

National risk assessment of money laundering and terrorist financing

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FOREWORD

Luxembourg is an open and fast-growing economy within the European Union and one of the main financial centres globally. At the centre of Europe with a dynamic and multinational working population, Luxembourg is home to many European institutions. It has become one of the primary financial centres in Europe serving both, the domestic economy but also servicing the needs of other countries in a variety of international businesses such as private banking, insurance, asset management and payments. The Luxembourg Government is well aware that this success also brings with it exposure to the ever-growing and evolving threat of money laundering and terrorist financing (ML/TF) across the world.

Luxembourg has long been committed to fighting ML/TF activities and ensuring that the risks arising from and within its jurisdiction are mitigated. Luxembourg authorities are committed to upholding the international standards and best practices in this fight, and do so jointly with their international partners in regular cooperation as well as through international bodies and fora.

To this end, in the last five years Luxembourg has implemented a series of reforms in its legal framework and institutional set-up, keeping up pace with the evolving nature of the risks faced, the increased sophistication of illicit activities and its perpetrators, and the higher common international standards agreed with international peers. Today Luxembourg has a robust and pro-active regime for combating money laundering and terrorism financing (AML/CFT) across prevention, detection and prosecution activities, and the recovery of the proceeds of their crimes. This has translated into tangible results. In 2017, private sector entities reported about 39,000 suspicious transactions, supervisors undertook over 100 on-site inspections, enforced over 80 remedial actions, and the judiciary authorities convicted more than 230 persons for ML/TF and seized

more than 30 million euros of criminal assets.

The first National Risk Assessment (NRA) has been completed in 2018, and the Government is pleased to present a summary report here. This exercise was a major step forward in further enhancing a comprehensive and shared understanding of the inherent risks, the strengths of the current AML/CFT regime and in identifying areas where defences across all involved bodies could be developed further. The NRA was a joint and coordinated effort across the main stakeholders in the Luxembourg AML/CFT regime, including policy-makers, supervisors, self-regulatory bodies, judiciary authorities and law enforcement authorities. In addition, considerable input was received from private sector participants and representative bodies. The Luxembourg government extends its appreciation to all involved.

This work is a valuable tool for the national competent authorities and coordinating bodies, to better understand the ML/TF risks that the country is facing, and to support their own risk assessments and ongoing supervisory, detection and law enforcement activities.

The NRA is also informing future actions at both the policy makers and national authorities level to further strengthen the AML/CFT regime, in line with a risk-based approach.

As such, the NRA contributes to building a strong foundation to continuously improve the country's response to ML/TF risks while keeping Luxembourg the open, conducive environment for business it is today.

Pierre Gramegna, Minister of Finance

EXECUTIVE SUMMARY

INTRODUCTION

Luxembourg has long been committed to fighting ML/TF activities and ensuring that the risks arising from and within its jurisdiction are mitigated. For this purpose, it is also committed to developing a deeper understanding of its own risks and capabilities, in the face of growing and evolving ML/TF risks and in line with international guidance. Therefore, Luxembourg has undertaken its first NRA starting mid-2016 and ending in 2018 permitting to identify, assess and understand money laundering and terrorist financing risks. Luxembourg intends to use the NRA to further form and guide its risk based approach to supervision, to support the prioritisation and allocation of resources in line with the risks identified and to establish required actions.

The process gathered input of a wide set of national stakeholders including ministries, national supervisors and other authorities, self-regulatory bodies, professional

associations and private sector participants (a total of over 20 bodies). The exercise was conducted throughout the period 2016–2018 and compiles an assessment of Luxembourg's current situation as of year-end 2017.

Consistent with a risk-based approach, special consideration has been paid to the analysis of Luxembourg's risk exposure arising from its role as a global financial centre. This is particularly important, given that the financial sector is the country's largest sector (27% of gross value added and 11% of employment in 2017) with many foreign institutions, foreign-owned assets and a leading centre for a variety of international financial services businesses in the Eurozone.

This report summarises the NRA inherent risk results.

1. ASSESSMENT OF INHERENT RISK: APPROACH

The approach combines qualitative and quantitative information and professional expertise. Data was collected from a variety of international and national (public and private) sources, including international studies and reports (e.g. OECD, Eurostat, Europol, EU SNRA) annual reports (e.g. CSSF, CRF, CAA), statistics (e.g. STATEC) and non-publicly available data from the supervisory authorities and law enforcement authorities. This was complemented with expert opinion through regular high-level interactions with the concerned authorities and the private sector to enrich findings. In line with a conservative approach, assessment of risks was deemed higher where detailed statistics or knowledge was missing.

As part of this process, Luxembourg authorities established a risk ranking for each economic sector using a classification of risk ranging from “very low” to “very high”, reflecting commonly used practices. These ratings should be understood as an assessment of *relative* risk within Luxembourg. That is, a sector with a “very high” risk is considered more likely to be abused or misused for ML/TF than one with “medium” risk, within Luxembourg. The level of granularity and the scope of the risk assessment were discussed and agreed at the start of the assessment. The NRA exercise performed by Luxembourg takes a national perspective, to contribute to the understanding of the risks primarily at a country and sector levels; this supports strategy determination and resource allocation at the national level across various competent authorities and law enforcement authorities. Where appropriate a lower level of granularity was also applied for an assessment at a sub-sector level to support the same goals within each competent authority. As such, the assessment focuses

mostly on national competent authorities, self-regulatory bodies, law enforcement authorities and cross-agency committees, where applicable.

Inherent risks are defined as ML/TF risks before mitigating factors in place are considered. It is a function of threats¹ (i.e. crimes generating proceeds to be laundered or to finance terrorist activities) and vulnerabilities² (e.g. sectors most exposed to being exploited for ML/TF purposes). The inherent risks assessed stem from Luxembourg’s economy, openness, and other structural factors, including its role as a large financial centre. It reflects in part the economic model that has made Luxembourg an attractive country for legitimate businesses.

The inherent risk assessment was conducted assessing both threats and vulnerabilities in order to determine inherent risks per sector and sub-sector on a scale of one to five (or very low to very high). Under threats, ML and TF are assessed separately given the differing nature of offenses. For vulnerabilities, although the purpose and nature of ML and TF may be different, criminals often use similar techniques to move illicit money. Due to the commonality of the methods used, the vulnerabilities assessment addresses both the exposure to ML and TF without differentiation under its analysis.

1 A threat is a “person or group of people, object or activity with the potential to cause harm to, for example, the state, society, the economy, etc.”, *FATF Guidance on National Money Laundering and Terrorist Financing Risk Assessment*, February 2013.

2 Vulnerabilities are “those things that can be exploited by the threat or that may support or facilitate its activities”, *FATF Guidance on National Money Laundering and Terrorist Financing Risk Assessment*, February 2013.

1. Assessment of inherent risk: Approach

Threats were assessed along the 20 predicate offences in line with FATF crime categories³, which map to granular offences in Luxembourg law. Threats were assessed on a scale of one to five (very low, low, medium, high, and very high), against a scorecard of criteria using a combination of national and international data available complemented by expert judgement, as well as a workshop with all judicial authorities to validate outcomes. Criteria included likelihood (frequency of crimes), size and complexity (e.g. estimate of proceeds, cash vs. noncash forms) and consequences.

The exposure to these threats was considered separately for domestic and foreign offences based on the criteria and process referred. This is because of Luxembourg's significant financial centre and open economy make it more vulnerable to illicit flows from abroad. The overall threat assessment is based on a weighted average between domestic and foreign exposure, with 25% and 75% weights respectively⁴.

Vulnerabilities were assessed across sectors and sub-sectors that could be exploited for ML/TF. The set of sectors and sub-sectors chosen for the assessment was based on FATF's guidance as a starting point, but adapting to Luxembourg's reality based on supervisory set up (for instance, the securities sector in the assessment only includes the

Luxembourg Stock Exchange, while fund and asset managers and securities brokers are included in the investment sector). Additionally, some additional sectors not under scope of the 2004 AML/CFT Law are analysed for comprehensiveness (such as legal entities and arrangements, hotels, bars and restaurants).

Given the complexity, size and number of sectors the methodology employed involved two levels. In a first, macro-level, sector vulnerabilities were assessed based on an outside-in assessment with international datasets and a benchmarking model. In a second, meso-level, vulnerabilities were assessed at a more granular, sub-sector level, based on national and supervisor-specific data as well as discussions with each competent authority. This was based on defining a set of criteria that was common to all sub-sectors, including size, fragmentation of market, ownership/legal structure of entities, products/activities, clients and interaction channels. Quantitative data and qualitative information was gathered from national data sources (some public, some confidential) along the dimensions of the assessment criteria. The data and information gathered was translated into an informed vulnerability rating on a scale of one to five against each criterion (five representing the highest impact of vulnerability to ML/TF).

³ As per *FATF Recommendations* (Glossary), with some minor adaptations. The final list of predicate offences analysed was: Fraud and forgery; Illicit trafficking in narcotic drugs and psychotropic substances; Robbery or theft; Tax crimes; Corruption and bribery; Insider trading and market manipulation; Trafficking in human beings and migrant smuggling; Sexual exploitation, including sexual exploitation of children; Counterfeiting and piracy of products; Participation in an organised criminal group & racketeering; Smuggling; Illicit trafficking in stolen and other goods; Environmental crimes; Illicit arms trafficking; Extortion; Murder, grievous bodily injury; Kidnapping, illegal restraint, and hostage taking; Counterfeiting currency; Piracy; Terrorism and terrorist financing.

⁴ The domestic/foreign weighing was agreed to reflect an average perceived split across offences and sectors, based on expert judgement and data, where available (for instance, share of assets under management outside of Luxembourg in the financial sector).

2. INHERENT THREAT OF MONEY LAUNDERING AND TERRORISM FINANCING

Overall, the inherent ML/TF threat (i.e. before taking into account the controls currently in place) is primarily driven by the importance of Luxembourg's financial system with significant incoming and outgoing financial flows, as well as by Luxembourg's open and diverse economy. This section briefly described the ML and TF threats for Luxembourg.

Money laundering (domestic and foreign crimes)

Money laundering of foreign criminal proceeds is the highest threat for Luxembourg. The magnitude, diversity and openness of financial flows transiting through Luxembourg contribute to this exposure. This is supported by data from the judicial authorities, international studies and expert assessment from the country's authorities. Luxembourg is ranked 21 on the Global Financial Centres Index⁵ and has high financial flows in and out of the country, with and from different geographies. Luxembourg is rated to have a very large share (12%) of international financial services. However, the large financial flows relative to the size of the country, as depicted in several studies, should also be put into context with its central role for these services in the EU common market.

Given the magnitude of the financial sector and its share of foreign financial flows, the potential for proceeds of foreign crimes to be laundered in Luxembourg and the sophistication employed in money laundering are considered to be significant as well. International studies and guidance point towards criminal proceeds being often laundered in distant places from where crimes were perpetrated to try to conceal the origin of funds.⁶ Estimates are varied, but for example one study⁷ estimates that as much as ~30% of worldwide unlawful earnings are laundered cross-border, making countries with significant shares of foreign direct flows more vulnerable. In effect, ML of foreign crimes account for a significant share of Legal Assistance Requests (LAR⁸) and asset seizures by Luxembourg authorities. Across all crimes, the Prosecution authorities report having received a total of ~240 ML-related LAR on aggregate in the past three years of 2015–17 (out of a total of ~1500 LAR, or 15–17% of total in each of the 3 years).⁹

The most likely external threats for Luxembourg in terms of ML are believed to be: tax crimes; fraud and forgery; drug trafficking, corruption and bribery. In fact, these four offences represent over 70% of estimated criminal proceeds generated globally¹⁰, over 70% of seizures following LAR to the Prosecution authorities in 2015–2017¹¹, and over 60% of LAR received by the Prosecution authorities in 2015–2017¹². This is also in line with expert assessment from the country's authorities.

5 Z/Yen, *Global Financial Centres Index 23*, March 2018.

6 See for example: UNODC, *Report Estimating Illicit Flows Resulting from Drug Trafficking and Other Transnational Organized Crimes*, 2011, or FATF, *FAQ on money laundering*.

7 R. W. Baker, *Capitalism's Achilles Heel: Dirty Money and How to Renew the Free-Market System*, 2005.

8 Legal Assistance Requests refers to a method of cooperation between states for obtaining assistance in the investigation or prosecution of criminal offences. A LAR is generally used for obtaining material that cannot be obtained on a police cooperation basis, particularly investigations that require coercive means, and can refer to different types of assistance requested by foreign countries from Luxembourg judicial authorities. In Luxembourg, as in other civil law jurisdictions, LAR is referred to as Commissions Rogatoires Internationales (CRI). LAR is also often referred to as Mutual Legal Assistance (MLA). LAR, MLA and CRI terms are used interchangeably.

9 Parquet Général Statistical Service.

10 UNODC, *Report Estimating Illicit Flows Resulting from Drug Trafficking and Other Transnational Organized Crimes*, 2011.

11 Parquet Général Statistical Service.

12 Parquet Général Statistical Service.

2. Inherent threat of money laundering and terrorism financing

The threat of laundering proceeds of domestic crimes is estimated to be significantly smaller, due to Luxembourg's relatively low crime rate and limited presence of organised crime. Fraud and forgery, drug trafficking and robberies or theft, emerge as the three most significant domestic threats. While some crimes might be perpetrated domes-

tically, this does not necessarily imply that their proceeds are laundered domestically, but might be taken abroad (e.g. offences committed by foreign organised crime groups, taking proceeds outside Luxembourg).

TABLE 1: NATIONAL EXPOSURE TO ML THREATS MAP

Designated predicate offense	External exposure (75 %)	Domestic exposure (25 %)	Weighted average exposure
Money laundering (average ML threat)	Very high	Medium	Very high
Drug trafficking	Very high	High	Very high
Fraud and forgery	Very high	High	Very high
Tax crimes	Very high	Medium	Very high
Corruption and bribery	Very high	Medium	Very high
Participation in an organised criminal group & racketeering	High	Medium	High
Counterfeiting and piracy of products	High	Medium	High
Sexual exploitation, including sexual exploitation of children	High	Medium	High
Smuggling	High	Low	High
Robbery or theft	Medium	High	High
Trafficking in human beings and migrant smuggling	Medium	Medium	Medium
Insider trading and market manipulation	Medium	Low	Medium
Illicit trafficking in stolen and other goods	Medium	Low	Medium
Environmental crimes	Medium	Low	Medium
Illicit arms trafficking	Medium	Low	Medium
Counterfeiting currency	Low	Low	Low
Extortion	Low	Very Low	Low
Murder, grievous bodily injury	Low	Very Low	Low
Kidnapping, illegal restraint, and hostage taking	Low	Very Low	Low
Piracy	Low	Very Low	Low
Terrorism and terrorist financing	Medium	Medium	Medium

2. Inherent threat of money laundering and terrorism financing

Terrorism and terrorist financing (TF)

The threats of terrorism and terrorist financing (TF) are assessed as medium overall. It should be noted that while portrayed jointly here¹³, the threats of terrorism and terrorist financing are different in nature. Still, both are closely connected and deemed overall moderate relative to ML in Luxembourg, even if due to different drivers (e.g. Luxembourg's geographical position for the threat of terrorism, the financial centre for the threat of terrorism financing).

The threat level is driven mainly by the possible abuse or misuse of Luxembourg's large financial sector by a terrorist group or a terrorist financier from abroad; nonetheless, considering data from the CRF, the Prosecution authorities and the Grand-Ducal Police, terrorism and terrorist financing appears to be a more moderate threat compared to ML. Accordingly, there are few TFTR and TFAR¹⁴ reported to the Luxembourg FIU, the CRF (across all submitting entities).

Terrorism: Despite no recent terrorism events and no known terrorist groups in Luxembourg, in view of recent terrorism events in neighbouring countries, Luxembourg raised its level of terrorism threat to 2 (on a scale of 4) in 2015, which was kept through 2016 and 2017.¹⁵ Luxembourg has also broadened its definition of the terrorism predicate offence to include for instance propaganda and training.¹⁶ Some factors (including external) might contribute to the exposure of Luxembourg to this threat in terms of likelihood, as for instance its geographical proximity to neighbour countries which have experienced terrorist attacks.

Terrorist financing: Terrorist financing is a more likely threat to Luxembourg than terrorism, given the country's position as a major non-domestic European financial centre, with significant financial flows transiting through the country. As with ML, Luxembourg's financial centre could be targeted by foreign terrorist groups, and the risk of a sector being abused by foreign terrorist groups or terrorist financiers is not to be excluded. Luxembourg's economic model exposes the country to some of the factors deemed as high risk for TF in international guidance (e.g. FATF's guidance, the EU's anti-money laundering directives, ESA guidance, EU SNRA), for instance its significant and sophisticated banking sector, a diversity of legal entities.

13 As referred jointly in FATF recommendations; FATF refers to "terrorism" and "terrorist financing" jointly in FATF Recommendation 6; similarly, FATF Immediate Outcomes 9 and 10 provide examples of useful statistics related to both "terrorism" and "terrorist financing".

14 Terrorist Financing Transaction Report (TFTR) and Terrorist Financing Activity Report (TFAR).

15 The level of terrorism threat was raised after the Paris attacks in November 2015, and kept at this level after the Brussels attacks in March 2016 as per communication by the Ministry of State. Level 2 (medium threat) defines a real yet abstract terrorist threat; it consists of increasing vigilance against an imprecise threat and to implement measures of vigilance, prevention and protection of variable and temporary intensity. See *Ministère d'Etat Luxembourg, Press Announcement on 23/03/2016*, 2016.

16 Council of Europe, Protocol to the Council of Europe Convention on the Prevention of Terrorism (CETS No 196) and Additional Protocol to the Council of Europe Convention on the Prevention of Terrorism (CETS No 217).

3. Inherent sectoral vulnerabilities to money laundering and terrorism financing

3. INHERENT SECTORAL VULNERABILITIES TO MONEY LAUNDERING AND TERRORISM FINANCING

Luxembourg's largest inherent ML/TF vulnerabilities (i.e. before taking into account the controls currently in place) stem from the banking sector, professional service provi-

ders and legal entities and arrangements. Other important vulnerabilities include the investment sector, money service businesses (MSBs) and real estate.

TABLE 2: INHERENT RISK – SUB-SECTORS

Sector	Inherent risk	Sub-sectors	Inherent risk
Banks	High	Retail & business banks (including payment services)	High
		Wholesale, corporate & investment banks	High
		Private banking	Very High
		Custodians and sub-custodians (including CSDs)	High
Securities	Low	Exchange and listed securities	Low
Investment sector	High	Wealth managers (gérants de fortune)	High
		Brokers and broker-dealers (non-banks)	High
		Traders/market-makers	Medium
		Collective investments	High
		Regulated securitisation vehicles	High
		Pension funds	Low
Insurance	Medium	Life insurers	High
		Non-life insurers	Low
		Traditional reinsurance	Low
		Reinsurance captives	Low
		Intermediaries	High
		PSA (insurance sector professionals)	Low
Money service businesses	High	Payment institutions	High
		E-money institutions	High
		Agents	Medium
Financial sector service providers	High	PSF spécialisés providing corporate services	High
		CSD/custodians (nonbanks)	Medium
Other financial sector professionals	Very Low	Other financial sector professionals	Very low
Professional service providers	High	Accounting professionals and tax advisors	High
		Economic advisors	Medium
		Prestataires de services aux sociétés et fiducies	High
		Commissaires	High
		Huissiers de justice	Medium
		Lawyers	High
		Notaires	High
		Experts comptables	High
		Réviseurs d'entreprises	High
		Gambling	Low
Sports betting	Very Low		
Ad hoc lotteries	Low		
National Lottery	Low		
Online gambling	Very Low		
Real estate	High	Real estate agents and developers (promoteurs)	High
		Other real estate activities	High
Dealers in high value goods	Medium	Art/antiques	Medium
		Luxury goods (e.g. maroquinerie)	Medium
		Precious metals, jewellers, clocks and used gold	Medium
		Car dealers	High
Hotels, bars, restaurants and other retail businesses	High	Hotels, bars, restaurants	High
		Other retail businesses	High
Freeport operators	High	Freeport operators	High

3. Inherent sectoral vulnerabilities to money laundering and terrorism financing

Sector	Inherent risk	Sub-sectors	Inherent risk
Legal entities and arrangements	High	Corporations ¹⁷	High
		Sociétés civiles	Medium
		Foundations	Low
		NGOs	High
		Other ASBLs	High
		Others	Very Low
		Domestic fiduciaries (“fiducies”)	High
		Foreign trusts	Very high

A summary rationale of these inherent risks is provided below.

Financial sectors:

The **banking sector** is inherently vulnerable to ML/TF risks due to a variety of drivers such as the large customer base, high transaction speed and the large volume of financial flows which, pursuant to the general understanding of ML practices world-wide, could potentially facilitate the concealment of illegal transactions. Luxembourg has a large banking sector with 139 banks from 28 different countries, and banking assets of €746 BN in assets¹⁸. These include retail and business banking, private banking, wholesale corporate and investment banks, and custodians and central securities depositories (CSDs). Amongst these the largest inherent risk lies with private banks, comparatively more fragmented (67 entities with ~€350 BN in assets, with top 5 entities representing only ~40% of market), a significant share of foreign ownership and a diverse client base including legal entities.

The **investment sector** in Luxembourg is large and diverse with a variety of entities such as wealth and asset managers, pension funds, broker-dealers, traders/market makers, collective investments and regulated securitisation vehicles. €4,160 BN net assets under management were invested in Luxembourg funds as of December 2017¹⁹, making Luxembourg the leading centre in Europe for investment funds. The detection challenges are not to be underestimated due

to high market fragmentation in terms of number of providers and intermediaries, the international nature of business and also the high volume of retail and institutional investors, which all together add to the supervision challenge. Trading and market-making activities are however more limited in Luxembourg. Additionally, while the Luxembourg Stock Exchange is large in terms of value and number of listings, it is mainly a debt issuance market with low actual transaction turnover and hence the securities sector has more limited inherent risk relative to other sectors.

The **insurance sector** is typically regarded as less vulnerable with regards to ML/TF risks since pay-outs are unpredictable or dependent on tail events and since products are complex for ordinary criminals not well versed with financial engineering. The vulnerability in Luxembourg is driven by the industry’s large size (€219 BN in assets and 7000 employees), in particular in the life insurance sub-sector, which is large, fragmented, oriented towards foreign residents (though mostly in EEA space) and retail in nature with a large presence of intermediaries.

Globally, **money service businesses** (including e-money and payment institutions) are commonly used by criminals engaging in ML/TF activities, given international payments, the speed and volume of transactions and geographical reach. Luxembourg has significantly large institutions in this sector (despite being a concentrated one, with only 13 entities), processing outflow transactions worth ~€40 BN; these are however mostly cross-border transactions within the European Union.

¹⁷ Note that a number of these corporations are regulated and supervised for AML/CFT purposes (e.g. financial sector, real estate agents).

¹⁸ Banque Centrale du Luxembourg, *Statistiques : Etablissements de crédit ; „tableau 11.01“ and „tableau 11.05“*, as of Decembre 2017.

¹⁹ ALFI and CSSF, *Net assets under management in Luxembourg funds*, May 2018.

3. Inherent sectoral vulnerabilities to money laundering and terrorism financing

Lastly, in the financial sector, some **specialised service providers** (namely, those offering trust and corporate services) are vulnerable to being abused or misused for ML/TF given their possible role in supporting the creation of complex or multi-jurisdiction legal structures.

Non-financial sectors:

Luxembourg has a significant, sizeable and sophisticated professional services industry supporting both the financial centre and other business activities. These include accountants, auditors, lawyers, tax and economic advisors, notaries and bailiffs, in aggregate totalling >9000 professionals (and mostly fragmented within each professional industry). These are exposed to significant ML/TF risks given their role as “gatekeepers” in accessing the financial system and other services and possible role in creating and managing legal structures (though these apply to different degree to different providers, e.g. notaries are legally required to register real estate transactions but do not provide financial services). Their role, expertise, fragmentation and size drive the inherent risk.

While **gambling** is generally regarded as particularly vulnerable to money laundering, the gambling sector in Luxembourg is limited and mostly concentrated around three activities: one casino, the National Lottery and ad hoc lotteries. There are no authorized domestic online gambling companies or sports betting firms as of 2017, with only the National Lottery conducting these activities (though in very low volumes). As a result, the risk of the sector domestically as a whole is limited.

The **real estate** sector is typically regarded as high risk globally, given the attractiveness of products (large-value transactions and assets enabling storage of value) and the possibility to conceal ownership via layering transactions. In Luxembourg, the risk is in line with the global risk rating -

as a large sector (~7-8% of the country’s gross value added in 2016-2017, and real estate transactions in 2016-2017 worth ~€17 BN²⁰), real estate is exposed to ML/TF.

Dealers in high value goods (e.g. car dealers, watchmakers, jewellers) are exposed to ML/TF given that they offer products that can be easily stored, transported and exchanged at a similar value offering storage of value and anonymity. The vulnerability to ML/TF in Luxembourg is limited as it is a large but concentrated sector, with risks being mostly driven by car dealers.

Hotels, bars, restaurants and other retail businesses in Luxembourg are also exposed to ML/TF due to the sector’s cash-intensive businesses, fragmentation and diversity. There are >10,000 registered entities with ~19,000 employees, generating a gross value added of ~2% of GDP in 2017.

Luxembourg’s **freeport and freeport operators** (within the Freeport of the Findel airport) offer long term storage of high value goods (such as artwork, vintage cars and fine wines). Free trade zones are considered by international guidance as potentially vulnerable to ML/TF

Finally, as the OECD observes, “almost every economic crime involves the misuse of corporate vehicles”²¹ since they may help conceal origin of funds, beneficial ownership or allow funds to be moved overseas. As in other countries, **legal entities and legal arrangements** in Luxembourg are vulnerable to abuse or misuse for ML/TF; with a high number of legal entities in varied legal forms (~117,000²² as of year-end 2017, including ~11,000 non-profit organisations), with a perceived high level of foreign ownership and international operations and businesses. Central registries for legal arrangements and trusts (“fiducies” or foreign trusts administered in Luxembourg) will be a determining factor in mitigating those risks.

²⁰ STATEC and AED data.

²¹ See for instance, OECD, *Behind the corporate veil: using corporate entities for illicit purposes*, 2001.

²² An additional ~30 000 corporations are under judicial or voluntary liquidation, or under insolvency proceedings under judicial control.

4. MITIGATION REGIME IN PLACE

Luxembourg has established a comprehensive AML/CFT regime across its legal and institutional set-up and competent authorities to mitigate the ML/TF inherent risks identified above. All key national stakeholders contribute to this including ministries (Finance, Justice, Foreign Affairs, State), national supervisors and administrations (CSSF, CAA, AED, ACD, ADA), intelligence bodies (CRF, SRE), judicial and law enforcement authorities (Prosecution authorities, Investigative Judges, the Police) and self-regulatory bodies (OEC, IRE, OAL, OAD, CdN).

Since 2009, Luxembourg has implemented a series of reforms in its legal framework and institutional set-up, to keep up pace with the evolving ML/TF risks and higher international standards. In particular, the 2004 AML/CFT Law was revised more than once over this period. These revisions transposed the EU directives on AML/CFT and new FATF recommendations, they clarified and increased the AML/CFT obligations of regulated entities, and they increased the powers and responsibilities of Luxembourg's competent authorities. In the CP (criminal code), the definition of ML/TF crimes was updated and aligned with FATF's definitions, and the administrative and criminal sanctions were increased.

This legal framework is upheld by **judiciary authorities and law enforcement authorities** – they conduct all necessary actions to investigate and prosecute criminal offences and recover crime-related assets. Prosecutors supervise to this end the activities of the Judicial Police (for preliminary investigations) and may transfer the case to an Investigative Judge to conduct a judicial investigation if coercive measures are required or if the offence is a felony. Investigative Judges may order measures that restrict individual freedoms (i.e. coercive measures) such

as provisional detention, searches, seizures, or auditions. Judicial Police execute the investigations as per orders of Prosecutors or Investigative Judges, and can use a wide range of investigative techniques (including undercover operations, intercepting communications, accessing computer systems, etc.). These powers and organizational model are fairly similar for both domestic and foreign cases, since Luxembourg receives and acts on an important number of LAR. The number of investigations, prosecutions and convictions for ML/TF has in fact significantly increased over the past years, with about ~240 persons convicted in 2017 (of which 217 with prison sentences). A large number of convictions relate however to self-laundering (i.e. cases where the ML offence is prosecuted on the perpetrator associated with the offence itself and not stand-alone ML) in drug trafficking, robbery or theft, fraud and forgery cases.

The legal framework was further strengthened in terms of asset confiscation and provisional measures for asset freezing, as legal provisions have been gradually broadened and with the set-up of an Asset Recovery Office (ARO)²³ in 2013. Judicial authorities have the authority to seize assets during a preliminary or judicial investigation without time limits, and the power to confiscate upon conviction (whereby the perpetrator forgoes ownership over his assets, which are transferred to the State). The judicial authorities can use these seizure and confiscation powers also within legal assistance provided to foreign countries.

Additional relevant reforms in the legal framework include those related to the implementation of international financial sanctions (including relating to TF) and tax transparency. The Ministry of Finance was designated as the competent authority for all matters relating to the financial aspects of international sanctions and their implementa-

²³ Bureau de Recouvrement des Avoirs (BRA); on the basis of Decision 2007/845/JHA, each EU State is to set up or designate a maximum of two Asset Recovery Offices to facilitate the tracing and identification of proceeds of crime and other crime-related property that may become the object of a freezing, seizure or confiscation order made by a competent judicial authority in the course of criminal or civil proceedings.

tion. In this role, the Ministry cooperates closely with all key stakeholders in matters of legislative and regulatory updates, approval and dissemination of best practices, identification of trends and sharing know-how among authorities and between authorities and the private sector as well as representation of Luxembourg in various international fora. In terms of tax transparency, a number of initiatives have been taken, by introducing the criminalisation of tax offences (aggravated tax fraud), adding six additional tax offences (aggravated tax fraud and tax evasion) to the catalogue of predicate offences to ML, enhancing MLA by suppressing the reservation of tax matters from the Additional Protocol to the European Convention on Mutual Assistance in Criminal Matters, as well as reinforcing mechanisms for national and international information exchange.

Luxembourg's AML/CFT regime is complemented by a prevention and supervision framework, covering the **private sector and AML/CFT competent supervisors**. While the private sector carries out its preventive role in line with regulations (e.g. customer due diligence, transaction monitoring), supervisors are responsible for defining applicable regulations and guidance (in line with national laws and competence of each supervisor), promoting and ensuring compliance of supervised entities with AML/CFT obligations, sanctioning non-compliance, and promoting awareness of ML/TF risks. These activities have been significantly enhanced in recent years, with a higher number and quality of on-site inspections, increased remedial actions issued, and strengthened regulations and procedures (e.g. licensing) by competent authorities. In 2017, AML/CFT competent supervisors in aggregate undertook >100 on-site inspections (likely more than double this amount in desk-based reviews), enforced >80 remedial actions (in form of sanctions and other warnings), and distributed >10 circulars (amongst other guidelines). An overview of the main supervisory authorities is provided below.

The **Commission de Surveillance du Secteur Financier (CSSF)** is the financial sector's prudential and AML/CFT supervisor. The CSSF supervises a broad range of financial sector professionals, including all banks (including retail and business banks, private banking, wealth, corporate & investment banks, custodians and CSDs), payments institutions, investment companies (collective investments, other), and FS service providers. The CSSF has strict licensing and authorisation requirements (e.g. fit and proper requirements, analyses for recommendation of authorisation to the Ministry of Finance), including ongoing review (e.g. upon change of shareholders) and with the power to revoke these licenses for non-compliance (on AML/CFT matters or other). Additionally, there is a dual authorisation process in place since November 2014 with euro-zone banks being under ultimate licensing authority of the European Central Bank (ECB).

The CSSF disposes of a wide range of supervisory powers that also apply to AML/CFT matters, including requesting and accessing information from supervised entities, exchanging information with other national and international authorities, carrying on-site and off-site inspections and investigations, imposing sanctions and requesting freezing of seizure of assets with the Prosecution authorities. These powers exhibit some differences across the different sub-sectors under CSSF's supervision (for instance, sanctioning powers are particularly extensive in CRR institutions). In the past 5-7 years, the CSSF has issued new regulations and guidance, established an internal whistleblowing process, and devised a risk-based approach to AML/CFT supervision, which is continuously refined to be applied to internal procedures (e.g. to prioritise resource allocation).

The **Commissariat aux Assurances (CAA)** is the insurance sector's prudential and AML/CFT supervisor (including insurers, reinsurers, intermediaries, pension funds and insurance sector professionals). The CAA has strict licensing

and authorisation requirements, has the power to request and access information, to conduct desk-based and on-site inspections and to penalise non-compliant entities (with sanctions including fines, penalties, other remedial action orders or blocking certain actions such as acquisitions). In recent years, the CAA, increased information exchange with other national and international authorities, and is continuously fine-tuning its risk-based approach to AML/CFT supervision mainly by launching revised or new questionnaires to supervised entities to inform its risk assessment.

The **Administration de l'Enregistrement, des Domaines et de la TVA (AED)** is Luxembourg's tax administration in charge of indirect taxes (e.g. VAT, stamp duty). It was given the responsibility to be AML/CFT supervisor for some non-financial sectors including real estate agents, accounting professionals, tax and economic advisors, corporate and fiduciary service providers, freeport operators and some dealers in high value goods²⁴. Disclosure obligations for AML/CFT are the same as for tax purposes, granting the AED significant powers to access and request information, as well as do inspections and issue fines to non-compliant entities. Data sharing protocols for AML/CFT purposes with a variety of national authorities are being enhanced. For its new mandate, in recent years it established a dedicated unit and staff for AML/CFT, a AML/CFT Consultative Committee to promote dialogue with business associations of supervised sectors, and is carrying out dedicated on-site inspections.

A number of **professional service provider professionals** in Luxembourg are mostly **self-regulated with regards to AML/CFT matters**, including certified professional auditors ("réviseurs d'entreprises"), certified professional accountants ("experts comptables"), notaries ("notaires") and lawyers ("avocats"). All self-regulated professions are subject to the same overarching AML/CFT obligations: customer due diligence, adequate internal organisation and cooperation requirements with authorities. Powers and practices differ across the professions and the self-regulatory body (SRB), also reflecting the specificities of their industry. In general however, SRBs have the power to set rules to their professionals to ensure compliance with AML/CFT obligations, to run (peer-based) controls and to sanction non-compliance. Additionally, many of these professionals can offer TCSP services, as can banks, investment professionals and other corporate service providers under CSSF's and AED's AML/CFT supervision. In Luxembourg, professionals legally authorised to offer what is categorised by TCSP services are either supervised by a supervisor, or an SRB²⁵. Furthermore all legal entities must register with the central company register (RCS) while a separate register on beneficial ownership is about to be set up.

The AML/CFT Prevention and Supervisory framework is further strengthened by specific rules and obligations for gambling operators (for instance, strict licensing requirements).

Detection activities are primarily driven by Luxembourg's financial intelligence unit, the **Cellule de Renseignement Financier (CRF)**. CRF responsibilities include receiving

²⁴ Natural or legal persons trading in goods, only to the extent that the payments are made in cash in an amount of €10.000 or more whenever a transaction is executed in a single operation or in several operations which appear to be linked.

²⁵ The 2004 AML/CFT Law defines company and fiduciary service providers ("prestataires de services aux sociétés et fiducies") as natural or legal persons who provide, in a professional capacity, any of the following services to third parties: a) Acting as an incorporation agent of legal persons; b) Acting (or arranging for another person to act as) a director or secretary of a company, a partner of a partnership, or a similar position in relation to other legal persons; c) Providing a registered office, business-, correspondence- or administrative address for a company, a partnership or any other legal person or arrangement; d) Acting as (or arranging another person to act as) a fiduciary of a fiducie or other similar legal structure; e) Acting as (or arranging for another person to act as) a nominee shareholder for another person. This includes banks, some investment firms, some specialized PSFs (all supervised by CSSF), insurance and reinsurance companies (supervised by CAA), business centers and independent directors (supervised by AED), chartered accountants, auditors, lawyers and notaries (all supervised by their respective self-regulatory body).

4. Mitigation regime in place

and analysing AML/CFT information, and dissemination of the intelligence it gathers to the relevant authorities. The CRF was set-up as an independent body headed by magistrates who operate independently as part of the judicial system, and sits within Luxembourg's Prosecution authorities (i.e. a judicial-type FIU). As magistrates, they carry out their tasks independently, managing their secure portal for the filing of suspicious transaction reports (STRs), deciding which operational or strategic analyses to perform, and disseminating information as appropriate (to national or international authorities). In the past three years, staff was increased, access to databases expanded, and IT tools enhanced (including the adaptation and implementation of a secure channel for STR filing as of 2017). In addition, legal provisions have been reinforced so that all public-sector authorities are obliged to report suspicious activities to the CRF, and that all supervisors, professionals and self-regulatory bodies are allowed to report suspicions to and share information with the CRF, without professional secrecy obligations applying and with identity protection. The number of STRs submitted to the CRF has increased rapidly in recent years, from ~7,000 in 2014 to ~39,000 in 2017. The CRF regularly meets with other national authorities and SRBs to exchange feedback on STRs and support in awareness-raising and training sessions. It integrates the Egmont Group and participates in multiple international fora. In addition, the CRF can freeze assets, and prolong cash seizures done at borders by ADA (as customs administration) from 24 hours for up to 3 months.

While the Luxembourg Inland Revenue (**ACD**) and the security intelligence service (**SRE**) are not AML/CFT competent authorities, they play an important role in supporting the prevention efforts. The ACD has relevant tax review pro-

cesses in place and information sharing that contributes to reduce the likelihood of tax crimes and increase the probability of detection should these occur. The SRE is Luxembourg's intelligence authority for national security and has an important role in the prevention of terrorism.

In terms of AML/CFT strategy and coordination, the **Ministry of Justice and the Ministry of Finance** both play a central role. The Ministry of Justice is responsible for national and international coordination on OECD and FATF matters²⁶, while the Ministry of Finance prepares the financial policy of the State. National coordination is ensured via coordination meetings and their sub-committees per topic, promoting discussion on several topics such as integration of sectors in AML/CFT Law revisions, additions of offences as predicate offences for ML, and working groups on relevant legislative changes.

Finally, **international cooperation** is at the basis of many of Luxembourg's AML/CFT activities given its open economy and diverse working population. This is ensured at the level of each competent authority (via membership in relevant international groups as well as information sharing mechanisms), law enforcement authorities (police cooperation, legal assistance requests, extraditions, and exchanges with other asset recovery offices) as well as national level conventions and bilateral and multi-lateral treaties. Importantly, Luxembourg has ratified/signed the Vienna Convention²⁷, the Palermo Convention²⁸, the Terrorist Financing Convention²⁹, the UN Convention against Corruption, the Council of Europe Convention on Cybercrime (2001) and the Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime and on the Financing of Terror-

26 Arrêté grand-ducal du 23 décembre 2013 portant constitution des Ministères.

27 UN Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, 1988.

28 UN Convention against Transnational Organized Crime, 2000 (and the Protocols Thereto).

29 International Convention for the Suppression of the Financing of Terrorism 1999 – adopted by the General Assembly of the UN in resolution 54/109 of 9 December 1999.

rism³⁰. In 2017, ~400 LAR were received by Luxembourg (of which ~70 ML-related), 44 extradition requests were executed from Luxembourg to another country (and 98 from another country to Luxembourg), 55 assistance requests were received by the Asset Recovery Office, and >1,500 police-to-police ML/TF related messages were exchanged with foreign counterparts.

³⁰ Warsaw Convention - Treaty No. 198 – Council of Europe Convention on Laundering, Search, Seizure, and Confiscation of the Proceeds from Crime and on the Financing of Terrorism.

5. LOOKING AHEAD

This stocktaking exercise provides a comprehensive assessment of Luxembourg's AML/CFT risks. By doing so, it enables Luxembourg authorities to enhance their shared understanding of the main threats and vulnerabilities, to further improve their mitigation actions and to articulate an all-encompassing AML/CFT strategy.

Luxembourg is aware that the fight against money laundering and terrorism financing requires continuous action. By implementing its first NRA, Luxembourg continues to build on and solidify its AML/CFT regime, thus contributing to the very important global efforts in this respect.

APPENDIX A.

GLOSSARY OF KEY TERMS AND DEFINITIONS

Term	Definition
ACD	Administration des Contributions Directes – Direct tax administration
AED	Administration de l'Enregistrement, des Domaines et de la TVA – Indirect tax administration
AML	Anti-money laundering
AML/CFT	Anti-money laundering and countering the financing of terrorism
ARO	Luxembourg's Asset Recovery Office (Bureau de Recouvrement des Avoirs – BRA)
BN	Billion
CAA	Commissariat aux Assurances Luxembourg's insurance supervisor
CFT	Countering the financing of terrorism
CRF	Cellule de Renseignement Financier – Luxembourg's FIU
CPP	Code of Criminal Procedure (Code de procédure pénale)
CRR	Certain type of investment firm under CSSF supervision (based on which activities the investment firm is authorised to perform)
CSSF	Commission de Surveillance du Secteur Financier Luxembourg's financial sector supervisor
Dealers in goods	Natural or legal persons trading in goods, only to the extent that the payments are made in cash in an amount of EUR 15.000 or more whenever a transaction is executed in a single operation or in several operations which appear to be linked (2010 AML/CFT Law)
ECB	European Central Bank
EEA	European Economic Area
Egmont Group	Informal network of 151 FIUs for the stimulation of international cooperation
EU	European Union
FATF	Financial Action Task Force
FIU	Financial Intelligence Unit – which is the Cellule the Renseignement Financier (CRF) in Luxembourg
Freeport operators	Operators in a free zone authorized to carry out their activity pursuant to an authorization by the ADA within the Community control type 1 free zone located in the municipality of Niederanven Section B Senningen called Parishaff L-2315 Senningerberg (Hoehenhof)
GDP	Gross Domestic Product
Investigative Judge	Juge d'instruction
IRE	Institut des Réviseurs d'Entreprises
Judicial Police	Police Judiciaire
LAR	Legal Assistance Request (sometimes referred to as Mutual Legal Assistance – MLA or Commission Rogatoire Internationale, CRI)
Magistrats	Magistrates, i.e. according to Luxembourg law on judicial organization either Investigative Judges or Prosecutors
ML/TF	Money laundering and terrorist financing
MM	Million
MSB	Money services business
NRA	National Risk Assessment
OAD	Ordre des Avocats de Diekirch
OAL	Ordre des Avocats de Luxembourg
OEC	Ordre des Experts Comptables
OECD	Organization for Economic Cooperation and Development
Parquet	State Prosecutors' Offices at the District level (Luxembourg and Diekirch)
Parquet Général	General State Prosecutor's Office
Parquet Général Statistical Service	Statistical Service of Prosecution authorities

Appendix A. Glossary of key terms and definitions

Term	Definition
Professionals	Professionals falling under the scope of the 2004 AML/CFT Law as defined in article 2 and subject to the professional obligations outlined under articles 3 to 8
Prosecution authorities	“Parquet” or “Ministère public”
Prosecutor	Procureur
PSFs	Professionnels du secteur financier – professionals as defined in the 1998 CSSF Law
RCS	Registre des du Commerce et des Sociétés (now called Luxembourg Business Registers – LBR)
Réviseurs d’Entreprises	Certified auditors as defined in the 2016 Auditors Law
SAR	Suspicious Activity Report
SARe	e-commerce related SAR
SRBs	Self-regulatory bodies
SRE	Service de Renseignement de l’Etat – Luxembourg Intelligence Service
State Prosecutor	Procureur d’Etat
STATEC	National Institute of Statistics and Economic Studies of the Grand Duchy of Luxembourg
STR	Suspicious Transaction Report
STRe	e-commerce related STR
STRs	All types of reports, ie STR, SAR, STRe, SARe, TFTR, TFAR
TCSP	Trust & Corporate Service Provider
TF	Terrorist financing
TFAR	Terrorist Financing Activity Report
TFTR	Terrorist Financing Transaction Report
UN	United Nations
UNODC	United Nations Office on Drugs and Crime
VAT	Value Added Tax
2004 AML/CFT Law	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 (as amended by following laws)



LE GOUVERNEMENT
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Ministère des Finances