



RIGA  
GRADUATE  
SCHOOL OF  
LAW

# **Risk-Based Approach in the European Anti-Money Laundering Legislation: Origins, Benefits, and Implications**

BACHELOR THESIS

AUTHOR: Jakovs Kaplans  
LL.B 2017/2018 year student  
Student number B015007

SUPERVISOR: *Dirk Linowski*  
*Prof. Dr. Dr. h.c.*

DECLARATION OF HONOUR:

I declare that this thesis is my own work, and that all references to, or quotations from, the work of others are fully and correctly cited.

(Signed) .....

RIGA, 2018

## SUMMARY

The following Thesis “Risk-Based Approach in the European Anti-Money Laundering Legislation: Origin, Benefits, and Implications” has the major objective of identifying the benefits and implications of the risk-based approach under the Third and the Fourth AML Directives.

The Thesis has three research questions. First, it aims to discover why did the European AML regime shift from the rule-based approach to the risk-based approach. Second, it aims to identify which benefits and implications does the risk-based approach bring. Third, it analyses how does the transition to the risk-based approach affect customer identification.

The methodology used in this Thesis rests on the comparative model: thus, each subsequent Directive is being compared with its predecessor. Subsequently, to show the impact of the AML laws on the customer identification in general and specifically on risk evaluation, a detailed explanation of risk categories as well as measures of risk assessment and mitigation would be discussed. Apart from qualitative data, quantitative data would be used, such as statistics, cost-benefit estimations and risk assessment models.

The Thesis is divided into eight Chapters, each devoted to a separate aspect of the research. Chapter 1 briefly outlines the concept of money laundering as well as explains the relevance of the topic. Chapter 2 is divided into three parts, unified by analysis of the First AML Directive. The first Section provides an examination of the 1990 FATF Recommendation, whereas the following Sections discuss the Directive’s background and scope as well as customer identification. Chapter 3 provides an analysis of the Second AML Directive: it focuses on the FATF Eight Special Recommendation of 2001 and the extension of the scope. Chapter 4 concludes the part on the rule-based approach, identifying its implications and emphasising its controversial character. Chapter 5 introduces the risk-based approach under the Third AML Directive and discusses the FATF Recommendations of 2003, background and scope of the Directive, customer due diligence, risk-sensitive categorisation, etc. It further highlights the strengths and the weaknesses of the Directive. Chapter 6 provides a discussion on advancing of the risk-based approach under the Fourth AML Directive. It analyses the amendments made and emphasises the legislative basis of the current European AML regime. Chapter 7 summarises the part on the risk-based approach as well as turns to the practical application of AML/CTF principles, such as risk-evaluation procedures and techniques used to provide the risk-based categorisation of the customer. Chapter 8 provides a brief discussion on the future development of the AML in the European Union.

The conclusion provides the findings of the study, answering each of the research questions as well as offering a future prognosis of the European AML/CTF policy.

## TABLE OF CONTENTS

<b>SUMMARY</b> .....	<b>1</b>
<b>LIST OF ABBREVIATIONS</b> .....	<b>3</b>
<b>1. MONEY LAUNDERING: CONCEPTUAL INTRODUCTION</b> .....	<b>4</b>
<b>2. FOUNDATIONS OF ANTI-MONEY LAUNDERING IN THE EU</b> .....	<b>7</b>
2.1. FATF RECOMMENDATIONS OF 1990 AS A BASIS FOR AMLD1 .....	7
2.2. BACKGROUND AND SCOPE .....	8
2.3. CUSTOMER IDENTIFICATION.....	9
<b>3. EVEN STRONGER RULE-BASED APPROACH</b> .....	<b>11</b>
3.1. FATF SPECIAL RECOMMENDATIONS OF 2001 AS A BASIS FOR AMLD2 .....	11
3.2. AIMS AND AMENDMENTS TO SCOPE.....	11
<b>4. FIRST AND SECOND AMLD: THE ESSENCE OF THE RULE-BASED APPROACH</b> .....	<b>13</b>
<b>5. INCEPTION OF THE RISK-BASED APPROACH</b> .....	<b>15</b>
5.1. FATF RECOMMENDATIONS OF 2003 AS A BASIS FOR AMLD3 .....	15
5.2. BACKGROUND AND SCOPE .....	16
5.3. RISK-BASED APPROACH TO CUSTOMER DUE DILIGENCE.....	18
5.4. RISK-SENSITIVE CATEGORISATION.....	20
5.5. POLITICALLY EXPOSED PERSONS .....	21
5.6. BENEFICIAL OWNERSHIP.....	22
<b>6. ENHANCED RISK-BASED APPROACH</b> .....	<b>24</b>
6.1. FATF RECOMMENDATIONS OF 2012 AS A BASIS FOR AMLD4 .....	24
6.2. BACKGROUND AND SCOPE .....	25
6.3. RISK-BASED APPROACH CRYSTALLISED.....	26
6.4. BENEFICIAL OWNERSHIP .....	29
6.5. BENEFICIAL OWNERSHIP REGISTER.....	30
<b>7. THIRD AND FOURTH AMLD: AN EVEN CLOSER LOOK AT THE RISK-BASED APPROACH</b> .....	<b>31</b>
7.1. METHODOLOGY OF RISK EVALUATION.....	31
7.2. RISK MANAGEMENT FRAMEWORK .....	34
7.3. IMPLICATIONS OF THE RISK-BASED APPROACH.....	36
<b>8. FIFTH AML DIRECTIVE: EXTENDING THE SCOPE OF AML/CTF REGIME IN EU</b> .....	<b>37</b>
<b>CONCLUSION</b> .....	<b>38</b>
<b>ANNEX</b> .....	<b>41</b>
<b>BIBLIOGRAPHY</b> .....	<b>54</b>

## LIST OF ABBREVIATIONS

AML	Anti-Money Laundering
AMLD	Anti-Money Laundering Directive
AMLD1	Council Directive 91/308/EEC of 10 June 1991 on prevention of the use of the financial system for the purpose of money laundering
AMLD2	Directive 2001/97/EC of the European Parliament and of the Council of 4 December 2001 amending Council Directive 91/308/EEC on prevention of the use of the financial system for the purpose of money laundering - Commission Declaration
AMLD3	Directive 2005/60/EC of the European Parliament and of the Council of 26 October 2005 on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing
AMLD4	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
CDD	Customer Due Diligence
CoE	Council of Europe
CTF	Combating Terrorist Financing
DD	Due Diligence
DNFBP	Designated Non-Financial Business and Profession
EDD	Enhanced Due Diligence
EU	European Union
FATF	Financial Action Task Force
FIU	Financial Intelligence Unit
KYC	Know Your Customer
ML	Money Laundering
NCCT	Non-Cooperative Country or Territories
NPO	Non-Profit Organisation
PEP	Politically Exposed Person
SDD	Simplified Due Diligence
TF	Terrorist Financing
UN	United Nations

## 1. MONEY LAUNDERING: CONCEPTUAL INTRODUCTION

Globalisation and the establishment of the common market resulted in businesses expanding their reach and going beyond the national borders, which, in turn, allowed goods, capital, technology, and information to move faster among the states. Integration made it possible to produce better, cheaper, and faster than ever before. Although the benefits of such a rapid development are self-evident, new risks and challenges have emerged, especially in the financial system, as a consequence of the increase in the number of transactions and the reduction of the time required for their processing. As reported by the European Central Bank, the number of transactions in the EU increased from 48 billion to 112 billion in 2000 and 2016 respectively.<sup>1</sup>

Growth of the globalised financial system enabled money launderers and criminals to inject proceeds of a crime in it and conceal their unlawful origin. Today, the issue of money laundering (ML) has become a major concern and is referred to as “a global problem requiring a global solution.”<sup>2</sup> To fight this large-scale problem, the international community responded with numerous countermeasures, including strict financial and banking regulation, more flexible legislation and effective enforcement tools.<sup>3</sup>

Due to historical and geographical reasons, Latvia has traditionally served and continues to serve as a bridge between the Commonwealth of Independent States (CIS) and the Western world. Recently, considerable public attention has been directed to the issue of ML in Latvia, because the United States Financial Crimes Enforcement Network (FinCEN) accused the third biggest bank in the country – ABLV Bank – of the involvement in the ML activity, which led to the bank’s self-liquidation.<sup>4</sup> It is not the first time when unlawful or suspicious banking practices of the Latvian banks drew the attention of the international community. The other two banks – Multibanka and VEF Banka – have also been listed for the special measures by FinCEN. It is worth mentioning that FinCEN list of sanctioned organisations contains in total 21 financial institutions, three of them of Latvian origin. Such a large number, in fact, is a warning signal for the national Anti-Money Laundering and Combating Terrorist Financing (AML/CTF) legislation and enforcement, which proves that the research on the European AML/CTF legislation is of vital importance, taking into account the specifics of the national banking sector.<sup>5</sup>

Despite the fact that money laundering is a widespread expression, it might be interpreted differently because of the lack of universally accepted definition of this phenomenon. Initially, money laundering referred to the money gained from the underground economy, including drug

---

<sup>1</sup> Annex 1.

<sup>2</sup> Rainer Hülse, “Creating Demand for Global Governance: The Making of a Global Money-laundering Problem,” in *Global Society*, Vol. 21, No. 2 (2007), p. 155. Available at:

<https://www.tandfonline.com/doi/abs/10.1080/13600820701201731>. Last accessed: 3 May 2018.

<sup>3</sup> William R. Schroeder, “Money Laundering: A Global Threat and the International Community's Response,” *FBI Law Enforcement Bulletin* 70, No. 5 (May 2001), p. 1-9. Available at:

<http://heinonline.org/HOL/P?h=hein.journals/fbileb70&i=142>. Last accessed: 3 May 2018.

<sup>4</sup> On the Process of Voluntary Liquidation of ABLV Bank, ABLV Bank Official Website. Available at:

<https://www.ablv.com/en/legal-latest-news/voluntary-liquidation-of-ablv-bank-as-to-protect-the-interests-of-clients-and-creditors/on-the-process-of-voluntary-liquidation-of-ablv-bank>. Last accessed: 3 May 2018.

<sup>5</sup> Special Measures for Jurisdictions, Financial Institutions, or International Transactions of Primary Money Laundering Concern, Financial Crimes Enforcement Network Official Website. Available at:

<https://www.fincen.gov/resources/statutes-and-regulations/311-special-measures>. Last accessed: 3 May 2018.

dealing, smuggling, fraud, etc.<sup>6</sup> Later, researchers included tax evasion and white collar crimes, such as invoice falsification and illegal capital flight.<sup>7</sup> For the sake of simplicity, the Financial Action Task Force (FATF) suggested a straightforward definition, which states: “Money laundering is the processing of criminal proceeds to disguise their illegal origin.”<sup>8</sup> However, money laundering does not relate to money only – the term encompasses virtually any property derived from the criminal activity.

The property in this context shall mean

assets of every kind, whether corporeal or incorporeal, movable or immovable, tangible or intangible, and legal documents or instruments evidencing title to or interests in such assets.<sup>9</sup>

FATF played a key role in the creation of the modern AML/CTF policy. According to its mandate, organisation’s main task is identification and analysis of ML/TF and other threats to integrity of the systems, including research of the methods, schemes and trends involved. Its mission is to evaluate the impact of the methods against the abuse of the international financial system, supporting national, regional and global risk assessments.<sup>10</sup>

There are three main FATF documents that are considered to have the most significance for the AML/CTF purposes. The first is the well-known FATF document – its 40 Recommendations. They set the framework for the comprehensive AML/CTF system, which has become the universally recognised standard.

The second set of documents is the country reports: FATF performs country evaluations (including, but not limited to, review of legislation, enforcement mechanisms, FIU operation, etc.) to assess the condition of AML/CTF systems and their compliance with FATF Recommendations with an aim of preventing misuse of the financial system.<sup>11</sup>

Lastly, FATF annually issues the list of the Non-Cooperative Countries and Territories (NCCT). The list contains the countries which are considered to have a detrimental effect in the fight against money laundering and terrorist financing (ML/TF).<sup>12</sup>

---

<sup>6</sup> Brigitte Unger, “The Gravity Model for Measuring Money Laundering and Tax Evasion,” *Workshop on Macroeconomic and Policy Implication of Underground Economy and Tax Evasion* (2009), p. 78-79.

<sup>7</sup> Friedrich Schneider and Dominik H. Enste, “Shadow Economies: Size, Causes, and Consequences,” *Journal of Economic Literature*, Vol. XXXVIII (March 2000), p. 79. Available at: <http://www.economics.uni-linz.ac.at/members/Schneider/files/publications/JEL.pdf>. Last accessed: 3 May 2018.

<sup>8</sup> Financial Action Task Force on Money Laundering (FATF), “The Forty Recommendations of the Financial Task Force on Money Laundering, With Interpretative notes,” *International Legal Materials* 35, No. 5 (1996), p. 1291. Available at: <http://www.jstor.org/stable/20698609>. Last accessed: 3 May 2018.

<sup>9</sup> United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, (Vienna, 1988), Article 1D. Available at: [https://www.unodc.org/pdf/convention\\_1988\\_en.pdf](https://www.unodc.org/pdf/convention_1988_en.pdf). Last accessed: 3 May 2018.

<sup>10</sup> The Financial Action Task Force (FATF), *Financial Action Task Force Mandate 2012-2020*, (Washington DC, 2012), p. 2. Available at:

<http://www.fatf-gafi.org/media/fatf/documents/FINAL%20FATF%20MANDATE%202012-2020.pdf>.

Last accessed: 3 May 2018.

<sup>11</sup> The Financial Action Task Force (FATF), *Methodology for Assessing Technical Compliance With the FATF Recommendations and the Effectiveness of AML/CTF Systems* (February 2018), p. 8. Available at:

<http://www.fatf-gafi.org/media/fatf/documents/methodology/FATF%20Methodology%2022%20Feb%202013.pdf>.

Last accessed: 3 May 2018.

<sup>12</sup> The Financial Action Task Force (FATF), *Annual Review of Non-Cooperative Countries and Territories 2006-2007: Eighth NCCT Review* (Paris, 2017), p. 3. Available at:

The mandate of FATF is not limited to the three aforementioned functions, yet, these are the main ones.<sup>13</sup> As for the institution itself, initially, its founders were the G-7 countries. Today, the list of members contains 35 countries and two regional organisations: the European Commission and the Gulf Cooperation Council. In order to ensure the implementation and enforcement of the FATF policy worldwide, various FATF-style regional organisations have been established, such as the Eurasian Group (EAG) and the Caribbean Financial Action Task Force (CFATF).<sup>14</sup>

It is worth pointing out that FATF is not the only organisation that tackled the ML problem. Initially, FATF based its Recommendations on the UN Vienna Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances.<sup>15</sup> In Strasbourg Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime, the Council of Europe (CoE) continued criminalisation of ML.<sup>16</sup> Since then, many other international governmental and non-governmental organisations made efforts to fight ML, the Organisation for Economic Co-operation and Development (OECD) being just one among many.<sup>17</sup>

Despite the significance of aforementioned organisations, FATF had the biggest impact on the European AML/CTF legislation.<sup>18</sup> Hence, along researching the evolution of the European AML legislation, it is necessary to first address FATF Recommendations. After all, it is exactly FATF that proposed the rule-based approach and later abandoned it in favour of the risk-based approach, thus setting the guidelines for the European Union. As various authors note, researching legislation on AML/CTF is never complete without the historical background to it.<sup>19</sup>

This Thesis has its primary focus on the risk-based approach as enshrined in the Third and Fourth European AML Directives. It aims to answer three research questions. First, why did the European AML regime shift from the rule-based to the risk-based approach? Second, which benefits and implications does the risk-based approach bring? Third, how does the transition to the risk-based approach affect customer identification?

Despite the fact that this Thesis discusses particular legal instruments, namely, the European AML Directives, a short historical background would be provided for each of them in order to trace the overall development of the field.

---

<http://www.fatf-gafi.org/media/fatf/documents/reports/2006%202007%20NCCT%20ENG.pdf>. Last accessed: 3 May 2018.

<sup>13</sup> Annex 2.

<sup>14</sup> The Financial Action Task Force (FATF) Official Website, FATF Members and Observers. Available at: <http://www.fatf-gafi.org/about/membersandobservers/>. Last accessed: 3 May 2018.

<sup>15</sup> UN Vienna Convention 1998, *supra* note 9, Article 3(b).

<sup>16</sup> Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime 1990, Article 6. Available at: <https://rm.coe.int/168007bd23>. Last accessed: 3 May 2018.

<sup>17</sup> The Organisation for Economic Co-Operation and Development (OECD), Money Laundering Awareness Handbook for Tax Examiners and Tax Auditors (2009), p.5. Available at: <http://www.oecd.org/tax/exchange-of-tax-information/43841099.pdf>. Last accessed: 3 May 2018.

<sup>18</sup> Report from the Commission to the European Parliament and the Council on the Application of Directive 2005/60/EC on the Prevention of the Use of the Financial System for the Purpose of Money Laundering and Terrorist Financing, COM(2012) 168 final, (11.4.2012), p. 2. Available at:

[http://ec.europa.eu/internal\\_market/company/docs/financial-crime/20120411\\_report\\_en.pdf](http://ec.europa.eu/internal_market/company/docs/financial-crime/20120411_report_en.pdf). Last accessed: 3 May 2018.

<sup>19</sup> Marcus Killick and David Parody, "Implementing AML/CFT measures that address the risks and not tick boxes," *Journal of Financial Regulation and Compliance*, Vol. 15, Issue: 2 (2007), pp.210-216. Available at: <https://doi.org/10.1108/13581980710744093> (permanent link)

The methodology used in this Thesis rests on the comparative model: thus, each subsequent Directive is being compared with its predecessor. Subsequently, to show the impact of the AML laws on the customer identification in general and specifically on risk evaluation, a detailed explanation of risk categories, as well as measures of risk assessment and mitigation, would be discussed. Apart from qualitative data, quantitative data would be used, such as statistics, cost-benefit estimations and risk assessment models.

The comparative nature of this paper suggests its aim – to explore the concept of the risk-based approach in the current AML legislation and identify its advantages as opposed to the alternative, i.e. rule-based approach.

## 2. FOUNDATIONS OF ANTI-MONEY LAUNDERING IN THE EU

### 2.1.FATF Recommendations of 1990 as a basis for AMLD1

The first reference to the question of the weak transaction reporting and the problem of money laundering by drug traffickers could be traced to European Parliament Resolution of October 1986.<sup>20</sup> Soon after, during the meetings of the Ministers, the Council proposed the Member States to consider mutual recognition as well as enhanced cooperation on freezing and confiscation of the drug traffickers' assets.<sup>21</sup> Next year, the European Community was engaged in the preliminary work on the Vienna Convention, which, among other things, covered the criminalisation of money laundering derived from drug-related offences.<sup>22</sup>

In July 1989, the decision of the G-7 nations urged the international community to fight against drug trafficking and laundering of its proceeds, which marked the creation of the Financial Action Task Force.

Less than in a year, the FATF 40 Recommendations were released to provide a *general (emphasis added)* guidance for the AML efforts to be universally applicable across both common and civil law systems. It equipped countries with a framework constructed to prevent, detect and punish money launderers.<sup>23</sup> The Recommendations covered criminal justice system and law enforcement as well as focused on the role of the financial system, governmental regulations and international cooperation in combating ML.<sup>24</sup> It was the first document of its kind, as it brought the overall framework to the unregulated field. Yet, it is important to note, that neither G-7 Declarations nor FATF Recommendations are legally binding.

---

<sup>20</sup> The European Parliament, Resolution on the drug problem. *Official Journal of the European Communities, Vol 29* (10 November 1986), No C 283/79 - 81.

<sup>21</sup> The Commission of the European Communities Secretariat-General, *Official Journal of the European Communities, Vol 29, No C 283/79-81* (10 November 1986), p.77

<sup>22</sup> Final Act of the United Nations Conference for the Adoption of a Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances. Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances 1988, p.1. Available at: [https://www.unodc.org/pdf/convention\\_1988\\_en.pdf](https://www.unodc.org/pdf/convention_1988_en.pdf).

Last accessed: 3 May 2018.

<sup>23</sup> Navin Beekarry, "The International Anti-Money Laundering and Combating the Financing of Terrorism Regulatory Strategy: A Critical Analysis of Compliance Determinants in International Law," *Northwestern Journal of International Law & Business* 31:137 (2011), p. 180.

<sup>24</sup> FATF Recommendation 1990, *supra* note 8, p.1293.



## 2.2. Background and scope

Shortly after the release of the original FATF Recommendations, in June 1991, the European Community adopted the Council Directive on Prevention of the Use of the Financial System for the Purpose of Money Laundering, also known as the First AML Directive. It was based on the above-mentioned FATF Recommendations, the 1988 UN Vienna Convention and the 1990 CoE Strasbourg Convention.<sup>25</sup> The Directive covered regulatory gaps and became the first attempt of coordination in the field of ML on the EU level. Thus, it served as a basis to the comprehensive European AML legislation and introduced basic measures to prevent ML. Further, it urged the Member States to prohibit money laundering and sought to harmonise legislation in the field.

As to the material scope, it covered prohibition of money laundering. In the Directive, money laundering was defined through another term – criminal activity, which mostly covered drug-related offences.<sup>26</sup>

As to the personal scope, the Directive was aimed to regulate financial and credit institutions as well as several professions involved in substantial cash transactions.<sup>27</sup>

Thus, the Directive marked the beginning of ML supervision and monitoring of customers and their transactions. Most importantly for the purposes of this work, it brought the customer and beneficiary identification, but also bookkeeping procedures and suspicious transaction reporting system. However, there were some substantial shortcomings too.

First, the competences of the European Community regarding judicial cooperation between the Member States in criminal matters have been established under the three-pillar system based on the 1992 Maastricht Treaty, which is a year after signing the Directive. Practically, before that the Directive could not regulate criminalisation issues and criminal matters that were under the Member States' discretion. This led to confrontations and lengthy negotiations to convince the Member States to introduce criminal liability for offences outside the framework of the Directive.<sup>28</sup>

Second, the Directive defined “criminal activity” as drug-related offences specified in Art. 3(1) of the Vienna Convention, and supplemented it with the wording “any other criminal activity designated as such for the purposes of this Directive by each Member State.”<sup>29</sup> As the Greek professor of law Dr. Konstantinos D. Magliveras noticed:

The definition of money laundering has been badly drafted because it leaves it to the discretion of Member States to decide which criminal activities should be designated. In effect, it allows for considerable disparities between national legislations.<sup>30</sup>

<sup>25</sup> Council Directive 91/308/EEC of 10 June 1991 on prevention of the use of the financial system for the purpose of money laundering, *Official Journal L 166*. Recitals. Available at: <http://eur-lex.europa.eu/legal-content/en/ALL/?uri=CELEX:31991L0308>. Last accessed: 3 May 2018.

<sup>26</sup> *Ibid.*, Article 1 and Article 2.

<sup>27</sup> *Ibid.*, Article 3.

<sup>28</sup> The Treaty on European Union 1992 (Maastricht Treaty), Article K.1. Available at:

[https://europa.eu/european-union/sites/europa.eu/files/docs/body/treaty\\_on\\_european\\_union\\_en.pdf](https://europa.eu/european-union/sites/europa.eu/files/docs/body/treaty_on_european_union_en.pdf). Last accessed: 3 May 2018.

<sup>29</sup> Directive 91/308/EEC, *supra* note 25, Article 1.

<sup>30</sup> Konstantinos Magliveras, “The European Community’s Combat Against Money Laundering: Analysis and Evaluation,” *Journal of International & Comparative Law Vol 5:93* (1998), p.99.

It did not specify other criminal offences to be covered and, as the content of the criminal codes differs among MS, the implementation was not unified.<sup>31</sup> As a result, this contributed to the creation of the so-called “safe” jurisdictions like Luxembourg or Portugal, where the least of activities were penalised.<sup>32</sup> Broad definitions of criminal activity and wide coverage of Article 1(c) brought ambiguity for which AMLD1 was criticized.

To the similar conclusion came Emma Radmore, Gautam Bhattacharyya and Miles Laddie. On the example of the UK, they argue that it would be complicated to determine whether activities carried out outside the country would constitute a criminal offence in the country (that is, the UK), especially if the activity is legal in other jurisdictions.<sup>33</sup>

One more criticism was that it should have contained a non-exhaustive list of predicate offences (with the possibility for the Member States to extend the list), which would reduce disparities between the domestic legislations. Alternatively, the creation of an exhaustive list might have been complicated by different approaches taken by the Member States with regard to crimes.<sup>34</sup>

Another disadvantage concerns the personal scope of the Directive: it was addressed to defined financial and credit institutions, which left unclear the status of non-financial undertakings. In other words, casinos, dealers in objects of high value and legal professionals carrying out financial activities were not explicitly covered by the scope, which eventually allowed criminals to explore new schemes, falling outside the financial sector.

### 2.3. Customer identification

According to Article 3 of AMLD1, financial institutions and insurance companies shall perform customer identification and/or identification of the beneficiary when entering into business relations and whenever single or allegedly related transaction threshold of 15 000 EUR was reached and when transactions might be subjectively identified as suspicious.<sup>35</sup>

Although the provision demanded identification of beneficiary (in case when the latter is presumed to be unknown) to be carried out, there were no procedures or definitions provided in the document, which resulted in heterogeneous implementation<sup>36</sup>. However, a positive

---

<sup>31</sup> The Commission of the European Communities, First Commission's Report on the Implementation of the Money Laundering Directive (91/308/EEC) to Be Submitted to the European Parliament and to the Council, COM(95) 54 Final, (03.03.1995), p.7. Available at: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:51995DC0054&qid=1525370717951&from=EN>. Last accessed: 3 May 2018.

<sup>32</sup> *Ibid.*, Annex III.

<sup>33</sup> Andrew Campbell, “The High-Street Solicitor and the Proceeds of Criminal Activity — The Risks”, *Journal of Money Laundering Control*, Vol. 1 Issue: 1 (1997), p. 8. Permanent link: <https://doi.org/10.1108/eb027115>

<sup>34</sup> Johanna Peurala. “The European Union’s Anti-Money Laundering Crusade – a Critical Analysis of the Responses by the EU/EC to Money Laundering,” *Reports of the Police College of Finland* 83/2009 (2009), p. 55. Available at: [https://www.theseus.fi/bitstream/handle/10024/86709/Raportteja\\_83.pdf?sequence=1](https://www.theseus.fi/bitstream/handle/10024/86709/Raportteja_83.pdf?sequence=1). Last accessed: 3 May 2018.

<sup>35</sup> Directive 91/308/EEC, *supra* note 25, Article 3.

<sup>36</sup> Commission of the European Communities, Second Commission Report to the European Parliament and the Council on the Implementation of the Money Laundering Directive Brussels, COM(1998) 401 final, (01.07.1998), p. 12. Available at: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:51998DC0401&from=EN>. Last accessed: 3 May 2018.

consequence was that banks and financial institutions refrained from opening anonymous bank accounts and/or from conducting transactions when the beneficiary's identity was not known.<sup>37</sup>

Another provision that raised issues was Art. 3(8), which allowed not to perform identification in case of insurance operations when a customer has already been identified.<sup>38</sup> The Commission then proposed to extend this exemption to all financial transactions (except for opening of the bank accounts), which was rejected. On the one hand, such solution could be efficient and could potentially reduce the costs. On the other hand, however, customer risk assessment might have been jeopardized because of weak control over electronic and telephone banking. In any event, because of the emergence of new technologies, AMLD1 weakly regulated direct banking.<sup>39</sup>

Nowadays, prevention of a crime is regarded as important as its repression. In this connection, the Chinese criminal law professor and researcher of the European AML/CTF policy He Ping concluded that the First AML Directive lacked effective methods of prevention of ML crimes. It was insufficiently developed to serve as a comprehensive preventive mechanism given the challenges of the money laundering schemes.<sup>40</sup>

In general, the Directive imposed rules to be followed by the MS, which later would become known as the rule-based approach. The attempt of harmonisation of the AML legislation established cooperation between the Member States, whereas the exchange of information among related authorities paved the way for the further development. Yet, this was only the beginning: FATF Recommendations were revised in 1996 to extend the list of predicate offences and include not only the drug-related offences but also other serious crimes. However, not all scholars have welcomed the extension of the definition of ML. British professor of international banking and finance law Andrew Campbell described the situation as follows:

If almost all forms of criminal activity of an economic nature are now covered this is a significant shift which ... is very disturbing. The Law Society was certainly of the opinion that the provisions should relate to drug trafficking offences only and there was no requirement in the Money Laundering Directive that the law should be extended to cover virtually all crimes.<sup>41</sup>

The extension as such was not revolutionary, as it has already been seen in the 1990 Strasbourg Convention, but it has set the tone for combating ML beyond the European Continent.<sup>42</sup> Based on the revised Recommendations in general and specifically on Recommendation 9 and its annex,<sup>43</sup> the Commission stressed the need to extend and clarify the scope of the Directive as a major shortcoming of the First Directive.<sup>44</sup>

<sup>37</sup> Konstantinos Magliveras, "The European Community's Combat Against Money", *supra* note 30, p.102.

<sup>38</sup> Directive 91/308/EEC, *supra* note 25, Article 3.

<sup>39</sup> First Commission's Report on the Implementation of the Money Laundering Directive, *supra* note 31, p.11.

<sup>40</sup> He Ping, "The new weapon for combating money laundering in the EU", *Journal of Money Laundering Control*, Vol. 8 Issue: 2 (2005), p. 119. Permanent Link: <https://doi.org/10.1108/13685200510621163>

<sup>41</sup> Andrew Campbell, "The High Street", *supra* note 33

<sup>42</sup> FATF Recommendation 1990, *supra* note 8, p.1291. Available at: <http://www.jstor.org/stable/20698609>. Last accessed: 3 May 2018.

<sup>43</sup> *Ibid.*, Recommendation 9 and Annex I.

<sup>44</sup> Second Report on the Implementation of the Money Laundering Directive, *supra* note 36, p. 11.

### 3. EVEN STRONGER RULE-BASED APPROACH

#### 3.1.FATF Special Recommendations of 2001 as a basis for AMLD2

In 2001, FATF released Eight Special Recommendations and introduced the first Counter-Terrorist Financing (CTF) standard.<sup>45</sup> Its First Recommendation stressed the need to sign and ratify the UN Conventions against Terrorist Financing, while other described efficient tools to fight this issue and, not surprisingly, extended the list of ML predicate offences.<sup>46</sup>

The scope of Recommendations was not limited to the financial sector, it has been extended to agents and legal entities involved in any type of money or value transferring. Furthermore, non-profit organisations (NPOs) were enlisted to the document, as most countries did not regulate them correctly, which resulted in the exploitation of the structure.<sup>47</sup>

The European Union reacted to the changes in international policy on AML/CTF by immediate action: one month later, the Directive 2001/97/EC, known as the Second AML Directive has been introduced.

#### 3.2.Aims and amendments to scope

Not only the events of 9/11 caused the European legislature to consider amendments to the Directive, but also the advancement of the schemes used by launderers. The European Parliament and the Council of the European Union characterised the situation as follows:

there is evidence that the tightening of controls in the financial sector has prompted money launderers to seek alternative methods for concealing the origin of the proceeds of crime.<sup>48</sup>

FATF came to the same conclusion in its 2002-2003 report on ML typologies, where 24 examples of cunning schemes of ML/TF were presented. It has been investigated that methods to disguise the true nature of the funds have developed and might exploit unprotected areas, e.g., NPOs, export/import companies, use of informal financial systems, etc.<sup>49</sup>

The main goal of the new document against ML was to adopt measures which shall protect the integrity and stability of the European financial system as well as close the known loopholes.<sup>50</sup>

---

<sup>45</sup> The Financial Action Task Force (FATF), Annual Report 2001-2002 (2002), p. 5. Available at: <http://www.fatf-gafi.org/documents/documents/fatfannualreport2001-2002.html>. Last accessed: 3 may 2018.

<sup>46</sup> *Ibid.*, Annex A.

<sup>47</sup> *Ibid.*

<sup>48</sup> Directive 2001/97/EC of the European Parliament and of the Council of 4 December 2001 amending Council Directive 91/308/EEC on prevention of the use of the financial system for the purpose of money laundering, *OJ L* 344, 28.12.2001. Recital 13. Available at:

<https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:32001L0097&from=EN>. Last accessed: 4 May 2018.

<sup>49</sup> The Financial Action Task Force (FATF), Report on Money Laundering Typologies 2002-2003 (14 February 2003), p. 1. Available at: <http://www.fatf-gafi.org/documents/documents/moneylaunderingtypologies2002-2003.html>. Last accessed: 4 May 2018.

<sup>50</sup> Directive 2001/97/EC, Recital 2 and Recital 5. Available at: <https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:32005L0060&from=EN>. Last accessed: 4 May 2018.

The Second Directive was not an independent document: instead, it presented the list of improvements and amendments to the First Directive.

First, the Second Directive amended the material scope by extending the notion of the criminal activity. The list went beyond drug-related offences and, apart from offences defined in Article 3(1)(a) of the Vienna Convention, included “the activities of criminal organisations as defined in Article 1 of Joint Action 98/733/JHA(12)”<sup>51</sup>, serious fraud “as defined in Article 1(1) and Article 2 of the Convention on the protection of the European Communities' financial interests”<sup>52</sup> and corruption.

The personal scope has been expanded to cover legal and natural persons of certain professions, which, due to the nature of their activities, were linked to substantial amounts of money. Thus, Article 2(a) included casinos, bureaux de change, auctioneers, auditors and lawyers, which are referred to as Designated Non-Financial Businesses and Professions (DNFBPS). To reinforce compliance among dealers in high-value goods, they were obliged to check customers in cases when the transaction reached the threshold of 15000 EUR in cash.

An obvious disadvantage of Article 2(a)(6) is best illustrated with the following example: had a person bought a piece of art for 15000 EUR in cash, the auctioneer would have to pass him through AML checks; yet, had a person bought the same piece of art for the same amount of 15000 EUR, but using credit card issued by some bank in Myanmar, the Directive would not be applicable.<sup>53</sup> Likewise, if a person would regularly buy jewellery for 14000 EUR every week in the same shop, irrespective of whether in cash or using the credit card, it would remain unclear – based on the wording of the Directive – whether the jeweller<sup>54</sup> would have to pass a person through identification checks.<sup>55</sup>

The inclusion of lawyers in the personal scope brought some difficulties, as the Directive insisted on lifting professional secrecy in case the when a lawyer knew of his client’s ML activities.<sup>56</sup> Although the Directive generally prescribed legal professionals to report suspicious transactions, Article 6(3) allowed derogations. As it was pointed out in the Directive itself,

---

<sup>51</sup> 98/733/JHA: Joint action of 21 December 1998 adopted by the Council on the basis of Article K.3 of the Treaty on European Union, on making it a criminal offence to participate in a criminal organisation in the Member States of the European Union, *Official Journal L 351*, 29.12.1998. Article 1. Available at: <http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:31998F0733&from=EN>. Last accessed: 6 May 2018.

<sup>52</sup> Convention drawn up on the basis of Article K.3 of the Treaty on European Union, on the protection of the European Communities' financial interests, *OJ C 316/49*, 27.11.1995. Article 1(1) and Article 2. Available at: [https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:41995A1127\(03\)&from=EN](https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:41995A1127(03)&from=EN). Last accessed: 6 May 2018.

<sup>53</sup> Myanmar was referred as non-cooperative jurisdiction. The Financial Action Task Force (FATF). Review to Identify Non-Cooperative Countries or Territories: Increasing the Worldwide Effectiveness of Anti-Money Laundering Measures. Second NCCTs review (06/2001). p.3. Available at: <http://www.fatf-gafi.org/media/fatf/documents/reports/2000%202001%20NCCT%20ENG.pdf>. Last accessed: 7 May 2018.

<sup>54</sup> In this fictional scenario, it is assumed that jeweller does not recognize the potential AML risk and his action is mocked up only according to the Second Directive.

<sup>55</sup> R.C.H. Alexander, *Insider Dealing and Money Laundering in the EU: Law and Regulation*. (London, Routledge: 2007). p.153.

<sup>56</sup> Directive 2001/97/EC, *supra* note 48, Recital 2.

It would not be appropriate ... to put these legal professionals in respect of these activities under an obligation to report suspicions of money laundering.<sup>57</sup>

The controversy around this legal norm caused several claims being filed to the European Court of Justice and the European Court of Human Rights to review compliance of the Directive's provisions with Articles 6 and 8 of the European Convention on Human Rights<sup>58</sup>, i.e. the right to fair trial and the right to respect for private life respectively.<sup>59</sup>

Article 3(11) brought a major advance towards the Know Your Customer (KYC) rule: it imposed stricter rules on non-face-to-face operations by requiring the customers to submit additional documentation to ensure their identification, such as an electronic signature.<sup>60</sup> This is a large step forward in comparison with the previous legislation, where operations via phone or email were not clearly covered.<sup>61</sup>

In addition, one of the most crucial changes was Article 10. It introduced domestic supervisory body over stock exchange, foreign exchange and financial market.<sup>62</sup> The aim of the body was to monitor national transactions and report to the relevant authorities in case of suspicion of ML. It was the first time when such bodies, which would later become known as Financial Intelligence Units (FIUs), were introduced. This is an important rule, as the FIUs are not just autonomous supervisory bodies but most often part of the whole national judicial system<sup>63</sup>, as they may need the access to administrative, enforcement or financial information.<sup>64</sup>

#### 4. FIRST AND SECOND AMLD: THE ESSENCE OF THE RULE-BASED APPROACH

To conclude on the First and Second AML Directives, the principles and methods they contain marked a creation of a united and coherent system against ML and TF. It has been seen that both Directives provided a system of rules aimed to detect and prevent misuse of the financial system composed of methods and techniques based on the *assumptions*.

In essence, the rule-based approach is based on one main assumption: that the field of ML is homogeneous, therefore, predetermined regulations would substantially cover potential risks.

---

<sup>57</sup> *Ibid.*, Recital 17.

<sup>58</sup> Sara De Vido, "Anti-Money Laundering Measures Versus European Union Fundamental Freedoms and Human Rights in the Recent Jurisprudence of the European Court of Human Rights and the European Court of Justice," *German Law Journal Vol. 16 No. 05* (2005), p. 1281.

Available at: [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2848202](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2848202). Last accessed: 7 May 2018.

<sup>59</sup> Convention for the Protection of Human Rights and Fundamental Freedoms as amended by Protocols Nos. 11 and 14 supplemented by Protocols Nos. 1, 4, 6, 7, 12 and 13. Article 6 and 8. Available at: [https://www.echr.coe.int/Documents/Convention\\_ENG.pdf](https://www.echr.coe.int/Documents/Convention_ENG.pdf). Last accessed: 16 March 2018.

<sup>60</sup> Directive 2001/97/EC, *supra* note 48, Article 3(11).

<sup>61</sup> Jane Welch, Javier Munoz del Guayo and others, "Comparative Implementation of EU Directives (II) – Money Laundering," *The British Institute of International and Comparative Law* (December 2006), p.11.

<sup>62</sup> Directive 2001/97/EC, *supra* note 48, Article 10.

<sup>63</sup> For example, the FIU in Latvia is Office for Prevention of Laundering of Proceeds Derived from Criminal Activity, which is a department under the prosecutor office.

<sup>64</sup> Financial Intelligence Units: An Overview. International Monetary Fund World Bank (2004), p.111. Available at: <https://www.imf.org/external/pubs/ft/FIU/fiu.pdf>. Last accessed: 7 May 2018.

Such approach implies an obligation of the covered persons and institutions to follow the rules, precluding additional initiative to manage the risk on their part.

Paolo Costanzo, the head of Italian FIU, has highlighted that the rule-based approach has at least two apparent benefits: first, it was simpler and, second, less costly to implement and follow the AML norms, since the rules and requirements were created in advance and did not vary depending on the situation.<sup>65</sup> It could also be argued that the rule-based approach required fewer efforts from the regulator, as threats and vulnerabilities were taken into consideration neither in the laws nor by the supervisory bodies. Conversely, the risk-based approach, which will be discussed in the chapters to follow, requires a shared understanding of risks between the financial institutions and the regulator, as well as some common view on financial institutions' obligations under each specific risk category.

It is argued, however, that deficiencies of such approach outweigh the benefits, not just in number but also in substance.

First, it was noted by the UK Financial Services Authority, the rule-based approach might be inefficient due to disproportionate measures and the “one size fits all” attitude.<sup>66</sup> The AML policy under the rule-based approach could have been easily manipulated by the launderers, as it is well illustrated by the jeweller example.

Second, the threshold system of suspicious transaction reporting fails to cover the instances when transactions are reaching *just below* the threshold. Such formalistic approach is not appropriate as it fails to attain the ultimate purpose of AML, that is, combating misuse of the financial system.

Third – and the most important – negative consequence logically follows from the previous one: the rule-based approach, in fact, allows financial institutions and risk managers to do *just enough* to be formally in compliance with the rules, which is known as the “tick-box approach”.<sup>67</sup> Thus, such approach has a somewhat “relaxing” effect on both the subjects and the agents, that is, on both the potential perpetrators and the supervisory bodies.

Additionally, besides the law itself, it is important to consider its implementation. European AML/CTF scholar Anna Simonova points out that the main problem of the Directives operated under the rule-based approach was the lack of enforcement tools:

No enforcement instruments were demanded and it seems that, like under the First Directive, enforcement was not truly a point of attention in the Second Directive.<sup>68</sup>

---

<sup>65</sup> Paolo Costanzo, “The risk-based approach to anti-money laundering and counter-terrorist financing in international and EU standards: what it is, what it entails”. Research Handbook on Money Laundering, (Cheltenham, UK: Edward Elgar Publishing, 2013), p.1. Available at: <https://doi.org/10.4337/9780857934000.00038>

<sup>66</sup> Abdullahi Bello and Jackie Harvey. “From a risk-based to an uncertainty-based approach to anti-money laundering compliance,” *Security Journal*, 30(1) (2017), pp. 24-38. Available at: [http://nrl.northumbria.ac.uk/26933/3/Harvey\\_Uncertainty%20based%20approach%20to%20AML%20submitted%20to%20Security%20journal.pdf](http://nrl.northumbria.ac.uk/26933/3/Harvey_Uncertainty%20based%20approach%20to%20AML%20submitted%20to%20Security%20journal.pdf). Last accessed: 7 May 2018.

<sup>67</sup> Marcus Killick, “Implementing AML/CFT measures” that address the risks and not tick boxes”, *supra* note 19, p. 215.

<sup>68</sup> Anna Simonova, “The risk-based approach to anti-money laundering: problems and solutions,” *Journal of Money Laundering Control*, Vol. 14 Issue: 4 (2011), p. 177. Permanent link to this document: <https://doi.org/10.1108/13685201111173820>

It is important to note, however, that the ruled-based and the risk-based approach are in no way mutually exclusive and, actually, are not *completely* contrary to each other. It is possible that certain elements of the former are present in the latter. As it will be discussed further, a relatively cheap and clear guidance proposed under the rule-based approach system supported the inception of the risk-based approach. As the creation of the latter required resources and time, the rule-based approach had a certain compensatory role until it fully crystallised.

Eventually, the rule-based approach became unsuitable to the new realities of financial market: the means of ML have evolved, which resulted in the decrease of the AML policy efficiency. Such developments required risk differentiation as well as more flexibility from financial institutions for AML laws to face new challenges, which consequently led to a creation of an entirely new system of risk evaluation.

## 5. INCEPTION OF THE RISK-BASED APPROACH

### 5.1.FATF Recommendations of 2003 as a basis for AMLD3

In 2003, a new milestone in the development of the European AML/CTF was brought by the second revision of the FATF Forty Recommendations, which was applicable not only to ML issues, but also to TF supported by Eight Special Recommendations aimed to provide an “enhanced, comprehensive and consistent framework of measures” to combat the mentioned problems.<sup>69</sup> Based on the 1988 UN Vienna and the 1990 Palermo Conventions, Recommendation 1 was amended so as to cover the widest range of predicate offences, encompassing numerous serious crimes beyond drug-related crimes.

Apart from the Recommendation itself, a pool of designated categories of offences was attached to avoid misinterpretation and provide a general guideline for each country to decide how it would translate definitions and principles to the national level.<sup>70</sup>

The amendments introduced a more profound and complex system of risk evaluation as well as provided guidelines on effective KYC principles.<sup>71</sup> The issue of due diligence (DD) rapidly became crucial for the functionality of the AML policy. Researcher and Chief Legal Advisor of the Bank of Portugal, Inês Sofia de Oliveira, referred to the due diligence as a recognized core and the most relevant element of AML.<sup>72</sup>

The reason behind the importance of the due diligence lies in need of the financial system to be informed as much as possible about the customers and their activity. FATF Recommendations are addressing the issue of information gathering, not control over financial institutions or sanctions to perpetrators, which is a fundamental feature of the modern risk-based approach.

<sup>69</sup> The Financial Action Task Force (FATF), The FATF Recommendations 2003 (October 2004), p.2. Available at: <http://www.fatf-gafi.org/media/fatf/documents/FATF%20Standards%20-%2040%20Recommendations%20rc.pdf>. Last accessed: 7 May 2018.

<sup>70</sup> *Ibid.*, p.15

<sup>71</sup> Basel Committee on Banking Supervision, Consultative Document Customer due diligence for banks (January 2001), p.3. Available at: <https://www.bis.org/publ/bcbs77.pdf>. Last accessed: 7 May 2018.

<sup>72</sup> Inês Sofia de Oliveira, “Anti-Money Laundering: the conditions for global governance and harmonisation,” *The University of Edinburgh* (2014), p.18. Available at: <https://www.era.lib.ed.ac.uk/handle/1842/15922?show=full>. Last accessed: 7 May 2018.



Likewise, the authors of the World Bank study materials on AML underlined the nature of the new system against previous entire rules controlled approach:

information, rather than control of the transactions, is the key to the basic “know your customer” approach of the FATF. More generally, the value of adequate information to guide the supervision of modern financial markets—in which there is a good measure of transparency and prudential regulation to ensure the fairness, soundness, and legality of the systems.<sup>73</sup>

However, as Australian AML/CTF researcher Jackie Johnson pointed out, the FATF Recommendations 2003 failed to provide adequate control over the gambling sector. She argues that the customer due diligence and reporting system proposed by the FATF are oriented towards the banking sector, leaving aside non-financial businesses. Therefore, not only the appropriate procedure of customer due diligence, but rather the tailor-made regulation is necessary to cover each ML-exposed sector.<sup>74</sup>

Last among major innovations, Recommendation 18 introduced a non-cooperation clause with the shell banks that are incorporated in non-regulated jurisdictions and are not legally affiliated with financial institutions. Although such banks are used as secrecy havens, which is mostly seen as having a detrimental effect, these jurisdictions are not necessarily being used by the criminals, so a total ban on dealing with them would be a disproportionate solution.<sup>75</sup>

## 5.2. Background and scope

In 2005, contrary to a conventional approach (that is, to wait for the Commission's report on the implementation of the Directive in force), the Council and the European Parliament released a new Directive. According to Mariano Fernández Salas, the plausible reason to hurry was the release of the revised FATF Recommendations of 2003 coupled with the willingness to reconcile definitions of the serious crimes with the Justice and Home Affairs Council framework.<sup>76</sup>

FATF brought a new concept for AML/CTF policy: the so-called risk-based approach (RBA), which envisaged a distribution of resources according to the potential customers' risk based on risk evaluation. While both previous Directives adopted a reactive approach, i.e. detecting the misuse after the actual crime has already been committed, the new AML/CTF policy included in the Third Directive offered a completely different – proactive – approach, focusing on *preventing* the flows of “dirty money” in the economy.

---

<sup>73</sup> The World Bank, *Combating Money Laundering and the Financing of Terrorism: A Comprehensive Training Guide*, Volume 1 (2009), p.19. Available at: <http://siteresources.worldbank.org/FINANCIALSECTOR/Resources/CombatingMLandTF.pdf>. Last accessed: 7 May 2018.

<sup>74</sup> Jackie Johnson, “An analysis of the obligations of gambling entities under the FATF's 2003 anti-money laundering recommendations”, *Journal of Money Laundering Control*, Vol. 9 Issue: 1 (2006), p.12. Permanent link to this document: <https://doi.org/10.1108/13685200610645184>

<sup>75</sup> The FATF Recommendation 2003, *supra* note 69, Recommendation 18.

<sup>76</sup> Mariano Fernández Salas, “The third anti-money laundering directive and the legal profession,” *European Association of Lawyers* (October 2005), p.2. Available at: <https://www.anti-moneylaundering.org/Document/Default.aspx?DocumentUid=7B528765-CB1F-4748-9733-68935E2C4745>. Last accessed: 7 May 2018.

Another reason for having the new Directive was the Community's realisation that the implementation of previous Directives was neither unified nor substantially effective, as each Member State tried to protect its own financial system. Thus, a more coordinated and profound inference of the European institutions was required.<sup>77</sup>

As to the material scope of the Directive, due to globalisation and overall technological advancement, the definition of property was extended to also cover electronic and digital assets, including electronic money. Extension of the definition allowed to cover e-money, as it represented a new, yet unexplored territory with even faster transactions, making ML a considerably more problematic area.<sup>78</sup> The issue of electronic money still remains topical and, within the scope of AMLD, is seen as failing to prevent cyber laundering. It is submitted by the author of this Thesis, however, that the inclusion of internet transactions was not a successful decision, as a separate framework is required to the fight cyber laundering phenomenon effectively.

The personal scope of the Third Directive was once again extended and encompassed any natural or legal persons trading in goods, which accept single or several transactions beyond 15000 EUR in cash.<sup>79</sup> This provision might be beneficial for some business sectors, but the problem of cash-credit cards and frequent purchases remained unanswered. The controversy still exists around the reasoning as to why the credit cards, which potentially could be used for ML purposes, fall out of the identification procedure (as opposed to in-cash operations).

Further, trusts and company service providers have also been included to the scope of the Directive. The aim was to restrict evasion from AML rules and establish control over essentially every institution engaged in a large number of transactions. Trusts and company service providers have been severely used by the criminals: their nature is similar to other financial related professions (e.g., advisors or lawyers) but they were out of the scope under the previous Directives. Thus, the idea behind the extension of the scope was to cover the previously uncovered entities. FATF came to the same outcomes in its report "The Misuse of Corporate Vehicles", where one of the major concerns was the lack of the regulation on trusts and company service providers, as those could have been easily established and easily liquidated due to legislative loopholes in certain jurisdictions.<sup>80</sup>

Lastly, Article 5 of the new Directive stated that the Member States may decide to adopt or retain in force stricter rules in the field covered by the Directive. Hence, the Directive foresaw the

---

<sup>77</sup> Directive 2005/60/EC of the European Parliament and of the Council of 26 October 2005 on the Prevention of the Use of the Financial System for the Purpose of Money Laundering and Terrorist Financing, *OJL 309/15*, 25.11.2005, Recital 2. Available at: <https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:32005L0060&from=EN>. Last accessed: 7 May 2018.

<sup>78</sup> *Ibid.*, Article 3(3).

<sup>79</sup> *Ibid.*, Article 2(3)(e).

<sup>80</sup> The Financial Action Task Force (FATF), *The Misuse of Corporate Vehicles, Including Trust and Company Service Providers* (13 October 2006), p. 1-2. Available at: <http://www.fatf-gafi.org/media/fatf/documents/reports/Misuse%20of%20Corporate%20Vehicles%20including%20Trusts%20and%20Company%20Services%20Providers.pdf>. Last accessed: 7 May 2018.

possibility of different AML regimes among the MS. In other words, only minimum harmonisation requirements have been imposed.<sup>81</sup>

### 5.3. Risk-based approach to customer due diligence

According to the FATF Recommendations<sup>82</sup>, the risk of ML/TF among customers and their transactions may vary and it is a duty of every entity covered by the scope of the Directive to evaluate such risk. It guarantees flexibility and provides measures according to the risk-sensitive differentiation, which distinguishes three major categories of risk: simplified, regular and enhanced customer due diligence (CDD), ordered accordingly by the level of posed risk.

Article 8(2) clearly explains the impact of the risk-based approach on the customer due diligence:

The institutions and persons covered by this [Third] Directive shall apply each of the customer due diligence ... but may determine the extent of such measures on a risk-sensitive basis depending on the type of customer, business relationship, product or transaction.<sup>83</sup>

The choice of the relevant due diligence procedure is not dictated but partially predetermined, which may be viewed as a legacy of the rule-based approach. The goal of the risk-based approach system is to recognise risks and ensure appropriate monitoring of the customers' activity. The approach, however, is not harmonised across the EU, as the Member States may shape their own systems and decide on the necessary techniques to be used by financial institutions.<sup>84</sup>

According to Article 7, the regular customer due diligence procedure shall be performed under certain circumstances: a) before establishing business relationships; b) when occasional single or several transactions which appeared to be linked reach the limit of EUR 15000; c) where there is suspicion of ML/TF (a rather traditional clause for AML policies); d) where information on customers/transactions, which was collected prior, is subject to doubts.<sup>85</sup>

The rule obliging to perform CDD before establishing business relationships brought some challenges. It was seen as complicated with regard to timing issues, so it was proposed to extend the period of fulfilment of CDD and allow performing it *after* the relationships have started, which, regrettably, was not upheld.

Furthermore, general obligations of customer due diligence under AMLD3 might be roughly divided into three stages: first, obtaining information confirming legal existence of the entity, name, address, structure of the company, directors, power to bind; second, the identification of

---

<sup>81</sup> Deloitte, European Commission DG Internal Market and Services - Budget Final Study on the Application of the Anti-Money Laundering Directive (2010), p.26. Available at: [http://ec.europa.eu/internal\\_market/company/docs/financial-crime/20110124\\_study\\_amld\\_en.pdf](http://ec.europa.eu/internal_market/company/docs/financial-crime/20110124_study_amld_en.pdf). Last accessed: 7 May 2018.

<sup>82</sup> Report from the Commission to the European Parliament and the Council on the Application of Directive 2005/60/EC on the Prevention of the Use of the Financial System for the Purpose of Money Laundering and Terrorist Financing, 52012DC0168, Point 2.1. Available at: <https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52012DC0168&from=EN>. Last accessed: 7 May 2018.

<sup>83</sup> Directive 2005/60/EC, *supra* note 77, Article 8(2).

<sup>84</sup> Report from the Commission, *supra* note 82, Point 2.1.

<sup>85</sup> Directive 2005/60/EC, *supra* note 77, Article 7.

the beneficial ownership; third, supplementary information on the purposes and the nature of the business relationships or a transaction.<sup>86</sup>

The collection of information is the cornerstone of the risk-based approach. Finding an independent and reliable source of information was regarded as the cornerstone of the identification process, which would allow assessing the risk properly. Moreover, it is accompanied by the ongoing monitoring, i.e. constant verification of the person. It is done in order to confirm, update and evaluate the information collected against ML/TF risks. As a consequence, all information gathered on the customer allows the institutions to divide all customer into groups on the risk-sensitive basis.<sup>87</sup>

Unsurprisingly, customer due diligence under AMLD3 does not stop when transactions or initial due diligence was executed. Instead, the information and records collected during the previous stages shall be stored for five years after the termination of the relationships with a client.<sup>88</sup> This is required in order to be able to provide necessary information to FIU or other institutions, which may need such information for investigation purposes or for statistical needs as a part of ML/TF research.<sup>89</sup>

Principles laid down in the customer due diligence constitute a dual system used in AMLD3.

First, the AML policy became risk-sensitive during the customer identification stage. Second, monitoring and storage of information ensure that data is complete and ready to be used as a reference. Consequently, the financial system has begun to exercise surveillance functions, as data collection and monitoring capacities were brought on a new level.

As for implications, the research made by the European Commission has shown that stakeholders experienced some issues concerning the implementation of the risk-based approach to the CDD. Most financial institutions have put the IT compliance systems into action, which are able to perform automated customers risk analysis. These systems, however, may require significant development and implementation costs, but the alternative of manually carrying out the customer analysis does not seem less costly or more adequate.<sup>90</sup>

Additionally, as the scope of the Directive was extended to cover non-financial institutions, they were also required to fulfil all AML requirements. Yet, in contrast to the financial sector, guidance provided for non-financial institutions was not sufficiently detailed with regard to the practical aspects of the risk-based approach. This is also complicated by the fact that the instructions provided by competent authorities were not always publicly available.

Likewise, non-financial professions also experienced lack of guidance. Reference to FATF<sup>91</sup> rules was considered insufficient, and stakeholders urged the need to have the rules adapted to their domestic situation.<sup>92</sup>

---

<sup>86</sup> *Ibid.*, Article 8.

<sup>87</sup> *Ibid.*

<sup>88</sup> *Ibid.*, Article 30.

<sup>89</sup> *Ibid.*, Article 33.

<sup>90</sup> Deloitte Study, *supra* note 81, p. 295.

<sup>91</sup> Such as FATF Guidance for Legal Professionals, FATF Guidance for Real Estate Agents, FATF Guidance for External Accountants, and FATF Guidance for Trust and Company Service Providers.

<sup>92</sup> Deloitte Study, *supra* note 81, p. 48.

## 5.4. Risk-sensitive categorisation

Simplified due diligence (SDD) procedure is applicable to the low-risk persons and entities. Practically, SDD means the absence of due diligence at all, because of the minimum level of risk posed by such customers.<sup>93</sup> According to Article 11, such instances are publicly traded companies (because of mandatory disclosure obligations that guarantees transparency), governmental institutions, pensions and insurance services under certain threshold, confirmed accounts of notaries and other independent legal professions, where customer due diligence procedure was *already* performed by financial institutions with recognised and efficient AML policy.<sup>94</sup>

Additionally, Article 11 introduced the so-called third-party equivalence principle, also known as the “white list”.<sup>95</sup> The idea was to indicate those jurisdictions where AML/CTF policy was equivalent to the EU in order to pass customers from those countries through lighter CDD checks. The jurisdictions of the “white list” are chosen and agreed by the MS, which makes the list acceptable and harmonised across the EU.<sup>96</sup> Worth noting, the idea of having such “white list” existed only in the Third AML Directive and was abolished already in the Fourth.

In comparison with AMLD3, FATF recommended granting exemption from the regular CDD not only to the legal professionals but to all DNFBPs that were effectively controlled as to their compliance with AML policy, as well as specific products and services, where it was least likely to be used in illicit purposes<sup>97</sup>. This constitutes a demonstrative example of the EU’s thorough and serious approach towards ML/CTF.

Notably, the covered persons and entities were reluctant to apply the SDD procedure but preferred to pass all their customers through the regular CDD. The justification was based on the entities’ anxiety that competent authorities could question the entities’ activities in case when the suspicious transaction reporting was missing. It is seen that application of SDD could add a level of complexity to the due diligence procedure, as entities would have to double check if a customer is truly eligible for SDD without negative consequences.<sup>98</sup>

Alternatively, the Directive envisaged enhanced due diligence (EDD) for high-risk customers, which, put simply, is additional attention from the financial institutions. The measures to monitor and reduce the risks include a closer review prior opening of an account and processing of the transaction along with more frequent ongoing checks.

Provision of services to high-risk groups is traditionally expensive and requires from financial institutions, in particular from private banks, additional measures to be taken. Exactly for these purposes, the Wolfsberg group has been created due to consideration that private banks were not

<sup>93</sup> Dennis Cox, *Handbook of Anti Money Laundering* (Wiley, 2015), p.71. Available at: doi: 10.1002/9780470685280.fmatter

<sup>94</sup> Directive 2005/60/EC, *supra* note 77, Article 11.

<sup>95</sup> *Ibid.*, Article 11(1).

<sup>96</sup> Common Understanding Between EU Member States on the Procedure and Criteria for the Recognition of Third Countries Equivalence Under Directive 2005/60/EC on the Prevention of the Use of the Financial System for the Purpose of Money Laundering and Terrorist Financing. Available at: [http://ec.europa.eu/internal\\_market/company/docs/financial-crime/3rd-country-common-understanding\\_en.pdf](http://ec.europa.eu/internal_market/company/docs/financial-crime/3rd-country-common-understanding_en.pdf). Last accessed 7 May 2018.

<sup>97</sup> FATF Recommendation 2003, *supra* note 69, p. 21.

<sup>98</sup> Deloitte Study, *supra* note 81, p. 288.

sufficiently involved in the fight against ML.<sup>99</sup> However, the discussion of the Wolfsberg Group falls outside the scope of this Thesis, as it is mostly known for the development of the KYC and AML/CFT policies designed to be part of risk management strategy of financial institutions.

The high-risk status of customers does not as such mean that these customers are criminals, because otherwise, for obvious reasons, provision of services to them would have been prohibited. To compensate risk, increased scrutiny and vigilant control over high-risk profiles is probably the only solution to keep them in the financial system. Therefore, detailed instructions on the high-risk management are the only acceptable way to safeguard the financial system from misuse whilst letting high-risk customers open accounts and make transactions.

As for the Directive, Article 13 specifies special occasions when financial institutions are obliged to pass the customer through an enhanced customer due diligence. The article explicitly covers three groups of high-risk profiles: when the customer is not present for identification, when the banking relationship with the corresponding account goes beyond the borders of the EU and in case of politically exposed persons (PEPs).<sup>100</sup>

Unlike previous Directives, AMLD3 lists specific measures so as to atone each case of a high-risk profile. For customers unavailable for physical identification, measures are focused on additional information gathering from reliable sources.<sup>101</sup>

In order to maintain cross-frontier banking relationships, financial institutions shall collect sufficient information to understand the true nature of the respondent's business and verify its reputation through publicly available sources. Further, it is required to confirm the AML/CTF policy of another financial institution and document obligations of each of them.<sup>102</sup>

Interestingly, the Directive explicitly obliged the employees of financial institution to obtain approval from the senior management in order to continue such relationships. The author supposes that the background for such rule comes from the cases where the banks cooperated with money launderers, and the senior management denied responsibility during the criminal investigation, arguing that they never knew that illegal activity was taking place at their institution.<sup>103</sup>

## 5.5. Politically exposed persons

The last group of the high-risk customers provided in Article 13 is politically exposed persons (PEPs) from other Member States or the third countries. The introduction of PEPs not only played an important role in the formation of the modern European AML policy, but became the main aspect of the international AML strategy as a whole. Politically exposed persons were specifically tackled in the new FATF Recommendations and were rapidly translated into the European Union legislation. PEPs are defined as “individuals who are or have been entrusted

---

<sup>99</sup> Doug Hopton, *Money Laundering Concise Guide for all business* (Gower Publishing, 2009), p.17.

<sup>100</sup> Directive 2005/60/EC, *supra* note 77, Article 13.

<sup>101</sup> *Ibid.*, Article 13(2).

<sup>102</sup> *Ibid.*, Article 13(3).

<sup>103</sup> *Ibid.*, Article 13(3)(c).

with prominent public functions [at a senior level in a foreign country]”<sup>104</sup> as well as their family relatives and close associates.

For example, PEPs are the Head of States, Members of high-level courts, Ambassadors and Members of Parliament. Generally, there are no difficulties regarding the primary definition of PEPs, but rather with relatives and close associates, as these groups are not clearly defined in the Directive and thus could be interpreted widely.

Another problem is that commercial databases used by entities to perform due diligence might be incomplete for several reasons: e.g., commercial databases might not contain data on family members and close associates of the PEP, or there might be no publicly available information to verify the source.<sup>105</sup> It is further unclear what should be the status of individuals who are no longer entrusted with prominent position, that is, whether they qualify or do not qualify as PEPs. Article 3(9) states that PEPs are “persons who *are* or *have been* entrusted with prominent public functions.”<sup>106</sup> This might be interpreted in a way that, once an individual is classified as a PEP, there is no way he or she could change their status, even, say, 20 years after one has left the position. Such interpretation could easily become a heavy burden on the financial system, as it requires constant monitoring and database updates. Finally, due to rotation of politicians, the database which contains current and previous PEPs could become onerous to manage and guarantee the privacy of such data.

The PEP status also requires additional measures to be taken in order to ensure that there is no exploitation of the senior position or involvement in bribery and corruption activities, which is a logical continuation of the scope extension. It implies that the financial institutions should have such a risk management system that detects PEPs and requires approval from the senior management prior the establishment of business relationships (the same approach as with cross-frontier cooperation). Additional measures shall constitute verification of the funds’ source and ongoing due diligence.<sup>107</sup> In general, the potential risk that PEPs bear and the influence of the politically exposed customers justify the alertness of the legislature.

To conclude, the flexibility of due diligence is the main advantage of categorization of the customers, which allows to reduce the costs and reallocate the resources wisely, as there is no need to examine the customer which is already known to fall into the low-risk category. Instead, this allows doubling check those customers who might pose an actually serious risk.

## 5.6. Beneficial ownership

During the due diligence procedure, a beneficial owner shall be established. Although the concept of the beneficial ownership has been seen in the previous Directives<sup>108</sup>, it was not considered as important as with the risk-based approach. In this connection, Greek lawyer Pavlos Neofytou Kourtellos points out that the importance of the principle coupled with a big concern around

<sup>104</sup> *Ibid.*, Article 3(9) and Recital 25.

<sup>105</sup> Deloitte Study, *supra* note 81, p.95.

<sup>106</sup> Directive 2005/60/EC, *supra* note 77, Article 3(9)

<sup>107</sup> The FATF Recommendation 2003, *supra* note 69, Recommendation 6.

<sup>108</sup> The initial concept was introduced but neither First AML Directive nor Second AML Directive contained clear understanding of beneficial ownership or regard beneficial ownership as a fundamental part of customer identification

beneficial ownership creates a tendency to use legal owners as a façade and disguise the real beneficial entity.<sup>109</sup>

The Third AML Directive introduced clear definitions and rules of identification. According to Article 3(6), a beneficial owner shall mean an exclusively natural person, who ultimately owns, controls and on whose behalf transactions are executed.<sup>110</sup> Therefore, during the due diligence procedure, financial institutions shall perform the risk-based investigation to find not just the legal holder of the account, but its *factual controller*. The Article also specifies the indicators of a person who can be classified as beneficiary. In case of corporate entities, for instance, it is a person who ultimately holds the direct or indirect control over shareholding/controlling or ownership interest over 25% threshold.

Alternatively, beneficial ownership of legal entities, including trusts and other legal arrangements which manage funds, is established through a more complicated procedure. The basic rule remains – a person who controls more than 25% of a property of the entity shall be considered as a beneficial owner. Additional provisions concern contracts where beneficiaries have already been predetermined. In the case when beneficiary individuals are not determined yet, a class of person in whose main interest a legal entity operates or was created in a first place shall be considered to be beneficial owners.<sup>111</sup>

Those rules, however, do not preclude financial institutions from setting a lower threshold. They have the discretion to set their own information collection procedures on beneficiary within the framework of the Directive. In fact, Article 43 shows the willingness to lower the 25% threshold, which, however, was never implemented.<sup>112</sup>

A logical continuation of the risk-based approach is that identification of the beneficial owner shall be established before the commencement of business relationships or at the time of the transaction. The risk-sensitive approach emphasises the need to understand the structure of the respondent entity and assess its the risk through the prism of critical analysis. By the same token, companies characterized by hidden natural persons and non-transparent transactions leading to Non-Cooperative Countries or Territories (NCCTs) shall be deemed as high-risk profiles, regardless of the success of identification.<sup>113</sup>

Beneficial ownership was created as a purely AML notion and raised interpretive issues on national levels, as it was not the term commonly used in company law, civil law, etc. Even more, complexity was brought by the external nature of the beneficial ownership, such as gaining information on a foreign client and identification of a legal structure of a foreign company.<sup>114</sup>

---

<sup>109</sup> Pavlos Neofytou Kourtellos, “Implications of the Third Money Laundering Directive. The Cyprus perspective,” (2014), p. 9. Available at:

<https://www.kourtelaw.com/uc/wp-content/uploads/2014/02/Implications-of-the-3rd-Money-Laundering-Directive.pdf>. Last accessed 7 May 2018.

<sup>110</sup> Directive 2005/60/EC, *supra* note 77, Article 3(6)(a).

<sup>111</sup> *Ibid.*, Article 3(6)(b).

<sup>112</sup> *Ibid.*, Article 43.

<sup>113</sup> Directive 2005/60/EC, *supra* note 77, Article 9.

<sup>114</sup> Indranil Ganguli, “The Third Directive: Some Reflections on Europe’s New AML/CFT Regime,” *Banking & Financial Services Policy Report, Volume 29, Number 5* (May 2010), p. 5.



Generally, one may conclude that beneficial ownership principle introduced by AMLD3 and FATF was applicable mostly to simple scenarios.<sup>115</sup> The complex structures of the entities, however, highlighted its deficiencies, as means of the identification were to some extent effective regarding locally based companies and often impractical regarding the companies with numerous layers of intermediate entities located in several jurisdictions.<sup>116</sup>

Thus, to conclude, the Third AML Directive became the breakthrough in the whole European AML policy, as it introduced an entirely new, unprecedented view at the AML in general and specifically at the customer identification with the due diligence procedures. However, as this was the first step in this new area, certain aspects appeared to be raw and required improvement, brought by the new FATF Recommendation and, subsequently, the Fourth AML Directive – discussed further below.

## 6. ENHANCED RISK-BASED APPROACH

### 6.1. FATF Recommendations of 2012 as a basis for AMLD4

The financial world has changed, the means of money laundering and terrorist financing crimes have altered as well. FATF concluded that, in order to effectively fight illicit money flows globally, predefined laws are no longer sufficient to cover the variety of schemes and methods used by the money launderers.<sup>117</sup> It was considered that constant evaluation, identification, apprehension and mitigation of ML/TF risks were the only solution to adopt effective measures against those risks.<sup>118</sup>

Hence, the main change brought by the FATF Recommendation of 2012 was a greater emphasis on the risk-based approach. In other words, a mixed approach (composed of the elements of both approaches) of the AML/CTF rules under the previous FATF policy shifted to the pure risk-based approach. Traditionally, the European AML regulation successfully mirrored FATF Recommendations, which also in this case resulted in the accelerated adoption of the risk-based approach in the EU. Put differently, customer due diligence, transaction monitoring and many other measures lost their rigid forms in favour of the dynamic risk assessment.<sup>119</sup>

<sup>115</sup> Deloitte Study, *supra* note 81, p. 64.

<sup>116</sup> Annex 4.

<sup>117</sup> The Financial Action Task Force (FATF). Financial Action Task Force Annual Report 2011- 2012 (2012), p.7. Available at:

<http://www.fatf-gafi.org/media/fatf/documents/brochuresannualreports/FATF%20annual%20report%202011%202012%20website.pdf>. Last accessed: 7 May 2018.

<sup>118</sup> Jennifer Hanley-Giersch, “The Fourth EU AML/CTF Directive: A holistic risk-based approach,” *Acams Today September-November 2015*, p. 75. Available at:

[http://www.globalriskaffairs.com/wp-content/uploads/2015/09/The-Fourth-EU-AML-Directive\\_A-Holistic-RBA-Approach.pdf](http://www.globalriskaffairs.com/wp-content/uploads/2015/09/The-Fourth-EU-AML-Directive_A-Holistic-RBA-Approach.pdf). Last accessed: 7 May 2018.

<sup>119</sup> 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, *OJL 141/73*, Recital 4. Available at: [http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:L\\_2015\\_141\\_R\\_0003&from=ES](http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:L_2015_141_R_0003&from=ES). Last accessed: 7 May 2018.

Recommendation 1 has clearly set the purpose of the new policy:

This approach should be an essential foundation to efficient allocation of resources across the anti-money laundering and countering the financing of terrorism (AML/CFT) regime and the implementation of risk-based measures throughout the FATF Recommendations.<sup>120</sup>

Another issue that was tackled by FATF was beneficial ownership. The Recommendations suggested an information-oriented way to strengthen the measures against the lack of transparency and deficiencies of the previous regulation. It also imposed a minimum requirement on identity information (such as name, proof of incorporation, list of directors, etc.) and sanctioned a special register of shareholders and members of the legal entities.<sup>121</sup> Special attention has been devoted to the storage of the customer information in order to ensure its accessibility to the competent authorities.

## 6.2. Background and scope

As to the material scope, the Directive was amended to encompass more predicate offences of ML/TF crimes.<sup>122</sup> According to FATF, the notion of “criminal activity” has been enlarged to cover tax crimes as well. While it is a logical result of the creeping policy of the AML Directives, the efficiency of having the Directive with such an expansive scope might be questioned.

Additionally, electronic and virtual money products have also been included in the scope. The introduction of electronic money products was mostly justified by its extensive popularity, especially among criminals and money launderers.<sup>123</sup> Electronic money reduces transparency and is commonly anonymous. Moreover, monitoring capacities of the electronic money institutions are not coherent; hence, it might be impossible to evaluate customers and transactions according to AML/CTF standards.<sup>124</sup>

As to the personal scope, the first thing one notices when reading the Directive is an elaborate Article 2 (scope and definitions). As it was seen in other European AML Directives, the scope of each next Directive keeps expanding to impose obligations on more entities. The Fourth

---

<sup>120</sup> The Financial Action Task Force (FATF). The FATF Recommendations 2012, February 2012, Recommendation 1. Available at: [http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF\\_Recommendations.pdf](http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF_Recommendations.pdf). Last accessed: 7 May 2018.

<sup>121</sup> Neil Jeans, “FATF Recommendations: What Do They Mean for the Corporate Treasurer?” *Thomsons Reuters. Risk Management Solutions*. Available at: <https://financial.thomsonreuters.com/content/dam/openweb/documents/pdf/financial/special-report-for-corporate-treasurers.pdf>. Last accessed: 7 May 2018.

<sup>122</sup> Directive 2015/849, *supra* note 119, Article 3(4)(f)

<sup>123</sup> The Financial Action Task Force (FATF). Money Laundering Using New Payment Methods (October 2010), p.52. Available at: <http://www.fatf-gafi.org/media/fatf/documents/reports/ML%20using%20New%20Payment%20Methods.pdf>. Last accessed: 7 May 2018.

<sup>124</sup> Report From the Commission to the European Parliament and the Council on the assessment of the risks of money laundering and terrorist financing affecting the internal market and relating to cross-border activities, COM(2017) 340 final, 26.6.2017, p.4. Available at: [http://ec.europa.eu/newsroom/document.cfm?doc\\_id=45319](http://ec.europa.eu/newsroom/document.cfm?doc_id=45319). Last accessed: 7 May 2018.

Directive is not an exception: the new group of entities has been added to the scope of AMLD4 scope – providers of gambling services.<sup>125</sup>

Previous AML regulations contained only casinos, but this time the EU went further and covered all types of services involving “wagering a stake with monetary value in games of chance.”<sup>126</sup> However, the Member States were granted discretion to provide partial or full exemptions to gambling providers on the basis of a proven low risk.<sup>127</sup>

Historically, various gambling services were regarded as exposed to ML risks. Land-based betting and poker are vulnerable to ML due to lack of appropriate control. The key characteristic of such gambling activities is a substantial amount of fast and anonymous transactions in cash or on a peer-to-peer basis, which is – obviously – not regulated effectively.

Online gambling is considered as a high-risk activity due to substantial non-face-to-face component and a large number of transactions. Not rarely online gambling platforms offer anonymous payment methods to ensure privacy of their customers, yet, from the AML perspective, this complicates the tracking of transactions.<sup>128</sup>

### **6.3. Risk-based approach crystallised**

As already noted above, the Fourth Directive is characterized by the shift from the mixed (rule-based and risk-based) to the enhanced risk-based approach, which assesses the risk on the multidimensional scale. In other words, the way of implementation of the risk-based approach has been altered. One may see that the development of the risk-based approach brought more flexibility for the AML policy, but it should be noted that, at the price of flexibility, it became more difficult for the entities to define what kind of specific measures organisations need to put in place in order to comply with the AML/CTF policy.<sup>129</sup>

The key feature of the enhanced risk-based approach under AMLD4 is the following: institutions are obliged to identify, understand and mitigate their ML risks with no reference to the good old rulebook that has been available earlier. The rulebook served as a guidance, especially in cases of dilemma between simplified and enhanced due diligence procedure. Now, organisations shall choose suitable procedures and evaluate risks on their own.

Additionally, all institutions are required to define their parameters of risk assessment, because they are now accountable for any decision made under their own risk-based evaluation. According to Recital 22 of the Directive, risk-based approach is not “an unduly permissive option for the Member States and obliged entities”<sup>130</sup> but rather the evidence-based decision-making tool in order to fight AML/CTF risks.<sup>131</sup>

<sup>125</sup> Directive 2015/849, *supra* note 119, Article 2(3)(f).

<sup>126</sup> *Ibid.*, Article 2(14).

<sup>127</sup> *Ibid.*, Article 2(2).

<sup>128</sup> Commission Report on the assessment of the risk of money laundering and terrorist financing, *supra* note 124, p.4.

<sup>129</sup> *Ibid.*, p.11.

<sup>130</sup> Directive 2015/849, *supra* note 119, Recital 22.

<sup>131</sup> Jennifer Hanley-Giersch, “The Fourth EU AML/CTF Directive: A holistic risk-based approach,” *Acams Today September-November 2015*. Available at:

Another amendment brought by the Fourth Directive is the introduction of the National Risk Assessment. The goal of the innovation is to introduce a supranational body to monitor ML activity in the EU. The content of such reports is stated in Recital 21:

In the risk assessment, Member States should indicate how they have taken into account any relevant findings in the reports issued by the Commission in the framework of the supranational risk assessment.<sup>132</sup>

Moreover, according to Article 8, the Member States shall oblige covered entities not only to identify, assess and understand ML risks, but also to keep them updated and available to competent authorities. Article also specifies the factors that shall be taken into consideration during the risk assessment: customer, geographic areas, products, services, transaction and delivery channels.<sup>133</sup> Such thorough risk assessment, as well as AML policy and controls, shall mitigate and manage AML/CTF risks.

Eventually, collected information is processed by the European Commission and published in the form of the Supranational Risk Assessment Report, which is intended to be “[the report] of the risks of ML and TF affecting the internal market and relating to cross-border activities.”<sup>134</sup> It seems that the EU has finally recognized the volatility of the financial sectors among the Member States and now keeps its hand on the pulse of the newly emerging tendencies, such as cryptocurrencies or crowdfunding platforms due to their risky and unpredictable nature.<sup>135</sup>

The customer due diligence has been amended as well. One of the oldest rules of the European AML Directives, i.e. the threshold of 15 000 EUR in cash transaction, experienced tightening – it was reduced to 10 000 EUR.<sup>136</sup> Mathematically, the reduction constitutes one-third of the previous threshold. However, from the macroeconomic point of view, the inflation gradually reduced the value of 15 000 EUR. Obviously, the amount of 15 000 EUR in 2015 (the year of the adoption of the Fourth Directive) does not hold the same value as in 1991 (when the rule was originally created).<sup>137</sup> The “real” value of 15 000 EUR in 1991 approximately equals to 28 000 EUR as of late 2015 due to a constant increase in consumer prices.<sup>138</sup> Ironically enough, the reduction of the threshold by one third in practice meant its historical diminution almost by three times. The reason to lower the threshold, however, is self-evident – the regulator wanted to increase control over the financial flows in the EU.

An additional concern is the wording used in Article 2(3)(e), namely, “several transactions which appear to be linked”. As there is no harmonised definition of the “link” provided by the Directive, it creates ambiguity in the implementation of the provision.<sup>139</sup>

---

<http://www.globalriskaffairs.com/wp-content/uploads/2015/09/The-Fourth-EU-AML-Directive-A-Holistic-RBA-Approach.pdf>. Last accessed: 7 May 2018.

<sup>132</sup> Directive 2015/849, *supra* note 119, Recital 21.

<sup>133</sup> *Ibid.*, Article 8.

<sup>134</sup> Commission Report on the assessment of the risk of money laundering and terrorist financing, *supra* note 124, p. 1

<sup>135</sup> European Commission. “Strengthened EU rules to tackle money laundering, tax avoidance and terrorism financing enter into force,” 26 June 2017. Available at: [http://europa.eu/rapid/press-release\\_IP-17-1732\\_en.htm](http://europa.eu/rapid/press-release_IP-17-1732_en.htm). Last accessed: 7 May 2018.

<sup>136</sup> Directive 2015/849, *supra* note 119, Article 2(3)(e).

<sup>137</sup> Directive 91/308/EEC, *supra* note 25, Article 3(1).

<sup>138</sup> Annex 5.

<sup>139</sup> Deloitte Study, *supra* note 81, p. 287.

In AMLD4, simplified due diligence was amended in the spirit of the enhanced risk-based approach too. Under the Third Directive, SDD was supplemented with a quite lengthy list of automatically exempted entities, such as publicly traded companies or governmental institutions.<sup>140</sup> Contrary to that, the Fourth Directive offers no such list, but instead *implies* individual risk assessment for every case. According to Article 15, decisions on the application of SDD now should be justified based on the risk-based evaluation and supported by appropriate documentation.<sup>141</sup>

The new SDD based on individual case assessment is also backed by the risk factor provided in Annex II to the Directive.<sup>142</sup> There are five main risk factors suggested by the non-exhaustive list: customer, product/service, transaction, delivery channel, and geographical risks.<sup>143</sup> Interestingly, customer risk may be lowered by the fact that company is publicly listed, yet, this is just one of many factors that shall be taken into consideration. Likewise, governmental institutions are not anymore automatically exempt from the regular customer due diligence simply because of their status – they shall go through risk assessment anyway.

Generally, it is considered to be a positive shift from the national interpretation of the rules to the detailed explanation of the rules within the Directive itself. It fosters harmonisation of the rules within the EU, reduces the vagueness, thus leaving less room for diverging interpretations.

Finally, enhanced due diligence was treated in the more prescriptive way. As mentioned in the previous section, the “white list” has been abolished but, surprisingly, the “black list” has been introduced. As the name suggests, such list contains jurisdictions with absent or low AML/CTF policy.<sup>144</sup>

Basically, EDD is now applicable in any case when customers from designated high-risk countries are processed.<sup>145</sup> Additional factors to be examined are the same as for SDD: customer, product/service, transaction, delivery channel, and geographical risks.

The Directive also provides examples of high-risk factors. For example, a customer who is involved in cash-intensive business shall be considered to be a potentially high-risk customer. Similarly, those residing in countries under EU/UN sanctions shall be considered high-risk customers as well.<sup>146</sup>

A particular case of EDD – politically exposed persons – has also been amended in the spirit of the enhanced risk-based approach. In Article 3<sup>147</sup>, the definition of politically exposed persons has become elaborate, contrary to one in AMLD3. It gives a clear description of the concept of PEPs and, more importantly, provides a definition of family members and close associates, which was marked as troublesome in previous legislation.

The new definition under AMLD4 broadens the notion and covers not only foreign PEPs (as has been the case before) but also introduces domestic PEPs, which goes in line with the 2012 FATF

---

<sup>140</sup> Directive 2005/60/EC, *supra* note 77, Article 11.

<sup>141</sup> Directive 2015/849, *supra* note 119, Article 15.

<sup>142</sup> *Ibid.*, Annex II.

<sup>143</sup> *Ibid.*

<sup>144</sup> *Ibid.*, Article 9.

<sup>145</sup> *Ibid.*, Article 18(1).

<sup>146</sup> Directive 2015/849, *supra* note 119, Annex III.

<sup>147</sup> *Ibid.*, Article 3(9).

Recommendations<sup>148</sup> and Article 52 of the 2003 United Nations Convention against Corruption.<sup>149</sup>

In practice, the above-described extension resulted in the need of the covered entities to re-examine and reclassify its customers as well as apply additional EDD measures.<sup>150</sup> Furthermore, Article 22 clarified the confusion with regard to the status of those PEPs who are no longer entrusted with a prominent public position: such persons shall be deemed to be PEPs and it is required to apply risk-sensitive procedures for at least 12 months and until such time when a person no longer poses risk associated with their political position.<sup>151</sup>

## 6.4. Beneficial ownership

The “25% rule of beneficial ownership” introduced in the AMLD3 was good on paper but faced a lot of difficulties in the application phase.<sup>152</sup> The problems arising out of this rule even outweigh the benefits, especially when it comes to the complex structure of the entity. As a result, the identification of the beneficial ownership might depend on different technical factors outside AML/CTF policy, such as diverging opinions on interpretation, incoherent risk evaluations, etc. Additionally, when the structure of the company is complex and its owners are scattered across various jurisdictions, the outcome of the beneficial owner identification is unpredictable.<sup>153</sup>

As it was found in the report on the implementation of the Third AML Directive, there are two options for how the Member States calculate beneficial ownership.<sup>154</sup> Option one also referred to as “top down”, defines the beneficial owner as a person who possesses or controls at least 25% of customer’s share or property. Option two, referred to as “bottom up”, defines the beneficial owner as a person who possesses or controls at least 25% of customer’s share or property *or if previous is not applicable*, as any other entity that owns at least 25% of the customer. The second option requires more efforts to identify the beneficiary, as it aims at finding the “lowest” possible beneficial ownership. The ultimate choice, however, depends only on the interpretation of the Directive by the MS. To illustrate, 13 Member States followed the “top down” approach, whereas 11 Member States followed the “bottom up”.<sup>155</sup>

<sup>148</sup> FATF Recommendation of 2012, *supra* note 114, Recommendation 12.

<sup>149</sup> United Nations Convention against Corruption, 9 December 2003. Available at:

[https://www.unodc.org/documents/brussels/UN\\_Convention\\_Against\\_Corruption.pdf](https://www.unodc.org/documents/brussels/UN_Convention_Against_Corruption.pdf). Last accessed: 7 May 2018.

<sup>150</sup> Daren Allen, “Comparison Table: Fourth Money Laundering Directive (4MLD)– Changes From 3MLD”. *Thomson Reuters Regulatory Intelligence*, October 21, 2016.

<sup>151</sup> Directive 2015/849, *supra* note 119, Article 22.

<sup>152</sup> Directive 2005/60/EC, *supra* note 77, Article 3(6)(a)(I).

<sup>153</sup> Hanley-Giersch, “Holistic risk-based approach”, *supra* note 125, p. 77. Available at:

<http://www.globalriskaffairs.com/wp-content/uploads/2015/09/The-Fourth-EU-AML-Directive-A-Holistic-RBA-Approach.pdf>

<sup>154</sup> Annex 6.

<sup>155</sup> European Bank Authority (EBA), European Securities and Markets Authority (ESMA) and European Insurance and Occupational Pensions Authority (EIOPA), Report on the legal, regulatory and supervisory implementation across EU Member States in relation to the Beneficial Owners Customer Due Diligence requirements under the Third Money Laundering Directive [2005/60/EC], *JC/2011/096 AMLTF/2011/05* (2011), p. 10. Available at: [https://eiopa.europa.eu/Publications/Reports/JC\\_2011\\_096\\_AMLTF\\_2011\\_05\\_-\\_UBO\\_Report\\_.pdf](https://eiopa.europa.eu/Publications/Reports/JC_2011_096_AMLTF_2011_05_-_UBO_Report_.pdf). Last accessed: 7 May 2018.

Consequently, the differences in implementation of the Third Directive are hardly harmonised, and may even preclude the Member States from cooperation in AML field, as well as increase compliance expenses.

In the Fourth Directive, it was considered vital to provide a common understanding of the concept of risk-based customer and of the beneficial ownership identification procedures in order to ensure stability and efficiency of AML policy.

The impetus for the development of the beneficial ownership identification has traditionally been brought by FATF. According to the FATF Interpretive Note to the Recommendation 10, there are two main stages in the identification of the beneficial ownership. First is a natural person who controls more than 25% or more of the entity in question.<sup>156</sup> If there are any doubts regarding the identified person, that is, whether the identified person is a real beneficiary or when there are no *natural* persons found at all, the institution shall search for other means to identify the beneficiary. The alternative solution in the case when natural persons are unidentifiable is that the institution shall identify the senior manager of such company and consider him or her to be the beneficial owner.<sup>157</sup>

This new solution to the beneficial ownership identification suggested by FATF is truly in line with the enhanced risk-based approach, as the emphasis is set on finding natural persons and not on the shares/percentages in the entity. This is another example of the dynamic risk assessment rather than the static rulebook attitude.

## 6.5. Beneficial ownership register

As pointed above, under the Third AML Directive, collection of information needed for the beneficiary identification became problematic for the covered institutions. Fortunately, the Fourth Directive offers a solution for this issue by introducing the beneficial ownership register.

The functions of such register are explained in paragraphs (1) and (3) of Article 30 of the AMLD4:

Member States shall ensure that corporate and other legal entities incorporated within their territory are required to obtain and hold adequate, accurate and current information on their beneficial ownership, including the details of the beneficial interests held. Member States shall ensure that the information ... is held in a central register in each Member State.<sup>158</sup>

Thus, information stored in the register could be accessed by the competent authorities, FIUs and “any persons or organisation who can demonstrate legitimate interest.”<sup>159</sup> Authorities and FIUs would certainly benefit from such an innovation, as this allows them to easily monitor ML/TF situation and access the needed financial information. According to Article 30(5), the content

---

<sup>156</sup> The Financial Action Task Force (FATF), Transparency and Beneficial Ownership (October 2014), p. 15. Available at: <http://www.fatf-gafi.org/media/fatf/documents/reports/guidance-transparency-beneficial-ownership.pdf>. Last accessed: 7 May 2018.

<sup>157</sup> FATF Recommendation of 2012, *supra* note 120, Interpretive note to Recommendation 10.

<sup>158</sup> Directive 2005/60/EC, *supra* note 77, Article 30(1) and Article 30(3).

<sup>159</sup> *Ibid.*, Article 30(5).

includes the name, date of birth, nationality, country of residence and information of beneficial ownership percentages.<sup>160</sup>

However, another group of persons to whom access might be granted is being introduced, namely, the persons who can demonstrate a “legitimate interest”. This, however, is a controversial solution.<sup>161</sup> Although such information is not considered sensitive and could potentially be obtained from other sources, two things remain unclear: first, why would anyone apart from authorities need it, and, second, how exactly the legitimate interest would be verified.<sup>162</sup>

The core principle of the Fourth AML Directive is that the risk-based approach remains valid even when the information has been already collected. This is enshrined in Article 30(8), which provides that, even though the information on the customer has already been collected and stored in the registers, the entities shall continue customer due diligence on these persons and could not refrain from repeated risk evaluation.<sup>163</sup>

On the one hand, the beneficial ownership register is one of the few – if not the only – solution allowing to keep beneficiaries information updated and accessible to the institutions and relevant authorities. On the other hand, such registers somewhat alter the nature of the financial system, making it not just commercial but also surveillance actor. Further, information is stored in the electronic database, it could be attacked, resulting in vulnerable financial information misuse.

To conclude, the Fourth AML Directive has put emphasis on transparency, cooperation, information exchange, enhanced monitoring procedures and a tailored approach towards customer identification and due diligence.

Despite the fact that both the Third and the Fourth AML Directives pursue the same aim and apply the same approach, they are still somewhat different in nature. While the Third AML Directive is sometimes called revolutionary – which it truly is because of novelty it introduces – the Fourth Directive is of a more evolutionary character, as it deepens the notion of the risk-based approach, the central point of the next chapter.

## **7. THIRD AND FOURTH AMLD: AN EVEN CLOSER LOOK AT THE RISK-BASED APPROACH**

### **7.1. Methodology of risk evaluation**

The risk-based approach is the governing principle of the European AML/CTF policy since 2005. However, the genuine value to the risk-based approach is given by the prerequisites that have to be understood and implemented not only by the covered entities, but also by the regulator.

---

<sup>160</sup> *Ibid.*

<sup>161</sup> William Fry, “New Rules on Beneficial Ownership Register – Immediate Action Required,” November 2016, p.2. Available at: <https://www.williamfry.com/docs/default-source/ezine-print-friendly-documents/new-rules-on-beneficial-ownership-register.pdf?sfvrsn=2>. Last accessed: 7 May 2018.

<sup>162</sup> Directive 2005/60/EC, *supra* note 77, Article 30(5).

<sup>163</sup> *Ibid.*, Article 30(8).



The first prerequisite is that the management of financial institutions is responsible for providing appropriate and proportionate risk evaluation systems. Appropriate, as it ensures that actions taken by the institutions during the due diligence procedure are adjusted to the specific type of business and to the clients' activities. Proportionate, because institutions have to recognise that, as the risk increases, so shall the intensity of the measures to mitigate the risk.<sup>164</sup>

The second prerequisite is that each institution has to adapt its own risk evaluation system to the needs of the institution, making it unique. Before establishing AML/CTF system, the institution must analyse and understand the environment where it operates, i.e. its risk tolerance policy and the overall risk profile of the business. It is the choice of the institution to set their risk tolerance policy and hence apply lower AML/CTF measures comparing with competitors with lower risk tolerance. Such approach is in line with AML laws until the management of the financial institution can demonstrate and explain how their systems are proportionate and appropriate.<sup>165</sup>

When prerequisites are in place, next component which distinguishes the risk-based approach from the rule-based one is risk profiling. In fact, the Fourth AML Directive contains several explicitly mentioned risk factors to be taken into consideration during the risk evaluation: customer risks, geographic area risks, product, service and transaction risk, and delivery channels risks.<sup>166</sup>

Customer risks are those risks that are coming from the customer himself. It encompasses the source of the income, legal or natural person, NPO or PEPs status, past activity records, beneficial ownership structure, etc. Before the implementation of the risk-based approach, customer risks were the centre of customer identification, i.e. the only factor which has been analysed by the institution.

High geographic area risk are the countries with weak legislation against AML/CTF, which pose a risk to the international anti-money laundering system. Alternatively, the risk might come from the high levels of corruption, terrorist activity, unstable political regime or when the jurisdiction is included in the FATF Non-Cooperative Countries and Territories list or sanctioned by UN or EU. It is the obligation of the financial institution to monitor the political/legal/economic condition of the country where its customers reside.<sup>167</sup>

Products, services and transactions risks usually refer to the products and services stemming from innovative technologies, usually characterized by customer anonymity. For example, electronic money, international wire transfer or "stored value" cards offered by the non-financial institution. In turn, the financial institution shall evaluate transactions of such clients in order to quantify the amount of debit-credit operations, the direction of money flows as well as the category of the customer who uses non-financial organisation services. As for the transactions, the institution

---

<sup>164</sup> Marcus Killick, "Implementing AML/CFT measures" that address the risks and not tick boxes", *supra* note 19, p. 211.

<sup>165</sup> *Ibid.*

<sup>166</sup> Directive 2005/60/EC, *supra* note 77, Annex III.

<sup>167</sup> Ernst & Young, "Wind of change: Risk Assessment Anti-Money Laundering, Countering Terrorism Financing, Application of International Sanctions," (2016), p. 2.

Available at: [https://www.apcf.ro/static/files/EY\\_Romania\\_Wind\\_of\\_Change\\_AML\\_Risk\\_Assessment.pdf](https://www.apcf.ro/static/files/EY_Romania_Wind_of_Change_AML_Risk_Assessment.pdf). Last accessed: 7 May 2018.

should also assess the complexity of the operations made by the customer and verify the nature of such transactions: e.g., as high value, cash sensitive etc.<sup>168</sup>

There are methods of provision of services or the product delivery lines which increase ML risks due to the fact that the business is very likely not to know the identity of the clients and not to understand their business activity. Therefore, the financial institution shall evaluate the amount of non-face-to-face transactions and involvement of intermediaries, as it increases ML risks as well. Importantly, a non-face-to-face transaction is not a high-risk factor *itself*. The risk would rather increase where the customer is new, as the financial institution would not know him and would need the time to decrease the level of risk as soon as the information confirming his activity would satisfy the institution.<sup>169</sup>

Under the risk-based approach, the emphasis is placed on the combination of the risk factors. This ensures measures to be proportionate and appropriate because the institution grounds its actions on the numerous characteristics of the customer. In comparison, the rule-based approach would rather stress the importance of the customer risk without analysing other factors that indeed have the same, or sometimes even greater importance, as the latter. Thus, instead of the rule-based approach one-dimensional risk matrix, the risk-based approach offers multidimensional risk evaluation, which tends to be more accurate in terms of resource allocation for the customer identification purposes.<sup>170</sup>

Whilst there are various ways to estimate risk and consequently come up with the risk profile of the customer, there are two variables which are considered to be the most generic way to do it, namely, likelihood and impact. One may argue that such model is simplistic, but using such two variables for a risk profile can be easily constructed. The two-dimensional matrix allows mapping of every risk factor: customer, product or any other, in order to establish the risk that financial institution is going to encounter.

The matrix consists of four quadrants - A, B, C, and D respectively. The risk falling in lower-left quadrant A is the risk characterised by the low likelihood and the low impact of occurring. Hence, the financial institution's efforts to mitigate such risks would be considered as wasted resources due to the fact that it will not result in the lower risk profile of the customer. Of course, it does not imply that the customer is totally risk-free, but rather that the risk would not affect the institution severely.<sup>171</sup>

---

<sup>168</sup> The Wolfsberg Group, Guidance on a Risk Based Approach for Managing Money Laundering Risks (March 2006), p. 5. Available at:

[https://www.wolfsberg-principles.com/sites/default/files/wb/pdfs/wolfsberg-standards/15.%20Wolfsberg\\_RBA\\_Guidance\\_%282006%29.pdf](https://www.wolfsberg-principles.com/sites/default/files/wb/pdfs/wolfsberg-standards/15.%20Wolfsberg_RBA_Guidance_%282006%29.pdf). Last accessed: 7 May 2018.

<sup>169</sup> European Bank Authority, Joint Guidelines under Articles 17 and 18(4) of Directive (EU) 2015/849 on simplified and enhanced 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, *JC 2017 37* (26.06.2017), p. 20. Available at:

<https://www.eba.europa.eu/documents/10180/1890686/Final+Guidelines+on+Risk+Factors+%28JC+2017+37%29.pdf>. Last accessed: 7 May 2018.

<sup>170</sup> Marcus Kilkick, "Implementing AML/CFT measures" that address the risks and not tick boxes", *supra* note 19, p. 211.

<sup>171</sup> Annex 7.

The risks represented in the quadrants B and C are the high likelihood-low impact and high impact-low likelihood respectively. These quadrants are those threats, where the institution shall dedicate efforts to reduce the risk, otherwise it would move to the D quadrant.

The high likelihood-high impact risk in quadrant D are the risks that most likely could not be mitigated at all. In order to achieve this, the financial institution would require implementing strict control measures that would eventually restrict most, if not all, business operations because of the ML/TF threat.

Therefore, AML/CTF by its nature is not a fool proof process. In order to reduce failures, the institutions and regulators must implement dynamic controls and monitor their customers.

The next chapter is dedicated to more advanced systems of the customer identification under the risk-based approach provided by the Fourth AML Directive.

## **7.2.Risk management framework**

In the risk management framework, the evaluation of the risk factors described in the previous chapter is the first step in executing the risk assessment of the customer. In the modern AML/CTF terminology, it is usually referred to as inherent risk. According to the Wolfsberg Group, inherent risk represents the vulnerability of a customer to the ML/TF, sanctions or corruption activity in the absence of any control of the environment implemented.<sup>172</sup>

As every financial institution has its unique balance of risk appetite and strategic objectives (profit, turnover, quality of customers, etc.), inherent risk evaluation may vary depending on the subjective model implemented by the institution. Nevertheless, the assessment procedure of the inherent risk basically constitutes scoring of each factor using the Low - Medium - High scale.<sup>173</sup>

Once the inherent risk is established, the financial institution shall assess the efficiency of the internal controls against the identified risks. There are various policies and control measures to protect the financial institution from the ML/CF threat and guarantee that the risk would be immediately identified. Examples of such controls are designated AML Compliance officers, developed KYC principles, AML/CTF training of the staff, etc. The evaluation of the internal policies allows an institution to estimate its efficiency and raise urgent actions to remedy the loopholes.<sup>174</sup>

Similarly, as with inherent risk evaluation, the findings of each policy or control shall be scored, and when aggregated, represent the institutions' strength of the organisations' ML control. Not rarely, some of the categories are assigned with an additional weight based on the importance recognized by the institution.

---

<sup>172</sup> The Wolfsberg Group, Frequently Asked Questions on Risk Assessments for Money Laundering, Sanctions and Bribery & Corruption, p.18. Available at: <https://www.wolfsberg-principles.com/sites/default/files/wb/pdfs/faqs/17.%20Wolfsberg-Risk-Assessment-FAQs-2015.pdf>. Last accessed: 7 May 2018.

<sup>173</sup> Karima Touil, "Risk-Based Approach Understanding and Implementation. Challenges between Risk Appetite and Compliance," *Acams Today* (2016), p.10. Available at: <http://files.acams.org/pdfs/2016/Risk-Based Approach Understanding and Implementation K Touil.pdf>.

Last accessed: 7 May 2018.

<sup>174</sup> The Wolfsberg Group, Frequently Asked Questions, *supra* note 172, p.11.

Once inherent risk and internal control have been analysed, the last step is evaluation of the residual risk. The residual risk is defined by the Wolfsberg Group as:

the risk that remains after controls are applied to the inherent risk. It is determined by balancing the level of inherent risk with the overall strength of the risk management activities/controls. The residual risk rating is used to assess whether the ML risks within the FI are being adequately managed.<sup>175</sup>

Therefore, the residual risk is crucial for the evaluation process, as it indicates whether ML/TF risks were properly managed by the financial institution and is measured depending on its available resources and capabilities. For example, there is the high-risk customer, but two financial institutions utilise different control and mitigation measures resulting in two different scenarios: first, high-risk but mitigated becoming low or medium-risk customer or, second, high-risk customer, the risk of which is not mitigated due to the policy chosen by the institution.

According to the residual risk evaluation, the financial institution chooses the type of the appropriate customer due diligence procedure: low-risk profiles – simplified due diligence, medium-risk profiles – regular customer due diligence, high-risk profiles – enhanced due diligence. Additionally, according to the residual risk evaluation, the results change the approval authority. In other words, if the customer is evaluated as having a high-risk profile, the financial institution would most likely require direct approval from the AML Committee, whereas for low-risk customer, approval from the regular customer relationship manager would be sufficient.<sup>176</sup>

In practice, financial institutions analyse many factors: the example provided in the Annex is a good illustration of the results of such evaluation.<sup>177</sup> Imagine there is a customer which resides in the United Arab Emirates, which is considered to be a low-risk country from the AML perspective, as there is effective AML/CTF policy in place. However, the company is registered in the British Virgin Islands, which is known as a tax haven and has weak control over companies. Further, the beneficial owner is Iranian. The customer's operational business is import and export of gas/oil products from Iran, which is considered to be a high-risk activity due to the fact that Iran lacks AML/CTF legislation, has high level of corruption and is tied to terrorist financing. It is also known that ISIL was engaged in oil smuggling, using Iran and Kurdistan as an intermediary to sell through.<sup>178</sup> The customer would like to ask for a letter of credit from the financial institution, which might be problematic due to the nature of the partners of such customer.

Thus, the financial institution aggregates the results of the evaluation and scores the customer. In the given case, the institution sets the score of four, which is a high risk. Hence, enhanced due diligence procedure shall be applicable and, for the further cooperation, the approval from the senior manager is required.

---

<sup>175</sup> The Wolfsberg Group, Frequently Asked Questions, *supra* note 172, p.19.

<sup>176</sup> Karima Touil, "Risk-Based Approach," *supra* note 173, p.10.

<sup>177</sup> Annex 8.

<sup>178</sup> D. McElroy, "Iraq Oil Bonanza reaps \$1 million a day for Islamic State; Exclusive: Islamic State strengthens grip on northern Iraq by raising millions from sale of oil through Kurdistan to Turkey and Iran", *The Telegraph*, (2014). Available at:

[www.telegraph.co.uk/news/worldnews/middleeast/iraq/10962160/Iraq-oil-bonanza-reaps-1-million-a-day-for-Islamic-State.html](http://www.telegraph.co.uk/news/worldnews/middleeast/iraq/10962160/Iraq-oil-bonanza-reaps-1-million-a-day-for-Islamic-State.html). Last accessed: 7 May 2018.

### 7.3. Implications of the risk-based approach

The European AML/CTF legislation and FATF Recommendations indeed contributed to the universal fight against ML/TF, however, they also had additional implications on the financial system.

First, financial institutions became very demanding in terms of evidence confirming the low-risk nature of the customer: e.g., small firms with short history would rather be considered high-risk customers. Thus, financial institutions have the grounds to refuse to cooperate with such customer as, theoretically, it might be involved in ML/TF activity.

Second, as already discussed in the previous chapters, the scope of the European AML Directives and obligations of organisations have been extended, which led to de-risking of the financial institutions. In other words, financial institutions cease the existing relationships with customers and close accounts because of a high risk of ML/TF. Today, the implementation of the de-risking can be seen in the Baltic region as well. The Latvian scandal, in which the banks were accused of the service provision to non-resident customers and dealing with transactions suspected of ML, resulted in large fines and liquidation of one the biggest banks in the country. To reduce ML/TF risks, Estonian financial institutions have decided to avoid serving foreign customers and close accounts of the existing ones.<sup>179</sup>

Third, as the consequence of the complex AML regime in the European Union, there are many countries which are considered to be high-risk jurisdictions. This may preclude European businesses from entering into new regions and lead to isolation of the poorer countries beyond the frontier as well. Consequently, it would widen the AML legislation gap.<sup>180</sup>

The last but probably the most important aspect of the European AML policy is the ratio of costs and benefits. The University of Utrecht in its report on the legal and economic effectiveness of the AML/CTF policy attempted to estimate the costs and benefits of AML/CTF policy per EU country.<sup>181</sup> Of course, there are unknown variables, including moral components, which are hard to estimate, but the findings are truly stunning: the costs exceed the benefits by 8-9 times on average.

Furthermore, the University of Utrecht estimated the costs and benefits for a theoretical country with 10 millions of population and a level of price equal to that in the U.S. It is seen that around 50% of the costs are the burden for the private sector to maintain AML/CTF policy in place. It becomes obvious that the measures undertaken by the EU against money laundering are largely inefficient because the benefits (income from fines and confiscations) will never cover the expenses.<sup>182</sup>

---

<sup>179</sup> Aili Vahtla, "E-Residency program under threat as banks closing foreigners' bank accounts," *Estonian National News Portal Eesti Rahvusringhääling*. Available at:

<https://news.err.ee/691549/e-residency-program-under-threat-as-banks-closing-foreigners-bank-accounts>.

Last accessed: 7 May 2018.

<sup>180</sup> Clay Lowery, Vijaya Ramachandran. "Unintended Consequences of Anti-Money Laundering Policies for Poor Countries," *Center for Global Development*, 2015. Available at:

<https://www.cgdev.org/sites/default/files/CGD-WG-Report-Unintended-Consequences-AML-Policies-2015.pdf>.

Last accessed: 7 May 2018.

<sup>181</sup> Annex 9.

<sup>182</sup> Annex 10.

Although the risk-based approach introduced a better customer identification and an enhanced risk management system, a truly effective implementation is not achieved yet. Strict rules of risk assessment as well as a small amount of benefits, especially for the private sector, question the need for such a demanding AML/CTF legislation. However, despite the risk-based approach materialized approximately a decade ago, it had not yet *crystallized* in the rigid structure, leaving the possibility that it will further develop, taking into account the implications that exist today.

## 8. FIFTH AML DIRECTIVE: EXTENDING THE SCOPE OF AML/CTF REGIME IN EU

The first proposal to the Fifth AML Directive was pronounced even before June 2017, the deadline for the implementation of the Fourth AML Directive. The rationale behind the urgency to amend the current AML/CTF legislation is the information found in the Panama Papers, which leaked in April 2016 as well as the belief that electronic money and prepaid cards were allegedly used by terrorists to finance the attacks in Paris in November 2015.<sup>183</sup> As for Panama Papers, it revealed money laundering schemes used worldwide and served as a bad signal for the current AML/CTF legislation, as it might not impose effective and harmonized rules on due diligence procedures as well as perform detailed monitoring of the high-risk jurisdictions.

According to European Parliament Committees Report, the personal scope of the next AML Directive, among minor changes, should be enlarged to introduce new enhanced control over electronic money and prepaid cards. It includes providers of the electronic money (such as Bitcoin, Ethereum, etc.) and its distributors, as well as providers of the exchange between electronic money and fiat currencies.<sup>184</sup> It is proposed to include the providers of custodian wallets, which allow the final customer to access cryptocurrency markets, into the scope. The regulator's intention to cover electronic money and cryptocurrencies is the result of the extensive popularity of such money in the recent years, especially in the fourth quarter of 2017, when capitalisation of the most popular cryptocurrency Bitcoin reached 237.62 billion U.S. dollars.<sup>185</sup> However, the ideology of cryptocurrencies – anonymity and decentralisation – might set a considerable barrier to the effective implementation of the future Directive. The Directives were traditionally created to provide financial institutions with a guidance to AML/CTF policy, but, if the scope is extended to cover cryptocurrencies-related businesses, the financial institutions might find it confusing and hardly applicable to the existing well-established financial sector.<sup>186</sup>

<sup>183</sup> Denis O'Connor, "EU Fifth Anti-Money Laundering Directive: Can Banks Handle It?" Available at: <https://kyc360.com/article/eu-fifth-anti-money-laundering-directive-key-points-banks/>. Last accessed: 7 May 2018.

<sup>184</sup> Report on the proposal for a directive of the European Parliament and of the Council amending Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing and amending Directive 2009/101/EC, COM(2016)0450 – C8-0265/2016 – 2016/0208(COD). Amendments to Article 1. Available at: <http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+REPORT+A8-2017-0056+0+DOC+XML+V0//EN>. Last accessed: 7 May 2018.

<sup>185</sup> Bitcoin - Statistics & Facts. Statista.com. Available at: <https://www.statista.com/topics/2308/bitcoin/>. Last accessed: 7 May 2018.

<sup>186</sup> Denis O'Connor. "EU Fifth Anti-Money Laundering Directive", *supra* note 177.

## CONCLUSION

The evolution of the European AML/CTF legislation provided in this Thesis<sup>187</sup> shows that the transition from the rule-based to the risk-based approach was quite rapid: within one decade, a radical shift took place. One of the purposes of this Thesis was to identify the reasons for the change of European AML regime from the rule-based to the risk-based approach.

The main reason for a quite rapid introduction of the risk-based approach is the apparent failure of the rule-based approach: the latter proved to be very formalistic and did not satisfy the needs of financial control. It contained loopholes that allowed money launderers to bypass the regulations, while the financial institutions applied the minimal effort approach.

Second, the plurality of customer characteristics made rule-based “one-size-fits-all” approach obsolete and unable to adequately evaluate the risks and mitigate them. Third, the overall influence of globalisation somewhat accelerated the shift as well.

Another purpose of this Thesis was to identify the benefits and implications of the new approach.

The risk-based approach is much more efficient, comparing to the previous one. First, it allows for a smarter allocation of resources, where customers are categorised, and groups possessing higher level of risk are being granted bigger attention. Second, risk-based approach is much more flexible, as it provides different mechanisms of risk mitigation for different groups of customers as well as allows the entities to build their own mechanisms of risk assessment. Third, risk-based approach requires active involvement of the covered entities (such as constant customer re-evaluation, creation of registers, etc.), which contributes to the overall security of the financial market. As to the implications, the risk-based approach is quite complex, comparing to the rule-based approach, as it only gives general guidelines without providing concrete detailed procedures. Thus, the burden of creating such individual procedures lies on the financial institutions, which might become problematic in case when it would have to explain why it has chosen this particular method or procedure of risk assessment to the regulator. This also brings the problem of ambiguity: with no clear procedure provided by the regulator, financial institutions and Member States are in some aspects free to interpret and apply the legislation as they deem correct. Second, despite its efficiency, such approach remains very expensive for the private sector (see Annex 10).

Finally, this Thesis aimed to identify how did the transition from the rule-based approach to risk-based approach affect customer identification.

To start with, risk-based approach introduced a new term – due diligence – which was divided into three groups according to the level of posed risk: simplified, regular, and enhance. Such categorisation allows to exercise stricter control over high-risk customers, which, as already noted above, leads to a wiser allocation of resources, as lower-risk customers are not being controlled in as high degree.

Second, enhanced due diligence introduced the notion of politically exposed persons, which contributes to combating of corruption and bribery. Despite the fact that the term was not clear enough when introduced in the Third Directive and had to be clarified in the subsequent one, its

---

<sup>187</sup> Annex 3

inclusion is still an advantage, as the previous – rule-based approach – did not have such specific measure at all.

Third, the risk-based approach introduced a completely new understanding of the beneficial ownership: while, previously, it was enough to indicate the beneficial owner “on paper”, currently, the purpose is to find the ultimate beneficial owner, even if it requires enormous efforts.

Finally, the risk-based approach offered risk scoring instead of the previously applied “checklist model”. Thus, instead of identifying whether the elements of the list are present, these elements are being individually evaluated, which makes the risk assessment multidimensional and more thorough. Thus, all elements are combined, and the whole assessment is no longer based on just one element but on aggregation of elements.

Yet, the future prospects might not be as bright: as the brief analysis of the proposal of the Fifth AML Directive shows, much bigger emphasis is now being put on stricken of control over the financial actors with special attention being given to electronic money/prepaid cards. As Navin Beekarry points out,

the more protected the financial system would be against this phenomenon [ML], the more money launderers would try to use alternative means to carry out their criminal activities.<sup>188</sup>

One may expect that regulation of the financial sector will continue to expand, as it was seen during the last 30 years of the AML/CTF development. New challenges, such as the decentralisation of financial systems, peer-to-peer platforms, initial coin offering (ICO), etc. will certainly disrupt the current market and function beyond the AML rules. However, contrary to the previous financial technologies, modern solutions put an emphasis on security and anonymity. Consequently, this may hinder the effective implementation of the laws, which might lead to a total ban from the regulator, in the same way as cryptocurrencies were banned in South Korea and China, due to high-risk nature of the such technology.

By the same token, AML/CTF laws already led to the so-called de-banking phenomenon. As the financial institutions refuse to serve the customers, the world will face a formation of the financially isolated group of people, who are categorised as high-risk profile – for whatever reason – and cannot afford services of the banks with a high-risk tolerance policy.

Today, risk assessment is done through the initial machine processing and subsequent manual evaluation, which requires considerable amount of labour and resources. It is evident that the future of the AML/CTF regulation lies in the automatisisation and machine learning, as the risk-evaluation systems become so much more complicated as well as multidimensional.

It is highly possible that, at some point, the European legislation shall come up with the standardised algorithms that would perform the risk assessment automatically, that is, with minimum human interference. The idea to use algorithms is not new, but today it becomes possible to set up comprehensive self-learning system. The outcome of such automatization, however, would only be beneficial for the organisations and for compliance purposes, whereas

---

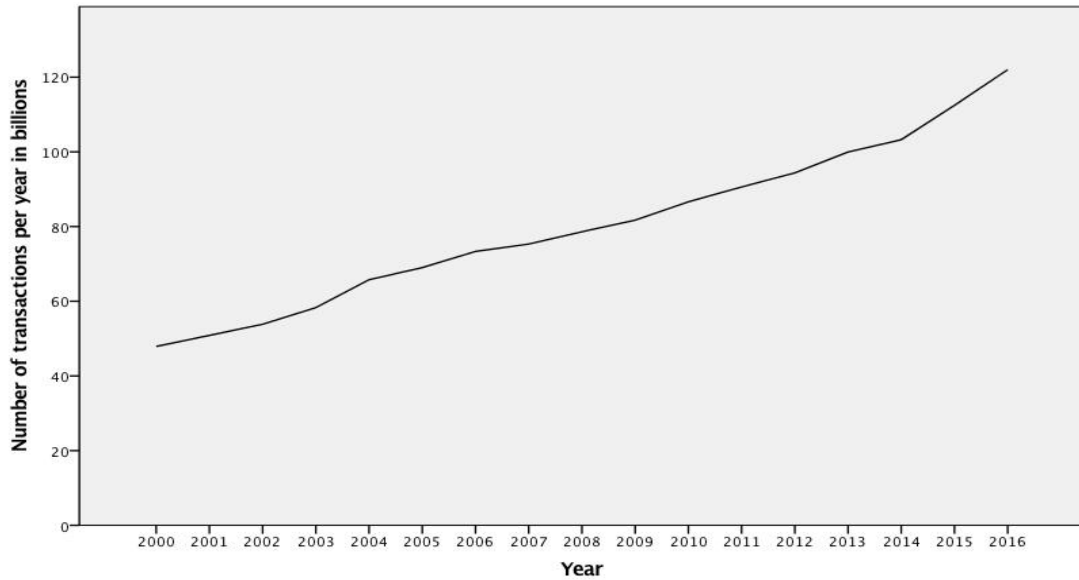
<sup>188</sup> Navin Beekarry, “The International Anti-Money Laundering”, *supra* note 23, p.7.



the customers would be constantly monitored without an option to cease the monitoring while still having an access to the financial system.

Indeed, such tendencies are somewhat worrisome, as it looks that Anti Money Laundering is moving towards Combating Terrorism Financing and – even more – large-scale financial surveillance over customers, conducted on the part of the regulator, which might – and, apparently, would – go *beyond the laundry rooms*.

## ANNEX

**Annex 1: Number of transactions per year (in billions) in the European Union.<sup>189</sup>**

Source: ECB

Year	Number of transactions (In Billions)	Year	Number of transactions (In Billions)
2000	47.9	2009	81.72
2001	50.86	2010	86.63
2002	53.84	2011	90.61
2003	58.31	2012	94.38
2004	65.78	2013	99.95
2005	69.02	2014	103.26
2006	73.35	2015	112.47
2007	75.33	2016	122.01
2008	78.62	2017	No data available

<sup>189</sup> European Central Bank. Number of total payment transactions involving non-MFIs - from EU (changing composition). Available at:

<http://sdw.ecb.europa.eu/browseSelection.do?type=series&q=PSS.A.D0.F000.I00.Z00Z.NT.X0.20.Z0Z.Z&node=SEARCHRESULTS&ec=&oc=&rc=&cv=&pb=&dc=&df=>. Last accessed: 7 May 2018.

## **Annex 2: Functions and tasks of the FATF.**<sup>190</sup>

In order to fulfil its objectives, the FATF carries out the following tasks:

1. Identifying and analysing money laundering, terrorist financing and other threats to the integrity of the financial system, including the methods and trends involved; examining the impact of measures designed to combat misuse of the international financial system; supporting national, regional and global threat and risk assessments;
2. Developing and refining the international standards for combating money laundering and the financing of terrorism and proliferation (the FATF Recommendations);
3. Assessing and monitoring its Members, through ‘peer reviews’ (‘mutual evaluations’) and follow-up processes, to determine the degree of technical compliance, implementation and effectiveness of systems to combat money laundering and the financing of terrorism and proliferation; refining the standard assessment methodology and common procedures for conducting mutual evaluations and evaluation follow-up;
4. Identifying and engaging with high-risk, non-cooperative jurisdictions and those with strategic deficiencies in their national regimes, and co-ordinating action to protect the integrity of the financial system against the threat posed by them;
5. Promoting full and effective implementation of the FATF Recommendations by all countries through the global network of FATF-style regional bodies (FSRBs) and international organisations; ensuring a clear understanding of the FATF standards and consistent application of mutual evaluation and follow-up processes throughout the FATF global network and strengthening the capacity of the FSRBs to assess and monitor their member countries;
6. Responding as necessary to significant new threats to the integrity of the financial system consistent with the needs identified by the international community, including the United Nations Security Council, the G-20 and the FATF itself; preparing guidance as needed to facilitate implementation of relevant international obligations in a manner compatible with the FATF standards (e.g., continuing work on money laundering and other misuse of the financial system relating to corruption);
7. Assisting jurisdictions in implementing financial provisions of the United Nations Security Council resolutions on non-proliferation, assessing the degree of implementation and the effectiveness of these measures in accordance with the FATF mutual evaluation and follow-up process, and preparing guidance as needed to facilitate implementation of relevant international obligations in a manner compatible with the FATF standards;
8. Engaging and consulting with the private sector and civil society on matters related to the overall work of the FATF, including regular consultation with the private sector and through the consultative forum;

---

<sup>190</sup> The Financial Action Task Force (FATF). Mandate of the Financial Action Task Force (2012-2020), p. 2.

Available at:

<http://www.fatf-gafi.org/media/fatf/documents/FINAL%20FATF%20MANDATE%202012-2020.pdf>. Last accessed: 7 May 2018.

9. Undertaking any new tasks agreed by its Members in the course of its activities and within the framework of this Mandate; and taking on these new tasks only where it has a particular additional contribution to make while avoiding duplication of existing efforts elsewhere.

**Annex 3: Development of the AML/CTF in the EU, the FATF, the UN and other organisations.**<sup>191</sup>

Year	EU	FATF	UN	Other
1980				Measures Against the Transfer and Safekeeping of Funds of Criminal Origin (CoE)  Offshore Group of Banking Supervisors (OGBS)
1988			UN Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances	Statement of Principles (Basel Committee)
1989		FATF founded		
1990		Original FATF 40 Recommendations		Convention on Laundering, Search, Seizure and Confiscation of Proceeds from Crime (CoE)
1991	First AML Directive (91/308/EEC)			
1992		1st Round of FATF Mutual Evaluations (start)		
1995				Creation of Egmont Group of Financial Intelligence Units
1996		FATF 40 Recommendations (revised) 2nd Round of FATF Mutual Evaluations		Creation of IMoLIN

<sup>191</sup> Inês Sofia de Oliveira. “Anti-Money Laundering: the conditions for global governance and harmonisation,” *supra* note 67, p.270.

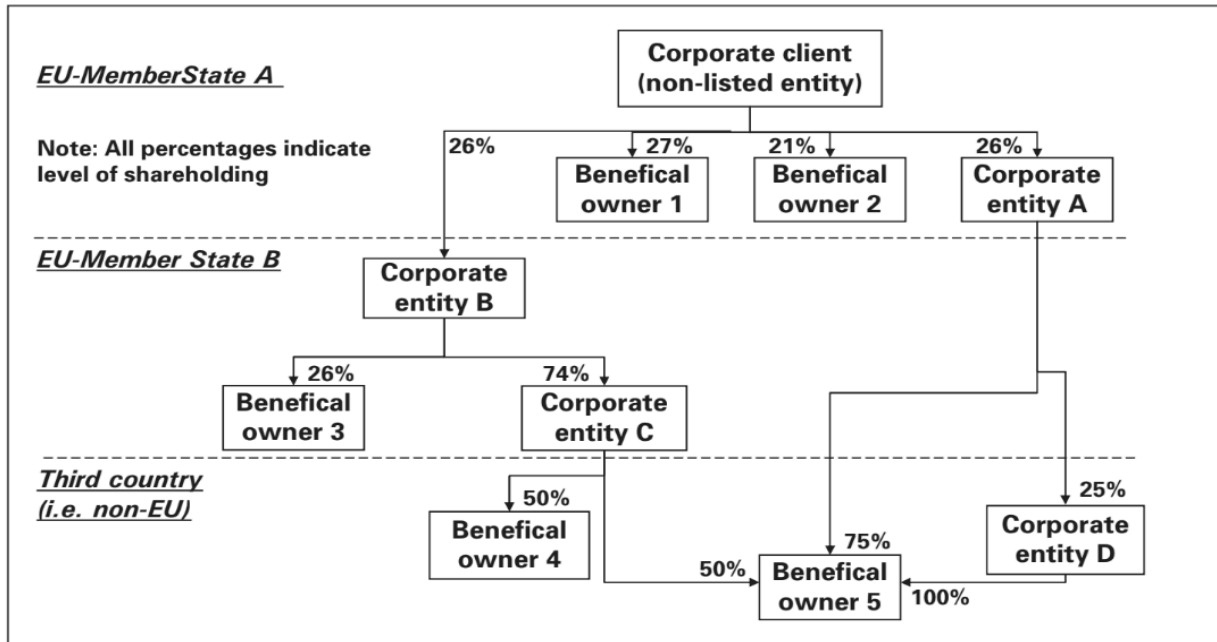
**Annex 3: Cont.**

Year	EU	FATF	UN	Other
1997	Action Plan to Combat Organised Crime (OJ C251, 15.08.1997)			CoE establishes MONEYVAL (as PC-R-EV)
1998	Joint Action on Corruption in the Private Sector (98/742/JHA)		UN Political Declaration and Action Plan against Money Laundering	OECD report on Harmful Tax Practices
1999		2nd Round of FATF Mutual Evaluations		
2000	Council Decision concerning arrangements for cooperation between financial intelligence units of the Member States in respect of exchanging information (2000/642/JHA)	FATF Report on NCCT	UN Convention against Transnational Organized Crime and the Protocols Thereto	Wolfsberg Global Anti-Money Laundering Guidelines for Private Banking
2001	Second AML Directive (2001/97/EC)  All EU States have FIUs	FATF 8 Special Recommendations on Terrorist Financing		US PATRIOT Act  Basel Committee Issues Report on Customer Due Diligence
2003	Council Framework Decision on Money Laundering, the Identification, tracing, freezing, seizing and confiscation of instrumentalities and the proceeds of crime (2001/500/JHA)	FATF Recommendations (revised)	UN Convention Against Corruption	

**Annex 3: Cont.**

Year	EU	FATF	UN	Other
2004		3rd Round of FATF Mutual Evaluations		
2005	Third AML Directive (2005/60/EC)			Convention on Laundering, Search, Seizure and Confiscation of Proceeds from Crime and on the Financing of Terrorism (CoE)
2006	Regulation (EC) No 1781/2006 on information on the payer accompanying transfers of funds			
2012		FATF Recommendations (revised)		
2014		4th Round of FATF Mutual Evaluations		
2015	Fourth AML Directive (Directive 2015/849)			
2016	Communication from the Commission to the European Parliament and the Council on an Action Plan for Strengthening the Fight Against Terrorist Financing COM (2016) 50 Final			

**Annex 4: Hypothetical structure of an entity, where beneficial ownership identification is complicated.**<sup>192</sup>



<sup>192</sup> Indranil Ganguli. “The Third Directive”, *supra* note 108, p. 5.



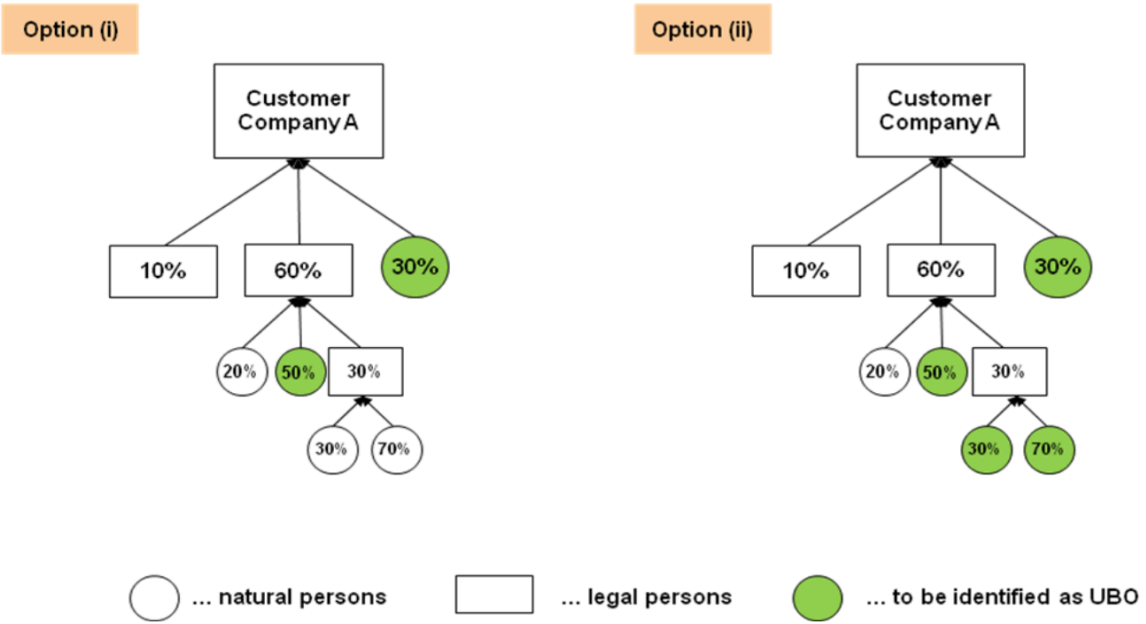
### Annex 5: Annual inflation in the European Union (1991 - 2015).<sup>193</sup>

Inflation in the European Union as measured by the consumer price index reflects the annual percentage change in the cost to the average consumer of acquiring a basket of goods and services that may be fixed or changed at specified intervals, such as yearly. The Laspeyres formula is generally used.

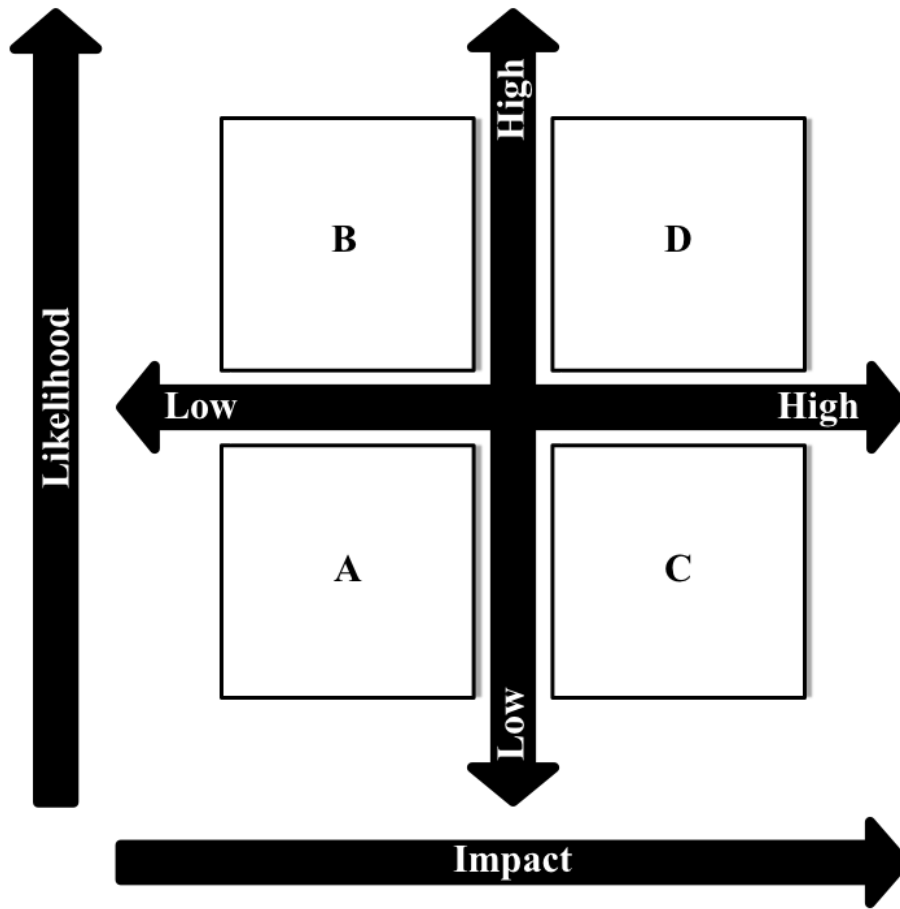
Year	Inflation, consumer prices (annual %)	Value of 15 000 EUR	Year	Inflation, consumer prices (annual %)	Value of 15 000 EUR
1991	-	15000	2004	2.3	22709
1992	5.1	15762	2005	2.5	23273
1993	4.6	16488	2006	2.6	23879
1994	4.7	17264	2007	2.6	24508
1995	4.3	18002	2008	4.2	25538
1996	3.3	18604	2009	1.0	25781
1997	2.7	19097	2010	1.7	26212
1998	2.4	19557	2011	3.3	27079
1999	2.2	19981	2012	2.7	27815
2000	3.2	20611	2013	1.4	28201
2001	3.2	21261	2014	0.2	28264
2002	2.3	21752	2015	-0.1	28247
2003	2.1	22208			

<sup>193</sup> Inflation, consumer prices (annual %). International Monetary Fund, International Financial Statistics and data files. Available at: <https://data.worldbank.org/indicator/FP.CPI.TOTL.ZG>

**Annex 6: Methods of beneficial ownership calculation.**<sup>194</sup>



<sup>194</sup> EBA, ESMA and EIOPA. Report on the legal, regulatory and supervisory implementation, *supra* note 149, p.10.

**Annex 7: Risk profiling matrix.**<sup>195</sup>

<sup>195</sup> Marcus Killick. "Implementing AML/CFT measures" that address the risks and not tick boxes", *supra* note 19, p. 212.

**Annex 8: Risk residuals.**<sup>196</sup>

Risk Factors	Risk Description	Description	Risk Rating
Customer type	Nature of the customer	General trading company dealing in export and import of Oil and Gas	4
AML screening result	AML screening result that in case of a match against SDN name or in relation to a financial crime	Customer being involved in Iran trading	5
Nationality /Country of incorporation	Country where the company is registered or incorporated	British Virgin Island	4
Country of residence	Country where the company is residing	United Arab Emirates	1
Business Activity	Type of business activities involved	Export and Import	4
UBO	Ultimate beneficial owner nationality	Iran	4
Partners	Partner nationality	Iran	4
Financial Products & Services	Type of banking product (to be) used by the customer	LC facility	3
Remarks:		Risk Scoring	4
		Approval Authority	Senior Manager
		Due diligence level	EDD

<sup>196</sup> Karima Touil. "Risk-Based Approach," *supra* note 167, p.18.

## Annex 9: Estimated annual cost and benefit analysis of AML/CTF policy in the EU by country.<sup>197</sup>

Country	Estimated costs of AML/CTF	Estimated benefits of AML/CTF
Austria	39.331.650 + 2 unknown	422.591 + 5 unknown
Belgium	52.109.975 + 2 unknown	559.885 + 5 unknown
Bulgaria	16.697.035 + 2 unknown	179.398 + 5 unknown
Cyprus	4.749.348 + 2 unknown	51.028 + 5 unknown
Czech Republic	34.239.484 + 2 unknown	367.879 + 5 unknown
Denmark	35.545.389 + 2 unknown	381.910 + 5 unknown
Estonia	4.355.149 + 2 unknown	46.793 + 5 unknown
Finland	28.707.338 + 2 unknown	308.440 + 5 unknown
France	320.821.916 + 2 unknown	3.447.008 + 5 unknown
Germany	378.177.540 + 2 unknown	4.063.254 + 5 unknown
Greece	46.737.736 + 2 unknown	502.164 + 5 unknown
Hungary	30.925.483 + 2 unknown	332.273 + 5 unknown
Ireland	23.870.414 + 2 unknown	256.471 + 5 unknown
Italy	286.270.198 + 2 unknown	3.075.774 + 5 unknown
Latvia	7.480.286 + 2 unknown	80.370 + 5 unknown
Lithuania	10.304.206 + 2 unknown	110.712 + 5 unknown
Luxembourg	2.517.861 + 2 unknown	27.053 + 5 unknown
Malta	1.477.812 + 2 unknown	15.878 + 5 unknown
Netherlands	80.858.428 + 2 unknown	868.767 + 5 unknown
Poland	109.126.093 + 2 unknown	1.172.484 + 5 unknown
Portugal	44.676.164 + 2 unknown	480.014 + 5 unknown
Romania	60.662.875 + 2 unknown	651.780 + 5 unknown
Slovakia	18.516.679 + 2 unknown	198.949 + 5 unknown
Slovenia	7.404.790 + 2 unknown	79.559 + 5 unknown
Spain	201.599.523 + 2 unknown	2.166.046 + 5 unknown
Sweden	49.501.570 + 2 unknown	531.860 + 5 unknown
UK	260.394.648 + 2 unknown	2.797.759 + 5 unknown
<b>EU-27</b>	<b>2.157.059.590 + 2 unknown</b>	<b>23.176.102 + 5 unknown</b>

<sup>197</sup> Brigitte Unger, Henk Addink. Project 'ECOLEF' The Economic and Legal Effectiveness of Anti Money Laundering and Combating Terrorist Financing Policy, p. 304. 2013. Available at: [http://www2.econ.uu.nl/users/unger/ecolef\\_files/Final%20ECOLEF%20report%20%28digital%20version%29.pdf](http://www2.econ.uu.nl/users/unger/ecolef_files/Final%20ECOLEF%20report%20%28digital%20version%29.pdf). Last accessed: 7 May 2018.

## Annex 10: Estimates of the annual cost and benefits of AML/CTF policy.<sup>198</sup>

<b>Costs</b>	<b>Best estimate (Bandwidth)</b>	<b>Benefits</b>	<b>Best estimate (Bandwidth)</b>
Ongoing policy making	896.754 (116.762 – 1.813.000)	Fines	Unknown
FIU	2.892.349 (685.460 – 9.860.636)	Confiscated proceeds	474.294 (14.715 – 1.039.896)
Supervision	14.332.941 (291.906 – 112.200.000)	Reduction in the amount of ML	Unknown
Law enforcement	1.423.565 (single estimate)	Less predicate crimes	Unknown
Judiciary	400.245 (single estimate)	Reduced damage effect on real economy	Unknown
Sanction costs (repressive)	2.142.911(single estimate)	Less risk for the financial sector	Unknown
Duties of the private sector	22.055.000 (single estimate)		
Reduction in privacy	Moral cost		
Efficiency costs for society and the financial system	Unknown		
<b>Total cost estimate</b>	<b>44.143.765 + 2 unknown</b>	<b>Total benefit estimate</b>	<b>474.294 + 5 unknown</b>

*Note: these are estimations for a hypothetical country with 10 million people and a price level equal to the US. The numbers are for illustration purposes only, since all estimates are very sensible to many possible biases and estimation procedures.*

<sup>198</sup> Brigitte Unger, Henk Addink. Project 'ECOLEF', *supra* note 191, p. 303.

## BIBLIOGRAPHY

### Primary sources

98/733/JHA: Joint action of 21 December 1998 adopted by the Council on the basis of Article K.3 of the Treaty on European Union, on making it a criminal offence to participate in a criminal organisation in the Member States of the European Union, Official Journal L 351, 29.12.1998. Article 1. Available at:

<http://eurlex.europa.eu/legalcontent/EN/TXT/HTML/?uri=CELEX:31998F0733&from=EN>

Convention drawn up on the basis of Article K.3 of the Treaty on European Union, on the protection of the European Communities' financial interests, OJ C 316/49, 27.11.1995. Article 1(1) and Article 2. Available at: [https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:41995A1127\(03\)&from=EN](https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:41995A1127(03)&from=EN)

[https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:41995A1127\(03\)&from=EN](https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:41995A1127(03)&from=EN)

Convention for the Protection of Human Rights and Fundamental Freedoms as amended by Protocols Nos. 11 and 14 supplemented by Protocols Nos. 1, 4, 6, 7, 12 and 13. Article 6 and 8. Available at: [https://www.echr.coe.int/Documents/Convention\\_ENG.pdf](https://www.echr.coe.int/Documents/Convention_ENG.pdf)

Council Directive 91/308/EEC of 10 June 1991 on prevention of the use of the financial system for the purpose of money laundering, Official Journal L 166. Recitals. Available at:

<http://eur-lex.europa.eu/legal-content/en/ALL/?uri=CELEX:31991L0308>

Council of Europe. Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime 1990, Article 6. Available at: <https://rm.coe.int/168007bd23>

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, OJ L 141/73, Recital 4. Available at: [http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:JOL\\_2015\\_141\\_R\\_0003&from=ES](http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:JOL_2015_141_R_0003&from=ES)

Directive 2001/97/EC of the European Parliament and of the Council of 4 December 2001 amending Council Directive 91/308/EEC on prevention of the use of the financial system for the purpose of money laundering, OJ L 344, 28.12.2001. Recital 13. Available at: <https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:32001L0097&from=EN>

<https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:32001L0097&from=EN>

Directive 2005/60/EC of the European Parliament and of the Council of 26 October 2005 on the Prevention of the Use of the Financial System for the Purpose of Money Laundering and Terrorist Financing, OJ L 309/15, 25.11.2005, Recital 2. Available at: <https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:32005L0060&from=EN>

<https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:32005L0060&from=EN>

Final Act of the United Nations Conference for the Adoption of a Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances. Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances 1988, p.1. Available at:

[https://www.unodc.org/pdf/convention\\_1988\\_en.pdf](https://www.unodc.org/pdf/convention_1988_en.pdf)

The European Parliament. Resolution on the drug problem. Official Journal of the European Communities, Vol 29 (10 November 1986), No C 283/79 - 81.

The Treaty on European Union 1992 (Maastricht Treaty), Article K.1. Available at: [https://europa.eu/europeanunion/sites/europa.eu/files/docs/body/treaty\\_on\\_european\\_union\\_en.pdf](https://europa.eu/europeanunion/sites/europa.eu/files/docs/body/treaty_on_european_union_en.pdf)

United Nations Convention against Corruption, 9 December 2003. Available at: [https://www.unodc.org/documents/brussels/UN\\_Convention\\_Against\\_Corruption.pdf](https://www.unodc.org/documents/brussels/UN_Convention_Against_Corruption.pdf)

United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, (Vienna, 1988), Article 1D. Available at: [https://www.unodc.org/pdf/convention\\_1988\\_en.pdf](https://www.unodc.org/pdf/convention_1988_en.pdf)

## Secondary sources

### The Financial Action Task Force Materials (reviews, recommendations, etc.)

Financial Action Task Force on Money Laundering (FATF). “The Forty Recommendations of the Financial Task Force on Money Laundering, With Interpretative notes,” International Legal Materials 35, No. 5 (1996), p. 1291. Available at: <http://www.jstor.org/stable/20698609>

The Financial Action Task Force (FATF) Official Website. FATF Members and Observers. Available at: <http://www.fatf-gafi.org/about/membersandobservers/>

The Financial Action Task Force (FATF). Annual Report 2001-2002 (2002), p. 5. Available at: <http://www.fatf-gafi.org/documents/documents/fatfannualreport2001-2002.html>

The Financial Action Task Force (FATF). Annual Review of Non-Cooperative Countries and Territories 2006-2007: Eighth NCCT Review (Paris, 2017), p. 3. Available at: <http://www.fatf-gafi.org/media/fatf/documents/reports/2006%202007%20NCCT%20ENG.pdf>

The Financial Action Task Force (FATF). Financial Action Task Force Mandate 2012-2020, (Washington, DC, 2012), p. 2. Available at: <http://www.fatfgafi.org/media/fatf/documents/FINAL%20FATF%20MANDATE%202012-2020.pdf>

The Financial Action Task Force (FATF). Financial Action Task Force Annual Report 2011- 2012 (2012), p.7. Available at: <http://www.fatfgafi.org/media/fatf/documents/brochuresannualreports/FATF%20annual%20report%202011%202012%20website.pdf>

The Financial Action Task Force (FATF). Mandate of the Financial Action Task Force (2012-2020), p. 2. Available at: <http://www.fatf-gafi.org/media/fatf/documents/FINAL%20FATF%20MANDATE%202012-2020.pdf>

The Financial Action Task Force (FATF). Methodology for Assessing Technical Compliance with the FATF Recommendations and the Effectiveness of AML/CTF Systems (February 2018), p. 8. Available at: <http://www.fatfgafi.org/media/fatf/documents/methodology/FATF%20Methodology%2022%20Feb%202013.pdf>



The Financial Action Task Force (FATF). Methodology for Assessing Technical Compliance with the FATF Recommendations and the Effectiveness of AML/CTF Systems (February 2018), p. 8. Available at: [http://www.fatf-gafi.org/media/fatf/documents/methodology/FATF%](http://www.fatf-gafi.org/media/fatf/documents/methodology/FATF%20Methodology.pdf)

The Financial Action Task Force (FATF). Money Laundering Using New Payment Methods (October 2010), p.52. Available at: <http://www.fatf-gafi.org/media/fatf/documents/reports/ML%20using%20New%20Payment%20Methods.pdf>

The Financial Action Task Force (FATF). Report on Money Laundering Typologies 2002-2003 (14 February 2003), p. 1. Available at: <http://www.fatf-gafi.org/documents/documents/moneylaunderingtypologies2002-2003.html>

The Financial Action Task Force (FATF). Review to Identify Non-Cooperative Countries or Territories: Increasing the Worldwide Effectiveness of Anti-Money Laundering Measures. Second NCCTs review (06/2001). P.3. Available at: <http://www.fatf-gafi.org/media/fatf/documents/reports/2000%202001%20NCCT%20ENG.pdf>

The Financial Action Task Force (FATF). The FATF Recommendations 2003 (October 2004), p.2. Available at: <http://www.fatf-gafi.org/media/fatf/documents/FATF%20Standards%20-%2040%20Recommendations%20rc.pdf>

The Financial Action Task Force (FATF). The FATF Recommendations 2012, February 2012, Recommendation 1. Available at: [http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF\\_Recommendations.pdf](http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF_Recommendations.pdf)

The Financial Action Task Force (FATF). The Misuse of Corporate Vehicles, Including Trust and Company Service Providers (13 October 2006), p. 1-2. Available at: <http://www.fatf-gafi.org/media/fatf/documents/reports/Misuse%20of%20Corporate%20Vehicles%20including%20Trusts%20and%20Company%20Services%20Providers.pdf>

The Financial Action Task Force (FATF). Transparency and Beneficial Ownership (October 2014), p. 15. Available at: <http://www.fatf-gafi.org/media/fatf/documents/reports/guidance-transparency-beneficial-ownership.pdf>

### **Official Documents (Consultative papers, reports, proposals etc.)**

Basel Committee on Banking Supervision. Consultative Document Customer due diligence for banks (January 2001), p.3. Available at: <https://www.bis.org/publ/bcbs77.pdf>

Commission of the European Communities. Second Commission Report to the European Parliament and the Council on the Implementation of the Money Laundering Directive Brussels, COM (1998) 401 final, (01.07.1998), p. 12. Available at: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:51998DC0401&from=EN>

Common Understanding Between EU Member States on the Procedure and Criteria for the Recognition of Third Countries Equivalence Under Directive 2005/60/EC on the Prevention of the Use of the Financial System for the Purpose of Money Laundering and Terrorist Financing. Available at: [http://ec.europa.eu/internal\\_market/company/docs/financial-crime/3rd-country-common-understanding\\_en.pdf](http://ec.europa.eu/internal_market/company/docs/financial-crime/3rd-country-common-understanding_en.pdf)

Deloitte. European Commission DG Internal Market and Services - Budget Final Study on the Application of the Anti-Money Laundering Directive (2010), p.26. Available at: [http://ec.europa.eu/internal\\_market/company/docs/financial-crime/20110124\\_study\\_amld\\_en.pdf](http://ec.europa.eu/internal_market/company/docs/financial-crime/20110124_study_amld_en.pdf)

European Bank Authority (EBA), European Securities and Markets Authority (ESMA) and European Insurance and Occupational Pensions Authority (EIOPA), Report on the legal, regulatory and supervisory implementation across EU Member States in relation to the Beneficial Owners Customer Due Diligence requirements under the Third Money Laundering Directive [2005/60/EC], JC/2011/096 AMLTF/2011/05 (2011), p. 10.

European Bank Authority. Joint Guidelines under Articles 17 and 18(4) of Directive (EU) 2015/849 on simplified and enhanced 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, JC 2017 37 (26.06.2017), p. 20. Available at: <https://www.eba.europa.eu/documents/10180/1890686/Final+Guidelines+on+Risk+Factors+%28JC+2017+37%29.pdf>

European Central Bank. Number of total payment transactions involving non-MFIs - from EU (changing composition). Available at: <http://sdw.ecb.europa.eu/browseSelection.do?type=series&q=PSS.A.D0.F000.I00.Z00Z.NT.X0.20.Z0Z.Z&node=SEARCHRESULTS&ec=&oc=&rc=&cv=&pb=&dc=&df=>

European Commission. “Strengthened EU rules to tackle money laundering, tax avoidance and terrorism financing enter into force,” 26 June 2017. Available at: [http://europa.eu/rapid/press-release\\_IP-17-1732\\_en.htm](http://europa.eu/rapid/press-release_IP-17-1732_en.htm)

Financial Intelligence Units: An Overview. International Monetary Fund World Bank (2004), p.111. Available at: <https://www.imf.org/external/pubs/ft/FIU/fiu.pdf>.

Inflation, consumer prices (annual %). International Monetary Fund, International Financial Statistics and data files. Available at: <https://data.worldbank.org/indicator/FP.CPI.TOTL.ZG>

Report from the Commission to the European Parliament and the Council on the Application of Directive 2005/60/EC on the Prevention of the Use of the Financial System for the Purpose of Money Laundering and Terrorist Financing, 52012DC0168, Point 2.1. Available at: <https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52012DC0168&from=EN>

Report from the Commission to the European Parliament and the Council on the assessment of the risks of money laundering and terrorist financing affecting the internal market and relating to cross-border activities, COM (2017) 340 final, 26.6.2017, p.4. Available at: [http://ec.europa.eu/newsroom/document.cfm?doc\\_id=45319](http://ec.europa.eu/newsroom/document.cfm?doc_id=45319).

Report on the proposal for a directive of the European Parliament and of the Council amending Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing and amending Directive 2009/101/EC, COM (2016)0450 – C8-0265/2016 – 2016/0208(COD). Amendments to Article 1. Available at: <http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+REPORT+A8-2017-0056+0+DOC+XML+V0//EN#title2>.

The Commission of the European Communities. First Commission's Report on the Implementation of the Money Laundering Directive (91/308/EEC) to Be Submitted to the European Parliament and to the Council, COM (95) 54 Final, (03.03.1995), p.7. Available at: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:51995DC0054&qid=1525370717951&from=EN>

The Commission of the European Communities. Secretariat-General. Official Journal of the European Communities, Vol 29, No C 283/79-81 (10 November 1986), p.77

The European Commission. Report from the Commission to the European Parliament and the Council on the Application of Directive 2005/60/EC on the Prevention of the Use of the Financial System for the Purpose of Money Laundering and Terrorist Financing, COM (2012) 168 final, (11.4.2012), p. 2. Available at: [http://ec.europa.eu/internal\\_market/company/docs/financial-crime/20120411\\_report\\_en.pdf](http://ec.europa.eu/internal_market/company/docs/financial-crime/20120411_report_en.pdf)

The Organisation for Economic Co-Operation and Development (OECD). Money Laundering Awareness Handbook for Tax Examiners and Tax Auditors (2009), p.5. Available at: <http://www.oecd.org/tax/exchange-of-tax-information/43841099.pdf>

The Wolfsberg Group. Frequently Asked Questions on Risk Assessments for Money Laundering, Sanctions and Bribery & Corruption, p.18. Available at: <https://www.wolfsberg-principles.com/sites/default/files/wb/pdfs/faqs/17.%20Wolfsberg-Risk-Assessment-FAQs-2015.pdf>

The Wolfsberg Group. Guidance on a Risk Based Approach for Managing Money Laundering Risks (March 2006), p. 5. Available at: [https://www.wolfsbergprinciples.com/sites/default/files/wb/pdfs/wolfsbergstandards/15.%20Wolfsberg\\_RBA\\_Guidance\\_%282006%29.pdf](https://www.wolfsbergprinciples.com/sites/default/files/wb/pdfs/wolfsbergstandards/15.%20Wolfsberg_RBA_Guidance_%282006%29.pdf)

The World Bank. Combating Money Laundering and the Financing of Terrorism: A Comprehensive Training Guide, Volume 1 (2009), p.19. Available at: <http://siteresources.worldbank.org/FINANCIALSECTOR/Resources/CombatingMLandTF.pdf>

Unger, Brigitte and Addink, Henk. Project 'ECOLEF' The Economic and Legal Effectiveness of Anti Money Laundering and Combating Terrorist Financing Policy, p. 304. 2013. Available at: [http://www2.econ.uu.nl/users/unger/ecolef\\_files/Final%20ECOLEF%20report%20%28digital%20version%29.pdf](http://www2.econ.uu.nl/users/unger/ecolef_files/Final%20ECOLEF%20report%20%28digital%20version%29.pdf)

### **Scholarly writings (journal articles, books, etc.)**

Alexander, R.C.H. Insider Dealing and Money Laundering in the EU: Law and Regulation. (London, Routledge: 2007). p.153.

Allen, Daren. "Comparison Table: Fourth Money Laundering Directive (4MLD)– Changes From 3MLD". *Thomson Reuters Regulatory Intelligence*, October 21, 2016.

Arnone, Marco and Borlini, Leonardo. "International anti- money laundering programs: Empirical assessment and issues in criminal regulation", *Journal of Money Laundering Control*, Vol. 13 Issue: 3 (2010) pp.226-271. Permanent link to this document: <https://doi.org/10.1108/13685201011057136>

Beekarry, Navin. "The International Anti-Money Laundering and Combating the Financing of Terrorism Regulatory Strategy: A Critical Analysis of Compliance Determinants in International Law," *Northwestern Journal of International Law & Business* 31:137 (2011), p. 180.

Bello, Abdullahi and Harvey, Jackie. "From a risk-based to an uncertainty-based approach to anti-money laundering compliance," *Security Journal*, 30(1) (2017), pp. 24-38. Available at:

[http://nrl.northumbria.ac.uk/26933/3/Harvey\\_Uncertainty%20based%20approach%20to%20AML%20submitted%20to%20Security%20journal.pdf](http://nrl.northumbria.ac.uk/26933/3/Harvey_Uncertainty%20based%20approach%20to%20AML%20submitted%20to%20Security%20journal.pdf)

Campbell, Andrew. "The High-Street Solicitor and the Proceeds of Criminal Activity — The Risks", *Journal of Money Laundering Control*, Vol. 1 Issue: 1 (1997), p. 8. Permanent link: <https://doi.org/10.1108/eb027115>

Campbell, Liz. "Dirty cash (money talks): 4AMLD and the Money Laundering Regulations 2017," *Criminal Law Review* (2018), p. 102-122. Available at: Westlaw UK.

Costanzo, Paolo. "The risk-based approach to anti-money laundering and counter-terrorist financing in international and EU standards: what it is, what it entails". *Research Handbook on Money Laundering*, (Cheltenham, UK: Edward Elgar Publishing, 2013), p.1. Available at: <https://doi.org/10.4337/9780857934000.00038>

Cox, Dennis. *Handbook of Anti Money Laundering* (Wiley, 2015), p.71. Available at: doi: 10.1002/9780470685280.fmatter

De Vido, Sara. "Anti-Money Laundering Measures Versus European Union Fundamental Freedoms and Human Rights in the Recent Jurisprudence of the European Court of Human Rights and the European Court of Justice," *German Law Journal* Vol. 16 No. 05 (2005), p. 1281. Available at: [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2848202](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2848202)

Ernst & Young. "Wind of change: Risk Assessment Anti-Money Laundering, Countering Terrorism Financing, Application of International Sanctions," (2016), p. 2. Available at: [https://www.apcf.ro/static/files/EY\\_Romania\\_Wind\\_of\\_Change\\_AML\\_Risk\\_Assessment.pdf](https://www.apcf.ro/static/files/EY_Romania_Wind_of_Change_AML_Risk_Assessment.pdf)

Ganguli, Indranil. "The Third Directive: Some Reflections on Europe's New AML/CFT Regime," *Banking & Financial Services Policy Report*, Volume 29, Number 5 (May 2010), p. 5.

Hanley-Giersch, Jennifer. "The Fourth EU AML/CTF Directive: A holistic risk-based approach," *Acams Today* September-November 2015, p. 75. Available at: <http://www.globalriskaffairs.com/wp-content/uploads/2015/09/The-Fourth-EU-AML-Directive-A-Holistic-RBA-Approach.pdf>

Hopton, Doug. *Money Laundering Concise Guide for all business* (Gower Publishing, 2009), p.17.

Hülse, Rainer. "Creating Demand for Global Governance: The Making of a Global Money-laundering Problem," *Global Society*, Vol. 21, No. 2 (2007), p. 155. Available at: <https://www.tandfonline.com/doi/abs/10.1080/13600820701201731>

Jeans, Neil. "FATF Recommendations: What Do They Mean for the Corporate Treasurer?" *Thomsons Reuters. Risk Management Solutions*. Available at:

<https://financial.thomsonreuters.com/content/dam/openweb/documents/pdf/financial/special-report-for-corporate-treasurers.pdf>

Johnson, Jackie, “An analysis of the obligations of gambling entities under the FATF's 2003 anti- money laundering recommendations”, *Journal of Money Laundering Control*, Vol. 9 Issue: 1 (2006), p.12. Permanent link to this document: <https://doi.org/10.1108/13685200610645184>

Killick, Marcus and Parody, David. “Implementing AML/CFT measures that address the risks and not tick boxes,” *Journal of Financial Regulation and Compliance*, Vol. 15, Issue: 2 (2007), pp.210-216. Available at: <https://doi.org/10.1108/13581980710744093> (permanent link)

Kourtellos, Pavlos Neofytou. “Implications of the Third Money Laundering Directive. The Cyprus perspective,” (2014), p. 9. Available at: <https://www.kourtelaw.com/uc/wp-content/uploads/2014/02/Implications-of-the-3rd-Monvey-Laundering-Directive.pdf>.

Lowery, Clay and Ramachandran, Vijaya. “Unintended Consequences of Anti–Money Laundering Policies for Poor Countries,” *Center for Global Development*, 2015. Available at: <https://www.cgdev.org/sites/default/files/CGD-WG-Report-Unintended-Consequences-AML-Policies-2015.pdf>.

Magliveras, Konstantinos. “The European Community’s Combat Against Money Laundering: Analysis and Evaluation,” *Journal of International & Comparative Law* Vol 5:93 (1998), p.102

O’Connor, Denis. “EU Fifth Anti-Money Laundering Directive: Can Banks Handle It?” Available at: <https://kyc360.com/article/eu-fifth-anti-money-laundering-directive-key-points-banks/>.

Oliveira de, Inês Sofia. “Anti-Money Laundering: the conditions for global governance and harmonisation,” The University of Edinburgh (2014), p.18. Available at: <https://www.era.lib.ed.ac.uk/handle/1842/15922?show=full>.

Peurala, Johanna. “The European Union’s Anti-Money Laundering Crusade – a Critical Analysis of the Responses by the EU/EC to Money Laundering,” *Reports of the Police College of Finland 83/2009 (2009)*, p. 55. Available at: [https://www.theseus.fi/bitstream/handle/10024/86709/Raportteja\\_83.pdf?sequence=1](https://www.theseus.fi/bitstream/handle/10024/86709/Raportteja_83.pdf?sequence=1).

Ping, He. “The new weapon for combating money laundering in the EU”, *Journal of Money Laundering Control*, Vol. 8 Issue: 2 (2005), p. 119. Permanent Link: <https://doi.org/10.1108/13685200510621163>

Salas, Mariano Fernández. “The third anti-money laundering directive and the legal profession,” *European Association of Lawyers* (October 2005), p.2. Available at: <https://www.anti-moneylaundering.org/Document/Default.aspx?DocumentUid=7B528765-CB1F-4748-9733-68935E2C4745>

Schneider, Friedrich and Enste, Dominik H. “Shadow Economies: Size, Causes, and Consequences,” *Journal of Economic Literature*, Vol. XXXVIII (March 2000), p. 79. Available at: <http://www.economics.uni-linz.ac.at/members/Schneider/files/publications/JEL.pdf>.

Schroeder, William R. “Money Laundering: A Global Threat and the International Community's Response,” *FBI Law Enforcement Bulletin* 70, No. 5 (May 2001), p. 1-9. Available at: <http://heinonline.org/HOL/P?h=hein.journals/fbibleb70&i=142>.

Simonova, Anna “The risk- based approach to anti- money laundering: problems and solutions,” *Journal of Money Laundering Control*, Vol. 14 Issue: 4 (2011), p. 177. Permanent link to this document: <https://doi.org/10.1108/13685201111173820>

Touil, Karima. “Risk-Based Approach Understanding and Implementation. Challenges between Risk Appetite and Compliance,” *Acams Today* (2016), p.10. Available at: [http://files.acams.org/pdfs/2016/RiskBased\\_Approach\\_Understanding\\_and\\_Implementation\\_K\\_Touil.pdf](http://files.acams.org/pdfs/2016/RiskBased_Approach_Understanding_and_Implementation_K_Touil.pdf).

Unger, Brigitte. “The Gravity Model for Measuring Money Laundering and Tax Evasion,” Workshop on Macroeconomic and Policy Implication of Underground Economy and Tax Evasion (2009), p. 78-79.

Welch, Jane, Javier Munoz del Guayo and others. “Comparative Implementation of EU Directives (II) – Money Laundering,” *The British Institute of International and Comparative Law* (December 2006), p.11.

William Fry. “New Rules on Beneficial Ownership Register – Immediate Action Required,” November 2016, p.2. Available at: <https://www.williamfry.com/docs/default-source/ezine-print-friendly-documents/new-rules-on-beneficial-ownership-register.pdf?sfvrsn=2>

### **Auxiliary sources**

Bitcoin - Statistics & Facts. Statista.com. Available at: <https://www.statista.com/topics/2308/bitcoin/>.

On the Process of Voluntary Liquidation of ABLV Bank. ABLV Bank Official Website. Available at: <https://www.ablv.com/en/legal-latest-news/voluntary-liquidation-of-ablv-bank-as-to-protect-the-interests-of-clients-and-creditors/on-the-process-of-voluntary-liquidation-of-ablv-bank>.

Special Measures for Jurisdictions, Financial Institutions, or International Transactions of Primary Money Laundering Concern. Financial Crimes Enforcement Network Official Website. Available at: <https://www.fincen.gov/resources/statutes-and-regulations/311-special-measures>.

Vahtla, Aili. “E-Residency program under threat as banks closing foreigners' bank accounts,” *Estonian National News Portal Eesti Rahvusringhääling*. Available at: <https://news.err.ee/691549/e-residency-program-under-threat-as-banks-closing-foreigners-bank-accounts>.

McElroy, D. “Iraq Oil Bonanza reaps \$1 million a day for Islamic State; Exclusive: Islamic State strengthens grip on northern Iraq by raising millions from sale of oil through Kurdistan to Turkey and Iran”, *The Telegraph*, (2014). Available at: [www.telegraph.co.uk/news/worldnews/middleeast/iraq/10962160/Iraq-oil-bonanza-reaps-1-million-a-day-for-Islamic-State.html](http://www.telegraph.co.uk/news/worldnews/middleeast/iraq/10962160/Iraq-oil-bonanza-reaps-1-million-a-day-for-Islamic-State.html).