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ANTI-MONEY LAUNDERING

Pick your fights

The EU's anti-money laundering efforts will be most effective if they focus on areas of real risk

Recent years have seen a steady stream of money laundering and terrorism financing scandals involving banking institutions and related failures by national supervisors. This has ensured that the topic of anti-money laundering (AML) and countering the financing of terrorism (CFT) — and particularly their supervision — have become a priority for the European institutions.

A banking authority supervising insurers?

The first major change adopted recently involved giving the European Banking Authority (EBA) a centralised role in the supervision of AML and CFT at European level for all "obliged entities", which means financial insitutions and designated non-financial businesses and professions, and therefore includes insurers.

This new responsibility for the EBA was introduced in the late stages of the review that was finalised in April 2019 of the Regulations establishing the European financial supervisory authorities. While a role was given to insurance supervisor EIOPA in assisting the EBA, this was not sufficient to alleviate insurers' concerns about bringing them under the jurisdiction of a banking authority.

Insurance = low risk

The EBA's first action as AML/CFT supervisor was to start updating the existing Risk Factors Guidelines, which are aimed at all obliged entities. This update was an opportunity for Insurance Europe to reiterate some of the key tenets of its position to the EBA. Insurance Europe particularly stressed one fact acknowledged by most institutions involved in AML/CFT, be it the European Commission at European level or the Financial Action Task Force (FATF) at international level: the insurance sector presents a very low money-laundering/terrorism-financing risk.

Indeed, the industry's only exposure to risk is in life insurance, and then only life insurance products with an investment element. In non-life insurance, the risk is nil, unless fraud is taken into account, yet fraud should be and is addressed in its own right by insurers.

The European institutions confirmed this by focusing on life insurance in the European framework and, in doing so, they followed the FATF, which clearly excludes non-life insurance from the scope of its work. Unfortunately, this approach is not followed consistently throughout Europe, with some member states choosing to leave non-life insurance within the scope of their national frameworks.

Be guided by risk

Another key principle that Insurance Europe defends is the need to take a risk-based approach to countering money laundering and terrorism financing; resources should be focused on the sectors, products, transactions and people that represent a real risk. Applying a risk-based approach means that — in most cases — life insurance transactions only require a simplified due diligence process.

A risk-based approach should be the guiding principle when considering the Commission's recent suggestion of a new EU AML/CFT supervisor. The EBA had barely started its mandate when new AML scandals in the banking sector prompted the EC to propose further and stronger reform of AML/CFT supervision in the EU. This was confirmed in 2020 when, in its Action Plan for a comprehensive EU policy, the Commission suggested a new supervisor for the cross-border activities of all obliged entities.

Since the problems that prompted this Action Plan were virtually all related to the banking sector, it would make sense for any new authority to be focused on banking. This would be consistent with the risk-based approach: focus the supervisory resources on the sector in which the risk resides.

> **"Resources should be focused on the sectors, products, transactions and people that represent a real risk."**

In any event, any such supervisor must have the skills and expertise to supervise all entities under its jurisdiction. The business models of different entities and their exposure to AML risks are very diverse and, as explained earlier, Insurance Europe is still wary of an institution with expertise in banking supervising the insurance sector.

Local knowledge is best

The allocation of supervisory powers to a new EU body must also be measured against the subsidiarity principle, meaning that powers should be transferred to EU level only if the objectives of AML/CFT supervision cannot be sufficiently achieved by national supervisors.

This important role played by national supervisors should be highlighted, as they are generally better placed to know and understand their home markets. In addition to having local expertise, they are also in direct contact with the entities under their jurisdiction. Where a supervisor fails on cases in a specific sector, this should be taken up with the supervisor concerned and within that sector, rather than leading to the creation of a new authority with EU-wide jurisdiction over all financial sectors.

The legal basis for including all obliged entities under the scope of an EU-level supervisor, irrespective of their exposure to AML risks, is therefore questionable. The time and effort required to set up such a structure can also seem disproportionate when compared to the exposure to money-laundering/terrorism-financing risks of sectors such as insurance.

European insurers remain as committed as ever to the fight against money laundering. For this fight to be successful, the risk-based approach must remain the cardinal rule on which any legislative framework is based.

A single EU-level AML/CFT supervisor with jurisdiction over a low-risk sector such as insurance does not seem consistent with that approach and should therefore be avoided.