DeutscherAnwaltVerein

Position Paper

of the German Bar Association by the Committees on European Affairs, on Professional Rules and on Lawyer-Notaries

on the European Commission's Anti-Money-Laundering package of 20 July 2021

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The German Bar Association (Deutscher Anwaltverein – DAV) is the professional body comprising more than 61.000 German lawyers and lawyer-notaries in 252 local bar associations in Germany and abroad. Being politically independent the DAV represents and promotes the professional and economic interests of the German legal profession on German, European and international level.

Summary

The legislative package on Anti-Money Laundering and Countering Financing of Terrorism published by the European Commission on 20 July 2021 provides for measures by means of various legislative acts, which further harmonise the rules on combating money laundering at a Member State and Union level. It also contains legislative acts for new supervisory modalities.

In the following, the German Bar Association will highlight some points that are particularly relevant from the perspective of the German legal profession and from the perspective of the lawyer-notaries.

The DAV believes that the regulatory intensity of some of the measures in the legislative package exceeds what is necessary. This concern the drafts of (i) a Regulation establishing a new European Anti-Money Laundering Authority ("AMLA"),"AMLA Reg", (ii) a Regulation on combating money laundering and terrorist financing, "AML Reg", with directly applicable provisions, inter alia, in the areas of customer due diligence and beneficial ownership, as well as (iii) the Sixth Money Laundering Directive, "6th AMLD".

First of all, the DAV points out that - as the Commission admits - there has not been sufficient time to evaluate the measures already taken at the European and Member State level and the effectiveness of the existing, already complex normative framework for combating money laundering and terrorist financing.[1] The Commission states that *"a*

[1] Cf. "RESULTS OF EX-POST EVALUATIONS, STAKEHOLDER CONSULTATIONS AND IMPACT ASSESSMENTS", Explanatory memorandum of the proposal of the 6th AMLD.

full ex-post evaluation of the current EU AML/CFT regime has not yet taken place, against the background of a number of recent legislative developments. The fourth AML Directive was adopted on 20 May 2015, with a transposition deadline for Member States of 26 June 2017. The Fifth AML Directive was adopted on 30 May 2018, with a transposition deadline of 10 January 2020. Transposition control is still ongoing."

The DAV is concerned about the legislative escalation in the fight against money laundering and terrorist financing which lacks empirical basis. Although there is a widespread unanimity that money laundering and terrorist financing must be fought effectively and sustainably, it is contrary to the principle of good legislation to come to far-reaching conclusions resulting in the amendment of existing legislation even before obtaining a sufficient empirical basis for evaluating said legislation. This applies in particular to the non-financial sector. The findings of the European Court of Auditors Special Report cited by the Commission in the Explanatory Memorandum are only relevant with regard to the financial sector. Considering the lack of empirical findings, there is no justification - which is, however, required under rule of law considerations - for burdening the bond of trust between clients and their lawyers and lawyer-notaries through ever-increasing audit obligations. Clients perceive the duties as a general lack of trust on the part of the lawyers towards their own clients.

In the impact assessment accompanying the legislative package and in the recitals of the proposal of the 6th AMLD the Commission complains that „the quality and intensity of supervision performed by self-regulatory bodies has been insufficient“[2]. In addition, the FATF recommendations provided that when AML supervision is performed by self-regulatory bodies such as bars, they should themselves be subject to supervision by a public authority.

With regard to the German legal profession, this reasoning does not reflect the factual and legal situation: Even if one assumes that the money laundering supervision performed by the German Federal Bar (which consists of the local bars and has no direct powers to intervene against the individual lawyers) has not been sufficient in the

[2] Impact Assessment accompanying the Anti-money laundering package, SWD(2021) 190 final, page 10; Recital 69 of the proposal of the 6th AMLD.

past, the legal situation has changed considerably in 2017: Since the amendment of the Anti-Money Laundering Act (AMLAct) in 2017, implementing the 4th Anti-Money Laundering Directive, the local bars have been responsible for the anti-money laundering supervision. Due to their proximity to the individual lawyers, the supervision is therefore significantly more efficient. Moreover there are no empirical findings suggesting a failure or even a lack of effectiveness in the exercise of the supervisory powers by the local bars. The reports published on the websites of the local bars show that violations of the provisions of the Anti-Money Laundering Act are in fact sanctioned. The Commission has to provide proof of where exactly it sees the alleged deficits and on which actual findings it bases its conclusions in this respect.

A fundamental flaw is that the Commission has not yet sufficiently evaluated the existing legal framework for the prevention of money laundering in the non-financial sector and especially with regard to the legal profession. With each new regulatory step, the design flaw of transferring a system that was originally designed and only suitable for the financial sector to the legal and tax advisory professions becomes increasingly apparent. Lawyers and lawyer-notaries are aware of the fact that money laundering is a criminal offence. They unreservedly support the objective of combating money laundering and terrorist financing, and therefore regularly advise their clients in a manner that avoids triggering reporting obligations. The fact that local bars, which are responsible for money laundering supervision of the local lawyers, report - in the view of the EU Commission - a low number of suspicious cases is primarily due to the fact that there are either no indications of money laundering or that lawyers reject potential clients before entering into a client relationship in the case of suspicious behaviour by the potential client. If the lawyer is already in an attorney-client relationship and recognises that the client is planning to engage in an activity that falls under the scope of money laundering, it is the lawyer's duty to advise the client not to carry out the planned activity. However, in this case the lawyer is not obliged to report the matter.

I. Establishment of a new European Money Laundering Authority (AMLA)

1. Lack of evidence for the need and efficiency of an AMLA

A proposal that establishes a new European supervisory authority and accuses the existing supervisory bodies of not being sufficiently efficient requires a suitable explanation and justification, which the Commission fails to provide.

The new AMLA is to be entrusted with the coordination of the supervision of the supervisory authorities. The coordination effort is likely to be considerable. The question therefore arises as to which efficiency gains can be expected. There is, for instance, the threat of an additional administrative burden for the bars, which will be subject to considerable reporting obligations vis-à-vis the AMLA. It is further questionable, why the AMLA, as a European supervisory authority, should supervise the legal profession. The legal profession is not per se engaged in cross-border activities, so that the proportionality of a supervisory authority established at the European level seems problematic.

2. Threat of direct supervision of obliged entities

According to Art. 32 AMLA Reg, the AMLA shall be able to examine whether the supervisory activities of the supervisory authorities in the non-financial sector are in compliance with legal requirements. Furthermore it will be able to assess the existence of possible deficiencies. If legal requirements are not complied with or deficiencies are identified, it can address recommendations directly to the supervisory authority in order to remedy such non-compliance. This contradicts the basic assumption that the AMLA should not exercise direct supervision over obliged entities in the non-financial sector, as the power to give instructions to the supervisory authorities may lead to such direct supervision.

Specifically, according to Art. 32 (3) AMLA Reg, following a request for information, AMLA first makes recommendations to the national authority, which then has to take steps to comply with Union law within ten days. Otherwise, the AMLA shall issue a

formal opinion to the national supervisory authority pursuant to Art. 32 (4) AMLA Reg. In this case, Art. 32 (6) AMLA Reg provides as follows:

“Where the formal opinion referred to in paragraph 4 is addressed to a supervisory authority which is a public authority overseeing a SRB, and where it does not comply with the formal opinion within the period specified therein, to remedy such non-compliance in a timely manner, the Authority may adopt an individual decision addressed to an SRB requiring it to take all necessary action to comply with its obligations under Union law".

Therefore, in this case, the AMLA replaces the self-governing body. In this respect, it is problematic that the substantive limits of the AMLA's authority to make recommendations are not defined in more detail. The AMLA's supervision thereby threatens to change the character of supervision from a legal supervision of the Federal Ministry of Justice (BMJV) to a technical supervision at the European level. The core of functional self-governance, i.e. the concept that the bars carry out the supervision independently without interference of the public administration authorities, would thus be jeopardised.

It is therefore necessary to include an exception to Art. 32 (6) AMLA Reg for the benefit of the legal profession. At the very least, Art. 32 (6) AMLA Reg must be amended in a way that the AMLA will not be able to require the supervisory authority to take concrete measures, but is limited to controlling the lawfulness of the measures taken by the supervisory authority. Contrary to the current AMLA Reg, the AMLA will not have its own discretionary power to decide on the measures which are to be taken.

Proposed amendment to Article 32 (6) AMLA Reg

Where the formal opinion referred to in paragraph 4 is addressed to a supervisory authority which is a public authority overseeing a SRB, and where it does not comply with the formal opinion within the period specified therein, to remedy such non-compliance in a timely manner, the Authority may adopt an individual decision addressed to an SRB requiring it to take all necessary action to comply with its obligations under Union law. **The choice of the measures necessary to comply with this request is at the discretion of the SRB. The AMLA may only control the lawfulness of the measures taken by the SRB.**

II. Stricter the due diligence obligations for lawyers and lawyers-notaries

The DAV rejects the proposed intensifications of the due diligence obligations by the AML Reg. Pursuant to Art. 3 a) AML Reg, these obligations also apply to lawyers and lawyers-notaries as obliged entities, provided that they engage in one of the enumerated activities. It seems that the regulation proposes stricter due diligence obligations without sufficient empirical basis, thereby distancing itself from a risk-based approach. Subject to possible regulatory technical standards by the AMLA according to Art. 22 AML Reg, many obligations apply irrespective of whether there is an increased risk of money laundering.

The AML Regulation proposes, among other things, the harmonisation of due diligence requirements (Chapter III AML Reg), provisions on transparency with regard to beneficial owners (Chapter IV AML Reg) as well as reporting obligations (Chapter V AML Reg). Provisions that were previously the subject of the money laundering directives that left the Member States some room for manoeuvre in implementation (most recently the 4th and 5th Money Laundering Directives) are now incorporated in a regulation.

In the opinion of the DAV, the proposed regulation provides for unjustified intensifications of due diligence requirements, in particular in the following areas:

1. Obligation to identify the contracting party

According to Art. 18 (1) AML Reg, the obligations to identify the contracting party will be expanded considerably. Pursuant to the existing legal framework, obliged entities must already collect information on the first name and family name, place and date of birth, nationality and residential or postal address of natural persons (cf. Article 11 (4) no. 1 AMLAct). According to Article 18 (1) (a) AML Reg, information on profession and tax identification number are now to be collected as well. Since Art. 18 (4) AML Reg stipulates that all information must be verified based on reliable and independent sources, it is no longer sufficient to present a passport or identity card. This results in considerable additional (bureaucratic) work for the obliged entities and for the clients. The administration of a mandate is considerably more difficult with these stricter requirements.

For legal entities, as well, in addition to the requirements under Article 11 (4) no. 2 AMLAct, further identification information such as the tax identification number and - if available - the so-called “Legal Entity Identifier” must be collected. Pursuant to Art. 18 (1) (b) (iii) AML Reg, obliged entities must also verify on the basis of accounting documents or other relevant information whether legal entities (i.e. the potential client) have engaged in business activities. However, any such provision does not take into account that it is, in fact, permissible not to engage in business activities (e.g. only to manage one’s own assets). Nor can the mere fact that no business activity is pursued have as its effect that the lawyer may not accept the mandate without bias or that notaries may not notarize. Furthermore, it is not specified what qualifies as business activity and how it can be determined whether this criterion is met in a given case.

A real need for this additional information does not exist and could solely be justified in areas where there is an increased risk of money laundering. Therefore, the existing due diligence obligations are sufficient to make the lawyer or the notary aware of transactions involving the risk of money laundering.

2. Obligation to identify the beneficial owner

a. Collection of information

The DAV also considers the new obligations to identify beneficial owners as excessive. Pursuant to Article 11 (5) first sentence AMLAct, obliged entities currently only have to collect the first name and family name of the beneficial owner. Other identifying characteristics only have to be collected "*insofar as this is appropriate in view of the risk of money laundering or terrorist financing in the specific case*".

The proposal of the EU Commission now provides in Art. 18 (2) first sentence AML Reg that every obliged entity must collect the information on the beneficial owner specified in Art. 44 (1) (a) AML Reg. This information might also entail information that is not appropriate for the purpose of the prevention of money laundering and terrorist financing.

With regard to legal entities incorporated in the EU, this obligation is supplemented on the one hand by the obligation of the beneficial owners of the respective legal entity to provide those legal entities with the aforementioned information, Art. 45 (1) third sentence AML Reg. On the other hand, the legal entities, for their part, must provide the obliged entities with the information that the latter must collect for the purpose of conducting customer due diligence, Art. 45 (1) second sentence AML Reg, so that the obliged entities can fulfil their obligations under Art. 18 (2) first sentence AML Reg. However, there is no provision that relieves obliged entities of the obligation to collect certain information if the legal entity itself must take steps to enforce its right to information pursuant to Art. 45 (1) third sentence AML Reg and the information in question cannot be collected by the obliged entity in any other way or cannot reasonably be expected to be collected by the obliged entity.

In addition, it seems reasonable to provide for an exception such that a legal entity only has to provide the information and an obliged entity only has to collect the information that the national central registers make available to the obliged entities. This would take into account Art. 13 of the 6th AMLD, which allows the national legislature to bear in mind the protection of legitimate private or data protection interests with regard to the obligation of the legal entity to provide information to the central registers. It is not understandable why, on the one hand, a legal entity should be exempted from providing certain information to the central registers, but on the other hand, the obliged entities has to collect this information from the legal entity.

According to Art. 45 (1) AML Reg, there is no obligation for legal entities incorporated outside the European Union to collect the information pursuant to Art. 44 AML Reg. Nevertheless, Art. 18 (2) first sentence AML Reg is phrased in a manner suggesting that the obliged entities also has to collect this information from these legal entities. This cannot be correct. It is completely unclear how obliged lawyers or notaries are to obtain this very detailed information.

In this respect, it must be taken into account that the beneficial owner is not the contractual party, i.e. the potential client. The lawyer has no right to collect the

necessary data directly from the beneficial owners, because there is no attorney-client relationship between them. The same applies to notaries. But how can personal data then be collected from clients who, for their part, are not obliged to provide this information to the lawyer or the notary? What kind of coercion should the lawyer exert? Should the consequence be that the client who is not an obliged entity may not be advised by the lawyer? This does not only burden the bond of trust in the attorney-client relationship significantly. As a result, the client is denied access to justice in spite of his lawful conduct. In the notarial practice, this also leads to a non-participation in important legal transactions, such as the acquisition of houses, which must be carried out by notaries.

Therefore, in the case of legal entities incorporated outside the EU, a solution that takes these difficulties into account must be found. Article 48 (1) AML Reg is unsuitable to solve this problem. It stipulates that legal entities incorporated outside the EU must provide information on the beneficial owner in the central registers not only when they acquire real estate in their territory, but also when they enter into a business relationship with an obliged entity. In principle, the provision can therefore be seen as an instrument to collect data on beneficial owners. What may be appropriate and proportionate for real estate transactions – given the comparatively high risk of money laundering in this sector – is not, however, appropriate and proportionate in other sectors. To extend this principle to all sectors and contracting parties without exception and irrespective of risk of money laundering in the respective sector is, in the opinion of the DAV, disproportionate. There is no justification as to why this would be necessary to protect the public interest in a concrete and appropriate manner. Moreover, the question arises as to whether this can be implemented in practice.

b. Verification of information

Article 18 (4) first sentence AML Reg establishes the same requirements for the verification of the beneficial owner’s information as for the verification of a natural person’s information as a contracting party.

With regard to legal entities incorporated in the EU, this contradicts the risk-based approach. This is because, unlike in the case of the contracting party, not only the obliged entity but also the legal entity must verify the information on the beneficial owner. It should therefore at least be clarified that the obligations are concurrent, i.e. that the obliged entity is not subject to more extensive obligations than the legal entity. Moreover, it is unclear why the central registers only play a minor role in this case. It would be more reasonable to make the central registers the primary source of verification. The information requirements set out in Article 18 (4) second sentence AML Reg should therefore have priority over the information requirements under Art. 18 (4) first sentence AML Reg: In order to verify the information the obliged entity should primarily consult the central registers. Additional measures to verify the information shall only be taken if this appears to be risk-appropriate. This would correspond to the current legal situation in Germany introduced by the Transparency Register and Financial Information Act (cf. Article 12 (3) third sentence AMLAct).

For legal entities incorporated outside the EU, the verifications requirements must in any case be adapted for the reasons mentioned under lit. a above.

III. Missing exemptions

1. Exemptions for in-house lawyers

According to Art. 3 (3) b) AML Reg, „the following entities are to be considered obliged entities for the purposes of this Regulation: [...]

notaries and other independent legal professionals, where they participate, whether by acting on behalf of and for their client in any financial or real estate transaction, or by assisting in the planning or carrying out of transactions for their client concerning any of the following:
(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) organisation of contributions necessary for the creation, operation or management of companies;
(v) creation, operation or management of trusts, companies, foundations, or similar structures;“

The term "other independent legal professionals" suggests that in-house lawyers are not covered by the AML Reg. This seems appropriate. However, according to Art. 3 (1) of the 6th AMLD, it appears possible for Member States to expand the scope of application of this provision. „Where the national risk assessment carried out by Member States pursuant to Article 8 identifies that, in addition to obliged entities, entities in other sectors are exposed to money laundering and terrorist financing risks, Member States may decide to apply the requirements of [the AML Reg] to those additional entities.“ Since in-house lawyers only serve one client - their employer or its affiliated companies - it must be ensured that they remain exempt as far as possible from additional, purely bureaucratic anti-money laundering obligations.

Proposed amendment to Article 3 (3) b) AML Reg

b) notaries and other independent legal professionals **who are not [in-house lawyers]**, if they carry out financial or real estate transactions in the name and on behalf of their client or participate in the planning or execution of transactions on behalf of their client involving one of the following acts:

2. Exemptions for persons subject to professional secrecy from reporting discrepancies

The DAV suggests including provisions in the 6th AMLD to exempt persons subject to professional secrecy from the obligation to report discrepancies, as established by the case law of the CJEU and the ECtHR.

Thus, in the case "Ordre des barreaux francophones and germanophone et al." [3], the CJEU held that lawyers would be unable to carry out satisfactorily their task of advising, defending and representing their clients, if they were obliged, in the context of judicial

[3] C-305/05

proceedings or the preparation for such proceedings, to cooperate with the authorities by passing them information obtained in the course of related legal consultations. This would deprive the clients of the rights conferred on them by Art. 6 ECHR. The ECtHR also stated in "Michaud v. France"[4] that *"two factors are decisive in the eyes of the Court in assessing the proportionality of the interference. Firstly, as stated above and as the Conseil d'Etat noted, the fact that lawyers are subject to the obligation to report suspicions only in two cases: where, in the context of their business activity, they take part for and on behalf of their clients in financial or property transactions or act as trustees; and where they assist their clients in preparing or carrying out transactions concerning certain defined operations (the buying and selling of real-estate or goodwill; the management of funds, securities or other assets belonging to the client; the opening of current accounts, savings accounts, securities accounts or insurance contracts; the organisation of the contributions required to create companies; the formation, administration or management of companies; the formation, administration or management of trusts or any other similar structure; the setting up or management of endowment funds). The obligation to report suspicions therefore only concerns tasks performed by lawyers which are similar to those performed by the other professions subjected to the same obligation, and not the role they play in defending their clients."*

In recognition of this case-law, recital 9 of the AML Reg stipulates that*" there should […] be exemptions from any obligation to report information obtained before, during or after judicial proceedings, or in the course of ascertaining the legal position of a client, which should be covered by the legal privilege. Therefore, legal advice should remain subject to the obligation of professional secrecy, except where the legal professional is taking part in money laundering or terrorist financing, the legal advice is provided for the purposes of money laundering or terrorist financing, or where the legal professional knows that the client is seeking legal advice for the purposes of money laundering or terrorist financing."*

In the opinion of the DAV, these considerations are reflected in Art. 51 (2) AML Reg, which is a mandatory provision and not subject to the discretion of the legislature.

[4] Application no. 12323/11

3. Exception for the supervisory authorities

In addition to an exemption clause for the persons subject to professional secrecy, the AML Reg should also include an exemption clause for supervisory authorities with regard to the reporting of suspicious activities, if a person subject to professional secrecy has obtained information in the context of legal advice or legal representation and is therefore not obliged to report. Similar provisions already exist in Germany (see Article 44 (1) AMLAct), and should also be included in the AML-Reg. The considerations laid down in recital 81 of the AML Reg should be included in the operating part of the regulation. Otherwise, there is a risk that the protection of professional secrecy will be circumvented by the supervisory authorities.