

Executive Summary

1. This report summarises the anti-money laundering and counter-terrorist financing (AML/CFT) measures in place in Luxembourg as at the date of the on-site visit: 2-18 November 2022. It analyses the level of compliance with the FATF 40 Recommendations and the level of effectiveness of Luxembourg's AML/CFT system and provides recommendations on how the system could be strengthened.

Key Findings

1. Luxembourg's first national risk assessment (NRA), completed in 2018, triggered several changes in its AML/CFT regime, such as improvements to the legal framework, establishment of new agencies, and investment in automated tools to increase efficiencies. These efforts are starting to bear fruit, in some authorities and sectors more than in others. However, Luxembourg needs to maintain a sustainable path to keep course with these efforts and align them with its role as international financial hub with significant cross-border financial flows, international clientele and high-risk products and services.
2. Luxembourg has a strong understanding of its money laundering (ML) risks and a reasonable understanding of its terrorist financing (TF) risks, which is reflected in its national, vertical and sub-sectoral risk assessments. Luxembourg's 2022 TF Vertical Risk Assessment was a positive development, and its methodological approach and general conclusions were sound, though not fully justified or substantiated. Most authorities' overall TF risk understanding is predominantly focused on smaller-scale TF. However, findings related to larger-scale TF stemming from Luxembourg's status as an international financial centre have not been sufficiently communicated to relevant public and private sector stakeholders. Key strengths of the Luxembourg system lie in its robust domestic co-ordination and co-operation on AML/CFT issues at both the policy and operational levels.
3. The CRF-FIU plays a key role in producing and disseminating a wide range of high-quality financial intelligence products, which are widely used by law enforcement authorities (LEAs) and other competent authorities to support their operational needs. However, its level of human resources and

increasingly complex role give rise to concerns about the CRF-FIU ability to continue effectively performing its various functions going forward.

4. Luxembourg has demonstrated a commitment to investigating and prosecuting ML at the policy level. However, resource limitations in investigative and judicial authorities, and the Council Chamber hamper effectiveness to this end. Unlike the overall volume, the types of ML investigations and prosecutions fall within Luxembourg's risk profile to a large extent.
5. Luxembourg makes effective use of tools for freezing and seizing criminal assets and confiscates proceeds of foreign predicate offences and property of equivalent value, as requested by its foreign counterparts. Management of property frozen, seized or confiscated was an issue for Luxembourg throughout the review period, where the competent authorities focused on confiscating cash and balance on accounts. A dedicated asset management office was established just before the on-site visit.
6. Luxembourg proactively identifies and investigates TF activity alongside terrorism related investigations. Luxembourg had no prosecutions or convictions for TF due to the mitigating measures in place. This is somewhat in line with Luxembourg's risk profile.
7. Luxembourg implemented TF targeted financial sanctions (TFS) generally within one working day, and PF TFS with some delay up to late 2020. Measures to remedy gaps in the TFS regime, several of which were only recently put into place, require further development. Luxembourg has not frozen assets related to TF or PF TFS; however, examples were provided where financial institutions (FIs) reacted immediately to designations under other UN sanctions regimes and froze substantial amounts of assets (i.e., cash and securities).
8. Luxembourg has identified the subset of non-governmental organisations (NGOs) that engage in development and humanitarian projects abroad (DNGOs) that are likely to be at risk of TF abuse. However, the Ministry of Foreign Affairs (MoFA) does not apply a risk-based approach in its supervision of the sector. The sector's understanding of TF risk is very low.
9. Understanding of ML risks and AML/CFT obligations is strong for FIs, good for virtual asset service providers (VASPs) and mixed among designated non-financial businesses and professions (DNFBPs). Real estate agents (REAs) and dealers in precious metals and stones (DPMS) have a weak understanding of ML/TF risks and AML/CFT obligations. Generally, for all sectors, there is a need to further strengthen and develop the understanding of TF risk and, for some FIs and DNFBPs, TFS obligations. Most DNFBPs submit low number of suspicious transaction reports (STRs) while many reports are driven by adverse media hits, which can be a valuable indicator for suspicion. The CRF-FIU provided statistics indicating that most of the STRs filed based on adverse media hits included some level of analysis. However, some FIs and a large number of DNFBPs and VASPs met by the assessment team indicated that they provided STRs based on adverse media without further analysis. Furthermore, the quality and relevancy of TF reporting by some obliged entities is extremely low. Overall, this reduces the reporting levels related to ML/TF suspicion and does not reflect Luxembourg's risk profile as an international financial centre.

10. Eight supervisory authorities and self-regulatory bodies (SRBs) supervise all FIs, DNFBPs and VASPs as defined by the FATF Standards. The Luxembourg supervisory regime started becoming increasingly mature in recent years, with supervisors having expanded supervisory and sanctioning powers, automizing tools and processes, increasing human resources, and combining off-site and on-site work. While there is a clear positive trend, particularly with risk-based supervision for FIs significantly enhanced during the review period, the comprehensiveness of a risk-based approach to supervision is in early stages for DNFBPs and VASPs, with inspections of some high risk DNFBP sectors (professional directors-supervised by the AED-TCSPs) not having started, limited resources in a few DNFBP supervisors, diverging application of sanctions, and the need for continued sustainable efforts to maintain the upward trend.
11. Luxembourg's increased efforts and focus on transparency of legal persons and legal arrangements has a positive impact on preventing misuse of corporate vehicles. At the heart of it are the registers on beneficial ownership for legal persons and legal arrangements. Authorities use a multipronged approach to obtain accurate and up-to-date beneficial ownership information in a timely manner. However, sanctions are applied to a varying extent: notably, only criminal penalties are available for violation of legal person information obligations requiring the involvement of the State Prosecutor and hence significantly limiting the proportionality and effective use of sanctions. The understanding of how legal persons can be or are misused for TF is less developed than that for ML.
12. International co-operation is critical and factors in all areas of Luxembourg's AML/CFT framework. Over the review period, Luxembourg consistently provided constructive, and good quality mutual legal assistance (MLA), extradition and international co-operation. Incoming MLA requests not requiring coercive measures are processed within three to four months. However, timeliness is an issue in some cases, as approximately 30% of incoming MLA requests requiring coercive measures are executed by Luxembourg in a timeframe longer than seven months.

Risks and General Situation

2. Luxembourg is an international financial centre with a large and globally interconnected financial system. The financial and insurance sectors are Luxembourg's largest economic sectors, contributing to approximately 23% of the national GDP. Luxembourg has a very high incoming foreign direct investment stock as a percentage of GDP in 2021, with 169% compared to the EU average of 62%. Luxembourg's banking sector is home to more than 120 credit institutions from 24 countries as of December 2022, and the banks located in Luxembourg specialise, amongst other things, in private banking, in providing custodian services for investment funds and fund administration, and in the distribution of shares in investment funds. With about EUR 5 545 billion net assets under management in Luxembourg funds (as of February 2022), Luxembourg is the leading centre in Europe for investment funds. Luxembourg also hosts major Payment and E-money Institutions (PIs/EMIs). Since March 2020, VASP are required to register with the

CSSF. As of November 2022, the VASP sector counts 9 VASPs. The DNFBP sector is large and fragmented consisting of lawyers, REAs, accountants, and trusts and company service providers (TCSPs) offered by a multitude of professionals (FIs and DNFBPs) including banks, investment firms, specialised Professionals of the Financial Sector providing Corporate Services (specialised PFS), business/office centres, professional directors, lawyers, chartered professional accountants (CPAs) and (approved) statutory auditors and audit firms. Luxembourg has only one land-based casino.

3. Given its position as an international financial hub, Luxembourg identified foreign predicate offences as its main ML threat. The foreign predicate offences that contribute significantly to the ML threat include fraud and forgery, tax crimes, corruption and bribery and drug trafficking. Banks (especially private banking), the investment sector, PIs, E-MIs, TCSPs, real estate activities and some legal persons (i.e., commercial companies) and legal arrangements are the most vulnerable to ML and TF. The threat of domestically generated proceeds being laundered through Luxembourg is less significant, given the low crime rate and limited presence of domestic organised crime. The threat level for certain types of offences (i.e., fraud and forgery, drug trafficking and robbery or theft) may increase due to Luxembourg's wealth, economy and geography, including its open borders within the Schengen area. Luxembourg assesses the threats of terrorism and TF as moderate to low. It has not experienced any terrorist attacks and no terrorist groups have been formed on its territory. As an international financial centre, TF is a likely threat, as funds may be moved through Luxembourg's financial system.

Overall Level of Compliance and Effectiveness

4. Luxembourg has strong results on technical compliance with the FATF Standards. On effectiveness, many of these changes have occurred in the three to five years before the on-site visit, or less, and while some initiatives are beginning to show results, other reforms have been too recent or are structural and require an appropriate period of time to become operational and lead to changes in the effectiveness of the overall system. Changes that were implemented earlier (e.g., introduction of goAML by CRF-FIU in 2017) have led to a material increase in effectiveness, whereas more recent changes (e.g., efforts to improve DNFBP supervision, asset management reform, changes to the 2004 AML/CFT law, and the TFS framework) are starting to show results, but are not yet fully effective.

Assessment of risk, co-ordination and policy setting (Chapter 2; IO.1; R.1, 2, 33 & 34)

5. Luxembourg has taken a range of steps since its last MER to increase its national ML/TF risk understanding. Luxembourg's first NRA (2018), followed by an update in 2020 provide a good basis for risk understanding and triggered additional topic-focused risk assessments on TF, virtual assets (VA)/VASPs and legal persons and legal arrangements. Luxembourg used bottom-up and top-bottom approaches and engaged with a range of authorities and representatives from the private sector. These initiatives have given Luxembourg a strong understanding of its ML risks stemming mainly from foreign predicate offences, the banking and investment sectors, PIs/EMIs, TCSPs, REAs and legal persons and legal arrangements. Luxembourg's May 2022 TF Vertical Risk Assessment (2022 TF VRA) employed a sound methodology and came to reasonable conclusions, but the analysis could be better supported with additional considerations. Most authorities' overall TF risk understanding is more recent and less well-developed as it focusses on smaller-scale TF and findings related to larger-scale TF stemming from Luxembourg's status as an international financial centre have not been adequately disseminated across all authorities and the private sector.
6. The risk assessments informed national AML/CFT policies and activities resulting in multiple national and agency-level action plans over the course of the past four years. This led to, for instance, a further harmonization of supervision, access to the beneficial ownership information registers by LEAs and the CRF-FIU, and the establishment of an asset recovery office. However, the prioritisation of action items has not been well-communicated to some government stakeholders critical to their implementation, and the fast-paced implementation of successive action plans required diverting resources from non-AML/CFT priorities for several years, raising the question of sustainability.
7. The key strength of the Luxembourg system is the very strong domestic co-ordination and co-operation on AML/CFT issues at both policy and operational levels. Results of risk assessments are extensively communicated to FIs, DNFBPs and VASPs in a proactive and consistent manner. However, the more comprehensive and informative findings of the confidential document of the 2022 TF VRA providing information related to larger-scale TF stemming from Luxembourg's status as an international financial centre have not been adequately communicated to the private sector stakeholders. As a result, private sector stakeholders have not been provided with a detailed assessment of TF risks associated with Luxembourg's status as an international financial centre, and the associated vulnerabilities.

Financial intelligence, ML investigations, prosecutions and confiscation (Chapter 3; IO.6, 7, 8; R.1, 3, 4, 29–32)

8. Competent authorities regularly access and use financial intelligence to support investigation of ML/TF and related predicate offences and trace assets for confiscation. The CRF-FIU plays a key role in producing and disseminating a wide range of good-quality financial intelligence products; however, its limited human resources give rise to concerns about the CRF-FIU's ability to continue effectively performing its various functions.

9. Luxembourg proactively identifies and investigates ML through a wide variety of sources. However, limitations in human resources impacted both on the ability of investigative and judicial authorities in conducting ML investigations, and the capacity of the Council Chamber to prioritise the review of ML cases before prosecution. ML investigations and prosecutions fall within Luxembourg's risk profile to a large extent; however, given the identified limitation in qualitative and quantitative data, the assessment has concerns over the extent to which Luxembourg prosecutes different types of ML more broadly.
10. Luxembourg prioritises confiscation as a prominent feature of its 2019 AML/CFT Strategy. Since 2020, Luxembourg actively confiscates the proceeds of foreign predicate offences, in line with its risk and context. However, statistics on domestic ML cases are not broken down between foreign and domestic predicate offences or stand-alone ML. Therefore, Luxembourg cannot demonstrate what portion of the confiscated sums relates to domestic and foreign predicate offences, other than the proceeds confiscated based on incoming MLA requests. Luxembourg has limited capacity to preserve and manage the value of assets other than cash and balance on accounts that are seized or confiscated, forcing authorities to focus primarily on liquid assets.

Terrorist and proliferation financing (Chapter 4; IO.9, 10, 11; R. 1, 4, 5–8, 30, 31 & 39)

11. Investigative authorities and LEAs have adequate experience and tools to identify and investigate possible TF activity. Competent authorities engage proactively with foreign counterparts to identify potential TF activity. Over the review period, Luxembourg conducted 30 investigations (preliminary and judicial) solely on TF. However, none of these investigations led to prosecution or conviction due to the mitigating measures in place. This is somewhat in line with Luxembourg's risk profile.
12. Luxembourg implemented TFS for TF generally within one working day and for PF with delay until late 2020. Since then, Luxembourg has put measures in place, some quite recently, to bridge the delay inherent in the EU framework and require all natural and legal persons to freeze the assets of these designated persons without delay and prior notification. Some elements of the TFS regime could be improved.
13. NGOs that engage in development and humanitarian projects abroad (DNGOs) are likely to be at risk of TF abuse. However, the MoFA does not apply a risk-based approach in its supervision of the sector. Since 2019, MoFA has enhanced its contacts with the sector. However, more outreach is necessary to improve the sector's understanding of TF risk, which is very low.
14. Awareness of PF-related TFS in the private sector varies. The financial sector generally has a strong understanding of its TFS obligations; however, this is not the case in some non-bank financial sectors. VASPs understand their TFS obligations and their vulnerability to potential violations of DPRK sanctions in light of the prevalent use of virtual assets in ransomware attacks. DNFBBPs' understanding varies.

Preventive measures (Chapter 5; IO.4; R.9–23)

15. Luxembourg has large and diverse financial and DNFBBP sectors. All FIs, DNFBBPs (as defined by the FATF) and VASPs are required to apply AML/CFT preventive

measures. In general, FIs, including VASPs, have demonstrated a stronger application of the range of preventive measures than DNFBBPs. Understanding of ML risks and AML/CFT obligations is strong for FIs, good for VASPs and mixed among DNFBBPs. Generally, for all sectors, there is a need to further develop the understanding of TF risks and, for some FIs and DNFBBPs, of TFS obligations. Overall, REAs, identified as a high-risk sector, and DPMS have a weak understanding of risks and application of AML/CFT obligations resulting in weaker risk-based mitigating measures. Entities broadly understand and implement their reporting obligations. However, this is not the case across all sectors and firms as evidenced by the low number of suspicious transactions reports (STRs) filed by most DNFBBPs. A large number of reports were based on adverse media hits, which can be a valuable indicator for suspicion particularly when analysed by the obliged entity to establish an actual suspicion of ML/TF. The CRF-FIU provided statistics indicating that most of the STRs filed based on adverse media hits included some level of analysis. However, some FIs and a large number of DNFBBPs and VASPs met by the assessment team indicated that they provided STRs based on adverse media without further analysis. Furthermore, the quality and relevancy of TF-related reports submitted by some obliged entities remains a concern as the level of reporting is low and it is not clear whether there are reports that include the aspect of financing or if they are all related to terrorism itself. This reduces the reporting levels related to ML/TF suspicion and does not reflect Luxembourg's risk profile as an international financial centre.

Supervision (Chapter 6; IO.3; R.14, R.26–28, 34, 35)

16. All FIs and DNFBBP sectors (as defined by the FATF) are supervised for AML/CFT compliance. In recent years, Luxembourg undertook steps to harmonize DNFBBP supervision and the Commission de Surveillance du Secteur Financier (CSSF) became responsible for registering and supervising VASPs. Consequently, the quality of supervision varies among the eight AML/CFT supervisors. The CSSF, the main supervisor of FIs and VASPs, implemented regular reforms in response to changing risks, such as increasing human resources and establishing a dedicated team for on-site inspections of the investment sector. It uses a multipronged approach by combining off-site supervision and monitoring with on-site inspections. The CSSF assisted other supervisors to bolster up their risk-based approach. DNFBBP supervisors are in the early stages of developing their methodology for risk-based supervision. Limited resources and organisational set-up impede some supervisors' ability to carry out their supervisory tasks. In particular, the Tax Authority on Registration Duties, Estates and VAT (AED) has a low number of staff to conduct on-site inspections, has not yet started the inspections of professionals providing directorship services under its supervision and does not fully execute supervision in line with risks, thus diverting resources that should be dedicated to higher risk professionals.
17. Measures to prevent criminals and associates from entering the market are robust. FI supervisors have a good ML/TF risk understanding, including through sub-sectoral risk assessments and regular interaction with the private sector and other authorities. DNFBBP supervisors have varying levels of ML/TF risk understanding, as they have recently begun to develop and implement their risk-based approach to supervision.

18. Luxembourg uses a range of enforcement measures to address non-compliance to a varying extent. For the CSSF, these have been dissuasive but public statements on enforcement cases convey very limited information on the nature of breaches to assist FIs in understanding what would constitute significant deficiencies, thus impacting the effectiveness. The *Commissariat aux Assurances* (CAA) made limited use of its sanctioning power. As for the DNFBP sectors, sanctions are not considered to be sufficiently dissuasive or effective for the REAs and notaries, which are higher risk.

Transparency and beneficial ownership (Chapter 7; IO.5; R.24, 25)

19. All legal persons incorporated in Luxembourg need to register basic information in the Trade and Company Register (RCS) and, since 2019, must also register beneficial ownership (BO) information in the RBE. Since 2020, BO information of legal arrangements must be registered in the Register of *Fiducies* and Trusts (RFT). Overall, Luxembourg has a good understanding of how legal persons could be misused for ML; however, there is a need to improve the understanding of where the TF threats emanate as risk analysis focusses on higher risk categories of legal persons used by NPOs and not on other forms of legal persons.
20. Competent authorities demonstrated an effective use of a multi-pronged approach to satisfy themselves of the accuracy and availability of BO information since the establishment of the RBE (2019) and RFT (2020). Competent authorities and obliged entities clearly understand their obligation to file discrepancy reports to the registrars should they discover inaccurate, missing or out of date information, which helps ensure accuracy.
21. Only criminal penalties are available for violation of legal person BO disclosure requirements and requires the involvement of the State Prosecutor, which detracts resources from higher AML/CFT priorities and limits the timely application of sanctions. Also, limited criminal fines have been imposed for not maintaining or updating lists of members or a register of shares.

International cooperation (Chapter 8; IO.2; R.36–40)

22. International co-operation is vital for Luxembourg given its status as an international financial centre. Over the review period, Luxembourg consistently provided constructive and good quality mutual legal assistance, extradition and asset recovery (including asset repatriation). Incoming MLA requests not requiring coercive measures are processed within three to four months. However, timeliness is an issue in some cases, as approximately 30% of incoming MLA requests requiring coercive measures are executed by Luxembourg in a timeframe longer than seven months.
23. Most Luxembourgish competent authorities proactively seek and provide (including spontaneously) international co-operation to exchange financial intelligence, supervisory, law enforcement, and basic and BO information, in an appropriate and timely manner with their foreign counterparts for AML/CFT purposes.

Priority Actions

Luxembourg should:

1. Substantially strengthen the detection, investigation, and prosecution of parallel ML investigations related to all higher risk predicate offences to ensure better alignment of investigations and prosecutions with Luxembourg's risk profile.
2. Enhance the capacity of the Asset Recovery Office (ARO), the Asset Management Office (AMO) and the Office of the Investigative Judge to better carry out their mandates on asset investigations, post-conviction asset investigations, asset management and international co-operation.
3. Further develop and disseminate its understanding of TF risks and vulnerabilities, including misuse of legal persons for TF purposes, stemming from its exposure as international financial centre. Luxembourg should also ensure that all public and private stakeholders have a better understanding of TF risk, methods and exposure to larger-scale TF through guidance or other forms of outreach.
4. Ensure that the MoFA develops and implements procedures to apply RBA to its oversight of the NPO sector and undertakes systematic outreach to enhance the sector's poor understanding of TF risk.
5. For DNFBPs, strengthen risk-based AML/CFT supervision, by enhancing comprehensiveness of off-site monitoring and on-site inspections, and applying an appropriate level of resources, including increasing supervisory resources of the AED and Order of Chartered Professional Accountants (OEC).
6. Ensure that penalties and remedial measures are proportionate and dissuasive and applied in a timely and effective manner to ensure a positive effect on compliance by FIs, DNFBPs and VASPs.
7. Luxembourg should take effective steps to reduce the identified delays in the execution of incoming MLA requests on coercive measures.

Effectiveness & Technical Compliance Ratings

Table 1. Effectiveness Ratings

IO.1 - Risk, policy and co-ordination	IO.2 International co-operation	IO.3 - Supervision	IO.4 - Preventive measures	IO.5 - Legal persons and arrangements	IO.6 - Financial intelligence
Substantial	Substantial	Moderate	Moderate	Substantial	Substantial
IO.7 - ML investigation & prosecution	IO.8 - Confiscation	IO.9 - TF investigation & prosecution	IO.10 - TF preventive measures & financial sanctions	IO.11 - PF financial sanctions	
Moderate	Moderate	Substantial	Moderate	Moderate	

Note: Effectiveness ratings can be either a High- HE, Substantial- SE, Moderate- ME, or Low - LE, level of effectiveness.

Table 2. Technical Compliance Ratings

R.1 - assessing risk & applying risk-based approach	R.2 - national co-operation and co-ordination	R.3 - money laundering offence	R.4 - confiscation & provisional measures	R.5 - terrorist financing offence	R.6 - targeted financial sanctions - terrorism & terrorist financing
C	C	C	LC	C	LC
R.7 - targeted financial sanctions - proliferation	R.8 - non-profit organisations	R.9 - financial institution secrecy laws	R.10 - Customer due diligence	R.11 - Record keeping	R.12 - Politically exposed persons
LC	PC	C	C	C	C
R.13 - Correspondent banking	R.14 - Money or value transfer services	R.15 - New technologies	R.16 - Wire transfers	R.17 - Reliance on third parties	R.18 - Internal controls and foreign branches and subsidiaries
C	C	LC	C	C	C
R.19 - Higher-risk countries	R.20 - Reporting of suspicious transactions	R.21 - Tipping-off and confidentiality	R.22 - DNFBPs: Customer due diligence	R.23 - DNFBPs: Other measures	R.24 - Transparency & BO of legal persons
C	C	C	C	C	LC
R.25 - Transparency & BO of legal arrangements	R.26 - Regulation and supervision of financial institutions	R.27 - Powers of supervision	R.28 - Regulation and supervision of DNFBPs	R.29 - Financial intelligence units	R.30 - Responsibilities of law enforcement and investigative authorities
C	C	C	C	C	LC
R.31 - Powers of law enforcement and investigative authorities	R.32 - Cash couriers	R.33 - Statistics	R.34 - Guidance and feedback	R.35 - Sanctions	R.36 - International instruments
C	LC	LC	C	LC	LC
R.37 - Mutual legal assistance	R.38 - Mutual legal assistance: freezing and confiscation	R.39 - Extradition	R.40 - Other forms of international co-operation		
C	C	C	LC		

Note: Technical compliance ratings can be either a C - compliant, LC - largely compliant, PC - partially compliant or NC - non compliant.