

Non paper on AMLA direct supervision

The European Commission has presented on July, 20th 2021, a legislative package aiming at strengthening the European framework for anti-money laundering and combatting the financing of terrorism (Hereafter “AML/CFT”). Among its proposals: the creation of a new AML/CFT European supervisor (hereafter “AMLA”) endowed with ambitious powers of direct supervision on some financial entities and of indirect supervision on the entire scope of obliged entities. This proposal has been tabled in response to the political expectations expressed by the Council and the European Parliament in 2019 and 2020.

Austria, Germany, Italy, Luxembourg, Netherlands and Spain (hereafter, the signatories) very much support this package and are of the view that the creation of the AMLA should aim at avoiding the reiteration of the past ML-TF incidents. They recall that those incidents have been triggered by all types of institutions, large and small, originating from a wide range of Member States and deriving from organisational, governance, exchange of information and cooperation failures. They also recall that the current reform should aim at creating an integrated European system of AML-CFT supervision. To that end, it should take example of the positive experiences and lessons learned from the SSM which should be adapted for AML-CFT purposes. **The signatories are thus of the view that the future scope of AMLA direct supervision will be absolutely key for the success of this reform. AMLA should supervise directly the riskiest financial entities and crypto-asset service providers (CASP), be they big or small, selected on the bases of objective risk criteria, while ensuring a comprehensive geographical coverage of the internal market.** To this end, AMLA’s selection process must be low in bureaucracy and thus fast, simple, fair and effective for AMLA itself, national supervisors as well as obliged entities.

The signatories make the following proposal:

Direct supervision should be exercised on the riskiest cross-border obliged entities among the EU credit institutions, financial institutions and CASPs. Given that the size of an entity is not proportionate to its risks, that risks are not exclusively carried by traditional credit institutions, and that the cross-border nature of an activity is not restrained to establishment, **the assessment process referred to in Article 12 of the AMLA regulation proposal should be amended to standardize the eligibility criteria, including those credit institutions, financial institutions and CASPs that operate in other Member States through free provision of services.** In this regard, it should be outlined that both, **establishment and free provision of services** raise coordination concerns between national supervisors, that activities under free provision of services can also carry important ML-TF risk and will keep developing in a context of growing use of digital technologies in the financial and crypto-asset sphere. In order not to overburden the AMLA in the course of the assessment process, it is proposed that credit institutions, financial institutions and CASP enter the assessment process where they operate **in at least 7 Member states** under either establishment or free provision of services. **At the same time**, it is essential to guarantee that – from the first step of the assessment process under Article 12 – the eligibility criteria **only consider actual cross-border activity.** AMLA should be entrusted with the task of setting out criteria to define when an obliged entity would be considered to actively provide services for the purpose of the risk assessment.

- 1. The assessment of obliged entities for the purposes of selection for direct supervision should be risk-based**, rely on a single methodology and sectoral benchmarks defined by the AMLA and shouldn’t differentiate credit from other financial institutions or CASPs. **The methodology to be defined should take into**

account the inherent risks related to customers, products, services, transactions, delivery channels and geographical areas of the assessed obliged entities. When developing the methodology AMLA should also consider incorporating the risk criteria listed in Annex I to III of the AMLR. In addition, **relying on an assessment of residual risks ensures focus on the riskiest obliged entities.** AMLA should establish benchmarks and a methodology to assess the residual risk, by taking into account the ML/TF risk management the obliged entity has put in place. **In order to ensure its homogeneity, the assessment procedure should be centralized by the AMLA.** It should result in a **single classification of the risk profile encompassing all domestic and cross-border activities of each assessed group or entity provided under establishment and free provision of services.**

2. **The AMLA should directly supervise the assessed cross-border groups or obliged entities** presenting the highest risk profile. The notion of group should also include EU undertakings with parent undertakings or head office entities that are not a credit or financial institution or that are based in a non EU Member State.
3. **The AMLA should directly supervise at least 1 obliged entity established in each Member State, identified on a risk based approach.** This approach should take into account that such direct supervision may also be established due to the obliged entity being part of a directly supervised group. In this context, the signatories are looking for more clarity, whether under the Commission's proposal joint supervisory teams will be deployed to all Member States where an obliged entity belonging to a directly supervised group is established. This comprehensive coverage of the internal market **does not aim at fairness but efficiency of the new EU system of supervision.** To successfully orientate national supervisors, the AMLA indeed needs for a concrete and comprehensive understanding of ML-TF risks throughout the EU. A concrete experience of supervision in each Member States appears also as a precondition for the AMLA to appropriately step in in the exceptional situations referred to in article 30 of the AMLA regulation and to undertake efficiently its task of indirect supervision. For the selected entities, this will besides ensure that direct supervision at EU level is part of a normal procedure and not a stigmatization. Eventually, this comprehensive presence built on the positive experiences of the SSM and appears necessary to give raise to an integrated EU AML/CFT system which could expand in future.
4. **To ensure continued high standards of supervision and with due consideration for the proportionality of the costs for obliged entities, the number of entities supervised by the AMLA should gradually increase in a manner proportionate to the resources and staff dedicated by the AMLA to direct supervisory activities.** This staged approach is explained below.

The redrafting proposal of articles 12 and 13 attached to this non-paper reflects the above principles.

As regards the assessment process under article 12:

- Paragraph 1: it is proposed to **merge the assessment of credit and other financial institutions** and/or groups as this distinction doesn't make sense in practice, given the overlaps in activities between these entities (for instance as credit institution and payment service provider or e-money institution). In order to ensure that the EU supervisory framework is future proof, it is proposed to **introduce CASPs** within the scope of the assessment process given their development potential. It is proposed

to put on an **equal footing free establishment and free provision of services** as modalities of cross-border activity. In order to **widen the scope of the assessment procedure beyond the largest credit institutions**, to also capture other obliged entities which can present risks for the internal market, **it is proposed to assess all credit institutions, other financial institutions, groups and CASPs which operate in at least 7 Member State under either an establishment or free provision of services or both**. It is also proposed to assign to the AMLA the task of setting out RTS defining criteria when an obliged entity would be considered to actively provide services for the purpose of the risk assessment.

- Paragraph 2: where in a Member state, no established entity qualifies as an assessed entity under the first paragraph, **the assessment procedure should cover the entire financial sector in order to enable, as of 2029**, that the AMLA directly supervises at least one entity established in this Member State. **The methodology to be implemented to that end would be the one developed by the AMLA**.
- Paragraph 4: it is proposed to **refine limb (c) on investment funds** to focus on managers and management companies and not on funds themselves. Investment funds are indeed just financial products and do not have legal personality. They rely on management companies or managers for the performance of their AML-CFT obligations. It is proposed to introduce **CASPs** in the list of the benchmarks to be developed by the AMLA.
- Paragraph 5: it is proposed to take into account **residual ML/TF risk**, by also considering the risk management obliged entities have put in place, while recognizing that a methodology for objective assessment has to be further defined. In case AMLA should be unable to assess the residual risk during the first selection process, it shall have the option to rely on inherent risk for assessing obliged entities' risk profiles and postpone the assessment of residual risk until the second selection process.
- Paragraph 6: it is proposed to change the methodology for classifying/scoring the risk profile of the assessed obliged entities in order to ensure that activities provided under free provision of services will be adequately taken into account. **Instead of a scoring of the assessed entity in each Member State where it operates, it is proposed to have one consolidated rating encompassing all domestic and cross-border activities under both establishment and free provision of services at group or entity level**. This scoring would take into account the inherent and, if possible, residual risk criteria assessed based on the benchmarks developed by the AMLA and referred to in paragraph 5. To enable this consolidated rating, the AMLA methodology to be adopted as a regulatory technical standard should specify the respective tasks of home and host supervisors, where appropriate the role of supervisory colleges referred to in article 36 of the AMLD proposal, ponderation rules between the different types of activities and cross-border modalities of the assessed group or entities... Homogeneity of the assessment and classification procedure will be key to ensure a level playing field and convergence of supervisory practices. As a result, **the AMLA should centralize those exercises** based on the data and information provided by national supervisors. **This active involvement of the AMLA should be legally reflected in a way that ensures compatibility with the Meroni-doctrine**. To that end, **the signatories call on the Presidency to submit this subject to the Council's legal services**.

As regards the selection process under article 13:

- Paragraph 1: it is proposed to **change the methodology of the selection process**. Relying on the risk profile of the assessed entities in a definite number of Member States doesn't enable to take into account the ML-TF risks carried by activities provided under free provision of services given the challenges host supervisors may face in this regard. **As the risk profile would be assessed at group or entity level for all the domestic and cross border activities pursuant to article 12 (6), the signatories propose that the obliged entities that are deemed highly risky qualify for direct supervision.**

Paragraph 2: **it is proposed to create an integrated system of AML-CFT supervision covering the entire financial market.** To that end, where in a Member state no established entity qualifies as a selected entity under paragraph 1, the AMLA should carry out direct supervision on the entity with the highest risk profile established in this Member state.

- Paragraph 4: it is proposed to adopt a **staged approach** on direct supervision. Where too many risky entities would be selected on the single base of the methodology referred to in article 12 (6), the AMLA would then focus, among those riskiest financial institutions, on the 40 entities with the highest **total asset value**. This combination of a risk criteria and of the total asset value, which is most of the time correlated to a degree cross-border activity, will help **focusing on the risky entities whose failure could trigger important systemic threats for the Member State and the internal market while taking into account the available resources of the AMLA**. As of the third year of direct supervision (second assessment round), **the AMLA should expand its scope of direct supervision to ensure that at least one obliged entity established in each Member states falls under its remit**. The same reasoning as above would apply as regards the selection of the entities to be supervised in the Member states where no obliged entity is selected pursuant to paragraph 1. In case the risk profile alone wouldn't enable the identification of only one entity, then the AMLA should directly supervise the riskiest obliged entity with the highest total asset value. **As of the sixth year of direct supervision, the AMLA should be able to extend by 10% every three year its scope of direct supervision for each assessment round, if its resources allow to.**