

# CSSF Circular 18/698: clarifications relating to combatting money laundering and terrorist financing

Insights - 14/03/2019

## Background

With circular 18/698 of 23 August 2018 on (i) the authorisation and organisation of Luxembourg investment fund managers, and (ii) provisions on combatting money laundering and terrorist financing applicable to investment fund managers and entities carrying out the function of registrar agent (the **Circular**), the Commission de Surveillance du Secteur Financier (**CSSF**) provides clarifications and, to some extent, introduces new requirements aimed at increasing transparency in the fight against money laundering and terrorist financing.

This briefing focuses particularly on the anti-money laundering and combating the financing of terrorism (**AML / CFT**) provisions set out in sub-chapter 5.4 of the Circular.

By way of background, the fifth anti-money laundering Directive (EU) 2018/843 of 30 May 2018 (the **5<sup>th</sup> AML Directive**) amending Directive (EU) 2015/849 of the European Parliament and the Council of 20 May 2015 (the **4<sup>th</sup> AML Directive**) was published in the Official Journal of the European Union on 19 June 2018 and entered into force twenty days thereafter. Member States are required to implement the fifth AML Directive into national law by 10 January 2020.

The 4<sup>th</sup> AML Directive partly transposed into Luxembourg legislation amongst others by (i) the law of 13 February 2018 widening obligations as regards the fight against money laundering and terrorist financing for in-scope professionals and (ii) the law of 10 August 2018 on the identification of beneficial owners of trusts, both amending the law of 12 November 2004 on the fight against money laundering and terrorist financing (the **AML Law**). The Luxembourg AML/CFT legislative framework is complemented by other laws and regulations as well as AML/CFT circulars<sup>[1]</sup> (the **AML/CFT Regulations**) regularly released/updated by the CSSF and addressed to professionals and entities subject to its supervision, such as the Circular.

The Circular is addressed to Luxembourg investment fund managers (hereinafter **IFMs**)[2]. Thus, both UCITS management companies and authorised AIFMs are captured. However, alternative investment fund managers subject to article 3 of the Luxembourg law of 12 July 2013 on alternative investment fund managers (the **2013 Law**) and not mentioned in the list of IFMs set out in the Circular are expressly out of scope[3].

It is noteworthy that certain provisions of the Circular relating to AML/CFT apply not only to IFMs but also to registrar agents.

Since the Circular entered into force on 23 August 2018 with immediate effect[4], market participants captured by the Circular should, to the extent not already complied with, immediately undertake efforts to comply in full with these requirements.

## Outline of AML / CFT Regulations' requirements

Sub-chapter 5.4 of the Circular clarifies the general framework and obligations to which IFMs and registrar agents are subject with respect to AML/CFT. It is divided into two sections:

- section 5.4.1 outlines the general framework applicable to IFMs irrespective of the functions they exercise pursuant to annex I of the 2013 Law; and
- section 5.4.2 relates to obligations applicable to IFMs (and/or registrar agents) depending on the manner in which the relationships with intermediaries involved in the marketing of the funds and/or such registrar agents are organised.

### Section 5.4.1

In a nutshell, the AML/CFT requirements specified in the Circular are as follows:

- any IFM must be vigilant and comply with AML/CFT Legislation in force from time to time. In this respect, the IFM must be in the position to implement and comply with new AML/CFT requirements as soon as they become applicable. Compliance with AML/CFT obligations must be subject to regular controls at a frequency determined in accordance with the risks to which the IFM is exposed and at least each time such obligations change;
- the CSSF not only encourages IFMs to follow publications regularly issued by the Financial Action Task Force (the **FATF**), but also, requires IFMs to follow the "Guidance for the Securities Sector" issued by FATF in October 2018;
- it is reminded that any IFM providing management services and other ancillary services listed in article 101(3) a) of the 2010 Law or article 5.4 of the 2013 Law are required to take appropriate measures to identify and monitor risks[5] of money laundering and terrorist financing to which it is exposed and take efficient measures to mitigate those risks;

- due diligence measures to be implemented by the IFM not only with respect to its clients, but also vis-à-vis its delegates (portfolio managers, investment advisors), the sponsors of the investment funds and the assets of those funds are specified. Enhanced due diligence measures are required with respect to nominees and other intermediaries subscribing for securities on behalf of clients;
- it is reminded that IFMs must appoint an AML/CFT compliance officer at the senior management level (the **Senior AML/CFT Compliance Officer**) and may, based on the principle of proportionality, be required to appoint an officer responsible for compliance with professional obligations with regard to AML/CFT. The CSSF clarifies that such functions must be exercised by qualified persons (i) having sufficient expertise and knowledge of the European and Luxembourg AML/CFT legislative and regulatory framework, (ii) in the position to dedicate a sufficient part of their time to their duties, (iii) resident in or able to travel on a daily basis to Luxembourg, and (iv) employed by the IFM. Any change in the aforementioned persons must be communicated in advance to the CSSF;
- on a yearly basis, the Senior AML/CFT compliance Officer is required to draw up a synthesis report on the IFM's compliance with the professional obligations relating to AML/CFT. The Circular specifies the items to be covered in this report<sup>[6]</sup>. Notably, where the IFM relies on third-parties to perform AML/CFT professional obligations, the results of the checks carried out on the compliance of the services provided by those third parties with applicable legal and regulatory AML/CFT requirements and the terms of the contract with such third parties, must be included in the report. Further the reasons of any change in the appointed delegates must be reported to the CSSF.

**Note:** The report must be submitted to the IFM's governing body for approval and filed with the CSSF within five months following the end of the financial year concerned. It is further noted that on a yearly basis, the internal audit function is also required to report to the IFM's governing body and the authorised management on compliance with the AML/CFT Legislation and must ensure that its recommendations and corrective measures are implemented.

## Section 5.4.2

This section of the Circular lays down four different scenarios and rules in respect of AML/CFT obligations depending on the manner in which the relationships with the IFM, the intermediaries involved in marketing and the registrar agent are organised<sup>[7]</sup>. For each of the scenarios, the CSSF specifies the obligations required to be assumed by IFMs (and/or registrar agents) and the level of duty of care to be performed by either according to whether they have direct or indirect relationships with investors, marketing intermediaries or carry out the registrar agent function.

- Scenario A: the IFM is in direct relationship with intermediaries and/or investors and is also acting as registrar agent.

The IFM is required to (i) implement and perform due diligences measures on those intermediaries and/or direct investors, (ii) enter into a written agreement with those intermediaries and (iii) provide a list of all intermediaries with whom the IFM has direct relationships to the CSSF on an annual basis[8].

In addition the IFM is required to establish appropriate ongoing measures to ensure that those intermediaries in turn comply with the provisions referred to in section 5.4.2 of the Circular[9].

Finally it is to note that as regards the AML/CFT obligations of the IFM acting also as registrar agent, the CSSF reminds that the obligations are the same as those set out in paragraphs 323 to 331, with the exception of paragraphs 324, 325, 330 a) and b) of the Circular, which are not applicable in this context.

- Scenario B: the IFM is in direct relationship with intermediaries and/or investors and the registrar agent function has been delegated to registrar agent(s).

With respect to intermediaries and investors with whom the IFM has direct relationships the IFM is required to comply with the requirements of paragraphs 323 to 331 of the Circular as summarized above.

As regards the relationship between the registrar agent and the IFM, the latter is required to comply with the provisions referred to in Chapter 6 of the Circular, in particular section 6.2.2[10], 6.2.3[11] and 6.2.4[12]. Pursuant to section 6.2.2, the registrar agent and the IFM must enter into a written agreement which shall determine the respective responsibilities of both parties in terms of compliance with AML/CFT obligations and shall contain clauses requiring both parties to make available to the other all necessary information they need to comply with their own AML/CFT obligations.

- Scenario C: the IFM has no direct relationship with intermediaries and/or investors and the registrar agent function has been delegated to registrar agent(s).

Similarly to scenario B, as regards the relationship between the registrar agent and the IFM, the latter is required to comply with the provisions referred to in Chapter 6 of the Circular, in particular section 6.2.2, 6.2.3 and 6.2.4.

The agreement between the registrar agent and the IFM shall notably determine their respective responsibilities in terms of compliance with AML/CFT obligations, including the provisions of paragraphs 323 to 331, with the exception of paragraphs 324, 325, 330 a) and b) of the Circular, which are not applicable in this context.

- Scenario D: the IFM carries out neither the marketing function nor that of registrar agent.

The IFM is required to establish appropriate measures to ensure compliance with AML/CFT obligations as specified in section 5.4.1 of the Circular. In this context, the agreement between the IFM and the investment fund shall contain clauses requiring the governing body of the fund to make available to the IFM all necessary information it needs to comply with its AML/CFT obligations.

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[1] such as, without limitation, the law of 27 October 2010 implementing in particular United Nation Security Council resolutions and acts adopted by the European Union regarding prohibitions and restrictive measures in financial matters, Grand Ducal Regulation of 1 February 2010, CSSF regulation n° 12-02, Circular 10/495, Circular 13/556, Circular 17/661 on the adoption of the joint guidelines issued by the three European Supervisory Authorities (EBA/ESMA/EIOPA) on money laundering and terrorist financing risk factors, Circular 18/684 etc.

[2] Pursuant to the Circular, IFM mean (i) management companies subject to chapter 15 and article 125-1 or 125-2 of chapter 16 of the Luxembourg law of 17 December 2010 on undertakings for collective investment, as amended (hereinafter the "2010 Law"), (ii) Luxembourg branches of IFM subject to chapter 17 of the 2010 Law, (iii) self-managed subject to article 27 of the 2010 Law, (iv) alternative investment fund managers authorised according to chapter 2 of the Luxembourg law of 12 July 2013 on alternative investment fund managers (hereinafter the "2013 Law") and (v) alternative investment funds internally managed.

[3] IFMs established in Luxembourg (i) in so far as they manage one or more AIFs whose only investors are the IFM or the parent undertakings or the subsidiaries of the IFM or other subsidiaries of those parent undertakings, provided that none of those investors is itself an AIF, (ii) which either directly or indirectly, manage portfolios or AIFs whose assets under management, including any assets acquired through use of leverage, in total do not exceed a total threshold of EUR 100,000,000, (iii) which either directly or indirectly, manage portfolios of AIFs whose assets under management in total do not exceed a threshold of EUR 500,000,000 when the portfolios of AIFs consist of AIFs that are unleveraged and have no redemption rights exercisable during a period of five years following the date of the initial investment in each AIF, and (iv) multilateral development banks exercising the activity of a management company pursuant to chapter 18 of the 2010 Law, are excluded.

[4] Paragraph 621 of the Circular.

[5] By taking into account *a minima* certain risks factors, notably the clients, countries or geographical zones, products, services, transactions or distribution channels.

[6] Paragraphs 318 and 319 of the Circular.

[7] It being understood that one and the same IFM may be found in several of the scenarios

identified.

[8] Paragraphs 323 to 325 of the Circular. The list required by point 325 of the Circular must be provided to the CSSF within five months following the end of the IFM's financial year.

[9] Paragraphs 326 to 328 of the Circular.

[10] Section 6.2.2 : Obligation to conclude a contract.

[11] Section 6.2.3 : Initial due diligence and ongoing monitoring of delegates.

[12] Section 6.2.4 : Specifics on ongoing monitoring.

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