CM2401

COMMENT ON THE EU ANTI MONEY LAUNDERING PACKAGE: PREVENTING DE-RISKING AND KEEPING ITS RISK-BASED CHARACTER IN PRACTICE

JANUARY 2024

As an independent group of experts, the Meijers Committee monitors the development and effectiveness of, amongst other areas, EU criminal law, including European Anti Money Laundering (AML) rules. Thus far, these rules were entered via directives and subsequently implemented by the Member States. In July 2021 an ambitious EU AML package was launched. The package introduces, amongst other things, a single rule book – via an AML Regulation – and a new overarching EU AML supervisor: the AML Authority (AMLA). Taking into account the ongoing expansion of the scope of the AML rules, the Meijers Committee has concerns that the use of resources is not sufficiently effective, that the risk of citizens being deprived of essential facilities as a result of this expansion is not sufficiently targeted and that the proposed AML package needs adjustments to remove these concerns.
In this comment, the Meijers Committee raises three questions:

1. Are the scarce resources (of both the obliged entities and their supervisors and enforcers) being used effectively at this moment?
2. Are the individual's rights, such as privacy, non-discrimination, presumption of innocence and proportionality, at risk of being compromised?
3. Does the proposed AML package address the abovementioned questions?

In light of the foregoing, specific recommendations are identified, which will be elaborated on in further detail in the attached comment.

Meijers Committee

Standing committee of experts on international immigration, refugee and criminal law

Meijers Committee

CM2401 EU Anti Money Laundering (AML) package: Preventing de-risking and keeping its risk-based character in practice

1. Introduction

As an independent group of experts, the Meijers Committee monitors the development and effectiveness of, amongst other areas, EU criminal law, including European Anti Money Laundering (hereafter: AML) rules. Thus far, these rules were entered via directives and subsequently implemented by the Member States. In July 2021 an ambitious EU AML package was launched.[1] The package introduces, amongst other things, a single rule book – via an AML Regulation – and a new overarching EU AML supervisor: the AML Authority (hereafter: AMLA). Taking into account the ongoing expansion of the scope of the AML rules, the Meijers Committee has concerns that the use of resources is not sufficiently effective, that the risk of citizens being deprived of essential facilities as a result of this expansion is not sufficiently targeted and that the proposed AML package needs adjustments to remove these concerns.

In the – justified – fight against money laundering (hereafter: ML) and terrorist financing (hereafter: TF) over the years, we have seen the EU AML rules expand over and over again. Not only the number of obliged entities subject to AML rules has grown significantly, also the "red flags" and the guidelines on how to perform the required customer due diligence have been more and more intensified and specified. Set up primarily to protect the obliged entities themselves from being misused for ML/TF purposes (and not to transfer the obliged entities into an extended arm of the police and the judiciary), the application of the AML rules nevertheless seems to have been transformed into rules that aim at detecting money laundering and their premediate criminal offences, making obliged entities part of the law enforcement agencies.

This development raises three questions:

1. Are the scarce resources (of both the obliged entities and their supervisors and enforcers) being used effectively at this moment?
2. Are the individual's rights, such as privacy, non-discrimination, presumption of innocence and proportionality, at risk of being compromised?
3. Does the proposed AML package address the abovementioned questions?

In the next paragraphs, these questions will be answered in more detail.

---

[1] The package encompasses:
-Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing (COM2021, 420 final);
-Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL establishing the Authority for Anti-Money Laundering and Countering the Financing of Terrorism and amending Regulations (EU) No 1093/2010, (EU) 1094/2010, (EU) 1095/2010 (COM/2021/421 final);
-Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on information accompanying transfers of funds and certain crypto-assets (COM/2021/422 final), meanwhile established on 31 May 2023 (Regulation 2023/1113, Pb 2023 L 150);
-Proposal for a Directive establishing the mechanisms that Member States should put in place to prevent the use of the financial system for the purposes of money laundering and terrorist financing and repealing Directive (EU) 2015/8496 (COM/2021/423 final).

2. Effective use of resources

From the outset, the starting point has been that it would not be realistic to require from the obliged entities to investigate each and every detail of each and every transaction and of the (legal) persons involved. Therefore, the third EU AML Directive[2] introduced the risk-based approach: AML measures, and the preceding customer due diligence, are supposed to focus on those transactions that in practice pose the greatest risk of money laundering. The idea was that the obliged entities could best assess from their own experience and practice which transactions presented the most risk and therefore which transactions should be monitored more intensively[3].

In order to give the obliged entities more guidance when prioritising transactions to which (enhanced) attention should be paid, specific "red flag" lists, derived from the Financial Action Task Force typologies, were drawn up for each sector in (supra)national and sector guidelines. The presence of a red flag does not immediately imply that the transaction in question is a suspicious transaction to be reported to the Financial Intelligence Unit, but it is an indication that – based on the risks involved – further investigation must be carried out in order to verify whether or not the transaction is 'suspicious' and should be reported. The obliged entity should assess whether a client or transaction would need a standard customer due diligence, an enhanced customer due diligence (when the risks of ML/TF involvement seem higher) or a simplified customer due diligence (the expected MF/TL risks are significantly low). This client and transaction risk profile is the institutions' responsibility and they can and should use their experience in the field as to how far a customer due diligence should go as long as the customer due diligence measures, taken on the basis of the risk profiles, were at all times 'adequate', i.e. tailored to the risk of the client, the transaction, the service and/or the country in which the transaction takes place.

Guidelines have been issued on the EU level (supranational guidelines) and national level (national and sector guidelines) to give the obliged entities some guidance on how to apply the AML rules. The Meijers Committee establishes that the supervisory guidelines over the years have become more and more intensified and specified, leading to the current situation where obliged entities have to conduct a customer due diligence into almost every client and transaction and are expected to search and disclose every possible relevant detail of a transaction. This practice approaches a rule-based system rather than a risk-based system. Even clearly low risk transactions and clients still need a significant customer due diligence or otherwise the obliged entity is breaching the AML rules and can be (and in practice is) punished for such breach.

---

[2] 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; L 309/15.

[3] From the 3rd Directive's Explanatory Memorandum [source]: "AML measures, and the preceding customer due diligence, are focused on those transactions that in practice pose the greatest risk of money laundering. The idea was that each of the institutions subject to the AML rules could best assess from their own experience and practice which transactions presented the most risk and therefore which transactions should be monitored most intensively."

The view that not all transactions can be monitored in every detail due to a lack of capacity at the obliged entities seems to have given way to the tendency, initiated by the Financial Action Task Force, strengthened by the successive AML Directives and culminating in the EU AML package, to increasingly expand and tighten the rules that obliged entities must comply with. The unrealistic goal seems to have become to eliminate all money laundering activities and this goal seems to justify all means. This leads to obliged entities in fact conducting a kind of police investigation, also into transactions that do not need that attention from an AML-risk perspective. And it leads to both obliged entities and their supervisors spending many resources on low(er) risk transactions and on documenting customer due diligence details.

The obliged entities' supervisors, moreover, want to see as many transactions as possible investigated and often take the position that obliged entities' customer due diligence has not been fully performed. In practice, the problem often is that the supervisory and enforcement authorities initiate an investigation into the customer due diligence conducted after they have already become aware that the transaction in question did indeed take place under suspicious circumstances. In this assessment, the authorities have more (concrete) information from hindsight than the obliged entity had at the time the transaction took place. Knowing that a transaction was suspicious, but was not reported by the relevant institution, the enforcement authorities, and supervisors (as well as judges) tend to assume that the (risk-based) customer due diligence of the obliged entity has been insufficient and therefore in violation of the AML rules. Clearly, there is a risk of 'confirmation bias' here.

Overall, it must be concluded that both obliged entities and supervisors spend precious time and resources on transactions that do not need such relatively intensive attention from an AML-risk perspective. Therefore, the Meijers Committee recommends the EU Commission and the EU Parliament to elaborate and have the Member States implement the AML package rules in such a way that more focus will be given on high-risk transactions and less focus will be given on low-risk transactions, thus spreading the resources more effectively across the transactions to be investigated.

3. Serious risk of discrimination

As a consequence of the volume of customer due diligence's to be conducted and the intensity of those customer due diligence's, obliged entities, financial institutions specifically, tend to "de-risk" their client portfolio by intensively scrutinizing transactions or not accepting a client at all.

The application of the customer due diligence measures by private actors such as banks and other financial institutions carry the risk of discrimination. In their search for individuals or organisations at risk of terrorist financing and money laundering, financial institutions may set up risk profiles. These profiles may be developed by hand or by developing algorithms. In the past, terrorism has been associated with certain non-EU countries and groups with an Islamic background. When setting up a risk profile, data relating to a non-EU, or a religious background may be included in datasets used to identify individuals, communities, or organisations as potential risks. This can result in

individuals or communities with a specific national, religious, or ethnic background being unfairly targeted or subjected to stricter scrutiny, leading to discrimination and a violation of their right.[4]

In the Netherlands, several examples have come to light of persons with an Islamic background who were banned from transferring money to a mosque during the holy month of Ramadan and organisations with an Islamic denomination who were denied a bank account. In such cases, many individuals, often already marginalised, may be unable to access essential banking services, making them vulnerable and effectively treated as "second-class citizens." This exclusion increases inequalities and restricts individuals' ability to participate fully in economic activities and society.[5]

Furthermore, charity foundations in general are intensively scrutinised and more and more denied banking services merely due to the fact that they use to transfer money to foreign charity projects and banks de-risking their portfolio.

Another clear example where EU AML rules go too far and violate the individual's right to privacy can be found in the EU Court of Justice (hereafter: CJEU) judgment of 22 November 2022. In that judgment, the CJEU declared Directive 2018/843 invalid in so far as it amended the AML directive in such a way that Member States had to ensure that information on the beneficial ownership of companies and of other legal entities incorporated within their territory was accessible in all cases to any member of the general public. [6] According to the CJEU, access to beneficial ownership should be restricted to obliged entities and Member State authorities only.

The complexity of AML regulations and processes can limit transparency and hinder individuals' ability to understand the reasons for account rejections or scrutiny. This lack of transparency and accountability can make it challenging for individuals to challenge unfair decisions or seek help for any violations of their rights.

Therefore, the Meijers Committee notes with approval the position the European Parliament takes in relation to this issue and strongly recommends to adopt a new article 41a in the AML Regulation proposed by the European Parliament.[7] The Meijers

---

[4] Jyske Finans, CJEU (C-668/15) and Netherlands Institute for Human Rights, opinion 22 February 2023, no. 2023-22.

[5] https://www.trouw.nl/religie-filosofie/nieuw-toeslagenschandaal-ontstaat-in-de-omgang-van-banken-met-moslims~b5689b20/.

[6] WM (C-37/20) and Sovim SA (C-601/20) vs Luxembourg Business Registers

[7] Trilogue document 2021/0239 (COD), pages 370/371:
Article 41a: Unwarranted de-risking, non-discrimination and financial inclusion
1. Credit and financial institutions shall have in place controls and procedures to ensure that and in the application of customer due diligence requirements provided under this Chapter does not result in the unwarranted refusal, or termination, of business relationships with entire categories of customers and that obliged entities comply with Article 15 and Article 16(2) of Directive 2014/92/EU. The internal policies, controls and procedures of credit and financial institutions shall include options for mitigating the risks of money laundering and terrorist financing that obliged entities will consider applying before deciding to reject a customer on the grounds of a risk of money laundering or terrorist financing. The internal policies and procedures of credit and financial institutions shall include options and criteria to adjust the features of products or services offered to a given customer on an individual and risk-

Committee further recommends not to restrict the scope of this article to refugees and asylum seekers, but to apply it to Member States residents as well, as it appears that (groups of) residents, whether or not of foreign origin, are impacted by the de-risking policies. Moreover, the Meijers Committee recommends to explicitly express that these 'de-risking rules' should be effectively applied and supervised. Finally, it recommends to prohibit using a specific national, religious, or ethnic background as a circumstance causing a red flag.

4. Proposals for an AML Regulation and for the establishment of an AML Authority (AMLA)

The EU AML package, announced in 2021, which aims to strengthen the fight against money laundering and terrorist financing, may in the view of the Meijers Committee reinforce the abovementioned development to expand the scope of AML rules to a level that is of concern to the Meijers Committee.

Neither in the proposed AML Regulation nor in the proposed regulation to establish an AML Authority could the Meijers Committee find a mechanism that aims at attributing resources in a more tailor-made way to high-risk clients and transactions. It all tends to qualify more and more clients and/or transactions as 'high-risk' clients/transactions as a result of which the number of intensive customer due diligence only grows. Based on article 8 of the AML Regulation, as amended by the European Parliament, the obliged entities are responsible for identifying and assessing the customer's and transaction's risk. However, in assessing the risks, article 8 also requires from the obliged entity to take into account eight elements[8], seven of which have a public authority origin. This raises serious concerns as to the input the eighth element ('own

sensitive basis and, where applicable, in accordance with the level of services offered under Directive 2014/92/EU.
2. Without prejudice to paragraph 1, credit and financial institutions shall have in place internal policies, controls and procedures to ensure that the application of customer due diligence requirements provided under this Chapter does not result in the undue exclusion of non-profit organisations and their representatives and associates from access to financial services exclusively on the basis of geographical risk.
3. Obliged entities shall not rely exclusively on information provided by public authorities from the third countries covered by Articles 23, 24 and 25, as well as from the third countries covered by a decision adopted in accordance with Chapter 2 of Title V of the Treaty on European Union providing for the interruption or reduction, in part or completely, of economic and financial relations.
4. By … [three years after the entry into force of this Regulation], AMLA and EBA shall jointly issue guidelines on the clarification of the relationship between requirements in this Chapter and access to financial services, including in relation to the interactions between this Chapter and Directive (EU) 2014/92 and Directive (EU) 2015/2366. Those guidelines shall include guidance on how to maintain a balance between financial inclusion of categories of customers particularly affected by de-risking, and AML/CFT requirements. The guidelines shall clarify how risk can be mitigated in relation to those customers and ensure transparent and fair processes for customers.

[8] (1) the risk variables set out in Annex I-III, (2) the findings of the supra-national risk assessment drawn up by the Commission, (3) the findings of the national risk assessments carried out by the Member States, (4) relevant guidelines, recommendations and opinions issued by AMLA, (5) the conclusions drawn from past infringements of AML/CFT rules by the obliged entity in question or any connection of the obliged entity in question with a case of money laundering or terrorist financing, (6) information from FIUs and law enforcement agencies, (7) information obtained as part of the initial customer due diligence process and ongoing monitoring, (8) own knowledge and professional experience.

knowledge and professional experience') effectively can have. This is the more important as it was this element that was supposed to keep up the AML-rules' risk-based character.

The proposals shift the task of issuing and updating guidelines regarding the application of the AML rules in general and the scope of the client due diligence specifically to a new EU AML rules supervising body, the AML Authority. Amongst other things, the Authority shall issue guidelines on:

- the extent of the obliged entities' internal policies, controls, and procedures (article 7.4 AMLA proposal);
- the risk variables and risk factors to be taken into account by obliged entities when entering into business relationships (article 16.3 AMLA proposal);
- ongoing monitoring of a business relationship and on the monitoring of the transactions carried out in the context of such relationship (article 21.4 AMLA proposal).

Furthermore, it will be the AMLA's task to develop:

- draft regulatory technical standards which shall specify (article 15.5 AMLA):
  (a) the obliged entities, sectors or transactions that are associated with higher money laundering and terrorist financing risk and which shall comply with thresholds lower than those set in paragraph 1 point (b);
  (b) the related occasional transaction thresholds;
  (c) the criteria to identify linked transactions;
- draft regulatory technical standards which shall specify (article 22.1 AMLA):
  (a) the requirements that apply to obliged entities pursuant to Article 16 [Customer due diligence measures] and the information to be collected for the purpose of performing standard, simplified and enhanced customer due diligence pursuant to Articles 18 and 20 and Articles 27(1) and 28(4), including minimum requirements in situations of lower risk;
  (b) the type of simplified due diligence measures which obliged entities may apply in situations of lower risk pursuant to Article 27(1).

As a consequence, the Meijers Committee has concerns that, without more attention for an effective risk-based character of the AML rules and without an explicit proactive attitude and policy of the AMLA and other EU bodies responsible for an effective fight against ML/TF, EU AML policy will continue to be less effective.

Therefore, the Meijer Committee recommends to give more weight, throughout all AML proposals, and especially the AMLA proposal, to the knowledge and experience in relation to risk assessment to the obliged entities themselves.

5. Recommendations

In light of the foregoing, the Meijers committee recommends:

- to elaborate and implement the AML package rules in such a way that more focus will be given on high-risk transactions and less focus will be given on low risk transactions;
- to allow obliged entities to exempt clearly low risk transactions from the obligation to conduct a client due diligence once they have substantiated adequate reasons for such exempt;
- to adopt the European Parliament's proposal of article 41a AML Regulation and ascertain the prevention of de-risking and encourage non-discrimination and financial inclusion in relation to both refugees, asylum seekers, migrants, and residents, whether or not of foreign origin;
- to have both obliged entities and supervisors focusing on the high-risk clients and transaction, thus attributing the scarce resources more effectively;
- to prohibit the use of sensitive and potential discriminatory data such as nationality, religious affiliation, country of birth, country of residence.
- to ensure that obliged entities' knowledge and experience carry more weight when it comes to risk assessing and low risk qualifying and that public authorities respect obliged entities' balanced choices;
- to accept the fact that the fight against ML/TF benefits mostly from a risk-based approach, but that the risk-based approach implies that many low and standard risk transactions will not, cannot and need not be investigated to the extent a high-risk transaction is investigated.