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FINANCIAL ACTION TASK FORCE

Mutual Evaluation Report Executive Summary

Anti-Money Laundering and Combating the Financing of Terrorism

Luxembourg

19 February 2010

Luxembourg is a member of the Financial Action Task Force. This evaluation was conducted by the FATF and was adopted as a third mutual evaluation by its Plenary on 19 February 2010.

EXECUTIVE SUMMARY

Background information

1. This report summarises the anti-money laundering and counter-terrorist financing measures (AML/CFT) that were in place in Luxembourg at the time of the on-site visit (4-15 May 2009) and immediately thereafter. It describes and analyses these measures and offers recommendations on how to strengthen certain aspects of the system. It also assesses Luxembourg's level of compliance with the 40+9 Recommendations of the Financial Action Task Force (FATF). See as well the table of ratings of compliance with the FATF Recommendations, below.

Key Findings

- Luxembourg is one of the most important financial centres in Europe and worldwide; it ranks second in the world for investment fund activities and is the most important centre for wealth management in the euro zone. Financial services occupy a very important place in the economy, accounting for around 25% of gross domestic product.

- The crime of money laundering is defined technically in a manner largely consistent with international standards. However, legal persons are not subject to criminal sanctions.[1] Moreover, practical implementation of the offence is very ineffective, so that sanctions (the level of which is generally low) have been imposed in only eight cases since 2003. The criminalisation of terrorist financing does not cover all the elements called for by international standards and does not include the financing of individual terrorists or terrorist groups other than as related to the commission of terrorist acts. Finally, the notion of a terrorist group applies only to associations of more than two persons.

- The confiscation mechanism in place is relatively satisfactory, despite some limitations that reduce its scope, particularly regarding confiscation of property held by a third party. Provisional measures that may be implemented in this context are inadequate and confiscation cases are rare in terms of ML and relate to secondary instrumentalities (*i.e.* not cash or high value assets). Terrorist assets may be frozen by the Financial Intelligence Unit (FIU), but this measure is limited to three months and is conditional upon the filing of a suspicious transaction report (STR), which does not ensure timely freezing and applies only to financial assets. In general, the procedure for freezing terrorist assets is confusing and falls short of international standards.

- The FIU was created in 2004 within the office of the Public Prosecutor of Luxembourg (the *Parquet*). At the time of the on-site visit it comprised six persons responsible for operational tasks, an inadequate staffing level in light of the steadily rising number of STRs filed. The FIU is not bound by any "speciality rule" but has jurisdiction over all offences detected in STRs. Among

[1] A draft law establishing criminal liability for legal persons was adopted by the Luxembourg Parliament on 4 February 2010.

the cases that it "disseminates", few cite the crime of money laundering. Prosecution authorities also focus their efforts on the predicate offence; the number of laundering investigations is low (there had never been an investigation into terrorist financing at the time of the on-site visit).

- Luxembourg's AML/CFT prevention mechanism is based on [European] Community instruments. It applies to the great majority of financial institutions that should be covered according to FATF rules, as well as designated non-financial businesses and professions (DNFBPs), and it has been extended to other professions. However, Luxembourg has not conducted an assessment of the ML/TFTF risks facing its financial institutions DNFBPs, and the approach adopted authorises, in many situations, an exemption from any due diligence measure.

- Financial sector supervisory authorities conduct few on-site AML/CFT inspections, and those inspections cover only accounts, to the exclusion of the AML/CFT policies and procedures implemented by institutions. Moreover, at the time of the on-site visit some categories of institutions had never undergone any form of inspection. The sanctions regime is unsatisfactory and in fact no penalty has ever been imposed in AML/CFT matters. Among the non-financial businesses and professions, only the legal and accounting professions are organised and supervised, and they have never been subjected to AML/CFT sanctions.

- Luxembourg has a system for registering legal persons, including non-profit organisations (NPOs). The register is readily accessible, including on-line, without charge. However, it does not reveal the beneficial owners. Some corporations can issue bearer shares; Luxembourg has not taken any steps to prevent their illicit use.

- When it comes to international co-operation, the powers of the authorities are the same as those in domestic matters. However, in most cases, dual criminality is required, and the capacity to co-operate is thus constrained by the gaps identified in the criminalisation of money laundering and terrorist financing.

Legal system and related institutional measures

2. Money laundering is criminalised in Luxembourg by articles 506-1 ff of the Penal Code and by articles 8-1 ff of the Law on the sale of medicinal substances and the fight against drug addiction (LSTUP). The penalty is a prison sentence of one to five years and/or a fine of EUR 1 250 to EUR 1 250 000. Only natural persons are subject to this penalty; legal persons are not held criminally liable in Luxembourg. Related offences are covered by the Penal Code and the LSTUP in a manner consistent with international standards. Those offences include the conversion, placement and concealment as well as the acquisition, possession and use of property; there is however some doubt as to application of the law to the disguising of assets. The definition of property in the Penal Code is consistent with international standards. While Luxembourg law does not require a conviction for the predicate offence in order to prove that the property constitutes the proceeds of the crime, it appears that in practice a conviction for laundering requires proof of the predicate offence and of the link between that offence and the laundered property. This requirement impedes efforts to combat money laundering. When it comes to the predicate offence, Luxembourg has opted for a combination approach embracing the threshold method and a list of serious offences containing a range of offences within each of the categories designated by FATF: terrorism and terrorist financing are not fully criminalised. Finally, there have been eight convictions for money laundering in Luxembourg since 2003. As the assessment team sees it, this small number of convictions and sanctions, and their low level, raise questions about the effectiveness with which the criminalisation of money laundering is implemented.

3. The analysis of Luxembourg's criminalisation of money laundering must be supplemented by the following observations. To begin with, the fact that laundering is not a "stand-alone" crime has been noted above. Second, the assessment team notes that, when the predicate offence has been committed abroad but the money-laundering takes place in Luxembourg, Luxembourg authorities make it a practice to refer the case to the foreign country where the predicate offence took place. The fact is that Luxembourg is a small country with a very important financial centre. Consequently, laundering in Luxembourg typically involves the investment by non-residents of funds obtained from crimes committed abroad. Apart from these elements, the fact that the non-resident launderer is not physically present in Luxembourg is also cited to justify this practice. While this approach may have its merits, in terms of international co-operation and information sharing, it is no proper substitute for effective enforcement of the criminalisation of money laundering. Given its importance, the Luxembourg financial centre is likely to attract capital at risk of being laundered, in particular through non-resident customers. The practice of referring prosecution to the State where the predicate offence was committed, even if this is done on a case-by-case basis, does not appear to send the proper signal to criminals. There are also some questions as to how these referrals are handled in practice. Moreover, it is not clear that Luxembourg actually initiates prosecution of the money laundering offence if it is not prosecuted abroad. Finally, the practice of referring cases to the foreign authority is based on the mistaken notion that proof of the predicate offence is required before laundering can be established.

4. A third point relating to practice should also be mentioned. While the crime of laundering applies to persons who commit the predicate offence, and to their accomplices, it appears that the prosecution often chooses not to pursue the laundering case even though a conviction may be possible for the predicate offence, if the proceeds of that crime have already been confiscated, which is the ultimate purpose of Luxembourg's criminal policy. According to the Luxembourg authorities, it is only in "significant cases" that the predicate offender would be charged with laundering. Jurisprudence shows that the cases where laundering charges are laid involve essentially ordinary crimes rather than financial crimes, and this should raise questions, given the links between laundering and economic crime as a whole. Moreover, the specific criminalisation of laundering as a "stand-alone" offence requires that this criminal conduct be punished in its own right, and indeed the penalties applicable to it in theory are heavy and often exceed those stipulated for the predicate offence.

5. The financing of terrorism is criminalised in article 135-5 of the Penal Code. That article covers the financing of terrorist acts as described in article 135-1, *i.e.* crimes and offences punishable by at least three years' imprisonment, that is crimes or offences punishable by imprisonment of up to at least three years committed with a specific terrorist intent, *i.e.* seriously intimidating a population; unduly compelling public authorities, an organisation or an international body to perform or abstain from performing any act; or seriously destabilising or destroying the fundamental political, constitutional, economic or social structures of a country, an organisation or an international body. With respect to the acts covered by international treaties, the financing of which must be criminalised, Luxembourg has not ratified the 1988 Convention for the suppression of unlawful acts of violence against the safety of maritime navigation or the Protocol to the 1988 Convention for the suppression of unlawful acts against the safety of fixed platforms located on the continental shelf. Moreover, it appears from a review of domestic provisions that not all types of conduct that should be criminalised have been transposed into Luxembourg law, and some measures are incomplete. Nor can these shortcomings be remedied by application of the general provisions of article 135-1, which requires proof of terrorist intent, whereas the acts targeted by the treaties are terrorist acts by definition. The financing of these acts, then, is not properly criminalised under Luxembourg law. The threshold indicated in article 135-1 is furthermore not entirely satisfactory with

regard to scope of application. As well, the crime of terrorist financing does not cover the financing of terrorist organisations and individuals other than when linked to the commission of a terrorist act. The notion of terrorist group does not cover a group consisting of only two persons, and the financing of such a group is therefore not a crime as such. Consequently, terrorist financing does not constitute a complete predicate offence to money-laundering. The penalty for the crime of terrorist financing is imprisonment of 15 to 20 years, or life imprisonment if the terrorist act has resulted in the death of one or more persons; an attempted terrorist act is also punishable. Under Luxembourg law, only natural persons may be held criminally liable. Finally, the effectiveness of the system could not be assessed because, at the time of the on-site visit, no crime involving terrorist financing had been investigated and prosecuted in Luxembourg.

6. Luxembourg's system for confiscating assets is relatively satisfactory with regard to international standards, with the limitation that confiscation of property that was used or intended to be used to commit the offence applies only if the property belongs to the convicted person. The same holds for confiscation of equivalent value, which cannot by applied to property held by third parties. Moreover, confiscation of equivalent value applies only to property that is the direct or indirect proceeds of crime. These two limitations reduce the scope of confiscation. Furthermore, Luxembourg's system is not implemented in an effective manner. Judicial decisions dealing with confiscation show that this measure is imposed only on an exceptional basis in cases relating to laundering and on very accessory property, which does not suggest effective implementation in this area. The links that must be established between the property to be confiscated and the predicate offence illustrate the practical difficulties in imposing a confiscation measure. Moreover, provisional measures relating to property subject to confiscation are inadequate. The freezing of funds by the FIU is conditional upon a prior STR; it therefore only applies to funds and is limited to three months. The Prosecutor's Office (*Parquet*), as the enforcement authority, has no authority to seize assets, except in *flagrant delicto* cases; in any other situations, an examining magistrate must be designated in order to take such a measure. The need to secure a warrant from the examining magistrate in order to obtain documents for tracing funds to be confiscated also entails a fairly cumbersome procedure, subject to conditions that are stricter than those imposed on the *Parquet*.

7. UN Security Council Resolutions 1267 and 1373 and their successor resolutions are applied in Luxembourg through Community regulations 881/2002 of 27 May 2002 and 2580/2001 of 27 December 2001 and their successor regulations. These regulations do not cover all of the situations intended by the Resolutions on which they are based, including the concepts of funds and economic resources controlled, directly or indirectly, by a listed person or entity or by a person acting in their name or at their direction, and the notions of joint ownership, possession and holding.[2] Following rulings by EU Courts in 2008 and 2009, Regulation 881/2002 was annulled for several persons who had originally been listed. New Community regulations have been issued, however, only to remedy this [particular] situation; this was done within the time limit for which the effects of the regulation had been maintained in order to prevent individuals concerned from gaining access to their funds. Nevertheless, given the grounds for those rulings, which revealed intrinsic shortcomings in the Regulation, it is likely that other listed persons and entities will file similar appeals, and indeed some are already pending. The gaps in the European system have not been filled by domestic measures. In the case of Regulation 2580/2001, it contains a list of persons, groups

[2] The EU Council document entitled "Guidelines on implementation and evaluation of restrictive measures (sanctions) in the framework of the EU Common Foreign and Security Policy", a non-enforceable document, gives an interpretation of these provisions which cover all of the cases required by international instruments. This interpretation is furthermore explicitly included in the Council Regulation (EU) 1286/2009 of 22 December 2009, adopted after the review period.

and entities classed in two categories: those with no links abroad, who are not subject to freezing measures but rather to enhanced police and judicial co-operation, and those who have links abroad, whose assets are to be frozen. Luxembourg has no power to freeze funds or other assets of persons or entities other than those covered by Regulation 2580/2001, *i.e.* it cannot freeze the assets of persons and entities other than those designated at the European Union level, or of persons or entities that are nationals of the European Union.

8. The freezing mechanism is applied in practice by the FIU pursuant to article 5.3 of the AML/CFT Law, which requires the prior filing of a suspicious transaction report (STR): this constitutes an additional restriction on the freezing mechanism, which is limited to the freezing of financial assets. The FIU's temporary freezing power (three months), with the need to seek a judicial order, does not guarantee the freezing of assets without delay. Luxembourg has adopted no procedure to supplement the Community mechanism, and it is therefore difficult in practice to understand how and on what basis the above-mentioned blocking could become a freeze measure consistent with Special Recommendation III. There are thus questions as to the effectiveness of Luxembourg's mechanism for freezing terrorist assets. In this matter, communication with financial institutions is handled through circulars, the quality of which is inadequate to allow those institutions to comply with their obligations to freeze terrorist assets, and they are ineffective given the time taken to prepare and distribute them. Generally speaking, Luxembourg has no procedures for de-listing, unfreezing and unblocking funds.

9. The FIU was created by the law of 12 November 2004 on combating money laundering and terrorist financing (AML/CFT Law). The FIU is an integral part of the office of the Public Prosecutor of the District Court of Luxembourg and is composed of its magistrates. It has national competence for receiving STRs. With respect to the analysis of STRs, at the time of the on-site visit it appeared that some of the STRs filed by one financial institution in particular were not being analysed by the FIU, on the presumption that the transactions, deemed suspicious by the financial institution, posed little risk because of their small amount. In fact, those particular STRs represent a significant portion of all the STRs filed by banks. The FIU reports that this gap was remedied after the on-site visit. The FIU has the right to require STR filers to provide any information necessary for analysing suspicious transactions. The Public Prosecutor of Luxembourg performs both the FIU functions and those of the authority that directs preliminary investigations and criminal prosecution. The information is not really disclosed, then, but is used in the investigation and prosecution of offences. The number of investigations opened in the wake of an STR is extremely low, which raises questions about the attention paid to AML/CFT matters in the FIU's processing of STRs and it obviously has an effect on the number of convictions. Because it is located within the Prosecutor's Office and reports directly to the State Prosecutor General and his deputy, the FIU in effect seems to drive the Prosecutor's policy. The FIU is not bound by any "speciality rule:" in practice the magistrates assigned to the FIU will decide, as prosecutors, how to handle cases opened on the basis of an STR, and they will do so in accordance with the objectives of the Public Prosecutor, which are to prosecute all crimes and not only those involving money laundering. The distinction between these two different roles held by the FIU magistrates should be clarified. Finally, the FIU had a staff of six persons handling operational tasks at the time of the on-site visit, a number that seems inadequate in light of the many complementary functions of the FIU magistrates (who moreover investigate criminal cases and must process the many requests received for international co-operation with respect to AML/CFT matters) and the increasing number of STRs. The FIU has been a member of the Egmont Group since its establishment in 1995.

10. The Public Prosecutor of Luxembourg has full jurisdiction to direct investigations and prosecution of ML/TF offences throughout the country. The examining magistrate has the jurisdiction to open an ML/TF investigation at the request of the Public Prosecutor. It seems that very few STRs give rise to an ML investigation and prosecution. This raises questions as to the overall effectiveness of the prosecution system. The authorities responsible for investigations have the prerogatives mentioned in Recommendation 28, but the powers of the Public Prosecutor are limited except in cases of *flagrante delicto*, and money laundering cases are rarely referred to an examining magistrate. Moreover, it is not evident in practice that prosecution authorities use these powers to combat money laundering and terrorist financing, given the very small number of investigations (and the fact that there has never been a TF investigation).

11. The system in place for detecting cross-border transfers of cash and bearer instruments in Luxembourg is governed by EC Regulation 1889/2005, which requires any natural person entering or leaving the Community and carrying cash of a value of EUR 10 000 or more to declare that sum to the competent authorities. In cases where, as a result of Customs controls, a natural person is found to be entering or leaving the Community with an amount of cash less than the threshold established by the regulation but where there are indications of illegal activities associated with this movement, a declaration form may also be required. This declaration system applies only to movements between Luxembourg and countries outside the European Union, and it excludes transport by freight or post. Moreover, Luxembourg Customs officers do not have the power to stop or detain currency and other bearer-negotiable instruments. At the time of the on-site visit, only 12 voluntary declarations had been received by the Luxembourg authorities. None was the subject of information sharing either with EU countries or with third countries, but copies of all declarations are sent to the FIU on a quarterly basis. The sanctions applicable to persons who fail to declare or who provide false declarations are not dissuasive, effective or proportionate. The effectiveness of the system for detecting cross-border movements of cash and bearer-negotiable instruments is not clear, given the low number of declarations made since the system was introduced, and considering the number of passengers entering and leaving Luxembourg.

Preventive measures - financial institutions[3]

12. The ML/TF prevention system in Luxembourg is based on instruments adopted at the level of the European Union, primarily Directive 2005/60/EC and Regulation 1781/2006. The Directive, which is not directly applicable in countries' domestic law, was transposed into Luxembourg law by the amended Law of 12 November 2004 on combating money laundering and terrorist financing (the AML/CFT Law). Under the AML/CFT Law, banks and financial institutions subject to the law are considered equivalent. The same holds for banks and financial institutions subject to the obligations of the Directive or to obligations equivalent to those of the law or those of the Directive, and for which there is supervision. For these purposes, Luxembourg has established, in the Grand-Ducal Regulation of 29 July 2008, a list of countries

[3] On 1 February 2010, Luxembourg adopted a Grand-Ducal Regulation that deals with, in particular, certain Recommendations on preventive measures that financial institutions and non-financial professions should apply. It has not been taken into account in the report, as it was adopted more than two months after the on-site visit.

that are deemed to impose equivalent AML/CFT obligations[4]. To these countries may be added the member countries of the EU/EEA.

13. The AML/CFT Law defines the categories of financial institutions subject to its provisions. It appears that the great majority of financial institutions as defined by the FATF are subject to AML/CFT obligations. Some institutions, such as the managers and advisers of collective investment funds and investment companies in risk capital (SICARs) and insurance (other than life insurance) companies and their intermediaries that engage in credit and surety transactions are not covered. The law introduces a risk-based approach: it requires enhanced due diligence measures when the ML/TF risk is high and allows all CDD measures to be waived in certain listed cases deemed to present a low ML/TF risk, which is not consistent with the FATF methodology. The AML/CFT legislation is supplemented, for purposes of its interpretation and implementation, by circulars issued by the financial sector supervisory authorities: the Financial Sector Supervisory Commission (*Commission de Surveillance du Secteur Financier*, CSSF) and the Insurance Commission (*Commissariat aux Assurances*, CAA). These circulars do not constitute legally binding or enforceable instruments.

14. Luxembourg expressly prohibits the keeping of anonymous accounts and savings passbooks, but the AML/CFT Law does not prohibit the keeping of numbered accounts and accounts in fictitious names. Financial institutions are required to apply due diligence measures in all the cases prescribed by the FATF rules, except in the case of exemptions (see below). They are required by law to identify the customer and to verify the customer's identity in the case of a natural or legal person. On the other hand, they are under no obligation to verify that any person purporting to act in the name of a legal person or legal arrangement is authorised to do so. The law requires financial institutions to identify the beneficial owner, but the obligation of verification is less strict than the FATF standard, according to which financial institutions must take adequate risk-based measures for verifying the identity of the beneficial owner. Financial institutions are not obliged to determine, for all customers (legal persons and natural persons), whether the customer is acting on behalf of another person, and to take reasonable steps to obtain sufficient information to verify the identity of that other person. The law requires financial institutions to conduct ongoing due diligence on customers' transactions and to ensure that documents, data and information collected are kept up-to-date and relevant. This obligation applies only in the context of ongoing due diligence. Financial institutions are obliged to obtain information on the purpose and intended nature of the business relationship. The methods of implementing these obligations, however, are only partially described in the circulars.

15. With regard to reduced or higher risks, Luxembourg has merely transposed the cases stipulated in the Third Directive and it has not evaluated the risks to which its financial institutions are exposed. Thus, the cases in which financial institutions must apply enhanced due diligence are those cited by the Directive, which reflect Recommendations 6, 7 and 8. Apart from these cases, the assessment of the ML/TF risk (and

[4] That list comprises Argentina; Australia; Brazil; Canada; the Dutch overseas territories of Aruba and the Netherlands Antilles; the French overseas territories of French Polynesia, Mayotte, New Caledonia, St. Pierre and Miquelon, Wallis and Futuna; Guernsey; Hong Kong, China; the Isle of Man; Japan; Jersey; Mexico; New Zealand; the Russian Federation; Singapore; South Africa; Switzerland; and the United States. This regulation was repealed on 1 December 2009. Consistent with the evaluation methodology, this report presents the situation as it was at the time of the on-site visit, and two months later. The report therefore takes into account the provisions of the Grand-Ducal Regulation.

hence any application of enhanced CDD in cases of high risk) is left to the institutions themselves. "Simplified due diligence measures" apply to the situation where the customer is a bank or financial institution established in an equivalent country, and customers and products meeting certain strictly defined conditions. However, these are not simplified measures within the meaning of the FATF standards, but rather a blanket exemption from all CDD measures.

16. Luxembourg has adopted measures applicable to politically exposed persons (PEPs), but its criteria are different from those of the FATF. For example, they do not apply to beneficial owners who are PEPs. Moreover, the scope of CDD exemptions is such that financial institutions are excused from due diligence even if the final customer is in fact a PEP. The scope of measures applicable to correspondent banking relations is confined to relations with financial institutions located outside the EU/EEA. Here, as with "payable-through" accounts, financial institutions are subject to a series of obligations, but they are not required to verify whether the institution in question has been the target of ML/TF investigation or action by the supervisory authority. Luxembourg financial institutions are under a general obligation to pay particular attention to any ML/TF threat resulting from products or transactions that favour anonymity, and the AML/CFT Law requires professionals to have in place supplementary CDD measures when entering into a non-face-to-face relationship, but it does not cover transactions where the customer is not physically present.

17. Luxembourg financial institutions are allowed to rely on third parties to conduct CDD measures. As with correspondent banking relations, Luxembourg law grants automatic third-party status to Luxembourg third parties, banks and financial institutions within the meaning of Directive 2005/60/EEC established in the EU/EEA and those in countries listed by the Grand-Ducal Regulation. For entities other than those qualified automatically as third parties, there are requirements relating to registration and equivalence of CDD and recordkeeping obligations, and supervision. The final responsibility for CDD measures remains with the professional who relies on the third party, yet the obligations with respect to transmitting information or copies of measures taken by the third party are not sufficient to guarantee this objective.

18. Financial institutions in Luxembourg are subject to professional secrecy. In AML/CFT matters, professional secrecy is lifted completely with respect to the supervisory authorities (CSSF and CAA) but not with respect to the FIU. This situation raises questions about the FIU's powers. Moreover, private sector representatives interviewed by the assessment team during the on-site visit said that they would analyse a suspicious transaction very thoroughly before reporting it to the FIU for fear of prosecution for violating professional secrecy, the penalty for which is higher than the penalty for failing to file an STR.

19. The obligations of Luxembourg financial institutions with respect to record keeping on transactions and customer identification are largely consistent with the FATF Recommendations. There is however no mention of the fact that the documentation must allow transactions to be reconstructed. The measures applicable to electronic transfers, pursuant to Regulation 1781/2006, are satisfactory in many respects, but supervision of these obligations is inadequate and the penalties applicable are not effective, proportionate or dissuasive.

20. Financial institutions in Luxembourg are required to pay particular attention to complex or particularly large transactions and all unusual kinds of transactions that have no apparent economic or lawful purpose, but they are not obliged to examine such transactions or to document the findings and keep them available for competent authorities and external auditors for at least five years. There is no obligation

for financial institutions to pay special attention in their business dealings and in their transactions with residents of countries that do not apply the FATF Recommendations or do so insufficiently, nor any obligation to examine these transactions, to record their findings, and to make them available to the competent authorities. The only countermeasure legally available to Luxembourg against countries that do not apply the FATF Recommendations, or do so insufficiently, is to issue a grand-ducal regulation making enhanced CDD mandatory. That measure had never been invoked at the time of the on-site visit.

21. Article 5 of the AML/CFT Law requires professionals, their managers and employees to co-operate fully with the Luxembourg authorities responsible for combating money laundering and terrorist financing, and in particular to report any suspicious transactions promptly, without consideration of a threshold or whether the transaction was concluded or merely attempted. However, it is uncertain whether professionals in practice report transactions that might involve fiscal violations, which are not predicate offences to money laundering. With respect to terrorist financing, in addition to the gaps identified in its criminalisation, it appears that, in practice, reporting is limited to transactions involving listed persons. The reporting mechanism does not seem to be effective: the number of STR filings is very low and involves a small number of reporting entities, and the statistics show that many STRs originate not from a suspicion but from the fact that the customer has been investigated or convicted. Moreover, it seems that financial institutions go further than they should in examining the predicate offences for fear of prosecution for violating banking secrecy. As noted above, the penalty for violating banking secrecy is stiffer than that for failing to file an STR. Entities filing an STR, and their employees, enjoy immunity from civil, criminal and disciplinary liability when acting in good faith. They are prohibited from disclosing to the customer concerned or to third parties the fact that an STR has been filed, but this ban does not apply to STRs in the process of being filed. There are a number of exceptions to the ban that are not authorised by the FATF Recommendation, as in the case of international requests for legal assistance and when the customer asks why the transaction was not carried out. The STR guidelines say little about professionals' obligations and include only general indications with respect to money laundering. Feedback is limited to the FIU annual report and acknowledgment of receipt of STRs. Luxembourg has no system for reporting cash transactions, and there is no evidence (apart from a short note dating apparently from 2004, which does not constitute a feasibility study) to show that Luxembourg has considered introducing such a system.

22. Financial institutions are required to institute appropriate and adequate AML/CFT procedures, but the law makes no reference to maintaining or updating these procedures. The issues addressed by these procedures are satisfactory, except for the detection of unusual transactions. Financial institutions (with the exception of insurance intermediaries) are required to have in place an internal control system, in accordance with the sector-specific laws, but there are no AML/CFT details stipulated. The law makes no mention of appointing an AML/CFT compliance officer or the positioning and powers of that officer; these are covered only in the circulars, which are not enforceable instruments. There is no reference to the staffing complement for internal control. There is no law or regulation requiring employee training, and only the circulars call for AML/CFT procedures to be followed when hiring employees. For foreign branches and subsidiaries of Luxembourg financial institutions, the mechanism distinguishes between those located in EU/EEA countries and equivalent countries listed in the Grand-Ducal Regulation, for which financial institutions have no obligation, and those established in other countries. In the latter cases, Luxembourg financial institutions are required to verify that the host country applies AML/CFT provisions equivalent to those in force in Luxembourg, but this relates only to CDD and record keeping obligations. Moreover, the insistence on conformity with Luxembourg standards is not satisfactory, as they themselves are not fully compliant with the FATF Recommendations. There is no specific reference to countries that do not apply the FATF Recommendations or that apply them insufficiently.

23. The Luxembourg system does not allow the establishment of shell banks in Luxembourg, and the AML/CFT Law prohibits banks from establishing or maintaining relations with a shell bank or with a bank known to allow a shell corporation to use its accounts. This is not fully consistent with the Recommendation, which requires that financial institutions be required to "ensure" – and this implies active investigation – that respondent financial institutions in a foreign country do not permit their accounts to be used by shell banks. Moreover, this ban is confined to banks, whereas all financial institutions should be covered.

24. As noted above, most financial institutions in Luxembourg are subject to the AML/CFT Law and they are supervised in their observance of these obligations. The licensing conditions for banks, investment firms and insurance companies were recently revised to include explicit AML/CFT requirements. However, the licensing mechanism cannot prevent criminals' associates, who are not themselves criminals, from holding or being the beneficial owner of a significant or controlling interest in a financial institution. The CSSF is the supervisory authority for banks and financial sector professionals (FSP). The Financial Sector Law (LSF) grants it broad oversight powers for this purpose, including on-site inspections, and allows it to require the submission of all necessary documentation and information. It also has coercive powers. The CAA is the supervisory authority for insurance companies and intermediaries. It conducts on-site inspections but, in contrast to the other areas of its jurisdiction, its powers of enforcement and sanction are not explicitly spelled out in the case of ML/TF.

25. The CSSF and the CAA conduct few on-site inspections, for AML/CFT or other purposes. Controls focus solely on the accounts, to the exclusion of institutions' policies and procedures, and do not include the strategic dimension of overseeing the risk-based approach. Moreover, some categories of financial institutions have never undergone an AML/CFT inspection. Nevertheless, most financial institutions are subject to an annual review of their AML/CFT mechanism by their external auditors, and this covers elements similar to those of CSSF inspections. The auditor's report is a supplementary element to the CSSF's infrequent on-site inspections, but it cannot be considered a substitute.

26. To date, the financial sector supervisory authorities have never imposed any AML/CFT penalty. The CSSF can impose a fine of up to EUR 12 500, which is hardly dissuasive, and the other administrative measures available to it are at the extremes of the sanctions scale (temporary ban on professional activity). They have never been used in AML/CFT matters. The range of sanctions available is therefore not satisfactory. The CAA can apply an acceptable range of sanctions, although the fines for insurance companies and intermediaries are very low. In contrast to the other areas of its jurisdiction, however, its powers of AML/CFT enforcement and sanction are not explicitly spelled out. Finally, among the sanctions imposed by the CSSF and the CAA in other than ML/TF matters none has been made public in full (naming the offender and detailing the offence), and this likely detracts from their dissuasive power. Apart from these sanctions, article 9 of the AML/CFT Law provides for a criminal penalty in the form of a fine ranging from EUR 1 250 to EUR 125 000. No such sanction has ever been imposed, and to do so requires proof of the offender's intent. In fact, most sanctions are applicable only to natural persons, and criminal penalties cannot be imposed on legal persons.

27. Supervisory authorities have issued circulars that provide instructions on practical application of the law, of which they specify certain elements. They merely repeat the law without, for the most part, indicating the supplementary measures that financial institutions should consider in order to implement effectively the AML/CFT measures specific to Luxembourg. They confine themselves to repeating, in an annex, the typologies developed by international agencies, and they contain no description of the ML/TF

techniques and methods found in Luxembourg. The CSSF circular takes no account of the specific features of the different sectors covered. The CAA circular letter is in all respects similar to the CSSF circular, except for certain references that are inapplicable to the insurance industry.

28. A license is required to offer professional services of money or value transfer (MVT) in Luxembourg. Persons and businesses offering MVT services are therefore subject to the same AML/CFT obligations as other Luxembourg professionals. Consequently, all the shortcomings and gaps identified previously, including those with respect to sanctions, are equally applicable to MVT services. The Luxembourg authorities do not actively look for persons or businesses that might be conducting such services illegally, and consequently their presence in Luxembourg cannot be excluded. The authorities maintain, however, that there is little demand for MVT services in Luxembourg.

Preventive measures - designated non-financial businesses and professions (DNFBP)[5]

29. In addition to financial institutions, the following non-financial businesses and professions are subject to the AML/CFT preventive mechanism: company auditors, accountants and accounting professionals, real estate agents established or acting in Luxembourg, notaries and lawyers (in the context of certain activities, consistent with FATF recommendations), persons providing trust and company services, casinos and gaming establishments, and persons trading in goods, to the extent that payments are made in cash in an amount of EUR 15 000 or more. With respect to trust and company service providers, it should be noted that the Luxembourg definition does not cover all the activities listed by FATF, and that in practice these activities are performed by other professions, which are subject to AML/CFT provisions. A person offering trust and company services and who would not otherwise be subject to AML/CFT obligations would be covered by reason of those services, but would not be supervised. It should also be noted that the category of persons trading in goods is very broad and covers dealers in precious stones and metals. With the exception of casinos, all the other categories of non-financial businesses and professions are subject to the same provisions as financial institutions. The shortcomings identified under Recommendations 5, 6 and 8 to 11 in section 3 are thus equally valid for DNFBPs. In the case of casinos, beyond these shortcomings, they are not required to identify the beneficial owner and to take reasonable steps to verify the identity of the beneficial owner.

30. The shortcomings identified under Recommendations 5, 6 and 8 to 11 in section 3 are equally valid for DNFBPs. Furthermore, the obligation to report suspicious transactions is not effectively implemented, in light of the very low number of STRs filed.

31. Casinos are subject to prior authorisation, as are all persons working in them. It is not clear that AML/CFT considerations are taken into account in examining applications for authorisation, either for the casino or for its employees. At present there is only one casino in Luxembourg. It is supervised by the Ministry of Justice, specifically its "gaming police" section, which conducts on-site inspections. The only sanction for violating AML/CFT obligations is the criminal penalty of the AML/CFT Law, which is applicable solely to natural persons. No sanction has ever been ordered to this date.

[5] On 1 February 2010, Luxembourg adopted a Grand-Ducal Regulation that deals with, in particular, certain recommendations on preventive measures that financial institutions and non-financial professions should apply. It has not been taken into account in the report, as it was adopted more than two months after the on-site visit.

32. There is no authority or self-regulatory organisation (SRO) responsible for monitoring and enforcing the AML/CFT obligations of real estate agents, dealers in precious stones and metals, and trust and company service providers other than those subject to the AML/CFT Law under another heading. Lawyers, notaries, accountants and company auditors have the support of a representative organisation endowed with disciplinary powers, but in all cases the law confines itself to giving them the power to oversee their members' observance of their AML/CFT obligations, without further specifying their powers. All SROs have a broad range of disciplinary sanctions available, in addition to the criminal sanction of the AML/CFT Law. No sanction has ever been imposed for an AML/CFT violation. Finally, the non-binding circulars addressed by the different authorities to non-financial businesses and professions have not been updated since the latest amendments to the AML/CFT Law and are often limited to reminding professionals of their legal obligations, without indicating how to comply with them and without considering the risks specific to each profession.

33. In addition to non-financial businesses and professions, Luxembourg has extended the scope of its ML/TF prevention mechanism to natural and legal persons dealing in goods and conducting cash transactions of EUR 15 000 or more as well as to persons providing tax and economic advice. It is not clear that Luxembourg has given further consideration to applying AML/CFT obligations to other professions since the adoption of the 2004 law, or that it is encouraging the development of modern and secure techniques of money management that are less vulnerable to laundering.

Legal persons and arrangements & non-profit organisations

34. Luxembourg has instituted a registration system that appears to cover many if not all legal persons located in the country. The Register of Businesses and Corporations (RCS) and the *Mémorial* (the legal portal of the Grand Duchy), which contain the same information as the RCS, are publicly accessible; both are on-line and free of charge. While the information in the RCS makes it possible to identify the executives of legal persons, it does not guarantee that the beneficial owners will be known in all cases. Moreover, the information reported for registration purposes is not subject to verification. Public companies and partnerships limited by shares can issue bearer shares; Luxembourg has not introduced any system for preventing their unlawful use.

35. When it comes to legal arrangements, there is no requirement to identify and verify the identity of the beneficial owner in accordance with AML/CFT provisions. Moreover, among the natural and legal persons who may be trustees, some are not subject to the AML/CFT Law. In the case of trustees that are subject to the law under another heading (for example, lawyers or notaries), there does not seem to be any oversight of the trust and company services they might provide. There is no oversight at all over service providers who are not the subject to the mechanism under another head. As a result, there is nothing to guarantee that information on the beneficial owner is accurate, adequate and up-to-date.

36. Non-profit organisations (NPOs) are registered under the same conditions as those described above. Luxembourg has not conducted any awareness campaigns among associations and foundations with respect to terrorist finance risks. There is no supervision of NPOs, although certain transactions over EUR 30 000 are subject to control. There is no provision for domestic co-operation or co-ordination. However, a draft law presented before the Chamber of Deputies would bring regulation into line with Special Recommendation VIII.

National and international co-operation

37. Subsequent to the on-site visit, Luxembourg created a committee for the prevention of money laundering and terrorist financing, which should allow all stakeholders to co-ordinate their efforts effectively. However, the committee is unlikely to improve operational co-operation among the competent national authorities, as its role is above all to take a strategic, comprehensive approach in the matter. Co-operation is essentially informal and therefore difficult to assess. The fact that the FIU is part of the Public Prosecutor's office should facilitate information sharing between these two services.

38. Luxembourg has signed and ratified the Vienna and Palermo Conventions and the Terrorist Financing Convention, and has largely implemented them. However, the team's analysis revealed some important gaps in the criminalisation of ML and TF and the sanctions that can be imposed, in confiscation and provisional measures for freezing, blocking and seizing assets, and in the mechanisms for international co-operation, suggesting that application of the conventions is not complete. UN Security Council Resolutions have been implemented through Community regulations (see above).

39. The regime applicable to requests for mutual legal assistance in criminal matters allows Luxembourg to perform a broad range of acts. The powers of investigation and prosecution are the same as those available to the competent authorities in purely domestic affairs. However, except for requests that do not involve coercive measures, dual criminality is a precondition for granting mutual assistance, and this limits Luxembourg's capacity to co-operate because of the gaps identified in the criminalisation of money laundering and terrorist financing. The existence of banking secrecy, as described above, and the appeals that can be lodged against requests may also impede mutual assistance. Finally, co-operation is not possible when the case involves fiscal questions, even accessory ones.

40. With respect to requests received by Luxembourg for confiscating and freezing the proceeds of laundering or predicate offences, Luxembourg authorities have the same powers as those pertaining to the purely domestic context, and those powers are thus subject to the same criticisms formulated above. The condition of dual criminality is likely to constrain Luxembourg's possibilities for cooperating. Various legal provisions apply to the sharing of frozen assets. Finally, Luxembourg has established an asset forfeiture fund, confined to drug trafficking.

41. Dual criminality is also a requirement for extradition, and this constrains Luxembourg's ability to respond to requests, because of the shortcomings in the criminalisation of money laundering and terrorist financing. Apart from requests submitted in the framework of the European arrest warrant, Luxembourg does not extradite its own nationals, yet it is not required to prosecute the offence for which extradition is sought. The assessment team was unable to evaluate the effectiveness of Luxembourg's extradition mechanism as it has never requested extradition in an AML/CFT case, and has received only one request.

42. The FIU shares a wide range of information with its foreign counterparts, in particular under its policy of forwarding laundering cases to the country where the predicate offence took place. However, in light of the doubts already expressed about the emphasis the FIU places on money laundering in its analyses, the assessment team questions whether the information transmitted really focuses on ML/TF aspects. The financial sector's supervisory authorities and the SROs of non-financial businesses and professions are authorised to co-operate in AML/CFT matters, but it is not clear that they actually exchange information with their counterparts.

Resources and statistics

43. Overall, the human, financial and technical resources allocated to the different authorities appear satisfactory. However, the number of magistrates assigned to the FIU is insufficient in light of the many tasks unrelated to the FIU that they must perform, and the steadily rising number of STRs. The CAA and the CSSF seem overall to be well-resourced, but in light of the limited number of AML/CFT inspections the assessment team wonders whether sufficient staff are assigned to on-site control. Moreover, the CSSF and the CAA also examine STRs, something that is scarcely relevant as this is the task of the FIU, which in fact informs the supervisory authorities of any shortcomings it detects in AML/CFT systems. Generally speaking, staff are subject to satisfactory rules of confidentiality and have the appropriate skills. However, the CSSF, in which many of their professional staff members come from the private sector, has not taken steps to deal with potential problems of independence and objectivity among its staff. With the exception of the CSSF and the Customs service, there is need for a major AML/CFT training effort.

44. The AML/CFT authorities generally keep adequate and clear statistics. While those of the FIU sometimes lend themselves to confusion and are difficult to understand and interpret, efforts have been initiated to provide more complete data. With regard to international co-operation, statistics such as those now kept are inadequate for understanding the current situation and they need to be reworked. The time taken to respond to requests is not recorded. Although authorities referred to the exchange of information with their foreign counterparts, no figures were offered on this aspect, except for the FIU. The CAA has not reported any detailed data on the inspections it conducts. Finally, no statistics are kept on the confiscation and freezing of terrorist assets.

TABLES

Table 1: Ratings of Compliance with FATF Recommendations

Table 2-3: Not translated, please see the original French document.

Table 1: Ratings of Compliance with FATF Recommendations

The rating of compliance vis-à-vis the FATF Recommendations should be made according to the four levels of compliance mentioned in the 2004 Methodology (Compliant (C), Largely Compliant (LC), Partially Compliant (PC), Non-Compliant (NC)), or could, in exceptional cases, be marked as not applicable (na).

Forty Recommendations	Rating	Summary of factors underlying rating[6]
Legal system		
1. ML offence	PC	• Terrorism and terrorist financing, predicate offences for money laundering, are not criminalised satisfactorily. • Doubts as to whether the material elements of the offence of money laundering as defined in national legislation apply to disguise. Effectiveness : • The implementation of the laundering offence is not satisfactory, given the low number of convictions for laundering (8 convictions between 2003 and 2009), in light of the importance of Luxembourg financial sector and the laundering risk related to the activities of private banks and of non-resident clientele. • In practice, money laundering is not an independent offence and effectively requires prior proof of the predicate offence and a link between this offence and the laundered proceeds. Furthermore, priority is given at the national level to prosecuting the predicate offence rather than the laundering offence. Finally, when the predicate offence is committed abroad, Luxembourg authorities prefer to refer the laundering activity to the country where the predicate offence took

[6] These factors are only required to be set out when the rating is less than Compliant.

Forty Recommendations	Rating	Summary of factors underlying rating[6]
		place. In this regard, it has not been established that Luxembourg prosecutes [the laundering offence] when the foreign state receiving the referral does not initiate such action.
2. ML offence – mental element and corporate liability	PC	• There is no criminal liability for legal persons, although no fundamental principle of domestic law prevents this. • There are serious doubts about the effectiveness of the sanctions regime in place, given Luxembourg's practice described under R.1, the country's specific situation, and the risks of laundering, as well as the low number of sanctions and level of penalties (prison sentences and fines) imposed.
3. Confiscation and provisional measures	PC	• Among the property used or intended for use in an offence, only those belonging to the perpetrator of the offence may be confiscated. • The same holds for confiscation of corresponding value, which is generally too restricted in its scope of application. • Available provisional measures for blocking/freezing assets are not sufficiently broad and effective. • The procedure for tracing assets is rendered cumbersome by professional secrecy. • The system's effectiveness cannot be tested in the absence of statistics (except those from the FIU) • Confiscation is not used in money laundering cases, despite the risks of laundering in Luxembourg. The links that must be established between the assets and a specific offence are problematic.
Preventive measures		
4. Secrecy laws consistent with the Recommendations	PC	• There is strict professional secrecy which can be invoked against the FIU. • Private sector representatives said they feared prosecution for violating professional secrecy in observance of their reporting and information obligations, and for this reason they carefully consider whether the transaction constitutes a predicate offence before reporting it. • The penalties (fines) incurred by financial institutions for violating their obligations to co-operate are less severe than those incurred for violating banking secrecy. For this reason, it appears that banking secrecy hinders implementation of the FATF Recommendations.

Forty Recommendations	Rating	Summary of factors underlying rating[6]
		• The effectiveness of the system is not demonstrated, given the low number of STRs.
5. Customer due diligence	PC	• Insurance and reinsurance companies and their intermediaries conducting lending and surety activities are not subject to AML/CFT provisions. The same holds for the following financial sector professionals: managers and advisers of collective investment and pension funds, and foreign professionals operating in Luxembourg outside a branch. • There is no legal or regulatory prohibition on holding accounts in fictitious names. • There is no legal or regulatory system for managing numbered accounts and passbooks. • There is no legal or regulatory requirement to verify that any person claiming to act in the name of a customer that is a legal person or arrangement is authorised to do so. • The obligation to verify the identity of the beneficial owner is not consistent with that of the FATF. • There is no obligation to verify whether the customer is acting on behalf of another person and to take all reasonable measures to obtain identification data sufficient to verify the identity of that other person. There has been no analysis of ML/FT risks in Luxembourg. • Consequently, apart from the enhanced CDD measures required by law, the obligation to perform enhanced CDD is limited to the situations deemed by the financial institutions themselves to present a high ML/FT risk. • There are no simplified or reduced CDD measures, but rather an exemption from all CDD. • The exemption covers all CDD measures: identification and verification of the customer and the beneficial owner, information on the nature and purpose of the business relationship, ongoing monitoring. • The exemption is allowed even when there are doubts about the veracity or adequacy of previously obtained customer identification data. • Luxembourg treats banks and financial institutions located in countries of the EU/EEA and those listed by the Grand-Ducal Regulation as equivalent to its own, as well as according to the circulars branches and subsidiaries regardless of their location, and completely exempts its financial institutions

Forty Recommendations	Rating	Summary of factors underlying rating[6]
		from any due diligence regarding these entities. • An exemption from due diligence may be applied to non-residents without there being a condition for such an exemption in all cases that the customer's country of residence respects the FATF Recommendations and applies them effectively. • The effectiveness of the prevention system has not been demonstrated: CDD exemptions apply to a significant portion of financial institutions' activities, producing a small number of STRs in light of the size of the financial sector.
6. Politically exposed persons	PC	• Not all financial institutions are covered. • The definition of PEP is not consistent with that of the FATF: not all important public functions and certain direct family members are not covered with the result that the PEP definition in Luxembourg is more restrictive than that of the FATF. • The enhanced due diligence obligation with respect to PEPs applies only to those PEPs who reside outside Luxembourg. • Lack of a legal or regulatory obligation to have a risk management system for determining whether the beneficial owner is a PEP. • Lack of a legal or regulatory obligation to obtain senior management approval before opening an account. Only "high-level" approval is required without this being specified in an enforceable provision. • There is no obligation to obtain senior management approval to continue a business relationship with a customer who has become a PEP. • The effectiveness of the system has not been demonstrated, given the lack of obligation to determine whether a PEP is the beneficial owner, and the scope of CDD exemptions.
7. Correspondent banking	NC	• Not all financial institutions are covered. • The law regulates correspondent banking relations only with respect to financial institutions located outside the EU/EEA. • The CSSF Circular contradicts the law by extending the legal exemption to financial institutions located in equivalent third countries. • Financial institutions are not required to verify whether the institution concerned has been subjected to ML/FT investigation or

Forty Recommendations	Rating	Summary of factors underlying rating[6]
		regulatory action. • There is no requirement to obtain senior management approval to establish a correspondent banking relationship. • The CSSF Circular is silent as to the implementation of these obligations; their effectiveness of their application cannot be measured.
8. New technologies & non face-to-face business	PC	• Not all financial institutions are covered. • The law does not require financial institutions to adopt policies or have measures to prevent the misuse of new technologies. • One of the supplementary CDD measures that must be taken when entering a non-face-to-face relationship does not allow for satisfactory management of the risks relating to the customer's absence. • There is no provision for transactions that do not involve the physical presence of the customer.
9. Third parties and introducers	PC	• Not all financial institutions are covered (see the introduction to Section 3). • The CSSF Circular and the CAA Circular Letter limit legislative requirements on conditions for granting third-party introducers status to banks and financial institutions of the EU or the EAA by automatically recognising them as third party introducers. • Financial institutions are under no legal or regulatory obligation to ensure that the third party introducer, when established outside Luxembourg, will immediately supply certain elements of the CDD process. • Financial institutions are also under no legal or regulatory obligation to ensure that the third party is able to supply, upon request and without delay, copies of all the documents obtained during the CDD process. • The copies of document that third parties must supply are limited to those relating to identification and verification of customer identity, to the exclusion of information on the nature and purpose of the business relationship.
10. Record keeping	LC	• Not all financial institutions are covered (see the introduction to Section 3). • There is no provision for extending the record keeping requirement beyond 5 years at the request of a competent authority. • The record-keeping obligation does not indicate that the documents kept must allow transactions to be reconstructed.

Forty Recommendations	Rating	Summary of factors underlying rating[6]
		• The obligation to provide documents and information in a timely manner to competent authorities applies only to credit and financial institutions.
11. Unusual transactions	PC	• Not all financial institutions are covered (see the introduction to Section 3). • There is no legal or regulatory obligation to examine the operations covered by Recommendation 11. • There is no legal or regulatory obligation to document the findings of such an examination. • There is no legal or regulatory obligation for making these findings available.
12. DNFBP – R.5, 6, 8-11	NC	• It is uncertain whether securitisation firms, excluded from the scope of the AML/CFT Law, are covered when performing TCSP activities. • The definition of trust and company services is not fully consistent with that of the FATF. • The shortcomings identified under Recommendations 5, 6 and 8 to 11 in Section 3 are also valid for DNFBPs. • In addition, DNFBPs have no obligation to make documents and information available to the authorities on a timely basis. • In addition to the shortcomings identified above, casinos have no obligation to identify the beneficial owner and to take reasonable steps to verify the identity of the beneficial owner.
13. Suspicious transaction reporting	PC	• Not all financial institutions are covered (see the introduction to Section 3). • The obligation to co-operate [with authorities] may fail to function properly due to the fear on the part of the financial sector professional, who has not fulfilled his obligations, that he might incriminate himself. • The FT offence, as a predicate offence for laundering, is not criminalised in accordance with Special Recommendation II. • It is unclear whether professionals are in practice authorised to report transactions that might involve tax offences that are not predicate offences to ML. Effectiveness: • The number of STRs is very low, distributed among a small number of reporters, and the statistics show that many STRs are motivated not by suspicion but by the fact that the customer has been investigated or convicted.

Forty Recommendations	Rating	Summary of factors underlying rating[6]
		• With respect to terrorist financing, the obligation is in practice limited to reporting transactions involving listed persons. • Moreover, it appears that financial institutions go further than normally necessary in examining the underlying offence.
14. Protection & no tipping-off	PC	• The tipping off prohibition only covers STRs that have already been submitted. • There are numerous exceptions to the tipping off ban which are not authorised by the Recommendation, in the case of international legal assistance requests and when the customer asks why the transaction was not carried out. • No sanctions were imposed for violations of tipping off detected in 2007 and 2008.
15. Internal controls, compliance & audit	PC	• Not all financial institutions are covered (see the introduction to Section 3). • Compliance is not required by the law or any other binding instrument, but only by the circulars issued by the supervisory authorities. • Legislative provisions governing internal control make no mention of ML/FT. • Only the non-binding circulars mention appropriate employee hiring procedures, and they provide no details as to what these procedures should include.
16. DNFBP – R.13-15 & 21	NC	• It is uncertain whether securitisation firms, excluded from the scope of the AML/CFT Law, are covered when performing TCSP activities. • The shortcomings identified under Recommendations 13, 14, 15 and 21 in Section 3 are also valid for DNFBPs. • No effective implementation given the very low number of reports.
17. Sanctions	NC	• Not all financial institutions are covered (see introduction of section 3) • The fine thresholds (criminal and administrative) are too low to be dissuasive or proportionate. • Apart from withdrawal of license, the administrative sanctions and other measures available to the CSSF are not applicable to legal persons. • The range of sanctions available to the CSSF is not broad enough (fine or prohibition of activity). • There are doubts about the applicability of

Forty Recommendations	Rating	Summary of factors underlying rating[6]
		CAA sanctions to the violation of AML/CFT obligations. • Having never been applied, the sanctions regime is not effective or dissuasive.
18. Shell banks	LC	• Only banks, and not all financial institutions in Luxembourg, are prohibited from establishing and maintaining correspondent banking relationships. • There is no requirement to ensure that the respondent banks do not allow shell banks to use their accounts.
19. Other forms of reporting	PC	• With the exception of a short note dating from 2004 and not in and of itself constituting a study, there is no evidence to show that Luxembourg has considered introducing a system for reporting cash transactions.
20. Other NFBP & secure transaction techniques	PC	• It is not clear that Luxembourg has given further thought, since the AML/CFT law came into force in 2004, to subjecting other non-financial businesses and enterprises to AML/CFT provisions. • It is also not clear that Luxembourg is encouraging the development of modern and secure techniques for conducting transactions that are less vulnerable to the risk of money laundering.
21. Special attention for higher risk countries	NC	• Not all financial institutions are covered (see the introduction to Section 3). • There is no obligation for financial institutions to pay special attention in their business dealings and in their transactions with residents of countries that do not apply the FATF Recommendations or do so insufficiently. • There are no effective measures for advising financial institutions of weaknesses in the AML/CFT systems of certain countries. • There is no obligation to examine the operations covered by Recommendation 21 and to document the findings. • There is no legal or regulatory obligation to document the findings of such an examination. • The counter-measures foreseen by the law are insufficient. • In the absence of counter-measures visible, the system is ineffective.
22. Foreign branches & subsidiaries	PC	• Not all financial institutions are covered (see the introduction to Section 3). • EU/EEA countries and countries listed in the Grand-Ducal Regulation are considered as

Forty Recommendations	Rating	Summary of factors underlying rating[6]
		equivalent; institutions are not required to determine whether the obligations of these countries are consistent with those of Luxembourg and the FATF Recommendations. • AML/CFT measures are limited to CDD and record keeping obligations. • There is no mention of countries that do not apply the FATF Recommendations or that do so insufficiently.
23. Regulation, supervision and monitoring	PC	• Not all financial institutions are covered (see introduction of section 3) • There are no obligations to prevent criminals' associates from holding or being the beneficial owner of a significant or controlling interest in a financial institution. • There is no oversight strategy allowing the competent authorities to assess or review the procedures adopted by financial institutions to determine and manage the level of risk or to examine the decisions taken by these institutions. • With the exception of credit institutions and collective investment funds, the CSSF has no inspection plan. • The CSSF carries out no inspections of any financial institutions other than credit institutions and collective investment funds. • The number and quality of AML/CFT inspections by the authorities is insufficient. • CSSF inspections do not cover institutions' AML/CFT internal procedures and policies. • The AML/CFT provisions on licensing procedures applicable to financial institutions and insurance companies came into force only recently and their effectiveness has not been tested.
24. DNFBP - regulation, supervision and monitoring	NC	• It is uncertain whether securitisation firms, excluded from the scope of the AML/CFT Law, are covered when performing TCSP activities. • There is no supervision for real estate agents, dealers in high-value goods and providers of trust and company services, apart from those covered under other activities. • There are serious doubts about enforcement powers and consequently no penalties for registered auditors, lawyers, notaries and accountants who breach their AML/CFT obligations. • In the absence of sanctions and evidence of controls conducted and their results,

Forty Recommendations	Rating	Summary of factors underlying rating[6]
		effectiveness has not been demonstrated.
25. Guidelines & Feedback	PC	Financial Institutions: • The STR guidelines say little about professionals' obligations and include only general indications with respect to money laundering. • Feedback is limited to the FIU annual report and acknowledgment of receipt of STRs. • Guidelines are not tailored to the various sectors of financial institutions' activities in Luxembourg and do not indicate the measures that institutions should take to meet their AML/CFT obligations effectively. DNFBPs: • No profession has updated guidelines reflecting the latest amendments to the AML/CFT Law. • The existing guidelines are not binding, but merely recall obligations without indicating how they should be applied and without considering the specific risks to which non-financial businesses and professions are exposed.
Institutional and other measures		
26. The FIU	LC	• At the time of the on-site visit, not all STRs were being analysed. • The quality of the annual report, in particular its confusing statistics and the absence of money laundering typologies. Effectiveness • The FIU's lack of specialisation, the fact that it is composed almost exclusively of prosecuting magistrates and its location within the Public Prosecutor's Office prevent it from focusing on ML/FT offences. • Apart from their FIU functions, its magistrates perform other functions relating to investigations and the execution of international mutual assistance requests in which money laundering has been designated by the requesting authority or where there is a link with a file prepared by the FIU, which interferes with their primary function of analysing STRs. • Lack of effectiveness of the system, as evidenced by the low number of cases giving rise to investigation, prosecution and conviction for ML/TF matters
27. Law enforcement authorities	PC	• The authorities designated for investigations focus their efforts on the predicate offences and not on ML/FT violations.

Forty Recommendations	Rating	Summary of factors underlying rating[6]
		• The effectiveness of the system, given the small number of money laundering investigations (no terrorist financing investigations.
28. Powers of competent authorities	LC	• Apart from *flagrant delicto* cases, the prosecutor's powers are very limited and (effectiveness) the examining magistrate is involved only rarely in ML/FT cases.
29. Supervisors	LC	• The AML/CFT control and sanctioning powers of the CAA are not explicitly described in law and there is a theoretical risk that their legality could be challenged. • The range of sanctions available to the CSSF is not broad enough and sanctions, apart from withdrawal of license, do not apply to legal persons. • The amounts of fines (disciplinary and administrative) are too low to be dissuasive.
30. Resources, integrity and training	PC	• The FIU and the supervisory authorities are short-staffed (supervisory authorities for on-site AML/CFT inspections). • The CSSF has not adopted a procedure for addressing potential problems with the independence and objectivity of its staff. • With the exception of Customs and the CSSF, AML/CFT training is inadequate and disorganised.
31. National co-operation	PC	• The effectiveness of the recently-created AML/CFT committee could not be tested. • The mechanisms of operational cooperation and coordination are essentially informal and their effectiveness could not be assessed.
32. Statistics	PC	• The available statistics on STRs drawn from the successive annual reports of the FIU are confusing and hard to understand and interpret. • It is only since 2008 that Luxembourg has been keeping statistics on the prosecution of predicate offences. • When it comes to mutual legal assistance and other international requests for cooperation, the statistics initially reported by Luxembourg were not understandable and had to be reformulated. The same holds for the shared information obtained or received spontaneously by the FIU. • No statistics were offered on information sharing between supervisory authorities. The CAA did not provide detailed data on its inspections. • There is no data on confiscations or on frozen

Forty Recommendations	Rating	Summary of factors underlying rating[6]
		terrorist assets.
33. Legal persons – beneficial owners	PC	• The RCS does not make it possible to know the beneficial owner of legal persons in all cases. • There is no mechanism to guarantee that the information contained in the RCS is accurate and up-to-date. • There is no appropriate measure to ensure transparency with respect to the shareholders of public companies and partnerships limited by shares that have issued bearer shares.
34. Legal arrangements – beneficial owners	NC	• For trust and company service providers subject to the AML/CFT law under another head, it is not clear that those services are supervised. • Trust and company service providers subject to the AML/CFT law under this head alone are apparently not supervised. • The information is accessible only in the course of criminal proceedings. • The mechanism is not effective, as identification of trusts and their beneficial owner is not systematic.
International Co-operation		
35. Conventions	PC	<u>Vienna Convention :</u> • The laundering offence does not appear to cover disguise. • Confiscation and freezing measures are limited to assets used or intended for use in committing an offence and belonging to the convicted offender; the same is true for confiscation of corresponding value which is too restrictive in its scope of application. • Inadequate provisional measures and powers for effective confiscation, seizure and freezing of assets. <u>Palermo Convention:</u> • The laundering offence of does not cover disguise. • Legal persons are not criminally liable. • Confiscation and freezing measures are limited to assets used or intended for use in committing an offence and belonging to the convicted offender; the same is true for confiscation of corresponding value which is too restrictive in its scope of application. • Inadequate provisional measures and powers for effective confiscation, seizure and freezing of assets. <u>Terrorist Financing Convention</u>:

Forty Recommendations	Rating	Summary of factors underlying rating[6]
		• Not all of the terrorist acts intended by the Convention are criminalised. • The crime of terrorist financing does not cover the financing of individual terrorists or groups apart from commission of a terrorist act. • Inadequate provisional measures and powers for effective confiscation, seizure and freezing of assets.
36. Mutual legal assistance (MLA)	LC	• The dual criminality requirement limits Luxembourg's ability to grant mutual legal assistance because of the gaps identified with respect to the ML and TF offences. • Professional secrecy and notification/appeal procedures can prejudice the effectiveness of responses to requests. • The Law of 8 August 2000 on co-operation in criminal matters does not allow co-operation on accessory fiscal issues and, generally, the data exchanged may not be used for tax purposes, even accessory ones. • Execution times seem relatively long (six months)
37. Dual criminality	C	
38. MLA on confiscation and freezing	LC	• The asset forfeiture fund is confined to drug trafficking. • The dual criminality requirement limits Luxembourg's ability to freeze, seize and confiscate because of the shortcomings identified in criminalisation and in implementation of Recommendation 1 and Special Recommendation II. • The same holds for the shortcomings identified concerning R3 and SR III.
39. Extradition	LC	• Law of 20 June 2001: Luxembourg refuses to extradite its nationals but does not undertake to prosecute the offence for which extradition is sought. • Law of 17 March 2004: Luxembourg may refuse to extradite its nationals without undertaking to prosecute the offence for which extradition is sought. • The dual criminality required by the Law of 20 June 2001 limits Luxembourg's ability to grant extradition because of the shortcomings identified in the criminalisation and prosecution of the laundering offence.
40. Other forms of co-operation	LC	• Given the criticisms about the AML/CFT orientation of the FIU's analytical work, it seems in consequence also doubtful that the information provided by the FIU focuses on

Forty Recommendations	Rating	Summary of factors underlying rating[6]
		ML/TF. • The effectiveness of the information exchange system has not been demonstrated for the CSSF, the CAA and the self-regulatory organisations.
Nine Special Recommendations	**Rating**	**Summary of factors underlying rating**
SR.I Implement UN instruments	PC	Terrorist Financing Convention: • Not all the terrorist acts of the Convention are criminalised. • The crime of terrorist financing does not cover the financing of individual terrorists or groups apart from commission of a terrorist act. • Legal persons are not criminally liable. UN resolutions • Not all the funds and other assets targeted by the Resolutions are covered by the Community regulations. • Freezing pursuant to S/RES/1373/2001 is limited to the non-Community persons and entities designated by Regulation 2580/2001. • Regulation 881/2002 has been annulled with respect to several persons and entities on the UN list. Its effects have been maintained temporarily, but it appears that other persons are likely to obtain annulment with respect to themselves. • There are no domestic procedures for (i) supplementing the Community mechanism and (ii) ensuring effective implementation of the mechanism. • Doubts about the effectiveness of the system and whether the freezing of funds and other assets is immediate.
SR.II Criminalise terrorist financing	PC	• The terrorist financing offence does not cover all the types of conduct targeted by the international conventions and protocols cited by the Convention on terrorist financing. • The terrorist financing offence does not cover the financing of terrorist organisations and individuals beyond the commission of an act of terrorism. • The notion of terrorist group does not cover a group formed by two persons, and therefore the financing of such a group is not a crime as such. • In the absence of a complete offence consistent with SR II, the financing of terrorism constitutes an incomplete predicate offence for money laundering. • There is no criminal liability for legal persons,

Forty Recommendations	Rating	Summary of factors underlying rating[6]
		although no fundamental principle of domestic law prevents this. • The effectiveness of the system cannot be tested in the absence of prosecution of terrorist financing.
SR.III Freeze and confiscate terrorist assets	PC	• There is uncertainty as to the continued effect of Regulation 881/2002 in light of the annulments ordered for certain persons listed in it. • The regulations do not cover all the funds and other assets referred to in resolutions S/RES/1267/1999 and 1373/2001. • The freezing possibilities pursuant to S/RES/1373/2001 are limited to persons and entities designated by Regulation 2580/2001. With respect to persons who have no link to a country outside the European Union, the measures are limited to enhanced police and judicial co-operation. • Lack of any procedure for de-listing or for unfreezing funds and other assets, unblocking funds and other assets frozen inadvertently, or accessing frozen funds and other assets under certain conditions. • Inadequate procedures for financial institutions and other persons liable to be holding terrorist assets. • Lack of monitoring of the implementation of the European regulations and impossibility to sanction. • The deficiencies identified under R.3 also apply to the freezing, seizure and confiscation of terrorist assets other than through the application of Resolutions 1267 and 1373. • Lack of effectiveness, and there are serious doubts that terrorist funds and other assets will be frozen without delay and on a continuing basis.
SR.IV Suspicious transaction reporting	NC	• Terrorist financing is not criminalised in accordance with SR II. • The obligation to co-operate [with authorities] may fail to function properly due to the fear on the part of the financial sector professional, who has not fulfilled his obligations, that he might incriminate himself. • The effectiveness of the system has not been established: in practice only transactions involving listed persons are reported to the FIU, and the number of STRs relating to terrorist financing is low.

Forty Recommendations	Rating	Summary of factors underlying rating[6]
SR.V International co-operation	PC	Mutual legal assistance: • The shortcomings identified under Recommendations 36 and 38 also apply in the framework of Special Recommendation V. • The dual criminality requirement limits Luxembourg's possibilities to grant mutual assistance because of the shortcomings identified in criminalisation of TF and implementation of Special Recommendations II and III. • There is no specific co-ordination mechanism or any fund or procedures for sharing seized assets. Extradition: • The shortcomings identified under Recommendation 39 are also applicable in the framework of Special Recommendation V. • The dual criminality required by the Law of 20 June 2001 limits Luxembourg's ability to grant extradition because of the shortcomings identified in implementation of Special Recommendation II. • In the absence of actual cases of terrorist financing, the overall effectiveness of the extradition system cannot be verified. Other forms of international cooperation: • With the exception of the FIU, it is not demonstrated that Luxembourg is sharing information on TF.
SR VI AML requirements for money/value transfer services	PC	• The shortcomings identified for the different recommendations and described throughout section 3 apply equally to MVT services. • There is no mechanism for detecting MVT services operating without a license.
SR VII Wire transfer rules	PC	• There is no provision, in the case of an intra-Community transfer, to make complete data on the payer available to the competent authorities within three days, and immediately to the law enforcement authorities. • Supervision is inadequate. • The penalty for failure to fulfil the obligations of the regulation is not proportionate, effective and dissuasive.
SR.VIII Non-profit organisations	PC	• There is no outreach program with associations and foundations. • There is no supervision, and oversight is limited to certain transactions exceeding EUR 30 000.

Forty Recommendations	Rating	Summary of factors underlying rating[6]
		• There is no comprehensive system of sanctions. • There is no provision for domestic cooperation and coordination.
SR.IX Cross Border Declaration & Disclosure	NC	• The system is limited to movements beyond the EU and does not cover shipments by freight, mail or legal persons. • Customs does not have powers to stop or restrain. • Domestic co-ordination and international co-operation are inadequate • Lack of dissuasive, effective and proportionate sanctions. • There are doubts as to the effectiveness of the system, in light of the low number of declarations.