

The Fifth Money Laundering Directive (MLD5)

Its meaning and significance

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“We need open, competitive, market economies... but at the same time with effective regulation and supervision”

Jose Manuel Barroso, Former President of the European Commission



Preface

The ink is not yet dry on the Fourth Money Laundering Directive (MLD4) as the European Commission is already pushing the EU member states to prepare for the Fifth Money Laundering Directive (MLD5).

The terror attacks in Brussels and Paris were a major game changer. Another even more pressing issue for lawmakers was the large scale tax evasion scandal known as the Panama Papers. To tackle terrorism funding and tax evasion alike, the European Commission amended the Fourth Money Laundering Directive even before its effective implementation by all member states.

The aim of the MLD5 is to provide an action plan against terrorism financing and tax evasion, as well as strengthening transparency.

The new regulative paper promises even tighter rules for financial institutions and related entities. An increasing number of companies are coming under tremendous pressure to properly identify the beneficial owners of funds accepted while doing business. Non-compliance with the requirements set forth in the Directives is not an option. For companies failing to live up to expectations, lawmakers are enforcing drastic penalties.

What does this mean for your company? Do you need to prepare for even tighter regulations? This white paper aims to provide you with an overview of the latest developments in the EU's regulatory fight against Money Laundering.

“Our findings show that the schemes revealed by the Panama Papers directly reduce the funds available to national authorities... there is likely to be a revenue loss of approximately EUR 19 billion in our sample of eight EU Member States alone. If this estimate is scaled up, this suggests a cost of the schemes to the EU28 in the range of EUR 109 billion – 237 billion.”

“The Impact of Schemes revealed by the Panama Papers on the Economy and Finances of a Sample of Member States”, Study for the PANA Committee, European Parliament.



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The Fourth Money Laundering Directive at a Glance

In the EU, financial institutions, related companies and other obliged entities are bracing for the Fourth Money Laundering Directive (MLD4), which EU member states must implement by 26 June 2017. In a previous white paper we outlined what the MLD4 means for your business in and with the EU and the effect it will likely have on Swiss operated businesses.

The MLD4 (or Directive EU 2015/849) seeks to strengthen regimes against money laundering and terrorist financing across the European Union, while also ensuring that the EU framework matches the recommendations of the OECD's Financial Action Task Force (FATF).

In addition, the MLD4 requires more transparency regarding beneficial owners and seeks severe penalties against entities failing to comply.

Beneficial Owner Register

The Fourth Money Laundering Directive requires EU member states to use a central register to provide information on beneficial ownership of corporate and other legal entities. Member states can make this register public or, at minimum, ensure that law enforcement authorities, obliged entities (for Customer Due Diligence purposes), and others with "legitimate interest" have access to such information.

Companies should obtain and present adequate, accurate and current information on their beneficial owners. The storing of said information does not relieve a company of its Customer Due Diligence obligations under the law.

Penalties

Lawmakers have defined heavy sanctions for those business entities failing to comply with the MLD4. The most severe financial penalties that could be levied for non-compliance include fines of up to at least EUR 5 million, or 10 percent of the annual turnover-enough to send some companies into bankruptcy.



The path to the Fifth Money Laundering Directive (MLD5)

With the Fifth Money Laundering Directive (MLD5), the European Commission aims to further reinforce the Anti-Money Laundering regulation to counter terrorism financing and further increase transparency regarding Beneficial Ownership.

The MLD5 was hastily drafted and proposed on 5 July 2016, one year before EU member states would implement the MLD4. Why the hurry? The MLD5 is a direct response by the European Commission to the terror attacks in Brussels (March 2016) and Paris (November 2015), and to a series of tax evasion scandals, notably the Panama Papers leak. More than 11 Million documents from the law firm Mossack Fonseca were leaked, revealing how individuals and companies avoided taxes and laundered money through offshore structures.

An Action Plan against terrorist financing

On 2 February 2016, the European Commission adopted an Action Plan on urgent measures against terrorist financing. The commission announced a wide range of measures to avoid the misuse of EU financial systems, to

cut terrorists off from their sources of revenue, and to trace terrorists' financial activities. Enhancing the effectiveness of sanctions and freezing assets within the EU and third countries are among the main priorities, as stated by the European Commission in a press release ([http://europa.eu/rapid/press-release - MEMO-16-2594_en.htm](http://europa.eu/rapid/press-release_MEMO-16-2594_en.htm)).

The Commission adopted on 5 July 2016 a proposal to further reinforce EU rules on anti-money laundering, counter terrorist financing, and increasing transparency of company and trust ownership. Nine days later, the European Commission also formally adopted a list of third countries "having strategic deficiencies in their regimes on anti-money laundering and countering terrorist financing".

Banks will now have to carry out additional checks ("enhanced due diligence measures") on financial flows from eleven "Risk" countries. Furthermore, the EU is planning targeted technical assistance to third countries in order to enhance their capacity to counter terrorist financing and improve anti-money laundering measures.



Tackling tax evasion

Following the publication of the Panama Papers Leak, the European Parliament's Committee of Inquiry to investigate alleged contraventions and maladministration in the application of Union law in relation to money laundering, tax avoidance and tax evasion (PANA Committee) requested a study to assess the impact of the schemes revealed in the Panama Papers.

The most significant impacts identified are the negative effects on Member States' budgets, with wider knock-on effects on economic growth and financial markets, states the report (http://www.europarl.europa.eu/cmsdata/116947/20170412_panama_papers_study_final.pdf).

"There is likely to be a revenue loss of approximately EUR 19 billion in our sample of eight EU Member States alone. If this estimate is scaled up, this suggests a cost of the schemes to the EU28 in the range of EUR 109 billion – 237 billion (inclusive of the Panama Papers and other schemes like it)".

Therefore, the authors of the study recommend:

- ◆ Promoting the establishment of registers that publicize beneficial ownership to prevent schemes revealed by the Panama Papers from remaining undetected.
- ◆ Encouraging higher tax good governance standards by ensuring that the EU's international partners implement higher standards. The EU itself must intensify its pressure in the global fora – particularly the G20 – to achieve this.
- ◆ The idea that only non-cooperative jurisdictions qualify as tax havens disregards that some jurisdictions may only appear cooperative while operatively remaining a tax haven. In the interest of neutrality, a grey-list or black-list should be established based on more nuanced criteria.
- ◆ Introducing measures to guarantee the protection of whistleblowers - this will improve the availability of the data and act as a driver against the use of tax haven schemes.
- ◆ Developing methodologies that can be used to generate publicly available, reliable and comparable data on the magnitude of tax avoidance and evasion, and methods of quantifying the impact of these incidents on countries' public finances and economic activities. This would mean exploring data collection methods on corporate tax avoidance and evasion, on which most research seems to focus to date, in addition to tax evasion by individuals.
- ◆ Promoting integrity and transparency in the financial sector within the framework of the European Semester. In more concrete terms this could translate into the EU monitoring and preventing the use of Panama Papers schemes, which could jeopardize macroeconomic stability (i.e. linked to real estate bubbles, banking crises, etc.), and fostering adjustment by means of appropriate policies.



What is new with the MLD5?

The aim of the MLD5 is to trace terrorists' financial movements and prevent them from moving funds or other assets by limiting the anonymity of transactions, particularly targeting virtual currencies such as bitcoins and prepaid cards, and enhancing the role of Financial Intelligence Units in bank and payment account registers and increased involvement with high risk third countries.

The other aim of the MLD5 is enhancing transparency of beneficial ownership information through the provision of clearer rules on the nature of and access to information (Proposal for a Directive amending Directive 2015/849, European Commission: <http://www.eesc.europa.eu/resources/docs/presentation-eesc-160916.pdf>).

Terrorist financing

To tackle terrorist financing, the European Commission proposes the following amendments to the MLD4:

- ◆ Virtual currency exchanges and custodian wallet providers shall be subject to the

same Anti-Money Laundering requirements as the obliged entities outlined in the MLD4. Customer Due Diligence measures would therefore apply for the above mentioned providers as well.

- ◆ Lower thresholds for identifying the holders of anonymous pre-paid instruments like prepaid cards from EUR 250 to EUR 150. There shall be no Customer Due Diligence exemption for the online use of prepaid cards.
- ◆ Enhance the power of Financial Intelligence Units (FIUs). FIUs shall have access to information from any obliged entity in centralized bank and payment account registers enabling them to identify account holders.
- ◆ Enhanced Customer Due Diligence towards high risk third countries. The European Commission has created a list of non-EU countries with deficiencies in their AML measures. The list is still under discussion among EU members.



Beneficial ownership

In order to tackle tax avoidance and money laundering, the MLD5 introduces the following measures:

- ◆ Full public access to beneficial ownership registers. Information about the ownership of companies and trusts involved in business-like activities shall be made public.
- ◆ For non-profit trusts, the information will only be available to those with a “legitimate interest”.
- ◆ EU-wide access to beneficial ownership information. Direct interconnection of the central registers of the EU member states to facilitate cooperation between them.
- ◆ The threshold for disclosure of beneficial owners of entities with a special risk of being used for money laundering and tax evasion is lowered to a stake of 10%. For all other entities, the threshold remains at 25% as required by the MLD4.
- ◆ Systematic monitoring of existing customers when they present a specific risk.



Members of Parliament disagree on list of high-risk third countries

The European Commission produced an inventory of countries thought to present risks of money laundering, tax evasion and terrorism financing. The Commission currently identifies eleven countries, including Afghanistan, Iraq, Bosnia and Herzegovina, and Syria, which it judges to be deficient in countering money laundering and terrorist financing.

People and legal entities from blacklisted countries face tougher than usual checks when doing business in the EU.

The European Economic and Social Committee (EESC) criticizes that the list of high-risk third countries, published on 14 July 2016, does not include many countries or jurisdictions which – on the basis of credible evidence

– are believed to be acting as tax havens for money laundering, including the 21 territories mentioned in the Panama Papers.

The EESC proposes that either a new list of high-risk third countries be drawn up, or the scope of the measures under Article 18a of 5AMLD be broadened.

The European Parliament already rejected a list drawn up last year as too limited. Members of the European Parliament state that the Commission should not be bound by the standards of the Financial Action Task Force on Money Laundering (FATF). They want the list to be more expansive. On 3 May 2017, the Parliament rejected the blacklist with 61 votes to 7 with 32 abstentions.



How to prepare for the MLD5?

The MLD4 aims to enhance corporate transparency through Member States having to establish central registers containing current information on the beneficial ownership of corporate and legal entities. The companies under the jurisdiction of a Member State should obtain and hold adequate, accurate and current information on their beneficial ownership.

The information contained in the registers shall be made available in all cases to competent authorities and financial intelligence units and

to those entities subject to the directive undertaking due diligence under the MLD4 framework. This information shall also be made available to any person or organisation able to demonstrate a “legitimate interest”.

However, the storing of beneficial ownership information shall not relieve obliged entities of their customer due diligence (CDD) obligations, which they will be required to continue to fulfill using a risk-based approach.

What happens next?

The Fifth Money Laundering Directive is under review. Discussions have been postponed to June 2017. However, obliged entities should be poised to implement the MLD5. Once approved and published in the Official Journal of the European Union, member states are expected to implement the MLD after a short period of six months.

If your company is affected, it is more vital than ever to be prepared for the tougher Customer Due Diligence requirements of the

MLD5. Choosing the right partner to assist you in all Customer Due Diligence related issues will prove necessary and cost effective in the long run.

“Collective European Union action could mean no hiding places for evaders, no safe haven for tax avoiders, and no treasure islands for money launderers.”

Gordon Brown, former UK Premier



Who are we

Through its state-of-the-art Due Diligence solutions, **Global Risk Profile** helps its clients to mitigate risks and comply with regulatory standards.

From simple screening to thorough investigations, our reports are effective means to **assess risks** associated with every kind of third party involved in your business model.

Based in Switzerland and mastering over twenty languages, our core team of experienced analysts, perform quality research **world-wide**.

Our network of local informants (i.e. former police or military force members, lawyers, private investigators and journalists) enables us to gather information from the target's immediate environment.

The Information you need

Risks may arise at any step of a business process.

We offer exhaustive checks on:

- ◆ Suppliers / Subcontractors / Distributors
- ◆ M&A and Joint-Ventures
- ◆ Existing and potential clients (**KYC reports**)
- ◆ Current staff and potential hires (**Background Checks**)
- ◆ Any other person / corporation of your interest

On demand, we also provide our clients with specific tailor-made services.

Get the Most out of the “Big Data”

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- ◆ Official Gazettes
- ◆ PEP Databases
- ◆ Sanction & Regulatory Enforcement lists
- ◆ Court files
- ◆ Media archives
- ◆ Proprietary Archives
- ◆ Local Search Engines
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