Anti-Money Laundering Services

Luxembourg AML Survey 2020

Executive Summary

Introduction

As the world continues to respond to the COVID-19 pandemic, criminals around the world are taking advantage of the situation, finding new ways to generate illicit funds.[1] As such, the fight against Money Laundering and Terrorist Financing (ML/TF) remains more important than ever.

The year 2020 saw a wide range of emerging ML/TF risks on a global scale, including government and private sectors' abilities to implement Anti-Money Laundering and Counter Terrorist Financing (AML/CTF) obligations from supervision, regulation and policy reform to suspicious transaction reporting and international cooperation.[2]

Both pre- and post-COVID-19, AML/CTF related matters continue to be amongst the top priorities for Luxembourg regulators as well as for European and international authorities.

From a Luxembourg perspective, there is not only the ongoing country assessment of the Financial Action Task Force (FATF), but also the implementation of certain key regulations and laws in 2020, such as the transposition of the 5th European Union (EU) AML Directive into local law.

About the 2020 AML survey

Considering the various AML/CTF challenges faced by our clients, both as a result of the COVID-19 pandemic and beyond, PwC launched the first dedicated AML/CTF Survey in order to analyse and portray the current state of play of the Luxembourg market regarding the setup and implementation status that exists across the different key areas of AML/CTF requirements.

Our report attempts to highlight the key challenges faced by the various industries in terms of AML/CTF compliance, whilst providing an industry-wide benchmarking standard for clients to measure themselves against in future.

Our survey and report has been developed and prepared by our core team of AML/CTF industry experts:

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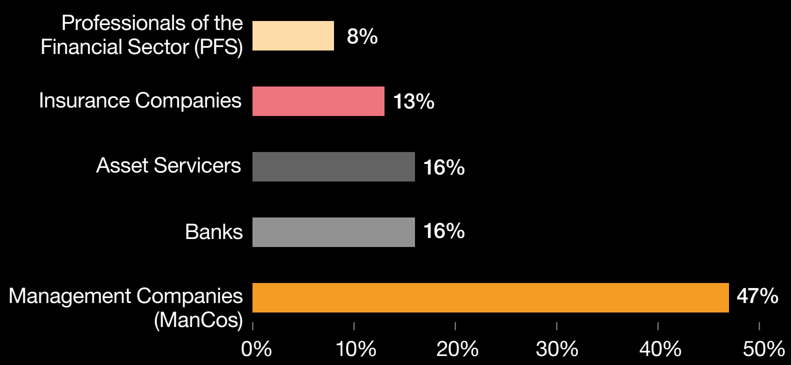
1. EUROPOL, Pandemic profiteering – How criminals exploit the COVID-19 crisis, 2020
2. FATF, COVID-19-related Money Laundering and Terrorist Financing Risks and Policy Responses, 2020

Our sample

PwC collected answers from 131 respondents over a two-month period between November and December 2020, with the majority of our respondents comprised of organisations in the Asset Management, Banking and Asset Servicing industries.

The respondents are divided into the following five main categories based on their industry type:



The positions of the respondents to the survey represented mainly senior representatives from functions like Compliance, Internal Audit, Management and Boards. The five main categories are made up of the following sub-categories:

ManCos/Funds	Asset Servicers	Banks	PFS	Insurance Companies
ManCos (IFM)	Custodian Banks	Board member (Bank)	Domiciliation Agent or Incorporation Services Provider (PFS)	Insurance Company (Life)
ManCos (AIFM)	Transfer Agents	Retail Bank	Investment Firm (PFS)	Insurance Company (Non-Life)
"Super ManCos" (respondents who answered both ManCos (IFM) and ManCos (AIFM)		Private Bank	Support PFS	Insurance company (Captive)
Other investment fund manager		Corporate Bank		Insurance Broker
Family office		E-money institutions		
Board member (investment fund)		Payment institutions		

The respondents are all based in Luxembourg.

Breakdown of survey areas

The survey is divided into the following key areas of interest:

1. AML/CTF environment overview
2. AML Governance
3. Risk-Based Approach (RBA), Risk Assessment and Risk Appetite
4. Due Diligence
5. Transaction Monitoring (TM) and Screening
6. Information/ Data quality and mapping
7. Outsourcing

Executive Summary

AML/CTF is at the top of the regulatory agenda in Luxembourg. In 2020, Luxembourg implemented a series of updates to its legal framework. Our survey's objective was to better understand the current AML/CTF landscape in Luxembourg in order to analyse the state of play around these topics. Our respondents represented a wide range of industries represented by ManCos (47%), Banks (16%), Asset Servicers (16%), Insurance Companies (13%) and PFS (8%).

Luxembourg actors are **very confident about the level of their AML/CTF compliance frameworks** since 89% of respondents rated themselves largely or fully confident with their level of compliance.

AML challenges keeping the financial sector busy: 1) Increased regulatory pressure, 2) Maintaining Know Your Customer (KYC) up-to-date and 3) Manual processes in the wider AML/CTF context. The top three rank at the top in almost each sector, closely followed by and data quality/management.

On the **investment side,** a clear trend concerns Automatisation/digitalisation, Data clean-ups and Customer Due Diligence (CDD) improvements. It is fair to assume that the three are mostly interdependent and digitalisation plays a key role, but it also shows that so far there was likely more talking about it then walking the talk. So **Tech is supposed to get more traction** looking forward, which is not surprising given the fact that this area was less focused on it in the past.

When looking at **cost implications** of AML/CTF, **85% of respondents report an increase of one-third or more of their AML related costs** over the last three years. All this clearly demonstrates the implications of a fast moving regulatory landscape, but it is worth referring to the often-cited statement of former US attorney McNulty "If you think compliance is expensive, try non-compliance".

Strong AML governance needs awareness and the level of awareness about the importance of AML/CTF is crucial for its success. It is reassuring that awareness is very high at the level of Senior Management and Control functions, **demonstrating a strong "tone from the top"**, since the Board of Directors (BoD) also score very high. Respondents consider that outsourcing may not foster such awareness within their own organisation, and will likely act with high level of care for that reason.

"Risk comes from not knowing what you are doing" (W. Buffet): The **AML Risk Assessment is** one of the key pillars of an AML/CTF framework and **well established in Luxembourg** and all respondents. It has a direct impact on regular updates of policies and procedures and the CDD approach as the vast majority of respondents confirmed.

The **Risk Appetite Statement (RAS)** is the newer sibling in the AML Risk family and 59% of all respondents have already formally implemented it. The definition of the RAS is largely driven by the Senior Management, Control Functions and the BoD being the ultimate responsible.

Customer due diligence – the core pillar of AML/CTF: **Luxembourg is traditionally strong** in due diligence and beneficial ownership identification, but also complementing factors like source of wealth information is reviewed diligently like the vast majority of respondents confirmed. Everybody properly documents beneficial ownership and the source of wealth according to our repsondents.

Tax compliance is center-stage for AML/CTF since four years now and systematically tackled by all respondents with a variety of combined measures: 62% request signed statements from clients about their tax compliance, followed by dedicated onboarding checks based on risk-criteria (46%). Banks and Asset Servicers are deliberately focused on leveraging in-house tax specialists for deeper assessments and obtaining formal tax specialist assessments.

Hot topics

"The recent past has seen a lot of new developments and trends in the technology field and in the options available to transform and digitalise the AML/CTF environment. An interesting result of the survey is that the real application and implementation of Tech is not yet very advanced but a clear investment target. One still sees a lot of traditional solutions and the much-hyped Artificial Intelligence is more and more available with strong propositions. However, the level of usage remains so far relatively low, not the least due to legacy environments and still paper-based information sources. In addition to the KYC aspect, TM and sanction screening are other fields of development where room for efficiency – and even more so – effectiveness could be leveraged by smart approaches supported by the right IT solution. This is because these are typical areas where heavy-lifting is required to cope with backlogs, look-backs or simply regular review cycles."

Michael Weis

Oversight or trust is good, control is better: The respondents who work in Asset Management indicated a broad array of subjects that they cover as part of their oversight process of service providers. The assessment of the RBA (87%), tax crimes (64%), KYC (71%), screening (92%) and suspicious TM and reporting (69%) are core elements of the oversight process. The percentages shown here are for ManCos only, but the answers have to be seen in perspective as the model between Asset Managers, ManCos and Transfer Agents are split. Service contracts may be in place where one actor provides the services to the other. Overall though the answers seem to indicate that - in this fragmented value chain set up - **every player, given this context, is carefully evaluating wether all of these oversight topics are properly covered** in order to comply with their own AML/CTF regulatory duties. 35% of respondents ensure that AML procedures in force at delegate level are equivalent to those applied in their organisations through the use of dedicated controls, performed on a regular basis and 24% perform on site visits. Nearly half of the respondents stated that they monitor the AML framework in place at intermediary level on an annual basis, but RBAs also allow other frequencies to be applied.

A **hot topic** is currently the risk scoring of assets and the screening of assets against blacklists. Regarding AML/CTF **risk scores, for each asset in their portfolio, a mixed picture still exists** where a slight majority of IFM respondents answered no and a slight majority of AIFM answered yes. The requirement to score assets and perform appropriate AML/CTF due diligence was recently introduced formally in CSSF Regulation 12-02, as amended in August 2020 and still seems to be under preparation by half of the players. When it comes to **"blacklist" screening of such assets, this is already widely adopted**, although not necessarily on a daily basis but more on a monthly or quarterly schedule in many cases.

Transaction Monitoring – a complex challenge finding the right mix between tools, scenarios, cost and operations. There is no clear and predominant set up since the spectrum spans from external supplier over internally developed to manual approaches. This is acceptable according to the regulations under certain conditions and the size of the organisation, but a growing trend to more automated system solutions should be expected with growing regulatory focus in this area, nationally and internationally. **System costs and value for money** are the two most prominent **challenges**, followed closely by resourcing of **skilled staff** and **false-positive numbers** of alerts.

When looking at the **"blacklist screening"** of clients, an overall 77% of respondents perform name screening on **a daily basis** through automatic batch screening processes and the daily approach is more or less the rule among Banks and Asset Servicers.

The devil is in the data (and the detail): Data and information storage has become an increasing concern for organisations, in particular during COVID-19 times where home-based working becoming the "new normal". A slight majority of respondents store their AML/CTF documentation electronically, followed closely by a **mix of paper-based and electronically.** KYC data is often unstructured and distributed across various media or systems, and this is not facilitating the use of technology.

Outsourcing - no pain, no gain: AML/CTF related processes are an often-debated topic for outsourcing. When looking at our results it seems to have **clear value in certain contexts but is also not the "silver bullet" it is often referred to as.** The biggest appetite seems to be around periodic KYC reviews and screenings both scoring at 2.6 on a range of 1 (very helpful) to 5 (not helpful). Regular KYC onboarding scores surprisingly low at 3. The largest appeal of outsourcing seems to be among ManCos, Insurance Companies and PFS, but still at a very modest level, since only ManCos rated Screening at 2.3, whereas all other sectors and topics were still rated at 2.5 or below. Instead of outsourcing their activities, **many respondents in Luxembourg are moving towards strategic investment in AML/CTF resources in-house**, demonstrating the importance and critical nature of the subject matter to most. When asked how they forecast the evolution of their AML/KYC team, more than half of the respondents forecast that the size of their AML/CTF team will increase.

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