

AML: New Guidance on Penalties for Breaches

In recent years there has been a growing emphasis on anti-money laundering and countering the financing of terrorism compliance (AML/CFT) as well as additional related regulatory requirements. However, the extent to which AML breaches could or should lead to the closure of businesses or revocations of regulatory authorisations has been unclear. The European Supervisory Authorities (the “ESAs”) published a joint report on 1 June 2022 (the “Report”) focusing on this issue and calling for the creation of a specific legal basis for license revocation of gross violations of AML/CFT rules.

Overview of the Report

The Report emphasizes the significance of incorporating AML/CFT issues within the framework of prudential regulation and oversight. It also describes the procedures and stages by which related policies ought to be implemented in future, as well as how each circumstance pertaining to a breach should be assessed. Finally, the Report notes that, while license revocation procedures are required, they are ultimately to be utilized as a last resort.

Withdrawal of Authorisation

Legal grounds already exist, either in EU legislation or directly in national provisions, alone or in conjunction with other grounds, to enable competent authorities in the EU to revoke an authorization or registration in the event of substantial AML/ CFT violations. Article 59 of the Anti-Money Laundering Directive is noteworthy in that it requires EU Member States to undertake the "withdrawal or suspension of authorisation" in circumstances of "serious, repetitive, and systematic breaches, or a combination thereof." Yet Directive 2013/36/EU (CRD) is the only sectoral statute that expressly provides for the revocation of authorization for serious violation or breaches of AML/CFT rules. Accordingly, the Report considers the benefits of legislative updates to include a specific legal foundation expressly permitting revocation of authorization or registration solely for serious violations breaches of AML/CFT rules and recommends the adoption of specific such provisions.

Definitions

According to Articles 8 and 59(1) of the Anti-Money Laundering Directive, 'AML/CFT rules' comprise the following:

1. Customer due diligence methods including risk evaluations for AML/ CFT, dependence on third parties, and transaction monitoring;
2. Reporting of suspicious transactions;
3. Record-keeping;
4. Internal AML/CFT procedures and controls, risk management systems, including AML/CFT risk assessments at operational levels.

The Report acknowledges that not all breaches of AML/CFT rules are regarded as equally serious, and that both the kind of AML/CFT provision breached and the characteristics of the breach should be evaluated. An AML/CFT supervisor should analyse and assess the criteria breaches on a case-by-case basis, taking contextual factors into account. There is currently no systematic relationship between a serious breach of AML/CFT rules and the revocation of authorization.

Criteria for Revocation

The Report cites four key determinants when considering if a licence revocation may be appropriate in the financial industry:

- a. lack of adequate oversight procedures to tackle the serious breach of AML/CFT rules;
- b. impact of revocation of authorisation (or registration) on financial health;
- c. lack of individual remedies to rectify the serious breach; and
- d. degradation of the firm's and/or the market's worth.

Legal Update

A failure to continue fulfilling the conditions under which the authorisation was granted is also noted as significant. The competent authorities have emphasised the importance of a specific AML/CFT risk assessment to be carried out at the time of granting authorisation – a requirement that is not set out in EU sectoral legislation.

To assess whether a breach is serious, the competent authorities should evaluate whether the following elements are present:

- i. Extended duration
- ii. Repetition
- iii. Egregious Nature
- iv. Knowledge of Breach by Senior Management
- v. Structured Failure of AML/CFT Systems
- vi. Impact on integrity, security or transparency of the financial system of a Member State or the Union as a whole
- vii. Impact on the viability of the obliged entity or the financial stability of a Member State or the Union as a whole.
- viii. Impact on the orderly function of financial markets
- ix. Facilitation of Financial Criminal Activity

Although the assessment of the competence rules will fall with the AML/CFT supervisor, the ultimate decision to withdraw authorisation will rest with a competent and prudential authority.

Criticalities and Scope

The ECJ has upheld the validity of the approach that regards revocation of authorization as a last resort step subject to discretionary and cases proportionate review (e.g. case T-351/18 or case T-27/19) In terms of scope, AML/CFT rules should apply to all entities that fall under the Anti-Money Laundering Directive.

Consequences

The Report has provided important clarifications on the circumstances in which firms should face the ultimate penalty for failing to ensure compliance by losing their authorisation.

Effective anti-money laundering and counter-terrorism financing regulations are critical to preserving the integrity of markets and the global financial system by mitigating the circumstances that allow financial misuse and accordingly appropriate penalties for failure to ensure compliance are vital. In the Irish context, following the publication of the Central Bank of Ireland's Behaviour and Culture Report in 2018, suitable culture and a thorough risk assessment are seen to be the pillars of a solid AML/CFT regime.

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