

The third anti-money laundering directive and the legal profession

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1. INTRODUCTION

On 7 June 2005, the Council of Ministers of the EU gave its political approval to a new directive on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing². The Council approval followed the opinion of the European Parliament on 26 May 2005³.

This directive will be the third in the field of anti-money laundering (the first as regards terrorist financing) and will repeal the existing directives in this matter⁴. It is not, however, a revolutionary text. Indeed, it builds on the policy already reflected in the 1991 and 2001 texts. However, it includes new elements and develops others, going to a large extent beyond the former directives⁵.

This paper aims at presenting the main content of the so-called third directive, with a particular focus on the treatment of the legal profession⁶. Thus, section 2 will deal with the context of the third directive, section 3 with its scope, section 4 with the obligations relating to customer due diligence procedures, section 5 with the reporting obligations, section 6 with the supporting measures, section 7 with supervision, monitoring and penalties and section 8 with the implementing measures. A conclusion will be provided in section 9.

2. THE CONTEXT OF THE THIRD DIRECTIVE

Why preparing a new directive?

¹ **This text is based on the presentation made by the author on 27 May 2005 in Brussels at a conference organised by the European Association of Lawyers.** The views expressed are purely those of the author and may not in any circumstances be regarded as stating an official position of the European Commission. The author is particularly grateful to Joeb Rietrae for his valuable comments on earlier versions of this text.

² See IP/05/682 of 7 June 2005.

³ See IP/05/616 of 26 May 2005.

⁴ Council Directive 91/308/EEC of 10 June 1991 on prevention of the use of the financial system for the purpose of money laundering, OJ L 166, 28.6.1991, p. 77; and Directive 2001/97/EC of the European Parliament and of the Council of 4 December 2001 amending Council Directive 91/308/EEC on prevention of the use of the financial system for the purpose of money laundering, OJ L 344, 28.12.2001, p. 76. Hereinafter, they will be referred as the first and second directives.

⁵ In that context, taking into consideration the new situations addressed as well as the fact that the first directive had already been substantially amended by the second directive in 2001, it was considered appropriate by the Commission, in order to provide clarity, to present a new comprehensive text formally repealing the existing ones. See recital 45.

⁶ At the moment of finalising this draft, the Directive has not yet been published in the Official Journal, pending the finalisation of the text by the legal-linguistic experts of the Council and the Parliament in the different official languages.

Taking into consideration that the second directive dated from 2001 and only entered into force later in June 2003, one could question the need for preparing a new directive in this field. Two main reasons, however, explain the presentation of a new text. Firstly, after the 9/11 terrorist attacks, the Financial Action Task Force (FATF)⁷ undertook the revision of the international standards on the fight against money laundering, extending them to terrorist financing. This revision led to the 2003 Forty Recommendations and the Special Recommendations on terrorist financing. Although in pure legal terms the FATF recommendations are not legally binding, members to the FATF made a commitment to incorporate this (global) standard into their legislation. Indeed, money laundering and terrorist financing are frequently carried out in an international context. Measures adopted solely at national or even Community level, without taking account of international coordination and cooperation, would have limited effects. Therefore, there is an interest in ensuring that the measures adopted by the Community in this field be consistent with the action undertaken at FATF level. In addition, there was a wide preference among EU Member States for a single EU implementation of the FATF recommendations (i.e. ensuring a level playing field in the financial system) rather than for 25 individual responses.

Secondly, the proposal for a new directive filled in the invitation by the Council in the second directive to bring the definition of serious crimes into line with the definition of serious crimes of the relevant Justice and Home Affairs Council framework decision.

Both reasons explain the fact that adoption of the third directive has been a political priority for the Commission, the Council as well as the European Parliament. Indeed, this has been reflected in the speed of the legislative procedure. It has taken less than 12 months since the presentation of the Commission proposal⁸ to reach an agreement on a text.

The third directive is not an isolated instrument.

It focuses on the preventive measures to avoid the misuse of the financial system in the EU by money launderers and terrorist financiers. In that sense, it is a first pillar legal instrument based on Article 47(2), first and third sentences and Article 95 of the Treaty, similarly to the existing directives. However, it is part of a wider (and evolving) legislative (and non legislative) framework addressing money laundering and terrorist financing at EU and international level. Without necessarily being exhaustive, this legal framework includes⁹:

⁷ The FATF, created in 1989, is an inter-governmental body whose purpose is the development and promotion of national and international policies to combat money laundering and terrorist financing. The FATF is therefore a “policy-making body” that works to generate the necessary political will to bring about legislative and regulatory reforms in these areas. For further information see www.fatf-gafi.org

⁸ See IP/04/832 of 30 June 2004. See as well document COM(2004)448.

⁹ On this issue see generally W. Gilmore, “Dirty Money. The evolution of international measures to counter money laundering and the financing of terrorism” (3rd Ed.), Council of Europe Publishing, 2004; and M. Condemni and F. De Pasquale (editors), “International profiles of the activity to prevent and combat money laundering”, Ufficio Italiano dei Cambi, 2005.

- third pillar texts¹⁰ such as the Council Framework Decision on money laundering and proceeds of crime¹¹, or the Council Decision on cooperation between Financial Intelligence Units¹²;
- international conventions, such as the United Nations (UN) Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances (1988), the UN Convention for the suppression of the financing of terrorism (1999), the UN Convention on transnational organised crime (2000), the UN Convention on corruption (2003) or the Council of Europe Conventions on laundering and proceeds of crime¹³;
- the regulation on cash controls at borders¹⁴ implementing FATF Special Recommendation IX;
- the draft regulation on funds transfers¹⁵, implementing FATF Special Recommendation VII;
- the possible directive on a new legal framework on payments¹⁶ that would complete the implementation of FATF Special Recommendation VI on “alternative remittance”; and
- the draft recommendation on a code of conduct for the non-profit sector¹⁷.

¹⁰ See generally the Communication from the Commission to the Council and to the European Parliament of 16.4.2004 on the prevention of and fight against organised crime in the financial sector, COM(2004)262, IP/04/517

¹¹ Council Framework Decision 2001/500/JHA of 26 June 2001 on money laundering, the identification, tracing, freezing, seizing and confiscation of instrumentalities and the proceeds of crime, OJ L182, 5.7.2001, p. 1.

¹² Council Decision 2000/642/JHA of 17 October 2000 concerning arrangements for cooperation between financial intelligence units of the Member States in respect of exchanging information, OJ L 271, 24.10.2000, p. 4.

¹³ Convention of 1990 on laundering, search, seizure and confiscation of proceeds of crime, and the new Convention of 2005 on laundering, search, seizure and confiscation of proceeds from crime and on financing of terrorism.

¹⁴ Adopted by the Council of Ministers on 12 July 2005 after approval by the European Parliament on 8 June 2005, see IP/05/702 of 9 June 2005. Not yet published.

¹⁵ Proposal for a Regulation of the European Parliament and of the Council on information on the payer accompanying transfers of funds, adopted by the Commission on 26 July 2005, see IP/05/1008 of 26.7.2005.

¹⁶ This directive may follow the consultation launched by the Communication from the Commission to the Council and the European Parliament of 2.12.2003 concerning a new legal framework for payments in the Internal Market, COM(2003)718.

¹⁷ See the open consultation launched by the Commission services on Draft Recommendations to Member States regarding a Code of Conduct for Non-profit Organisations to Promote Transparency and Accountability Best Practices, available at http://europa.eu.int/comm/justice_home/news/consulting_public/news_consulting_public_en.htm

3. SCOPE

Material Scope.

The third directive prohibits both the laundering of money and the financing of terrorism. Indeed, the extension of the anti-money laundering defences to the fight against terrorist financing is one of the main changes of the scope of the directive. Despite the Commission proposal requesting it, the directive does not, however, impose as such the “criminalisation” of money laundering and terrorist financing activities. The Council and the Parliament rejected the inclusion of the criminalisation requirement in a first pillar directive.

The definition of money laundering remains unchanged compared to the existing directive. However, an important change brought by the directive in this context is the new definition of serious crimes at the origin of the proceeds to be laundered¹⁸. As explained in the introduction, aligning this text with the definition of serious crimes in the third pillar instruments was one of the main reasons for the new text. The option has been to maintain an all-crime approach by considering a serious crime “*all offences which are punishable by deprivation of liberty or a detention order for a maximum of more than one year or, as regards those States which have a minimum threshold for offences in their legal system, all offences punishable by deprivation of liberty or a detention order for a minimum of more than six months*”. In any case, Member States still have a large margin of manoeuvre in the implementation of this provision. Further to this clause, it is also clarified in the text, as was already done in the first directive, that terrorist activities (as defined in Articles 1 to 4 of Council Framework Decision 2002/475/JHA), drug offences (as defined in Article 3(1)(a) of the 1988 United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances), activities of criminal organisations (as defined in Article 1 of Joint Action 98/733/JHA), fraud (as defined in Article 1(1) and 2 of the Convention on the protection of the European Communities’ financial interests) and corruption are serious crimes.

Personal Scope: the treatment of the legal profession

As regards the personal scope, there are no changes compared to the first directive (as amended) concerning the situations in which independent legal professions should apply the anti-money laundering rules¹⁹: i.e. “*when they participate, whether by acting on behalf of and for their client in any financial or real state transaction, or by assisting in the planning or execution of transactions for their client concerning the: (i) buying and selling of real property or business entities; (ii) managing of client money, securities or other assets; (iii) opening or management of bank, savings or securities accounts; (iv)*

¹⁸ See Article 3(5).

¹⁹ It is noted in this regard that Article 2 of the second directive requires the Commission to conduct an examination on the “*specific treatment of lawyers and other independent legal professionals*” by the directive. In replies to questions from members of the European Parliament (see replies to oral question H-212/05 and to written question 447/05, available at the website of the European Parliament), the Commission has committed to prepare this report by June 2006 (e.g. 3 years after the end of the implementation period for the second directive), lack of relevant and comparable data to do it before. It is also noted that Article 39 of the new directive also calls for the preparation of a report on the treatment of lawyers and other professionals within two years of the expiry of the deadline for transposition (which is two years after entry into force of the directive).

organisation of contributions necessary for the creation, operation or management of companies; (v) creation, operation or management of trust, companies or similar structures.”

The question of the applicability of the anti-money laundering rules to the legal profession is, however, controversial in the sector. There are some legal proceedings challenging the constitutionality of the national legislation in some EU countries (e.g. Belgium or Poland) or foreign countries enacting similar legislation (e.g. Canada) and part of the law profession in the EU brought a petition to the European Parliament in relation to the application of the second money laundering directive to the legal profession²⁰.

However, the personal scope of the directive does not remain unchanged and new persons have been made subject to the obligations of the directive²¹. From the perspective of the legal profession, the most important addition relates to trust and company service providers²². These persons are brought under the directive obligations, to the extent that they were not already covered as independent legal professionals or as auditors, external accountants or tax advisors. Further to avoiding the creation of loopholes in the system, this change should ensure that those professionals who provide services in competition with regulated legal professionals are subject to similar obligations²³. By “Trust and company services providers” the directive understands²⁴ *“any natural or legal person which by way of business provides any of the following services to third parties: (a) forming companies or other legal persons; (b) acting as or arranging for another person to act as a director or secretary of a company, a partner of a partnership, or a similar position in relation to other legal persons”²⁵; (c) providing a*

²⁰ Petition 693/2003 by Paul-Albert Iweins, on behalf of the Paris Bar, the National Bar Council and the Conference of Chairmen of the Bar.

²¹ See generally Article 2 of the directive. The term “institution” is used in the directive to refer to the credit and financial institutions, while the term “person” is meant to refer to the other (natural or legal) persons conducting an activity listed in Article 2. In this paper, the word “person” should be understood, however, as meaning both.

²² Further to the addition of trust and company service providers, the directive (see Article 3(2)(e)) includes insurance intermediaries within the definition of financial institutions and brings in all providers of goods (but not of services despite the proposal by the Commission), if payments in cash above Euro 15000. This is an extension compared to the existing directive where the obligation is limited to high value dealers.

Concerning branches and subsidiaries of Community credit and financial institutions in third countries, where the legislation in this area in third countries is deficient, they should, in order to avoid the application of very different standards within an institution or group of institutions, apply the Community standard with regard to customer due diligence and record keeping or notify the competent authorities of the home Member State if this is impossible. See Article 31 and recital 35.

²³ In this context, it has been signalled that unfair competition situations may arise between lawyers and other liberal professions which subject to the directive obligations in all circumstances while lawyers are not: e.g. tax advisors are subject to the directive while lawyers providing tax advice are not. See the report adopted on 11 May 2005 by the European Economic and Social Committee, not yet published, in particular paragraphs 3.1.9 and 3.7.1.2.

²⁴ See Article 3(7).

²⁵ It has been clarified in Recital 17 of the directive that acting as a company director or secretary does not of itself make someone a trust and company service provider, the scope of the definition only

registered office, business address, correspondence or administrative address and other related services for a company, a partnership or any other legal person or arrangement; (d) acting as or arranging for another person to act as a trustee of an express trust or a similar legal arrangement; (e) acting as or arranging for another person to act as a nominee shareholder for another person other than a company listed on a regulated market that is subject to disclosure requirements in conformity with Community legislation or subject to equivalent international standards.”

An important clarification is provided in recital 14 by stating that the provisions of the directive should also apply if the activities of the persons covered by this directive are performed on the Internet.

Minimal harmonisation directive

Finally, it should be noted that, similarly to the previous legislation, the third directive is a minimal harmonisation directive. On the one hand, in accordance with Article 5²⁶, Member States may adopt stricter provisions in the field covered by the directive. On the other hand, in accordance with Article 4²⁷, Member States should extend the scope of the preventive measures contained in the directive to other professions and categories of undertakings that although not included in the directive, engage in activities which are particularly likely to be used for money laundering or terrorist financing purposes.

4. OBLIGATIONS RELATED TO CUSTOMER DUE DILIGENCE (CDD) PROCEDURES

The first directive (as amended), though imposing a customer identification obligation, contained relatively little detail on the procedures. In view of the crucial importance of this aspect of money laundering and terrorist financing prevention, the European legislator considered appropriate to introduce, in accordance with the new international standards, more specific and detailed provisions relating to the identification and verification of the customer and of any beneficial owner.

In which circumstances should CDD be conducted?

Article 7, in conjunction with Article 3(9), of the directive clarifies that the persons covered by the directive shall apply CDD procedures: (i) when entering into a business, professional or commercial relationship which is connected with the professional activities of the person subject to the rules and which is expected, at the time when the contact is established, to have an element of duration; (ii) in the case of occasional transactions above the euro 15000 threshold (whether a single operation or several linked operations); (iii) when there is a suspicion of money laundering or terrorist financing,

covers those persons that act as a company director or secretary for a third party and by way of business.

²⁶ See Article 15 of the first directive, as amended.

²⁷ See Article 12 of the first directive, as amended.

independently of any threshold, derogation or exemption; and (iv) when there are doubts about previously obtained identification data²⁸.

What should be done when conducting CDD procedures? – the risk based approach.

As described in Article 8, CDD procedures essentially consist of: (i) identifying the customer and verifying its identity by using documents, data or information obtained from a reliable and independent source; (ii) identifying, where applicable, the beneficial owner (see below); (iii) obtaining information on the purpose and intended nature of the business, professional or commercial relationship; and (iv) ongoing monitoring of such relationship.

CDD procedures should be conducted following a risk based approach. Indeed, the risk of money laundering and terrorist financing is not the same in every case and persons can therefore adapt the extent of the measures to apply depending on the type of customer, business relationship, product or transaction. In any event, the persons subject to the directive should be in a position to demonstrate to the authorities that the measures taken are appropriate in view of the risks faced. The risk based approach is a key aspect of the directive and should facilitate its smooth application.

Additionally, the directive maintains a special care duty for the persons covered: i.e. they should pay special attention to any activity which they regard as particularly likely, by its nature, to be related to money laundering or terrorist financing and in particular to complex, unusual large transactions and all unusual patterns of transactions which have no apparent economic or visible lawful purpose²⁹.

The question of the beneficial owner is dealt with in much more detail in the new directive compared to the first directive³⁰. According to the third directive³¹, the beneficial owner should be identified while the verification of the identity is to be performed only to the extent possible, by taking risk-based and adequate measures. Indeed, it is left to the persons whether they make use of public records of beneficial owners, ask their clients for relevant data or get the information otherwise, taking into account that the extent of such customer due diligence measures relates to the risk of money laundering and terrorist financing, which itself depends on the type of customer, business relationship, product or transaction.

In this context, the directive contains a (complex) definition of “beneficial owner” in its Article 3(6). This definition provides in the first place a general catch-all clause stating that the beneficial owner means “*the natural person(s) who ultimately owns or controls the customer and/or the natural person on whose behalf a transaction or activity is being conducted*”. As a second step, the definition establishes minimum clarifications (“*The beneficial owner shall at least include...*”) as regards corporate entities, on the one hand, and legal entities (e.g. foundations and similar) and legal arrangements (e.g. trusts and

²⁸ In addition to these general situations, the directive foresees a special regime for anonymous accounts and anonymous passbooks (see Article 6), and for casinos (see Article 10).

²⁹ See Article 20 of the directive and Article 5 of the first directive (as amended).

³⁰ See Art. 3(7) of the first directive as amended.

³¹ See Article 8(1)(b).

similar) which administer and distribute funds, on the other hand. This is done by reference, where appropriate, to a relevant percentage of controlling interests (e.g., in the case of corporate entities, “*the natural person(s) who ultimately owns or controls a legal entity through direct or indirect ownership or control over a sufficient percentage of the shares or voting rights in that legal entity, including through bearer share holdings, other than a company listed on a regulated market that is subject to disclosure requirements consistent with Community legislation or subject to equivalent international standards; a percentage of 25% plus one share shall be deemed sufficient to meet this criterion*”; in the case of legal entities or arrangements, “*the natural person(s) who exercises control over 25 % or more of the property of a legal arrangement or entity*”) or to a relevant percentage of the benefits (in the case of legal entities or arrangements, “*where the future beneficiaries have already been determined, the natural person(s) who is the beneficiary of 25 % or more of the property of a legal arrangement or entity*”). It is interesting to note in this regard that the Commission originally proposed a lower percentage (10%). In the case of corporate entities, the beneficial owner should also include “*the natural person(s) who otherwise exercises control over the management of a legal entity*” (e.g. on the basis of a contract, agreement etc.).

Identifying a beneficial owner is not always easy. This difficulty is especially higher in the case of legal entities, such as foundations, and arrangements, such as trusts. This is particularly so when individual beneficiaries are yet to be determined and it is therefore impossible to identify an individual as the beneficial owner. In those cases, it would suffice to identify the “class of persons” who are intended to be the beneficiaries of the foundation or trust. This requirement does not include the identification of the individuals within that class of persons.

The directive also clarifies that the obligation to identify the beneficial owner does not apply in the cases when trust relationships are widely used in commercial products as an internationally recognized feature of the comprehensively supervised wholesale financial markets³².

The question of the beneficial owner is very much linked to the issue of the transparency of legal entities. The Commission is currently conducting further work on this issue and an external study on a “cost benefit analysis of transparency requirements in the company/corporate field and banking sector relevant for the fight against money laundering and other financial crime”, is in the process of being commissioned³³.

At what moment in time CDD procedures are to be carried out?

Two situations should be distinguished. As regards new customers, CDD is to be conducted before the establishment of a business, professional or commercial relation or the execution of transaction. CDD procedures may however take place during the establishment of such relation if needed not to interrupt the “normal conduct of business” and provided there is little risk of money laundering or terrorist financing³⁴. As regards

³² See Recital 13.

³³ The call for tender was published in the OJ S 112-110854 of 11.06.2005.

³⁴ See Article 9 paragraphs 1 and 2, respectively. In paragraphs 3 and 4, there are specific circumstances allowing for the verification of the identity of the customer at a different moment in time in relation to life insurance business and opening of bank accounts.

existing customers, CDD procedures are to be conducted at any moment, on a risk sensitive basis³⁵.

It should be recalled that ongoing monitoring of the business, professional and commercial relation is to be conducted at any moment in time and also forms part of the CDD obligations.

What happens if CDD is unsuccessful?

The general rule is that if the persons subject to the directive are unable to identify the customer (and verify its identity), to identify the beneficial owner (if applicable) or to obtain information on the purpose or intended nature of the business, professional or commercial relationship, that person should not perform a transaction or establish a business, professional or commercial relationship, or shall terminate such transaction. Additionally, it shall consider informing the relevant authorities (see below on reporting obligations).

However, there is a particular derogation for independent legal professionals in Article 9(5). Member States shall not be obliged to apply the provision requiring not to enter into a business relation/perform a transaction in situations when notaries, independent legal professionals, auditors, external accountants and tax advisors are in the course of ascertaining the legal position for their client or performing their task of defending or representing that client in, or concerning judicial proceedings, including advice on instituting or avoiding proceedings.

Enhanced and Simplified CDD.

Further to the risk-based approach principle developed in Article 8, the directive provides for situations in which enhanced CDD should be conducted and simplified CDD should or may be conducted.

Certain situations present a greater risk of money laundering or terrorist financing and there are cases where particularly rigorous customer identification and verification procedures are required (on a risk sensitive basis). These situations requesting enhanced CDD procedures are, at minimum, non face to face operations, cross-frontier correspondent banking relations with third countries and relations with non domestic “Politically Exposed Persons”³⁶.

On the contrary, Member States may decide that for the list of persons or products mentioned in Article 11 of the directive, simplified CDD procedures are applicable. Only in the case of credit and financial institutions acting as customers, the application of simplified CDD is compulsory (this was already the case in the first directive, as amended). It should be noted in this context that the derogation concerning the identification of beneficial owners of pooled accounts held by notaries or other independent legal professionals is without prejudice to the obligations that those notaries

³⁵ See Article 9(6).

³⁶ See generally Article 13. According to Article 3(8), “politically exposed persons” means natural persons who are or have been entrusted with prominent public functions and immediate family members or persons known to be close associates of such persons. This has been one of the most debated issues during the legislative process.

or other independent legal professionals have according to this directive. This includes the need for such notaries or other independent legal professionals themselves to identify the owners of the pooled accounts held by them³⁷.

Can other persons be relied upon for conducting CDD? – Third party performance

In order to avoid repeated customer identification procedures, leading to delays and inefficiency in international business, the directive allows Member States, subject to suitable safeguards, to permit customers to be introduced whose identification has been carried out elsewhere. In those cases where a person relies on a third party, the ultimate responsibility for the customer due diligence procedure remains with the person to whom the customer is introduced. The third party, or introducer, shall be a person subject to the directive (or to equivalent requirements if from a third country). Indeed, he also retains his own responsibility for all the requirements in the directive to the extent that he has a relationship with the customer that is covered by the directive, including the requirement to report suspicious transactions and maintain records³⁸.

The third party performance opens an important door for the legal profession, in particular in cross-border situations. However, its effective application depends of the willingness of Member States during the implementation process, as Member States are not obliged to allow these procedures, which are optional. In any event, as far as the legal profession is concerned, the directive establishes that in those cases where a Member State permits its independent legal professionals to be relied on as a third party domestically, that Member States shall in any case permit them to recognise and accept the outcome of the CDD procedures carried out in accordance with the directive by an auditor, external accountant, tax advisor, an independent legal professional, or a trust or company service provider meeting the requirements of the directive. This recognition and acceptance of the outcome should be possible even if the documents or data on which these requirements have been based are different from those required in the Member State to which the customer is being referred.

A different situation is that of agency or of outsourcing relations. In those cases there is a contractual basis between the persons covered by this directive and the person performing the CDD procedure. In those cases, the outsourcing service provider or the agent is to be regarded as part of the person covered by the directive. If the outsourcing service provider or agent are external natural or legal persons not covered by the scope of the directive, any anti-money laundering and anti-terrorist financing obligations for these agents or outsourcing providers as part of the persons to the directive, may only arise from contract and not from the directive. In any event, the responsibility for complying with the directive remains with the person covered by it³⁹.

5. REPORTING OBLIGATIONS

Alongside the application of the CDD procedures, the second main element of the directive obligations relates to the obligation to report suspicions of money laundering

³⁷ See also recital 23.

³⁸ See recital 27.

³⁹ See Article 19 and recital 28.

and/or terrorist financing. Concerning the reporting obligations of independent legal professionals, there are important changes compared to the situation under the first directive.

Independent legal professionals should report suspicions of money laundering and/or terrorist financing.

The directive maintains the obligation for independent legal professionals to report, on own initiative, suspicions of money laundering and/or terrorist financing⁴⁰. This reporting obligation applies unless the situation is covered by the legal privilege exception in the second paragraph of Article 23⁴¹. There is no material change compared to Article 6(3) of the first directive (as amended).

The rationale is that where independent members of professions providing legal advice which are legally recognised and controlled, such as lawyers, are ascertaining the legal position of a client or representing a client in legal proceedings, it would not be appropriate under the directive to put these legal professionals in respect of these activities under an obligation to report suspicions of money laundering or of terrorist financing. Exemptions from the obligation to report relates to information obtained either before, during or after judicial proceedings, or in the course of ascertaining the legal position for a client.

Thus, legal advice in the context of ascertaining the legal position of a client or representing a client in legal proceedings shall remain subject to the obligation of professional secrecy unless: the legal counsellor is taking part in money laundering or terrorist financing activities, the legal advice is provided for money laundering or terrorist financing purposes or the lawyer knows that the client is seeking legal advice for money laundering or terrorist financing purposes⁴².

In addition to the reporting obligation on own initiative, independent legal professionals are also subject to the obligation to provide the Financial Intelligence Units (FIUs), at their request, with all necessary information, in accordance with the procedures established by the applicable legislation at national level⁴³.

⁴⁰ See generally Article 22. The other institutions and persons covered by the Directive are also subject to this reporting obligation. In addition, public authorities should also inform (as already required in Article 10 of the first directive, as amended), in particular authorities supervising “institutions and persons” have an obligation, in accordance with Article 25(1) to inform of facts related of money laundering or terrorist financing; and financial markets supervisory bodies have a similar obligation in accordance with Article 25(2).

⁴¹ In order to treat direct comparable services in the same manner when practised by any of the professionals covered by the directive, the same exception applies in the case of auditors, external accountants and tax advisors who, in some Member States, may defend or represent a client in the context of judicial proceedings or ascertain a client’s legal position. See recital 21.

⁴² See recital 20.

⁴³ It is noted that a special obligation is created for credit and financial institutions (Article 32): they should be able to respond rapidly to requests for information on whether they maintain business relationships with named persons (and the nature of the relation). For the purpose of identifying such business relationships in order to be able to provide that information quickly, credit and financial institutions should have effective systems in place which are commensurate with the size and nature of the business. In particular for credit institutions and larger financial institutions it would be

As far as law firms (not individual lawyers) are concerned, it is noted that Article 34 refers to the need that persons have “compliance management” in place. In practice, this means that a compliance officer would be appointed in most cases to ensure swift compliance with the reporting obligations.

The consequences of reporting: the non-execution of the transactions

The general principle set out in Article 24 is to refrain from carrying out transactions which persons know or suspect to be related to money laundering or terrorist financing until they have reported their suspicions to the competent authority. The directive foresees in this case that, in conformity with national legislation, instructions may be given by a competent authority not to execute the transaction.

However, as a derogation from the general prohibition to carry out suspected transactions, the entities subject to this directive may execute suspected transactions before informing the competent authorities where refraining from the execution is impossible or likely to frustrate the efforts to pursue the beneficiaries of a suspected money laundering or terrorist financing operation. This, however, is without prejudice to the international obligations accepted by the Member States to freeze without delay funds or other assets of terrorists, terrorist organisations and those who finance terrorism, in accordance with the relevant United Nations Security Council resolutions⁴⁴.

Protecting those who report

Two different provisions are concerned. The first one constitutes an important novelty in the directive. It requires Member States to take all appropriate measures in order to protect employees of the persons who report the suspicions of money laundering or terrorist financing either internally or to the financial intelligence unit⁴⁵. Although the directive cannot interfere with Member States’ judicial procedures, protection of employees is a crucial issue for the effectiveness of the anti-money laundering and anti-terrorist financing system. Therefore, Member States are expected to do whatever they can to protect employees who report their suspicions of money laundering from threats or harassment. This provision has been particularly welcomed by the European Economic and Social Committee⁴⁶.

The second provision relates to the protection from liability in case of disclosure in good faith pursuant to a report filed in accordance with the directive⁴⁷. Indeed, such a report should not constitute a breach of any restriction on disclosure of information imposed by contract or by any legislative, regulatory or administrative provision, and shall not

appropriate to have electronic systems at their disposal. This provision is of particular importance in the context of procedures leading to measures such as freezing or seizing of assets (including terrorist assets), pursuant to applicable national or EU legislation with a view to combating terrorism (see recital 36).

⁴⁴ See Recital 30.

⁴⁵ See Article 27 and recital 32.

⁴⁶ See the report adopted on 11 May 2005 by the European Economic and Social Committee, not yet published, in particular paragraph 3.6.1.

⁴⁷ See Article 26.

involve the person or its directors or employees in liability of any kind. There is no substantial change, as regards this provision, compared to the previous directive⁴⁸.

How to report? –The role of the self-regulatory bodies and of the Financial Intelligence Units

The general principle in the directive is that suspicious transactions should be reported to the financial intelligence unit⁴⁹. The FIU serves as national centre for receiving, analysing and disseminating to the competent authorities suspicious transaction reports and other information regarding potential money laundering or terrorist financing. However, this should not compel Member States to change their existing reporting systems where the reporting is done through a public prosecutor or other law enforcement authorities, as long as the information is forwarded promptly and unfiltered to financial intelligence units allowing them properly to conduct their business, including international cooperation with other financial intelligence units.

However, as far as the legal profession is concerned, Member States MS may designate a self regulatory body of the profession concerned as the recipient of information in the first instance in place of the FIU⁵⁰. In such a case, the self- regulatory body shall forward the information to FIU “*promptly and unfiltered*”. This regime constitutes an evolution compared to Article 6(3) of the first directive (as amended). To the extent that the self-regulatory bodies have an immediate obligation to forward the information, the question about laying down appropriate forms of cooperation between the self-regulatory body and the authorities responsible for combating money laundering loses its value.

What remains untouched from the regime in the previous directive is the legal privilege exemption⁵¹. Indeed, Member States are not obliged to apply the reporting obligations to “*notaries, independent legal professionals, auditors, external accountants and tax advisors with regard to information they receive from or obtain on one of their clients, in the course of ascertaining the legal position for their client or performing their task of defending or representing that client in, or concerning judicial proceedings, including advice on instituting or avoiding proceedings, whether such information is received or obtained before, during or after such proceedings.*” It is noted that this is a faculty, not an obligation, for Member States.

To the extent that a Member State has decided to use this exemption, it may allow or require the self-regulatory body representing those persons not to transmit to the financial intelligence unit any information obtained from these persons in the conditions laid down in that provision⁵².

The growing importance of the Financial Intelligence Units

⁴⁸ See Article 9 of the first directive, as amended.

⁴⁹ See generally Article 22 and recital 29.

⁵⁰ See Article 23(1).

⁵¹ See Article 23(2).

⁵² See Recital 31.

The directive confirms the growing importance of the FIUs in the fight against money laundering and terrorist financing. This is shown by the specific request contained in the directive to have an FIU as central national unit in place with adequate resources and able to have access, either directly or indirectly, to the necessary information, whether financial, administrative or related to law enforcement, that it needs to properly function⁵³.

The central role of FIUs is amplified by the large structured networks to which they belong and where they can exchange information: e.g. Egmont Group at world level, or FIU-NET at EU level. The importance of cross-border cooperation is recognised in Article 38 that foresees the possibility for the Commission to lend assistance (possibly including EU funding) to the European FIUs.

Prohibition of disclosure: no tipping off allowed

The general principle is well established in Article 28(1): it is prohibited to disclose to the customer or to third parties that information has been transmitted to the FIU or that a money laundering or terrorist financing investigation is being or may be carried out. This prohibition of tipping off the customer also affects the legal profession. In that sense, it constitutes a change compared to the regime in the previous directive⁵⁴.

Law professionals (as well as auditors, external accountants and tax advisors), however, may seek to dissuade a client from engaging in illegal activity without this being considered to be a disclosure within the sense of the directive⁵⁵.

Having said that, disclosure is allowed by the directive in restricted circumstances⁵⁶:

- Firstly, disclosure to the authorities (including self-regulatory bodies of professions within this meaning) or for law enforcement purposes is allowed.
- Secondly, law professionals (as well as auditors, external accountants and tax advisors) may disclose information among themselves provided they perform their professional activities (whether as employees or not) within the same legal person or network. Network is understood as meaning the larger structure to which the person performing the professional activities belongs and which shares common ownership, management or compliance control. This particular exemption would allow for example lawyers and auditors working in the same firm to exchange information.
- Thirdly, disclosure is also allowed among this group of professionals and credit and financial institutions in cases related to the same customer and the same transaction provided that those exchanging information are from the same professional category and are subject to equivalent obligations as regards professional secrecy and personal data protection.

⁵³ See Article 21.

⁵⁴ See Article 8(2) of the first directive, as amended.

⁵⁵ See Article 28(6).

⁵⁶ See Article 28, paragraphs 2, 4 and 5 respectively. A further disclosure possibility relates to disclosure within the group of companies for credit and financial institutions only (see Article 28, paragraph 3).

Finally, the directive clarifies⁵⁷ that disclosure of information as referred to in Article 28 should be in accordance with the rules on transfer of personal data to third countries as laid down in Directive 95/46/EC of the European Parliament and of the Council of 24 October 1995 on the protection of individuals with regard to the processing of personal data and on the movement of such data. Moreover, the provisions in Article 28 cannot interfere with national data protection and professional secrecy legislation.

6. SUPPORTING MEASURES

The directive also contains some obligations on persons requiring them to adopt measures in support of the main obligations (e.g. CDD and reporting). These supporting measures essentially relates to record keeping, internal policies and procedures and to training.

First, records of documents and information in relation to the CDD procedures (including those in connection to business, professional and commercial relationship and to transactions) should be kept for at least 5 years⁵⁸.

Second, the directive imposes some requirements in relation to adequate and appropriate policies and procedures of CDD, reporting, record keeping, risk assessment, risk management, compliance management and communication⁵⁹. All of these requirements will have to be met by each of the persons under this directive, while Member States are expected to tailor the detailed implementation of these provisions to the particularities of the various professions and to the differences in scale and size of the persons covered by this directive.

Third, there are training obligations for persons⁶⁰. In this regard, the directive clarifies the situation of law professionals that undertake their professional activities on an independent basis but within the structure of a legal person by requiring that the training obligations apply to the legal person, rather than the natural person. However, those professionals shall remain independently responsible for the compliance with the rest of the provisions of the directive⁶¹.

In addition, national authorities have some related obligations that should facilitate the compliance with the directive obligations by the persons covered⁶². Hence, Member States should ensure that the persons have access to up-to-date information on the typologies of money laundering and terrorist financing and on indicators leading to the recognition of suspicious transactions. Additionally, feedback should, where practicable, be made available to them on the usefulness and follow-up of the reports they present. To make this possible, and to be able to review the effectiveness of their systems to combat

⁵⁷ Recital 33.

⁵⁸ See Article 30.

⁵⁹ See Article 34 and recital 37.

⁶⁰ See Article 35.

⁶¹ See Recital 42.

⁶² See Articles 35(2) and (3), 33, and recital 38.

money laundering and terrorist financing, Member States should keep and improve the relevant statistics.

7. SUPERVISION, MONITORING AND PENALTIES

The new directive has strengthened the anti-money laundering and counter-terrorist financing regime by establishing minimum rules on supervision and monitoring of the activities of the persons covered with a view to ensure compliance with the directive. Hence, authorities should at least effectively “monitor” and take the necessary measures to that end⁶³. In the case of independent legal professionals (and other professions), supervisory functions may be performed on a risk sensitive basis.

As to who can perform the supervisory functions, the directive allows self regulatory bodies to act as supervisors for the purposes of the directive if some conditions are met. First, supervisors should have adequate powers, including the possibility to compel the production of any information that is relevant to monitoring compliance and perform checks⁶⁴. Second, they should have adequate resources.

The directive also requires Member States to ensure that natural and legal persons are liable for infringements of the national law provisions adopted pursuant to the directive and that penalties should be effective, proportionate and dissuasive⁶⁵. This is standard language also contained in other directives in the financial area and allows for flexibility in the national implementation. Only in the case of credit and financial institutions, the directive requires that without prejudice to criminal sanctions, Member States should ensure that the appropriate administrative measures can be taken or administrative sanctions can be imposed. Liability of legal persons is also foreseen in the directive.

8. IMPLEMENTING MEASURES

An important novelty contained in the third directive is the possibility for the Commission to adopt implementing measures within a comitology procedure with the assistance of a new regulatory Committee on the Prevention of the Money Laundering and Terrorist Financing⁶⁶.

The Commission’s powers are subject to strict procedural conditions detailed in recital 47 and are limited in time by a sunset clause (four years). In addition, the implementing measures are only foreseen for a limited number of issues:

- clarification of the technical aspects of some definitions (e.g. beneficial owner);

⁶³ See generally Article 37.

⁶⁴ The power to conduct on site inspections would not be required. See 37(3) *a contrario*

⁶⁵ See generally Article 39.

⁶⁶ See generally Articles 40 and 41.

- establishment of technical criteria for assessing whether situations represent a low or high risk of money laundering or of terrorist financing in relation to the application of the simplified and enhanced CDD procedures;
- establishment of technical criteria for assessing whether it is justified not to apply the directive to certain legal or natural persons carrying out a financial Activity on an occasional basis;
- the adaptation of the amounts referred to in different provisions of the directive; and
- issues in relation to third country equivalence.

9. CONCLUSION

The third directive is an important step forward for the reinforcing of the prevention of the use of the financial system for the purpose of money laundering, and also now of terrorist financing. It certainly gives a clearer indication of what is expected from the persons subject to the obligations of the directive while trying to adapt those obligations to the real risk that may appear in any situation. As regards the law professionals, there are no major changes concerning the scope of the obligations. However, the new directive does no longer give Member States the possibility to allow law professionals to disclose to their clients that a report on suspicions of money laundering has been filed with the competent authorities (so called “tipping off”). That possibility could clearly undermine any subsequent investigation. It is also true that the new directive reinforces the key role of the financial intelligence units in the reporting process and, as a result, the role of the self-regulatory bodies diminishes. This shows the need to have money laundering (and terrorist financing) related information treated by specialised bodies. Indeed, it is doubtful whether the self-regulatory bodies are in a position to do a similar job. After all, the goal of the directive is to make life difficult for money launderers (and terrorist financiers) and hinder their ability to use the financial system for unlawful purposes.