts by competent authorities, including the AMLA, and potentially inconsistent outcomes;
- how to ensure sufficient transparency and consistency when selecting institutions for direct supervision and when transferring supervisory powers in respect of those institutions between NCAs and the AMLA.

D. General observations on the selection criteria for groups

25. With the establishment of the AMLA, the Commission aims to mitigate the heightened ML/TF risks associated with cross-border operations of some groups by introducing a more harmonised and effective EU-level AML/CFT supervisory framework. To that end, the AML/CFT experts note that the current proposal in Article 12 of the draft AMLAR refers to individual institutions, rather than to

⁵¹ For more information on AML/CFT supervisory colleges, refer to the factsheet on 'AML/CFT Supervisory Colleges' and the factsheet on 'the EBA's approach to monitoring the functioning of AML/CFT colleges' published by the EBA in December 2021, available here: <https://www.eba.europa.eu/news-press/communication-materials>

⁵² Opinion on ML/TF risks is published by the EBA in accordance with Article 6(5) of Directive (EU) 2015/849 every 2 years.

'groups' as defined in Article 2(29) of the draft AML Regulation. This means that the scope of Article 12 is limited to those groups where the parent undertaking or head office entity is a credit institution or a financial institution. As a result, other types of groups, which have credit or financial institutions within their group structure, but where these credit or financial institutions are not the consolidating entities, will not be eligible for direct supervision by the AMLA.

26. In the AML/CFT experts' experience, such groups include those where:

- a) the parent undertaking or head office entity is not a credit or financial institution as defined in Articles 2(5) and 2(6) of draft AML Regulation. This means that, although such groups might provide financial services across the EU through credit or financial institutions that are part of this group, they would not be eligible for direct supervision by the AMLA.
- b) the parent undertaking or head office entity is based in a third country, without having any consolidating entity within the EU. This means that the EU branches and subsidiaries of such groups do not meet the eligibility criteria set out in Article 12(1) of the draft AMLAR, which requires that the group should be headquartered in the EU, regardless of the level of ML/TF risk to which this group may expose the EU's financial sector. Since, in those cases, there is no single national group-level or consolidating supervisor who would have a group-wide view of the ML/TF risks, the experts consider that EU-level supervision by the AMLA would bring a specific added value to the AML/CFT supervision of these groups.
- c) mixed activity groups. The current text in Articles 12(1) and 13(1) appears to consider only those groups that operate in the same sector and it is not clear from the draft legal text how the fulfilment of the selection criteria will be determined in situations where the group is made up of both credit and financial institutions or a group that operates in financial and non-financial sectors. For example, the current draft AMLAR does not specify whether the selection criteria set out in point a) or point b) of Article 12(1) should be applied if a group is made up of both credit institutions that operate in less than seven Member States and other financial institutions like investment firms, payment institutions and life insurance undertakings.

27. AML/CFT experts note that groups described in points a) to c) above are currently operating in the EU. Some of these groups present a high level of ML/TF risk due to the nature of their business and the extent of their operations in the EU. In the AML/CFT experts' view, it would be important that these groups be eligible for direct supervision by the AMLA.

Proposal 4:

28. AML/CFT experts suggest that the co-legislators and the European Commission may wish to consider expanding and clarifying the criteria in Articles 12(1) and 13(1) of the draft AMLAR to ensure that:

- a) different types of groups, which comprise credit and financial institutions, can be considered for direct supervision by the AMLA, including those where credit or financial institutions
- i. are part of a wider group, in which the head office /parent entity is not a credit or financial institution;
 - ii. are established in the EU as a branch or subsidiary but are part of a wider group, which is headquartered in a 3rd country;
 - iii. are part of a wider group, which consist of both credit and financial institutions and may also entail non-financial institutions.
- b) for the purposes of Article 13(1), the ML/TF risk associated with 3rd country groups' operations in the EU, is adequately addressed. This may require for the threshold in terms of the number of Member States in which the group operates in the EU to be set lower than the seven Member State criterion applied to other groups. Alternatively, co-legislators and the European Commission may wish to consider adopting a similar approach to that applicable to the 3rd country groups in the context of AML/CFT colleges as prescribed in the ESAs AML/CFT Colleges Guidelines⁵³. This would mean that those groups, which operate in three or more Member States, would be eligible for direct supervision but would qualify only on the basis of their ML/TF risk profile.

E. Selection criteria for credit and financial institutions

29. In Articles 12(1) and 13(1), the draft AMLAR sets out criteria that the AMLA should consider when selecting credit and financial institutions that will be directly supervised by it. The criteria focus on the extent of the institutions' operations across the EU and set specific requirements in terms of the number of Member States in which the institution's inherent ML/TF risk profile must be rated as high. The draft AMLAR requires that an additional aspect relating to material breaches previously identified by supervisors in the institutions' AML/CFT systems and controls framework is also considered when determining whether a credit institution is to be directly supervised by the AMLA. The AML/CFT experts note that the selection criteria for credit institutions are different from those applicable to financial institutions, which might not be justified by the level of ML/TF risks presented by them.

- Eligibility selection criteria pursuant to Article 12(1) of the draft AMLAR

30. The eligibility criteria set out in Article 12(1) of the draft AMLAR prescribe the number of Member States in which credit or financial institutions should operate with or without an establishment to be considered for direct supervision. The criteria differ significantly depending on whether the

⁵³ ESAs joint guidelines (JC 2019 81) on cooperation and information exchange for the purpose of Directive (EU) 2015/849 between competent authorities supervising credit and financial institutions

obliged entity is a credit or financial institution, in terms of the extent of the cross-border operations and also in the way how cross-border services are provided by these institutions.

31. In respect of **credit institutions**, Article 12(1)(a) of the draft AMLAR determines that the AMLA should consider for direct supervision those institutions that are *'established in at least seven Member States, including the Member State of establishment and the Member States where they are operating via subsidiaries or branches'*.
32. In this regard, AML/CFT experts' insights gained as part of AML/CFT colleges suggest that the application of this criterion may inadvertently lead to the exclusion of certain high-risk credit institutions from being eligible for direct EU-level AML/CFT supervision in spite of their significant operations in a large number of EU Member States or their strategic importance in some Member States or certain geographic regions. This is because this criterion does not take into account that the provision of products and services may carry significant ML/TF risks even in circumstances where the credit institution in question does not have an establishment as defined in Article 12(1)(a) of the draft AMLAR.
33. Some examples of credit institutions that will not be eligible for direct supervision under the current proposals include credit institutions which have branches and subsidiaries in six or less Member States, but which operate in other Member States through the free provision of services without an establishment. This means that most digital-based institutions, such as digital-only institutions or challenger banks, which, as highlighted in the EBA's 'Report on the impact of FinTech on incumbent credit institutions', predominantly focus on the mobile application experience and have no physical branches⁵⁴, would be excluded from the AMLA's selection process, irrespective of the number of Member States in which they provide their services or the magnitude of their EU operations. The criteria also exclude those incumbent or traditional credit institutions which are undergoing digital transformation and, as a result, are reducing their network of branches and providing more services online⁵⁵, however the nature of their activities or their geographical reach and exposure to ML/TF risks don't change. In the AML/CFT experts' experience, all these institutions may be exposed to high ML/TF risks and, therefore, the determination of their ineligibility based only on the lack of physical presence, in the experts' view, cannot be justified.
34. The cross-border criterion, as currently laid down in Article 12(1), may present certain ambiguity in terms of the extent of cross-border activities. The experts note that some institutions, which have expressed their intention to operate across borders in certain Member States, but do not operate in some of those Member States yet, may be considered as eligible for direct supervision, if the decision is based merely on their passporting notification, without considering the institutions' actual activities. Similarly, there may be cases of institutions considered eligible even though their cross-border activities are limited.

⁵⁴ EBA's report on the impact of FinTech on incumbent credit institutions' business models, published 03 July 2018, available: <https://www.eba.europa.eu/eba-assesses-risks-and-opportunities-from-fintech-and-its-impact-on-incumbents-business-models>

⁵⁵ EBA's report on the impact of FinTech on incumbent credit institutions' business models, published 03 July 2018, available: <https://www.eba.europa.eu/eba-assesses-risks-and-opportunities-from-fintech-and-its-impact-on-incumbents-business-models>

35. Nevertheless, should the eligibility criteria remain as currently drafted, the information currently available to AML/CFT experts from AML/CFT colleges suggests that directly supervised institutions may be concentrated only in half of the EU Member States. This is because credit institutions in some parts of Europe do not meet the seven Member State threshold, even if they are credit institutions with substantial cross-border operations in those regions, and which are exposed to the highest levels of ML/TF risks due to their customer base, distribution channels, products and services offered by them or their cross-border activities in these geographical areas. For example, the AML/CFT experts' observations from a number of AML/CFT colleges show that some of the colleges are established in respect of credit institutions, which, despite being the most significant credit institutions with the highest ML/TF risk profile in certain geographical areas, they do not meet the seven Member State criterion and therefore are not eligible in accordance with Article 12(1). In some instances, the risk exposure of these institutions is increased due to their operations or other links with third countries, including high-risk ML/TF jurisdictions. If those institutions remain ineligible for direct supervision, AML/CFT experts are concerned that many institutions exposed to high ML/TF risks in a number of Member States or regions will not be directly supervised by the AMLA.
36. Article 12(1)(b) of the draft AMLAR sets out the eligibility criteria for **financial institutions**. To be considered eligible, financial institutions must *'operate in at least ten Member States, including the Member State of establishment, another Member State where they are operating via a subsidiary or a branch, and all other Member States where they are operating by means of direct provision of services or via a network of representative agents'*.
37. As is the case for credit institutions, AML/CFT experts are concerned that some financial institutions, which are exposed to high levels of ML/TF risks, but do not meet the threshold of ten Member States, are automatically ineligible for direct supervision by the AMLA, regardless of any other ML/TF risk increasing factors, which may be present. Also, Article 12(1)(b), as currently drafted, may be interpreted as if all financial institutions operate in other Member States through establishments and free provision of services or via agents.
38. AML/CFT experts question why financial institutions are subjected to different eligibility criteria than credit institutions. Notably, based on the current draft of Articles 12(1)(a) and 12(1)(b), it appears that if there was a situation where a credit institution and a financial institution both operated through a branch in one Member State and through free provision of services in another eight Member States, then only the financial institution would be eligible for direct supervision by the AMLA. This is because the free provision of services is not considered as part of the eligibility selection criteria for credit institutions. It is not clear to AML/CFT experts why the ML/TF risk associated with the free provision of services should be approached differently if the institution is a credit institution or financial institution as they have seen no evidence in their work to support such differing approach.
39. Finally, AML/CFT experts note that key terms used in Article 12(1)(b), such as term *'direct provision of services'* or *'a network of representative agents'*, are not currently defined. In the absence of a definition, there is a risk that these terms may be interpreted inconsistently.

- **Qualifying selection criteria pursuant to Art. 13(1) draft AMLAR**

40. The draft AMLAR envisages that the scope of eligible institutions be further narrowed down based on the number of Member States in which their inherent ML/TF risk profile has been assessed as high. As is the case for eligibility criteria, the qualifying criteria differ significantly depending on whether the obliged entity is a credit or financial institution.
41. In relation to **credit institutions**, Article 13(1)(a) determines that only those credit institutions that *'are assessed pursuant to Article 12 and have a high inherent risk profile in at least four Member States'* qualify for direct supervision by the AMLA.
42. AML/CFT experts welcome the risk-sensitive approach adopted by the Commission in Article 13(1)(a) but question the adequacy of the four Member State threshold set by this criterion. From the AML/CFT experts' observations in AML/CFT colleges, it is evident that in some of the largest banking groups in the EU, ML/TF risk is often concentrated in the Member State in which these groups are headquartered. Contrariwise, often branches may be exposed to lower levels of ML/TF risk because customers and transactions are booked through the head office or parent entity. For example, in one AML/CFT college for a credit institution that operates in 12 different Member States, the institution has a high ML/TF risk profile only in one Member State. Another AML/CFT college covers a credit institution that operates in 15 Member States, but it has a high-risk profile only in three of those Member States, including the one where it is headquartered. In addition, different branches and subsidiaries may present different levels of ML/TF risk in one Member State and it is not clear from Article 13 whether an average or the highest risk level would be considered for the purposes of this criterion. Therefore, in the experts' view, the four Member State threshold should be replaced with the requirement to have a group-level ML/TF risk profile, which, for the purposes of this qualifying selection criterion, should be determined by the AMLA as explained in Proposal 7 below.
43. In relation to **financial institutions**, Article 13(1)(b) determines that only those financial institutions will qualify for direct supervision that are *'assessed pursuant to Article 12 and have a high inherent risk profile in at least one Member State where it is established or operates via a subsidiary or a branch, and at least five other Member States where it operates via direct provision of services or via a network of representative agents'*.
44. AML/CFT experts note that the qualifying criteria for financial institutions appear to be significantly different from those for credit institutions. Based on AML/CFT experts' experience, the ML/TF risks associated with some financial institutions are often the same as, or even higher than, those associated with credit institutions. Therefore, the experts consider that the qualifying selection criteria for financial institutions should be aligned with those for credit institutions and the final determination should, similarly to credit institutions, be based on the level of ML/TF risk to which the entire group is exposed, instead of on the level of ML/TF of individual institutions.

- **The 'material breaches' selection criterion pursuant to Article 13(1)(a) of the draft AMLAR**

45. In respect of **credit institutions**, Article 13(1)(a) contains an additional criterion, which provides that only those credit institutions will qualify for the direct supervision by the AMLA that have been under *'supervisory or other public investigation for material breaches of the acts referred to in Article 1(2) in at least one of those Member States in the previous three years'*.

46. There is no similar requirement relating to material breaches applicable to financial institutions. AML/CFT experts are of the view that this criterion, if retained for credit institutions, may have unintended consequences, for the following reasons:

- a) 'Material breaches' are not defined in any of the proposed legislative acts. While the EBA's draft RTS on the AML/CFT Database⁵⁶ contains a definition of 'material weaknesses', which may include material breaches, AML/TF experts note that the draft AMLAR makes no references to this RTS, which, in any case will cease to be applicable as the underlying legal provision in Article 9a of the EBA's founding regulation⁵⁷ would be repealed⁵⁸. The AML/CFT experts also note that the proposed Directive⁵⁹ (AMLD6) in Article 39(7) mandates the AMLA to develop a draft RTS⁶⁰ on breaches, however, it is not clear from the current draft whether the mandate in Article 39(7) extends to a definition of the materiality of breaches. Also, the timing of this RTS does not appear to be aligned with the first round when obliged entities would be selected by the AMLA and the AML/CFT experts experience shows that it may take a number of years until the RTS are drafted, negotiated and published by a European agency, adopted by the European Commission and thereafter applied and enforced by NCAs. Therefore, it is possible that a reliable and comparable basis for this criterion will only exist around ten years from when the AMLA takes up its functions. As a result, in the absence of a clear definition and approach, AML/CFT experts share the views reflected in the EBA's response to the Commission's Call for Advice on the future legal AML/CFT framework⁶¹, which suggests that a consistent application and interpretation of this criterion by the AMLA or NCAs will be difficult to enforce.
- b) 'Material breaches' are not a reliable indicator of the current effectiveness of AML/CFT systems and controls in place at an institution. Similarly, the absence of supervisory measures is not necessarily an indicator of effective controls within the institution. Instead, it may be the result of inaction by NCAs, who might not have carried out any recent

⁵⁶ European Banking Authority's draft regulatory technical standards (EBA/RTS/2021/16) under Article 9a (1) and (3) of Regulation (EU) No 1093/2010 setting up an AML/CFT central database and specifying the materiality of weaknesses, the type of information collected, the practical implementation of the information collection and the analysis and dissemination of the information contained therein; published 20 December 2021

⁵⁷ Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC

⁵⁸ Article 89(4) of the draft AMLAR

⁵⁹ Proposal for a Directive (2021/0250) of the European Parliament and of the Council on the mechanisms to be put in place by the Member States for the prevention of the use of the financial system for the purposes of money laundering or terrorist financing and repealing Directive (EU) 2015/ 849

⁶⁰ Article 39(7) of the AMLD6 provides that 'by [2 years after the date of entry into force of this Directive], AMLA shall develop draft regulatory technical standards [...] that shall define indicators to classify the level of gravity of breaches and criteria to be taken into account when setting the level of administrative sanctions or taking administrative measures pursuant to this Section.'

inspections in the institution or might have failed to identify breaches, for example because the inspection focused on different aspects of the institution's AML/CFT compliance. This means that there is a risk that this criterion will lead to the selection of institutions with a history of compliance failures that have since been addressed instead of institutions with material AML/CFT systems and controls weaknesses that have not yet been addressed or identified. This might not be the most effective use of the AMLA's resources.

- c) If applied, this criterion would result in frequent changes to the list of directly supervised credit institutions as institutions against whom enforcement action was taken more than three years ago would be replaced by those against whom action was taken more recently. AML/CFT experts consider that such frequent changes are not desirable and may potentially be disruptive for supervisors as well as for institutions, as it makes the establishment of a robust and effective supervisory plan over time very difficult. In addition, AML/CFT experts are concerned that any changes to the list may be attributed to this criterion only and, as a result, some credit institutions appearing on the list may find themselves exposed to an increased reputational risk.
- d) Provisions relating to national AML/CFT supervision will remain in the AMLD6, which means that divergent approaches to the risk-based supervision applied by NCAs will continue to exist due to differences in the national transposition of the directive. As a result, it would be challenging for the AMLA to ensure the objective and consistent application of this criterion. This means that it is possible that not all credit institutions which should be considered by the AMLA under this criterion will be identified.

Proposal 5:

47. AML/CFT experts suggest that, in addition to the changes recommended in Proposal 7, the co-legislators and the European Commission may wish to consider what adjustments may be necessary in Article 12 and 13 of the draft AMLAR to address concerns about a potentially large number of cross-border institutions, which are exposed to high ML/TF risks in a number of Member States or regions, will not be directly supervised by the AMLA, therefore limiting the AMLA's direct exposure to ML/TF risks. As part of this, it may be useful to draw on the EBA's approach to selecting AML/CFT colleges for active monitoring⁶² because the cross-border element is also a key feature in AML/CFT colleges and therefore there are many synergies between the AML/CFT colleges framework, and the future AMLA's approach.

48. AML/CFT experts recommend that the Commission and co-legislators may wish to consider adjusting certain provisions in Articles 12 and 13 and specifically may wish to focus on:

⁶¹ EBA Report (EBA/REP/2020/25) on the future AML/CFT framework in the EU in response to the European Commission's Call for Advice on defining the scope of application and the enacting terms of a regulation to be adopted in the field of preventing money laundering and terrorist financing

⁶² For more information on AML/CFT supervisory colleges, refer to the factsheet on 'AML/CFT Supervisory Colleges' and the factsheet on 'the EBA's approach to monitoring the functioning of AML/CFT colleges' published by the EBA in December 2021, available here: <https://www.eba.europa.eu/news-press/communication-materials>

- e) aligning the selection criteria for financial institutions set out in Articles 12(1)(b) and 13(1)(b) with those for credit institutions set out in Article 12(1)(a) and 13(1)(a), including the changes suggested by the AML/CFT experts above;
- f) expanding the eligibility selection criteria set out in Article 12(1)(a) to consider also credit institutions that carry out operations on a cross-border basis in other Member States through the free provision of services, although these services should only be taken into account for the purposes of risk profiling in accordance with Article 12(2) when they have been significantly realised in practice, not just notified in the passporting notification;
- g) amending the qualifying selection criteria in Article 13(1)(a) of the draft AMLAR by removing the criterion relating to ‘material breaches’;
- h) reviewing the cross-border component of the eligibility criteria set out in Article 12(1)(a) with a view to making it possible for the AMLA to directly supervise also those credit institutions that have substantial cross-border activities and which are exposed to high ML/TF risks in a number of Member States or geographical regions, but which may not meet the seven Member State criterion;
- i) reviewing the qualifying selection criterion set out in Article 13(1)(a) to ensure that cross-border groups are selected for direct supervision based on the ML/TF risk exposure of the entire group as determined by the AMLA, instead of that of individual institutions in certain Member States, as explained in Proposal 7 below.

F. Entities excluded from direct supervision

49. In accordance with Article 12(1) and Article 13(1) of the draft AMLAR, entities that are not classified as credit institutions or financial institutions⁶³ are not eligible for direct supervision by the AMLA, regardless of the level of ML/TF risk presented by these institutions to the internal market. This means that entities such as Crypto Asset Service Providers (CASPs) will not be directly supervised by the AMLA.

50. AML/CFT experts have observed a rapid growth of this sector in recent years and consider that this sector is exposed to very high ML/TF risks based on the nature of products and services offered, which often allow anonymity, the prevalence of large volumes of cross-border transactions, and business models that are often complex and unusual. If CASPs remain excluded from direct supervision by the AMLA, the main concern is that the increased risks associated with them may not be managed effectively at the level of the EU. In the AML/CFT experts’ view, it is crucial to implement effective AML/CFT regime in this sector with the AMLA playing the leading role to ensure that the AML/CFT framework is implemented effectively.

⁶³ Credit institutions and financial institutions are defined in Article 2(5) and (6) of the proposal for a Regulation (2021/0239) of the European Parliament and of the Council on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing.

Proposal 6:

- 51.AML/CFT experts suggest that the co-legislators and the European Commission consider the possibility for expanding the eligibility selection criteria in Article 12(1) to ensure that the eligible high-risk CASPs may also be directly supervised by the AMLA and that the draft AMLAR provide the necessary legal gateways to facilitate this.
- 52.AML/CFT experts consider that CASPs should be subjected to the same eligibility and qualifying selection criteria as those set out in Articles 12 and 13 in respect of credit- and financial institutions.

G. Risk profiling of selected obliged entities

- 53.Article 13(1)(a) and (b) of the draft AMLAR refers to the risk profiling of credit and financial institutions, which would determine whether they qualify for direct supervision by the AMLA, and Article 12(2) explains how the risk profiling should be carried out by requiring that *'the inherent risk profile of the assessed obliged entities [...] shall be classified as low, medium, substantial or high in each jurisdiction they operate in, based on benchmarks and following the methodology set out in the RTS referred to in Article 12(5)'*.
- 54.The draft text is not explicit on whether the AMLA or NCAs are responsible for the risk profiling. Should the risk profiling be carried out by NCAs, in AML/CFT experts' view there is a risk that divergent approaches among NCAs may continue to exist and the outcomes of such risk profiling may not always be comparable, even if the methodology for it will be set out in the RTS, as this involves some subjective elements
- 55.To this end, AML/CFT experts consider a group-level ML/TF risk profile developed by the AMLA, instead of individual assessments by NCAs, to be a more accurate representation of the ML/TF risk to which it is exposed and a more appropriate criterion for selecting groups that qualify for direct supervision by the AMLA. In the absence of a group level ML/TF risk assessment, AML/CFT experts are concerned that the likelihood and impact of some risk factors and potentially weights assigned to them, if assessed individually by NCAs, might not provide a true reflection of the inherent ML/TF risks to which the entire group is exposed. This includes the risks arising from the groups' operations in third countries and also any potential risks presented by non-financial entities within the group, to the extent that they impact on credit and financial institutions within the group.
- 56.AML/CFT experts note that there are provisions in Article 12(4) of the draft AMLAR and also in Articles 31(1)(c) and 31(2) of the proposed AMLD6 which, in both instances, refer to the risk profiling of obliged entities and any differences or interdependencies between the two risk profiles are not apparent. Articles 31(1)(c) and 31(2) of the proposed AMLD6 require NCAs to carry out risk profiling of obliged entities, including credit and financial institutions, for the purposes of the risk-based supervision in accordance with the draft RTS setting out *'the benchmarks and a methodology for assessing and classifying the inherent and residual risk profile of obliged entities'*. AML/CFT experts are concerned that two different procedures and methodologies to carry out risk profiling of the same institutions may lead to inconsistent approaches among NCAs and may potentially

increase a burden on credit and financial institutions, which may be required to provide two sets of different information at different times to feed into the two risk profiling processes. As a result, it would have an adverse effect on the consistent interpretation and implementation by NCAs and the AMLA of the risk-based approach to AML/CFT supervision.

57. Furthermore, AML/CFT experts note that the list of risk indicators provided in Article 12(4) of the draft AMLAR, although not exhaustive, focuses mainly on indicators related to payment systems and customers. It does not include explicit references to other risk indicators, including those connected with distribution channels, products/services and geographies as described in the ESAs risk factors guidelines⁶⁴. In the AML/CFT experts' opinion, this could give rise to uncertainty and divergent interpretations of this provision.

58. Finally, regarding the timing of the risk profiling of institutions, Articles 12(2) and 12(5) of the draft AMLAR determine that the assessment should be *'based on the benchmarks and following the methodology set out in the regulatory technical standards [...], which draft shall be submitted by the AMLA to the Commission by 1 January 2025'*. Thereafter, Article 13(2) provides that the AMLA *'shall commence the first selection process on 1 July 2025'*. This means that either the AMLA or NCAs, depending on the assigned roles and responsibilities, will have only 6 months to complete the risk assessment in accordance with the new methodology, and assign the risk profile. AML/CFT experts are concerned that this timeframe might be extremely ambitious and that it might not allow sufficient time to gather the necessary data and information so that the risk profiling can be carried out effectively in accordance with the new methodology.

Proposal 7:

59. AML/CFT experts suggest that the co-legislators and the European Commission may wish to clarify in the draft AMLAR who is responsible for performing the risk profiling for the purposes of selecting eligible institutions that qualify for direct supervision in accordance with Article 13(1) and how this assessment should be carried out. In particular, they view that the co-legislators and the European Commission should consider whether to:

- a) amend Article 12(2) of the draft AMLAR to specify that the AMLA should carry out the risk profiling at a group-level for those institutions or groups, which are deemed eligible in accordance with Article 12(1). Where the institution or group is not already directly supervised, the AMLA may use information provided to it by competent authorities to carry out the risk profiling.
- b) ensure that any links and possible interdependencies between the risk profiling, including benchmarking, conducted in accordance with Article 12(2) of the draft AMLAR and that conducted in accordance with Articles 31(1)(c) and 31(2) of the draft AMLD6 are sufficiently addressed. To ensure efficiency and consistency of the risk profiling and to avoid any

⁶⁴ EBA Guidelines (EBA/GL/2021/02) on customer due diligence and the factors credit and financial institutions should consider when assessing the money laundering and terrorist financing risk associated with individual business relationships and occasional transactions ('The ML/TF Risk Factors Guidelines') under Articles 17 and 18(4) of Directive (EU) 2015/849; published 1 March 2021

duplication of tasks, it is crucial that one harmonized risk profiling methodology is developed by the AMLA in respect of the assessment of inherent and residual risks. The inherent risk assessment methodology can also be used for the selection purposes of eligible institutions in accordance with Article 13(1) of the draft AMLAR;

- c) consider whether there is a need for a list of risk indicators set out in Article 12(4) of the draft AMLAR, in particular in light of the RTS which will be developed by the AMLA in accordance with Article 12(5) of the AMLAR. As the RTS mandate also includes setting benchmarks for inherent risk, to allow defining the benchmarks in a greater detail, it may be more appropriate for the list to be incorporated in the RTS instead of the AMLAR;
- d) review the timing for the risk profiling of selected obliged entities in accordance with Article 13(2) of the draft AMLAR to allow sufficient time to gather the necessary information, which may potentially involve some system changes, and to carry out the risk profiling in accordance with the methodology set out in the RTS.

H. Methodology for applying the criteria

60. Article 13(2) of the draft AMLAR includes high-level provisions that *'the AMLA shall commence the first selection process on 1 July 2025 and shall conclude the selection within one month. The selection shall be made every 3 years...'*. AML/CFT experts note that Article 13(2) makes no reference to the methodology that the AMLA will apply to assess and evaluate the criteria set out in Article 12 and 13 of the draft AMLAR. In the absence of such methodology, it may prove to be difficult for the AMLA to ensure transparency of the selection process, which may result in outcomes of the selection process being challenged by credit and financial institutions.

Proposal 8:

61. To enhance the transparency of the selection process, AML/CFT experts recommend that the co-legislators and the European Commission may wish to consider including an explicit mandate in the draft AMLAR requiring the AMLA to develop a draft RTS where it sets out the methodology for the selection process of obliged entities for direct supervision by the AMLA. In particular, the methodology should clarify:

- a) the sequence in which each selection criterion set out in Articles 12 and 13 of the draft AMLAR will be assessed by the AMLA;
- b) whether and how any weights would be given to different selection criteria;
- c) how the criteria set out in Articles 12 and 13 will be evaluated and applied in respect of credit institutions, financial institutions, CASPS and different types of groups, including mixed activity groups; and

- d) whether there are any other relevant criteria that may be considered by the AMLA as part of the selection process, like, for example, the group's exposure to residual ML/TF risks (i.e. the level of risks after the implementation of systems and controls).

I. Transition of supervisory powers between NCAs and the AMLA

62. Article 13(2) of the draft AMLAR stipulates that *'the AMLA shall commence the direct supervision of the selected obliged entities 5 months after the publication of the list'*. Article 13(3) further explains that an institution *'shall remain subject to direct supervision by the AMLA until the AMLA commences the direct supervision of selected obliged entities based on a list established for the subsequent selection round which no longer includes that obliged entity'*.

63. AML/CFT experts note that the legislative proposal does not include any provisions on the practical modalities for the transition of direct supervisory powers between NCAs and the AMLA. For example, the legal text is not explicit on whether the AMLA will assume direct supervision of the entire group or merely those institutions within the group, which have a high ML/TF risk profile and what level of cooperation is expected between the supervisors during this process. Although Article 14 of the draft AMLAR goes some way to clarify the extent of cooperation between the AMLA and NCAs, it refers only to a one-way exchange of information, whereby NCAs are required to provide information to the AMLA, without having a corresponding requirement for the AMLA. Therefore, AML/CFT experts are concerned that the lack of any legal provisions in respect of practical modalities may lead to uncertainty, inefficiencies and disruptions to the supervisory approaches for supervisors and also for selected obliged entities, particularly for those groups that may fluctuate between the AMLA and NCAs' supervision every three years.

Proposal 9:

64. AML/CFT experts propose that the co-legislators and the European Commission consider how to ensure a smooth transition of direct supervisory powers between the AMLA and NCAs to ensure that the transition does not result in major gaps or disruptions to the supervisory approach because of the handover. In particular, the co-legislators and the European Commission should consider:

- a) explaining the process and the type of information that should be exchanged between the AMLA and NCAs at the time of the handover of direct supervisory powers. If this is to be addressed through Article 14 of the draft AMLAR, then the co-legislators and the European Commission should ensure that the proposed implementing technical standards⁶⁵ are explicit that there should be a two-way exchange of information and that equal obligations to cooperate apply to both the AMLA and NCAs. In such a case, Article 13 would merit from an explicit cross-reference to Article 14 in respect of cooperation.

⁶⁵ Article 14(4) of the draft AMLAR

- b) clarifying how the transition of powers will impact on supervisory strategies and plans and those supervisory activities or enforcement processes, which may have commenced but have not yet been finalised at the time of handover, such as clarifying
 - i. whether the transfer of supervisory responsibilities would be delayed until ongoing processes like inspections or enforcement proceedings are finalised. In the absence of a harmonised approach to administrative sanctions and measures in the EU, it is essential that the sanctioning process is carried out and completed by the competent authority that identified breaches or weaknesses in the institution's AML/CFT compliance framework to which the sanctions relate; and
 - ii. who would be responsible for the follow up on the measures taken by the institution to remedy breaches or shortcomings identified during the inspection.

- c) where the AMLA is taking over the supervision of the group in accordance with Article 13(2), amend the legal text to ensure that the AMLA would take over the AML/CFT supervision of the entire group or all credit and financial institutions within the group, if the group is involved in a mix of financial and non-financial activities, rather than supervise only those institutions within the group that are exposed to high risks of ML/TF.