



LUXEMBOURG

FINANCIAL SECTOR ASSESSMENT PROGRAM

TECHNICAL NOTE—ANTI-MONEY LAUNDERING AND COMBATting THE FINANCING OF TERRORISM

August 2017

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July 2017

TECHNICAL NOTE

ANTI-MONEY LAUNDERING AND COMBATING THE FINANCING OF TERRORISM (AML/CFT)

Prepared By
Legal Department

This Technical Note was prepared by IMF staff in the context of the Financial Sector Assessment Program in Luxembourg. It contains technical analysis and detailed information underpinning the FSAP's findings and recommendations. Further information on the FSAP can be found at <http://www.imf.org/external/np/fsap/fssa.aspx>

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Glossary

4AMLD	Fourth EU Anti-Money Laundering Directive
AML	Anti-Money Laundering
CAA	<i>Commissariat aux Assurances</i>
CDD	Customer Due Diligence
CFT	Combating the Financing of Terrorism
CSSF	<i>Commission de Surveillance du Secteur Financier</i>
DNFBPs	Designated Non-Financial Businesses and Professions
FATF	Financial Action Task Force
FIU	Financial Intelligence Unit
FSAP	Financial Sector Assessment Program
GDP	Gross Domestic Growth
LBA	Luxembourg Bar Association
MER	Mutual Evaluation Report
ML	Money Laundering
MoF	Ministry of Finance
MoJ	Ministry of Justice
NRA	National Risk Assessment
OECD	Organisation for Economic Cooperation and Development
SRB	Self-Regulatory Bodies
STR	Suspicious Transaction Report
TCSPs	Trust and Company Service Providers
TF	Terrorist Financing
TN	Technical Note
VAT	Value-Added Tax

EXECUTIVE SUMMARY

This technical note (TN) sets out the findings and recommendations made in the 2017 Financial Sector Assessment Program (FSAP) Update for Luxembourg in a few selected areas of Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT). It summarizes the findings of a targeted review of Luxembourg's progress in addressing vulnerabilities in its AML/CFT framework that have been identified by staff as being most significant in context, namely those with respect to tax crimes as predicate offenses to money laundering (ML), access to adequate beneficial ownership information of legal persons and arrangements, AML/CFT supervision of banks, trust and company services providers (TCSPs), and lawyers, and the detection and exchange of financial intelligence. The TN also provides a factual update on the key measures taken by the authorities since Luxembourg's 2011 FSAP. This is not an evaluation or assessment of Luxembourg's AML/CFT system. Luxembourg is scheduled to undergo an assessment against the prevailing standard—the Financial Action Task Force (FATF) 2012 40 Recommendations—in 2020.

Due to the size, interconnectedness and attractiveness of its financial sector, Luxembourg faces potentially significant inherent ML/TF risks, in particular from proceeds of foreign tax crimes. Concerns have been raised in the past by the FATF (notably with respect to insufficient transparency over the beneficial ownership of legal persons) and the Organisation for Economic Cooperation and Development (OECD) (with respect to insufficient coverage of tax crimes). More recently, the media highlighted, notably in the context of the so-called Panama papers, the alleged use by intermediaries around the world, including Luxembourg banks and other intermediaries, of opaque corporate structures that potentially facilitate tax crimes.

Since the last FSAP update, important steps have been taken to strengthen the AML/CFT regime. As reflected in the 2011 FSSA, the FATF 2010 mutual evaluation report of Luxembourg highlighted significant shortcomings in the AML/CFT framework. A substantial number of legislative and regulatory measures were taken shortly after the evaluation to address the most important deficiencies identified. Luxembourg also took steps to implement the new requirements of the 2012 FATF standard, notably by initiating a national assessment of its ML/TF risks. Work is underway to implement the 4th EU Anti-Money Laundering Directive (4AMLD), and the authorities are actively engaged in the ongoing discussions within the EU on a 5th EU Anti-Money Laundering Directive (5AMLD). Measures are also being taken to assess the allegations in the media of potential misuse of corporate structures.

Luxembourg's risk profile appears to be evolving as a result of the authorities' push for increased tax transparency. Over recent years, several important remedial measures were introduced, the most recent ones being the recent inclusion of tax crimes in the AML/CFT framework, and the mechanism for automatic exchange of tax information with a substantial number of foreign tax authorities based on OECD and EU standards. These two measures have been communicated to the public prior to their January 1, 2017 entry in force, and this communication appears to have contributed to a reduction of the incentive to use Luxembourg's financial sector for tax evasion purposes. At the moment, the understanding of the risks faced and posed by the various

professions that may act as TCSPs appears to be fragmented between the various competent supervisory and monitoring authorities. The ongoing national risk assessment (NRA) is anticipated to shed light on the current risks faced by Luxembourg, and guide the authorities in developing adequate mitigating measures.

Transparency of the beneficial ownership of legal persons has also improved. This is in particular the case for companies that may issue bearer shares, with the required immobilization of these shares with appointed depositories. The authorities are also taking steps to verify that shares issued in bearer form have effectively been deposited or cancelled.

AML/CFT supervision has been strengthened in recent years but challenges remain, including with respect to lawyers. The supervisor of banks and main TCSPs, i.e., the *Commission de Surveillance du Secteur Financier* (CSSF), has considerably strengthened its AML/CFT supervision by increasing the number of staff, as well as the duration of its onsite visits. The Luxembourg Bar Association (LBA) has also made efforts to increase its monitoring function, and this has notably led to greater awareness amongst lawyers of their AML/CFT obligations and of the ML/TF risks that they face. Overall, however, the intensity of monitoring by the LBA appears modest and the CSSF's supervisory resources may become stretched if the NRA points to a need for increased supervisory efforts. AML/CFT monitoring of TCSPs operating under the purview of other authorities is unclear.

Progress is also evident in the exchange of financial intelligence with foreign counterparts, but the authorities need to ensure that the Financial Intelligence Unit (FIU) resources remain adequate. The FIU has been proactive in sharing a large number of suspicious transaction reports (STRs) with foreign counterparts on a spontaneous basis, and has received positive feedback in response. The FIU's resources have been strengthened in light of the increase in the number of STRs and the potential further increase that may result from the inclusion, from January 1, 2017 onwards, of tax crimes as predicate offenses to ML. The FIU nevertheless remains small relative to the size of Luxembourg's financial sector and of the number of STRs received, and may see its resources stretched if the new tax crimes generate a larger number of STRs than anticipated.

Table 1. Luxembourg: Main Recommendations for AML/CFT

Recommendations	Time Frame*	Authorities
General		
Ensure that the 2016/2017 national risk assessment (NRA) focuses adequately on the risks of TCSPs as defined in the FATF standard.	I	MoF
Complete the NRA in a timely fashion, and share its findings within the government and with the private sector as appropriate.	I	MoF
On the basis of the completed NRA, take the necessary risk mitigation policy and operational measures.	NT	MoF
Tax crimes as Predicate Offenses to Money Laundering		
Issue guidance on the reporting of suspicions of tax crimes and ML related to tax crimes to reporting entities not supervised by the CSSF, including by clarifying the type of information that reporting entities should collect and providing a list of potential red flags of tax crimes.	I	FIU, and DNF�Ps regulators
Access to Beneficial Ownership Information		
Finalize the targeted supervisory program related to the Panama Papers and take necessary mitigating and enforcement actions that the review may call for.	I	CSSF
Detection and Exchange of Financial Intelligence Information		
Update the FIU Law regarding international cooperation in line with the current FATF Recommendations.	MT	MoJ
Monitor the resources of the FIU in light of the NRA results and inclusion of tax crimes as predicate offenses to ML, and ensure that they remain commensurate with the workload.	MT	MoJ, FIU
AML/CFT Supervision of Banks, TCSPs and Lawyers		
Further increase intensity (i.e., frequency and depth) of AML/CFT monitoring of lawyers by the Bar Association.	NT	MoJ, LBA
Ensure that sufficient resources are available for risk-based AML/CFT supervision of banks and TCSPs.	MT	CSSF, and all other TCSP regulators
If necessary, align the current risk classification of banks and TCSPs under the CSSF's purview in light of the findings of the NRA.	NT	CSSF
Ensure that AML/CFT monitoring of TCSPs outside the CSSF and LBA purview is adequate and commensurate to ML/TF risks.		Tax administration; MoF, Order of accountants
* Time Frame: C = continuous; I (immediate) = within one year; NT (near term) = 1–3 years; MT (medium term) = 3–5 years.		

INTRODUCTION¹

1. This TN provides a targeted review of Luxembourg's AML/CFT system in the context of the 2017 FSAP.² This review is not an assessment or evaluation of Luxembourg's AML/CFT system. As noted below, a comprehensive assessment against the current FATF standard will take place after the completion of this FSAP.

2. Luxembourg has a large, highly interconnected financial center. It notably has a world-leading financial services industry. The main components of the financial system are the investment and money market fund industry³ (€3.7 trillion in assets under management, 72 times GDP),⁴ banking industry (€773 billion in assets, 14 times GDP), insurance industry (€219 billion, 4 times GDP), and financial market infrastructures (FMIs) that clear and settle payments and securities transactions. Its fund administration sector is the second largest in the world, and its private banking sector is the largest in the Eurozone and is ranked sixth in the world.

3. Due to its size and other features⁵ that make it attractive for international commercial and financial intermediation, Luxembourg is vulnerable to ML/TF risks, and both the FATF and the OECD have raised financial integrity concerns. As indicated in the June 2011 FSAP update,⁶ Luxembourg's AML/CFT framework was assessed by the FATF in 2009 and was found to be deficient in a number of important areas.⁷ The OECD Global Forum on Transparency and Exchange

¹ This note was prepared by Nadine Schwarz and Richard Berkhout, Legal Department, IMF.

² Under FSAP policy, every FSAP should incorporate timely and accurate input on AML/CFT issues. Where possible, this input should be based on a comprehensive AML/CFT assessment conducted against the prevailing standard. In instances where a comprehensive assessment against the prevailing standard is not available at the time of the FSAP, (as is the case with Luxembourg) staff may derive key findings on the basis of other sources of information, including already available information or information obtained in the context of the FSAP. See the Acting Chair's Summing Up—Review of the Fund's Strategy on Anti-Money Laundering and Combating the Financing of Terrorism—Executive Board Meeting 14/22, March 12, 2014 (<http://www.imf.org/external/np/sec/pr/2014/pr14167.htm>).

³ Money market fund (MMF) assets account for just €246 billion of the total.

⁴ The assets under management of the investment fund industry are not directly equivalent to balance sheet assets in the banking industry. Investment firms operating collective investment vehicles do not retain investment risk.

⁵ As noted in other areas of this FSAP, Luxembourg presents a number of other characteristics which render its financial sector attractive, such as an AAA-rating, political stability, fiscal prudence, and a highly skilled multi-lingual workforce.

⁶ IMF: Financial Sector Assessment update—Luxembourg, June 2011, paragraph 32 (page 23–24), IMF Country Report No. 11/148.

⁷ FATF: *Rapport d'Evaluation Mutuelle du Luxembourg* (Mutual Evaluation Report of Luxembourg), February 19, 2010 (<http://www.fatf-gafi.org/countries/j-m/luxembourg/documents/mutualevaluationofluxembourg.html>). The report identified several significant shortcomings concluded that, overall, Luxembourg's AML/CFT efforts were not proportional to the risks associated with its role as a key international financial center. For instance, shortcomings were identified in the areas of customer due diligence (CDD), correspondent banking, suspicious transaction reporting and internal controls; supervisory authorities conducted few on-site AML/CFT inspections; the sanctions regime was inadequate; access by competent authorities to accurate and up-to-date information on the beneficial

of Information for Tax Purposes (the Global Forum) assessed the exchange of information in practice from 2009 to 2011. It highlighted several positive features in Luxembourg's framework, as well as areas for further improvement.

4. Substantial progress has since been made. The FATF explicitly recognized that Luxembourg had addressed the main deficiencies identified in its mutual evaluation report (MER).⁸ The follow-up report to the Global Forum assessment also found that Luxembourg had brought its framework to a satisfactory level of compliance with the relevant standard. Due to the limitations of the FATF follow-up process, the measures taken with respect to some of the other deficiencies were noted but not analyzed by the FATF. This note provides an update in some of these respects.

5. Luxembourg has a comprehensive AML/CFT legal, regulatory and institutional framework based for the most part on EU instruments and FATF standard. The legal framework consists primarily of the AML/CFT law of November 12, 2004 as amended,⁹ a number of provisions in the Criminal Code, notably Articles 506-1 and 135-6 which criminalize respectively ML and TF, the Code of Criminal Procedure, and several sectorial laws. Several Grand-Ducal Regulations and Regulations issued by the FIU and the AML/CFT supervisors supplement that framework.

6. Luxembourg will be assessed against the current FATF standard after the completion of this FSAP. The FATF standard and assessment methodology were revised in 2012 and 2013, respectively, placing a greater emphasis on a risk-based approach to AML/CFT and on assessing the effectiveness of the AML/CFT regime. Luxembourg is tentatively scheduled to undergo an assessment by the FATF in mid-2020.¹⁰ The relevant mutual evaluation report is anticipated to be discussed and adopted by the FATF in February 2021.

7. As discussed with the authorities at the beginning of this exercise, staff's review focused on a few AML/CFT issues of particular relevance in Luxembourg's context. In selecting

ownership of legal persons was insufficiently timely; no steps had been taken to prevent the illicit use of bearer shares; and there were gaps in the criminalization of ML/TF. As a result of these -and other- deficiencies, Luxembourg was placed under enhanced scrutiny by the FATF's International Cooperation Review Group. Significant progress was made shortly thereafter, thus enabling Luxembourg to be removed from such scrutiny.

⁸ Since the adoption of its MER, Luxembourg reported six times to the FATF on the progress made, and was removed from the FATF follow-up process in February 2014.

⁹ Loi du 12 novembre 2004 relative à la lutte contre le blanchiment et contre le financement du terrorisme portant transposition de la directive 2001/97/CE du Parlement européen et du Conseil du 4 décembre 2001 modifiant la directive 91/308/CEE du Conseil relative à la prévention de l'utilisation du système financier aux fins du blanchiment de capitaux et modifiant : 1. le Code pénal ; 2. le Code d'instruction criminelle ; 3. la loi modifiée du 7 mars 1980 sur l'organisation judiciaire ; 4. la loi modifiée du 23 décembre 1998 portant création d'une commission de surveillance du secteur financier ; 5. la loi modifiée du 5 avril 1993 relative au secteur financier ; 6. la loi modifiée du 6 décembre 1991 sur le secteur des assurances ; 7. la loi modifiée du 9 décembre 1976 relative à l'organisation du notariat ; 8. la loi modifiée du 10 août 1991 sur la profession d'avocat ; 9. la loi modifiée du 28 juin 1984 portant organisation de la profession de réviseurs d'entreprises ; 10. la loi du 10 juin 1999 portant organisation de la profession d'expert-comptable ; 11. la loi modifiée du 20 avril 1977 relative à l'exploitation des jeux de hasard et des paris relatifs aux épreuves sportives ; 12. la loi générale des impôts ("Abgabenordnung").

¹⁰ The next evaluation will focus mainly on the effectiveness of the AML/CFT framework.

the issues for discussion, staff relied on publicly available information, especially from the Article IV consultation and the FATF. The TN sets out the progress made in addressing the main deficiencies identified in the previous assessment and in implementing a central feature of the 2012 standard (i.e., the requirement on countries to assess the ML/TF risks that they face). The TN also discusses measures taken with respect to a few other elements of the standard that were identified as most relevant in Luxembourg's context, namely tax crimes as predicate offenses to ML; access to beneficial ownership information of legal persons and arrangements; the detection and exchange of financial intelligence regarding nonresidents; and AML/CFT supervision of banks, TCSPs, and lawyers.

8. Staff analysis was based on a range of materials and benefited from discussions with the authorities and private sector representatives. Staff reviewed available information, including information submitted by Luxembourg to the FATF on progress made between June 2010 and February 2014 in addressing the deficiencies identified in its last AML/CFT assessment,¹¹ and answers provided by the authorities to an extensive questionnaire submitted ahead of the FSAP. During its mission to Luxembourg (December 5–12, 2016), staff held discussions with a range of competent authorities involved in AML/CFT, namely: the Ministry of Finance (MoF), the Tax Administration; the Ministry of Justice (MoJ); the Public Prosecution, the FIU; and the *Commission de Surveillance du Secteur Financier* (CSSF). It also met with representatives of the LBA and other professions (banks, investment funds, domiciliation companies, and asset management firms). The review was conducted against the backdrop of the 2012 FATF Recommendations and 2013 assessment methodology.

PROGRESS SINCE THE LAST FSAP ASSESSMENT

A. Implementation of 2010 Assessors' Recommended Actions

9. Since the FATF evaluation and 2011 FSAP, the authorities have made significant progress in addressing the AML/CFT shortcomings identified. They implemented a speedy remedial action plan, which included legislative, institutional and regulatory changes. In February 2014, the FATF concluded that Luxembourg had sufficiently addressed key shortcomings related to (i) the criminalization of ML; (ii) confiscation of illicit proceeds; (iii) licensing of financial institutions and their supervision; (iv) sanctions for non-compliance; (v) implementation of international instruments; (vi) the freezing of terrorist assets and mutual legal assistance in CFT efforts.¹² It therefore concluded that Luxembourg had reached a level of compliance at least equivalent to Largely Compliant for all the key and core FATF Recommendations.¹³ Additional measures have also

¹¹ The Luxembourg authorities submitted six progress reports to the FATF. The 6th report of February 2014 can be found at <http://www.fatf-gafi.org/countries/j-m/luxembourg/documents/fur-luxembourg-2014.html>

¹² FATF: Mutual Evaluation of Luxembourg: 6th Follow-up Report, February 2014, on www.fatf-gafi.org.

¹³ The FATF recognized 16 of the then 40+9 Recommendations as “key” and “core” for a sound AML/CFT system (including, for example, previous Recommendations 1 and 5, respectively on the ML offense and customer due diligence requirements). The focus of the follow-up process was on these 16 Recommendations. Since 2012, the FATF Recommendations have been updated, and the follow-up process has changed.

been taken since then in response to other deficiencies identified in the 2010 FATF report, notably with respect to bearer shares (discussed below).

B. Bringing the AML/CFT Framework in Line with the 2012 Standard

10. Luxembourg is taking steps to implement the 2012 standard, notably by assessing its ML/TF risks. The authorities initiated an NRA in July 2016. The process is led by the MoF in collaboration with a broad range of other authorities involved, directly or indirectly, in Luxembourg's AML/CFT efforts (e.g., MoJ, the FIU, law enforcement agencies, intelligence services, supervisors, Tax administration, Customs, Ministry of Foreign Affairs) and private sector representatives (including the LBA). At the time of drafting of this note, discussions between public sector stakeholders focused on the methodology to be used, the mapping of the activities and sectors to be included in the NRA, and on the type of the data to be collected. An agreement had been reached to focus the exercise on the residual risk (i.e., the combination of the inherent risks-in terms of threats and vulnerabilities-and the effectiveness of existing mitigating measures). Discussions with private sector representatives had also been planned, and the authorities anticipated to bring the NRA to a close no later than mid-2017. These efforts are welcome, as conducting the NRA is a critical first step for countries to develop or adjust mitigating action. As of the time of the FSAP visit, no decision had been taken as to whether the NRA or parts thereof will be published, or whether alternative means of communication will be used. Other measures taken in implementation of the 2012 standard are indicated in the following chapters.

11. Luxembourg is also in the process of implementing European requirements. As a member of the European Union, Luxembourg is required to transpose the 4th EU AML Directive (4AMLD)¹⁴ into its national law by June 2017. In addition, discussions are currently ongoing at the European level on a 5th EU AML Directive (5AMLD) which may amend some of the requirements of the 4AMLD. The authorities have already implemented some of the EU requirements (such as the inclusion of tax crimes as predicate offenses to ML, as discussed below) and are currently working on a legislative package with the aim of implementing the 4AMLD by the transposition deadline, notably with respect to the creation of a register of beneficial ownership of legal entities (discussed below). Some elements of the package may need to be adjusted, depending on the outcome of the EU discussions on the 5AMLD, which may affect certain requirements of the 4AMLD (such as the central register containing information on beneficial ownership of legal arrangements).

C. Conclusions and Recommendations

12. The authorities have significantly enhanced the AML/CFT legislative and regulatory framework, and should continue their efforts to implement the 2012 FATF standard in an effective way. Current plans linked to the completion of the NRA and the implementation of the EU

¹⁴ Directive (EU) 2015/849 of the European Parliament and of the Council of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, amending Regulation (EU) No 648/2012 of the European Parliament and of the Council, and repealing Directive 2005/60/EC of the European Parliament and of the Council and Commission Directive 2006/70/EC (Text with EEA relevance).

4AMLD are to be commended as they will further strengthen the AML/CFT regime. Going forward, in addition to addressing the issues discussed in the chapters below, the authorities should:

- Ensure that the 2016/2017 NRA focuses adequately on the risks of TCSPs as defined in the FATF standard. It is recommended that, in doing so, all the professions that may act as TCSPs be considered in a holistic way.
- Complete the NRA in a timely fashion, and share its findings within the government and with the private sector as appropriate. In order to ensure a common understanding of Luxembourg's risks, among competent authorities as well as among private sector entities, publication of the NRA's main findings could be considered.
- On the basis of the completed NRA, take the necessary risk mitigation policy and operational measures.

TAX CRIMES AS PREDICATE OFFENSES TO MONEY LAUNDERING

A. Introduction

13. Pursuant to the 2012 FATF Recommendations, serious tax crimes should be predicate offenses to ML.¹⁵ While the standard does not define "tax crimes," it specifies that they should include a range of tax offenses relating to direct and indirect taxes. It also clarifies that, when deciding on the range of offenses to be covered as predicate offenses, countries may decide, in accordance with their domestic law, how they will define those offenses and the nature of any particular elements of these offenses that make them serious offenses.

14. Tax crimes are predicate offenses in Luxembourg since January 1, 2017. Article 506-1 of the Criminal Code criminalizes ML and lists a wide range of predicate offenses, which, since the January 1, 2017 entry into force of the tax reform Law of December 23, 2016, includes six tax crimes.

B. Criminalization of Tax Offenses

15. In December 2016, Luxembourg strengthened the criminalization of tax offenses. The tax reform law of December 23, 2016, was published on December 27, 2016, and came into force on January 1, 2017. Under the current legislation, the main tax offenses (which apply with respect to income tax, value-added tax (VAT) and inheritance tax) are:

- Tax evasion (*fraude fiscale*), i.e., fraudulently obtaining undue tax advantages for oneself or for a third party, or intentionally reducing the state's tax income (Section 396(1) of the

¹⁵ Predicate offenses are the underlying crimes that generate assets to be laundered. The FATF established a list of 21 categories of crimes (including tax crimes, as well as others such as corruption and bribery, fraud and organized crime) that should be considered as predicate offenses. Tax crimes were added as predicates in 2012.

General Tax Law). It is an administrative offense punishable by an administrative fine ranging from 10 to 50 percent of the amount of evaded taxes.

- Aggravated tax evasion (*fraude fiscale aggravée*, Section 396(5) of the General Tax Law) which consists of the same elements as tax evasion, with the addition, however, of two thresholds, namely, the evaded taxes exceed (i) 25 percent of the annual taxes to be paid, while exceeding the amount of €10,000 (relative threshold), or (ii) €200,000 of annual taxes (absolute threshold). It is punishable by a criminal fine ranging from €25,000 to six times the evaded amount of taxes and imprisonment (one month to three years).
- Tax fraud (*escroquerie fiscale*) and its attempt (Section 396(6) of the General Tax Law) is a criminal offense consisting of the systematic use of fraudulent acts aimed at concealing relevant facts to avoid paying taxes or to be reimbursed for paid taxes.¹⁶ It is punishable by a criminal fine ranging from €25,000 to 10 times the evaded amount of taxes and imprisonment (one month to five years).

16. Luxembourg's tax crimes now appear on par with those in neighboring countries. The criminal sanctions for aggravated tax evasion (*fraude fiscale aggravée*) and for tax fraud (*escroquerie fiscale*), i.e., up to three- to five-year imprisonment, and up to six to ten times the evaded amount of taxes, appear proportionate and dissuasive, also in comparison to the sanctions available for comparable offenses in most neighboring countries. In particular, depending on the specific circumstances of the case, false or incorrect or non-filing of taxes may constitute either aggravated tax evasion (*fraude fiscale aggravée*) or tax fraud (*escroquerie fiscale*) when the thresholds and criteria for these offenses are met.

17. **The tax reform law also introduced additional supporting measures.** These include strengthened national coordination and international cooperation provisions.

C. Tax Offenses as a Predicate Offense for ML

18. **As of January 1, 2017, six forms of tax crimes (and their attempt) constitute predicate offenses to ML.** In addition to aggravated tax evasion and tax fraud mentioned above (respectively Sections 396(5) and 396(6) of the General Tax Law), four other tax crimes are listed as predicate offenses: (i) aggravated tax evasion within the meaning of article 29 of the law of January 28, 1948 on registration fees and inheritance tax, as modified, as well as its attempt; (ii) tax fraud within the meaning of article 29 of the Law of January 28, 1948 on registration fees and inheritance tax, as modified, as well as its attempt; (iii) aggravated tax evasion within the meaning of article 80 (1) of

¹⁶ The tax reform bill clarifies that "inaccurate declaration is the material element of fraud, but if it is based on inaccurate accounting for more likelihood, then there is maneuver." The notion of "maneuvers" covers the means used to trick the confidence of a person. The maneuvers must, in addition, be fraudulent in the sense that they must aim to abuse a third party (i.e., the tax administration). Pursuant to a court decision n°1344/2008 dated April 24, 2008, this implies that maneuvers must (i) be fraudulent; (ii) have an external form; (iii) be determinant for the delivery, and (iv) aim to abuse confidence or credulity. The "fraudulent maneuvers" must in addition be "systematic," which, pursuant to a court decision n°354/2002 dated February 14, 2002, refers to maneuvers used consistently, as well as to maneuvers applied continuously."

the law of February 12, 1979 regarding VAT, as modified, as well as its attempt; and (iv) tax fraud within the meaning of article 80 (1) of the law of February 12, 1979 regarding VAT, as modified, as well as its attempt. This seems a sufficiently broad range of serious tax offenses to meet the requirement of the 2012 FATF standard.

19. The inclusion of tax crimes in Luxembourg's AML/CFT framework constitutes significant progress. In addition to bringing the ML offense in line with the standard, it strengthens the framework by limiting an important vulnerability.

20. Representatives of the private sector welcomed the change and highlighted the need for guidance. At the time of the FSAP discussions (December 2016), the tax reform bill was pending adoption by Parliament. Nevertheless, the various supervisory authorities and self-regulatory bodies (in particular the CSSF and the LBA), as well as representatives of the private sector met were well aware of the proposed changes, as the latter had been made public in the course of 2016. Representatives of the private sector welcomed the proposed changes but also indicated that the scope of the new offenses and their implications on the performance of some of their AML/CFT obligations were not entirely clear to them. Therefore, they called for guidance to assist in (i) the performance of customer due diligence (CDD) measures, more specifically on the type of documents that would need to be collected from customers going forward, and (ii) the detection of potential suspicions of tax crimes. At the time of the mission, the FIU and CSSF were working on a joint circular that would notably set out their common understanding of the new offenses. The circular has since been finalized and published on the CSSF website.¹⁷ It is addressed to reporting entities supervised by the CSSF, and provides guidance with regard to the practical implementation of the tax reform law. It also includes potential indicators of laundering of the proceeds of tax crimes.

D. Additional Measures Taken

21. As a result of the Luxembourg government's commitment to increased transparency in tax matters, a number of additional measures have been taken, notably to fight tax evasion.

They include the following:

- i. Luxembourg has signed and ratified the Multilateral Joint Council of Europe/OECD Convention on mutual administrative assistance in tax matters and its Protocol, and thus has a network of information exchange mechanisms covering 108 jurisdictions. With regard to the procedures applicable in relation to exchange of information upon request, Luxembourg has reinforced its legal framework, as confirmed by the Law of November 25, 2014 on the exchange of information. The law also introduced an anti-tipping off provision applicable to the information holder.
- ii. Luxembourg is one of the signatories of the Common Reporting Standard (CRS) multilateral Competent Authorities Agreement which provides for the automatic exchange of information. Developed by the OECD, the CRS calls on jurisdictions to obtain information

¹⁷ <https://www.cssf.lu/surveillance/criminalite-financiere/lbc-ft/circulaires/>

from their financial institutions and automatically exchange that information with other relevant jurisdictions on an annual basis. It aims at reducing tax evasion by ensuring that information on accounts held by nonresidents in Luxembourg is shared with the tax authorities in the account holders' country of tax residence. The automatic exchange of information enters into force in Luxembourg on January 1, 2017 with 54 countries. It is expected that exchanges with some 100 countries will become possible in 2018, in addition to the exchange with the US based on the Foreign Account Tax Compliance Act.

- iii. With a view to increasing transparency, Luxembourg has also passed the Law of July 28, 2014 in relation to the immobilization of bearer shares and the keeping of a register of bearer shares (see below).
- iv. At the European level, Luxembourg has implemented in 2015 the Directive on mandatory automatic exchange of tax information (2014/107/EU), which introduces the CRS and its obligations between member states.
- v. In addition, the authorities reported having taken steps to implement a 2015 EU Directive (2015/2376/EU; agreed under Luxembourg's Presidency of the European Union) calling for the automatic exchange of information on cross-border tax rulings, as well as EU Directive 2016/881/EU on country-by-country reporting.

22. These additional measures are welcome. While not directly called for in the FATF standard, they are expected to strengthen Luxembourg's AML/CFT framework by reducing the country's exposure to proceeds of tax crimes.

E. Conclusions and Recommendations

23. The recent tax reform law strengthens the AML/CFT framework further. Some key features of the law (in particular the inclusion of tax crimes in the AML/CFT framework, and strengthened national coordination and international cooperation), as well as the automatic exchange of tax information considerably bolster Luxembourg's means to prevent and fight the misuse of its financial sector for ML purposes. To ensure that all reporting entities implement the new requirement to detect and report suspicions of tax crimes in an effective way, it is important that they understand the scope of the relevant tax offenses, and the regulatory expectations with respect to CDD.

24. Going forward, the authorities should:

- Issue guidance on the new reporting requirements to reporting entities not supervised by the CSSF, including by clarifying the type of information that reporting entities should collect and providing a list of potential red flags of tax crimes.

ACCESS TO BENEFICIAL OWNERSHIP INFORMATION OF LEGAL PERSONS AND ARRANGEMENTS

A. Introduction

25. All legal persons established in Luxembourg must be registered in the Registry of Businesses and Corporations (*Registre de Commerce et des Sociétés*). Commercial companies have a legal personality distinct from that of their members. Several types of commercial companies may be established under Luxembourg law, namely, the general partnership (*société en nom collectif*), the limited partnership (*société en commandite simple*), public or joint stock company (*société anonyme*), partnership limited by shares (*société en commandite par actions*), the (private) limited liability company (*société à responsabilité limitée*), the cooperative (*société cooperative*) and the European company (*société européenne*).¹⁸

26. The *fiducie* (a legal arrangement similar to the Common Law trust) may also be established in Luxembourg.¹⁹ Only supervised entities, i.e., professionals acting in a licensed capacity (e.g., banks, financial sector professionals, investment managers) may act as *fiduciaire* (i.e., trustee). According to the authorities, most are supervised for AML/CFT purposes by the CSSF and the *Commissariat aux Assurances* (CAA, the supervisor for insurance companies), except lawyers, who are self-regulated by the relevant Bar Associations (see below). It is not established whether and to what extent other professions, such as TCSPs not monitored by the CSSF, CAA and LBA (see below) also act as *fiduciaires*. According to the authorities and the Global Forum,²⁰ very few Luxembourg *fiducies* have been established.

27. In addition, foreign trusts are set up and administered in Luxembourg under the relevant foreign jurisdiction's legislation. Foreign trusts are recognized under the conditions laid

¹⁸ For a description of the commercial companies available under Luxembourg law, see pp. 15–18 of the MER. Commercial companies are distinct from the commercial associations or partnerships (*association commerciales*), temporary partnerships (*associations commerciales momentanées*) and joint ventures (*associations en participation*), which do not have legal personality.

¹⁹ The Law of July 27, 2003, approving the Hague Convention of July 1, 1985, on the law applicable to trusts and on their recognition, establishes new regulations for fiduciary contracts, and amends the Law of September 25, 1905, on the transcription of real property rights. Pursuant to article 5 of the law of July 27, 2003, the *fiducie* is a contract by which one person, the settlor (*fiduciant*), agrees with another person, the fiduciary (*fiduciaire*) that, subject to the obligations determined by the parties, the fiduciary becomes the owner of assets which shall form a fiduciary property. In contrast to a trust, a *fiducie* involves a definitive transfer of ownership of the assets placed in *fiducie*. Article 6, however, stipulates that the fiduciary property is distinct from the property of the fiduciary, and that the fiduciary must, in its accounts, record the fiduciary property separately from its own property.

²⁰ OECD Report, Global Forum on Transparency and exchange of information for tax purposes, Peer Review Report Phase 2, 2013, p. 47.

out in the Law of July 27, 2003.²¹ The exact number of foreign trusts administered in Luxembourg is unclear. According to the authorities, the majority of TCSPs in Luxembourg provide *corporate* services, rather than services to domestic or foreign trusts. This includes providing a registered office to companies without exerting significant influence (also known as domiciliation services). It also includes fund administration services, human resources and payroll services, special purpose vehicle management services and tax compliance services.

28. Concerns have been raised in the past about the lack of transparency of legal entities and arrangements in Luxembourg. This was notably the case of the FATF in 2010,²² and the Global Forum in 2011 and 2013.²³ The FATF noted that the register of legal persons did not allow for the identification of the beneficial owner in all cases, that there was no measure in place to guarantee that the registered information was accurate, and that no measure was in place to ensure adequate transparency of legal persons that issue bearer shares. The Global Forum raised similar concerns in 2011 and 2013, but in 2015 also recognized the progress Luxembourg had made to address some of these concerns.²⁴ More recently, Luxembourg, alongside other financial centers, came under public scrutiny after the April 2016 leaks of confidential information in the context of the "Panama Papers."²⁵ According to the ICIJ's analysis of the papers, four Luxembourg banks (two of which have since stopped operating) were among the ten banks that had requested the most offshore companies for clients, and in these papers Luxembourg ranked fourth in the list of countries with the most active intermediaries and seventh where intermediaries operate. While these leaks do not necessarily point to problems of transparency in Luxembourg itself, they have raised questions about the role of Luxembourg intermediaries (both banks and TCSPs) in the creation of opaque structures using foreign legal entities and arrangements, and in facilitating crimes including ML and tax crimes. According to the authorities, the Luxembourg banks' adherence to the International

²¹ Trusts established under the law of other jurisdictions are recognized in Luxembourg under the conditions laid out in the Law of July 27, 2003, approving the Hague Convention of July 1, 1985 on the law applicable to trusts and on their recognition.

²² Find the AML/CFT mutual evaluation report of Luxembourg here: <http://www.fatf-gafi.org/countries/j-m/luxembourg/documents/mutualevaluationofluxembourg.html>.

²³ Global Forum's 2011 and 2013 Peer Review Reports of Luxembourg (Phases 1 and 2): http://www.oecd-ilibrary.org/taxation/global-forum-on-transparency-and-exchange-of-information-for-tax-purposes-peer-reviews_2219469x.

²⁴ In its Supplementary Report of 2015, the Global Forum recognized that the authorities made progress since then by taking steps to increase the transparency of (i) legal persons that issue bearer shares by passing a law providing for the immobilization of bearer shares, and (ii) legal arrangements such as trusts by requiring service providers to retain information on the settlers and beneficiaries of trusts and *fiducies*. However, it also noted that further measures were necessary to ensure that information on the beneficial ownership of legal persons is readily available to the competent authorities.

²⁵ The so-called Panama Papers refers to the leak of some 11.5 million documents created over more than 30 years by a Panamanian law firm, Mossack Fonseca, and covering the financial and attorney-client information for more than 210,000 offshore entities. While the papers point to potential misuse of corporate entities to notably hide assets, avoid taxes, evade financial sanctions, etc. in many countries and not only Luxembourg, the ICIJ also explicitly recognized that there are legitimate uses for offshore companies and trusts.

Capital Market Association (ICMA) Private Wealth Management Charter of Quality, which is monitored by the CSSF, provides assurances that the Panama Papers do not reflect current practices.

B. Measures in Place and Actions Taken

29. As mentioned above, the register of companies includes information on the legal ownership of companies, which may—but does not necessarily—coincide with beneficial ownership information. The register is publicly available. The information it contains is, however, not verified.

30. All FIs and Designated Non-Financial Businesses and Professions (DNFBPs) designated under the AML/CFT law are required to identify the beneficial owner of their customer as part of regular CDD. Article 3 paragraph 2b of the AML/CFT law requires all reporting entities to identify the beneficial owner (which the law defines in a way that is consistent with the standard) and to take reasonable measures to verify his/her identity, and, in the case of corporate customers, *fiducies* and similar legal arrangements, to take reasonable measures to ensure that they understand the ownership and control structure of the entity. These requirements also apply to TCSPs who may act as nominee director for a company, and for professional trustees. The implementation of these obligations is supervised by the CSSF in the case of financial institutions other than insurance companies and for some TCSPs, the CAA in the case of insurance companies, and a range of other supervisors and SRBs, including some other TCSPs, in the case of most DNFBPs.

31. Access to beneficial ownership information held by financial institutions and DNFBPs is currently possible for judicial authorities²⁶ as part of an investigation. The threshold for opening an investigation is relatively low, and thus does not prevent law enforcement from requesting information when needed, even at an early stage of a case. Similarly, the FIU has broad powers to request information, including outside the receipt of an STR.

32. The quality of information collected on the beneficial owners appears to be good. The CSSF and the LBA indicated that reporting entities under their purview generally performed well in identifying the ultimate beneficial owner (or refusing the relationship and reporting the case to the FIU when identification was not possible) and adequately verified the information received. This view was shared by the FIU. According to the CSSF and LBA, deficiencies in that respect were rare, and have been subject to CSSF enforcement action (but not of LBA actions). Representatives of the private sector (including banks, asset management firms, and TCSPs (in particular from a *société de domiciliation*) indicated that in most instances, the identification of the ultimate beneficial owners was not a major challenge because customers, including new customers, are aware of the need, for Luxembourg's reporting entities, to collect beneficial ownership information, and are generally willing to cooperate.

²⁶ The notion of “judicial authorities” includes the instructing *juge* (*juge d’instruction*) as well as the public prosecutor.

33. The authorities are responding quickly to assess concerns raised in the media about the potential use of (mainly foreign) opaque structures. In particular, immediately following the publication of the "Panama papers," the CSSF initiated a targeted supervisory review of a number of banks. An initial survey was sent to selected banks seeking information on their activities.²⁷ A more in-depth review was conducted of "outlier banks," namely those selected on a risk-basis according to their scoring under the specific criteria.²⁸ On the basis of the information received, a working group was established within the CSSF Risk Division of the Banking Supervision Department, and identified a sample of 30 banks for further onsite examination with the assistance of external auditing firms (which had to be other than the regular auditor of the bank). Thereafter, the CSSF has assessed the identified risk banks for compliance with the relevant AML/CFT obligations. The final report detailing the results of the in-depth review is expected to be finalized in late Q2 2017. So far, the review led to four STRs being filed. It also revealed that, between 2007 and 2016, assets of offshore structures under management in Luxembourg decreased by 35 percent, and the number of offshore structures by 52 percent. According to the CSSF, three quarters of Luxembourg's banks do not offer any administrative services to offshore vehicles at least since 2012.

34. Some interviewees raised concerns that the focus of the authorities in this regard is directed too heavily on banks. Whereas banks are being reassessed in this area, TCSPs are not examined in so much depth.

35. Further improvements in relation to the transparency of legal persons and arrangements are to be expected with the implementation of the 4AMLD. The 4AMLD requires that countries register beneficial ownership information of legal entities set up in their country. Luxembourg is in the process of drafting legislation to implement this requirement, which will make beneficial ownership information available to the authorities, reporting entities, and others on a need-to-know basis. The legislation is expected to be enacted in June 2017. Implementation of similar requirements regarding legal arrangements is also underway. Depending on the outcome of the discussions on the 5AMLD, which may change key provisions of the EU requirements in this area the measures might have to be adapted at a later stage.

C. Bearer Shares

36. Luxembourg has abolished bearer shares through a registration requirement. Pursuant to legislation in force since 2014, all existing and new bearer shares should have been deposited

²⁷ Information was sought on: (i) the scope of their business with off-shore companies; (ii) their level of administrative services offered to off-shore structures; (iii) the measure taken to ensure compliance with the Charter of the International Capital Market Association (ICMA) and in particular tax compliance; (iv) the role of the legal and compliance departments as well as the internal audit to check and report about ICMA rules.

²⁸ The criteria used are the following: number of offshore accounts; evolution of accounts numbers from 2012 to 2016; assets under management; percentage of accounts linked to Mossack Fonseca; administrative services provided to offshore vehicles; measures taken to ensure compliance with ICMA Charter; role of the legal and compliance department as well as internal audit.

with one of eight approved types of a depositaries.²⁹ The depository is appointed by the management of the legal person, and a register of shares must be kept by the depository. The transfer of shares without update to the register does not have any legal effect, and all shares that have not been registered by February 2016 must be cancelled, and their value deposited with the Treasury's *Caisse de Consignation*. The resulting capital reduction amounted to approximately €1.4 billion being deposited in the *Caisse de Consignation*. The number and value of shares immobilized with a depository are not known. As a mean to verify whether the requirements of the 2014 law have been effectively implemented, the Direct Tax Administration and the *Administration de l'Enregistrement et des Domaines* will seek additional information on bearer shares. Sanctions for non-compliance with the requirements of the 2014 law are fines ranging from €5,000 to €125,000.

D. Conclusions and Recommendations

37. Important progress has been made to increase the transparency of Luxembourg legal persons and swift action was taken to assess concerns of misuse by Luxembourg banks of potentially opaque foreign structures. The steps taken to increase the transparency of legal persons, and the dematerialization of all bearer shares in particular, are encouraging. Similarly, the CSSF is to be commended for its approach in seeking to identify potential instances of use of opaque offshore structures, especially as the sector is assessed against today's norms and legal framework. Going forward, the authorities are encouraged to:

- Finalize the CSSF targeted supervisory program related to the Panama Papers and take necessary mitigating and enforcement action that the review may call for.
- Consider measures to facilitate access to beneficial ownership and control information by financial institutions and DNFBPs. In this respect the implementation of the relevant 4AMLD/5AMLD provisions may be useful, including to ensure the availability of beneficial ownership information of legal persons and arrangements established in Luxembourg and that are not customers of a financial institution or DNFBP in Luxembourg.

²⁹ Pursuant to Article 2 of the law of July 28, 2014, only the following professionals can be appointed as depositaries: credit institutions; private portfolio managers; distributors of units/shares in UCIs; specialized professionals of the financial sector (PFS), authorized as Family Office, as corporate domiciliation agent, as professional providing company incorporation and management services, as registrar agent or as professional depository of financial instruments; *avocats à la Cour* (attorneys-at-law) included in list I and European lawyers pursuing their professional activities under their original professional title included in list IV of the list of lawyers referred to in Article 8(3) of the law of August 10, 1991, on the legal profession, as amended; notaries; *réviseurs d'entreprises* (statutory auditors) and *réviseurs d'entreprises agréés* (approved statutory auditors); chartered accountants.

DETECTION AND EXCHANGE OF FINANCIAL INTELLIGENCE RELATED TO NONRESIDENTS

A. Introduction

38. The detection and exchange of financial intelligence related to nonresidents is key to small jurisdictions like Luxembourg with low domestic crime rates and large regional or global financial centers. The ability for financial institutions to detect potential misuse of the financial sector by nonresidents is a critical element of an effective AML/CFT framework. To that end, it is important that information on suspicious transactions performed by nonresidents be spontaneously exchanged with relevant foreign FIUs. The 2010 FATF MER pointed to serious shortcomings with regard to the detection of potential misuse, with existing requirements related to CDD, reporting of suspicious transactions to the FIU and supervision rated as partially compliant. Concerns about the lack of effectiveness of the system were raised in 2010 on the basis of the low number of cases giving rise to ML investigation, prosecution and conviction. Luxembourg's follow-up reports to the FATF indicate that significant progress has since been made with regard to the legal framework, but they do not enable one to form a view on the implementation of the revised legal framework, particularly due to the lack of sufficient information related to the conduct of onsite AML/CFT supervision.

B. Detection by Reporting Entities

39. The number of reported of STRs has significantly increased in recent years. The vast majority of STRs are filed by the professionals in the financial sector (approximately 96 percent in 2013, 97 percent in 2014, and 98 percent in 2015). The last two years saw a considerable increase in the number of STRs filed by electronic money/payment institutions (i.e., those active in e-commerce): in 2015, they filed approx. 57 percent of the STRs emanating from financial institutions, while banks filed some 37 percent. According to the FIU, the vast majority of STRs filed by e-money/payment institutions pertain to very low amounts (e.g., €0,99 for mobile applications), while STRs filed by banks typically involved larger amounts. In 2015, a large portion of the persons included in the STRs originated from Luxembourg or neighboring countries (France 14 percent, Luxembourg 9 percent, Belgium 6 percent, and Germany 4 percent). As far as country of residence is concerned, the largest group of persons resided in Luxembourg (27 percent), followed by France (9 percent), Belgium (5 percent) and Germany (4 percent), with the remaining persons residing in many other countries. According to the FIU's analysis, 82 percent of the STRs analyzed in 2015 potentially pertained to falsification (e.g., of documents) and fraud. They reflect an increasing trend of "CEO fraud"³⁰ and falsified banking instructions. The NRA is expected to establish whether the recent trends in reporting are in line with Luxembourg's risk profile.

³⁰ *Escroquerie au président*, which includes, for example, persons posing as an employee's superior to order transfers of funds.

C. Exchange of Financial Intelligence Regarding Nonresidents

40. Similarly, the number of information exchanges between the Luxembourg's FIU and other countries has generally increased over the past few years. Whereas the number of information exchanges in 2014 was lower than in 2013, there was a significant increase in 2015 compared to 2013. Most of Luxembourg's requests for information and spontaneous exchanges were with the United Kingdom, Germany, Italy, France, the United States, and Spain (each more than 500 transmissions). Luxembourg's FIU received most requests from France, Belgium, Italy, the Netherlands, the United Kingdom, Germany, and the United States (each more than ten requests).

41. The number of reports submitted to other jurisdictions by Luxembourg far exceeds the number of requests received by Luxembourg. The number of exchanges with the United Kingdom's FIU, in particular, was four times greater in 2015 than in 2013. This is mainly, but not only, due to the fact that Luxembourg forwards STRs that are reported by e-commerce businesses based in Luxembourg to the relevant FIUs of the country where the actual business took place.³¹ It is the policy of the FIU to spontaneously share these STRs or analysis with the concerned countries, without specifically asking for feedback in all cases (in order not to burden the other FIU). In some cases, the Luxembourg FIU has received positive feedback from other countries. Interviewed financial sector professionals also noted receiving follow-up information requests from third countries on STRs that they had reported to the Luxembourg FIU, and that apparently had been shared with foreign jurisdictions. This suggests that the information that is shared by Luxembourg with foreign partners is being used and is helpful.

42. In light of the increased workload, the FIU's resources have increased over the last years, but may nevertheless be overstretched in the near future. The FIU currently has a staff of 15, including its director, three magistrates, five analysts, five administrative assistants, and one IT expert. Nevertheless, some of the feedback received from reporting entities suggests that the FIU's staff resources may come under pressure, especially if the number of STRs increases significantly as a result of the inclusion of tax crimes as predicate offenses to ML. The authorities should remain vigilant and continue to reflect on the staff budget of the FIU, which is key to its long term effectiveness.

43. The authorities are also working on an update of the FIU Law, which will extend the FIU's information exchange capabilities with its EU counterparts. Although, in practice, the FIU is already able to exchange information as required, the proposed additional clarification in the law is welcome.

³¹ An example of this would be a payment for goods by a customer in a third country on a market place based in Luxembourg. Whereas the e-payment provider for the market place will have to report any STR related to that transaction to the Luxembourg FIU, the Luxembourg FIU promptly copies the STR to the FIU of the third country where the customer is based. This is very efficient.

D. Conclusions and Recommendations

44. Going forward, the authorities should:

- Finalize the update to the FIU Law regarding international cooperation in line with the current FATF Recommendations.
- Monitor the resources of the FIU and ensure that they remain commensurate with the workload.
- Ensure that the NRA establishes whether the current reporting trends are in line with Luxembourg's risk profile and, if necessary, take appropriate mitigating action.

AML/CFT SUPERVISION OF BANKS, TCSPS, AND LAWYERS

A. Supervision of Banks and TCSPS

45. AML/CFT supervision is improving. The FATF evaluation highlighted important deficiencies in the AML/CFT supervisory framework, as well as in the number and quality of AML/CFT inspections. The 2014 follow-up report indicates, however, that good progress has been made since then.

46. Over the past years, the CSSF has significantly increased the resources for AML/CFT supervision of banks and TCSPs under its purview. The CSSF supervisory department now has a staff of 84 employees (compared to 72 in early 2016) for 142 banks, 23 employees for 109 investment firms, and 13 employees for 125 TCSPs. Within the on-site inspections department, 13 staff are dedicated to AML/CFT (compared to 9 in early 2016).

47. The number and duration of AML/CFT on-site inspections are also increasing, but challenges may remain. The supervision department uses multiple sources of information for its surveillance work, such as reports from banks, on-site visits, self-assessment questionnaires, information from other authorities and foreign partners, and open source information. The duration of the CSSF onsite inspections has increased and ranges from several days to several weeks.³² Over the past three years, the number of onsites dipped, before picking up again. The AML/CFT on-site inspection program for 2012–2015 covered an average of 12.5 banks inspected onsite per year, and 9 investment firms, 14 TCSPs, and 3.5 other supervised entities (such as e-money institutions and management companies). These averages appear low relative to the overall number of entities.³³

³² It is worth mentioning that onsite inspection days do not include the drafting of the CSSF report, which is done offsite.

³³ For 2012: 17 Banks, 8 Investment Firms, 12 professionals of the financial sector (PSFs), 1 e-money institution, 4 SICAR, and 3 management companies; For 2013: 9 Banks, 13 Investment Firms, 18 PSF's, 1 risk capital investment

This view was shared by some supervised entities, which, although they considered the CSSF's AML/CFT supervision to be helpful, nevertheless suggested that it should be intensified, with more frequent on-site inspections for all entities (including themselves).

48. Detected irregularities are addressed through a range of remedial actions. These include administrative fines, reprimands, supervisory imposition of business restrictions, letters, and follow-up inspections, and fit and proper measures. Sanctions have been issued for issues related to CDD, record keeping, high-risk customers, targeted sanctions programs, and internal controls.

49. In 2016, CSSF re-assessed the ML/TF risks of banks and other professionals of the financial sector under its purview to guide its 2017 onsite supervisory work. All banks and TCSPs (as supervised by CSSF) are classified according to their level of ML/TF risks (low risk, medium-low risk, medium-high risk, and high risk) pursuant to five risk criteria. The determining factor for a high risk qualification, compared to medium-high risk, is the detection of significant AML/CFT shortcomings during inspections. The majority of banks and TCSPs are classified as low or medium-low risk. Five percent of banks and 0.8 percent of TCSPs are defined as high risk. The risk classification is based on a 2010 internal circular, as updated. It was undertaken for the first time in 2015 and the authorities mentioned their intention to improve and refine it further going forward, notably on the basis of the findings of the NRA.

50. TCSPs include a range of different professions, subject to AML/CFT supervision or monitoring by different authorities or self-regulatory bodies (SRB), as shown in the table below. The respective roles of the CAA, Order of accountants and tax administration were mentioned after the team's onsite visit and could therefore not be discussed.

51. The intensity of the AML/CFT oversight of TCSPs varies greatly across supervisors. Supervision by the CSSF appears more comprehensive than the LBA's monitoring (described below). The extent of the AML/CFT supervisory program of the tax administration and of the Order of accountants is unclear and could not be analyzed. There appears to be limited dialogue between the competent authorities, for example on the risks that the TCSP sector faces, and limited general overview of the sector as a whole.

company (SICAR), and 1 undertaking for collective investment (OPC); For 2014: 14 Banks, 12 Investment Firms, 12 PSF's and 1 e-money institution; For 2015: 10 Banks, 2 Investment Firms, 13 PSF's, 1 payment institution, and 2 management companies.

Businesses and professions that may act as TCSPs	Designated AML/CFT supervisory authorities or SRB
Banks	CSSF
Other "professionals of the financial sector"	CSSF
Lawyers	Bar Associations
Insurance companies	CAA
Accountants ("Experts comptables")	<i>Ordre des experts comptables</i> – Order of accountants
Real estate agents	<i>Administration de l'Enregistrement et des Domaines</i> (one of the three tax administrations in Luxembourg)
Other professionals acting as TCSPs	<i>Administration de l'Enregistrement et des Domaines</i>

B. Supervision of Lawyers

52. Most of the lawyers that are relevant from an AML/CFT perspective in Luxembourg's context are monitored by the Luxembourg Bar Association (LBA). Lawyers in Luxembourg are monitored by two Bar Associations, namely the LBA (which counts approximately 2400 to 2500 members) and the Bar Association of Diekirch (which counts approximately 30 members). Both associations are recognized as SRBs and entrusted with AML/CFT functions. In instances of failure to comply with AML/CFT requirements, they may issue fines, reprimands, and injunction letters, or conduct follow-up inspections. The vast majority of lawyers who perform the activities subject to AML/CFT measures under the FATF standard are located in the city of Luxembourg and registered with the LBA. For these reasons, the mission focused on the lawyers in the city of Luxembourg and on the LBA.

53. Since 2010, the LBA has strengthened its AML/CFT monitoring of lawyers. It notably issued several Circular Letters and Internal Regulations which contain requirements related to AML/CFT, and created, in 2011, an AML/CFT Committee (initially consisting of four lawyers and now expanded to five lawyers and one compliance officer), that undertakes on-site inspections. Of the approximately 2,400 to 2,500 lawyers accredited to the LBA, 450 have been inspected in 2012/2013, 116 in 2013/2014, and 150 in 2014/2015. These 716 lawyers work in 37 law firms. According to the LBA, an average inspection visit takes about two to three hours.

54. The inspections conducted between 2012 and 2015 have not detected significant failures by lawyers or law firms that would require AML/CFT sanctions to be imposed. The LBA nevertheless noted areas for further improvements. It has therefore provided advice to lawyers as to how to improve their level of compliance with their AML/CFT obligations. No examples of the practical areas of improvement detected were provided.

55. Lawyers in Luxembourg have been filing an increasing, but still low number of STRs. Luxembourg imposed AML/CFT measures on lawyers in November 2004 following the 2AMLD. The number of STRs filed ranges from 17 in 2012/2013 to 27 per year in 2015/2016. The filing of STRs have may have benefited from a range of supporting documents that the LBA issued in 2012, and which included a standardized client check list, a customer form, an identification form, and a transaction details form, among others, but is still low compared to the number of lawyers.

C. Conclusions and Recommendations

56. AML/CFT supervision has been strengthened with respect to banks, TCSPs subject to the CSSF's view, and lawyers, but challenges to ensure it is commensurate with the ML/TF risks faced by these sectors remain. The CSSF's efforts to classify banks and TCPS under its purview according to their respective risk is to be commended. It is not clear, however, to what extent the risk assessments conducted were driven by existing resources, rather than by the actual risks, and current resources may prove inadequate if the NRA identifies higher risks in the banking and TCSP sector. Monitoring by the LBA has also increased but remains relatively weak, which, given the lawyers' key role as gatekeepers, could constitute an important vulnerability in Luxembourg's AML/CFT framework. The limited time devoted to supervision and inspections tend to indicate that supervision is superficial. In these circumstances, it is unclear whether the lack of sanctions is appropriate. Furthermore, the numbers of LBA accredited lawyers is growing by about 10 percent per year. This poses future challenges for the workload of the AML/CFT Committee.

57. Going forward, the authorities should:

- Further increase intensity (i.e., frequency and depth) of AML/CFT monitoring of lawyers by the Bar Association.
- Ensure that sufficient resources are available for risk-based AML/CFT supervision of banks and TCSPs in light of the findings of the NRA to allow the intensity of supervision to increase.
- If necessary, align the current risk classification of banks and TCSPs in light of the findings of the NRA.