

# Denmark: Selected Issues



# DENMARK

## SELECTED ISSUES

June 2019

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June 7, 2019

Approved by  
**European Department**

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## Glossary

AML/CFT	Anti-Money Laundering and Combating the Financing of Terrorism
AMLD	Anti-Money Laundering Directive
CBR	Correspondent Banking Relationship
CDD	Customer Due Diligence
CIS	Commonwealth of Independent States
DFSA	Danish Financial Supervisory Authority
DNFBPs	Designated Non-Financial Businesses and Professions
EEA	European Economic Area
EU	European Union
FATF	Financial Action Task Force
FI	Financial Institution
FIU	Financial Intelligence Unit
FSSA	Financial System Stability Assessment
IO	Immediate Outcome
IT	Information Technology
MER	Mutual Evaluation Report
ML/(TF)	Money Laundering (and Terrorist Financing)
MLF	Money Laundering Forum
MLS	Money Laundering Secretariat
MOU	Memorandum of Understanding
NRA	National Risk Assessment
R	Recommendation (as in R.26, meaning "Recommendation 26")
RBA	Risk-Based Approach
SPSEIC	State Prosecutor for Serious Economic and International Crime
SRA	Sectoral Risk Assessment
SSM	Single Supervisory Mechanism
STR	Suspicious Transaction Report

# REINFORCING DENMARK'S CROSS-BORDER AML/CFT BANKING SUPERVISION: KEYS TO MAINTAINING MOMENTUM<sup>1</sup>

*In light of the Danske Bank case and in the context of a highly integrated Nordic-Baltic financial sector, this paper compares the money laundering (ML) threats and related supervisory vulnerabilities facing the region's largest economies, highlights Denmark's ongoing efforts to address those vulnerabilities, notes critical next steps, and provides recommendations aimed at maintaining the country's current momentum for reform.*

## Summary

The paper finds that Denmark has taken important steps to strengthen its anti-money laundering and combating the financing of terrorism (AML/CFT) supervision over the last two years—including via amendments to the AML Act, a significant increase in supervisory resources, and a concomitant increase in on-site inspections—and that these steps represent relevant and necessary responses to the ML risks facing Denmark.

The paper then recommends that the Danish authorities continue to build on this progress by: (i) adopting a comprehensive institutional risk assessment model or “scoreboard” that includes critical cross-border ML risk factors; (ii) intensifying AML/CFT on-site inspections by increasing their length and depth, particularly for higher-risk financial institutions (FIs) and with respect to the risk-based sampling of customer files;<sup>2</sup> (iii) expanding the powers of the Danish Financial Supervisory Authority (DFSA), including the authority to issue administrative fine notices for non-compliance with AML/CFT requirements; (iv) pursuing memoranda of understanding (MOUs) with the financial sector supervisors of all the non-European Union (EU)/non-European Economic Area (EEA) countries in which Danish banks maintain (or intend to open) overseas branches or subsidiaries; and (v) holding discussions within the Danish Cabinet, in consultation with all relevant authorities, as to ways to further integrate/consolidate AML/CFT supervision at the regional or sub-regional levels.

<sup>1</sup> Prepared by Jay Purcell (LEG), with contributions from Chun Jin (EUR), Maksym Markevych (LEG), and Ben Park (EUR).

<sup>2</sup> While the lengthening of on-site inspections is not a goal in and of itself, the current length of the average on-site inspection (one-to-two days) is insufficient to conduct all necessary supervisory activities, including the risk-based sampling of customer files.

## A. Introduction

### 1. **The Danske Bank case has drawn international scrutiny to the state of cross-border AML/CFT supervision in the Nordic-Baltic region and accelerated the momentum for reform.**

The possible laundering of approximately €200 billion in transfers through the Estonian branch of Danske Bank, Denmark's largest FI, has attracted the attention of national regulators and law enforcement agencies, as well as of international banking groups and members of the media. Given the high level of integration of the Nordic-Baltic financial sector—and other cross-border ML cases emerging in the Nordic countries—this attention has amplified the drive to strengthen AML/CFT supervision throughout the region.

**2. The Financial Action Task Force (FATF) has noted gaps in the AML/CFT supervisory frameworks of all the Nordic economies.** The FATF is the global AML/CFT standard-setter. Over the past five years, it has prepared mutual evaluation reports (MERs)—i.e., comprehensive, peer-led assessments—of Denmark (2017), Finland (2019), Norway (2014), and Sweden (2017), the Nordic-Baltic region's four largest economies. It found that the most significant gaps in Denmark's AML/CFT supervisory framework related to the authorities' lack of resources, as well as to their application of the risk-based approach (RBA), communication with supervised entities, and enforcement of compliance with relevant requirements.

**3. The Danish authorities have already addressed a number of these gaps and have demonstrated a high-level commitment to the implementation of additional reforms.** The parties comprising the outgoing Danish government, along with most of the other parties in parliament, concluded three political agreements—in June 2017, September 2018, and March 2019—aimed at reinforcing Denmark's efforts to counter money laundering and terrorist financing (ML/TF). Those agreements facilitated the adoption of a National AML/CFT Strategy and the enactment of AML/CFT legislation (Act No. 651 of 8 June 2017). The latter established, in law, the Money Laundering Forum (MLF), which is the key mechanism for domestic AML/CFT coordination, and required financial groups to implement group-wide programs to counter ML/TF, in line with the EU's fourth AML Directive (AMLD IV). Laws adopted in June and December 2018 enabled the DFSA to revoke an FI's license in response to gross violations of the AML Act and substantially increased the fines that may be levied in response to failures to comply with that act.<sup>3</sup> The increase was achieved by requiring courts to index their fines to companies' net turn-over at the time of violation. As of July 2019, fit and proper requirements will be applicable to AML/CFT compliance officers.<sup>4</sup>

**4. Moreover, the Danish government has allocated substantial new resources to AML/CFT.** The outgoing Danish government boosted the budgets of both the Money Laundering Secretariat (MLS, Denmark's Financial Intelligence Unit) and the DFSA. The MLS hired additional staff in 2018 and will continue to hire in 2019; not including the head of the Unit, it will have 26 full-time

<sup>3</sup> Act No. 442 of 11 May 2007, as amended.

<sup>4</sup> Per Act No. 552 of 7 May 2019 (The Financial Business Act).

equivalents by July 1, 2019. The DFSA established an AML Division and increased the number of AML-dedicated staff from 3.5 to 14.5, developed a new institutional risk scoring and assessment model, and significantly increased its conduct of AML/CFT on-site inspections. (See Table 1, below, for a brief summary of Denmark's key AML/CFT institutions and their respective roles.)

<b>Table 1. Key AML/CFT Institutions in Denmark</b>	
<b>Institution</b>	<b>Role</b>
<b>Danish Financial Supervisory Authority</b>	<b>Supervision</b> – Monitor and enforce FIs' compliance with AML/CFT-related obligations, exchange information with foreign counterparts, chair the Money Laundering Forum, head Denmark's delegation to the FATF.
<b>Money Laundering Forum</b>	<b>Coordination</b> – Coordinate risk assessments and other ML/TF measures as between the relevant supervisory and law enforcement authorities.
<b>Money Laundering Secretariat</b>	<b>Financial Intelligence</b> – Receive, analyze, and disseminate suspicious transaction reports (STRs); exchange information with foreign counterparts.
<b>Police Districts</b>	<b>Law Enforcement</b> – Investigate and, as appropriate, prosecute ML/TF.
<b>State Prosecutor for Serious Economic and International Crime</b>	<b>Law Enforcement</b> – Investigate and, as appropriate, prosecute ML and the violation of related obligations under Danish law.

**5. This paper provides recommendations aimed at further strengthening Denmark's AML/CFT supervisory framework and its effectiveness in mitigating cross-border ML risks.**

Fund staff has not attempted to duplicate the FATF process or reproduce or otherwise revisit the conclusions of the authorities' January 2019 *Report on the Danish FSA's Supervision of Danske Bank as Regards the Estonia Case*. Rather, it has crafted a forward-looking assessment built on two pillars. First—and at the request of the Danish authorities—staff conducted a desk-based benchmarking exercise to estimate Denmark's ML risk as a function of the relative threats and vulnerabilities facing the four largest economies of the Nordic-Baltic region (Denmark, Finland, Norway, and Sweden). This exercise supported staff's effort to understand Denmark's risk profile and, ultimately, to gauge the sufficiency of its AML/CFT supervisory efforts and resources. Second, staff performed a targeted analysis to: (i) evaluate the ability of Denmark's AML/CFT supervisory framework to mitigate current cross-border ML risks; and (ii) identify recommendations to bolster its effectiveness.

## **B. Benchmarking ML Risks in Denmark**

### **Threats**

**6. Fund staff conducted a desk-based analysis of Nordic banks' exposure to potentially higher-risk countries, proxied by their networks with, and inflows from, those countries.** Staff defined the networks by mapping the branches, subsidiaries, and correspondent banking relationships (CBRs) of Danish, Finnish, Norwegian, and Swedish banks in and with countries presenting potentially higher ML risks in the Nordic context. Those countries were selected based on the dynamics of several recent ML cases in the region, all of which involved the possible laundering of funds that originated in the Commonwealth of Independent States (CIS) and passed through intermediary countries, including the Baltics, on their way to other, primarily Western, FIs. Staff also analyzed copyright-protected third-party statistics on the financial flows to the Nordic countries from both the CIS and the Baltics.

**Table 2. AML/CFT Supervision in Denmark: Recommendations<sup>1</sup>**

<b>Recommendations</b>	<b>Lead Authority</b>	<b>Time Frame</b>
<b><i>International and Domestic Cooperation</i></b>		
<i>Pursue MOUs with DFSA counterparts in all the non-EU/EEA countries where Danish banks maintain (or intend to open) overseas branches or subsidiaries.</i>	DFSA	Near-Term
Ensure that the MLS is proactive in sharing with the DFSA analysis of STRs that may indicate a shift in banks' institutional risk profiles or changes in the approach or quality of their reporting.	MLS	Near-Term
Complete and adopt the planned update to the MLF MOU.	All Authorities	Near-Term
Participate, as feasible, in both periodic and event-driven joint inspections of Danish banks' higher-risk overseas branches and subsidiaries.	DFSA	Near-Term
Reinforce existing stand-alone or embedded MOUs with foreign counterparts, as necessary and feasible, to fill procedural gaps and establish a certain degree of automaticity with respect to key forms of cooperation (e.g., information exchange and the conduct of joint inspections).	DFSA	Medium-Term
<i>Hold discussions within the Danish Cabinet, in consultation with all relevant domestic authorities, as to ways to further the integration/consolidation of AML/CFT supervision at the regional or sub-regional levels and arrive at a formal governmental position on this issue.</i>	Cabinet	Medium-Term
Issue findings on the feasibility and benefits of a private sector-led CDD utility, and its potential mobilization to support AML/CFT supervision.	MLF+	Medium-Term
<b><i>Implementing the Risk-Based Approach</i></b>		
<i>Adopt a comprehensive institutional risk assessment model or "scoreboard" that includes specific, cross-border ML risk factors.</i>	DFSA	Near-Term
Issue annual, electronic questionnaires to banks and other critical segments of the financial sector—or establish automatic reporting requirements—to gather the institution-level data that will be required for the planned adoption of a new DFSA "scoreboard."	DFSA	Near-Term
Conduct an internal review, at the conclusion of the 2019–2020 inspection cycle, to determine whether the current on-site inspection plan was sufficiently flexible to address fast-moving developments and permit adequate follow-up on suggestive initial findings.	DFSA	Medium-Term
<b><i>DFSA Resources, Procedures, and Powers</i></b>		
<i>Fully and expeditiously implement, in law, the March 2019 political agreement to expand the DFSA's powers, including the authority to issue administrative fine notices for non-compliance with AML/CFT requirements.</i>	Cabinet, Parliament	Near-Term
Develop a comprehensive AML/CFT on-site inspection manual.	DFSA	Near-Term
<i>Intensify AML/CFT on-site inspections by increasing their length and depth, particularly for higher-risk FIs and with respect to the risk-based sampling of customer files.</i>	DFSA	Near-Term
Complete the hiring and training of new inspectors to bring the DFSA's AML Division to full strength and develop a formal staff retention plan.	DFSA	Near-Term
Update the DFSA's standard follow-up procedures with respect to observed violations of AML/CFT requirements so as to incorporate the full range of its current and future sanctioning powers.	DFSA	Medium-Term
Maintain comprehensive statistics regarding the DFSA's actions in line with its current and future enforcement powers, both to ensure the consistent treatment of FIs and to enable an accurate evaluation of effectiveness.	DFSA	Medium-Term

<sup>1</sup> Priority recommendations are noted in *italics*. Near-Term is one year; Medium-Term is two–three years.



**7. Staff’s analysis of the level of ML threat facing the Nordic countries is subject to four important caveats.** First, banking networks are an integral part of the worldwide “financial plumbing” through which millions of payments and other legitimate transactions flow; their mere presence does not imply abuse. Second, the data analyzed do not reveal the nature or extent of the financial flows moving through each of these networks; some bank branches may serve only a small number of specific (e.g., corporate) clients and some CBRs may go largely unused over extended periods of time. Third, the banks headquartered in Denmark ranked second to last in terms of their overall assets in April 2019, according to Banker’s Almanac, a figure that bears noting for context. And fourth, no single indicator can fully or fairly capture the level of ML threat facing a country. Still, staff considers the data regarding bank networks in potentially higher-risk countries, along with the flows from these countries to the Nordics, to be reasonable proxies for the level of ML threat, as they reflect the Nordics’ exposure to customers living, operating, or maintaining other ties in countries presenting relatively elevated ML threat levels.

**8. Compared to its Nordic peers, the extent of Danish banks’ exposure to potentially higher-risk countries suggests a substantial level of ML threat.** Of the four Nordic economies analyzed in this paper, Denmark had the second most extensive banking network in potentially higher-risk countries, measured by branches, subsidiaries, and CBRs, as of April 2019.<sup>5</sup> These results are consistent with the data on financial inflows described above, which also suggest that Denmark faces a substantial level of ML threat by comparison with its Nordic peers.

## Vulnerabilities

**9. Fund staff reviewed the supervision-focused sections of the most recent FATF MERs for the largest countries in the Nordic region.**<sup>6</sup> Staff compared the Nordic countries’ ratings and associated analysis for Recommendation 26 (R.26) and Immediate Outcome 3 (IO.3) to capture the most relevant gaps in their AML/CFT supervisory regimes.<sup>7</sup> <sup>8</sup> In combination with the “threats” identified in the previous section, these gaps, which function as proxies for the Nordic countries’ ML/TF “vulnerabilities,” are critical to understanding Denmark’s risk profile.

<sup>5</sup> Changes in the banking network that occurred after April 2019 were not considered as part of this analysis. Note, for example, Danske Bank’s February 2019 announcement that it would close its Russian subsidiary and Baltic branches by the end of the year.

<sup>6</sup> Specifically, staff reviewed the MERs of Denmark (August 2017), Finland (April 2019), Norway (December 2014), and Sweden (April 2017), as well as the follow-up reports submitted by Denmark (in October 2018), Norway (in March 2018 and March 2019), and Sweden (in June 2018).

<sup>7</sup> R.26 assesses the extent to which financial institutions are subject to both comprehensive licensing requirements and active, risk-based AML/CFT supervision. IO.3 assesses the extent to which supervisory authorities are effective in preventing criminals from holding controlling interests or management functions within FIs and identifying and addressing the violation of AML/CFT-related requirements.

<sup>8</sup> Other FATF recommendations (e.g., R.18, R.40) and immediate outcomes (e.g., IO.2, IO.4), contain elements related to cross-border AML/CFT supervision, but the corresponding ratings are determined by a much broader range of factors, making them ill-suited for inclusion in this focused comparison.

**10. Denmark's AML/CFT supervisory regime ranked just behind those of its Nordic peers, suggesting that its financial system was somewhat more vulnerable to ML/TF threats.** The FATF rated Denmark "partially compliant" with its key recommendation on AML/CFT supervision.<sup>9</sup> It rated as "low" the Danish authorities' effectiveness in mitigating ML/TF risks via supervision.<sup>10</sup> These ratings effectively rank Denmark's AML/CFT supervisory regime just behind those of its Nordic peers. The current ratings for all four countries are presented in Table 3, below.

<b>Table 3. Nordic Countries' FATF Ratings for AML/CFT Supervision</b>		
<b>Country (MER Year)</b>	<b>Rating on R.26 (Technical Compliance)<sup>1</sup></b>	<b>Rating on IO.3 (Effectiveness)</b>
<b>Denmark</b> (2017)	Partially Compliant	Low
<b>Finland</b> (2019)	Largely Compliant	Low
<b>Norway</b> (2014)	Compliant <sup>2</sup>	Moderate
<b>Sweden</b> (2017)	Partially Compliant	Moderate
<sup>1</sup> Both Denmark and Sweden have received re-ratings from the FATF since the adoption of their 2017 MERs, however these re-ratings did not address R.26 and, as such, they are not reflected in this table. <sup>2</sup> Norway was rated "partially compliant" on R.26 when its MER was first published, in December 2014. Since then, the FATF has re-rated Norway twice, based on its progress in addressing the identified deficiencies in its AML/CFT supervisory framework. Norway is now assessed to be "Compliant" with R.26.		

### C. Focusing on Key Elements of Cross-Border AML/CFT Supervision in the Danish Banking Sector: International and Domestic Cooperation

**11. International and domestic cooperation are critical to effective cross-border banking supervision.** As Danish banks maintain branches and subsidiaries overseas, as well as a significant number of CBRs—sometimes with FIs in higher-risk countries—the DFSA's ability to exchange information with foreign counterparts, conduct joint inspections, and work closely with other Danish stakeholders is critical to effective cross-border banking supervision. Close international and domestic cooperation may enable the early detection of new and evolving threats, support the identification of deficiencies in banks' internal controls, and facilitate law enforcement investigations.

#### International Cooperation to Mitigate Cross-Border ML/TF Risks

**12. Danish law permits the DFSA to exchange information with EU/EEA counterparts and within supervisory colleges, even in the absence of specific bilateral agreements.** Since the enactment of Act No. 1556 of 21 December 2010, Denmark has maintained the necessary authorities to exchange information with its counterparts in EU/EEA countries and with other members of either the Nordic Supervisory College or of bank-specific supervisory colleges within the EU, whether spontaneously or upon request. In addition, the agreements underpinning each supervisory college

<sup>9</sup> This is the second-lowest of the four available ratings for technical compliance: "Non-Compliant," "Partially Compliant," "Largely Compliant," and "Compliant."

<sup>10</sup> This is the lowest of the four available ratings for effectiveness: "Low," "Moderate," "Substantial," and "High."

contain “embedded” MOUs that address the conduct of joint inspections, the sharing of the results, and cooperation in the case of possible violations.

**13. The DFSA interprets Danish law as establishing an “obligation” to cooperate with EU/EEA counterparts, even if foreign authorities may not recognize any reciprocal obligation.**<sup>11</sup>

Prior to the full, EU-wide transposition of AMLD V, the absence of bilateral MOUs between the DFSA and its closest (EU/EEA) counterparts represents a temporary gap in the regional framework, whereby the key forms of cooperation noted above are currently enabled, but not guaranteed. This means, for example, that DFSA requests for information or cooperation from its EU/EEA partners may be denied or responses to those requests may be delayed without any law, MOU, or other agreement having been breached.

**14. Outside of the EU/EEA and of supervisory colleges, the DFSA may only exchange information on the basis of a bilateral MOU or international cooperation agreement.** Thus far, the DFSA has concluded only one AML/CFT-specific MOU, with its counterpart in Dubai.

**15. The range of the DFSA’s arrangements for international supervisory cooperation is too narrow, given the current networks of Denmark’s international banking groups.** Although only four Danish banks currently maintain branches or subsidiaries abroad, some are in non-EU, non-EEA countries in which the DFSA has yet to conclude MOUs with its local counterparts, i.e., Australia, Brazil, Hong Kong SAR (China), India, Russia, Singapore, and Switzerland.

**16. Further testing will be required before the effectiveness of those arrangements can be fully assessed.** Over the past three years, the DFSA has not exchanged AML/CFT-related information with non-EU/non-EEA counterparts, nor has it made or received AML/CFT-related spontaneous disclosures to/from such counterparts. Outside of the two supervisory colleges in which it currently participates, the DFSA has not shared inspection reports with foreign counterparts, although abridged versions of those reports are published on-line, such that interested supervisory authorities may have access to the information they need without issuing a formal request. The first joint AML/CFT on-site inspection of a Danish FI took place only recently: at Danske Bank in March 2019, with the participation of the Finnish, Norwegian, and Swedish financial supervisory authorities, as members of the Danske supervisory college. As of April 2019, the DFSA had not taken part in a joint AML/CFT on-site inspection outside of Denmark.

**17. The authorities support greater international cooperation on AML/CFT supervision and are exploring the possibility of enhanced information-sharing at the national and EU levels.**

The authorities universally acknowledge the utility—and necessity—of bolstering international cooperation on AML/CFT supervision, particularly within established regional groupings and supervisory colleges. Indeed, on May 8, 2019, the financial supervisory authorities of all the Nordic-Baltic states formed a permanent working group to maintain regular contact and exchange experiences and information with the goal of bolstering their effectiveness in combating ML.<sup>12</sup>

<sup>11</sup> Specifically, Section 56, Sub-Section 3 of the AML Act.

<sup>12</sup> Denmark, Estonia, Finland, Iceland, Latvia, Lithuania, Norway, and Sweden.

**18. However, there is no settled view within the country as to the desirability of formally integrating AML/CFT supervision, whether at the regional or sub-regional levels.** A political decision, likely made within the Cabinet, would be necessary for Denmark to support—let alone pursue—the formal/legal integration of AML/CFT supervision at the Nordic, Nordic-Baltic, or European levels.<sup>13</sup> The primary options for doing so are: (i) strengthening existing structures and mechanisms for *ad hoc* AML/CFT supervisory cooperation; (ii) consolidating off-site supervision at the regional (European) or sub-regional (Nordic-Baltic) levels; (iii) integrating AML/CFT supervision at the Nordic or Nordic-Baltic levels, outside the context of the EU treaties; (iv) integrating AML/CFT supervision among interested European partners, in the context of the EU’s “enhanced cooperation” procedure; and (v) fully integrating AML/CFT supervision with the EU, under the auspices of an EU agency (Table 4).<sup>14</sup> Some Danish stakeholders view greater and broader European AML/CFT integration as a key step toward strengthening the supervision of international banking groups. Others prefer to enhance cooperation as-needed, to address specific cases, or only within the narrower confines of the Nordic-Baltic region, e.g., the Nordic-Baltic Stability Group. Either way, there is consensus that the Danish government should empower and encourage the (now better resourced) DFSA to make full use of both new and longstanding structures and mechanisms for international cooperation while considering more substantial changes.

### **Domestic Cooperation to Mitigate Cross-Border ML/TF Risks**

**19. The Danish authorities took an important step toward enhancing domestic cooperation to mitigate cross-border ML/TF risks by enshrining in law the role of the MLF.**

The MLF is the primary forum for AML/CFT-related cooperation within Denmark, including as between the relevant supervisory and law enforcement authorities. Although it has been in existence for over 13 years and has an MOU dating from 2013, it was established in law in 2017, via Section 74 of the AML Act. That section requires the Minister of Industry, Business, and Financial Affairs to establish the MLF, which is to “coordinate the authorities’ risk assessments and general measures against money laundering and financing of terrorism.” The MLF functions at the technical (vs. political) level; the full scope and specific modalities of its work are laid out in an MOU that is currently being updated.

**20. The DFSA and the financial intelligence unit (FIU), have a collaborative working relationship.** Danish law effectively requires the DFSA and the FIU (the MLS) to cooperate, including with respect to the sharing of information originally obtained from the private sector, and collaborative working relationships have developed at the staff and leadership levels. The DFSA and the MLS interact both formally, via the MLF, and informally, via *ad hoc* discussions. Going forward, the National AML/CFT Strategy calls for an analytical center to be stood up as the “operational arm”

<sup>13</sup> In the context of the 2018 Euro Area Financial System Stability Assessment (FSSA), Fund staff recommended considering the establishment of a European-level institution responsible for AML/CFT supervision. The full assessment may be accessed on-line at: <https://www.imf.org/en/Publications/CR/Issues/2018/07/19/Euro-Area-Policies-Financial-System-Stability-Assessment-46100>.

<sup>14</sup> Future arrangements will need to consider that Iceland and Norway are not EU members, and that Denmark and Sweden do not currently participate in the Single Supervisory Mechanism (SSM).

of the MLF. This initiative is mentioned in the March 2019 political agreement, which states the intention to foster closer cooperation among the DFSA, the MLS, and other key authorities. The center would work to ensure that the full range of administrative, intelligence, and law enforcement tools is brought to bear on the handling of individual ML/TF cases.

**21. The DFSA and the FIU share information to support their respective activities.** Prior to AML/CFT on-site inspections, the DFSA requests information from the MLS on the quantity and quality of STRs received from the relevant bank or money remitter.<sup>15</sup> The MLS also provides insight into any changes in the FI's reporting patterns, including in the context of broader reporting trends. Separately, the MLS sends the DFSA occasional spontaneous disclosures, whether based on its own analysis of STRs or on information provided by foreign counterparts. By contrast, it appears relatively rare that the MLS shares with the DFSA and other relevant domestic supervisors impromptu analysis of emerging ML risks, trends, or methods, suggesting a potential area for increased interaction. The MLS maintains the capacity for such analysis, as demonstrated by its preparation of quarterly reports detailing STR reporting patterns and highlighting new or evolving ML/TF threats. Those reports put a heavy emphasis on cross-border financial flows. For its part, the DFSA is a reporting entity by law. Hence, it has both the ability and obligation to submit STRs as necessary and appropriate, for example, upon discovering transactions that it would view as suspicious or potentially suspicious during an on-site inspection, but that were not considered as such by the relevant FI and so never reported. In practice, however, it is somewhat exceptional for the DFSA to submit an STR, as it may also order an FI to revisit certain transactions and report (or consider reporting) them to the MLS directly.

**22. The DFSA and the State Prosecutor for Serious Economic and International Crime (SPSEIC) also have a close and productive working relationship.** The DFSA and SPSEIC, which is the parent body of the (operationally independent) MLS, concluded an MOU in 2016. The MOU is sufficient to cover the two primary contexts in which the DFSA and SPSEIC have reason and occasion to work closely together: DFSA referrals to the SPSEIC of cases of apparent FI non-compliance with AML/CFT-related obligations (for investigation and possible prosecution) and DFSA support of financial investigations led by the SPSEIC (via the provision of expertise regarding complex transactions or of information from the DFSA's foreign counterparts). In addition, the DFSA and SPSEIC meet quarterly to coordinate their work at the technical level and at least twice a year at the top management level. This means that these authorities benefit from close bilateral cooperation, even if the results of that cooperation are only visible to the public in certain, specific cases. Since 2016, the DFSA has reported three FIs to the SPSEIC for (potential) violations of the AML Act: the first was fined for its failure to obtain adequate information on its correspondents; the second is still being investigated; and the third was referred for resolution.

<sup>15</sup> STRs are confidential disclosures made by banks, other financial institutions, and designated non-financial businesses and professions (DNFBPs), such as accountants, lawyers, and notaries, to a national FIU, based on the suspicion that a client may be engaged in money laundering, terrorist financing, or related criminal activity. STRs are then analyzed by the FIU and, when appropriate, disseminated to law enforcement for possible investigation.

**Table 4. Options for AML/CFT Supervisory Integration at the Regional or Sub-Regional Levels**

Option	Description	Necessary Conditions/Pre-Conditions
<b>Strengthen Existing Structures and Mechanisms</b>	Enhancing AML/CFT supervisory cooperation via the full use of existing structures (e.g., supervisory colleges) and mechanisms (e.g., bilateral MOUs).	<ul style="list-style-type: none"> <li>Coordination among existing structures, in cases of overlap.</li> <li>Willingness to conclude new MOUs as and when necessary or desirable, and to update existing “embedded MOUs,” to reduce ambiguity.</li> </ul>
<b>Consolidation of Off-Site Supervision at the EU or Nordic-Baltic Levels</b>	Requiring FIs to report information to a regional or sub-regional authority in charge of <i>off-site</i> supervision (to include generating institutional risk profiles, determining parts of the inspection plans of the competent national authorities, and receiving and analyzing those authorities’ on-site inspection reports).	<ul style="list-style-type: none"> <li>The support of Denmark’s Nordic-Baltic or European partners.</li> <li>If pursued within the EU framework, consideration of any impediments posed by the Danish EU opt-out(s) and the relevant EU procedures.</li> <li>Changes to applicable national laws (in particular, those that assign AML/CFT supervisory and related sanctioning powers).</li> <li>Full analysis and understanding of relevant differences in national AML/CFT laws.</li> </ul>
<b>Integration at the Nordic or Nordic-Baltic Levels</b>	Formally integrating AML/CFT supervision at the Nordic or Nordic-Baltic levels, outside the context of the EU treaties (e.g., via the Nordic-Baltic Stability Group).	<ul style="list-style-type: none"> <li>The support of Denmark’s Nordic-Baltic partners.</li> <li>Changes to applicable national laws (in particular, those that assign AML/CFT supervisory and related sanctioning powers).</li> <li>Full analysis and understanding of relevant differences in national AML/CFT laws.</li> <li>Governance arrangements that maximize transparency, consistency, and effectiveness.</li> </ul>
<b>Integration via the EU’s “Enhanced Cooperation” Procedure</b>	Formally integrating AML/CFT supervision among a “vanguard” of at least nine interested EU members, with other EU members retaining the right to join the enhanced cooperation at any time.	<ul style="list-style-type: none"> <li>An extended stalemate within the EU as a whole.</li> <li>Consideration of any impediments posed by the Danish EU opt-out(s).</li> <li>The support of at least eight other EU members.</li> <li>Authorization from the EU Council, based on a proposal of the EU Commission, after obtaining the consent of the European Parliament.</li> <li>Changes to applicable national laws (in particular, those that assign AML/CFT supervisory and related sanctioning powers).</li> <li>Full analysis and understanding of relevant differences in national AML/CFT laws.</li> <li>Governance arrangements that maximize transparency, consistency, flexibility (given that other countries could ultimately choose to participate), and effectiveness.</li> </ul>
<b>Full Integration within the EU</b>	Formally integrating AML/CFT supervision within the EU, under the auspices of an EU agency (in effect, EU agreement to establish something akin to the “single supervisory mechanism”, but for AML/CFT supervision and on an obligatory basis).	<ul style="list-style-type: none"> <li>Consideration of any impediments posed by the Danish EU opt-out(s).</li> <li>The support of all EU members.</li> <li>Changes to applicable national laws (in particular, those that assign AML/CFT supervisory and related sanctioning powers).</li> <li>Full analysis and understanding of relevant differences in national AML/CFT laws.</li> <li>Governance arrangements that maximize transparency, consistency, and effectiveness.</li> </ul>



**23. To foster public-private cooperation, the authorities have established the “MLF+,” which is exploring the possibility of a common customer due diligence (CDD) utility.** The MLF+ was designed to enable FIs and other relevant private actors to discuss “problems and experiences” with the authorities comprising the MLF, while providing a platform to advance initiatives for AML/CFT-related cooperation within the private sector. One such initiative would leverage technological solutions to strengthen CDD processes within the Danish financial sector. The vision of a “common infrastructure” is still being refined based on the March 2019 political agreement, but it could include tools to verify customers’ identities, track familial connections, or capture the names of individuals and entities that present higher ML/TF risks, according to agreed criteria. Going forward, the Danish authorities also appear keen to explore the establishment of such a utility at the EU level. There could be a number of advantages to developing common CDD infrastructures, whether in terms of efficiency, accuracy, or the facilitation of AML/CFT supervision. The latter advantage would depend on the extent of the DFSA’s access to the data maintained by the utility, as such access could enable the DFSA both to identify networks of high-risk customers and determine whether FIs are appropriately monitoring their accounts. Therefore, the Danish private sector, in consultation with the authorities, should prioritize the completion of the visioning process, bearing in mind both the potential advantages noted above and the potential drawbacks, including in the realms of privacy, data protection, and due process of law.

## Recommendations

**24. To reinforce Denmark’s international and domestic cooperation on cross-border AML/CFT banking supervision, staff recommends:**

- Pursuing MOUs with DFSA counterparts in all the non-EU/EEA countries where Danish banks maintain (or intend to open) overseas branches or subsidiaries.
- Ensuring that the MLS is proactive in sharing with the DFSA analysis of STRs that may indicate a shift in banks’ institutional risk profiles or changes in the approach or quality of their reporting.
- Completing and adopting the planned update to the MLF MOU.
- Participating, as feasible, in both periodic and event-driven joint inspections of Danish banks’ higher-risk overseas branches and subsidiaries.
- Reinforcing existing stand-alone or embedded MOUs with foreign counterparts, as necessary and feasible, to fill procedural gaps and establish a certain degree of automaticity with respect to key forms of cooperation (e.g., information exchange and the conduct of joint inspections).
- Holding discussions within the Danish Cabinet, in consultation with all relevant domestic authorities, as to ways to further the integration/consolidation of AML/CFT supervision at the regional or sub-regional levels and arriving at a formal governmental position on this issue.
- Issuing findings on the feasibility and benefits of a private sector-led CDD utility, and its potential mobilization to support AML/CFT supervision.

## D. Implementing the Risk-Based Approach to AML/CFT Supervision

**25. Full implementation of the risk-based approach enables supervisors to make efficient use of limited resources and respond nimbly to changing threats and vulnerabilities.** Despite its recently increased budget allocation and staff complement, neither the DFSA nor any other financial sector supervisor can monitor and inspect every bank at every moment. As such, the RBA is a realistic response. It involves assessment of ML/TF risks at the national, sectoral, and institutional levels; varying the timing, frequency, scope, and intensity of inspections based on those risks, as well as on the quality of institutional controls, policies, and procedures; and making the necessary allowances to update risk profiles or conduct snap inspections in response to critical events and developments.

### Conducting National and Sectoral Risk Assessments

**26. The MLS finalized a new ML national risk assessment (NRA) in April 2019 and published a sanitized version on its website.** The FATF assessors raised several concerns with Denmark's 2015 ML NRA, including insufficient coordination in its preparation; the failure to adopt a whole-of-government approach; methodological deficiencies related to input, design, and scope; and a lack of statistics regarding the effectiveness and efficiency of the country's AML systems. In response, a new ML NRA was prepared by the MLS based on interviews with all the relevant authorities, a full analysis of ML cases concluded in 2016, an updated risk matrix, and a certain degree of input from the private sector. A confidential version was circulated within the Danish government and provided to industry associations (to assure dissemination to obligated entities); an outreach strategy will be discussed at the next meeting of the MLF. The public version is currently available only in Danish; an English-language translation will be complete by the end of June 2019.

**27. In parallel, the DFSA has prepared and issued comprehensive new guidance on the AML Act, which contains current risk factors and typologies.** In October 2018, the DFSA issued *Finanstilsynet's Guide on the Act on Preventive Measures against Money Laundering and Financing of Terrorism (the Money Laundering Act)*. This guidance—which was prepared in close cooperation with the private sector as part of a joint working group—contains explanatory notes on the AML Act, as well as ML/TF risk factors and typologies, including examples of scenarios and transactions that would represent higher vs. lower risks within the different segments of the financial sector. That working group has now been made permanent to facilitate the preparation of annual updates to the guidance, the first of which is to be released in late 2019.

**28. The DFSA's assessment of risk in the Danish financial sector is currently updated twice a year; its most recent update includes a substantial ML component.** Every six months, the DFSA updates its sectoral risk assessment (SRA), which includes analysis of evolving macro-financial and "transverse" risks.<sup>16</sup> It also includes analysis of risks that are specific to the various market segments under its supervision: banks, mortgage and credit institutions, pension and life insurance companies, property and casualty insurance, and capital markets. The most recent sectoral assessment made

<sup>16</sup> Note that the DFSA's semi-annual SRAs focus on financial stability; it has yet to conduct an ML/TF-specific SRA.



available by the authorities (dated November 21, 2018) considers ML to be a macro-financial risk, addressing it in appropriate detail within the sections on the banking sector, mortgage sector, and “transverse” risks. An updated SRA will be made public in August 2019, and will contain an extended chapter on AML/CFT. AML/CFT issues will also be addressed within the chapters for each sub-sector.

**29. The DFSA assesses that ML risks have diminished owing to “increased attention” to the issue but sees the possibility for ML to become a growing challenge for smaller banks.** The DFSA’s November 2018 SRA concludes that the “increased attention” to ML generated by the Danske Bank case has reduced the overall level of ML risk in the banking sector, presumably owing to increased awareness of the threat and increased motivation to address the related vulnerabilities. However, the underlying information on which this conclusion is based is not specified in the assessment, suggesting that additional, concrete data will need to be gathered on the reforms made in the wake of the Danske Bank case.<sup>17</sup> Examples of such data include the nature and scope of changes to banks’ internal controls and the reach of those reforms within the financial sector, given that some may be at an initial stage of implementation and others may be confined only to the country’s international financial groups. Indeed, the DFSA sees a possible shift of risk from larger to smaller banks, as the former tighten their controls and criminal actors respond by seeking out new customer relationships with the latter, believing them less likely to have robust AML/CFT systems. Going forward, ML risks are to be analyzed and included in every DFSA SRA.

## Conducting Institutional Risk Assessments

**30. The DFSA overhauled its risk model in 2018 and now updates its institution-level assessments on an ongoing basis.** The new model calculates each FI’s inherent risk as a function of: (i) the overall risk assigned to credit institutions by the ML NRA; (ii) the overall risk assigned to credit institutions by the most recent SRA (see above); and (iii) two bank-specific factors, one objective and the other based primarily on any tips or other information obtained by the DFSA. It assigns residual risk by producing a subjective DFSA rating, based, again, on any specific tips or other information it should obtain, including in the context of prudential inspections.<sup>18</sup> The resultant institution-level “scoreboard”—a spreadsheet of inherent and residual risk ratings—is updated each time the DFSA receives new information.

**31. The new risk model represents a step in the right direction, but it should be further developed, as planned, to aggregate and account for specific, cross-border ML risk factors.** As implied above, the institution-specific factors in the current model are quite limited, both in number and in scope. The model should therefore be further developed over the course of 2019–2020, as planned, to aggregate and account for specific ML risk factors.<sup>19</sup> These should include factors

<sup>17</sup> Data on the reforms made by individual FIs (for example, to their compliance structures or AML/CFT policies) could be gathered via the electronic questionnaires or automatic information reporting requirements recommended in this paper.

<sup>18</sup> For example, regarding governance, risk management, systems and controls, or operational risk and resilience.

<sup>19</sup> The DFSA plans to hire a consultant (or consulting firm) and to conduct exchanges with foreign counterparts in support of its ongoing effort to design a risk model that reflects the full range of international best practices.

related to cross-border ML risks, for example: the number, locations, and size of overseas branches or subsidiaries; the gain or loss of CBRs; the number of non-resident customers; and the volume of international financial flows, both at the group and branch-level, particularly as compared to the associated bank assets or customer deposits. To gather such information, staff recommends the eventual issuance of (electronic) questionnaires to—or the establishment of automatic reporting requirements for—banks and other critical segments of the financial sector. Indeed, the DFSA has indicated that it is currently studying this possibility and will soon propose amendments to the relevant law(s), including so as to specify an obligation to transmit certain, proprietary data on an annual or semi-annual basis.

### **Implications of Institutional Risk Assessments for On-Site Supervision**

**32. The DFSA’s annual and institution-specific on-site inspection plans are increasingly risk-based.** Each April, the DFSA draws up an annual inspection plan based on a snapshot of the scoreboard, i.e., an assessment of the institutional risk ratings as they stand at that time. The AML Division is aware of, and actively working to balance, the need to conduct more frequent inspections of higher-risk institutions with the need to ensure that periodic inspections of lower-risk institutions are (also) carried out within a reasonable timeframe. The DFSA may conduct either “ordinary”/full scope or “thematic”/targeted inspections, both of which are to be designed to ensure the coverage of higher-risk areas.

**33. A typical AML/CFT on-site inspection lasts one to two days, as part of a three-to-four-month process, from the announcement of an on-site to the issuance of the final report.** There is an inherent tension between the number of on-site inspections that can be carried out over a given year and the length/intensity of those inspections. The DFSA indicates that its AML inspections of banks typically last one to two days—as little as one day for the lowest risk cases and as many as two days for the highest risk cases—with a rough average of 300 (or more) hours of work required before and after the inspection itself, to solicit and review documentation from the supervised entity, prepare the on-site component, and produce and publish the final report. While the total length of this process may be roughly in line with international practices, the length of a typical on-site is not. The DFSA’s AML/CFT on-site inspections appear to be far shorter, and therefore far less intense, than those of its foreign counterparts, based on wide-ranging anecdotal evidence.

**34. The DFSA is continually refining its on-site inspection planning, building in a degree of flexibility.** Based on its experiences in 2017 (10 AML/CFT on-site inspections within Denmark) and 2018 (45 AML/CFT on-site inspections within Denmark), the DFSA has planned 35 AML/CFT on-site inspections within Denmark for 2019, having concluded that it would be preferable to decrease their number while increasing their length/intensity. Moreover, the DFSA has built a degree of flexibility into its 2019 inspection plan, reserving certain dates for inspections without specifying the names of the FIs to be visited or staff to be assigned. This change is welcome, as it will effectively permit the AML Division to refine its plans in response to evolving institutional risk profiles. Going forward, the DFSA should evaluate its new approach to on-site inspection planning, to determine whether it has delivered enough flexibility to enable snap inspections to be conducted when necessary and inspections already underway to be extended, as warranted by the initial findings. One lesson that

has certainly emerged from the recent, high-profile ML cases in the Nordic-Baltic region is that effective AML/CFT supervision requires responsiveness to fast-arriving news and fast-moving events.

## Recommendations

### 35. To further Denmark's implementation of the RBA in relation to AML/CFT supervision, staff recommends:

- Adopting a comprehensive institutional risk assessment model or "scoreboard" that includes specific, cross-border ML risk factors.
- Issuing annual, electronic questionnaires to banks and other critical segments of the financial sector—or establishing automatic reporting requirements—to gather the institution-level data that will be required for the planned adoption of a new DFSA "scoreboard."
- Conducting an internal review, at the conclusion of the 2019-2020 inspection cycle, to determine whether the current on-site inspection plan was sufficiently flexible to address fast-moving developments and permit adequate follow-up on suggestive initial findings.

## E. Taking Stock of the DFSA's Resources, Procedures, and Powers

**36. Every supervisory authority must have the resources, procedures, and powers necessary to carry out its mandate effectively.** In this context, "resources" are financial, human, and technological; the DFSA, like every supervisory authority, must have the budget, staff, and computer systems necessary to carry out its mandate effectively. Ideally, those resources should be available on a reliable basis year-over-year, to enable properly planned, longer-term investments in infrastructure, training, and technology improvements. "Procedures" may refer to institutional risk assessment guidelines, inspection manuals, or graduated processes for notifying banks of violations and applying available sanctions. As such, comprehensive procedures serve to promote efficiency, enhance consistency, and smooth transitions of leadership or of staff. Finally, "powers" refers to the full range of authorities available to the DFSA, e.g., to compel the production of information on the part of banks, exchange information with foreign and domestic authorities, conduct thorough inspections, or levy sanctions for non-compliance. The DFSA's powers are generally provided for in law, such that they may be harder to change or to supplement than its resources and procedures.

## Resources

**37. The DFSA's annual budget is substantially higher today than it was in fiscal year (FY) 2018, having benefited from a series of increases.** As of FY2018, the DFSA's annual budget stood at DKK 348.8M (\$52.7M). The DFSA's budget was DKK 350.8M (\$53M) at the start of FY2019 but was increased by 20 percent in March; it now stands at DKK 421M (\$63.6M). Although the AML Division does not have its own, dedicated budget, the DFSA's leadership understands that the primary purpose of the recent budget increase(s) is to bolster Denmark's AML/CFT supervisory capacity. Indeed, the March 2019 political agreement envisions further DFSA budget increases of DKK 54 million (\$8 million) in 2020, and an increase of DKK 48 million (\$7 million) per year starting in

2021.<sup>20</sup> The agreement specifies that the planned increases “must be spent on the enhanced efforts against financial crime”.

**38. The DFSA’s AML Division now has 11.5 dedicated AML/CFT inspectors working in a unit of 14.5 dedicated staff.** With its increased budget—and in line with the renewed focus on AML/CFT supervision—the DFSA established a separate AML Division in June 2017. That division has hired 11 (new) staff over the last two years, giving it a total current complement of 14.5 full-time employees responsible for the AML/CFT supervision of approximately 1,500 financial companies, including 104 Danish banks and foreign bank branches.<sup>21</sup> Moreover, the extraordinary, mid-year budget increase described above will enable the AML Division to create and fill 5.5 new positions, giving it a planned complement of 20 staff by the end of 2019.<sup>22</sup> As a result, the DFSA is likely to have among the largest such divisions in the Nordic region, even if it remains to be determined whether it is large *enough* to yield the desired leap in effectiveness with respect to AML/CFT supervision.<sup>23</sup> A separate, supplementary infusion of resources may be necessary to address the longstanding capacity constraints of the DFSA’s prudential divisions.

**39. The AML Division puts a strong emphasis on staff training and retention.** The AML Division consists of three sections—the Supervisory Task Force; the International Relations Section, which handles international supervisory cooperation; and the Regulation and Information Section—although the staff nominally assigned to each section remain primarily responsible for planning and carrying out inspections. The most recently hired AML/CFT inspectors have been trained in two ways: via an on-the-job apprenticeship program spanning the AML and prudential divisions and an external continuing education program that enables staff to take academic courses and participate in international seminars. Continuing education is also a key tool for staff retention, along with job content and a shared sense of mission. The DFSA has sometimes struggled to retain its inspectors, who are in very high demand within the private sector.

**40. The DFSA has a robust information technology (IT) infrastructure for domestic and international AML/CFT supervisory cooperation.** The AML Division uses the same IT system as its prudential counterparts, such that insights gained during AML and prudential inspections can be shared in real-time and information possessed by the DFSA remains fully integrated. Moreover, all Danish banks have secure, government-assigned e-mail addresses for the management of official correspondence; the DFSA sends notifications of inspections, requests for information, and all other formal communications to those addresses. The DFSA is contributing to the Finance Denmark-led visioning process for a country-wide common platform for the conduct of CDD, and the supervisory

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<sup>20</sup> The DFSA budget is set by the government, but funded by the Danish financial sector.

<sup>21</sup> Note that the AML Division is also responsible for preparing relevant legislation and for the DFSA’s AML/CFT-related international cooperation, including with respect to the FATF.

<sup>22</sup> This is in addition to the four staff members working on AML/CFT outside the AML Division. As such, by the end of 2019, there will be 24 total staff working on AML/CFT at the DFSA.

<sup>23</sup> The FATF will not reassess the effectiveness of Denmark’s AML/CFT supervisory regime until 2022, as part of its standard five-year update procedure.

colleges in which the DFSA participates maintain closed systems to allow for secure exchanges among their members.

## Procedures

**41. The DFSA maintains general inspection procedures but lacks an AML/CFT-specific inspection manual, as well as tailored guidance for on-site visits to large, complex FIs.** The DFSA has not yet developed an AML/CFT-specific inspection manual, whether for full-scope inspections (covering the full range of AML/CFT-related obligations) or for thematic inspections (focusing, for example, on the management of cross-border flows). A key, near-term objective of the AML/CFT Division is therefore to (re)develop the necessary business procedures “from scratch.” At a minimum, the resultant manual should cover basic inspection techniques, list the types of employees to be interviewed and subjects to be covered, provide an AML/CFT-specific methodology for sampling customer files and transaction records, and detail the systems and processes to be verified; ideally, it would also include special procedures to follow in inspecting more complex FIs, such as large international banking groups, which typically require more intense scrutiny.

**42. Importantly, the DFSA has yet to develop procedures to verify compliance with the new requirement that banking groups establish and implement group-wide AML/CFT policies.** Act No. 651 (8 June 2017) introduced new requirements related to (typically large, international) banking groups, in line with AMLD IV. Banking groups must now maintain written policies and procedures for the exchange of information in view of combating ML/TF within the group; the undertakings that are part of a group must comply with those (and all other) policies and procedures; and, of particular interest in the context of this paper, such undertakings must also exchange information within the group regarding funds “suspected of being the profits of criminal activity or of being associated with financing of terrorism,” once an STR related to those funds has been submitted to the MLS. Procedures for verifying compliance with these requirements should be included in the planned AML/CFT-specific inspection manual or in any supplement specifically related to the inspection of banking groups.

**43. The implementation of comprehensive new procedures should result in more intense AML/CFT inspections, particularly for higher-risk FIs.** As noted in paragraph 33 of this paper, with a staff of 14.5, including 11.5 inspectors, the AML division carried out 45 on-site inspections in 2018, with those for banks lasting one to two days each. The planned 22 percent reduction in the number of on-sites for 2019 could therefore result in a (desirable) lengthening of the average inspection. But even further lengthening is almost certain to be needed for the DFSA’s AML/CFT on-site inspections to achieve an optimal level of intensity in terms of the quantity, quality, and range of interviews conducted; the number of transaction records and customer files analyzed; and the extent of the system and procedure testing carried out, including with respect to the monitoring software and other relevant IT solutions that may be in place. This point is especially pertinent with respect to Denmark’s higher-risk FIs; spending only two days on-site at a high-risk bank is not conducive to conducting AML/CFT inspections that reflect the full range of international best practices. To avoid difficult tradeoffs (e.g., consideration of another reduction in the number of on-site inspections performed each year), such lengthening could be achieved via the allocation of additional staff time.

As noted above, the DFSA intends to use the bulk of the additional resources received pursuant to the March 2019 political agreement to complete a second round of hiring within the AML Division.

**44. The DFSA will also benefit from the planned update to its internal procedures for addressing violations of AML/CFT requirements.** Within the context of a self-described “educational approach,” the DFSA has traditionally relied primarily on “social trust” (the good faith of banks instructed to take remedial action) and “reputational risk” (the fear of reputational damage from the publication of compliance orders) to promote and enforce adherence to AML/CFT-related requirements. Even if such an approach is reasonably effective in most cases, the DFSA should continue to prioritize the update of its internal procedures to address those cases in which it struggles to achieve compliance—or to do so in a timely manner. The enforcement-related policy paper now being updated for presentation to the DFSA’s managing board appears aimed at specifying the circumstances and timeframes in which the DFSA would use its new and likely future sanctioning powers. The objectives are straight-forward: to maximize the consistency and predictability of the DFSA’s enforcement actions while ensuring that violations do not linger unaddressed, whether indefinitely or over an extended period of time.

## Powers

**45. In 2018, the DFSA acquired the power to revoke the license of an FI in response to gross violations of the AML Act.** Law No. 706 of 8 June 2018 provided the DFSA the authority to revoke the license of a bank or other FI in response to gross violations of the AML Act. (Note that this authority was available to the DFSA previously, but only in response to gross violations of the Financial Business Act.) Although it is likely that the DFSA will impose this new sanction only in exceedingly rare circumstances, its mere existence—in combination with the substantially increased fines that may now be levied in response to failures to comply with AML/CFT-related obligations—should function as an important deterrent to the knowing facilitation of cross-border ML.<sup>24</sup>

**46. In July 2019, the DFSA will acquire the power to make critical fit and proper determinations related to AML/CFT.** In line with the June 2017 political agreement, the Danish parliament enacted Law No. 552 of 7 May 2019 (The Financial Business Act), which extended fit and proper requirements to AML/CFT compliance officers and expanded the existing fit and proper assessment of directors and management committee members to include a determination as to whether they have a sufficient understanding of the AML Act. Moreover, the DFSA was empowered to decide that board members and AML/CFT compliance officers are unsuitable to assume—or shall be required to resign—their positions based on a determination that they have been involved in past breaches of AML/CFT-related obligations. This power is vital to ensuring that the leadership of banks and other FIs is both aware and respectful of Denmark’s AML/CFT legal framework.

**47. Going forward, the vast majority of Denmark’s political parties have committed to an additional, significant expansion of the DFSA’s sanctioning powers.** Pursuant to the March 2019

<sup>24</sup> In 2018, the DFSA revoked the license of an FI based on multiple violations of both prudential and AML/CFT-related requirements.



political agreement, the Danish Parliament intends to empower the DFSA to: (i) place short-term observers or “monitors” in banks; (ii) temporarily bar the onboarding of new customers or of certain types of new customers (e.g., non-residents); and (iii) issue administrative fine notices in response to non-compliance with key provisions of the AML Act.

**48. But that expansion has not yet occurred; crucially, the DFSA remains unable to issue administrative fine notices in response to non-compliance with the AML Act.** The FATF cited this gap as a key deficiency in Denmark’s 2017 MER. Not only does the inability to issue administrative fine notices reduce the DFSA’s leverage in effecting corrective action on the part of supervised entities, it also delays the imposition of consequences for chronic, low-level non-compliance. Unless and until it is indeed empowered to issue administrative fine notices, the DFSA will have to continue referring observed (criminal) violations to the SPSEIC for investigation, and the DFSA’s standard for making any such referral is the likelihood of eventual conviction. This is potentially a slow and cumbersome process, and one that appears incurably impractical. As Danish lawmakers design this reform with a view to achieving technical compliance with the FATF Standard, the laws and regulations in place elsewhere in the Nordic region may prove instructive.<sup>25</sup> The DFSA’s counterparts in Finland, Norway, and Sweden already have the power to levy administrative sanctions for non-compliance with (most, if not all) AML/CFT requirements.

**49. Separately, the DFSA is not required to conduct AML/CFT-related inquiries on behalf of foreign counterparts outside the context of established supervisory colleges.** At first glance, this would appear to be a serious gap in Denmark’s AML/CFT legal framework, and so a real impediment to its ability to conduct and support comprehensive cross-border AML/CFT supervision. But this gap is not unique to Denmark and does not appear to have had significant practical consequences, as the DFSA may conduct inquiries on its own initiative—whether based on its own or others’ concerns—and share the results in accordance with laws and agreements already in place. Furthermore, and as noted in paragraph 13, above, the DFSA interprets Danish law as requiring it to cooperate with EU/EEA counterparts, including with respect to requests for the conduct of inquiries. The DFSA reports that it received no such request in 2018.

## Recommendations

**50. To ensure that the DFSA has the resources, procedures, and powers to maximize the effectiveness of its cross-border AML/CFT supervision, staff recommends:**

- Fully and expeditiously implementing, in law, the March 2019 political agreement to expand the DFSA’s powers, including the authority to issue administrative fine notices for non-compliance with AML/CFT requirements.
- Developing a comprehensive AML/CFT on-site inspection manual.<sup>26</sup>

<sup>25</sup> See FATF Recommendations 27.4 “Powers of Supervisors” and 35 “Sanctions.”

<sup>26</sup> In some countries, “inspection manuals” are referred to as “testing procedures.”

- Intensifying AML/CFT on-site inspections by increasing their length and depth, particularly for higher-risk FIs and with respect to the risk-based sampling of customer files.
- Completing the hiring and training of new inspectors to bring the DFSA's AML Division to full strength and developing a formal staff retention plan.
- Updating the DFSA's standard follow-up procedures with respect to observed violations of AML/CFT requirements so as to incorporate the full range of its current and future sanctioning powers.
- Maintaining comprehensive statistics regarding the DFSA's actions in line with its current and future enforcement powers, both to ensure the consistent treatment of FIs and to enable an accurate evaluation of effectiveness.

## F. Conclusion: Next Steps for Reinforcing Denmark's Cross-Border AML/CFT Supervisory Regime

**51. There is strong political will to continue strengthening Denmark's AML/CFT regime, including its AML/CFT supervisory framework.** In light of the findings in Denmark's 2017 FATF MER and the intense scrutiny—from foreign and domestic media, politicians, and law enforcement—that has accompanied the Danske Bank case, the Danish authorities are determined to address known and, in some cases, longstanding deficiencies with respect to the country's AML/CFT supervisory regime. Indeed, the authorities aim to position Denmark “among the European elite” (i.e., as a regional leader) with respect to AML/CFT supervision and are well aware of the steps they will have to take to do so. The full realization of the most recent (March 2019) political agreement would represent important progress toward achieving that objective.

**52. Denmark has already taken many significant steps in this regard—and that, over a relatively short period of time.** The surge of interest and attention to (cross-border) AML/CFT supervision has already led to important progress, including: (i) the increased resourcing of the DFSA; (ii) its hiring and training of new inspectors; (iii) the introduction of new legal requirements related to AML/CFT policies and information-sharing within banking groups; (iv) the stiffening of the penalties for non-compliance with AML/CFT requirements; and (v) the conclusion of a political agreement to expand the DFSA's sanctioning powers, with the possibility of enabling it to issue administrative fine notices.

**53. Yet the ML risks in the Danish financial sector remain significant and are almost certainly evolving.** ML risk is generally understood to be a function of threat and vulnerability. It therefore bears noting that Denmark remains exposed to higher-threat regions via a relatively extensive network of bank branches and subsidiaries and CBRs. By contrast, Denmark's overall vulnerability does appear to have diminished, owing to recent reforms, even if it remains high (see paragraphs 9 and 10 of this paper). Meanwhile, and in line with the DFSA's own analysis, varying vulnerability levels among Danish FIs may be helping to drive an evolution of ML risks, to the extent that criminals respond to strengthened controls at larger banks by seeking out new customer



relationships with smaller, potentially less sophisticated institutions, relying even more heavily on complex corporate vehicles to conceal the true purpose of their transactions, or both.

**54. The key is therefore to maintain and build on the momentum Denmark has already established.** The skills of newly hired inspectors will take time to build, the elaboration of a comprehensive institutional risk assessment model and AML/CFT supervisory manual will take time to complete, and strengthened working relationships with foreign counterparts will take time to establish and operationalize. Yet, the more time that passes the greater the risk that the current momentum could slow, raising the specter of slowed—or even stalled—reforms. Thus far, however, the available indications are that Denmark has indeed achieved a national consensus to implement both necessary and encouragingly forward-looking reforms. When complete, those reforms should help to mitigate the reputational effects of the Danske Bank case and position Danish banks for future stability and growth in the context of an increasingly integrated regional and global financial system.

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