

A better European Union architecture to fight money laundering

Joshua Kirschenbaum and Nicolas Véron

Executive summary

JOSHUA KIRSCHENBAUM (jkirschenbaum@securingdemocracy.org) is a Senior Fellow at the German Marshall Fund (Washington DC)*

NICOLAS VÉRON (nicolas.veron@bruegel.org) is a Senior Fellow at Bruegel and the Peterson Institute for International Economics**

* Kirschenbaum was formerly at the US Treasury's Office of Foreign Assets Control and Financial Crimes Enforcement Network (2011 to 2018).

** Véron is an independent non-executive director at the Global Trade Repository arm of DTCC, including DTCC Derivatives Repository plc (London), which is supervised by the European Securities and Markets Authority.

A SERIES OF banking scandals in multiple European Union countries including Cyprus, Denmark, Estonia, Latvia, Malta, the Netherlands and the United Kingdom has underlined the shortcomings of the European Union's anti-money laundering (AML) regime. Many of these cases have involved staggering sums, with billions of dollars laundered through accounts at one bank. The impact of the EU's AML shortcomings has been further underlined by changing geopolitics and by the new reality of European banking union.

THE EU LEGAL framework combines a strong, enforceable single market with national AML supervision of banks and other financial and non-financial firms in which the mechanisms to ensure EU-wide supervisory consistency are insufficient. This combination fosters a vicious circle of erosion of supervisory effectiveness in those member states where money launderers tend to concentrate their activity, which undermines the integrity of the entire European system.

THE IMPERATIVE OF establishing sound supervisory incentives to fight illicit finance effectively demands a stronger EU-level role in AML supervision. We recommend a unitary architecture centred on a new European AML Authority that would work on the basis of deep relationships with national authorities such as financial intelligence units and law enforcement agencies. The new authority should have high standards of governance and independence, publish all its decisions and be empowered to impose sufficiently large fines to deter malpractice. It would also act as a catalyst for further EU harmonisation of the AML legal regime.

1 Introduction

Tackling money laundering in the European Union has become more urgent in the wake of the US Treasury Department's targeting of ABLV Bank in Latvia in February 2018, and following a number of other high-profile cases of confirmed or alleged money laundering in large and small EU countries (Annex 1), and the 2015-16 disclosure of the so-called Panama Papers¹. Tackling money laundering is also a sensitive issue for the euro area's fledgling banking union because national AML supervisory failures result in reputational risk for the European Central Bank (ECB) in its new capacity of prudential supervisor. Current debates about AML policy also take place amid greater awareness in Europe of the linkage between illicit finance and security threats, not least the risk of interference by Russia and other third countries in EU domestic matters, and of the imperative for Europeans to have the capacity to address such threats credibly and autonomously if need be².

The ECB has made clear that it is not responsible for AML supervision under the existing legal framework, but it has also expressed its dissatisfaction with the *status quo*. In March 2018, ECB Supervisory Board Chair Danièle Nouy said of the US Treasury Department's AML intervention in relation to ABLV³ that it was “*very embarrassing to depend on the United States to do the [AML] job. This has to change [...] We need a European institution that is implementing in a thorough, deep, consistent fashion this [AML] legislation in the euro area*”⁴. In September, ECB Executive Board Member Benoit Coeuré said: “*We support any initiative that leads to a more harmonised and more coordinated approach to anti-money laundering. Ideally this would be a single [AML supervisory] agency*”⁵.

The international media has echoed these concerns. In March 2018, a *Bloomberg View* editorial argued that “*responsibilities over money laundering should be handed to a European institution, and EU rules should be changed to give the ECB more freedom to promptly withdraw banking licenses*”⁶. In July 2018, a *Financial Times* editorial titled ‘The EU is losing its battle against money laundering’ concluded that, until there is “*political will*” to “*create a centralised European body for dealing with money laundering [...], the international McMafia will continue to find plenty of ways to funnel its illicit billions through the pipework of the European financial system*”⁷. Another *Financial Times* editorial, on 5 September 2018, was titled ‘EU needs a central body to stop money laundering’.

This Policy Contribution focuses primarily on the architecture for AML supervision in the European Union and its internal market. It is obvious, however, that even radical reform in that area should not be viewed as a panacea that that would address all the problems of Europe's current AML policy. AML is difficult and will remain so. Even so, a better supervisory architecture could make a material difference and significantly enhance the effectiveness of the EU's AML efforts.

1 The Panama Papers, a set of millions of documents leaked in 2015 from the Panama-based law firm Mossack Fonseca, exposed the widespread use of anonymous companies and offshore bank accounts in furtherance of activity that may breach AML rules.

2 The related challenge of combating the financing of terrorism (CFT), often paired with AML, eg in G20 discussions and largely reliant on the AML institutional infrastructure, is not separately covered in this paper.

3 The US Treasury Department found under Section 311 of the US PATRIOT Act that ABLV was of “*primary money-laundering concern*”. The bank went into voluntary liquidation shortly afterwards. See Annex 1.

4 Quoted from Ivan Camilleri, ‘Pilatus Bank incident ‘embarrassing’, says European Central Bank supervisor’, *Times of Malta*, 28 March 2018, and from European Parliament (2018b). The video of Ms Nouy's 26 March hearing is available at <http://www.europarl.europa.eu/ep-live/en/committees/video?event=20180326-1500-COMMITTEE-ECON>.

5 Francesco Guarascio and Jan Strupczewski, ‘ECB's Coeuré says EU should have agency to fight money laundering’, *Reuters*, 7 September 2018.

6 Bloomberg Opinion Editorial Board, ‘Latvia's ABLV Bank Has a Lesson for the ECB’, *Bloomberg View*, 19 March 2018.

7 *Financial Times*, ‘The EU is losing its battle against money laundering’, 5 July 2018.

We start in the next section by briefly outlining the general features of AML policy, before summarising the current supervisory arrangements and ongoing policy developments in the EU (section 3). Section 4 describes the AML supervisory framework in the United States, which is doubly relevant to the EU debate, as both a significant comparison point and as a high-impact environmental factor – as illustrated by ABLV. Section 5 details the challenges faced by the EU’s current AML supervisory architecture and explores options to address them⁸.

2 AML: basic concepts

Money laundering is the execution of a financial transaction involving the proceeds of a criminal act with the intent to conceal the origin of the funds⁹. A common shorthand for the steps involved is ‘placement, layering, and integration,’ which refers to the injection of criminal proceeds into the financial system (placement), the transfer of those proceeds to obscure their origin (layering) and the successful investment, use, or withdrawal of the laundered money (integration). An AML regime is a set of rules requiring financial institutions or other entities to maintain controls and processes (an AML programme) to detect and report such activity, with the goal of enabling the government to discover, track, prevent or punish it. As a consequence, cases of AML violations may be disconnected from cases of actual money laundering. A bank’s failure to put adequate reporting systems in place, for example, might constitute a serious AML violation even in the absence of any criminal activity. Conversely, criminals might successfully launder money through a bank without the aid of a breakdown in the bank’s AML programme. Moreover, an AML supervisor imposing an administrative AML fine might not seek, or even be able, to determine that a bank actually facilitated the laundering of criminal proceeds.

Countries began to establish AML regimes in the 1970s and 1980s to assist criminal investigations, largely related to the laundering of the cash proceeds of drug trafficking and other organised criminal activity¹⁰. Over time, the purpose and scope of AML regimes have evolved. With increased financial globalisation and unrestricted cross-border financial flows, AML regimes have shifted their focus from cash to electronic transactions. As the regimes themselves have become more sophisticated, criminals and their facilitators have responded, leading to an AML arms race between governments and criminals. The end of the Cold War and the lull in great-power conventional military conflicts led to an increased focus on unconventional security threats, including terrorist finance¹¹, tax evasion, weapons proliferation, human trafficking, sanctions circumvention and kleptocracy. Governments now expect their AML regimes to help address all of these issues in a manner that was not foreseen fifty years ago, such that their scope is best described as countering all forms of illicit finance¹².

8 This structure is intended to address the authors’ observation of significant unmet needs for mutual understanding in this area on both sides of the Atlantic. The inevitable consequence is that some parts of the paper’s argument will be of little information value to sections of its readership. Thus, section 2 is probably best skipped by AML experts in general, section 3 by EU banking experts, and section 4 by US AML or banking experts.

9 See eg the definitions by the Financial Action Task Force and the US Treasury, available respectively at <http://www.fatf-gafi.org/faq/moneylaundering/> and <https://www.fincen.gov/history-anti-money-laundering-laws>.

10 The history of AML legislation in the United States since 1970 is developed on the US Financial Crimes Enforcement Network website at <https://www.fincen.gov/history-anti-money-laundering-laws>.

11 Although terrorist financing would typically make up a small percentage of illicit finance activity in most jurisdictions, the 11 September 2001 attacks on the US galvanised the overhaul of AML regimes and increased the political salience of illicit finance. Efforts to combat terrorism in general and terrorist financing in particular draw on the financial information collected under AML regimes and combine it with other reporting streams, including intelligence collection and law-enforcement investigations.

12 Reuter and Truman (2004) review and critique the US and global AML frameworks as existed at that date.

Global standards for AML regimes were first formulated in 1989 following the creation of the Financial Action Task Force (FATF) at the G7 Summit in Paris¹³. Since then, FATF has set out 40 standards ('recommendations') that cover AML rules for financial and other entities to be enforced by public authorities, the proper criminalisation and prosecution of money laundering, the creation of financial intelligence units and transparency steps such as the availability of information about the beneficial owners of legal entities and arrangements such as trusts¹⁴. FATF has 35 member countries, including the 15 pre-2004 EU member states, plus two regional members, the European Commission and the Gulf-Co-operation Council. Most of the world's other jurisdictions are members of nine FATF-Style Regional Bodies (FSRBs), such as MONEYVAL for (mostly) eastern Europe, which includes the other 13 EU countries¹⁵. FATF and the FSRBs organise mutual evaluations of their member jurisdictions for compliance with FATF recommendations. FATF also implements a process to identify jurisdictions with strategic AML (or CFT) deficiencies (greylisting) or those whose failure to address such deficiencies is ongoing and might require action by other members (blacklisting)¹⁶.

The efforts of individual jurisdictions to combat money laundering rest on three pillars:

- **The first pillar consists of administrative authorities:** AML supervisors. AML supervisors examine entities for adherence to the jurisdiction's AML regime and typically have the power to impose fines for non-compliance. These entities include banks and other financial firms but can also include casinos, precious metals dealers and – in the European Union – art dealers, lawyers and accountants. The United States puts less emphasis than the European Union on AML supervision of non-financial firms (see section 4). Correspondingly, the scope of entities subject to AML supervision is often referred to as "*covered financial institutions*" in the United States, while the European Union uses the broader expression "*obliged entities*". As a result, several sector-specific AML supervisors coexist in most, though not all, jurisdictions¹⁷. In accordance with FATF recommendations, most AML regimes require obliged entities to maintain a risk-based AML programme, meaning the extent of surveillance and controls over activity at the institution should be commensurate with the risk profiles of the various clients and lines of business. Such programmes oblige these entities to identify and perform due diligence on their customers, conduct transaction monitoring, retain and produce certain records and file suspicious activity reports¹⁸.

For obliged entities that are also subject to a prudential supervision regime, such as

13 A permanent FATF Secretariat is hosted in Paris at the Organisation for Economic Co-operation and Development (OECD).

14 The most recent set of FATF standards/recommendations was published in 2012 and is available at <http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF%20Recommendations%202012.pdf>. In addition, FATF has issued nine special recommendations focused on combating the financing of terrorism.

15 MONEYVAL, or the Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism, is a permanent body of the Council of Europe that was established (under a different name) in 1997. It includes 25 countries in central, eastern and southeastern Europe and the Caucasus (including Moldova, Russia and Ukraine), plus nine small western European jurisdictions (Andorra, Gibraltar, Guernsey, Jersey, Liechtenstein, the Isle of Man, Monaco, San Marino and the Vatican). The European Commission and Secretariat-General of the Council have observer status. More detail is at <https://www.coe.int/en/web/moneyval/moneyval-brief>. A list of all FSRBs and their membership is available on the FATF website at <http://www.fatf-gafi.org/countries/>.

16 As of end-September 2018, there were eight greylisted jurisdictions (Ethiopia, Pakistan, Serbia, Sri Lanka, Syria, Trinidad and Tobago, Tunisia and Yemen) and two blacklisted ones (Iran and North Korea; see <http://www.fatf-gafi.org/countries/#high-risk>).

17 In the United States, FinCEN is the sole AML supervisor in principle, but in practice it delegates many of the tasks to other agencies (see section 4). Some EU jurisdictions also have a single AML supervisor (section 3).

18 In the United States, the Federal Financial Institutions Examination Council (which brings together various supervisors) maintains a Bank Secrecy Act/AML Examination Manual, available at https://www.ffiec.gov/bsa_aml_infobase/pages_manual/manual_online.htm. The closest equivalent at the EU level is the AML/CFT Guidelines published by the ESAs Joint Committee in June 2017, available at <https://www.eba.europa.eu/-/esas-publish-aml-cft-guidelines>. There are also national guidelines/manuals in individual EU member states.

banks, there are synergies between prudential supervision and AML supervision. In many jurisdictions, the two functions are performed by the same supervisory institution. Even when that is not the case, prudential supervisors rely on AML supervisors for information that is relevant to their authorisation and review processes, and conversely, AML supervisors often delegate supervisory tasks to prudential authorities. But there are also significant differences in terms of supervisory arrangements, culture and practices. One example is in the approach to cross-border activities. While the prudential supervision of banks' foreign branches is (under the Basel Concordat and subsequent legislation in individual jurisdictions) the responsibility of home supervisors (ie those of the parent bank's country), the AML supervision of bank branches is a matter for host-country authorities, even as the home supervisor has responsibility for the bank's overall governance and risk controls.

- **The second pillar consists of Financial Intelligence Units (FIUs)**, which collect, analyse and disseminate the reporting submitted by obliged entities under applicable AML programme requirements. There is only one FIU for each jurisdiction. Their organisational setups are not uniform, however: FIUs may be units of administrative agencies, law enforcement bodies or the judiciary, or even stand-alone agencies of their own. FIUs aim to support the activities of AML supervisors and law enforcement agencies. They participate in a dedicated global body, the Egmont Group¹⁹. Facilitated by Egmont, FIUs share financial intelligence with their foreign counterparts, either proactively or upon request. The bar for such sharing is lower than the threshold necessary to obtain evidence for trial under a mutual legal assistance treaty request²⁰.
- **The third pillar consists of law enforcement agencies and the justice system.** They are responsible for the investigation and prosecution of individuals and entities that commit criminal violations related to money laundering. Such violations most often take one of two forms. The first is the traditional criminal offense that most people think of in connection to money laundering. In many jurisdictions, criminal money laundering charges require prosecutors to prove that the accused knowingly conducted a transaction with funds derived from criminal proceeds, ie that an underlying crime, known as a 'predicate offence', occurred²¹. Although it can be brought as a standalone charge, money laundering is often appended to charges related to the predicate offence itself. The second type of offence that can be criminally prosecuted is the intentional violation of AML programme requirements by an obliged entity or its officers, a charge that prosecutors must prove in court using a criminal standard of evidence.

This global framework for AML has grown organically. It has attracted criticism, for example, for causing certain categories of stakeholders to be cut off from access to banking or remittance services, a theme often referred to as 'de-risking' (eg Global Centre on Cooperative

19 The Egmont Group of FIUs was formed in 1995 at a meeting that took place at the Egmont Palace in Brussels, thus its name. It established a permanent secretariat in Toronto in 2008. Among its 156 members are the FIUs of all EU member states and also those of Andorra, Anguilla, Aruba, Bermuda, the British Virgin Islands, Iceland, Jersey, Guernsey, Liechtenstein, the Isle of Man, Monaco, Norway, San Marino, Sint Maarten, Switzerland and the Vatican.

20 The lack of a similar channel to facilitate the direct sharing of information between AML supervisors is a significant gap in the current global framework to combat money laundering.

21 See for example, for the United States, Section 2101 of the Department of Justice (DOJ) U.S. Attorneys' Manual, available at <https://www.justice.gov/usam/criminal-resource-manual-2101-money-laundering-overview>, and the DOJ's Money Laundering and Asset Recovery Section, available at <https://www.justice.gov/criminal-mlars>. In many countries, prosecutors or investigative judges can also pursue asset forfeitures (seizure or confiscation of assets by public authorities) as part of money laundering proceedings, although asset forfeitures are not limited to financial crimes. In the EU, a draft directive on the criminalisation of money laundering (COM(2016) 826 published on 21 December 2016 and expected, at time of writing, to be enacted and published shortly) opens up the possibility of prosecution for money laundering without proving a predicate offence to a criminal standard, as is already the case in, for example, Sweden.

Security and Oxfam, 2015). Others have criticised contemporary AML for in effect passing on policing responsibilities to financial institutions. However, we take the framework as it is and do not attempt to address those fundamental critiques, focusing instead on how the EU can improve its framework.

3 Current supervisory framework and AML policy developments in the EU

Ten years ago, the EU financial services (including AML) policy framework consisted of legislation that was partly harmonised at EU level and enforced almost exclusively at national level. This landscape has undergone radical changes in the past decade. The resulting structure is extremely complex, with an awkward coexistence of national and supranational features, many new and untested aspects, and widespread expectations of more change to come in the near future. Box 1 gives an overview of the structure of EU financial regulation and supervision.

Box 1: EU financial legislation, regulation and supervision

EU laws can be ‘directives’, framework laws that demand additional legislation (‘transposition’) in each member state, or ‘regulations’ – laws that are directly applicable in all member states with no need for national transposition. ‘Maximum harmonisation’, or the establishment of identical legislative arrangements in all EU countries (as opposed to minimum standards or ‘minimum harmonisation’), is most easily achieved through regulations, even though these might also leave flexibility to member states on how to implement them. In terms of financial services laws, most (though not all²²) EU directives and regulations are based on Article 114 of the Treaty on the Functioning of the European Union (TFEU), which forms the basis for all European single market laws. Such laws are always initially proposed by the European Commission, then negotiated by the Council of the EU (composed of representatives from all member states) and the European Parliament (whose members are elected by universal suffrage to a five-year term)²³. Confusingly, what are known in the United States (and in many EU member states) as regulations, ie rules issued by administrative agencies under a general framework established by laws, are referred to as ‘binding technical standards’ when issued at the EU level, typically by the European Commission upon the proposal of the relevant European supervisory authority²⁴.

The ‘Single Rulebook’ is a non-legal expression that refers to the aim of maximum harmonisation in EU financial services rulemaking, or to the subset of applicable rules which is maximally harmonised. An example of the Single Rulebook is the Capital Requirement Regulation (Regulation No. 575/2013), enacted in 2013 on the basis of the Basel III Accord of 2010,

22 A significant exception is the SSM Regulation of 2013, which is based on Article 127(6) TFEU and had thus to be adopted by unanimous vote of the member states with only a consultative role for the European Parliament.

23 The Council of the EU, or the Council, and the European Parliament are together known in EU-speak as the co-legislators. The Council is not to be confused with the European Council, which refers to meetings of the EU member states’ heads of state and government to provide policy direction but without formal involvement in the EU legislative process, or with the Council of Europe, which is a human rights organisation not directly related to the European Union and with a significantly broader geographical scope and membership.

24 An exception is ECB rules that are also known as ECB Regulations. The ESAs also issue documents known as regulatory guidelines and recommendations, which are generally observed by market participants but are not legally binding.

that sets largely uniform capital requirements for banks throughout the European Union with a transition period that expires in January 2019. The expression Single Rulebook was coined in a landmark report by a task force led by former central banker Jacques de Larosière in 2008-09 (European Commission, 2009). The Larosière Report also set the basis for the creation of three so-called European Supervisory Authorities (ESAs) that help to coordinate financial regulation and supervision in the European Union: the European Banking Authority (EBA) in London (which will move to Paris because of Brexit), the European Insurance and Occupational Pensions Authority (EIOPA) in Frankfurt, and the European Securities and Markets Authority (ESMA) in Paris²⁵. All three were established on 1 January 2011. The banking union, currently consisting of the Single Supervisory Mechanism (SSM)²⁶ and the Single Resolution Mechanism (SRM), was initiated in mid-2012 and entered into full force in November 2014 (SSM) and January 2016 (SRM). Draft legislation proposed by the European Commission, but not at the time of writing adopted by the co-legislators, includes a November 2015 proposal for a European Deposit Insurance Scheme, which if adopted would represent a significant step towards completing the banking union, and a September 2017 proposal for significant reform of the ESAs ('ESAs Review').

The geographical scope of the ESAs' authority is the entire European single market, including the 28 EU member states and other members of the European Economic Area (EEA), namely Iceland, Liechtenstein and Norway²⁷. By contrast, the geographical scope of the banking union, and thus of the SSM and SRM, is currently limited to the 19 euro-area countries. It might expand in the future through the process of 'close cooperation' that allows non-euro member states to join the banking union voluntarily²⁸.

The banking union for prudential supervision of banks

The founding legislative basis of the banking union, the Single Supervisory Mechanism (SSM) Regulation of 2013, stipulated the transfer of all bank licensing authority in the euro area from national banking supervisors to the Frankfurt-based European Central Bank²⁹. In principle, ECB prudential supervisory decisions are made (like other ECB decisions) by the Governing Council, the ECB's highest body, but in practice the central decision-maker is the SSM Supervisory Board, an internal body of the ECB, whose decisions the Governing Council almost never declines to endorse.

The SSM Regulation introduced a major distinction between banks or banking groups deemed Significant Institutions (SIs), for which the ECB has sole prudential supervisory

25 Contrary to what their name suggests, the ESAs currently do not have direct supervisory authority over financial firms for either prudential or AML purposes. ESMA alone has direct conduct-of-business supervisory authority over some firms (see section 5). All three ESAs have the authority to impose direct decisions on financial firms in special circumstances such as emergency, which have however never been invoked yet since the ESAs' establishment in 2011.

26 As explained below, the supervisory authority of the SSM extends only to bank prudential matters and does not cover the AML supervision of banks.

27 Some territories and dependencies of EU or EEA member states, for example Jersey or Svalbard, are outside of single market, even though they might benefit from special *ad-hoc* arrangements. The four other sovereign microstates of Western Europe (Andorra, Monaco, San Marino and the Vatican) are similarly outside of the single market. Gibraltar has special arrangements which make it for most practical purposes a participant in the single market. Switzerland is not in the single market for financial services. At the time of writing, it remains to be determined whether the UK will leave the single market, and if so, when.

28 Bulgaria is expected to enter close cooperation in mid-2019 as part of a process to eventually join the euro area. Several other non-euro countries are at various early stages of consideration or preparation of close cooperation.

29 This framework is in some respects more centralised than in the United States, where many banks operate on a state license (or charter) not a federal one - see section 4. A minor exception to the ECB monopoly of bank licensing is for euro-area branches of banks domiciled in non-EEA countries, the licensing of which remains the responsibility of national authorities. Unlike subsidiaries, such branches do not benefit from a single market passport.

authority, and (generally smaller) Less Significant Institutions (LSIs), the day-to-day supervision of which remains at the national level. SIs include all banks above €30 billion in total assets, plus others according to certain additional criteria³⁰. There were 116 SIs and slightly fewer than 3,000 LSIs as of mid-2018³¹. As of end-2017, SIs represented about 81.5 percent of the system's total assets (ECB, 2018a). Ninety-one of the 116 SIs were banking groups headquartered in the euro area, while the other 25 were euro-area operations of banking groups headquartered elsewhere³².

For SIs, while the ECB has sole prudential supervisory authority, relevant national agencies, referred to as National Competent Authorities (NCAs)³³, also participate in the process through Joint Supervisory Teams (JSTs). A JST brings together supervisory staff at the ECB in Frankfurt (up to a dozen for the largest banks) together with staff from the NCAs of the countries where the supervised banking group has significant operations. The JST is led at the ECB by a JST coordinator (functionally equivalent to a Central Point of Contact in the US Federal Reserve system), while each NCA's staff group within the JST is led by a JST sub-coordinator. The coordinator and sub-coordinators prepare supervisory decisions together; in case of disagreement, the decision proposal is made by the coordinator alone, with mention of the dissenting opinion(s).

For LSIs, day-to-day prudential supervisory decisions are made by the relevant NCA, including setting regulatory requirements, assessing the bank's soundness and vetting of management and supervisory board appointments to ensure that all banks' key decision-makers are fit and proper (F&P). By contrast, common procedures apply to authorisation processes in which decisions are made by the ECB for LSIs and SIs alike. These common procedures include decisions on bank licensing (including issuance of new licenses and the withdrawal of existing ones) and the vetting of acquisitions of qualifying holdings (ie changes in ownership that may influence the bank's governance and control). The NCAs' day-to-day prudential supervision of LSIs is subject to the ECB's formal processes of supervisory oversight, sometimes referred to as indirect supervision.

In non-euro-area member states, all prudential supervisory tasks are carried out by the relevant NCA, eg the UK Prudential Regulation Authority (PRA) which is itself controlled by the Bank of England. The EBA has authority to foster supervisory coordination and convergence, in addition to its role in the preparation of EU banking legislation and binding technical standards. For example, the EBA is the central coordinator and publisher of regular pan-European stress testing exercises, which are conducted by the SSM (in the euro area) and NCAs (elsewhere in the Internal Market).

The other existing pillar of the banking union, the SRM, is not detailed here as it has no direct role in the AML framework.

AML rules and enforcement framework

EU legislation on AML was first initiated in the early 1990s, following AML developments in individual member states. To date, there have been five successive AML Directives (AMLDs)³⁴.

30 Thus, for example, ABLV was a SI before its liquidation, despite having only €3.6 billion in total assets, because it was one of the three largest banks headquartered in Latvia.

31 ECB (2018b) lists 119 SIs, but three of these are cases of double-counting, namely Slovakian subsidiaries of banking groups headquartered elsewhere in the euro area.

32 In 19 of these 25 cases, the parent group was headquartered in another European internal market country (Norway, Sweden and UK; the listing predates the move of Nordea's headquarters from Stockholm to Helsinki). The remaining six were controlled, respectively, by Citi, JP Morgan, Bank of New York Mellon, State Street, Russia's VTB and Venezuela's Banesco. This latter group is expected to expand because of Brexit.

33 Depending on the euro-area country, the NCA for prudential banking supervision is either the national central bank, eg in Italy or the Netherlands, or a specialised agency, eg in Finland or Germany.

34 Namely, AMLD of 1991 (91/308/EEC, amended by AMLD2 and repealed by AMLD3); AMLD2 of 2001 (2001/97/EC, repealed by AMLD3); AMLD3 of 2005 (2005/60/EC, repealed by AMLD4); AMLD4 of 2015 ((EU)2015/849); and AMLD5 of May 2018 ((EU)2018/843). Other acts of EU legislation are relevant for AML, for example the Fund Transfer Regulation of 2015 ((EU)2015/847).

AMLD4 has been in force since June 2015 with a deadline for transposition by member states of 26 June 2017³⁵. The deadline for transposition of most of AMLD5 is 10 January 2020. The successive AMLDs have generally followed (or even exceeded) FATF recommendations and expanded the scope of obliged entities subject to AML supervision, tightened the definitions of suspicious activities and the processes to identify and report them, put gradually greater emphasis on ultimate beneficial ownership and risk-based approaches, and lifted obstacles that prevented communication between relevant authorities³⁶.

AML supervision in EU member states is conducted by a wide range of national authorities. Annex 2 lists individual countries' FIUs and authorities responsible for the AML supervision of banks (the AML supervisors of non-bank obliged entities are not listed). As this list illustrates, EU member states exhibit many different combinations, typically inherited from complex histories. Depending on the country, the FIU may be part of the finance ministry, the central bank, the national police, the interior ministry, the prosecutorial service, the customs service, the justice ministry or could be a dedicated independent agency with its own governance and accountability framework. The AML supervisor of banks is generally the same as their prudential supervisor, but this is not universally the case. In the UK the AML supervisor is the Financial Conduct Authority (FCA), and in Malta, Poland, and Spain, the AML supervisor is the FIU even though it may delegate certain tasks to the prudential supervisor. In keeping with the global practice, and unlike in prudential supervision, AML supervisors in the EU are responsible for both domestic banks and branches of non-domestic institutions, which can introduce complications if the supervisor of the parent is not aware of goings-on at the branch.

The EBA oversees member states' AML supervision of banks much as it does their prudential supervision. In particular, under Article 17 of its eponymous Regulation, the EBA may investigate cases of "breaches of Union law" and even in some circumstances override individual decisions of national authorities. This, however, can typically only happen after a large-scale (prudential or AML) supervisory failure and not more proactively, which is why the EBA has described its breach-of-Union-law powers as "a rather blunt tool" (European Parliament, 2018a). The EBA's first-ever finding of breach of Union law for AML matters was reported in its recommendation to the Maltese FIU following the case of Pilatus Bank, published in July 2018 (EBA, 2018b). Ongoing investigations are underway at time of writing in Denmark, Estonia, and Latvia (Annex 1). EIOPA and ESMA (see Box 1) have similar mandates to foster supervisory convergence in their respective (non-bank) sectors. The Joint Committee that facilitates coordination among the three ESAs has an AML sub-committee, known as AMLC³⁷.

Other EU institutions also play a role. A computer network known as FIU.net was developed in the 2000s following a Council decision in 2000³⁸, and in 2016 was integrated into the EU Agency for Law Enforcement Cooperation, known as Europol. According to Europol, "FIU.net is designed to facilitate the highly secure connections required for these exchanges of information [among FIUs]"³⁹. The European Commission and EBA have explored ways to further improve cooperation between EU FIUs, including the establishment in 2006 of the EU

35 As of July 2018, at least six member states (Greece, Ireland, Latvia, Malta, Romania and Spain) had failed to fully transpose the AMLD4. See European Commission press release, 'Infringements: Commission refers Greece, Ireland and Romania to the Court of Justice for not implementing anti-money laundering rules', available at http://europa.eu/rapid/press-release_IP-18-4491_en.htm.

36 The European Commission (2018) observed, however, that even if the changes associated with the future implementation of AMLD5 are factored in, "Cooperation between prudential authorities and AML supervisors is also largely dependent on the good faith and willingness of the relevant authorities."

37 A description of AMLC is at <https://esas-joint-committee.europa.eu/Pages/Activities/Anti-Money-Laundering-Objectives-and-Tasks.aspx>.

38 'Council Decision of 17 October 2000 concerning arrangements for cooperation between financial intelligence units of the Member States in respect of exchanging information', available at <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32000D0642&from=EN>.

39 Source: Europol's website at <https://www.europol.europa.eu/about-europol/financial-intelligence-units-fiu-net>.

FIUs' Platform, an informal group that supports occasional projects⁴⁰. The European Union's Judicial Cooperation Unit, known as Eurojust and established in 2002, works to coordinate criminal investigations and prosecutions of cross-border crimes in the European Union, including money laundering cases. Eurojust, however, has no autonomous powers to investigate or prosecute.

Recent policy developments

In May 2018, the European Commission initiated joint work on AML reform with the ECB and the three ESAs⁴¹. The first outcome of this work was a reflection paper sent to member states in late August 2018. This paper has not been made public by the EU institutions, but its text was commented on in the media⁴² and later posted online by a member of the European Parliament⁴³.

On 12 September 2018, in his yearly State of the European Union address, European Commission President Jean-Claude Juncker announced new measures to reinforce the effectiveness of AML enforcement, and the European Commission on the same day published proposals for corresponding amendments to the ESAs Review legislation. If adopted, these amendments would, among other things, confer on the EBA additional authority to request that national AML supervisors investigate potential breaches and consider actions, and in extreme cases of non-compliance by the national authority, to impose some direct decisions (though not fines) on individual firms. It would also empower the EBA to carry out periodic independent reviews of AML issues and risk assessment exercises and to collect data on AML supervision in the European Union (European Commission, 2018). Unlike existing EBA competencies, this new authority would extend beyond the banking sector to other categories of supervised financial firms. This would effectively deprive EIOPA and ESMA of their existing AML roles, and as a consequence, the AMLC would be integrated into the EBA. As with the rest of the ESAs Review, however, the likelihood of adoption of these amendments before the end of the current EU parliamentary term in the spring of 2019 is hard to assess at the time of writing.

European AML in practice

AML enforcement in the European Union is extremely heterogeneous. It is also impossible to observe comprehensively from publicly available information sources, because disclosure practices vary considerably from one national authority to another⁴⁴. For example, AML fines have so far either been entirely anonymised or not published at all in Denmark, Germany and Spain. In France, Sweden and the UK, by contrast, fines are published and their subjects identified in most or all cases⁴⁵. Even in the latter circumstance, however, the publication format has often made it difficult or impossible to understand the exact nature of the violations, and thus to assess their seriousness, and, as a consequence, the punitive or deterrent impact of a given fine. In principle, Article 60 of AMLD4 mandates member states to publish most

40 See European Commission (2017), section 2.2.4. and accompanying staff working document, and EU FIUs' Platform (2016), the final report of an extensive collaborative study.

41 The letter of 8 May 2018 establishing this work process was signed jointly by the Commission's First Vice-President Frans Timmermans, Vice-President Valdis Dombrovskis and Commissioner Vera Jourova. It refers to "a number of high profile incidents in recent months" as a reason for the endeavour. It was published by *Politico* and is available at https://www.politico.eu/wp-content/uploads/2018/05/Letter-to-SSM-EBA-EIOPA-and-ESMA_signed.pdf.

42 Jim Brunsten, Caroline Binham, and Claire Jones, 'Scandals expose weakness of EU's dirty money fight, say watchdogs', *Financial Times*, 5 September 2018.

43 Available at https://sven-giegold.de/wp-content/uploads/2018/09/COM-Reflection-paper-on-elements-of-a-Roadmap-for-seamless-cooperation_Sept-2018.pdf.

44 A number of quantitative indicators were collected on an EU-wide comparative basis and published in the final report of the European Commission-sponsored ECOLEF Project five years ago (Unger, 2013).

45 Some countries, such as France, have exceptions in case of a perceived threat to financial stability or of disproportionate impact to the fined entity in case of disclosure.

decisions including the identity of the affected person or entity and the nature of the breach⁴⁶, but it is not clear that all member states comply with this requirement, and the deadline for transposition (June 2017) is too recent for a firm assessment. From discussions with practitioners conducted for this paper, the UK FCA appears to have a reputation for imposing higher fines for AML violations than most other national authorities, even as fines are often much higher still in the United States⁴⁷. Among other EU member states, interviewees mention Italy and Germany as imposing very low fines for AML violations, whereas France is somewhere in between. Mutual evaluation reports published by FATF and MONEYVAL provide some qualitative detail but do not allow for a comprehensive comparison of AML enforcement and its effectiveness across EU/EEA member states.

Recent cases for which some information is publicly available are summarised in Annex 1. Many of these events occurred in smaller euro-area countries, where resources for supervisory oversight are typically constrained. There are two important caveats, though, that suggest caution about causality in that observation. First, major money laundering incidents at EU banks have not been limited to smaller jurisdictions and have also occurred in major financial centres such as London. Second, it is intrinsically hard to ascertain whether more publicised cases of prominent money laundering reflect a greater frequency of money laundering in a given jurisdiction, or, conversely, a greater willingness on the part of the jurisdiction's authorities to root out problems and tackle illicit activity – or both.

4 AML in the United States

The AML regime in the United States is based on a body of laws referred to as the Bank Secrecy Act (BSA), which is found in Titles 12 and 31 of the country's code of federal laws (the United States Code or USC) and further implemented via regulations in Title 31 of the Code of Federal Regulations (CFR)⁴⁸.

The US Treasury Department has the authority to administer the BSA and delegates that authority to the Financial Crimes Enforcement Network (FinCEN), a bureau within Treasury, by Treasury Order 180-01. FinCEN is both the AML supervisor in the United States – setting rules for financial institutions, providing interpretive guidance and issuing penalties – and the country's FIU, supporting law enforcement and other regulators⁴⁹.

As of 2013, FinCEN directly employed approximately 340 people (Shasky Calvery, 2013). Most of these personnel are devoted to its financial intelligence analysis, policymaking and technology functions, rather than to enforcement and supervision.

FinCEN relies on other federal financial supervisors⁵⁰, which are much larger organisations and to which FinCEN has delegated its AML supervisory authority, for the efficient examination of most covered financial institutions⁵¹. With respect to AML supervision of the

46 Article 60 of AMLD4 also has exceptions in case of disproportionate impact or financial stability risk.

47 Very recently, the Dutch central bank has also moved to impose large fines as documented in Annex 1. Article 59 of AMLD4 raised and harmonised the maximum amount of AML fines to “at least €5 million or 10 percent of the total annual turnover” of the affected entity. As with publicity of decisions, however, it is too soon to assess the extent to which this new legislation has fostered convergence of actual behaviour of national AML supervisors.

48 The relevant statutory framework is found at 12 USC 1829, 12 USC 1951-1959 and 31 USC 5311-5314, 5316-5332. The implementing regulations are codified at 31 CFR Chapter X.

49 FinCEN programmes are detailed at https://www.fincen.gov/sites/default/files/shared/Appendix_A.pdf.

50 Throughout this section, we adopt the European habit of referring to authorities that supervise financial institutions as ‘supervisors’ rather than ‘regulators’, even though the latter term is also commonly used in the United States. Specifically, a bank's prudential supervisor at the federal level is called its Primary Federal Regulator.

51 There does not appear to be a specific headcount of the staff that focuses on AML tasks within these supervisory agencies.

banking sector alone, these agencies include the Office of the Comptroller of the Currency (OCC), the Federal Reserve System, the Federal Deposit Insurance Corporation (FDIC) and the National Credit Union Administration (NCUA). The OCC supervises federally (or nationally) chartered banks, many of which are also members of the Federal Reserve System. The Federal Reserve System supervises its member banks that are state-chartered, and other entities such as bank holding companies⁵² and foreign banking organisations. The FDIC is the federal supervisor of state-chartered banks that are not members of the Federal Reserve System, typically the smaller ones, and insures all bank deposits, which entails special (backup) supervisory authority over all banks. The NCUA is the supervisor of credit unions and insures their deposits⁵³. The responsibility for the issuance and revocation of banking licenses, F&P checks of management and board members, and review of ownership changes, either belongs to one of these federal supervisors or (for state-chartered banks) to the relevant state-level supervisor, or both⁵⁴.

The US system of AML supervision, then, is a complex patchwork that developed organically and has not been streamlined. This has advantages and disadvantages. On the negative side, there are multiple oversight authorities, none of which has the complete picture of operations inside a large financial institution, and coordination among agencies can be cumbersome. In a big universal bank (ie diversified banking group), the depository bank is typically chartered and supervised by the OCC; large portions of business activity, including investment banking and securities and derivatives trading, are under the jurisdiction of the Securities and Exchange Commission, the Commodity Futures Trading Commission and their associated self-regulatory organisations, the Financial Industry Regulation Authority (FINRA) and the National Futures Association (NFA); and the holding company is supervised by the Federal Reserve⁵⁵. The OCC would not necessarily be able to identify AML violations across non-bank business lines, but neither might the Federal Reserve. When penalties are imposed on a bank for serious AML violations, the OCC, the Federal Reserve, FinCEN and (if the violations rise to a criminal level) the Department of Justice might all be involved. This is not to mention the ability of state-level banking supervisors or prosecutors to join in, particularly the New York State Department of Financial Services. Moreover, while FINRA and the NFA are professional and competent, a private-sector self-regulatory organisation simply cannot fill the shoes of an actual government agency, and neither should it be expected to adopt the same enforcement posture.

One idea to untangle this jumble was proposed by FinCEN's former Chief Counsel, Carlton Greene, in April 2018 in testimony to the US House of Representatives Financial Services Committee. Greene (2018) called for a solution:

52 In US financial parlance, 'banks' generally refers to individual deposit-taking (depository) institutions, whereas bank holding companies are the consolidating entities of banking groups that may also include other (non-bank) activities, such as securities trading, investment banking or asset management. By contrast, banks and banking groups are often confused in EU financial discussions. This is partly linked to history, as many European countries have long relied on 'universal' banks, whereas in the United States, banks for many decades could not undertake many non-bank financial activities under the Glass-Steagall legislation of 1933.

53 Credit unions are financial cooperatives that are a separate category from banks under US law, but are similar to Europe's cooperative banks.

54 Outside the banking sector, the Securities and Exchange Commission (SEC) supervises securities firms (among others), and the Commodity Futures Trading Commission (CFTC) supervises futures commission merchants trading in derivatives. Both in turn delegate a substantial portion of their supervisory responsibility, including certain AML examinations, to their affiliated self-regulatory organisations. Kirschenbaum (2018d) explores the challenges of AML supervision of non-bank firms in the context of the United States.

55 The Federal Reserve Board delegates the corresponding supervisory tasks to the Federal Reserve Bank of the region where the relevant entity is registered. There are 12 regional Federal Reserve Banks covering the entire territory of the United States. Unlike those of national authorities in the European Union, the geographic boundaries of US Federal Reserve Districts typically do not coincide with state borders - for example, the state of Missouri is home to two different regional Federal Reserve Banks, respectively in Kansas City and Saint Louis.

“that includes closer collaboration between FinCEN and the federal functional regulators and greater authority for FinCEN to establish BSA examination and enforcement priorities across these agencies and similarly to control interpretations of BSA rules. FinCEN, by design, is uniquely positioned to understand the threats posed by illicit finance and to understand the regulatory trade-offs needed to address those threats. In addition to the benefits to FinCEN’s mission, such an approach also could substantially lessen the burdens for regulated financial institutions, and give them greater freedom to innovate and partner with FinCEN to find better solutions to illicit finance threats”

This more centralised approach would require the allocation of additional resources and personnel to FinCEN.

Two other structural weaknesses in the US AML regime – on which the European Union has made much more progress – are, first, the lack of beneficial ownership information for legal entities, which is complicated in the United States by the fact that companies are formed at the state rather than national level; and, second, the lack of AML programme requirements for managers of private investment funds such as hedge funds and private equity firms, and for intermediaries or professional service providers such as accountants, lawyers and real-estate agents.

The US does however have experienced, competent and well-resourced regulatory and law enforcement agencies with track records of aggressive enforcement and large fines. The US government history of imposing fines of hundreds of millions and even billions of dollars for AML and sanctions violations is singular⁵⁶. And while prosecutions of bankers and other sophisticated financial facilitators for criminal money laundering under the relevant statutes⁵⁷ are rare⁵⁸, and financial crime cases difficult to prove, the possibility that law enforcement and prosecutors will secure a conviction and serious prison time is more tangible in the United States than in many other countries. The United States tends to make up for certain structural weaknesses with more active enforcement. Another advantage is the membership of the Treasury Department, through its Office of Intelligence and Analysis, of the US Intelligence Community⁵⁹.

The United States also enjoys access to a powerful weapon in its AML arsenal – Section 311 of the PATRIOT Act⁶⁰. Title III of this contains numerous changes to the Bank Secrecy Act. The US Congress enacted this legislation in the wake of the terrorist attacks of 11 September 2001. The Section 311 authority, which the Treasury Department has delegated to FinCEN, enables the US government to target administratively foreign financial institutions that it determines are “*of primary money laundering concern*” (an undefined term). It can condition, restrict or cut off those institutions’ access to the US financial system, including prohibiting the pro-

56 In 2018, US Bancorp was fined over \$600 million for AML violations, and Rabobank was fined nearly \$370 million. JPMorgan in 2014 was assessed AML penalties in excess of \$800 million. HSBC paid \$665 million for AML violations in 2012. The announcements are available on the Department of Justice’s website, respectively at <https://www.justice.gov/usao-sdny/pr/manhattan-us-attorney-announces-criminal-charges-against-us-bancorp-violations-bank>, <https://www.justice.gov/opa/pr/rabobank-na-pleads-guilty-agrees-pay-over-360-million>, <https://www.justice.gov/usao-sdny/pr/manhattan-us-attorney-and-fbi-assistant-director-charge-announce-filing-criminal>, and <https://www.justice.gov/opa/pr/hsbc-holdings-plc-and-hsbc-bank-usa-na-admit-anti-money-laundering-and-sanctions-violations>.

57 18 USC §§ 1956 & 1957.

58 Though not unheard of, such as a Miami-based Venezuelan corruption case in which the Justice Department secured a banker’s guilty plea in August of 2018. See <https://www.justice.gov/opa/pr/former-swiss-bank-executive-pleads-guilty-role-billion-dollar-international-money-laundering>. In addition to the federal Title 18 violation, money laundering is also criminalised at the state level.

59 The US Intelligence Community is a formal grouping of US government agencies with intelligence functions. In relation to the US Treasury Department, see <https://www.treasury.gov/about/organizational-structure/offices/Pages/Office-of-Intelligence-Analysis.aspx>.

60 Section 311 of the USA PATRIOT Act amended the Bank Secrecy Act by creating a new Section 5318A of Title 31 of the US Code.

vision of US correspondent accounts, effectively ending their ability to make international payments cleared in dollars. In recent years, FinCEN has targeted banks in three European countries: Andorra, Cyprus and Latvia⁶¹.

5 Challenges and options to improve the EU framework

A broad-based perception has crystallised since the ABLV case erupted in February 2018 that the European Union has an AML problem (see section 1 and Annex 1). A surge of headline-grabbing cases has entrenched the narrative that, in the words of a prominent commentator, “EU banks have become a money launderer’s dream”⁶².

Pinpointing Europe’s AML supervisory problem

Given the difficulty of observing and quantifying money laundering, it is not self-evident that malpractice has actually become more widespread in recent years. It is also possible that acceptance of it has decreased. Factors that might have led to heightened AML awareness in Europe include:

- An assertive recent stance from the United States, as illustrated by the ABLV case;
- An erosion of the perception of structural alignment between EU and US interests and a correspondingly rising perception of the need for Europe to develop its own capacity to identify threats and ensure its security;
- A greater sensitivity of the European Union and many of its member states to risks emanating from Russia;
- Improvements brought about by the implementation of AMLD4; and
- The emergence of dedicated European authorities with a mandate to oversee banking practices: first the EBA in 2011 and especially the SSM in 2014.

The last of these might have reduced overall European tolerance of supervisory failures, in contrast to an earlier era in which all relevant authorities were national and many were inclined to defend national banking champions. Irrespective of whether the problem is growing or not, it is evident that recent AML supervision in the EU has been embarrassingly ineffective, and that deep reform thus needs to be considered.

The core problem is one of supervisory incentives and of supervisory architecture. It results from the coexistence of an integrated, enforceable single financial market policy with the national structures of AML supervision. As a consequence, AML supervisory weakness in any one EU/EEA member state leads to that country becoming attractive for money launderers who can use it for access to the entire single market. This, in turn, creates a constituency in the country against forceful AML enforcement, bringing together the criminals and their representatives, an array of service providers, and potentially also government authorities that have failed in their past AML supervisory duties. If sufficiently large, this aggregate constituency might weigh on national political processes and outcomes, even in cases that stop short of outright government capture. The resulting pressures further weaken the AML supervisory framework. In sum, the combination of EU/EEA single market and national AML

61 These cases, and more in other parts of the world, are listed on FinCEN’s website at <https://www.fincen.gov/resources/statutes-and-regulations/311-special-measures>. Zarate (2013) provides narrative detail about the creation and early use of this potent instrument.

62 Patrick Jenkins, ‘Why EU banks have become a money launderer’s dream’, *Financial Times*, 17 September 2018

supervision generates national vicious circles, which tend to be self-perpetuating rather than self-correcting⁶³.

In this 'AML vicious circle' analytical framework, money-laundering and AML violations end up being asymmetrically distributed in the European Union. Some member states become weak links from which clients can be served throughout the entire single market, for those activities for which a passporting regime exists. Not all member states need be weak links for money launderers to achieve their objectives. As long as at least one weak link exists, the entire AML system is at risk of failure. A corollary is that, even if some EU member states have highly effective AML frameworks, it does not disprove the assessment of the AML problem as systemic and a matter of EU supervisory architecture. Furthermore, it is not enough to eliminate a weak link – even if the vicious circle is broken in one member state, it is likely to reappear in another. Also, not all weak-link countries need be smaller member states. While insufficient administrative capacity may be a more acute problem in very small countries, undue influence from certain special interests or other forms of institutional failure can affect larger countries as well. The variety of patterns of deficiencies in AML regimes in the European Union are illustrated in Annex 1.

To be sure, in theory national AML authorities in the other member states check transactions originating in the weak-link countries and should be able to spot suspicious activity. But this can be ineffective in practice, given national authorities' capacity constraints and priorities, and given the dense web of relationships and interdependencies that exist between them within the single market. Furthermore, within the euro/banking union area, any national authority's AML supervisory failure potentially compromises the integrity of the entire prudential supervisory framework (and of the licensing, qualifying holdings and F&P review processes) to the extent that it relies on AML assessments, as ABLV and other cases have shown. Moreover, the likely future development of financial technology and of new business models for financial intermediation and services that are inherently cross-border is likely to exacerbate the tension between the single market framework and national AML supervision⁶⁴.

Addressing the AML vicious circle: two-tier vs unitary architecture

To deal with the European Union's core AML supervisory problem, the incentives of AML supervisors should be aligned with the objective of effectively enforcing the AML framework and fighting money laundering throughout the entire single market. Breaking the vicious circle thus requires the introduction of a significant element of EU-level supervision, beyond the limited oversight that already exists.

On that basis, the EU faces a choice between two models. In an enhanced two-tier architecture that builds on the present situation, the ultimate responsibility for AML supervision of individual firms would remain at the national level, but an EU authority would be empowered to exercise some form of surveillance over national AML supervisors ('supervisor of supervisors')⁶⁵. In a unitary architecture, a European agency would have ultimate AML supervisory responsibility for firms, though this responsibility might be exercised through a network that involves national agencies and other European-level bodies.

This has become a familiar distinction in matters of European financial supervision over the past decade. Before the 2009 Larosière Report, financial supervision was entirely

63 Panicos Demetriades, a former governor of the Central Bank of Cyprus, gave a vivid description of this vicious circle: "The 'political pressure' on supervisors in small EU states with large offshore sectors, such as Cyprus, Estonia, Latvia, and Malta 'is so great that it's very hard for them to do the right thing,' Demetriades said." Quoted in Andrew Rettman, 'Cyprus: Russia's EU weak link?', *EUobserver*, 25 September 2018.

64 This argument is made more broadly for conduct-of-business supervision of fintech firms by Demertzis *et al* (2018).

65 A two-tier architecture might also entail technical assistance from the central hub to the member states that need it to improve their national frameworks.

national⁶⁶. Subsequently, a comprehensive two-tier architecture was established with the creation of the three ESAs, encompassing prudential, conduct-of-business and AML supervision of financial firms. In 2011, ESMA was assigned direct supervisory authority over credit rating agencies (CRAs), and, in 2013, over trade repositories (TRs), thus establishing a unitary supervisory system for these two market segments. The SSM is an almost pure unitary system⁶⁷. In a different area, competition policy enforcement in the European Union is also a unitary architecture centred on the European Commission's Directorate-General for Competition⁶⁸.

Given the experience of the SSM, and taking into account the differences between prudential and AML supervision, a well-designed unitary architecture for AML supervision would be a practical proposition, as would a reinforced two-tier model as proposed in mid-September 2018 by the European Commission (section 3). To be sure, current AML legislation in the European Union is less of a single rulebook than many other areas of financial legislation, including the capital requirements that the SSM enforces. But a situation in which a European-level authority would be in charge of enforcing poorly harmonised national law is not unprecedented, and, while clearly sub-optimal, can be made to work. One example is the ECB's fit-and-proper vetting of senior executives of the euro area's SI banks (see section 3). The experience of the SSM, and in particular of its work on so-called Options and National Discretions since 2015, suggests that the establishment of a unitary European supervisory mandate can be a catalyst for the development of policy expertise towards further regulatory harmonisation. There is in principle no legal obstacle to the imposition of fines or other restrictions on individual firms by a European agency, as illustrated by the existing practice of the SSM (for banks) and of ESMA (for CRAs and TRs)⁶⁹. In sum, the establishment of a unitary architecture need not await the creation of a single rulebook for AML supervision and can be expected to vastly accelerate its emergence⁷⁰.

A unitary architecture would entail a significantly simpler system, essentially resolving all issues of information sharing between AML supervisors and of allocation of tasks between home and host authorities within its geographical scope. The reduced risk of confusion of responsibilities would be positive for the overall legitimacy and accountability of the supervisory system, and for its effectiveness. The reduced administrative friction between different supervisory authorities would reduce both overall operating costs and the risk of errors and omissions; the efficiency of the system would be further enhanced by economies of scale, eg in terms of specialist expertise and skills. If implemented with a proper articulation of operational tasks between the national and European levels, as is broadly the case with JSTs in the SSM (see section 3), a unitary system would not entail a loss of local knowledge or of the ability to communicate properly with supervised entities, national law enforcement agencies or national FIUs. As Ms Nouy has repeatedly argued in describing the SSM's supervision of euro-area SIs, such arrangements provide *"the best of both worlds: the experience of national supervisors, while also keeping some distance from individual banks"* and the related risks of

66 The three sector-specific bodies that prefigured the ESAs in the 2000s, known as the Lamfalussy Level-3 Committees, were not authoritative enough to be viewed as 'supervisors of supervisors'.

67 The European Commission's initial draft of the SSM Regulation in September 2012 envisaged a pure unitary system for the prudential supervision of all banks in the euro area. In the legislative discussion that followed, Germany successfully insisted on keeping the day-to-day supervision of LSIs at the national level (see section 3), but the ECB, not NCAs, is the ultimate decision-maker for bank licensing and the other common procedures, implying that it is much more than a mere 'supervisor of supervisors'.

68 The competition directorate-general, in turn, has delegated back to national competition authorities the handling of cases that lack a European dimension.

69 The ability of EU agencies such as the ESAs to make decisions that are binding on individual firms has been established by the jurisprudence of the Court of Justice of the European Union, including the *Meroni* judgment of 13 June 1958 (case 9-56) and the *short-selling* judgment of 22 January 2014 (case C-270/12).

70 There is no compelling case for introducing in AML supervision a divide similar to that in the SSM between SIs and LSIs. This is because the most significant and complex AML breaches often occur in comparatively small firms. Therefore, the EU principle of proportionality does not apply to AML supervision the same way as it does to prudential supervision.

‘On balance, a unitary architecture for AML supervision in the EU is feasible, simpler, likely more effective, compliant with the subsidiarity principle, and generally preferable.’

political interference⁷¹. Once in place, a unitary architecture also reduces the scope for political conflict between European and national authorities in the event of diverging views, which is embedded in any two-tier system.

On the basis of the SSM experience since 2014, the supervisory effectiveness of the European agency under a unitary architecture should be significantly greater than that of the weaker member states’ AML supervisors, and not necessarily less than the best current national practice. Conversely, in a two-tier system, even with forceful capacity at the hub, weak links will inevitably remain. As such, even to the extent that an effective two-tier system may be able to spot malpractice, a unitary system is bound to do so at an earlier stage and to be more proactive in taking appropriate action. For similar reasons, a unitary system would be more resilient than a two-tier system against the possibility of erosion of the rule of law in a given member state, even though it would cover only AML supervision and not the FIU and law-enforcement pillars of the AML framework.

A unitary system would also greatly enhance and facilitate the European AML supervisor’s cooperation and information-sharing with its counterparts in other jurisdictions, not least the United States. While this would not deprive the US government of its ability to act unilaterally, eg by wielding its authority under Section 311 of the PATRIOT Act (see section 4), it would likely help ensure that the use of such instruments would remain selective, as it appears to have been so far. At the global level, a unitary European architecture would reduce the complexity of FATF processes, as fewer European participants would need to be directly involved.

Conversely, the main advantage of a two-tier architecture is the more incremental nature of the change compared to the status quo. But for it to be effective, the central agency will need to have strong powers in terms of access to information and enforcement capabilities, which ultimately raise similar political challenges as those inherent in a unitary system⁷². On balance, a unitary architecture for AML supervision in the European Union is feasible, simpler than a two-tier system, likely to be significantly more effective, compliant with the principle of subsidiarity and generally preferable.

There are parallels between the AML vicious circle and the bank-sovereign vicious circle that ultimately led to the establishment of Europe’s banking union. In both cases, the coexistence of the single market and euro-area frameworks with national banking supervision (respectively prudential and AML) led to perverse incentives for national authorities and ultimately to pervasive supervisory and crisis-management failures (Véron, 2013). In both cases, an attempt was made to address the problem with a two-tier architecture: the EBA was created in 2011 in the midst of Europe’s decade-long banking system crisis, which was ultimately resolved thanks to the creation of the SSM. Unlike the earlier institutional mismatch in the prudential space, Europe’s AML problem should be comprehensively tackled before it grows to a critical systemic dimension.

Which agency at the hub?

If a decision to move towards a unitary architecture is taken, then one or several European agency/ies needs to be empowered to that effect. The European AML supervisor(s) may be an existing agency, or a new one, or different agencies for different categories of obliged entities. There are at least seven different options:

- The ECB as single AML supervisor of euro-area banks, in addition to its existing role as prudential supervisor (Option 1);
- Each ESA for its respective area: EBA for banks, EIOPA for insurers and ESMA for other financial firms (Option 2);

71 As paraphrased, for example, in the Council of the EU’s partial summary record of the meeting of the ECON Committee of the European Parliament held in Brussels on 3-4 November 2014, available at <http://data.consilium.europa.eu/doc/document/ST-15376-2014-INIT/en/pdf>.

72 The European Commission’s proposal of 12 September 2018 stopped well short of that objective.

- EBA for all financial firms or even all obliged entities (Option 3)⁷³;
- ESMA for all financial firms or even all obliged entities (Option 4);
- A joint venture of the three ESAs, building on the existing AMLC (Option 5);
- A dedicated new agency, which may be referred to as the European AML Authority or EAMLA (Option 6)⁷⁴;
- A dedicated new agency with authority over only a subset of member states, established through a process of enhanced cooperation (Option 7).

The following analysis is intended as a preliminary exploration of the main advantages and shortcomings of these options, pending a more comprehensive assessment. Option 7 is only a fall-back option in case all others would lead to political deadlock. This is unlikely to be the case, however, since Options 2-6 can all be implemented through EU single market legislation (on the basis of Article 114 TFEU), which only requires approval by a qualified majority of EU member states⁷⁵.

Option 1 has immediate appeal given the generally solid performance of the ECB as a banking supervisor, and it has been mentioned in public by a senior German official⁷⁶. But it also has several drawbacks. Like Option 7, it does not cover the entire single market, leaving space for a continued AML vicious circle affecting countries outside the banking union area. This is a concern in any case, and particularly if, as appears possible at the time of writing, the UK remains in the European single market for an undetermined period of time following its planned exit from the European Union in late March 2019⁷⁷.

Moreover, Option 1 would presumably be based on Article 127(6) TFEU, like the SSM, raising challenges of both procedure (unanimity) and legal robustness⁷⁸. Article 127(6) also specifically refers to “*credit institutions and other financial institutions with the exception of insurance undertakings*”, so the sectoral scope beyond banks would be correspondingly limited. Furthermore, adding the AML task to the ECB’s already heavy burden of responsibilities might create too much centralisation of authority in a single institution, given the comparatively fragile framework for general-purpose executive authority and democratic scrutiny at the European level⁷⁹.

Options 2, 3, 4 and 5 all build on the existing structures of the three ESAs. Option 2 is the most straightforward but has the drawback of entrenching fragmentation of AML supervision along sectoral lines, which the US experience suggests is suboptimal (section 4). The drawbacks of such sectoral fragmentation can be expected to be increasingly significant in the future, as the emergence of new financial technologies might blur the boundaries between

73 This option is hinted at as a long-term outcome by the European Commission Communication of 12 September 2018 (COM(2018) 645). However, the European Commission’s legislative proposal of the same day stops short of Option 3, since it entails a two-tier and not a unitary architecture for AML supervision.

74 A variant of Option 6, which we do not here further explore, might be the creation of a dedicated new European Commission directorate-general, modelled on the existing framework for competition policy under the competition directorate-general, which would take over the AML supervisory mandate directly. This would not be functionally very different from a new EU agency, but it would entail a different framework for governance, accountability and funding.

75 In the EU context, ‘qualified majority’ refers to a specific supermajority of member states defined in the EU treaties. Under the currently applicable Lisbon Treaty, it implies approval by at least 55 percent of member states (16 out of 28) representing at least 65 percent of the EU population.

76 See Alexander Weber, ‘Money-Laundering Scandals Prompt EU Rethink on Policing Banks’, *Bloomberg*, 2 October 2018, which quotes State Secretary Jörg Kukies from Germany’s Federal Finance Ministry.

77 If the UK leaves the single market it will be treated as a third country for AML purposes, as is currently the case with Switzerland.

78 It is not clear that the reference in Article 127(6) TFEU to “*specific tasks [...] concerning policies relating to [...] prudential supervision*” can be understood as including AML supervision in addition to the prudential supervisory tasks already conferred on the ECB by the SSM Regulation. It is also not clear that the ECB could be granted an AML supervisory mandate under another treaty article, eg Article 114 TFEU.

79 Similar considerations led in 2012-13 to the decision to build the SRM entirely outside of the ECB, a decision that the ECB supported.

‘The creation of a new European AML Authority emerges as the best response to the challenges of AML in the EU!’

subsectors of finance and correspondingly open new avenues for regulatory arbitrage.

Option 3 might be justified by the fact that publicly identified AML failures have been particularly prominent in the European banking sector, and that the EBA has been so far the most active of the three ESAs in the AML field⁸⁰. But the EBA does not otherwise have experience with, or a mandate for, direct supervision, and it is unlikely to gain such authority in the future. Moreover, the members of the EBA’s Board of Supervisors are designated by national prudential supervisory authorities, not all of which have AML duties, creating a potential governance misalignment. Having the EBA supervise firms other than banks may create further awkward mismatches.

By contrast, ESMA (Option 4) has existing direct supervisory experience and is likely to gain more in the future (eg over central counterparties). It also has more experience with cross-sectoral oversight⁸¹. Option 5 has the advantage of being cross-sectoral but may suffer from too much complexity and a deficit of accountability in the corresponding governance arrangements.

The obvious drawback of Option 6 is that the creation of a new agency would add to the complexity of the EU financial regulatory landscape in general. But it would provide a straightforward and cross-sectoral solution to the specific challenge of AML supervision. It would also benefit from the possibility of learning from the early experience of the three ESAs and of other European bodies, including the SSM and the Single Resolution Board (the Brussels-based hub of the SRM). The EAMLA could thus be provided with an optimised governance and funding framework from the outset. This model would have further potential advantages from the standpoint of the ‘twin-peaks’ vision, as it would be separated from the prudential concerns of the ESAs and the SSM. A separate agency might also be preferable in terms of ring-fencing sensitive information about potentially criminal activity.

An initial blueprint for EAMLA

From the options analysed, the creation of a new European AML Authority (Option 6) emerges as the best response to the current challenges of AML in the European Union. Its establishment would inevitably take some time, but the decision to set it up need not be postponed. EU leaders’ current heightened awareness of AML challenges justifies an overhaul of the EU’s AML supervisory architecture without delay. While enacting new legislation within the current European Parliament term might not appear realistic, leaders could take a decision in principle in the immediate near term, with a mandate for the next European Commission to propose legislation accordingly.

If so, one could realistically envisage an effective transfer of supervisory authority to EAMLA starting around late 2022, allowing for one year’s legislative debate and two years for institutional build-up and recruitment, which is significantly more than was the case for the ESAs or the SSM. The transfer could itself be gradual to allow for lessons from early experience, eg starting with banks in 2022 and subsequently adding other categories of obliged entities. Before 2022, the existing two-tier architecture would remain in place, possibly with the limited enhancement proposed by the European Commission on 12 September 2018.

The governance of EAMLA should take into account the experience of the ESAs, including ongoing debates on the ESAs Review, and of the Single Resolution Board. It should rely on a compact collective decision-making board of fewer than ten members, including the agency’s chair⁸². All members of that board should be individually vetted by the European Parliament,

80 The EBA’s existing capacity and experience should not be exaggerated however, since the August 2018 discussion paper (see footnote 43) states that its entire staff for AML tasks is fewer than two full-time equivalents.

81 Furthermore, there is a scenario in which ESMA could acquire some supervisory responsibilities in the future over banks and insurers, if the EU adopts a ‘twin-peaks’ vision for the long-term evolution of its general financial supervisory architecture, ie a separation of prudential oversight from conduct-of-business supervision (Schoemaker and Véron, 2017).

82 A larger body could be set up with every member state represented, but only for consultative purposes in the process of drafting new rules, not for individual supervisory decisions.

thus creating legitimacy and accountability. The agency's funding should be through a levy directly collected from supervised entities, similar to the funding of the SSM.

The steady-state size of EAMLA staff depends on how much of its supervisory work would be delegated to other bodies – other EU agencies such as the SSM (for banks), or national AML supervisors, or both. EAMLA would need staff for policy work and rule drafting, similarly to the ESAs⁸³. For supervisory work, EAMLA could rely on hybrid teams of its own staff and those of other supervisors for both regular and targeted examinations. In the banking sector, delegation to prudential supervisors would create significantly less friction than is the case in the United States, because the institutional framework is significantly more integrated with an all-encompassing role for the SSM (in the banking union area) and no reliance on private-sector self-regulatory organisations (unlike FINRA and the NFA in the US). Even so, the staff needs of an effective EAMLA could easily reach several hundred, especially if (as might be desirable) it is granted AML supervisory authority over all categories of obliged entities including non-financial entities.

Other matters

Getting the supervisory architecture right is the current central challenge of AML policy in the European Union, but it is not the only challenge. The content of applicable AML legislation might also be ripe for improvement. But the fact that AMLD5 was very recently enacted and is not yet transposed, let alone enforced, suggests a more delayed timetable for the corresponding policy discussions. Given that experience, it makes sense to create a European AML supervisor ahead of any attempt at, for example, an AML Regulation (AMLR) that would move EU law in that area closer to the vision of a single rulebook⁸⁴. As we have noted, the experience of the SSM, which has played and continues to play a catalyst role for the gradual elimination of options and national discretions in the prudential rulebook for banks, argues in favour of such sequencing.

Similarly, supervisory integration should unlock improvements in two areas where the European Union has substantial scope for improvement, namely AML fines (in terms of both cross-border consistency and overall size) and the transparent publication of individual AML decisions (which is currently lacking in a number of member states; see section 3). The EU should aim to impose fines with a genuinely dissuasive impact and should expect detailed public announcements of all individual decisions containing the name of the subject entity, the nature of the alleged AML violations and the size of the penalty. Since some member states already impose large fines and/or publish their decisions with appropriate detail, it is presumed that no obstacle to this exists in EU law. Any lingering legal obstacles should be removed, as they are unlikely to be linked to fundamental principles.

Other AML-related issues deserve the attention of the EU and its institutions. One example is the longstanding matter of high-denomination euro notes, which provide a user-friendly way to move large amounts of cash and thus potentially to evade AML controls. In May 2016, the ECB announced it would no longer issue new €500 notes (even though the outstanding stock remains legal tender)⁸⁵, but it has not yet extended this action to the €200 let alone €100 notes. For comparison, the highest-denomination notes are of 100 units for the US dollar, 50 for the British pound and 100 for the Chinese renminbi⁸⁶.

83 Under the *Meroni* and *short-selling* jurisprudence (footnote 69), EAMLA is unlikely to be empowered as an autonomous rulemaker (beyond the issuance of non-binding opinions, guidelines and recommendations) but would draft binding technical standards for approval by the European Commission.

84 An AMLR may or may not be needed to achieve maximum harmonisation, which can also be pursued through directives. Correspondingly, it is possible that the optimal steady state includes a combination of regulation(s) and directive(s), as is currently the case for the EU bank capital requirements legislation. No in-depth investigation of the corresponding trade-offs has been done in the preparation of this paper.

85 ECB announcement available at <https://www.ecb.europa.eu/press/pr/date/2016/html/pr160504.en.html>.

86 See eg Sands (2016) for the case for eliminating high-denomination notes, and Hellwig (2017) for a sceptical perspective from Germany.

We leave open the question of whether the FIU pillar of Europe’s AML regime should also undergo supranational integration in the future. The creation of an EU-level FIU was recommended in a 2016 report (EU FIUs’ Platform, 2016); was considered but ultimately rejected in the European Parliament discussion of AMLD5 (Giegold, 2017); and more recently was recommended by Latvia’s Finance Minister, among others⁸⁷. Since the most notable recent AML cases in the European Union have tended to be concentrated in the banking sector and linked to failures of AML supervision, AML supervisory integration appears more urgent than a European FIU. Establishing an EU FIU also appears comparatively more challenging from both political and technical perspectives, given how the activities of FIUs are embedded in member states’ specific arrangements for criminal justice, law enforcement and intelligence gathering and analysis. If the creation of a European AML Authority is undertaken and succeeds, then the case for a European FIU might become more realistic than it is now.

The authors are grateful for their insight and feedback to Jesper Berg, Sarah Boiteux, Per Callesen, Martin Chorzempa, Maria Demertzis, Panicos Demetriades, Juan Luis Díez Gibson, Charlotte Dijkstra, Markus Forsman, Michael Gibson, Piers Haben, Michel Heijdra, Patrick Honohan, Jacob Funk Kirkegaard, Alexander Lehmann, Herwin Loman, Scott Marcus, Sylvain Maréchal, Kadri Martin, Tobias Mackie, Priscille Merle, G.J. Michiels van Kessenich, Maria Nieto, Francesco Papadia, Thierry Philippinat, Marcus Pleyer, Adam Posen, Sébastien Raspiller, Elina Ribakova, Pawel Samecki, Dirk Schoenmaker, Elleonora Soares, Edwin (Ted) Truman, Liviu Voinea, Boris Vujcic, Harald Waiglein, Steve Weisman, Thomas Wieser, Guntram Wolff, Pierre Wunsch, Stavros Zenios and others who have opted to remain anonymous.

References

- Bristow, Keith (2015) ‘Transnational organized crime as a national security threat’, speech at George Washington University, January, available at <http://www.nationalcrimeagency.gov.uk/publications/503-dg-washington-speech-jan-2015/file>
- Demertzis, Maria, Silvia Merler and Guntram B. Wolff (2017) ‘Capital Markets Union and the Fintech Opportunity’, *Policy Contribution 22/2017*, Bruegel, available at <http://bruegel.org/wp-content/uploads/2017/09/PC-22-2017.pdf>
- EBA (2018a) ‘Introductory statement by EBA Director Piers Haben at the public hearing: “Combat of Money Laundering in the EU Banking Sector” of the European Parliament’s Special Committee on Financial Crimes, Tax Evasion and Tax Avoidance (TAX3)’, European Banking Authority, 26 April, available at <https://www.eba.europa.eu/documents/10180/2199803/Introductory+statement+by+EBA+Director+Piers+Haben+TAX+3.pdf>
- EBA (2018b) ‘Recommendation to the Maltese Financial Intelligence Analysis Unit (FIAU) on action necessary to comply with the Anti-Money Laundering and Countering Terrorism Financing Directive’, European Banking Authority, 11 July, available at <https://www.eba.europa.eu/-/eba-issues-recommendation-to-the-maltese-financial-intelligence-analysis-unit-in-relation-to-its-supervision-of-pilatus-bank>
- ECB (2018a) *ECB Annual Report on Supervisory Activities 2017*, European Central Bank, available at <https://www.bankingsupervision.europa.eu/press/publications/annual-report/pdf/ssm.ar2017.en.pdf?63a120afab30be18171c083089709229>
- ⁸⁷ “Latvian Finance Minister Dana Reizniece-Ozola called for ‘the creation of a financial intelligence unit at the EU level as the scope of combating money laundering and terrorism financing goes far beyond the supervision of the financial sector.’” Quoted in Alexander Weber, ‘Money-Laundering Scandals Prompt EU Rethink on Policing Banks’, *Bloomberg*, 2 October 2018.

- ECB (2018b) 'List of supervised entities – Cut-off date for significance decisions: 1 July 2018', European Central Bank, August, available at https://www.bankingsupervision.europa.eu/ecb/pub/pdf/ssm_list_of_supervised_entities_201807.en.pdf
- EU FIUs' Platform (2016) *Mapping Exercise and Gap Analysis on FIU's Powers and Obstacles for Obtaining and Exchanging Information*, 15 December, available at <http://ec.europa.eu/transparency/regexpert/index.cfm?do=groupDetail.groupDetailDoc&id=33583&no=2>
- European Commission (2009) *Report of the High-Level Group on Financial Supervision in the EU Chaired by Jacques de Larosière*, Brussels, available at http://ec.europa.eu/economy_finance/publications/pages/publication14527_en.pdf
- European Commission (2017) 'Report 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, available at <https://publications.europa.eu/en/publication-detail/-/publication/ce3cb15d-5a5a-11e7-954d-01aa75ed71a1>
- European Commission (2018) 'Strengthening the Union framework for prudential and anti-money laundering supervision for financial institutions', COM(2018) 645, available at <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52018DC0645&from=EN>
- European Parliament (2018a) 'Public Hearing: Combat of Money Laundering in the EU Banking System', Committee on Financial Crimes, Tax Evasion and Tax Avoidance (TAX3), verbatim report, 28 April, available at http://www.europarl.europa.eu/cmsdata/150740/TAX3%2026%20April%202018_Verbatim%20report_EN.pdf
- European Parliament (2018b) 'Regular Public hearing with Danièle Nouy, Chair of the ECB Supervisory Board: ECON on 19 June 2018', European Parliament Economic Governance Support Unit, available at http://www.europarl.europa.eu/thinktank/en/document.html?reference=IPOL_BRI%282018%29614517
- Giegold, Sven (2017) 'Won and Lost: Details of the Compromise on the European Anti-Money Laundering Directive', blog post, 15 December, available at <https://sven-giegold.de/lost-and-won-details-of-the-compromise-on-the-european-anti-money-laundering-directive/>
- Greene, Carlton (2018) 'Testimony before the Subcommittee on Financial Institutions and Consumer Credit, United States House of Representatives', 27 April, available at <https://financialservices.house.gov/uploadedfiles/hhrg-115-ba15-wstate-cgreene-20180427.pdf>
- Hellwig, Martin (2017) 'Zur Diskussion um Bargeld und die Null-Zins-Politik der Zentralbank', Board of Academic Advisors of the Federal Ministry for Economic Affairs and Energy, February, available at http://docs.dpaq.de/12122-170209_gutachten-bargeld.pdf
- Kirschenbaum, Joshua (2018a) 'Estonian Regulators and European Central Bank Move Forcefully Against Russian Money Laundering', *GMF Alliance for Securing Democracy blog*, 30 March, available at <https://securingdemocracy.gmfus.org/estonian-regulators-and-european-central-bank-move-forcefully-against-russian-money-laundering/>
- Kirschenbaum, Joshua (2018b) 'Latvian Banking: Recent Reforms, Sustainable Solutions', *GMF Alliance for Securing Democracy Brief*, May, available at <https://securingdemocracy.gmfus.org/latvian-banking-recent-reforms-sustainable-solutions/>
- Kirschenbaum, Joshua (2018c) 'The Other "Cyprus Problem"', *GMF Alliance for Securing Democracy blog*, 5 July, available at <https://securingdemocracy.gmfus.org/the-other-cyprus-problem/>
- Kirschenbaum, Joshua (2018d) 'Russian Investments in the United States: Hardening the Target', *German Marshall Fund blog*, 22 August, available at <http://www.gmfus.org/blog/2018/08/22/russian-investments-united-states-hardening-target>
- Kirschenbaum, Joshua (2018e) 'Europe Needs Money Laundering Penalties That Hurt', *German Marshall Fund blog*, 12 September, available at <https://securingdemocracy.gmfus.org/europe-needs-money-laundering-penalties-that-hurt/>
- Global Center on Cooperative Security and Oxfam (2015) *Understanding Bank De-Risking and its Effects*

on *Financial Inclusion*, Research Report, November, available at https://www.oxfam.org/sites/www.oxfam.org/files/file_attachments/rr-bank-de-risking-181115-en_0.pdf

Sands, Peter (2016) 'Making it Harder for the Bad Guys: The Case for Eliminating High Denomination Notes', *M-RCBG Associate Working Paper 52*, Harvard Kennedy School Mossavar-Rahmani Center for Business and Government, available at <https://www.hks.harvard.edu/sites/default/files/centers/mrcbg/files/Eliminating%20BHDNfinalXYZ.pdf>

Schoenmaker, Dirk, and Nicolas Véron (2017) 'A 'Twin Peaks' Vision for Europe', in A. Godwin and A. Schmulow (eds) *The Cambridge Handbook of Twin Peaks Financial Regulation*, Cambridge University Press, forthcoming in 2018, available at SSRN: <https://ssrn.com/abstract=3067858>

Reuter, Peter, and Edwin M. Truman (2004) *Chasing Dirty Money: The Fight against Money Laundering*, Institute for International Economics, November

Shasky Calvery, Jennifer (2013) 'Testimony before the Committee on Homeland Security and Government Affairs, United States Senate', 18 November, available at <https://www.hsgac.senate.gov/imo/media/doc/Testimony-Calvery-2013-11-18.pdf>

Unger, Brigitte, and ECOLEF Team (2013) *Project 'ECOLEF': The Economic and Legal Effectiveness of Anti-Money Laundering and Combating Terrorist Financing Policy – Final Delivery to the EU*, Utrecht University, February, available at [http://www2.econ.uu.nl/users/unger/ecolef_files/Final%20ECOLEF%20report%20\(digital%20version\).pdf](http://www2.econ.uu.nl/users/unger/ecolef_files/Final%20ECOLEF%20report%20(digital%20version).pdf)

Véron, Nicolas (2013) 'Banking Nationalism and the European Crisis', speech to the EVCA Annual Symposium in Istanbul, June, available at <http://bruegel.org/2013/10/banking-nationalism-and-the-european-crisis/>

Zarate, Juan C. (2013) *Treasury's War: The Unleashing of a New Era of Financial Warfare*, Public Affairs Publishers, New York

Annex 1: Selected bank-related AML developments in the European Union

Austria (covered by the Single Supervisory Mechanism – SSM)

In 2018, Austria's Financial Market Authority (FMA) fined Raiffeisen Bank (SI) €2.7 million for AML violations, including beneficial ownership and customer due diligence failures⁸⁸. The FMA also fined Hypo Vorarlberg Bank (LSI) €414,000 for AML violations that year.

Cyprus (SSM)

In 2018, the Central Bank of Cyprus (CBC) fined Cyprus Development Bank (LSI) €715,000 for AML violations⁸⁹. Also in 2018, the CBC issued a circular previewing forthcoming regulations that will restrict the holding of accounts for shell companies⁹⁰. Similar fines were imposed in 2017 and 2016 against RCB Bank (SI) and Hellenic Bank (SI)⁹¹. In 2014-15, the CBC initiated resolution and liquidation proceedings for FBME Bank and revoked its branch license⁹².

88 Announcement available on the FMA's website at <https://www.fma.gv.at/en/announcement-sanction-imposed-against-raiffeisen-bank-international-ag-for-a-breach-of-due-diligence-requirements-for-the-prevention-of-money-laundering-and-terrorist-financing/>.

89 Announcement available on the CBC's website at <https://www.centralbank.cy/en/announcements/imposition-of-fine-on-cyprus-development-bank-ltd>.

90 Elias Hazou, 'Under the US cosh? The crackdown on money laundering', *Cyprus Mail*, 30 June 2018. See also Kirshenbaum (2018c).

91 Announcements available on the CBC's website at <https://www.centralbank.cy/en/announcements/imposition-of-fine-on-rcb-bank-ltd> and <https://www.centralbank.cy/en/announcements/15072016>.

92 FBME in Cyprus was a branch of FBME Bank Ltd, headquartered in Tanzania, but it conducted the bulk of the consolidated group's activity.

FBME had been the subject of a US Treasury Department action under Section 311 of the PATRIOT Act in 2014⁹³.

Czech Republic (non-SSM)

In 2016, the Czech National Bank revoked the license of ERB Bank, which it found lacked a functioning AML system⁹⁴.

Denmark (non-SSM)

In 2018, Danish prosecutors announced a new probe into Danske Bank after the bank's publication of an internal report that disclosed that over €200 billion in transactions flowed through its Estonian branch over a nine-year period, of which at least 40 percent was potentially suspicious. The Danish Financial Supervisory Authority (FSA) also announced a new investigation, and the bank's CEO resigned⁹⁵. In September 2018, at the European Commission's request, the European Banking Authority (EBA) started a breach-of-Union-law preliminary enquiry into AML supervision of Danske Bank in Denmark and Estonia⁹⁶. In 2017, Danish prosecutors had fined the bank DKK 12.5 million following the receipt of a 2015 referral from the FSA.

Estonia (SSM)

In 2018, prosecutors opened a criminal investigation into the Estonian branch (LSI) of Danske Bank⁹⁷. In September 2018, the EBA started a breach-of-Union-law enquiry into AML supervision of Danske Bank in Denmark and Estonia (see Denmark). Also in 2018, the Estonian FSA announced that the ECB had withdrawn the license of Versobank (LSI) at its request⁹⁸.

France (SSM)

In 2017 and 2018, the *Autorité de Contrôle Prudential et de Résolution* (ACPR) fined two entities of the Crédit Mutuel group (SI) a total of €2.5 million, a member bank of the Crédit Agricole group (SI) €2 million, Société Générale (SI) €5 million, and BNP Paribas (SI) €10 million for AML violations, including failures related to the filing of suspicious transaction reports and the detection of suspicious activity⁹⁹.

93 Announcements available respectively on FinCEN's website at <https://www.fincen.gov/news/news-releases/fincen-takes-action-protect-us-financial-system>, on the CBC's website at https://www.centralbank.cy/images/media/pdf/ENG_KDP_356.2014_FBME.pdf, and in the District Court judgment available at https://www.gzg.com.cy/media/filer_public/dd/36/dd3634f0-d6b0-4743-b35c-f33d61b6df0f/fbme_liquidation_application_judgment_10052017.pdf.

94 Announcement available on the Czech National Bank's website at https://www.cnb.cz/en/public/media_service/press_releases_cnb/2016/20161024_erb_bank_licence.html.

95 Danish FSA memorandum and internal report available on Danske Bank's website at <https://danskebank.com/-/media/danske-bank-com/pdf/investor-relations/fsa-statements/fsa-decision-re-danske-bank-3-may-2018--la=en.pdf> and <https://danskebank.com/-/media/danske-bank-com/file-cloud/2018/9/report-on-the-non-resident-portfolio-at-danske-banks-estonian-branch--la=en.pdf>. See also Teis Jensen, 'Under fire Danske bank faces fresh money laundering inquiry', Reuters, 20 September 2018; Stine Jacobsen and Jacob Gronholt-Perdersen, 'Denmark to investigate Danske Bank over money laundering allegations', Reuters, 6 August 2018; and Danske Bank's own announcement of the 2017 fine at <https://danskebank.com/news-and-insights/news-archive/company-announcements/2017/ca21122017>.

96 The European Commission's letter is available at <https://www.eba.europa.eu/documents/10180/2101654/Letter+from+Tiina+Astola+requesting+an+investigation+on+possible+BUL+under+Article+17+of+Regulation+%28EU%29%20No+10932010+-+21092018.pdf>.

97 Teis Jensen, 'Estonia to investigate Danske Bank over money laundering allegations', Reuters, 31 July 2018.

98 Announcement available on the Estonian FSA's website at <https://www.fi.ee/index.php?id=22632>; see also Kirshenbaum (2018a).

99 Announcements available on the ACPR's website respectively at https://acpr.banque-france.fr/sites/default/files/media/2018/04/19/180418_decision_cfcme.pdf, https://acpr.banque-france.fr/sites/default/files/media/2018/07/06/180705_decision_cfcme_publicee.pdf, <https://acpr.banque-france.fr/sites/default/files/media/2017/10/13/20170704-decision-sanction-crcam-av.pdf>, https://acpr.banque-france.fr/sites/default/files/546ta17_20170719_societe_generale-en.docx, and https://acpr.banque-france.fr/sites/default/files/20170630_bnp_paribas.pdf.

Germany (SSM)

Germany's Federal Financial Supervisory Authority (BaFin) does not publish individual sanction decisions. According to press reports, BaFin fined Deutsche Bank (SI) €40 million for AML violations in 2015¹⁰⁰.

Ireland (SSM)

In 2017, the Central Bank of Ireland fined Bank of Ireland (SI) €3.1 million for AML violations, including the failure to file suspicious transaction reports¹⁰¹.

Latvia (SSM)¹⁰²

In 2016, the Financial and Capital Markets Commission (FCMC) imposed an AML fine against ABLV (SI), and in 2018 ABLV was the subject of an action by the US Treasury Department under Section 311 of the PATRIOT Act (see section 4) and was subsequently liquidated¹⁰³. Subsequently, at the European Commission's request, the EBA started a breach-of-Union-law preliminary enquiry into AML supervision of ABLV¹⁰⁴. In 2017, the FCMC fined five banks – Baltikums Bank (LSI), Privatbank (LSI), Regional Investment Bank (LSI), Norvik Bank (LSI), and Rietumu Bank (LSI) – for AML violations including violations related to activity involving North Korea¹⁰⁵. On the recommendation of the FCMC, the ECB in 2016 withdrew the license of Trasta Komercbanka (LSI) on the grounds of capital adequacy problems and AML violations¹⁰⁶.

Luxembourg (SSM)

In 2017, the *Commission de Surveillance du Secteur Financier* fined DNB Luxembourg SA (LSI), Nordea Bank SA (LSI) and local operations of Crédit Agricole (SI) and Novo Banco (SI), for AML violations¹⁰⁷.

Malta (SSM)

In 2018, the Maltese FSA filed a referral to the ECB recommending the withdrawal of Pilatus Bank (LSI)'s license¹⁰⁸. The EBA conducted a preliminary enquiry into the Pilatus case under its breach-of-Union-law authority and found “*general and systematic shortcomings in the FIAU's application of AMLD3*” (EBA, 2018b).

Netherlands (SSM)

In 2018, the Netherlands Public Prosecution Service fined ING (SI) €775 million for money laundering violations that facilitated illicit activity including bribery in Uzbekistan. The Dutch National Bank said in a letter to the finance minister that other Dutch banks might also have

100 See Arno Schuetze and Jonathan Gould, 'Bafin fines Deutsche Bank for anti-money laundering flaws: source', *Reuters*, 24 June 2016.

101 Announcement available on the Central Bank of Ireland's website at <https://www.centralbank.ie/docs/default-source/news-and-media/legal-notices/settlement-agreements/public-statement-relating-to-settlement-agreement-between-central-bank-of-ireland-and-bank-of-ireland.pdf>.

102 A detailed analysis of recent AML-related developments in Latvia is provided in Kirschenbaum (2018b).

103 Announcement available on the FCMC's website at <http://www.ftk.lv/en/publications/press-releases/5769-fcmc-and-ablv>. FinCEN's statement on ABLV is available at <https://www.fincen.gov/news/news-releases/fincen-names-ablv-bank-latvia-institution-primary-money-laundering-concern-and>.

104 The European Commission's letter is available at <https://www.eba.europa.eu/documents/10180/2101654/Letter+from+Tiina+Astola+requesting+an+investigation+on+possible+BUL+under+Article+17+of+Regulation+%28EU%29%20No+10932010+-+01032018.pdf>.

105 Announcements available on FCMC's website at <http://www.ftk.lv/en/publications/press-releases/5769-fcmc-and-ablv> and <http://www.ftk.lv/en/media-room/press-releases/6429-fcmc-in-collaboration-with-u-s-law-enforcement-authorities-identifies-weaknesses-and-imposes-monetary-fines-on-three-banks.html>.

106 Announcement available on FCMC's website at <http://www.ftk.lv/en/publications/press-releases/5636-withdrawal-of-authorisation-of-jsc-trasta-komercbanka.html>.

107 See Martine Huberty, 'Panama Papers: Fines for 9 Financial Institutions', *Delano*, 21 December 2017.

108 Announcement available on the Maltese FSA's website at <https://www.mfsa.com.mt/pages/readfile.aspx?f=/files/Announcements/PressReleases/2018/MFSA%20PR%2030%20June%20Pilatus.pdf>.

inadequate AML controls¹⁰⁹. In 2017, the Fiscal Information and Investigation Service raided Amsterdam Trade Bank (LSI) as part of an investigation into the bank's failure to comply with suspicious activity reporting and customer due diligence obligations¹¹⁰.

Portugal (SSM)

In 2016, the EBA liaised with the Bank of Portugal regarding its implementation of the qualifying holdings approval process in two instances in which an Angolan politically exposed person purchased stakes in Banco BIC (LSI) and BPI (SI)¹¹¹.

Spain (SSM)

In 2017, prosecutors started an investigation into suspected money laundering through the Madrid branch of Industrial and Commercial Bank of China's Luxembourg subsidiary (LSI)¹¹². In 2016, the Supreme Court upheld a €1 million AML fine against Banco Santander (SI) imposed by Spain's Executive Service of the Commission for the Prevention of Money Laundering and Monetary Offences and approved by the Council of Ministers in 2015¹¹³.

Sweden (non-SSM)

In 2015, the Swedish FSA imposed AML fines against Nordea and Handelsbanken of SEK 50 million and SEK 35 million, respectively. Both banks were found to have committed violations related to non-resident customers, politically exposed persons, private banking and correspondent banking¹¹⁴.

United Kingdom (non-SSM)

In 2017, the UK Financial Conduct Authority fined Deutsche Bank (SI) £163 million for AML violations related to \$10 billion in securities 'mirror trades'¹¹⁵. In 2015, the FCA fined Barclays £72 million for inadequate AML controls related to a high-value transaction for politically exposed persons¹¹⁶. The head of the UK National Crime Agency declared that "*many hundreds of billions of pounds of criminal money is almost certainly laundered through UK banks and their subsidiaries each year*" (Bristow, 2015).

109 See Kirschenbaum (2018e) and Bart Meijer, 'Dutch banks too lax on money laundering: central bank', *Reuters*, 25 September 2018.

110 See Aleya Begum Lønsetteig, 'Amsterdam Trade Bank under new money laundering investigation', *Global Trade Review*, 20 December 2017.

111 See EBA letter to Ana Gomes MEP, 16 December 2016, available at <http://www.anagomes.eu/Public-Docs/261636e6-407c-4dda-b6be-4b4735a2b1e1.pdf>.

112 See Angus Berwick, David Lague and Jesús Aguado, 'Spain probes ICBC's European unit over money laundering', *Reuters*, 11 September 2017.

113 See Paul Day and Angus Berwick, 'Banco Santander fined 1 mln euros for failing to stop money laundering', *Reuters*, 28 November 2016; and Reyes Rincón, 'Multas de un millón de euros al Santander porque Banesto incumplió la ley contra el blanqueo', *El País*, 28 November 2016.

114 See Jonathan Boyd, 'Swedish regulator fines, Nordea, Handelsbanken for AML failures', *Investment Europe*, 19 May 2015, and FSA announcements at <https://www.fi.se/contentassets/b9fcac7ee33843b6b027b4832ed3848f/nordea-13-1784-eng2.pdf> and <https://www.fi.se/contentassets/cc3028bcd3ce45b7b789713b277448b7/handelsbanken-13-1783-eng.pdf>.

115 Announcement available on the Financial Conduct Authority's website at <https://www.fca.org.uk/news/press-releases/fca-fines-deutsche-bank-163-million-anti-money-laundering-controls-failure>. Given the absence of disclosure by BaFin, it is impossible to know if this case is related to the German case also referred to in Annex I.

116 Announcement available on the Financial Conduct Authority's website at <https://www.fca.org.uk/news/press-releases/fca-fines-barclays-%C2%A372-million-poor-handling-financial-crime-risks>.

Annex 2: AML supervisors for banks and Financial Intelligence Units in EU/EEA countries

Country	AML Supervisor for banks	FIU (acronym) (*)	FIU setup
Austria	Financial Market Authority (FMA)	Austrian FIU (A-FIU)	Division of the Federal police force (Bundeskriminalamt)
Belgium	Financial Services and Markets Authority (FSMA)	Belgian Financial Intelligence Processing Unit (CTIF-CFI)	Agency supervised by the Ministries of Justice and Finance
Bulgaria	Bulgarian National Bank (BNB)	Financial Intelligence Directorate, State Agency for National Security (FID-SANS)	Directorate within the national counterintelligence agency
Croatia	Croatian National Bank (HNB)	Anti-Money Laundering Office (AMLO)	Independent unit within the Ministry of Finance
Cyprus	Central Bank of Cyprus (CBC)	Unit for Combating Money Laundering (MOKAS)	Unit within the independent Law Office of the Republic
Czechia	Czech National Bank (CNB)	Financial Analytical Unit (FAU-CR)	Independent unit of the Ministry of Finance
Denmark	Finanstilsynet (Danish FSA)	Money Laundering Secretariat (FIU Denmark)	Unit of the Prosecution Service
Estonia	Finantsinspektion (Estonian FSA)	FIU Estonia (Money Laundering Information Bureau / MLIB)	Independent unit of the Police and Border Guard Board
Finland	Finanssivalvonta (Finnish FSA)	FIU (RAP)	Unit of the National Bureau of Investigation, part of the national police
France	Autorité de Contrôle Prudential et de Résolution (ACPR) under the Banque de France	Intelligence Processing and Action against Illicit Financial Networks Unit (TRACFIN)	Intelligence unit under the Ministry of Finance
Germany	Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin)	FIU Germany	Unit of the Customs Service, part of the Ministry of Finance
Greece	Bank of Greece	Hellenic FIU	Unit of the Hellenic Anti-Money Laundering Authority (HAMLA)
Hungary	Hungarian National Bank (MNB)	Hungarian FIU (HFIU)	Unit of the National Tax and Customs Administration
Iceland	Fjármálaeftirlitið (Icelandic FSA)	FIU Iceland (FIU-ICE)	Unit within the National Police
Ireland	Central Bank of Ireland (CBI)	Bureau of Fraud Investigation (MLIU)	Unit of the Garda National Economic Crime Bureau, part of the national police
Italy	Bank of Italy and Ministry of Finance	FIU of Italy (UIF)	Independent unit hosted by the Bank of Italy
Latvia	Financial and Capital Markets Commission (FCMC)	Office for Prevention of Laundering of Proceeds derived from Criminal Activity (Control Service) (KD)	Independent authority under the supervision of the Prosecutor's Office
Liechtenstein	Financial Market Authority (FMA)	FIU Liechtenstein (EFFI)	Independent administrative agency
Lithuania	Bank of Lithuania	Financial Crime Information Service (FCIS)	Service under the Ministry of the Interior
Luxembourg	Commission de Surveillance du Secteur Financier	FIU (CRF)	Unit of the Economic and Financial Prosecution Service under the Ministry of Justice

Malta	Financial Intelligence Analysis Unit (FIAU)	FIAU	Independent agency
Netherlands	Dutch National Bank (DNB)	FIU Netherlands (FIU-NL)	Independent agency
Norway	Finanstilsynet (Norwegian FSA)	FIU Norway (EFE)	Police specialist agency and prosecutor body
Poland	General Inspector of Financial Information (GIFI)	GIFI	Unit of the Ministry of Finance
Portugal	Bank of Portugal	FIU Portugal (UIF-Portugal)	Department within the Criminal Police
Romania	National Bank of Romania (BNR)	National Office for Prevention and Control of Money Laundering (ONPCSB)	Independent government agency
Slovakia	National Bank of Slovakia	FIU of the National Crime Agency (FSJ)	Unit of the Ministry of the Interior
Slovenia	Bank of Slovenia	Office for Money Laundering Prevention (OMLP)	Unit of the Ministry of Finance
Spain	Executive Service of the Commission for the Prevention of Money Laundering and Monetary Offences (SEPBLAC)	SEPBLAC	Unit of the Commission for the Prevention of Money Laundering and Monetary Offences (CPBCIM) under the Ministry of Economic Affairs
Sweden	Finansinspektionen (Swedish FSA)	FIU Sweden	Unit of the Swedish Police Authority
United Kingdom	Financial Conduct Authority (FCA)	UK FIU (NCA)	Unit of the National Crime Agency, a national law enforcement agency
Gibraltar	Financial Services Commission (FSC)	Gibraltar FIU (GCID-GFIU)	Unit of the Co-ordinating Centre for Criminal Intelligence and Drugs

Sources: websites of the Egmont Group, of the Anti-Money Laundering Forum (<https://www.anti-moneylaundering.org/>) and of selected national agencies, consulted 2 September 2018. Note: Gibraltar is included in the list above because of its inclusion in the Internal Market. FSA refers to Financial Supervisory Authorities in Nordic countries and Estonia. (*) as listed by the Egmont Group.