The Proposal for a Fourth Anti-Money Laundering Directive

Joint Position of CEPI, the European Council of Real Estate Professions, and CEI, the European Confederation of Real Estate, on the proposal by the European Commission for a directive on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing published on 5 February 2013

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SUMMARY

The issue of anti-money laundering is of great importance to the real estate sector and estate agents are directly concerned by the requirements of Directive 2005/60/EC on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing. On 5 February 2013 the European Commission published a proposal for the revision of the Directive. In our position on the proposal we focus on a number of points including in particular:

- The inclusion of letting agents in the definition of estate agents amongst the obliged entities. We ask that this be deleted because we consider this to be a decision best made at the level of Member State according to the relevant risk attached to the letting sector in a particular country.

- The loss of the exemption for legal and natural persons who engage in a financial activity on an occasional or very limited basis. We ask for the recognition of the usefulness of such an exemption in the real estate sector and that it is made available to the obliged entities.

- Clarification of the parties to be checked in a real estate transaction. Here we suggest that the most appropriate way of identifying an estate agent's customer is by reference to the payment of the estate agent.

- Clarity concerning the rules on simplified due diligence. We ask that the requirements imposed on obliged entities concerning the identification of low risk transactions be reasonable and for clarification concerning the position of credit or financial institutions.

- The extended definition of politically exposed persons (PEPs). We think there is a particular concern here in the establishment of the source of wealth of foreign PEPs.

- Clarity concerning the rules on the prohibition of disclosure. In particular we would like the limited right of disclosure afforded to some obliged entities to be extended to estate agents.

- Clarity on third party reliance. Whilst recognizing the differences in national legal systems we ask for guidance as to how these rules should be applied.

- The identification of beneficial owners. We welcome the requirements imposed on Member States in this respect but are concerned that this information must be available to obliged entities without disproportionate cost.

- Clarity on reporting obligations. We ask that national authorities give clear guidance on the timing of transactions in the event of reporting.

- The sanctions available to authorities under the terms of the proposal which are harsher than in the current Directive. It is important that the sanctions are not disproportionate to the risk in a particular sector and do not present an unreasonable burden for SMEs.

- The requirement for criminal checks on obliged entities. We question how this can work in the real estate sector which is largely unregulated. Is the approach to regulation in the real estate sector consistent overall?

In conclusion we ask that these remarks be taken into account in consideration of the wording of the proposal and its eventual implementation.

Brussels, 16 May 2013

CEPI and CEI Position Paper on the 4th AML Directive

Introduction

The revision of the Third AML Directive is an important topic for the real estate sector. We support the fight against money laundering and recognise the need for action and collaboration at EU level. Clearly it is necessary to have strong rules in place at a European level but it is vital that those rules be proportionate to the risk involved in the particular activities concerned and that they do not represent an unreasonable burden on professionals working in the sector.

With regard to the detailed proposal for the revision of the Directive we have the following comments concerning the actual wording of the Directive, its eventual implementation and the issue of regulation in general.

1. The wording of the Directive

1.1. The inclusion of letting agents: Article 1

The activities of real estate professionals vary between countries (according to differences in national markets and legal systems). It is possible for such professionals to specialise in a particular activity or act in different capacities according to the nature of the transaction involved.

Estate agents are already included in the current Directive. This now applies also to letting agents who are included amongst the obliged entities in the current proposal, although without definition. This will potentially bring many more professionals in the real estate sector into the scope of anti-money laundering requirements. To refer to lettings agents here separately is confusing. In most countries in the EU (except notably the UK) letting agents do not exist as a separate profession.

It needs to be established that there is a genuine need at European level to justify this addition which could lead in some areas to unnecessary regulation. It may result in a lot of extra administration for minimum effect as in general letting agents are not seen as being as directly concerned as other agents by the risk of money laundering. Indeed at present letting agents are not required to comply with money laundering rules in some European countries in which it has been decided that the letting sector may be excluded because the level of risk is low.

In this respect we note that Article 4 of the proposed directive allows a Member State to apply the provisions to professions other than the obliged entities referred to in Article 2(1) if they engage in activities which are particularly likely to be used for money laundering or terrorist financing purposes. The level of risk associated with letting practices needs to be carefully assessed (i.e. are they holding client's money and the size of the market in different countries). The decision as to the inclusion of letting agents needs to be made at national level according to the level of risk and therefore it would be preferable to leave it to individual Member States to decide if letting agents should be included according to national particularities.

We ask that the words "including letting agents" be deleted from Article 1. (3) (d).

1.2. Removal of the exemption for occasional or limited activity: Article 2

Article 2(2) of the Third AML Directive provides an exemption for occasional or limited activity which is helpful and encourages proportionality. There is a remaining exemption for financial activity on an occasional or limited basis

in Article 2.2. of the proposal but it is not available to the obliged entities including estate agents. The new conditions attached to the exemption have considerably reduced its applicability. It is common for some estate agents to do a small amount of additional work which is ancillary to their main activity, for example trust and company work, or accountancy services. In our experience these ancillary services are only provided to customers who also use the principal service.

With regard to Article 2(2)(e) we cannot understand why occasional and limited activity cannot be exempt if it is performed by a legal or natural person that undertakes another Article 2(1) activity. Unless this is changed legal or natural persons providing a range of services will be disadvantaged as they will need to perform AML in situations in which single service companies will not. This cannot reflect either the risk based approach or the reference in recital (8) to directly comparable services being treated in the same manner. In fact there may be an argument that if additional services are provided the risks are decreased because if a range of services is provided a more holistic view can be formed of the customer.

A second supervisory cost may also be incurred unless Article 2(2)(e) is amended because self-regulation is allowed for estate agents but not for trust and company service provision. Therefore estate agents in a Member State that allows an SRO to supervise sales/lettings will need to be supervised separately for any trust and company work and this is likely to incur a separate fee.

We are concerned about the loss of the exemption and ask for recognition of the usefulness of such an exemption in the real estate sector. We ask that Article 2(2) (e) be deleted.

1.3. Who is an estate agent's customer?: Article 3

The proposal requires obliged entities to apply CDD measures when establishing a business relationship (Article 10(a)). The question for estate agents is when is a business relationship established and also which parties to a transaction must be checked? This is a point which should be clear to avoid confusion and duplication. We are also alarmed by reports from some of our members that some agents are being required to make checks on all potential customers, in other words all potential buyers who perhaps enquire about a property or view it, e.g. in Germany. This cannot be the intention behind the customer due diligence requirement.

Practice varies between countries as to whether an agent acts for one party only, seller or buyer or both. For example in the UK and the Netherlands it is common practice for an estate agent to act only for one party, seller or buyer but not both. In other countries, for example in Germany, Bulgaria and Austria, it is common practice for an estate agent to act for both buyer and seller.

There are other elements to this because in some countries it will be another estate agent (the principal agent) who has instructed the agent on a sub-agency basis. The customer of the sub-agent will be the other agent. Also according to Article 12(5) CDD requirements are to apply not only to new customers but also at appropriate times to existing customers on a risk sensitive basis. An estate agent may have a number of ongoing transactions for a particular customer, or a customer he/she has acted for in the past.

The information to which the agent has access concerning the respective parties will be different according to the level of involvement with that person. In the circumstances we consider that it is important that this point is made clear to avoid confusion and duplication. One of the reasons for the current confusion is the inconsistent use of the terms "customer" and "client" amongst agents in different Member States. The most satisfactory solution would be to agree that the party on which checks are to be carried out is the party or parties who actually pay the agent. In some countries this will be both buyer and seller (according to local practice) but in other countries it will be only one party.

It is important to know who an estate agent's customer is because this determines the identity of the person or legal entity to be checked. Our view is that the customer should be the natural person or legal entity who pays the bill.
We ask that the following addition be made to Article 3
(12) "customer" for the purposes of defining an estate agent's customer means the natural person who, or legal entity which, pays the estate agent.

1.4. Burden of responsibility on obliged entities: simplified due diligence: Articles 13-15 and Annex II

Obliged entities may apply simplified CDD measures in areas of lower risk as long as they first ascertain that the customer relationship or transaction presents a lower degree of risk and they carry out sufficient monitoring of the transaction or business relationship to enable the detection of unusual or suspicious transactions. However it is difficult for an estate agent to know the whole context of a transaction, and an estate agent is not an official state body. Because of this a more proportionate approach is needed.

The obligation is on the obliged entity to first make sure that this is a low risk transaction which is potentially unfair to businesses. This is a point which needs to be clarified together with the definition of an existing customer.
We ask that Article 13.2. be amended to read "obliged entities shall take all reasonable steps to ascertain that the customer relationship or transaction presents a lower degree of risk".

Whilst we support the risk based approach, the lack of any prescription in the area of simplified due diligence will be very unhelpful to obliged entities, and may also be unhelpful to Member States. The clarity of the Third AMLD in relation to credit and financial institutions was particularly helpful to estate agents when they acted for such institutions in relation to repossessions.

We ask that the substance of Article 11 (1) of the Third AMLD be added to Annex II of the proposal which provides a list of factors and types of evidence of potentially lower risk as:
(1) (d) Customers being a credit or financial institution covered by this Directive, or a credit or financial institution situated in lower geographical areas as set out in paragraph (3).

We also notice that the exemption for financial institutions in relation to beneficial owners of pooled accounts held by notaries and other independent lawyers contained in the Third AML Directive is not included in the proposal. We have already argued in the past that this exemption should be extended towards pooled accounts held by estate agents. Recital (8) of the fourth AMLD states that directly comparable services should be treated in the same manner when provided by any of the professionals covered by the Directive. In fact monies held by lawyers often relate to property transactions, and similarly monies held by agents also relate to property transactions. For this reason a consistent approach must be taken if the exemption is reinstated.

We ask that the exemption currently in Article 11.2. (b) of the Third AML Directive be reinstated and extended to pooled accounts held by estate agents. This could be added to Annex II of the proposal as:
(1) (e) Beneficial owners of pooled accounts held by notaries, other independent legal professionals and estate agents from the Member States or lower risk geographical areas as set out in paragraph (3), provided that the information on the identity of the beneficial owner is available, on request, to the institutions that act as depository institutions for the pooled accounts.

1.5. Politically exposed persons: Article 18(c)

The requirement to take adequate measures to establish the source of wealth and source of funds applies to foreign PEPs, and to domestic PEPs in cases of higher risk business. We question the source of wealth element as it can be very difficult to establish the provenance of funds. Legitimate wealth can come from a number of sources, such as inheritances, savings, or earnings from businesses or proceeds of property sales. One interpretation is that 'adequate measures' requires an analysis of these sources, which we view as an onerous obligation. The problem is aggravated further by the fact that foreign PEPs are likely to have foreign sources of wealth, which may be even more difficult for an agent to probe. We question whether this requirement is within the spirit of Article 8 which refers to proportionality in relation to the nature and size of the obliged entity.

We ask that in Article 18(c) the words "source of wealth" be deleted.

1.6. Prohibition of disclosure: Article 38(4), (5) & (6)

The Third AMLD, as well as these proposals, allows some categories of obliged entities and persons to disclose to each other when they act for the same customer in the same transaction. We request that these categories are now broadened to include estate agents and that the current limitation to disclosures between entities or persons in the same professional category is loosened.

In Member States where estate agents and lawyers work closely together on real estate transactions they regularly talk to each other about progress and problems. We believe it would assist law enforcement's own objectives if lawyers and agents could speak to each other, in confidence, about reports they have made to their FIU. Estate agents in all Member States have been subject to AML since the implementation of the Second AML Directive, and they have been subject to supervision since the implementation of the Third AML Directive. On this basis we believe that there is sufficient understanding in our sector to justify the amendment we are suggesting.

According to Article 38 of the proposal, obliged entities shall not disclose to the customer concerned or third parties that information has been transmitted or that an investigation is being carried out. There is a limited derogation from this in Article 38.4. However this does not extend to estate agents. We fail to see why this should not apply as it could be useful to groups in the real estate sector. The same point applies to Article 38.6. Therefore estate agents should be added to Article 38(6) as they also seek to dissuade clients (customers) from engaging in illegal activity. Agents often play a role in terms of taxes on real estate transactions, and also in relation to a range of other compliance issues connected to property that can be criminalised on breach, e.g. safety certificates.

We ask for recognition of the relevance of this issue to the real estate sector and that the obliged entities in Article 1. (3) (d). be incorporated into Articles 38.4, 38.5 and 38.6.

2. The eventual implementation of the Directive

2.1. Third party reliance: Article 24

The issue of third party reliance is an important one for the real estate sector because of the number of different parties involved in a real estate transaction. Indications are that this is little used, possibly because the party relying on a third party remains liable.

Third party reliance has the potential to significantly reduce the compliance costs borne by the public when making the biggest purchase of their lives in the acquisition of residential property. One of the major issues in this

context is the reference in Article 24 of the proposal to ultimate responsibility remaining with the obliged entity relying on the third party. In addition there are timing issues around when an estate agent forms a business relationship (as referred to previously in 1.3.).

There are practical problems around encouraging parties to agree to being relied upon, especially in circumstances where there is unlikely to be an ongoing relationship between the party relying and the party being relied upon. The professionals involved in real estate transactions may only deal with each other once or infrequently. In contrast financial institutions handle multiple transactions for multiple customers on a daily basis. There are also serious concerns posed by rules on data protection and identity theft.

There is also the problem that the estate agent is generally the first point of contact with the customer. However estate agents could also receive information from other obliged entities (for example, a previous estate agent that intervened in the dossier, a lawyer who could give information with regards to a company's statutes etc.). Therefore we believe that it should be made easier for agents to rely on others who may indeed be better informed about the financial structure behind transactions and would like to see the issue of third party reliance be reviewed with particular reference to the real estate sector.

We ask that guidance be issued to Member States as to how this should be implemented to avoid duplication and additional cost. For example this could be in the form of a framework for non-financial professionals setting out roles and responsibilities of different parties allowing reliance to greater extent on measures carried out by other covered entities.

2.2. Information about beneficial ownership: Articles 29 & 30

We welcome the greater clarification on beneficial owners in the proposal. This is a challenging issue for estate agents, particularly in the case of property transactions involving companies. It is often tax efficient for the ownership of assets that are as valuable as real property to be transferred to a corporation or trust which may be established solely for this purpose. Therefore the burden of checking beneficial ownership is of real significance for estate agents.

Access to accurate information is vital for estate agents if they are to meet their obligations. This information may be difficult or expensive to obtain from commercial databases. It can be particularly difficult and time consuming in the case of foreign registered or owned companies when it is not clear where the information is to be obtained. Therefore we welcome the provisions in the proposal concerning the provision of beneficial ownership information by companies, legal entities and trusts, but are concerned that Member States must not only implement these obligations in such a way as to prevent undue cost to obliged entities but must also enforce the requirement.

The obligation to require the availability of information about beneficial ownership must be implemented in such a way as to ensure that information on beneficial ownership is available readily and without disproportionate cost. It must also be clear that this is a responsibility for Member States which must be met in order for the obliged entities to be able to comply.

2.3. Reporting obligations: Article 34

We appreciate the importance of Article 34 (1), namely that Members States may give instructions not to carry out transactions. This is essential for asset confiscation. The issue for us is whether this needs to be balanced with some recognition of the speed of transactions. For example to be effective any instructions that a transaction must not go ahead must be prompt.

In the UK the Proceeds of Crime Act (2002) includes a system of 'appropriate consent' which requires reporters to delay transactions for a relatively short period after reporting, but also gives reporters the assurance of knowing that they can safely continue with transactions after the relevant time period has elapsed.

Member States should be encouraged to enter into a dialogue with their obliged entities about what would work best in this area. This is a particularly important area given the difficult situation that obliged entities can face if they are unable to proceed with a transaction but are unable to disclose why not because of the prohibition of disclosure, Article 38.

We ask that a request be addressed to national authorities to give clear guidance on this point in the implementation of the Directive.

2.4. Sanctions: Articles 55-58

Whilst we welcome the greater consistency of the proposal concerning the application of sanctions, the sanctions to be imposed are seen as harsh and represent a large increase from current figures. It is important that they are not disproportionate to the risk involved. It is to be hoped that guidance will be given concerning this in the implementation of the Directive.

The sanctions to be imposed must take account of damage caused and should not be unfair to SMEs

3. Regulation

We welcome the extension of the involvement of self-regulatory bodies to estate agents in Article 45(9). We are grateful for this inclusion and would expect any self-regulatory bodies in the sector taking on this role to comply with the requirements. There are additional points which we would like to make now concerning professional regulation which is an issue of great interest to the real estate sector**.**

The proposal foresees in Article 44(3) that Member States must ensure that competent authorities take the necessary measures to prevent criminals or their associates from being the beneficial owner or holding a management function in obliged entities. There are wide differences in levels of regulation in the real estate sector in which the professions are semi-regulated. Where regulation does exist, there are differences in detail and degree.

Whilst it is appropriate for Member States to control who can provide the services that have been defined as higher risk for money laundering, including estate agency, we question whether different DNFBP sectors should be supervised differently. As estate agents can hold vast amounts of money a check on personal solvency may be justifiable, and it may be easier to make a solvency check under the auspices of a broader fit & proper test.

We have followed for some time the debate in the EU over the issue of professional regulation and services. Over the period of recent years there has been a tendency towards deregulation, in particular with the Services Directive requiring the removal of unjustified professional restrictions which may impact on mobility. We are currently concerned with the modernisation of the Directive on the recognition of professional qualifications which foresees a mutual evaluation, or transparency exercise, between Member States concerning remaining professional restrictions.

Nevertheless, we also see a general trend towards the introduction of regulation in some areas which impact directly on the work of real estate professionals. We are thinking here for example of the requirements relating to

the energy efficiency of buildings in the recast Energy Performance of Buildings and the Energy Efficiency Directive. Estate agents carrying out ancillary work as intermediaries may also be concerned by the current proposals for a Directive on mortgage credit relating to residential property or the revision of the Insurance Mediation Directive.

Increasingly technical requirements are being imposed on professions which are not regulated in a number of EU Member States. We have to ask if this is a coherent approach – or should Europe look to support and complement these measures by introducing minimum rules for the real estate professions? Without such minimum rules it is difficult to foresee how authorities will be able to ensure that these requirements are met and indeed carry out the form of checks which are foreseen in this proposal.

Fit and proper tests, together with criminal checks, may be appropriate for all of the obliged entities covered by Article 2(1) (3). This implies preventative measures and it is likely that preliminary checks will have to be put in place.
This may be difficult to implement in the real estate sector which is largely unregulated. We question if it can work without some form of regulation being put in place.

Conclusion

It is important to know if the rules in the current Third AML Directive are effective, and if not, for what reasons. Rates of reporting in the real estate sector are low. It may be that this is due to a lack of awareness; it may also be that the rules are too complicated. It should be remembered that many of those businesses active in the real estate sector are SMEs. It is difficult for smaller real estate businesses in particular to comply with requirements which may be seen as bureaucratic and time consuming. We are happy to see that Recital 18 of the proposal recognises that it is appropriate to take account of the characteristics and needs of small obliged entities which fall within the scope of the Directive to ensure a treatment which is appropriate to their specific needs. We hope very much that this guidance will be fully followed in the implementation of the rules.

The implementation of the rules must also be consistent. Currently there are differences in the degree to which the Third AML Directive has been implemented with much stricter rules in some EU countries than others. Professionals need help from the authorities if they are to provide accurate and timely information. They also need more feedback from the authorities, such as when a report has been made concerning action which they should take. The authorities can also support professionals by, for example, providing clearer definitions of politically exposed persons (PEPs) and lists of such persons known to them. This is particularly relevant now that the proposal for the Fourth AML Directive extends its requirements to cover domestic PEPs.

There must be clear and effective rules in place against money laundering for the real estate sector. We support efforts to ensure that these are based on a risk-based approach and are proportionate to the risks and nature of activities involved. However in conclusion we also see a need for the simplification of the rules for professionals together with a need to avoid a disproportionate burden on SMEs, to ensure consistent implementation and to provide feedback for obliged entities. There must be clearer definitions, and reporting must be safe and confidential for the informant. Most importantly professionals need strong support from the authorities in order to be able to meet their obligations. Therefore we ask for the full co-operation of all concerned to ensure that rules against money laundering function properly in the real estate sector.