

Translation

The division of responsibilities between the supervisory authorities of the home and host countries with regard to Anti-Money Laundering

1. INTRODUCTION, BACKGROUND AND CONCLUSION

For the purpose of a report to the Danish Ministry of Industry, Business and Financial Affairs (*Erhvervsministeriet*), the Danish Financial Supervisory Authority (*Finanstilsynet*) has requested an opinion on which country's supervisory authority is competent to supervise and sanction breaches of anti-money laundering law when the breaches take place in a branch established in another EU country than the home country of the financial institution. The report is drawn up by the Danish Financial Supervisory Authority to the Danish Ministry of Industry, Business and Financial Affairs and concerns experience from the money laundering matter of the Estonian branch of Danske Bank A/S (the "Bank").

In relation to the Estonian branch's non-compliance with the anti-money laundering rules in the period 2007 to 2015, the question has arisen as to whether the handling and supervision of the critical matters at issue were rightfully subject to the financial supervision of the Danish or the Estonian authorities.

The factual circumstances under review by the Financial Supervisory Authority regarding Danske Bank's management and control of the Estonian branch took place when the Third Anti-Money Laundering Directive¹ was in force. Had the circumstances taken place today, they would have been subject to the Fourth Anti-Money Laundering Directive².

¹ Directive (EU) 2005/60 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.

² Directive (EU) 2015/849 of the European Parliament and of the Council of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing.

It is my opinion and conclusion that the division of responsibilities between two supervisory authorities pursuant to both the Third and the Fourth Anti-Money Laundering Directives was - and still is - such that the host country has the supervisory obligation to ensure that national anti-money laundering law is complied with by a branch of a financial institution domiciled in another EU country.

In specific terms, this means that the Estonian financial supervisory authority was - and currently is - responsible for supervising the Bank's Estonian branch's compliance with anti-money laundering law.

2. THE LEGAL BASIS

2.1 The Third Anti-Money Laundering Directive

The intended distribution of powers between the supervisory authorities of the home and the host country is not expressly stated in the Third Anti-Money Laundering Directive, neither in the recitals nor in the body of the Directive.

However, Article 22(1), point (a) states that institutions covered by the Directive are obliged to fully cooperate by promptly informing the Financial Intelligence Unit (FIU) if the institutions suspect money laundering activities.

According to Article 22(2), the proceedings of such notification are the following:

"The information referred to in paragraph 1 shall be forwarded to the FIU of the Member State in whose territory the institution or person forwarding the information is situated."

It follows from the preparatory works of the Anti-Money Laundering Act of 2006 then in force³, which implemented the Third Anti-Money Laundering Directive, that the Act applies to the branches and agents of foreign undertakings pursuing business in Denmark according to points (1) to (8) and (10), cf. s.1(1), point (9) of the 2006 Act.

In this connection, it follows from s.1(1), point (9) of the preparatory works that:

"The provisions of point (9) partially implements Article 2(2), cf. Article 3(2) point (f), of the Directive. According to Article 3(2) point (f), the Directive covers branches of undertakings and persons which are financial institutions pursuant to Article 3(2) points (a) to (e), including undertakings which carry out activities of currency exchange and of transmission or remittance of money and other assets."

³ Act no. 117 of 27 February 2006 on measures to prevent money laundering of dividends and terrorist financing.

However, the Bill only covers the branches of foreign undertakings in Denmark which carry out activities in accordance with points (1) to (8). The reason for this is that, within the European Union or countries with which the Union has concluded agreements in the financial area, it is as a general rule the duty of the supervisory authority of the home country to supervise the branch of a foreign undertaking exercising the activities referred to in points (1) to (8).

Hence, it is not for the supervisory authority of the country in which the branch carries out activities to supervise the branch. If, for example, an English bank sets up a branch in Denmark, it is as a general rule the duty of the English supervisory authorities to supervise the branch.

The provisions of point 9 derogate from the general rule of home country supervision in relation to undertakings covered by points (1) to (8) in that s.34 of the Bill entails that it is the responsibility of the Danish Financial Supervisory Authority to supervise compliance with this Act by the branches of the above undertakings in Denmark.

The fact that the Directive derogates from the principle of home country supervision reflects the necessity of leaving the territorial jurisdiction with the Member State in which the activities are carried out (the host country).

A branch of an undertaking outside the European Union or a country with which the Union has not concluded an agreement in the financial area is also covered by point (9).

Investment associations and special-purpose associations, collective investment undertakings, restricted associations, innovation associations as well as hedge funds, see point (10) of the provision, undertakings carrying out activities of currency exchange and transmission or remittance of money and other assets, see point (11), and other persons whose business it is to carry out one or more of the activities referred to in Annex 1, see point (12), are not covered by the basic principle of home country supervision.

If and to the extent that other foreign undertakings than those mentioned in points (1) to (8) are entitled under other legislation to set up branches in Denmark, the activities of, for example, transmission or remittance of money, carried out by the branch will be covered by the Bill. This means that the activities that the branch carries out in Denmark are subject to Danish supervision." (my emphasis)

This interpretation of the distribution of responsibilities is emphasised by the Danish implementation of the First Payment Services Directive, which caused changes to the Danish Anti-Money Laundering Act then in force.

With the legislative amendment in 2012, a new provision was introduced in s.34(8)⁴ of the Anti-Money Laundering Act with the following wording:

"The supervision of branches and agents of payment institutions and e-money institutions domiciled in another country within the European Union or in a country with which the Union has concluded an agreement in the financial area is to be carried out in cooperation with the supervisory authority of the home country of the institution." (my emphasis)

It follows from the preparatory works of s.34(8) of the 2012 Act that:

"Pursuant to s.34(1), the Danish Financial Supervisory Authority shall supervise undertakings and persons covered by s.1(1), point (12) ("Other undertakings and persons pursuing a business of one or more of the activities referred to in Annex 1") and branches of foreign undertakings carrying out such business.

However, Directive 2007/64/EC of the European Parliament and of the Council of 13 December 2007 on payment services in the internal market and Directive 2009/110/EC on the taking up, pursuit and prudential supervision of the business of electronic money institutions, implemented in Denmark by Act on Payment Services and Electronic Money, provides for the scope of home country supervision of payment institutions and e-money institutions domiciled in another country within the European Union or in a country with which the Union has concluded an agreement in the financial area to also cover the branches and agents of such undertakings in other EU/EEA Member States.

The Payment Services Directive provides detailed rules for the cooperation between the supervisory authorities of the home and host countries regarding the supervision of branches and agents in the host country, but the power to grant and revoke licences etc. rests with the authorities of the home country.

It is therefore proposed that it be specified in the provision that the Danish Financial Supervisory Authority's supervision of branches and agents of payment institutions and e-money institutions domiciled in another EU/EEA country must be carried out

⁴ Act no. 155 of 28 February 2012

in cooperation with the supervisory authority of the institution's home country. (my emphasis)

Finally, the third recital of the Second Anti-Money Laundering Directive⁵ provides that:

"The Directive does not establish clearly which Member State's authorities should receive suspicious transaction reports from branches of credit and financial institutions having their head office in another Member State nor which Member State's authorities are responsible for ensuring that such branches comply with the Directive.

The authorities of the Member States in which the branch is located should receive such reports and exercise the above responsibilities." (my emphasis)

2.2 The Fourth Anti-Money Laundering Directive

It follows from recitals 52 and 53 of the Fourth Anti-Money Laundering Directive that the host country is the appropriate competent authority with responsibility for ensuring compliance with the Directive, notwithstanding that the financial undertaking in question is otherwise subject to the supervision of the supervisory authorities of its home country.

The supervisory authorities of the home country, however, are responsible for the supervision of the policies etc. at group level that are required under the anti-money laundering rules, see recitals 52 and 53 which provide as follows:

"(52) Where an obliged entity operates establishments in another Member State, including through a network of agents, the competent authority of the home Member State should be responsible for supervising the obliged entity's application of group-wide AML/CFT policies and procedures. This could involve on-site visits in establishments based in another Member State.

The competent authority of the home Member State should cooperate closely with the competent authority of the host Member State and should inform the latter of any issues that could affect their assessment of the establishment's compliance with the host AML/CFT rules.

(53) Where an obliged entity operates establishments in another Member State, including through a network of agents or persons distributing electronic money in accordance with Article 3(4) of Directive 2009/110/EC, the competent authority of the host Member State retains responsibility for enforcing the establishment's compliance

⁵ 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.

with AML/CFT rules, including, where appropriate, by carrying out onsite inspections and offsite monitoring and by taking appropriate and proportionate measures to address serious infringements of those requirements.

The competent authority of the host Member State should cooperate closely with the competent authority of the home Member State and should inform the latter of any issues that could affect its assessment of the obliged entity's application of group AML/CFT policies and procedures.

In order to remove serious infringements of AML/CFT rules that require immediate remedies, the competent authority of the host Member State should be able to apply appropriate and proportionate temporary remedial measures, applicable under similar circumstances to obliged entities under their competence, to address such serious failings, where appropriate, with the assistance of, or in cooperation with, the competent authority of the home Member State. (my emphasis)

Article 2 of the Fourth Anti-Money Laundering Directive is implemented into Danish law by s.1(1), point (9) of the Anti-Money Laundering Act which states that the Anti-Money Laundering Act applies to the branches of foreign undertakings which pursue activities as, inter alia, financial institutions in Denmark.

In this connection, the following is provided in the explanatory notes:

"If establishment has taken place, the authorities of the host country are responsible for supervising the branch's, the distributor's or the agent's compliance with the rules on measures to prevent money laundering and terrorist financing, whereas the home country retains responsibility for supervising the undertaking that provides the cross-border activity, including to ensure that the group has implemented policies and procedures, see in that regard ss.9 and 31 of the Bill.

The Fourth Anti-Money Laundering Directive provides in such cases for a close co-operation between the supervisory authorities of the home and host countries, see recital 52 of the Fourth Anti-Money Laundering Directive."

Similarly, the provisions of s.47(3) of the Anti-Money Laundering Act provide that:

"The Financial Supervisory Authority shall cooperate with the competent authorities of the EU or EEA Member States on participation in supervisory activities, on-site controls or inspections in Denmark in respect of undertakings and persons covered by s.1(1) point (9) which are subject to supervision in another EU or EEA Member State or a Danish undertaking or person covered by s.1(1) points (1) to (13) which is

subject to Danish supervision, but which operates in other EU or EEA Member States."

This provision is an implementation of Article 48(5) of the Fourth Anti-Money Laundering Directive.

As a new element, the Fourth Anti-Money Laundering Directive has directly considered how groups of companies domiciled in one Member State but with branches in other Member States are to deal with national anti-money laundering regulation. Accordingly, Article 45(2) provides that:

"Member States shall require that obliged entities that operate establishments in another Member State ensure that those establishments respect the national provisions of that other Member State transposing this Directive."

This provision thus establishes that a group of companies is obliged to ensure that the branches comply with the national anti-money laundering rules of the Member State in which the branch is located.

As the supervision of compliance with other legislation than Danish legislation rests solely with the authorities of the Member State concerned, this provision also emphasises that the supervision of branches rests with the financial supervisory authority of the Member State concerned.

The requirement of actual anti-money laundering policies was not introduced until the Fourth Anti-Money Laundering Directive. Therefore, the question of which country's supervisory authorities is responsible under the Third Anti-Money Laundering Directive for anti-money laundering policies, and thereby also the supervision of compliance with anti-money laundering policies etc. at group level, has not been considered separately.

3. OPINION

3.1 The supervision of compliance with anti-money laundering rules locally

The distribution of supervisory competence and powers in situations where a financial undertaking has set up branches in other Member States is regulated in detail in the EU directives when it comes to, for example, solvency supervision.

A similar explicit regulation of the distribution of responsibilities came somewhat later in the field of anti-money laundering and was thus only very explicit in the Fourth Anti-Money Laundering Directive.

Although the Third Anti-Money Laundering Directive does not explicitly regulate the distribution of responsibilities between national authorities, the effect of Article 22(2) of the Third Anti-Money Laundering Directive must be that if information of breach of anti-money laundering law is to be forwarded to the local financial intelligence unit, then the power to respond to the branch's breach of national anti-money laundering law must likewise rest with the supervisory authority of the Member State in which the branch is situated.

In my opinion, this means that in regard to money laundering, the supervisory responsibility under the Third Anti-Money Laundering Directive rests with the supervisory authority of the Member State in which the branch is situated, i.e. the host country. This interpretation of the Directive is also very clearly conveyed in the preparatory works of the Danish Anti-Money Laundering Act of 2006 in force at the time.

Similarly, it is my view that the amendment of the Danish Anti-Money Laundering Act in 2012 following the implementation of the First Payment Services Directive is in line with this view of the distribution of powers. The addition to the Danish Anti-Money Laundering Act, i.e. the specification of the supervision of a branch of payment institutions etc., would thus have been unnecessary if the former distribution of powers was not such that the responsibility of supervising branches rested with the supervisory authority of the host country.

In the drafting of the Fourth Anti-Money Laundering Directive, the distribution of responsibilities between the supervisory authorities of the home and host countries is clearly stated in both the recitals and the body of the Directive.

It is emphasised in particular that the supervisory authority of the host country is responsible for enforcing compliance with anti-money laundering rules, including by carrying out onsite inspections. This is motivated by the need for the competent authority to be the Member State in which the activities are in practice carried out, i.e. the host country.

On the basis of the above examination of the Third and Fourth Anti-Money Laundering Directives as well as the Danish implementation of the Directives it is my opinion that the Estonian financial supervisory authority was responsible for supervising compliance with the anti-money laundering rules by the Bank's Estonian branch throughout the entire period under review by the Danish Financial Supervisory Authority.

This opinion of the distribution of responsibilities between the Danish and Estonian financial supervisory authorities is supported by the joint statement by the two supervisory authorities of 28 May 2018.⁶

⁶ "Joint Statement by the Estonian FSA and the Danish FSA", dated 28 Maj 2018. The statement is available at the website of the Danish Financial Supervisory Authority.

According to the statement, the two supervisory authorities share the understanding that, as a general rule, the prudential supervising activity for cross-border operating banks lies with the financial supervisory authority of the home country.

At the same time, it follows from the joint statement that pursuant to the Fourth Anti-Money Laundering Directive the responsibility for supervising compliance with anti-money laundering rules by a branch rests with the supervisory authority of the host country, whereas the responsibility for supervising compliance with anti-money laundering rules at group level rests with the supervisory authority of the home country.

The joint statement does not consider whether the matter should be viewed differently on the basis of the Third Anti-Money Laundering Directive. As seen above, it is my opinion that the same distribution of powers in relation to the specific supervision of branches applied under the Third Anti-Money Laundering Directive.

3.2 The supervision of compliance with policies etc. at group level

As mentioned above, supervision at group level is not considered separately in the Third Anti-Money Laundering Directive, and the question thus remains whether the Danish Financial Supervisory Authority, due to its obligation to supervise the bank's Danish parent at group level, was nevertheless the competent supervisory authority to address breaches of anti-money laundering rules in the Estonian branch.

It is my opinion that the overall distribution of responsibilities, common to both the Third and the Fourth Anti-Money Laundering Directives, is such that the supervision of branches concerning money laundering matters rests with the local financial supervisory authority. The reasons for this according to recitals 52 and 53 of the Fourth Anti-Money Laundering Directive are that precisely a local supervisory authority is required in order to be able to control specific breaches of anti-money laundering law.

It is expressly stated in recitals 52 and 53 that the national supervisory authority is the competent authority, and it is also emphasised that undertakings are obliged to comply with the anti-money laundering rules of the country in which their branches are situated. Accordingly, the powers of the Danish Financial Supervisory Authority are not deemed to include addressing specific breaches committed by the bank's Estonian branch directly with the bank itself. This would be in breach of the principle that the supervision of compliance with anti-money laundering rules is territorial, and would imply a double supervisory obligation for the same matter.

The rule that the home country's supervisory authorities are responsible for supervising the compliance by branches with policies etc. at group level was not introduced until the Fourth Anti-Money Laundering Directive.

Hence, a similar provision did not apply at the time of the bank's breaches of anti-money laundering rules via the Estonian branch.

The question remains, however, whether the Danish Financial Supervisory Authority was nevertheless obliged, from a group level perspective, to supervise the lawfulness of the practices of foreign branches of Danish financial institutions. This is assessed not to be the case, since the Third Anti-Money Laundering Directive does not grant any real power to the supervisory authorities of the home country. Any active measures on the part of the authorities of the home country are therefore not assessed to be required.

On the basis of the above, it is my conclusion that the supervision of a branch's compliance with anti-money laundering rules rests with the local financial supervisory authorities, i.e. the supervisory authorities of the host country. In the matter at issue this means that the Estonian financial supervisory authority is responsible for supervising the Estonian branch's compliance with the anti-money laundering rules in Estonia. This follows from the territorial delimitation of the anti-money laundering rules. At the same time, pursuant to the Fourth Anti-Money Laundering Directive, the Danish Financial Supervisory Authority, in its capacity of supervisory authority of compliance at group level, is responsible for supervising that the requirements for anti-money laundering policies etc. are complied with.

If it should come to the attention of the Danish Financial Supervisory Authority that the anti-money laundering rules were not appropriately complied with at a group level, so that this had a spillover effect on the compliance with the rules by the bank's foreign branches, this would entail an obligation on the part of the Danish Financial Supervisory Authority to report to the competent supervisory authority of the relevant bank's branch, see recital 52 of the Directive.

As for the money laundering matter at issue, which concerns events that occurred in the period *before* the adoption of the Fourth Anti-Money Laundering Directive, the anti-money laundering law in force at the time did not include such supervisory obligation at group level on the part of the supervisory authority of the home country. Pursuant to the anti-money laundering rules then in force, the Danish Financial Supervisory Authority was not obliged to address matters relating to the bank's Estonian branch, including in relation to the content or enforcement of money laundering policies etc.

If a similar matter should occur today, the Danish Financial Supervisory Authority would due to its supervisory obligation at group level be obliged to notify the national supervisory authorities of any matters at group level that may affect compliance by foreign branches with local anti-money laundering rules, if the Danish Financial Supervisory Authority should be in possession of such information.

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