Fourth Anti-Money Laundering Directive

Introduction

The use of the financial system for money laundering and terrorist financing purposes has received significant media attention in recent times. Such activity has increased in sophistication and volume, leading to a European policy imperative in establishing enhanced anti-money laundering ("**AML**") rules. The Fourth Anti-Money Laundering Directive ("**AML IV**") is the European Union's most recent response to this threat, setting out a more risk focused and sophisticated framework in addressing money laundering and terrorist financing.

AML IV came into force on 25 June 2015, and member states must implement it fully into in their domestic legislation by 26 June 2017. It replaces the Third Anti-Money Laundering Directive of 2005, which will be repealed in its entirety.

AML IV applies to credit institutions, financial institutions, and trust company service providers ("**Designated Persons**") in the same manner as previous legislation. A number of enhancements to the framework set out under previous legislation will require businesses to adjust their internal AML procedures and policies. To ensure compliance in time for the full implementation, it is advisable that Obliged Entities consider the key changes under AML IV as soon as possible.

1 Key New Changes

1.1 Adopting a Risk-Based Approach

Under the previous AML legislation, a defined list of situations and their respective money laundering risk was set out, in addition to requiring a risk-based approach. This prescribed element is no longer retained. Instead, at the heart of AML IV is an even more pronounced risk-based approach, whereby Obliged Entities must take appropriate steps to identify and assess the risks of money laundering and terrorist financing in each of their individual business relationships and transactions. At the same time, however, the Directive sets out a prescribed list of matters which must be covered in AML assessment.

The objective of this risk assessment is to identify and manage the risk of money laundering and terrorist financing. Obliged Entities will consequently be required to implement policies, controls, and procedures to mitigate the associated risks arising from their assessments. Crucially, this risk-based approach will require notably refined internal policies and procedures in comparison to existing frameworks.

1.2 Beneficial Ownership and Trustee Beneficial Ownership

Entities will be required to identify individuals holding ultimate beneficial ownership. This information is required to be accurate and current, and must be provided to the national

competent authority to compile a centralised beneficial ownership register. The Central Bank of Ireland is the designated competent authority in this jurisdiction. This register will then be made accessible to competent authorities, Obliged Entities under the legislation, and others who can demonstrate a "*legitimate interest*". The Department of Finance concluded a Consultation Process canvassing businesses' views on the level of public access to this register, with the outcome expected in due course.

AML IV also introduces new rules in respect of the beneficial ownership of trusts. Where the trust gives rise to tax consequences, beneficial ownership information must be held on a central register maintained by the national authorities. However, this particular register will only be accessible to competent authorities and financial intelligence units. There is no allowance for those holding a "*legitimate interest*" to access this trustee register.

1.3 Politically Exposed Persons

Under AML IV, both domestic and foreign Politically Exposed Persons ("**PEPs**") are included under the rules. This is a notable change from previous legislation, including the recent Irish Criminal Justice Act 2010, where only foreign PEPs were subject to the mandatory enhanced regime.

AML IV also expressly states that Obliged Entities must have in place appropriate risk management systems, including risk-based procedures, to determine whether the customer or the beneficial owner of the customer is a PEP. The measures mandated in cases of business relationships with PEPs, such as obtaining senior management approval for continuing the relationship, remain the same as under previous legislation.

1.4 Amendments to Simplified Due Diligence Procedure

The automatic entitlement to apply Simplified Due Diligence ("**SDD**") when Obliged Entities deal with specified categories of customers is removed under AML IV. The use of SDD procedures is still allowed, but must now be justified on the basis that the business relationship or transaction carries a lower degree of risk. In this regard, the Directive provides a non-exhaustive list of potential low risk categories, including public companies listed on a stock exchange, and customers resident in states where there are generally low levels of corruption.

Further guidelines of the risk factors relevant in the assessment of SDD will be issued by ESMA before the implementation deadline of 26 June 2017. The Consultation Process on this issue concluded in January 2016.

2 Areas of AML IV Requiring Further Clarification

2.1 Implications and Parameters of the Risk-Based Approach

Clearly, the new risk-based approach goes beyond previous rules. But there is a lack of clarity as to the extent of this change. The European Supervisory Authorities ("**ESAs**") are obliged to

release technical standards on risk factors by the implementation deadline of June 2017, and it is hoped that this will inform how Obliged Entities will apply the risk-based approach.

2.2 Extent of Permissible Usage of SDD Procedure

Similarly, the ESAs are required to provide elaboration on when the SDD procedure and related risk assessment can be applied. This will relate closely with the detailed rules on the Risk-Based Approach from above; if the technical standards for the latter are sufficiently clear, it will be relatively straightforward to identify when the SDD procedure is appropriate.

2.3 Beneficial Ownership and Data Protection

It is possible that the new rules on compilation and transfer of information on beneficial owners may conflict with data protection law. By its very nature, personal details such as the owner's name and nationality must be conveyed to national competent authorities. The authorities then compile this information in a central register that is accessible by any party with a "*legitimate interest*." It remains to be seen who will be able to acquire access to this sensitive information under this heading, and whether this is in breach of data protection law.

3 Preparatory Actions for Businesses

AML IV can be seen as building on the previous anti-money laundering legislation. It is unlikely that businesses will need to radically change their AML systems. Rather, the new Directive will require businesses to review their existing systems, and adjust their processes and internal procedures to adhere to the additional layers of obligation that AML IV now imposes. Obliged Entities should address matters now, to ensure compliance with the Directive by the implementation date in June 2017:

- Arguably the main change in the new Directive relates to increased focus on the Risk-Based Approach. Each individual business relationship and transaction category will have to be reviewed for compliance with enhanced AML requirements. This will potentially require greater staff resources and training in respect of new risk factors;
- Allied to this, it will be necessary to implement policies, controls, and procedures to mitigate the associated risks arising from the above assessments;
- The increased transparency focus on beneficial owners will require clear action. Obliged Entities will need to maintain, review, and convey accurate information on beneficial owners to national competent authorities. A crucial change is the requirement that the beneficial ownership of trusts is recorded and processed;
- Enhanced due diligence is required when assessing PEPs and related internal policies will need to be reviewed. Systems designed to assess PEPs are likely to have an increase in output and adjustments should be made for this; and

- Businesses will be required to overhaul their SDD procedures. The automatic application of SDD is removed and so previous systems may be inadequate and need to be updated.

- The Central Bank's "*Dear CEO*" letter of 2012 highlighted the necessity for businesses to anticipate regulatory change and firms are advised to consider the impact of AML IV in line with this expectation.

4 How Matheson Can Help

All Obliged Entities should review their AML frameworks to assess compliance with the new obligations set out under AML IV. We provide a number of services to assist clients in the area of AML, including:

- Reviewing policies and procedures and undertaking a full gap analysis against the expectations of AML IV;

- Undertaking a full and detailed review of a firm's risk assessment;

- Undertaking a mock-inspection to assess the extent of compliance, in practice, with the firm's own internal policies and procedures in relation to AML;

- Assessing the governance structures, roles and responsibilities, and reporting structures in place to ensure a robust AML framework is in place that complies with the expectations of AML IV. This includes reviewing board minutes to ensure sufficient engagement at senior management level in relation to AML matters is being captured, and assessing the adequacy of reports provided by delegates to the board of directors; and

- Providing annual and ad hoc update training to relevant staff and senior management, to ensure any regulatory or legal changes are notified to the relevant staff and senior management in a timely manner. We also offer AML interactive workshops.

Contacts

Joe Beashel
Partner
Tel: +353 1 232 2101
joe.beashel@matheson.com

Edmond O'Hanlon
Associate
Tel: +353 1 232 2249
edmond.ohanlon@matheson.com

Colm Dawson
Solicitor
Tel: +353 1 232 2162
colm.dawson@matheson.com