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**COMMITTEE ON THE PREVENTION OF  
MONEY LAUNDERING AND TERRORIST FINANCING**

**DOC. N° 06/FEB/3 REV.1 – 15.2.2006**

**Working document on possible implementing measures to Directive 2005/60/EC of the European Parliament and of the Council of 26 October 2005 on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing**

**INVITATION FOR PUBLIC COMMENT**

DG Internal Market services are making public a Working Document related to Chapter VI of Directive 2005/60/EC of the European Parliament and of the Council on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing. Chapter VI of this directive provides for the adoption of **implementing measures** by the Commission.

This working document is available on the European Commission's website. Publication of this Working Document is part of the open and transparent regulatory process the Commission follows for drawing up technical implementing measures in the financial area (see recital 47 of the Directive).

**This Working Document is therefore informal and not definitive. It does not have the status of a Commission official draft for implementing measures and is without prejudice to any final decisions that might be taken by the Commission in this area. The Commission may in particular decide not to take measures at all.** The document covers only part of the possible implementing measures that the Commission is entitled to adopt.

Since this working document is not a formal Commission proposal, **the period for the Committee on the Prevention of Money Laundering and Terrorist Financing to vote on the measures, and for the European Parliament to consider them, is not triggered at this stage.**

**Any comments on this working document should be sent to the Commission to the following e-mail address by 16 March 2006:** Markt-F2@cec.eu.int (with the mention "money laundering"). All comments sent to the Commission may be made public and posted on the above-mentioned website, unless authors specifically request the contrary.

# Introduction

**Directive 2005/60/EC**<sup>1</sup> (the so-called Anti-Money Laundering Third Directive) entered into force on 15 December 2005. Article 40 of this Directive provides for the adoption of implementing measures by the Commission in order to complete the legal framework created by the Directive. The novelty of this empowerment is that in respect of two issues (i.e. simplified customer due diligence and occasional or very limited financial activity), the Council and the European Parliament have imposed on the Commission to adopt implementing measures before 15 June 2005.

**The Commission services made public on 12 September 2005 a working document containing a general orientation** with regard to the possibility to adopt implementing measures in this field. In particular, it prioritised the subjects, proposing to concentrate, at this stage, on those measures that are regarded as essential for the effective entry into force of the Directive. This working document called for the opinion of interested parties on a series of possible proposals in relation to the different subjects addressed; notably the definition of a politically exposed person, the simplified customer due diligence procedures, the definition of the financial activities carried out on an occasional or very limited basis. The opinion of interested parties was also requested on the treatment of third countries and other issues.

**Around 30 replies were received following that public consultation to the public.** Overall, respondents provided a broad support to the line proposed. Suggestions for improvements and/or modifications of this line were also made. Both a summary of the replies as well as copies of the replies received are available on the website of DG Internal Market and Services.

Following this consultation and several discussions at the Money Laundering Contact Committee with the Member States, DG Internal Market and Services prepared **a working document containing draft legislative language on possible implementing measures to this Directive.** This draft was limited to: (1) the clarification of what should be understood by "politically exposed person"; (2) strictly defined technical criteria allowing to derogate from the normal customer due diligence procedures in relation to certain types of low risk customers, products and transactions; and (3) technical criteria for assessing whether it is justified not to apply the directive to persons carrying out a financial activity on an occasional or very limited basis. This text is a revised version of the earlier draft following the discussions at the Committee for the Prevention of Money Laundering and Terrorist Financing of 8 February 2006.

The draft language in this working document is necessarily limited to those aspects for which the Commission is empowered to adopt implementing measures and cannot therefore deal with possible supporting initiatives such as guidance papers or similar proposals that were addressed in the previous consultation paper.

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<sup>1</sup> Directive 2005/60/EC of the European Parliament and of the Council of 26 October 2005 on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing, OJ L 309 of 25.11.2005, p. 15.

## *Article 1*

### **Subject matter and scope**

This Directive

- clarifies the technical aspects of the definition in Article 3(8) of Directive 2005/60/EC, in accordance with Article 40(1)(a) of that Directive;
- establishes technical criteria for assessing whether situations represent a low risk of money laundering or terrorist financing as referred to in Article 11(2) and (5) of Directive 2005/60/EC, in accordance with Article 40(1)(b) of that Directive;
- establishes technical criteria for assessing whether, in accordance with Article 2(2) of Directive 2005/60/EC, it is justified not to apply that Directive to certain legal or natural persons carrying out a financial activity on an occasional or very limited basis, in accordance with Article 40(1)(d) of that Directive.

## *Article 2*

### **Definitions**

For the purposes of this Directive the following definitions shall apply

- (1) 'high level judicial body' shall mean a body whose decisions cannot generally be subject to further appeal, except in exceptional circumstances, and shall encompass as a minimum: supreme courts, courts specialised in dealing with constitutional affairs, courts generally dealing with appeals from lower courts, European and international courts;
- (2) 'person able to discharge managerial responsibilities' means a person who is
  - (a) a member of the administrative, management or supervisory bodies of the company;
  - (b) a senior executive, who is not a member of the bodies as referred to in point (a), having the power to make managerial decisions affecting the future developments and business prospects of the company.

### Article 3

#### Politically exposed persons<sup>234567</sup>

1. For the purposes of Article 3(8) of Directive 2005/60/EC, natural persons who are or have been entrusted with prominent public functions shall at least include
  - (a) heads of State, heads of government, ministers, deputy or assistant ministers;
  - (b) members of legislative bodies;
  - (c) members of high level judicial bodies and high-ranking public prosecutors;
  - (d) members of the boards of the bodies or authorities which monitor or control compliance with legal obligations by other public bodies or regulated entities and which enjoy a certain degree of independent or autonomy, such as courts of auditors, central banks and similar institutions;
  - (e) high-ranking diplomats, high-ranking officers in the armed forces, high-ranking officers in the police, and other high-ranking officials exercising public functions within the administrative structure of these bodies referred to in

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<sup>2</sup> Possible recital: Directive 2005/60/EC requires institutions and persons covered to apply, on a risk-sensitive basis, enhanced customer due diligence measures in respect of transactions or business relationships inter alia with politically exposed persons residing in another Member State or in a third country. Politically exposed persons are understood as those entrusted with prominent public functions as well as their immediate family members or persons known to be close associates of such persons.

<sup>3</sup> Possible recital: Drawing up an exhaustive list of categories of persons to be considered as politically exposed persons will be a too rigid approach that risks leaving aside relevant persons. Indeed, any list cannot be definitive taking into consideration the social, political and economic differences between countries concerned, which in the end are essential for defining what a politically exposed person is. As a result, it is considered more appropriate that the clarification of the technical aspects in the implementing measures is limited to the interpretation of the three main parts of the definition: prominent public functions; immediate family members; and persons known to be associates of PEPs.

<sup>4</sup> Possible recital: Public functions exercised at levels lower than national should normally be considered prominent, at least in relation to members of governments and of parliaments of federated states or similar level of government. Member States should also consider whether the mayors of major cities should also be included in the definition.

<sup>5</sup> Possible recital: Institutions and persons covered by Directive 2005/60/EC may fail to identify a customer as falling within one of the politically exposed person categories, despite having taken reasonable and adequate measures in this regard. In those circumstances, Member States, when exercising their powers in relation to the application of that Directive, should give due consideration to the need to avoid an automatic liability of those persons for such failure. Member States should additionally consider facilitating compliance with the Directive by providing the necessary guidance to institutions and persons in this connection.

<sup>6</sup> Possible recital: When dealing with legal entities or legal arrangement whose beneficial owner is a politically exposed person, an immediate family member of that person or a person known to be close associate of that person, institutions and persons covered by Directive 2005/60/EC should extend the consideration of politically exposed persons to those entities or arrangements.

<sup>7</sup> Possible recital: Institutions and persons covered by the directive are required to identify close associates of natural persons who are entrusted with prominent public functions to the extent that this relation is publicly known or that the institution or person has reasons to believe that such relation exists. Hence, knowledge of this condition does not presuppose an active research by the institutions and persons covered by the directive.

points (a) to (d) or of other bodies or organs of public nature, provided that the public functions of these high-ranking officials allow them to control or otherwise exercise dominant influence in the decision making process or in the major public expenditure of these bodies or organs;

- (f) persons able to discharge managerial responsibilities within State owned enterprises charged with the exploitation of natural resources, or which obtain monopoly revenues, or whose profits or other type of economic compensation paid to the State, constitute a material part of the State revenue;

or any other person that, although not falling under any of the above categories, is known to exercise similar powers or influence in the public domain<sup>8</sup>.

None of these categories should be understood as covering middle ranking or more junior individuals.

Categories (a) to (e), where applicable, shall also encompass positions at the European and international level.

2. For the purposes of Article 3(8) of Directive 2005/60/EC, immediate family members of the persons referred to in paragraph 1 shall mean the spouse of that person, or any partner of that person considered by national law as equivalent to the spouse, the children, including in-laws, and parents of that person.
3. For the purposes of Article 3(8) of Directive 2005/60/EC, persons known to be close associates of the persons referred to in paragraph 1 shall mean
  - (a) any natural person who is known as having close business relations with a person referred to in paragraph 1, including in particular joint beneficial ownership of legal entities and legal arrangements;
  - (b) any legal entity or legal arrangement whose beneficial owner is the person referred to in point (a) [alone] and which is known to have been set up for the benefit of the person referred to in paragraph 1.
4. Without prejudice to the application, on a risk-sensitive basis, of enhanced customer due diligence measures, in the case that a person is no longer entrusted with prominent public functions within the meaning of paragraph 1 for a period of at least 1 year, institutions and persons referred to in Article 2(1) of Directive 2005/60/EC shall not be obliged to consider such a person as a politically exposed person.

#### *Article 4*

### **Simplified customer due diligence<sup>9</sup>**

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<sup>8</sup> Possible recital: In some cases, there are persons able to exercise significant powers or influence in the public domain, despite not being formally part of the executive, legislative, judicial or administrative branches. This may be particularly the case for high ranking positions in the structure of the ruling political party in those countries where there is a single or largely dominant political party and the identification between the administration and that ruling political party is high.

1. For the purposes of Article 11(2) of Directive 2005/60/EC, Member States may allow the institutions and persons covered by that Directive not to apply customer due diligence in respect of any customer representing a low risk of money laundering or terrorist financing which meets the following technical criteria:
  - (a) in the case that the customer is a public authority or body<sup>10</sup>:
    - (i) the customer has been entrusted with public functions pursuant to the Treaty on the European Union, to the treaties on the European Communities and/or to European Community secondary legislation; or  
the customer has been entrusted with public functions in the field of international finance pursuant to an international treaty or agreement to which either the European Community or the Member States or both are parties; and
    - (ii) the customer's identity is publicly available, transparent and certain; and
    - (iii) the activities of the customer, as well as its accounting practices, are transparent;
    - (iv) the customer is accountable either to a European institution or to EU Member States authorities, or otherwise appropriate check and balance procedures exist ensuring control of the customer's activity;
  - (b) in the case that the customer is a legal entity which does not enjoy the quality of public authority or a public body<sup>11</sup>:

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<sup>9</sup> Possible recital. Institutions and persons covered by Directive 2005/60/EC may adapt, on a risk-sensitive basis, the general customer due diligence procedures to the situations in which the risk of money laundering and terrorist financing is low. This approach based on the evaluation of the risks involved is the general tool in Directive 2005/60/EC to deal with low risk situations. Taking this into account and the fact that cases of simplified customer due diligence procedures require adequate checks and balances elsewhere in the system aiming at preventing money laundering and terrorist financing, the scope of situations of simplified customer due diligence regarding selected customers and identified products and transactions in this text is limited.

<sup>10</sup> Possible recital: Domestic public authorities acting as customers are generally considered as low risk customers within their own Member State and, in accordance with Directive 2005/60/EC, may be subject to simplified customer due diligence procedures. In this context, the Directive allows for a wide interpretation of "domestic public authority" so as to cover also bodies (including bodies having corporate form) entrusted with public tasks, functions or services and subject to public accountability, which are generally regarded as part of the public administration. However, none of the European institutions, bodies, offices and agencies, including the European Central Bank (ECB), directly qualify in the Directive for simplified customer due diligence under the "domestic public authority" category. Neither does the ECB qualify under the "credit and financial institution" category. A similar situation exists in respect of international financial institutions, such as the World Bank or the International Monetary Fund. However, these entities do not appear to present a high risk of money laundering or terrorist financing. Therefore, they could be recognised as low risk customers and benefit from the simplified customer due diligence procedures.

<sup>11</sup> Possible recital. In the case of other legal entities, it is important to stress that the key elements for allowing the application of simplified customer due diligence procedures to customers perceived as presenting low risk of money laundering or terrorist financing, is the existence of sufficient

- (i) the customer is an entity which is itself subject to the obligations of national legislation pursuant to Directive 2005/60/EC, including entities caught under national legislation in the case foreseen in Article 4 of that Directive, or to the obligations of legislation from a third country which imposes requirements equivalent to those laid down in that Directive. This criterion should only apply to the customer, not to its subsidiaries, unless they also fulfil the criteria on their own; and
- (ii) the customer's identity is publicly available, transparent and certain; and
- (iii) the customer is subject to mandatory licence by national law for the undertaking of financial activities and licensing may be refused if competent authorities are not satisfied that the persons who effectively direct or will direct the business of such entity or its beneficial owner are fit and proper persons. The activity conducted by the customer shall be supervised by competent authorities. Supervision is to be understood in this context as meaning the type of supervisory activity with the highest supervisory powers, including the possibility to conduct on-site inspections. Such inspections should include the review of policies, procedures, books and records, and should extend to sample testing; and
- (iv) the customer is subject to supervision, within the meaning of paragraph 3 of Article 37 of Directive 2005/60/EC, by competent authorities as regards the compliance with the national legislation pursuant to the that directive obligations and, where applicable, additional obligations under national legislation; and
- (v) the customer's lack of compliance with the obligations under (i) is subject to effective, proportionate and dissuasive sanctions including the possibility to take appropriate administrative measures or impose administrative sanctions.

2. For the purposes of Article 11(5) of Directive 2005/60/EC, Member States may allow the institutions and persons covered by that Directive not to apply customer due diligence in respect of any product or transaction linked to such product representing a low risk of money laundering or terrorist financing which meets the following technical criteria:<sup>12</sup>

- (a) the product or the transaction in relation to such product has a contractual base; and

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transparency as to their identity and of adequate control mechanisms elsewhere in the system, in particular enhanced supervision.

<sup>12</sup> Possible recital: Simplified customer due diligence procedures may be applied to products and transactions in limited circumstances, such as in situations where the benefits of the product in question cannot generally be realised for the benefit of third parties and those benefits are only realisable in the long term, such as investment insurance policies or saving products, provided the transactions are done through bank accounts and are below an appropriate threshold. State controlled products, such as saving products for the benefit of children, may be in a position to benefit from simplified customer due diligence procedures even if all the criteria are not fulfilled.

- (b) the transactions in relation to the product are done through an account with a credit institution of the EU or of third countries imposing requirements equivalent to those laid down in Directive 2005/60/EC ; and
- (c) the benefits of the product or the transaction in relation to such product are only realisable in the long term and cannot be realised for the benefit of third parties, except in the case of death, disablement, reaching a predetermined advanced age or similar insurance events; and
- (d) there is a predetermined limit of a maximum annual amount for the product or the transaction in relation to such product, whether the transaction is executed in a single operation or in several operation which appear to be linked.

For the purposes of paragraph (d), the thresholds established in Article 11(5)(a) of Directive 2005/60/EC shall apply in the case of similar insurance policies. For any other type of product or transaction in relation to such product, the threshold established in Article 7(b) of Directive 2005/60/EC shall apply.

Member States may derogate to the precedent technical criteria in the case of products defined and controlled by their relevant domestic public authorities, provided the product has a contractual base, the transactions are done through an account with a credit institution or by way of deduction from wages, and the benefits of the product are only realisable in the long term.

3. In assessing whether the customers or products and transactions referred to in paragraphs 1 and 2 represent a low risk of money laundering or terrorist financing, Member States shall pay special attention to any activity of these customers or to any type of products or transactions which may be regarded as particularly likely, by its nature, to be used or abused for money laundering or terrorist financing purposes.

Member States shall equally take adequate measures to check that there is no information available to suggest that the risk of money laundering or terrorist financing may not be low. In so doing, Member States shall consider the relevant evaluations, at national, European or international level, on trends and typologies in relation to money laundering and terrorist financing.<sup>13</sup>

#### *Article 5*

### **Financial activity on an occasional or very limited basis<sup>14</sup>**

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<sup>13</sup> Possible recital: In the case of simplified customer due diligence procedures, the requirements for institutions and persons, though simplified, do not disappear. Amongst others, institutions and persons are expected to conduct on-going monitoring of the business relations to a certain extent in order to be able to detect complex or unusually large transactions and all unusual patterns of transactions which have not apparent economic or visible law purpose.

<sup>14</sup> Possible recital: In certain circumstances, natural persons or legal entities may provide financial activities in an occasional or very limited basis, as a complement to other non financial activities, such as hotels that provide currency exchange services to its clients. Directive 2005/60/EC allows Member States to decide that the provision of a financial activity on an occasional or very limited basis is outside

1. For the purposes of Article 2(2) of Directive 2005/60/EC, Member States may decide, provided that there is little risk of money laundering or terrorist financing occurring, that legal and natural persons who engage in a financial activity do not fall within the scope of Article 3(1) or (2) of that Directive when such a financial activity is conducted on occasional or very limited basis in accordance with the following technical criteria:
  - (a) the financial activity shall be limited in absolute terms by ensuring that the total turnover of the financial activity does not exceed a sufficiently low threshold. This threshold shall be established at national level, depending on the type of financial activity; and
  - (b) the financial activity shall be limited on a transaction basis by applying a maximum threshold per customer and single transaction, whether the transaction is carried out in a single operation or in several operations which appear to be linked. The maximum threshold shall be established at national level, depending on the type of financial activity, and shall be sufficiently low in order to ensure that the types of transactions in question are an impractical and inefficient method for laundering money or for financing terrorism; and
  - (c) the financial activity shall not be the main activity of the legal or natural person by ensuring that the turnover of the financial activity does not exceed 5%, or a similar sufficiently low threshold established at national level, of the total turnover of the legal or natural person; and
  - (d) the financial activity shall be ancillary, directly related to the main activity of the legal or natural person, but not a totally independent activity<sup>15</sup>; and
  - (e) the main activity of the legal or natural person shall not be an activity falling under any of the situations mentioned in Article 2(1) of Directive 2005/60/EC, except the activity referred to in 2(1)(3)(e); and
  - (f) the financial activity shall be provided to the customers of the main activity only and shall not be generally offered to the public<sup>16</sup>.
2. In assessing whether there is little risk of money laundering or terrorist financing occurring for the purposes of paragraph 1, Member States shall pay special attention

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the scope of that Directive. The assessment of the occasional or very limited nature of the activity should be made by reference to quantitative thresholds in relation to the transactions and the turnover of the business concerned. These thresholds are to be decided at national level, depending on the type of financial activity.

<sup>15</sup> Possible recital. Additionally, it will generally be expected that a person engaging in a financial activity on an occasional and very limited basis will not be providing a full range of financial services to the public but only those needed for improving the performance of its main business. However, when the main business of the person relates to an activity covered by Directive 2005/60/EC, the exemption should not be granted, except in relation to traders in goods.

<sup>16</sup> Possible recital. When the provision of the occasional or limited financial activity is provided to own customers only and is not generally advertised, the risk of money laundering is limited because the number of customers is reduced and the customers in question will in any event be forced to pay for the delivery of (possibly more expensive) non-financial services.

to any financial activity which is regarded as particularly likely, by its nature, to be used or abused for money laundering or terrorist financing purposes<sup>17</sup>.

Member States shall equally take adequate measures to check that there is no information available to suggest that the risk of money laundering or terrorist financing may not be low. In so doing, Member States shall consider the relevant evaluations, at national, European or international level, on trends and typologies in relation to money laundering and terrorist financing.

3. Any decision pursuant to Article 2(2) of Directive 2005/60/EC, whether addressing an individual legal or natural person, or a category of those, shall be based on justified grounds. Member States shall provide for the possibility to withdraw the exemption decision in case of changing circumstances<sup>18</sup>.
4. Member States shall take adequate measures to ensure that the exemption possibility granted by decisions pursuant to Article 2(2) of Directive 2005/60/EC is not abused by possible money launderers or terrorist financiers to circumvent the scope of application of the directive. They shall consider establishing effective, proportionate and dissuasive penalties, risk-based monitoring activities or any other appropriate mechanism.<sup>19</sup>

#### *Article 6*

1. Member States shall bring into force the laws, regulations and administrative provisions necessary to comply with this Directive by 15 December 2007 at the latest. They shall forthwith communicate to the Commission the text of those provisions and a correlation table between those provisions and this Directive.

When Member States adopt those provisions, they shall contain a reference to this Directive or be accompanied by such a reference on the occasion of their official publication. Member States shall determine how such reference is to be made.

2. Member States shall communicate to the Commission the text of the main provisions of national law which they adopt in the field covered by this Directive.

#### *Article [...]*

This Directive shall enter into force on the [...] day following that of its publication in the *Official Journal of the European Union*.

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<sup>17</sup> Possible recital. Some financial activities, such as money transmission and remittance services, are more likely to be used or abused for money laundering or terrorist financing purposes. Therefore, it would not be appropriate that these or like financial activities be exempted from the scope of application of Directive 2005/60/EC.

<sup>18</sup> Possible recital. Exemption decisions pursuant to Article 2(2) of Directive 2005/60/EC should not be a general blank exemption on the definition of the scope of the law. To that extent, the possibility to revert to the original situation on a sufficiently short period of time needs to be provided for.

<sup>19</sup> Possible recital: In certain cases, such as the provision of financial services onboard ships, the monitoring activities of national authorities may be more difficult as a result of overlapping competences. In those circumstances, Member States shall consider not to adopt a decision exempting that kind of financial activity from the scope of application of Directive 2005/60/EC.

*Article [...]*

This Directive is addressed to the Member States.

Done at Brussels, [...]

*For the Commission*

*[...]*

*Member of the Commission*