TAX3

Special Committee on Financial Crimes, Tax Evasion and Tax Avoidance

PUBLIC HEARING

COMBAT OF MONEY LAUNDERING IN THE EU BANKING SYSTEM

THURSDAY, 26 APRIL 2018

09.00 - 12.30

Room: József Antall (JAN) 4Q1

Brussels

CONTRIBUTIONS

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European Parliament
Brussels, 26.04.2018
***Pēters Putniņš, C*hairman,**
Financial and Capital Market Commission of the Republic of Latvia

Latvia: Vision on Future Developments

Domestic/Foreign Deposits as a Challenge

(Slide No 2) The total number of commercial banks in Latvia – 3 domestic customer and 12 named as foreign customer banks. The presence of considerable number of foreign customers (mainly from the eastern parts of Europe) has been always an extra challenge and risk factor for the banking sector supervision in Latvia already since the 1990s. Therefore the FCMC has requested the banks to maintain increased level requirements to ensure compliance with regulatory provisions (capital, liquidity ratio etc.). Now, the Latvian banks must undertake a thorough revision of further strategies and build other business models.
(Slide No 3)

Combating Money Laundering

The level of foreign deposits reached its peak in 2015 with 54.8 % of total deposits. Following the tightened global AML standards and Latvia's joining the OECD (in 2016) the supervisory approach has changed, namely, the new FCMC management (since February 2016) now is calling the banks for essential revision of their customer base and avoidance of the money of questionable origin. Currently, as a result of mentioned efforts, there is a decrease in foreign deposits of 31%. This is the lowest level of foreign deposits in 20 years, and this decline will continue because of the required self-cleaning work to relieve the Latvian banks and the state of reputational risk burden.
(Slide No 4)
Moreover, today the global geopolitical situation has changed. It is apparent that the confrontation of ideas and values becomes severer between the West, involving also Latvia and other Baltic States, and a different view of the world coming from the East, the key source of risky financial resources in Latvia. The Government's position is to maintain 5% of foreign money in the total deposit volume of the banking sector, at the same demonstrating its ability to control the deposits. To specify the 5% threshold, – it could be also 9% in any of banks, while in other bank 1.2%, but the average ratio should not exceed 5%.
(Slide No 5)

Sanctions and Corrective Measures *(ABLV Bank)*

The bank's risk appetite must align with its internal control system ability to manage risks in accordance with the AML regulatory provisions. If there are radical changes in the national

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regulations, then – of course – the regulator ensures their implementation and the banks proactively react by changing their approach to the servicing of risky customers. The Association of Latvian Commercial Banks (ALCB) strongly supports this approach.

It should be noted that supervision over ABLV has been very tight on part of FCMC in particular over the last years; therefore we are not caught unawares. One cannot deny that Latvia is still facing the AML-related problems. However, significant remedial work has been done in the Bank by the FCMC over last two years. The fines, largest ones than ever in Latvia, have been imposed on ABLV Bank for respective breaches. Investments that we have required for improvements of the Bank's internal control systems amount to almost 20 million euro. And the first agreement with the Bank about addressing the deficiencies has been completed. There has been no such precedent for cooperation previously. Today's developments to a great extent have been affected by the past events, having a great impact on the Bank's fate at present. These are the aftermaths of historical legacy.

(Slide No 6)

Enforcement Actions

We all have a common interest in the sustainable long-term development of the financial sector without any additional threats, and this requires reducing the AML/TF risk exposure to our country. The first steps towards setting-up new arrangements in the banking sector appear promising. The high stability ratios set on the foreign banks by the FCMC have proven, and now there is a firm basis for fulfilment obligations to the customers and at the same for changing the business models.

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FINANŠU UN KAPITĀLA TIRGUS KOMISIJA

LATVIAN FINANCIAL SECTOR: MANAGING THE CHANGE

***Pēters Putniņš*, Chairman**
Financial and Capital Market Commission
Republic of Latvia
Brussels, 26.04.2018

BANKING SECTOR IN LATVIA 2018

Standard liquidity requirement 30%

FCMC sets enhanced regulatory requirements for foreign deposits:

20-40% - liquidity requirement 40%

40-70% - liquidity requirement 50%

70% and more - 60%

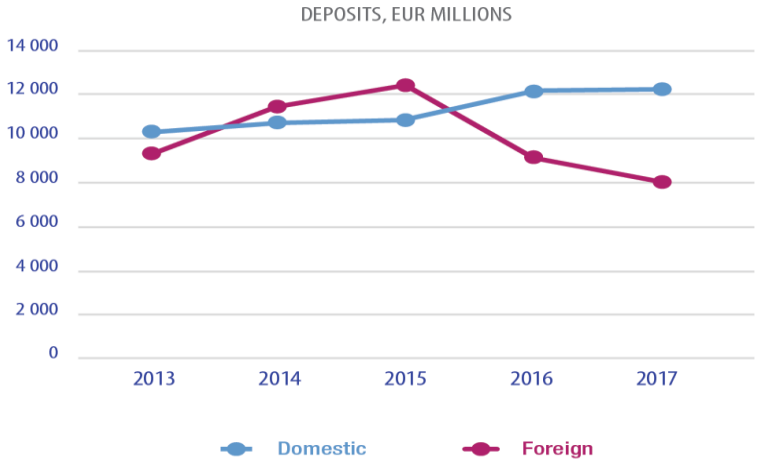
CHALLENGE TO SUPERVISION: significant presence of foreign customers since 1990s

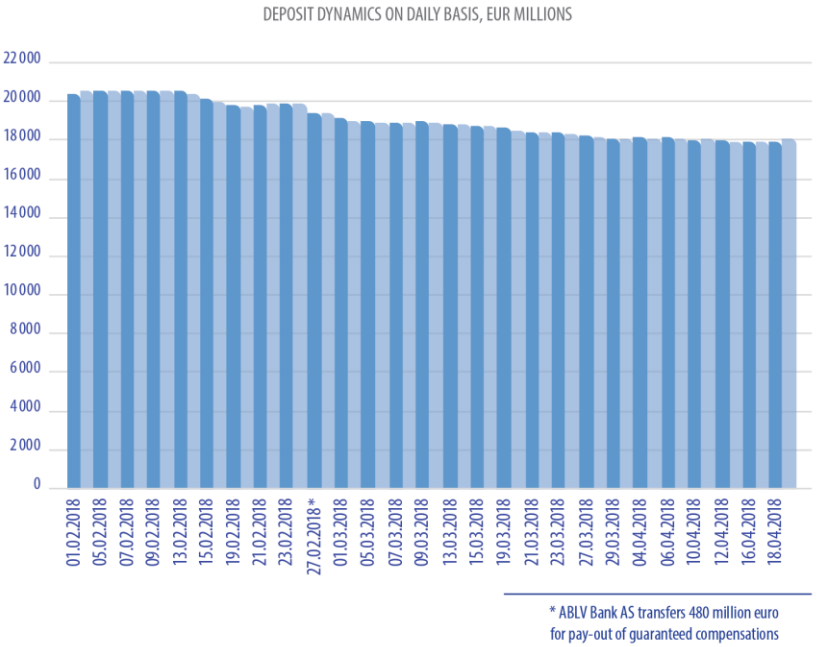
55%

March 2015

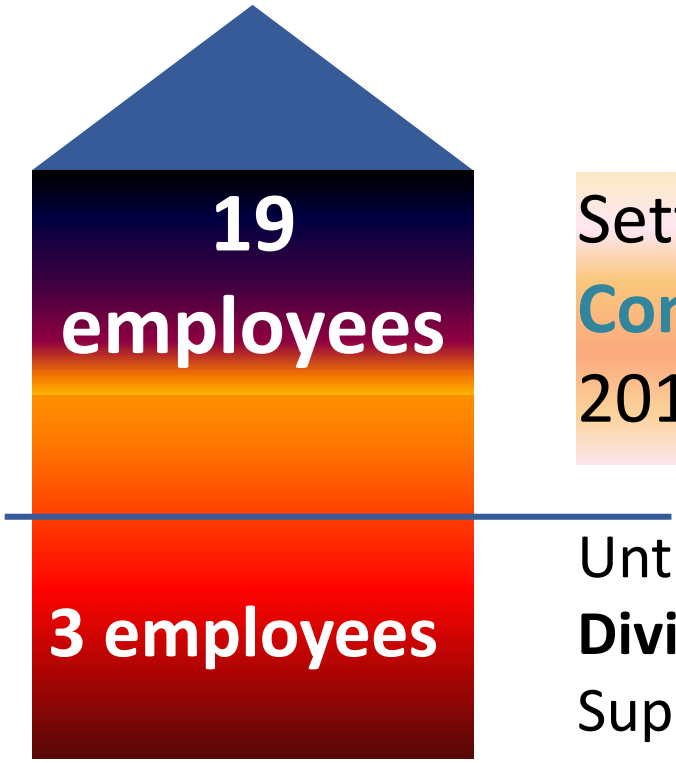
31%

Today





2016: CHANGE IN SUPERVISION APPROACH – Enhanced AML Controls



Setting up of **Compliance Control Department** – April 2016

Until 2016 – **Financial Integrity Division** as structural unit of FCMC Supervision Department

FCMC sanctions/corrective measures applied to banks 2014 - 2017

2014
Joining the euro area /sanctions publications started

Total: 70 000 euro fine on 1 bank;
2 warnings to banks.

2015
Before accession to the OECD

Total: 2.4 million euro fines on 4 banks;
Fines on 4 bank's board members ~ 145 000 euro;
2 warnings to 1 bank.

2016
Latvia's accession to the OECD 01.07.

ABLV Bank

+6 million euro investment in improvement of control systems *(ABLV Bank)*

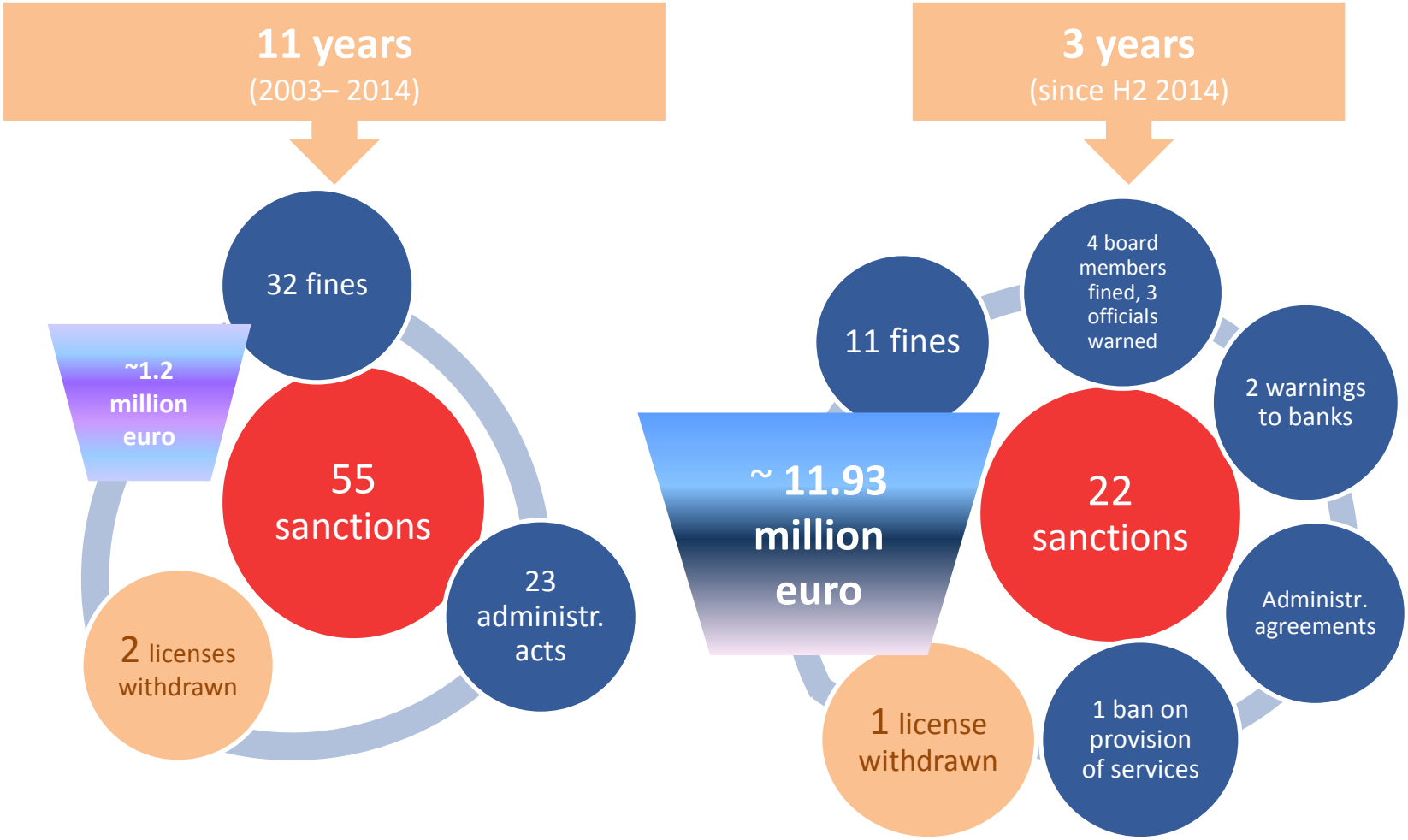
Total : 5.96 million euro fines on 4 banks;
1 bank: restrictions and withdrawal of authorization;
1 bank: ban on provision of services in Latvia.

2017

+12.5 million euro should be invested in improvment of control system until 2020 *(ABLV Bank)*

Total: 3.5 million euro fines on 5 banks (including in cooperation with FIB for circumventing sanctions on North Korea);
Public warnings issued to 3 bank officials

FCMC sanctions applied in AML/TF field since 2003



SESSION of Q&A

***Pēters Putniņš*, Chairman**
Financial and Capital Market Commission

Nora Dambure, Director
Supervision Department, Member of Board

Gvido Romeiko, Director
Legal and Licensing Department, Member of Board

DEPARTMENT OF THE TREASURY

Financial Crimes Enforcement Network

31 CFR Part 1010

RIN 1506–AB39

Proposal of Special Measure Against ABLV Bank, AS as a Financial Institution of Primary Money Laundering Concern

AGENCY: Financial Crimes Enforcement Network (FinCEN), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: FinCEN is issuing a notice of proposed rulemaking (NPRM), pursuant to Section 311 of the USA PATRIOT Act, to prohibit the opening or maintaining of a correspondent account in the United States for, or on behalf of, ABLV Bank, AS.

DATES: Written comments on the notice of proposed rulemaking must be submitted on or before April 17, 2018.

ADDRESSES: You may submit comments, identified by RIN–1506–AB39, by any of the following methods:

- *Federal E-rulemaking Portal:http://www.regulations.gov*. Follow the instructions for submitting comments. Include Docket Number FinCEN–2017–0013 and RIN–1506–AB39 in the submission.
- *Mail:* The Financial Crimes Enforcement Network, P.O. Box 39, Vienna, VA 22183. Include RIN–1506–AB39 in the body of the text. Any comments submitted by mail must be postmarked by the due date for comments indicated above. Please submit comments by one method only.
- Comments submitted in responseto this NPRM will become a matter of public record. Therefore, you should submit only information that you wish to make publicly available.
- *Inspection of comments:* FinCEN uses the electronic, internet-accessible dockets at *Regulations.gov* as its complete docket; all hard copies of materials that should be in the docket, including public comments, are electronically scanned and placed there. **Federal Register** notices published by FinCEN are searchable by docket number, RIN, or document title, among other things, and the docket number, RIN, and title may be found at the beginning of such notices. In general, FinCEN will make all comments publicly available by posting them on *http://www.regulations.gov.*

FOR FURTHER INFORMATION CONTACT: The FinCEN Resource Center at (800)949–2732.

SUPPLEMENTARY INFORMATION:

I. Statutory Provisions

On October 26, 2001, the President signed into law the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001, Public Law 107–56 (the USA PATRIOT Act). Title III of the USA PATRIOT Act amends the anti-money laundering (AML) provisions of the Bank Secrecy Act (BSA), codified at 12 U.S.C. 1829b, 12 U.S.C. 1951–1959, and 31 U.S.C. 5311–5314, 5316–5332, to promote the prevention, detection, and prosecution of international money laundering and the financing of terrorism. Regulations implementing the BSA appear at 31 CFR Chapter X. The authority of the Secretary of the Treasury (the Secretary) to administer the BSA and its implementing regulations has been delegated to FinCEN.

Section 311 of the USA PATRIOT Act (Section 311), codified at 31 U.S.C. 5318A, grants FinCEN the authority, upon finding that reasonable grounds exist for concluding that a jurisdiction outside of the United States, one or more financial institutions operating outside of the United States, one or more classes of transactions within or involving a jurisdiction outside of the United States, or one or more types of accounts is of primary money laundering concern, to require domestic financial institutions and domestic financial agencies to take certain ''special measures.'' The five special measures enumerated in Section 311 are prophylactic safeguards that defend the U.S. financial system from money laundering and terrorist financing. FinCEN may impose one or more of these special measures in order to protect the U.S. financial system from these threats. Special measures one through four, codified at 31 U.S.C. 5318A(b)(1)–(b)(4), impose additional recordkeeping, information collection, and reporting requirements on covered U.S. financial institutions. The fifth special measure, codified at 31 U.S.C. 5318A(b)(5), allows FinCEN to prohibit,

or impose conditions on, the opening or maintaining in the United States of correspondent or payable-through accounts for, or on behalf of, a foreign banking institution, if such correspondent account or payable-through account involves the foreign financial institution found to be of primary money laundering concern.

Before making a finding that reasonable grounds exist for concluding that a foreign financial institution is of primary money laundering concern, the Secretary is required to consult with both the Secretary of State and the Attorney General.[1] The Secretary shall also consider such information as the Secretary determines to be relevant, including the following potentially relevant factors:

- The extent to which such a financial institution is used to facilitate or promote money laundering in or through the jurisdiction, including any money laundering activity by organized criminal groups, international terrorists, or entities involved in the proliferation of weapons of mass destruction (WMD) or missiles;
- The extent to which such a financial institution is used for legitimate business purposes in the jurisdiction; and
- The extent to which such action is sufficient to ensure that the purposes of Section 311 are fulfilled, and to guard against international money laundering and other financial crimes.[2]

Upon finding that a foreign financial institution is of primary money laundering concern, the Secretary may require covered financial institutions to take one or more special measures. In selecting which special measure(s) to take, the Secretary ''shall consult with the Chairman of the Board of Governors of the Federal Reserve System, any other appropriate Federal banking agency (as defined in Section 3 of the Federal Deposit Insurance Act), the Secretary of State, the Securities and Exchange Commission, the Commodity Futures Trading Commission, the National Credit Union Administration Board, and in the sole discretion of the Secretary, such other agencies and interested parties as the Secretary [of the Treasury] may find appropriate.'' [3] In imposing the fifth special measure, the Secretary must do so ''in consultation with the Secretary of State, the Attorney General, and the Chairman of the Board of Governors of the Federal Reserve System.'' [4]

In addition, in selecting which special measure(s) to take, the Secretary shall consider the following factors:

- Whether similar action has been or is being taken by other nations or multilateral groups;
- Whether the imposition of any particular special measure would create a significant competitive disadvantage, including any undue cost or burden associated with compliance, for financial institutions organized or licensed in the United States;
- The extent to which the action or the timing of the action would have a significant adverse systemic impact on the international payment, clearance, and settlement system, or on legitimate business activities involving the particular jurisdiction, institution, class of transactions, or type of account; and
- The effect of the action on United States national security and foreign policy.[5]

II. Summary of Notice of Proposed Rulemaking

This NPRM sets forth (i) FinCEN's finding that ABLV Bank, AS (ABLV), a commercial bank located in Riga, Latvia, is a foreign financial institution of primary money laundering concern pursuant to Section 311, and (ii) FinCEN's proposal of a prohibition under the fifth special measure on the opening or maintaining in the United States of a correspondent account for, or on behalf of, ABLV. As described more fully below,[6] FinCEN has reasonable grounds to believe that ABLV executives, shareholders, and employees have institutionalized money laundering as a pillar of the bank's business practices. As described in further detail below, ABLV management permits the bank and its employees to orchestrate and engage in money laundering schemes; solicits the high-risk shell company activity that enables the bank and its customers to launder funds; maintains inadequate controls over high-risk shell company accounts; and seeks to obstruct enforcement of Latvian anti-money laundering and combating the financing of terrorism (AML/CFT) rules in order to protect these business practices. In addition, illicit financial activity at the bank has included transactions for parties connected to U.S. and UN-designated entities, some of which are involved in North Korea's procurement or export of ballistic missiles.

III. Background on Latvia's Non-Resident Deposit Sector and ABLV Bank

1. Latvia's Non-Resident Deposit Banking Sector

Due to geography, linguistic profile, and a stable and developed banking system, Latvia serves as a financial bridge between the Commonwealth of Independent States (CIS),[7] European Union (EU) and U.S. financial systems. While it lacks a legal framework that formally separates domestic banking business and non-resident banking, most Latvian banks conduct the majority of their business in either domestic retail/commercial banking or non-resident banking services, not both. Non-resident banking in Latvia allows offshore companies, including shell companies, to hold accounts and transact through Latvian banks. CIS-based actors often transfer their capital via Latvia, frequently through complex and interconnected legal structures, to various banking locales in order to reduce scrutiny of transactions and lower the transactions' risk rating.

According to Latvia's Financial Capital and Market Commission (FCMC), the primary banking regulator, non-resident banking services contribute between 0.8 and 1.5 percent to Latvia's gross domestic product (GDP). Non-resident deposits (NRDs) in Latvia are equal to roughly $13 billion. Latvian NRD banking activity transiting the U.S. financial system is estimated in recent years to have reached billions of dollars annually.

The Latvian banking system's reliance on NRD funds for capital exposes it to increased illicit finance risk. A 2014 report by the European Commission's Directorate General for Economic and Financial Affairs (ECFIN) singled out Latvia's reliance on NRD banking as a risk to Latvia's private sector, for a variety of reasons, including the fact that ensuring compliance with anti-money laundering rules may be more challenging for non-resident banks as verifying clients' background and business activities could prove difficult. Criminal groups and corrupt officials may use elaborate offshore services to hide true beneficiaries or create fraudulent business transactions.

[1] 31 U.S.C. 5318A(c)(1).

[2] 31 U.S.C. 5318A(c)(2)(B).

[3] 31 U.S.C. 5318A(a)(4)(A).

[4] 31 U.S.C. 5318A(b)(5).

[5] 31 U.S.C. 5318A(a)(4)(B).

[6] FinCEN has relied on a variety of sources including nonpublic information in preparing this proposed rule. When a statement is sourced in publicly available information, FinCEN will post an exhibit containing the public source. These exhibits will be posted with this proposed rule at https://www.regulations.gov.

[7] The Commonwealth of Independent States (CIS) is a loose confederation of states making up most of the former Soviet Union. *See* http://www.cisstat.com/eng/cis.htm. For the purposes of this notice, the CIS region encompasses all members, associate members, and former members of the CIS.

In a positive development, since 2015, the FCMC has led significant efforts to reform Latvia's AML/CFT regulations and enforcement regime. However, as noted in the aforementioned 2014 ECFIN report, positive changes need to be consistently implemented jointly with the banks. The need to improve the institutional capacity remains a long-term challenge due to the complexities of investigating and prosecuting money laundering.

2. ABLV Bank

Established in 1993, ABLV Bank, AS (ABLV) is headquartered in Riga, Latvia. According to data provided by the Association of Latvian Commercial Banks, ABLV is the second largest bank in Latvia by assets, with the equivalent of roughly $4.6 billion as of March 31, 2017. ABLV is Latvia's largest NRD bank by assets. As further described below, the majority of ABLV's customers are high-risk shell companies registered outside of Latvia.

ABLV offers banking, investment, and advisory services. ABLV currently does not maintain correspondent accounts directly with U.S. banks, but instead accesses the U.S. financial system through nested U.S. dollar correspondent relationships with other foreign financial institutions. Those foreign financial institutions, in turn, hold direct U.S. correspondent accounts.

ABLV holds several subsidiary entities, including a subsidiary bank, ABLV Bank, Luxembourg, S.A., located in Luxembourg. The beneficial owners of ABLV are Ernests Bernis and Oleg Fils. Bernis holds 4.93 percent of shares in the bank directly, and 43.12 percent of shares indirectly via Cassandra Holding Company, SIA. Fils holds 43.13 percent of shares in ABLV indirectly through SIA ''OF Holding.'' Unspecified ''other shareholders'' own the remaining equity.

IV. Finding ABLV To Be a Foreign Financial Institution of Primary Money Laundering Concern

Based on information available to the agency, including both public and nonpublic reporting, and after performing the requisite interagency consultations and considering each of the factors discussed below, FinCEN finds that reasonable grounds exist for concluding that ABLV is a financial institution operating outside the United States of primary money laundering concern.

1. The Extent to Which ABLV Has Been Used To Facilitate or Promote Money Laundering, Including by Entities Involved in the Proliferation of Weapons of Mass Destruction or Missiles

According to information available to FinCEN, ABLV executives, shareholders, and employees have institutionalized money laundering as a pillar of the bank's business practices. ABLV management orchestrates, and permits the bank and its employees to engage in, money laundering schemes. Management solicits the high-risk shell company activity that enables the bank and its customers to launder funds, maintains inadequate controls over high-risk shell company accounts, and is complicit in the circumvention of AML/CFT controls at the bank. As a result, multiple actors have exploited the bank in furtherance of illicit financial activity, including transactions for parties connected to U.S. and UN-designated entities, some of which are involved in North Korea's procurement or export of ballistic missiles. In addition, ABLV management seeks to obstruct enforcement of Latvian AML/CFT rules. Through 2017, ABLV executives and management have used bribery to influence Latvian officials when challenging enforcement actions and perceived threats to their high-risk business.

ABLV's business practices enable the provision of financial services to clients seeking to evade financial regulatory requirements. Bank executives and employees are complicit in their clients' illicit financial activities, including money laundering and the use of shell companies to conceal the true nature of illicit transactions and the identities of those responsible. ABLV is considered innovative and forward leaning in its approaches to circumventing financial regulations. The bank proactively pushes money laundering and regulatory circumvention schemes to its client base and ensures that fraudulent documentation produced to support financial schemes, some of which is produced by bank employees themselves, is of the highest quality.

In 2014, ABLV was involved in the theft of over $1 billion in assets from three Moldovan banks, BC Unibank S.A., Banca Sociala S.A., and Banca de Economii S.A., in which criminals took over the three Moldovan banks using a non-transparent ownership structure, partly financed by loans from offshore entities banking at ABLV. Separately, ABLV previously developed a scheme to assist customers in circumventing foreign currency controls, in which the bank disguised illegal currency trades as international trade transactions using fraudulent documentation and shell company accounts.

As referenced in Section III of this notice, Latvian NRD banks cater to offshore shell companies, and ABLV is Latvia's largest NRD bank. Offshore shell company business poses inherent money laundering risks because of its lack of transparency, and financial institutions must manage the risks associated with providing financial services to shell companies. As described in detail below, ABLV's continuing failure to implement adequate AML controls commensurate with this high risk has caused the bank to facilitate transactions for shell companies owned or controlled by illicit actors engaged in transnational organized criminal activity, corruption, and sanctions evasion. Oftentimes, these actors take advantage of ABLV's propensity to facilitate high-risk shell company business, using shell company accounts to obscure the transparency of their illicit activities.

ABLV does not mitigate these risks effectively. ABLV does not adequately conduct know-your-customer (KYC) checks or customer due diligence (CDD) on a number of its customers, does not collect or update supporting documentation from its customers to justify transactional activity, and uses fraudulent documentation in some of its CDD files. Furthermore, the bank has had deficiencies in its internal control system, including insufficient customer due diligence and monitoring of transactions.

In an example demonstrative of ABLV's failures to mitigate these risks, ABLV received a substantial amount of funds from a Russia-based bank in a manner consistent with an illicit transfer of assets. FinCEN assesses that ABLV should have known that the shell companies receiving the Russian bank-sourced funds in their ABLV accounts were related to the ultimate beneficial owners of the Russia-based bank. Such a pattern is a hallmark of asset-stripping. In addition, ABLV has facilitated public corruption through the provision of shell company accounts for corrupt CIS-based politically exposed persons (PEPs) and other corrupt actors. Through 2014, for example, Ukrainian tycoon Serhiy Kurchenko funneled billions of dollars through his ABLV shell company accounts. Treasury's Office of Foreign Assets Control (OFAC) designated Kurchenko in 2015, finding that he was responsible for, complicit in, or had engaged in, directly or indirectly, the misappropriation of state assets of Ukraine or of an economically significant entity in Ukraine. ABLV

maintained at least nine shell company accounts linked to Kurchenko. In another example, an Azerbaijani PEP engaged in large-scale corruption and money laundering used a shell company account at ABLV to make a payment.

ABLV's business practice of banking high-risk shell companies without appropriate risk mitigation policies and procedures has also caused the bank to facilitate transactions for parties connected to U.S.- and UN-designated Democratic People's Republic of Korea (DPRK or North Korea) entities. These designated entities include Foreign Trade Bank (FTB), Koryo Bank, Koryo Credit Development Bank, Korea Mining and Development Trading Corporation (KOMID), and Ocean Maritime Management Company (OMM), some of which are involved in North Korea's procurement or export of ballistic missiles. ABLV facilitated transactions related to North Korea after the bank's summer 2017 announcement of a North Korea ''No Tolerance'' policy.

Widely available public documents describe North Korean sanctioned entities' use of front and shell companies and financial representatives to evade international sanctions. As early as 2014, the UN Panel of Experts (UN POE) noted in its report that sanctioned North Korean entities used front companies to evade international sanctions by hiding the sources of funds. Subsequent UN POE reports expanded on these findings, highlighting specific examples and methodologies used by North Korea-related entities to evade sanctions. Since 2011, the Financial Action Task Force (FATF) has called upon its members and urged all countries to apply effective countermeasures to protect their financial systems from the money laundering, terrorist financing, and proliferation financing threat emanating from the DPRK. More recently, the FATF has highlighted the DPRK's frequent use of front companies, shell companies, and opaque ownership structures for the purpose of evading international sanctions.

FinCEN has found that the DPRK is a foreign jurisdiction of ''primary money laundering concern.'' [8] In its finding, FinCEN highlighted North Korea's propensity to use front companies and agents to evade U.S. and international sanctions. Finally, nongovernmental research organizations have provided in-depth case studies of DPRK-linked entities' use of front companies and representatives to evade international sanctions.

[8] 81 FR 78715; November 9, 2016.

FinCEN assesses that the public nature of these reports, advisories, and actions should have provided ABLV the necessary guidance to apply appropriate due diligence to accounts and transactions that fit the typologies described in these public documents. However, ABLV's pursuit of high-risk shell company business and its failure to heed these public warnings and implement an appropriate risk-mitigating CDD and KYC program enabled certain customers to exploit ABLV's weaknesses to conduct transactions with parties connected to designated entities. Certain customers' counterparties have also been designated by OFAC, further demonstrating their links to the DPRK.

Ninety percent of ABLV's customers are high-risk per ABLV's own risk rating methodology and are primarily high-risk shell companies registered in secrecy jurisdictions. FinCEN assesses that, beginning in 2012 and continuing into 2017, ABLV conducted a high volume of transactions for shell companies registered outside of Latvia in offshore secrecy jurisdictions totaling tens of billions of dollars. FinCEN is aware that ABLV frequently fails to respond to other financial institutions' questions concerning the nature of the transactions that ABLV is processing. Multiple U.S. financial institutions have proactively closed ABLV's U.S. correspondent accounts. Nonetheless, ABLV's indirect correspondent activity with the U.S. financial system and its business model of facilitating non-transparent transactions for shell companies both continue.

While publicly stating that it is implementing plans to reform its AML/CFT compliance program, ABLV owners and executives have privately expressed an unwillingness to meaningfully alter ABLV's high-risk business practices. This fact, combined with ABLV's AML/CFT compliance issues to date raise serious concerns about the entity's commitment to implementing these plans. These concerns are further supported by the fact that ABLV management seeks to obstruct enforcement of Latvian AML/CFT rules and has used bribery to influence Latvian officials. Any institution that undermines enforcement actions through such corrupt acts presents a significant risk that it will continue practices which facilitate illicit activity.

2. The Extent to Which ABLV Is Used for Legitimate Business Purposes

As an NRD bank catering to non-Latvian customers, the majority of ABLV's customers are not based in Latvia and do not conduct business in Latvia outside of holding a bank account at ABLV. As described above, Latvia's NRD banking sector is a financial bridge between the CIS region's financial systems and the West. ABLV provides entities, typically controlled by CIS region-based actors, access to U.S. dollar, euro, pound sterling, and Swiss franc accounts, and ABLV's correspondent relationships enable its customers to transact with counterparties holding accounts at banks across the globe, including U.S. and EU financial institutions. Oftentimes, NRD customers are shell companies registered in corporate secrecy jurisdictions that are owned or controlled by parties in third jurisdictions, typically in the CIS region.

ABLV may be used for some legitimate purposes. However, the high number of shell company customers banking at ABLV, some of which are themselves engaged in money laundering or illicit activity, as described above, indicates that ABLV is extensively used for illicit purposes.

While it may carry certain risks or an additional AML/CFT compliance burden, non-resident banking is not inherently suspicious or illicit. For example, any non-Latvian entity banking in Latvia would maintain a ''non-resident'' account. Such non-Latvian clients may include lower-risk entities, such as publicly traded companies in the United States or other well-regulated jurisdictions. While such entities may be engaged in non-proximate banking, the customers' lines of business, ownership, and activity would be transparent, and the customers may be considered low-risk pursuant to the bank's internal policies and procedures and the relevant regulatory framework.

However, 90 percent of ABLV's customers are high-risk per ABLV's own risk rating methodology, and are primarily high-risk shell companies registered in secrecy jurisdictions, as discussed previously. FinCEN assesses that ABLV's shell company customers' involvement in a wide range of illicit and suspicious activity through ABLV indicates that ABLV does not properly control NRD accounts to ensure they are used primarily to conduct legitimate business

As noted above, FinCEN does not believe that ABLV, or its shareholders and executives, plan to meaningfully implement AML/CFT reforms. While publicly stating that it is implementing plans to reform its AML/CFT compliance program, ABLV owners and executives have privately expressed an unwillingness to meaningfully alter ABLV's high-risk business practices.

ABLV's ineffective reform measures are exemplified by its facilitation of transactions related to North Korea after the bank's summer 2017 announcement of a North Korea ''No Tolerance'' policy, as previously mentioned. Another illustration of ineffective reform measures is the facilitation of the aforementioned illicit transfers from a Russian bank, which occurred while ABLV was under an AML/CFT compliance audit.

2. The Extent to Which This Action Is Sufficient To Guard Against International Money Laundering and Other Financial Crimes

FinCEN assesses that ABLV is used to facilitate money laundering, illicit financial schemes and other illicit activity conducted by its customers and other illicit actors, including actors associated with transnational organized crime, North Korea's procurement or export of ballistic missiles, sanctions evasion, and large-scale corruption. Given the national security threat posed by such activity, FinCEN believes that imposing a prohibition under the fifth special measure would be sufficient and necessary to prevent ABLV from continuing to access the U.S. financial system. This action would guard against international money laundering activity and other financial crimes involving ABLV.

Although U.S. financial institutions have proactively closed direct U.S. correspondent relationships with ABLV, many U.S. financial institutions continue to process transactions for or on behalf of ABLV through indirect correspondent banking relationships. This action, if finalized, would sever ABLV's access to U.S. correspondent accounts, direct or otherwise.

V. Proposed Prohibition on Covered Financial Institutions From Opening or Maintaining Correspondent Accounts in the United States for ABLV

After performing the requisite interagency consultations, considering the relevant factors, and making a finding that ABLV is a foreign financial institution of primary money laundering concern, FinCEN proposes a prohibition under the fifth special measure. A prohibition under the fifth special measure is the most effective and practical measure to safeguard the U.S. financial system from the illicit finance risks posed by ABLV.

1. Factors Considered in Proposing a Prohibition Under the Fifth Special Measure

Below is a discussion of the relevant factors FinCEN considered in proposing a prohibition under the fifth special measure with respect to ABLV.

A. Whether Similar Action Has Been or Will Be Taken by Other Nations or Multilateral Groups Against ABLV

FinCEN is not aware of an action by another nation or multilateral group that would prohibit or place conditions on ABLV's correspondent banking relationships. However, according to press reports, the National Bank of Ukraine issued an advisory on August 28, 2016 to Ukrainian banks warning that ABLV, among other foreign banks, was suspected of being related to risky financial operations, including laundering the revenues of criminal activities. In addition, the FCMC has conducted examinations of ABLV and issued a fine and reprimand of a board member in May of 2016. None of these actions, however, sufficiently protect the U.S. financial system from the illicit finance risk posed by ABLV.

B. Whether the Imposition of the Fifth Special Measure Would Create a Significant Competitive Disadvantage, Including Any Undue Cost or Burden Associated With Compliance, for Financial Institutions Organized or Licensed in the United States

While ABLV is a large bank among Latvian financial institutions, it is not large by international standards and is not a major participant in the international payment system. Therefore, FinCEN does not believe that imposing a prohibition under the fifth special measure would cause a significant competitive disadvantage or place an undue burden or cost on U.S. financial institutions.

The special due diligence obligations proposed in this rulemaking would not create undue costs or burden on U.S. financial institutions. U.S. financial institutions already generally have systems in place to screen transactions in order to identify and report suspicious activity and comply with the sanctions programs administered by OFAC. Institutions can modify these systems to detect transactions involving ABLV. ABLV does not currently hold U.S. correspondent bank accounts. While there may be some additional burden on U.S. financial institutions in conducting due diligence on foreign correspondent account holders and notifying them of the prohibition, FinCEN believes that any such burden will likely be minimal, and certainly not undue, given the threats posed by ABLV's facilitation of money laundering.

C. The Extent to Which the Proposed Action or Timing of the Action Will Have a Significant Adverse Systemic Impact on the International Payment, Clearance, and Settlement System, or on Legitimate Business Activities of ABLV

As noted previously, although ABLV is a large bank among Latvian financial institutions, it is not large by international standards, is not a major participant in the international payment system, and is not relied upon by the international banking community for clearance or settlement services. Thus, the imposition of a prohibition under the fifth special measure against ABLV will not have an adverse systemic impact on the international payment, clearance, and settlement system. FinCEN also considered the extent to which this action could have an impact on the legitimate business activities of ABLV and concludes that the need to protect the U.S. financial system from ABLV, a bank that facilitates illicit financial activity, strongly outweighs any such impact.

FinCEN notes that ABLV as of July 2017 maintained euro, Japanese yen, Hong Kong dollar, pound sterling, and Australian dollar correspondent accounts, according to a commercial database, and thus is not necessarily limited to U.S. dollar transactions in its international wire transfer activity. A prohibition on the opening or maintaining of U.S. correspondent accounts under the fifth special measure would not prevent ABLV from conducting legitimate business activities in foreign currencies as long as such activity does not involve a correspondent account maintained in the United States.

D. The Effect of the Proposed Action on United States National Security and Foreign Policy

As described in detail above, financial activity that ABLV has conducted through the U.S. financial system has consisted largely of international funds transfers between shell entities registered in offshore secrecy jurisdictions. FinCEN assesses that this financial activity includes money laundering and other transactions conducted by a range of illicit actors that threaten the national security of the United States. Furthermore, ABLV's business practice of banking high-risk shell companies without adequate risk mitigation policies and procedures has caused the bank to facilitate transactions for entities linked to North Korea. Ensuring the effectiveness of the North Korea sanctions program is a top

national security and foreign policy priority of the United States.

Prohibiting covered financial institutions from maintaining a correspondent account for ABLV, and preventing ABLV's indirect access to a U.S. correspondent account, will enhance national security. The proposed action serves as a measure to prevent illicit actors from accessing the U.S. financial system. It will further the U.S. national security and foreign policy goals of thwarting sanctions evasion and preventing other illicit financial activity from transiting the U.S. financial system. The imposition of a prohibition under the fifth special measure would also complement the U.S. government's worldwide efforts to expose and disrupt international money laundering.

2. Consideration of Alternative Special Measures

Under Section 311, special measures one through four enable FinCEN to impose additional recordkeeping, information collection, and information reporting requirements on covered financial institutions. The fifth special measure also enables FinCEN to impose conditions as an alternative to a prohibition on the opening or maintaining of correspondent accounts. FinCEN considered alternatives to a prohibition under the fifth special measure, including the imposition of one or more of the first four special measures, as well as imposing conditions on the opening or maintaining of correspondent accounts under the fifth special measure. For the reasons explained below, FinCEN believes that a prohibition under the fifth special measure would most effectively safeguard the U.S. financial system from the illicit finance risks posed by ABLV.

Given ABLV's apparent disregard of regulatory reform and enforcement measures, FinCEN does not believe that any condition, additional recordkeeping requirement, or reporting requirement would be an effective measure to safeguard the U.S. financial system. Such measures would not prevent ABLV from accessing directly or indirectly the correspondent accounts of U.S. financial institutions, thus leaving the U.S. financial system vulnerable to processing the types of illicit transfers that pose a national security and money laundering risk. In addition, no recordkeeping requirement or conditions on correspondent accounts would be sufficient to guard against the risks posed by a bank that processes transactions that are designed to obscure the transactions' true nature and are ultimately for the benefit of illicit actors or activity. Therefore, a prohibition under the fifth special measure is the only special measure that can adequately protect the U.S. financial system from the illicit financial risk posed by ABLV.

VI. Section-by-Section Analysis for the Proposal of a Prohibition Under the Fifth Special Measure

1010.661(a) – Definitions

1. ABLV Bank, AS

The proposed rule defines ''ABLV'' to mean all subsidiaries, branches, and offices of ABLV Bank, AS operating as a bank in any jurisdiction. As noted above, FinCEN is aware of one subsidiary bank, ABLV Bank, Luxembourg, S.A., located in Luxembourg.

2. Correspondent Account

The proposed rule defines ''Correspondent account'' to have the same meaning as the definition contained in 31 CFR 1010.605(c)(l)(ii). In the case of a U.S. depository institution, this broad definition includes most types of banking relationships between a U.S. depository institution and a foreign bank that are established to provide regular services, dealings, and other financial transactions, including a demand deposit, savings deposit, or other transaction or asset account, and a credit account or other extension of credit. FinCEN is using the same definition of ''account'' for purposes of this proposed rule as was established for depository institutions in the final rule implementing the provisions of Section 312 of the USA PATRIOT Act requiring enhanced due diligence for correspondent accounts maintained for certain foreign banks.[9] Under this definition, ''payable through accounts'' are a type of correspondent account.

In the case of securities broker-dealers, futures commission merchants, introducing brokers-commodities, and investment companies that are open-end companies (''mutual funds''), FinCEN is also using the same definition of ''account'' for purposes of this proposed rule as was established for these entities in the final rule implementing the provisions of Section 312 of the USA PATRIOT Act requiring enhanced due diligence for correspondent accounts maintained for certain foreign banks.[10]

3. Covered Financial Institution

The proposed rule defines ''covered financial institution'' with the same definition used in the final rule implementing the provisions of Section 312 of the USA PATRIOT Act, which in general includes the following:

- An insured bank (as defined in section 3(h) of the Federal Deposit Insurance Act (12 U.S.C. 1813(h));
- a commercial bank;
- an agency or branch of a foreign bank in the United States;
- a Federally insured credit union;
- a savings association;
- a corporation acting under section 25A of the Federal Reserve Act (12 U.S.C. 611);
- a trust bank or trust company;
- a broker or dealer in securities;
- a futures commission merchant or an introducing broker-commodities; and
- a mutual fund.

4. Foreign Banking Institution

The proposed rule defines ''foreign banking institution'' to mean a bank organized under foreign law, or an agency, branch, or office located outside the United States of a bank. The term does not include an agent, agency, branch, or office within the United States of a bank organized under foreign law. This is consistent with the definition of ''foreign bank'' under 31 CFR 1010.100.

5. Subsidiary

The proposed rule defines ''subsidiary'' to mean a company of which more than 50 percent of the voting stock or analogous equity interest is owned by another company.

1010.661(b) – Prohibition on Accounts and Due Diligence Requirements for Covered Financial Institutions

1. Prohibition on Opening or Maintaining Correspondent Accounts

Section 1010.661(b)(1) and (2) of this proposed rule would prohibit covered financial institutions from opening or maintaining in the United States a correspondent account for, or on behalf of, ABLV. It would also require covered financial institutions to take reasonable steps to not process a transaction for the correspondent account of a foreign banking institution in the United States if such a transaction involves ABLV. Such reasonable steps are described in 1010.661(b)(3), which sets forth the special due diligence requirements a covered financial institution would be required to take when it knows or has reason to believe that a transaction involves ABLV.

2. Special Due Diligence for Correspondent Accounts

As a corollary to the prohibition set forth in section 1010.661(b)(1) and (2),

[9] *See* 31 CFR 1010.605(C)(2)(i).

[10] *See* 31 CFR 1010.605(c)(2)(ii)–(iv).

section 1010.661(b)(3) of the proposed rule would require covered financial institutions to apply special due diligence to all of their foreign correspondent accounts that is reasonably designed to guard against such accounts being used to process transactions involving ABLV. As part of that special due diligence, covered financial institutions would be required to notify those foreign correspondent account holders that the covered financial institutions know or have reason to believe provide services to ABLV that such correspondents may not provide ABLV with access to the correspondent account maintained at the covered financial institution. A covered financial institution may satisfy this notification requirement using the following notice:

Notice: Pursuant to U.S. regulations issued under Section 311 of the USA PATRIOT Act, see 31 CFR 1010.661, we are prohibited from opening or maintaining in the United States a correspondent account for, or on behalf of, ABLV. The regulations also require us to notify you that you may not provide ABLV, including any of its subsidiaries, branches, and offices with access to the correspondent account you hold at our financial institution. If we become aware that the correspondent account you hold at our financial institution has processed any transactions involving ABLV, including any of its subsidiaries, branches, and offices we will be required to take appropriate steps to prevent such access, including terminating your account.

The purpose of the notice requirement is to aid cooperation with correspondent account holders in preventing transactions involving ABLV from accessing the U.S. financial system. FinCEN does not require or expect a covered financial institution to obtain a certification from any of its correspondent account holders that access will not be provided to comply with this notice requirement.

Methods of compliance with the notice requirement could include, for example, transmitting a notice by mail, fax, or email. The notice should be transmitted whenever a covered financial institution knows or has reason to believe that a foreign correspondent account holder provides services to ABLV.

Special due diligence also includes implementing risk-based procedures designed to identify any use of correspondent accounts to process transactions involving ABLV. A covered financial institution would be expected to apply an appropriate screening mechanism to identify a funds transfer order that on its face listed ABLV as the financial institution of the originator or beneficiary, or otherwise referenced ABLV in a manner detectable under the financial institution's normal screening mechanisms. An appropriate screening mechanism could be the mechanisms used by a covered financial institution to comply with various legal requirements, such as the commercially available software programs used to comply with the economic sanctions programs administered by OFAC.

3. Recordkeeping and Reporting

Section 1010.661(b)(4) of the proposed rule would clarify that the proposed rule does not impose any reporting requirement upon any covered financial institution that is not otherwise required by applicable law or regulation. A covered financial institution must, however, document its compliance with the notification requirement described above.

VII. Request for Comments

FinCEN invites comments on all aspects of the proposed rule, including the following specific matters:

1. FinCEN's proposal of a prohibition under the fifth special measure under 31 C.5318A(b), as opposed to special measures one through four or imposing conditions under the fifth special measure;

2. The form and scope of the notice to certain correspondent account holders that would be required under the rule; and

3. The appropriate scope of the due diligence requirements in this proposed rule.

VIII. Regulatory Flexibility Act

When an agency issues a rulemaking proposal, the Regulatory Flexibility Act (RFA) requires the agency to ''prepare and make available for public comment an initial regulatory flexibility analysis'' that will ''describe the impact of the proposed rule on small entities.'' (5 U.S.C. 603(a)). Section 605 of the RFA allows an agency to certify a rule, in lieu of preparing an analysis, if the proposed rulemaking is not expected to have a significant economic impact on a substantial number of small entities.

1. Proposal to Prohibit Covered Financial Institutions From Opening or Maintaining Correspondent Accounts With Certain Foreign Banks Under the Fifth Special Measure

A. Estimate of the Number of Small Entities to Whom the Proposed Fifth Special Measure Will Apply

For purposes of the RFA, both banks and credit unions are considered small entities if they have less than $550,000,000 in assets.[11] Of the estimated 6,192 banks, 80 percent have less than $550,000,000 in assets and are considered small entities.[12] Of the estimated 6,021 credit unions, 92.5 percent have less than $550,000,000 in assets.[13]

Broker-dealers are defined in 31 CFR 1010.100(h) as those broker-dealers required to register with the Securities and Exchange Commission (SEC). For the purposes of the RFA, FinCEN relies on the SEC's definition of small business as previously submitted to the Small Business Administration (SBA). The SEC has defined the term small entity to mean a broker or dealer that: (1) Had total capital (net worth plus subordinated liabilities) of less than $500,000 on the date in the prior fiscal year as of which its audited financial statements were prepared pursuant to Rule 17a–5(d) or, if not required to file such statements, a broker or dealer that had total capital (net worth plus subordinated debt) of less than $500,000 on the last business day of the preceding fiscal year (or in the time that it has been in business if shorter); and (2) is not affiliated with any person (other than a natural person) that is not a small business or small organization as defined in this release.[14] Based on SEC estimates, 17 percent of broker-dealers are classified as small entities for purposes of the RFA.[15]

Futures commission merchants (FCMs) are defined in 31 CFR1010.100(x) as those FCMs that are registered or required to be registered as a FCM with the Commodity Futures Trading Commission (CFTC) under the Commodity Exchange Act (CEA), except persons who register pursuant to section 4f(a)(2) of the CEA, 7 U.S.C. 6f(a)(2). Because FinCEN and the CFTC regulate substantially the same population, for the purposes of the RFA, FinCEN relies on the CFTC's definition of small business as previously submitted to the SBA. In the CFTC's ''Policy Statement and Establishment of Definitions of

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[11] *Table of Small Business Size Standards Matched to North American Industry Classification System Codes,* Small Business Administration Size Standards (SBA Oct. 1, 2017) [hereinafter ''*SBA Size Standards*'']. .) (*https://www.sba.gov/sites/default/files/files/Size_Standards_Table_2017.pdf*)

[12] Federal Deposit Insurance Corporation, *Find an Institution, http://www2.fdic.gov/idasp/main.asp; select* Size or Performance: Total Assets, *type* Equal or less than $: ''550000'' and *select* Find.

[13] National Credit Union Administration, *Credit Union Data, http://webapps.ncua.gov/customquery/; select* Search Fields: Total Assets, *select* Operator: Less than or equal to, *type* Field Values: ''550000000'' and *select* Go.

[14] 17 CFR 240.0–10(c).

[15] 76 FR 37572, 37602 (June 27, 2011) (the SEC estimates 871 small broker-dealers of the 5,063 total registered broker-dealers).

'Small Entities' for Purposes of the Regulatory Flexibility Act,'' the CFTC concluded that registered FCMs should not be considered to be small entities for purposes of the RFA.[16] The CFTC's determination in this regard was based, in part, upon the obligation of registered FCMs to meet the capital requirements established by the CFTC.

For purposes of the RFA, an introducing broker-commodities dealer is considered small if it has less than $38,500,000 in gross receipts annually.[17] Based on information provided by the National Futures Association (NFA), 95 percent of introducing brokers-commodities dealers have less than $38.5 million in adjusted net capital and are considered to be small entities.

Mutual funds are defined in 31 CFR 1010.100(gg) as those investment companies that are open-end investment companies that are registered or are required to register with the SEC. For the purposes of the RFA, FinCEN relies on the SEC's definition of small business as previously submitted to the SBA. The SEC has defined the term ''small entity'' under the Investment Company Act to mean ''an investment company that, together with other investment companies in the same group of related investment companies, has net assets of $50 million or less as of the end of its most recent fiscal year.'' [18] Based on SEC estimates, seven percent of mutual funds are classified as ''small entities'' for purposes of the RFA under this definition.[19]

As noted above, 80 percent of banks, 92.5 percent of credit unions, 17 percent of broker-dealers, 95 percent of introducing broker-commodities dealers, no FCMs, and seven percent of mutual funds are small entities.

B. Description of the Projected Reporting and Recordkeeping Requirements of a Prohibition Under the Fifth Special Measure

The proposed prohibition under the fifth special measure would require covered financial institutions to provide a notification intended to aid cooperation from foreign correspondent account holders in preventing transactions involving ABLV from being processed by the U.S. financial system. FinCEN estimates that the burden on institutions providing this notice is one hour.

Covered financial institutions would also be required to take reasonable measures to detect use of their correspondent accounts to process transactions involving ABLV. All U.S. persons, including U.S. financial institutions, currently must comply with OFAC sanctions, and U.S. financial institutions have suspicious activity reporting requirements. The systems that U.S. financial institutions have in place to comply with these requirements can easily be modified to adapt to this proposed rule. Thus, the special due diligence that would be required under the proposed rule—*i.e.,* preventing the processing of transactions involving ABLV and the transmittal of notice to certain correspondent account holders—would not impose a significant additional economic burden upon small U.S. financial institutions.

2. Certification

For these reasons, FinCEN certifies that the proposals contained in this rulemaking would not have a significant impact on a substantial number of small businesses.

FinCEN invites comments from members of the public who believe there would be a significant economic impact on small entities from the imposition of a prohibition under the fifth special measure regarding ABLV.

IX. Paperwork Reduction Act

The collection of information contained in this proposed rule is being submitted to the Office of Management and Budget for review in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)). Comments on the collection of information should be sent to the Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Office of Management and Budget, Paperwork Reduction Project (1506), Washington, DC 20503 (or by email to *oirasubmission@omb.eop.gov*) with a copy to FinCEN by mail or email at the addresses previously specified. Comments should be submitted by one method only. Comments on the collection of information should be received by April 17, 2018. In accordance with the requirements of the Paperwork Reduction Act and its implementing regulations, 5 CFR 1320, the following information concerning the collection of information as required by 31 CFR 1010.661 is presented to assist those persons wishing to comment on the information collection.

The notification requirement in section 1010.661(b)(3)(i)(A) is intended to aid cooperation from correspondent account holders in denying ABLV access to the U.S. financial system. The information required to be maintained by that section would be used by federal agencies and certain self-regulatory organizations to verify compliance by covered financial institutions with the provisions of 31 CFR 1010.661. The collection of information would be mandatory.

Description of Affected Financial Institutions: Banks, broker-dealers in securities, futures commission merchants and introducing brokers-commodities, and mutual funds.

Estimated Number of Affected Financial Institutions: 5,787.

Estimated Average Annual Burden in Hours per Affected Financial Institution: The estimated average burden associated with the collection of information in this proposed rule is one hour per affected financial institution.

Estimated Total Annual Burden: 5,787 hours.

FinCEN specifically invites comments on: (a) Whether the proposed collection of information is necessary for the proper performance of the mission of FinCEN, including whether the information would have practical utility; (b) the accuracy of FinCEN's estimate of the burden of the proposed collection of information; (c) ways to enhance the quality, utility, and clarity of the information required to be maintained; (d) ways to minimize the burden of the required collection of information, including through the use of automated collection techniques or other forms of information technology; and (e) estimates of capital or start-up costs and costs of operation, maintenance, and purchase of services to report the information.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a valid OMB control number.

X. Executive Order 12866

Executive Orders 12866 and 13563 direct agencies to assess costs and benefits of available regulatory alternatives and, if regulation is necessary, to select regulatory approaches that maximize net benefits (including potential economic, environmental, public health and safety effects, distributive impacts, and equity). Executive Order 13563 emphasizes the importance of quantifying both costs and benefits, of reducing costs, of harmonizing rules, and of promoting flexibility. It has been determined that the proposed rule is not a ''significant regulatory action'' for purposes of Executive Order 12866.

[16] 47 FR 18618, 18619 (Apr. 30, 1982).

[17] SBA, Size Standards to Define Small Business Concerns, 13 CFR 121.201 (2016), at 28.

[18] 17 CFR 270.0–10.

[19] 78 FR 23637, 23658 (April 19, 2013).

List of Subjects in 31 CFR Part 1010

Administrative practice and procedure, banks and banking, brokers, counter money laundering, counter-terrorism, foreign banking.

Authority and Issuance

For the reasons set forth in the preamble, part 1010, chapter X of title 31 of the Code of Federal Regulations, is proposed to be amended as follows:

PART 1010—GENERAL PROVISIONS

■1. The authority citation for part 1010 continues to read as follows:

Authority: 2 U.S.C. 1829b and 1951–1959; 31 U.S.C. 5311–5314, 5316– 5332; Title III, sec. 314 Pub. L. 107–56, 115 Stat. 307; sec. 701 Pub. L. 114–74, 129 Stat. 599.

■2. Add § 1010.661 to read as follows:

§ 1010.661 Special measures against ABLV

(a) Definitions. For purposes of this section:

(1) ABLV means all subsidiaries, branches, and offices of ABLV Bank, AS operating as a bank in any jurisdiction.

(2) Correspondent account has the same meaning as provided in § 1010.605(c)(l)(ii).

(3) Covered financial institution has the same meaning as provided in § 1010.605(e)(l).

(4) Foreign banking institution means a bank organized under foreign law, or an agency, branch, or office located outside the United States of a bank. The term does not include an agent, agency, branch, or office within the United States of a bank organized under foreign law.

(5) Subsidiary means a company of which more than 50 percent of the voting stock or analogous equity interest is owned by another company.

(b) Prohibition on accounts and due diligence requirements for covered financial institutions—

(1) Opening or maintaining correspondent accounts for ABLV. A covered financial institution shall not open or maintain in the United States a correspondent account for, or on behalf of, ABLV.

(2) Prohibition on use of correspondent accounts involving ABLV. A covered financial institution shall take reasonable steps not to process a transaction for the correspondent account in the United States of a foreign banking institution if such a transaction involves ABLV.

(3) Special due diligence of correspondent accounts to prohibit use.

(i) A covered financial institution shall apply special due diligence to its foreign correspondent accounts that is reasonably designed to guard against their use to process transactions involving ABLV. At a minimum, that special due diligence must include:

(A) Notifying those foreign correspondent account holders that the covered financial institution knows or has reason to believe provide services to ABLV that such correspondents may not provide ABLV with access to the correspondent account maintained at the covered financial institution; and

(B) Taking reasonable steps to identify any use of its foreign correspondent accounts by ABLV, to the extent that such use can be determined from transactional records maintained in the covered financial institution's normal course of business.

(i) A covered financial institution shall take a risk-based approach when deciding what, if any, other due diligence measures it reasonably must adopt to guard against the use of its foreign correspondent accounts to process transactions involving ABLV.

(ii) A covered financial institution that knows or has reason to believe that a foreign bank's correspondent account has been or is being used to process transactions involving ABLV shall take all appropriate steps to further investigate and prevent such access, including the notification of its correspondent account holder under paragraph (b)(3)(i)(A) of this section and, where necessary, termination of the correspondent account.

(4) *Recordkeeping and reporting.* (i) A covered financial institution is required to document its compliance with the notice requirement set forth in this section.

(ii) Nothing in paragraph (b) of this section shall require a covered financial institution to report any information not otherwise required to be reported by law or regulation.

Dated: February 12, 2018.

Jamal El-Hindi,

Deputy Director, Financial Crimes Enforcement Network.

[FR Doc. 2018–03214 Filed 2–15–18; 8:45 am]

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MFSA

MALTA FINANCIAL SERVICES AUTHORITY

Combat of Money Laundering in the EU Banking System - Public Hearing

TAX3 – Special Committee on Financial Crimes, Tax Evasion and Tax Avoidance

European Parliament - 26 April 2018

Marianne Scicluna - Director General

Introduction

Mr Chairman, Members of the committee, thank you for inviting us to speak to you today about the Pilatus Bank case and what needs to be done to improve our ability to combat money laundering in the EU's banking system.

The MFSA is strongly committed to working with European institutions to advance the development of effective criteria and rigourous methodologies to prevent potential exposure to Money Laundering and Financing Terrorist (ML/FT) risks.

We applaud the initiative taken by the European Commission last week through its Proposal for a Directive to lay down new rules to facilitate the use of financial and other information to combat criminal activities. This is an important first step in strengthening the financial system as a whole. The case of Pilatus and other cases show the need for stronger cooperation and convergence of supervisory practices between competent authorities and policy makers.

We therefore welcome the opportunity to share with the Committee our experience on the Pilatus Bank case. I would ask you to note however that this is an ongoing investigation and that, as a financial regulator, we are still obliged to keep details of that investigation confidential.

I would like to focus on four main areas today: (i) the role of the MFSA in fighting money laundering and financial crime, (ii) the actions adopted by the MFSA on Pilatus Bank, (iii) how the MFSA has enhanced its approach to better address ML/FT risk, and (iv) our views on areas where the European framework could be strengthened.

The MFSA's role in combatting money laundering and financial crime

Our role within the Maltese regulatory landscape is to regulate and supervise financial institutions based on European Directives. We act within the scope of the Banking Union, applying the common methodology and approach to authorization and supervision. In parallel, the Maltese Financial Intelligence Analysis Unit-the FIAU-acts as the lead supervisor for AML, Counter-Terrorist Financing (CTF) and broader financial crime issues. Under the Prevention of Money Laundering Act the FIAU is responsible for monitoring and ensuring that financial institutions and other obliged persons comply with AML/CFT laws, regulations and procedures.

Under the terms of the same law, the FIAU may request a supervisory authority to carry out compliance examinations on its behalf or jointly with the FIAU. As I will outline below, in recent years, the MFSA

has sought to strengthen its ability to work with the FIAU and support them in supervising the AML risk institutions pose.

The licensing and supervisory approach and actions taken in the case of the Pilatus Bank

The MFSA's approach for granting a licence to a new applicant follows conditions, procedures and processes contained in local regulations that mirror the EU requirements set forth in the Capital Requirements Directive. Applicants for a banking license are required to submit comprehensive documentation which is then examined by our Authorisation Department. In considering their application, the MFSA is bound by rules of due process and the requirement to provide evidence to support any decision it makes.

As with any other entity applying for a license, Pilatus Bank submitted all the documentation required which included background and justification for requesting the license. These documents included information on the intended activities and business model. The MFSA further requested and received financial information as well as information on shareholders, management board and key function holders. Our staff reviewed the application, raising a number of questions on topics including the business model, the ownership structure, controls and governance, requiring the applicant to submit significant additional information and asking numerous follow up questions. We also took the additional step of commissioning an independent, third party intelligence report on the single shareholder from a reputable firm that supplies financial intelligence services to many Member States. After in depth scrutiny of all documents, information and individuals involved over more than fifteen months, we authorised the Bank. I would stress that this is a normal length of time for authorisation and that throughout we followed established procedures for a license application.

Since that moment, Pilatus Bank has been subject to high degree of ongoing supervision, including multiple on-site inspections, off-site reviews and investigation and the commissioning of an updated due diligence on the ultimate beneficial owner of the Bank.

An initial full on-site inspection was undertaken in September 2015, in line with our supervisory practices and approach for new licensed entities. Our review focused on monitoring whether the conditions for the license were being maintained, whether the Bank was adhering to its stated business plan and whether business was being conducted in compliance with banking regulations. The inspection identified a high concentration of PEP clients and, in line with cooperation arrangements with the FIAU, we reported this immediately to them and suggested they undertake an AML-focused inspection. In March 2016, the MFSA participated in a joint on-site inspection conducted by the FIAU focused specifically on money laundering and financial crime. In August 2016, we once again participated in another follow-up on-site inspection conducted by the FIAU.

Updated independent intelligence checks were carried out on the Ultimate Beneficial Owner of the Bank. There was also close liaison on this matter with other international regulators including the FCA. In addition, we informed the ECB and kept them updated.

Throughout, the MFSA continued its active prudential supervision of the bank, undertaking another on-site inspection in November 2017 focusing on the business model risks and internal governance. Soon after we launched a comprehensive and in-depth examination of the bank, including a review of all accounts and transactions. That examination is still ongoing.

Finally, as soon as we became aware of decisions by the US authorities to indict the shareholder of the bank, we felt we had legal basis to act. And we acted quickly and decisively. We immediately removed the Chairman, put a third party administrator in place and brought the institution's assets under control, preventing any withdraws.

The MFSA is closely monitoring the situation and analysing the results of its reviews to determine the next steps to be taken.

Our actions to enhance our approach to better address ML/FT risks

While the MFSA is not the lead supervisor for AML issues, we treat these matters with the utmost seriousness and we have significantly strengthened and renewed our focus on AML issues in recent years, backed by greater capacity and more resources.

We have restructured and increased resourcing for AML surveillance. In 2016 the MFSA established a centralised AML / CFT team to support the work of the FIAU. The Director of this Unit, Anton Bartolo is here with me today. Since then, we continued to invest in expanding the Unit's resourcing and deepening its expertise.

Together with the FIAU we have introduced a new risk based methodology for AML/CFT supervision to align with European standards and put tools that enable a more stringent and fit for purpose approach into the hands of supervisors. As part of this approach, we are also in the process of strengthening the scrutiny applied to banks' business models and the financial sector as a whole, working within the SSM.

And, importantly, we have reinforced our collaboration with the FIAU. Starting last year The FIAU now undertakes its inspections jointly with the MFSA's Enforcement Unit, using shared standards and procedures.

These continuing reforms in supervision in Malta show our strong commitment to combatting money laundering and strengthening the supervisory network.

However, we acknowledge that we need to continue to improve. We recognise that as a jurisdiction we must carry on working to strengthen our approach, not least to further enhance collaboration between the MFSA and FIAU and learn the lessons of recent experiences both in Malta and overseas.

That's why we welcome the new national anti-money laundering and terrorist financing strategy supported by a new co-ordination mechanism (the National Co-Ordination Committee on Combatting Money Laundering and Funding of Terrorism) to strengthen co-operation between different agencies in the fight against financial crime and ensure better collaboration between the relevant national authorities.

The importance of EU actions

However, to have maximum impact, and in light of the experiences and challenges faced with Pilatus Bank, we believe that renewed national action will need to be accompanied by new guidelines and frameworks at European level.

We are still developing our thinking but based on our experience, we would like to highlight three specific areas where European action could assist the ability of National Competent Authorities to ensure convergence in interpreting the framework and implementing supervisory actions to fight money laundering:

1. Assessment of banks business models. The EU framework does not currently provide precise criteria on how to assess business models that could potentially represent a high risk from a ML/FT perspective. National Competent Authorities would benefit from more precise criteria in order to assist enhanced scrutiny in their consideration of whether to refuse a license to a high risk institution. For instance, criteria on the type of information to be submitted, how different features of a business model could drive risk and how the overall level of risk should

be assessed could not only add rigour to the process, but also provide stronger basis for refusing to authorize an institution.

2. Treatment of ownership structures. Following on from the previous point, clear criteria that provide grounds in certain circumstances for refusing to license institutions that feature either a sole shareholder or a holding structure comprised of entities posing a potential ML/FT risk could also be of great value. For instance complex shareholding could be defined as a red flag and single shareholding – whilst being allowed by the current framework – in certain circumstances could be considered a risk to be avoided.
3. Depth of ongoing due diligence and monitoring. Under the current regulatory framework, institutions have to inform their NCA of any changes in their capital and shareholding structure, board membership and key functions as well as of any other significant changes to the information upon which their authorization was based. The current framework is silent on how ongoing monitoring should be conducted and the tools and analytic frameworks national authorities should use. Further guidance here would help strengthening the framework. For instance such guidance would provide concrete examples or recommended action plans that could be linked to the risks identified.

Providing further guidance on these areas would assist national authorities to better understand the risk exposure and how to calibrate the supervisory responses and the intensity of the actions undertaken.

Tied to this, we believe it would make sense to use this opportunity to explore further how the rules on removing licenses work and whether current EU Directives give sufficient weight to AML concerns. As I said earlier, our ability to act earlier on Pilatus Bank was limited by legal parameters and the importance of due process.

Conclusion

Money laundering is a critical issue and a huge challenge not only for Member States but for Europe as a whole. We remain utterly determined to take on money laundering to protect our shared financial system and look forward to working with the ECB, the EBA and others to build a stronger system together – a critical requirement given the growing concerns.

Thank you very much.

Special Committee on Financial Crimes, Tax Evasion and Tax Avoidance (TAX3)

"Combat of Money-Laundering in the EU Banking System"

Thursday 26 April 2018

European Parliament's Premises (Room JAN4Q1), Brussels

Dear Chairman

Dear members of the European Parliament,

I would like to take this opportunity to thank you for inviting us to participate in this public hearing in order to contribute towards the enhancement of our systems aimed at combatting money laundering and funding of terrorism within the European Union.

Introduction and brief overview

The Maltese Financial Intelligence Analysis Unit (FIAU) is a government agency established under the Prevention of Money Laundering Act. The Unit has two main distinct and separate functions. These are the analytical and supervisory function.

- The analytical function of the Unit is tasked with the receipt of suspicious transaction reports, and the analysis and dissemination of information. This section of the FIAU is also responsible for the exchange of information with FIUs, Law Enforcement Authorities, and Supervisory Authorities, both nationally and internationally.
- The supervisory function of the Unit is responsible for supervising subject persons, such as banks, to ensure that they are adhering to their AML/CFT obligations.

Our Unit plays other key roles in the fight against money laundering and funding of terrorism in Malta.

- The FIAU plans, leads and coordinates various initiatives such as the drafting of laws, regulations and binding guidance notes;
- The FIAU organises and participates in training sessions delivered to subject persons;
- The FIAU provides guidance and assists subject persons with AML/CFT queries;

- The Unit engages with subject persons in remediation, de-risking, follow-ups and other ancillary activities;

The Unit's remit is wide, and therefore challenging. To be effective, especially in a constantly changing environment within the financial and non-financial sectors, the Unit is continuously striving to develop and strengthen its resources. In fact, the FIAU's staff complement has grown significantly over the past few years, and so have the FIAU's technical and financial resources.

Nevertheless, the fight against money laundering and funding of terrorism is a difficult one indeed. Having the required resources can only do so much unless the right mechanisms are in place across the globe to combat crime such as money laundering and funding of terrorism.

These crimes are global phenomena, cross border and transnational crimes. Criminals engaged in such illegal activities know that not all countries are equal – and they take advantage of this.

Hence, we should evaluate whether the EU regulations and directives, coupled with the FATF recommendations, mutual evaluations and other types of evaluations, are really yielding the desired results. They certainly help – but are they enough?

We hope that the current round of evaluations, which use the latest revised FATF methodology that focuses on effectiveness, will help answer this question. But in the meantime, the evaluations that have been concluded so far under the revised methodology show that more than half of the European Union members states that have been evaluated achieved a moderate level of effectiveness or lower on FATF Immediate Outcome 6 and 7 – that is:

- Financial intelligence and all other relevant information are appropriately used by competent authorities for money laundering and terrorist financing investigations; and
- Money laundering offences and activities are investigated and offenders are prosecuted and subject to effective, proportionate and dissuasive sanctions.

According to FATF, a moderate level of effectiveness means that major improvements are needed. As for a low level of effectiveness, this means that fundamental improvements are needed.

We too have our own experiences. As we have already highlighted in our feedback to your questions, we are of the opinion that there are various initiatives that should be tackled and dealt with at a European level and beyond in order to complement and refine the current EU AML/CFT regime.

Building stronger cooperation on AML/CFT supervision across the EU

Throughout the past years, the European Union embarked on various legislative initiatives to address and enhance FIU to FIU cooperation. We truly welcomed this initiative, however, we wish to see similar initiatives which cover AML/CFT supervisory authorities. In the area of cooperation between AML/CFT supervisory, limited progress has been made. This has led to a fragmented system whereby Member States are working in silos and sharing of information, best practices and concerns is very limited or embraced on an informal basis. Whilst awaiting the publication of the 5th AMLD, which will seek to address this matter, we feel that more needs to be done in this regard.

Lack of technical support and guidance

The European Union has been highly effective in issuing and reviewing EU directives and regulations and this is essential in view of the ongoing changes and innovations taking place within the area. On the other hand, the EU has not put the same level of emphasis to provide technical support, general guidance notes and to organise technical/experts group meetings to assist supervisors and obliged entities in the implementation of these rules. Whilst we acknowledge that the 4th AMLD has mandated the European Supervisory Authority (ESA) to develop technical standards and guidance to assist credit and financial institutions in the fulfilment of their AML/CFT obligations, the latter mentioned approach was not adopted with non-financial services and professions. Hence, the EU should coordinate efforts to facilitate the implementation of the regulations both within the financial and non-financial sectors.

AML Regulatory Fatigue

We understand that the revision of laws and regulations is crucial to keep up with the fast-paced developments, however, more emphasis should be placed on the effective implementation of such laws and regulations. We need to find the right balance between making new rules and giving them time to work and have an effect.

Use of FIUs Intelligence

Latest statistics across Europe indicate that positive results are being registered in submission of STRs and quality of FIU to FIU cooperation. However, limited results are being registered in terms of investigations, prosecutions, convictions and finally confiscation of proceeds of crime in ML/TF cases. The latter is manifested across the EU and worldwide, and this is clearly evident from the results obtained during the latest mutual evaluations carried out by the FATF or FATF-Style Regional Bodies. EU wide efforts should be deployed to evaluate why progress registered in these areas is not leading to more positive results when it comes to prosecutions and confiscations.

Ultimately, this is key. What is the point of having so many regulations in place that contribute to a strong reporting mechanism when very few of those reports lead to a conviction and a confiscation?

Finantsinspektsioon

Overview of AML/CFT policy

Andre Nõmm

Member of the Management Board

26 April 2018

Disclaimer

- Proceedings conducted by Finantsinspektsioon are not public
- Information can only be disclosed in limited cases, *inter alia*, when:
  - Specific person concerned cannot be ascertained
  - A motivated decision to disclose has been taken in order to protect investors, clients and/or public
  - There are other specific grounds

Who does what: Finantsinspektsioon and Estonian FIU, etc

Finantsinspektsioon (Estonian FSA)

- To supervise whether credit and other financial institutions have
  - resources and other organisational processes,
  - systems and controls

  in place to prevent criminals from financing terrorism (TF) or from concealing or disguising, i.e. from laundering (ML), proceeds of crime (AML/CFT supervision)

The Financial Intelligence Unit (FIU)

- To collect and analyse STRs
- To disseminate analysed STRs that point to a criminal case

The Police and the Prosecutor's Office

- To conduct criminal proceedings, i.e. to investigate a criminal case and to prosecute

Finantsinspektsioon strategy since 2014

The new management board from 2014

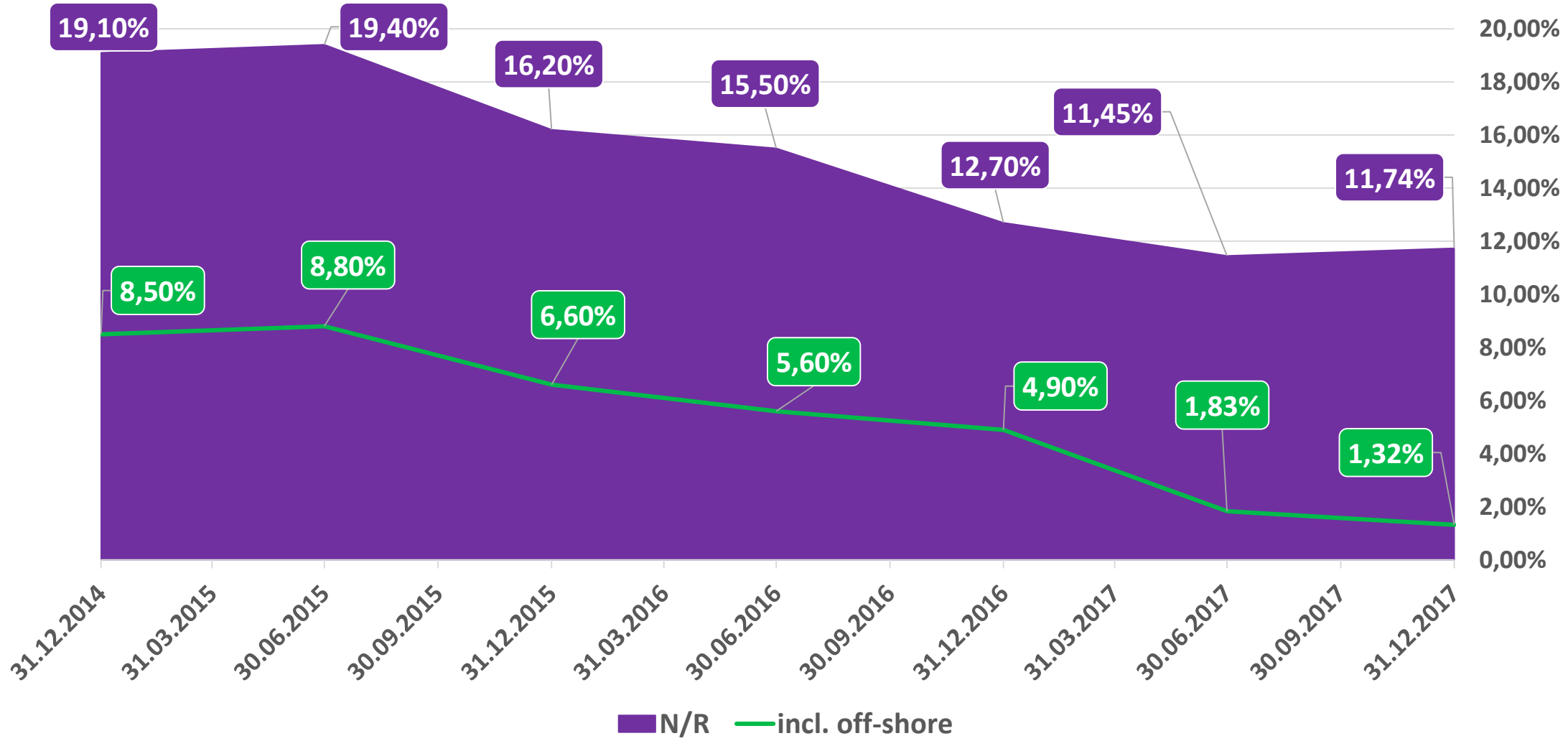
- Finantsinspektsioon re-organised its AML/CFT supervision methods
- Efforts on a risk-based basis to mitigate ML and TF risks
- Clear message to bank managers: Estonia is not a place for opaque banking (change of official strategy)
- **An immediate exercise (2014) to identify market participants with intolerable risk appetite**

The focus of Finantsinspektsioon (FSA) is on the lifecycle of financial services and products, with an emphasis on **anti-money laundering and combating the financing of terrorism**, development of financial services and products, and veracity of published information

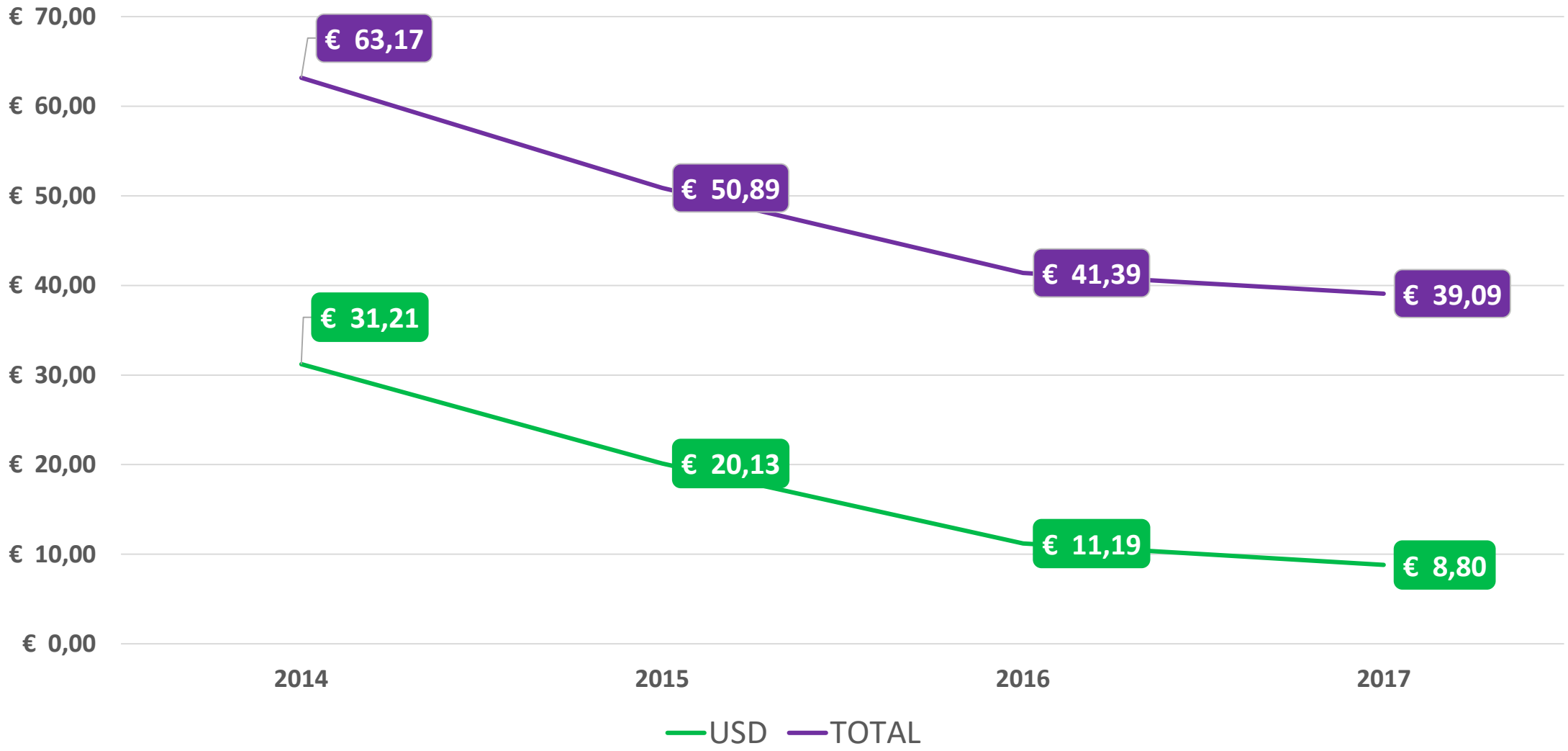
Supervisory actions in numbers

2014 – 2017					
	Number of entities (end of 2017)	Number of on-site visits conducted	Number of Ad hoc examinations	Number of off-site examinations	Actions combined with general supervision
Credit institutions and foreign branches	17	9	75	70	3
Investment Firms	3	0	0	9	1
Fund Management Companies	16	0	0	16	6
Life Insurance	4	4	0	8	0
PSP-s	13	3	4	37	13
E-Money SP	N/A	N/A	N/A	N/A	N/A
Consumer credit providers	62	5	0	62	62

Dynamics of non-resident deposits



Statistics of outgoing payments in Estonia (billion euros)



AML/CFT supervision is ongoing

- We have achieved results in the field of AML/CFT
- We continue with full commitment to ensure that credit and financial institutions have systems and controls in place to combat ML and TF
- Estonia is not the place to launder money or finance terrorism

Thank you!

Finantsinspektsioon

Introductory statement of the EBA Director of Banking Markets, Innovation and Consumers before the Special Committee on Financial Crimes, Tax Evasion and Tax Avoidance (TAX3)

26 April 2018

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)

Brussels, 26 April 2018

Dear Chairman, dear Members of the TAX3 Special Committee,

On behalf of the European Banking Authority, I would like to thank you for inviting me to take part in this public hearing.

This public hearing comes at a time when AML/CFT supervision is in the spotlight perhaps more than ever before. The Financial Action Task Force and MoneyVal, in their Mutual Evaluations, question the adequacy of some competent authorities' approaches to AML/CFT supervision; Members of national parliaments, as well as yourselves, are looking into supervisors' responses to various ML/TF scandals and find them to be wanting; and continuing allegations of breaches by financial institutions of applicable AML/CFT rules have led some commentators to question whether a more robust and consistent approach to testing financial institutions' AML/CFT compliance could have prevented these from happening.

These are important questions and observations, which we take very seriously: money laundering and terrorist financing not only undermine the integrity of the financial system but ultimately affect the society as a whole.

What, then, can we do, or should we do, to strengthen checks and controls and reduce ML/TF risks in the EU? And where does the EBA fit into all of this?

I would like to start by briefly outlining our role in relation to AML/CFT. I will then provide you with an overview of what we have already done, and what we are planning to do, to improve the European AML/CFT landscape. And I would like to conclude with some thoughts on how to enhance the effectiveness of the EU's approach to tackling financial crime.

The EBA's role

The EBA is an independent EU Authority. Our objective is to maintain the stability and effectiveness of the EU's financial system. As part of this, we promote sound, effective and consistent regulation and supervision and work to safeguard the integrity, transparency and orderly functioning of financial markets.

We also have a legal duty to foster the consistent and effective application of the Anti-Money Laundering Directive (AMLD).

The EBA's powers

We have a number of tools at our disposal to achieve our objectives. These range from issuing opinions, recommendations or guidelines to drafting legally binding standards, where this is foreseen by EU legislation. We also work to promote the effective implementation of our standards and EU law through training, peer reviews and facilitating the exchange of best practices, among others.

However, our powers to enforce our standards and guidelines are limited: we do not supervise individual financial institutions; and we do not currently have the legal tools to enforce compliance in a way that would compel a competent authority to change its approach. Of course, where we become aware of malpractice or suggestions that a competent authority may be in breach of Union law, we will investigate and, should a breach of Union law be confirmed, issue recommendations. However, these recommendations can only address breaches of union law and cannot make up for weak provisions in Union Law and associated weak or ineffective supervisory practices.

The EBA's AML/CFT work

We work closely with ESMA and EIOPA to have a consistent approach to AML/CFT across the Union's financial services industry. To the extent that this is possible under the AML Directive's minimum harmonisation framework, we work to promote a common supervisory culture and a shared understanding of the rules competent authorities seek to enforce to ensure that financial institutions, with similar ML/TF risk exposures and profiles, are treated consistently wherever they operate in the Single Market. This is important to prevent regulatory arbitrage and to protect the integrity of the EU's financial system: financial crime respects no borders.

To this end, over the last 18 months, we published three opinions, and issued two draft regulatory technical standards and three guidelines that come into force in the course of this year. Once implemented, they will help to bring AML/CFT practices together. For example,

- our risk factors guidelines foster a common understanding of the risk-based approach to AML/CFT. They provide financial institutions with the tools they need to make informed, risk-based and proportionate decisions on the effective management of ML/TF risk and help competent authorities assess whether the ML/TF risk assessment and management systems and controls of EU financial institutions are adequate;

- our risk-based supervision guidelines set out how competent authorities should assess the ML/TF risk associated with financial institutions and how they should reflect that assessment in their approach to AML/CFT supervision; and

- our draft regulatory technical standards on the application of group-wide AML/CFT policies and procedures in third countries establish a more harmonised approach to tackling ML/TF risk where a third country's law places restrictions on obtaining and processing customer data. Such restrictions limit a financial institution's ability to understand who their customers are and can also facilitate tax crimes, as highlighted in the context of the Panama and Paradise Papers.

Another area of focus, which results from our findings in our February 2017 joint opinion on ML/TF risk and our review of competent authorities' responses to the Panama Papers, is the promotion of cooperation and information exchange between competent authorities. Recent revisions to the AML

Directive will bring some much-needed legal certainty in this regard, and we are complementing this through own-initiative work on a framework to structure that co-operation and information exchange and create the conditions for it to be applied in practice. For example, we will expect that competent authorities that are responsible for the AML/CFT supervision of financial institutions that operate on a cross-border basis liaise regularly with their counterparts in other Member States.

These standards and guidelines constitute an important first step on the road towards a more consistent and effective European AML/CFT regime. Going forward, we will concentrate on their effective implementation. They have to be embedded in the AML/ CFT framework in all Member States and applied in practice by financial institutions as well as competent authorities. Over the last year, we already put on three very successful training events for competent authorities on various aspects of the new AML/CFT regime, and more events are planned. Following communications from a number of Members of the European Parliament, we conducted a preliminary enquiry into a potential breach of Union law in one Member State, Portugal, and made a number of suggestions based on our findings; and we are currently conducting preliminary enquiries into two further possible breaches of Union law, in Malta and Latvia. We have also drawn up an AML/CFT strategy that sets out how we will review AML/CFT supervision in a number of other Member States. When prioritising competent authorities for review, we will, of course, take due account of relevant information Members of the European Parliament have shared with us.

Enhancing the effectiveness of the EU's approach to AML/CFT

With the new AML directives and supporting guidelines and standards, we have taken one step towards a more harmonised approach to AML/CFT supervision and strengthening the financial sector's AML/CFT defences, and I believe we are on the right track. However, we are now approaching the limits of the EBA's powers and resources, and the limits of what is possible under the current legal framework.

We have identified three areas where we believe, based on our work thus far, that change is needed if Europe's AML/CFT regime is to be more effective.

- The AMLD's minimum harmonisation and directive-based approach does not eliminate national differences, and limits how much convergence our guidelines and standards can achieve: competent authorities and financial institutions will not be able to comply with our guidelines if national law stands in the way. Divergence of national practices exposes the Union's internal market to significant ML/TF risks, and a necessary first step towards a more effective AML/CFT regime is therefore a move towards greater harmonisation of the EU's legal AML/CFT framework.

- The EU's rules on authorisations and fitness and propriety rely heavily on national transpositions and interpretations. They leave little room for the development of a consistent approach to addressing ML/TF risk effectively in these contexts. Despite guidelines we have issued, concerns remain that some competent authorities think that they are unable to act on ML/TF concerns unless they can find evidence of criminal convictions. This is worrying, because once an individual is approved, or a financial institution is authorised, the passporting process enables them to provide their services across the Union unhindered. It is, therefore, important to re-think the way these legal provisions are drafted to ensure AML/CFT issues are given the attention they need and that competent authorities can intervene where necessary.

- The EBA needs to have the right powers and sufficient resources to take action where necessary to support the correct and consistent application of our standards and guidelines. The power to conduct independent reviews, with 'comply or explain' recommendations - such as the independent staff-led reviews and assessments of competent authorities' activities that are considered in the context of the current ESAs review –if accompanied by the resources needed to undertake such reviews would go some way towards addressing current shortcomings.

If these points sound familiar, this is no coincidence: my colleague, Isabelle Vaillant, made much the same points when she appeared before the PANA committee in October 2016, as did the EBA's chair, Andrea Enria, in communications with the co-legislators when the 5AMLD was being negotiated and in response to letters from several MEPs who wrote to us to share their AML/CFT concerns.

Thank you for your attention.

Introductory statement by Mauro Grande, Member of the Single Resolution Board

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)

26 April 2018

[To be checked against delivery]

Mr Chairman,

Honourable Members of the European Parliament,

Thank you for inviting me to discuss the important topic of how to strengthen checks and controls to reduce money-laundering risks in the banking system.

The mission of the Single Resolution Board is to ensure an orderly resolution of failing banks with minimum impact on the real economy, the financial system, and the public finances of the participating Member States and beyond. This does not mean that we wait for resolution cases to handle. Our role is proactive: we focus on resolution planning and preparation, to ensure resolvability of banks under our remit and minimise the potential negative impact of a bank failure.

As such, it is clearly not within the mandate of the SRB to detect and tackle money laundering. This said, the SRB has a natural interest in the topic, given the impact that money laundering, and related allegations can have on a bank's viability.

We are therefore happy to share the lessons we drew from the recent case of ABLV (discussed in the first panel): my introductory remarks today will focus on ABLV, and present reflections from the perspective of a resolution authority.

On 13 February 2018, the U.S. Department of the Treasury's Financial Crimes Enforcement Network (FinCEN) issued a notice of proposed rulemaking seeking to prohibit the opening or maintaining of a correspondent account in the US for, or on behalf of, ABLV. FinCEN proposed this measure based on its finding that ABLV is "a financial institution of primary money laundering concern". This was communicated to the ECB, which then informed the SRB, only shortly before publication of the notice.

The announcement by FinCEN gave rise to a sudden wave of deposit withdrawals and requests for withdrawals; and a lack of access to US Dollars funding, which resulted in ABLV being unable to make payments in US dollars. To stop the liquidity outflow, on 18 February, the National Competent Authorities of the parent company in Latvia and of the subsidiary in Luxembourg, instructed by the ECB, suspended all payments by the banks.

On 23 February, the ECB reached the conclusion that ABLV Latvia and ABLV Luxembourg were deemed to be failing or likely to fail (FOLTF): the significant deterioration of their liquidity position was making them unable to pay their debts or other liabilities as they fell due. Following this development, the SRB concluded that for these two banks resolution action was not in the public interest, as they did not provide critical functions for the economy of one or more Member States and their failure was not expected to have a significant adverse impact on financial stability in Latvia, Luxembourg or other Member States.

We have already discussed this case with members from the Committee on Economic and Monetary Affairs, and our views on how it highlights the need to harmonise national bank insolvency proceedings and align them with the FOLTF criteria. These are important lessons learnt for us and for legislators but are not the topic of this hearing.

With regard to "money laundering risks", for us the ABLV case is a reminder that when these risks materialise, similar to other operational risks, they can lead to an immediate loss of trust in the bank. This can trigger sudden and significant outflows of liquidity, and make the bank fail in a very short time-frame. This leaves the SRB with an extremely narrow window to assess whether it is in the public interest to resolve the bank, and, if so, to adopt an appropriate resolution scheme.

As such, from our perspective as resolution authority, this case recalled the importance of taking into due account different types of operational risks, including reputational risk, as part of our resolution planning and particularly in our dialogue with the supervisor.

The first lessons we can draw is that, to inform this dialogue between us and the supervisors, it is key that relevant information on AML risks is communicated to the supervisors, and to us, as soon as possible. In our view, the fifth review of the Anti-Money Laundering Directive makes some progress in this respect, as it clarifies the basis for exchange of information between the national authorities responsible for AML and prudential supervisors. Enforcement and operationalisation of such exchange of information is key.

Secondly, once information is improved, the dialogue with supervisor could better assess business models more "susceptible" to reputational risk, and take this into account when considering the possible scenarios of failure of the banks under SRB remit (e.g. in light of the specific speed of failures due to materialisation of reputational risks).

Beyond these lessons learnt from the perspective of resolution authority, let me share some more general thoughts on the AML policy framework and enforcement.

AML rules in the EU are still subject to only a minimum harmonisation, through a Directive rather than a Regulation. Moreover, the enforcement of these rules is entrusted to different national authorities across the EU Member States. Legislators should assess whether not only the exchange of information, but also the level of harmonisation of AML rules, and the split of competences is still fit for purpose or if, for instance, a Regulation rather than a Directive, and a centralised enforcement with an EU authority would improve the consistency and effectiveness of the framework. This is why we welcome the provision of AMLD 5 requiring the European Commission to consider proposing the establishment of a European FIU in future.

Coming to a conclusion, trust is a key premise of the banking sector. When trust is eroded, the financial situation of an institution can very quickly deteriorate. ABLV is the only the most recent reminder of this theorem. While we stand ready to minimize the negative repercussions of a bank failure - which can indeed be due to the materialisation of operational risks such as money-laundering activities – it is in everybody's interest to address risks before they can materialise.

Therefore, we support any attempt to ensure that the EU is equipped with a sound, up-to-date legislative framework, rigorously enforced to prevent, detect and address money-laundering risks (as well as other operational risks).

EUROPEAN CENTRAL BANK

BANKING SUPERVISION

Introductory remarks for the TAX3 Special Committee hearing on "Combat of Money-Laundering in the EU banking system"

Introductory statement
by Roberto Ugena, Deputy Director General
26 April 2018

Mr Chair,

Honourable Members of Parliament,

It's a pleasure to address you here today on behalf of ECB. Before I go into the question of how to strengthen the EU anti-money laundering framework, allow me to lay out for you the role of ECB Banking Supervision in relation to anti-money laundering efforts. I do this also to clarify on which kind of questions I will be able to provide meaningful answers during this hearing, and how the ECB can contribute to the fight against money laundering. For those of you who have followed the hearing of the Chair of the ECB Supervisory Board one month ago, some of this will seem familiar to you.

First and foremost, it is important to note that when creating the Single Supervisory Mechanism, the legislator clearly chose not to confer the supervisory tasks in the area of combatting money laundering to the ECB. In this context, it should be noted that Article 127(6) of the Treaty on the Functioning of the European Union, which has been the basis for the SSM Regulation, contains limits both as to the scope of the

supervisory tasks which can be conferred on the ECB and of the entities which could be supervised by the ECB.

The implementation and enforcement of anti-money laundering, or AML, legislation is therefore not a competence of the ECB. However, the ECB cooperates with the national authorities which are competent for AML supervision, to the extent permitted by law. [Owing to the principle of professional secrecy, such information exchange requires a clear legal basis.]

This distribution of competences implies that for the ECB to be able to reflect the findings and concerns of AML authorities in the prudential supervision, the ECB needs to be informed by the national AML authorities about such findings and concerns.

How this distribution works in practice:

When assessing the need for supervisory measures under the Pillar II framework, the ECB takes into account legal risks, which include the costs related to criminal prosecution, as well as reputational, operational, governance and other risks arising for banks from AML concerns where relevant information is available. But, without information received from the national AML authorities, the capacity of the ECB to act is extremely limited.

In the case of withdrawals of banking licences, serious breaches of national AML provisions can also justify the withdrawal of authorisation by the ECB. However, the fact that AML powers lie at national level means that one of the reasons for licence withdrawal remains essentially under the control of national authorities. In order to decide on a withdrawal of authorisation due to AML-related breaches of national

provisions, the ECB needs to be informed by the relevant national authority of all relevant facts and circumstances justifying the withdrawal.

Based on the outcome of assessments conducted by the AML authorities and within the boundaries of the applicable national law, the ECB also takes AML-related findings into account, when conducting the fit-and-proper assessments of banks' managers.

Let me stress that systematically identifying AML risks independently from the input of national AML authorities is not feasible for us.

Against this background and taking a forward-looking perspective, it is clear that much depends on the pro-active information sharing of national AML authorities with the ECB. The ongoing legislative process for the AMLD5 will help enhance the exchange of confidential AML-related information.

A more European approach on combatting money laundering could be considered. Taking into account the dual nature of AML, at the crossing between supervisory and judicial spheres, the review of the AML Directive might not suffice to ensure smooth and all-encompassing cooperation. The spectrum contributing to an all-encompassing cooperation can go from having a formalised exchange forum between national competent authorities on money laundering or even go up to a centralised authority.