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# CBDCs and the AML regulatory framework

// Bergen CBDC Conference //

Norges Bank – UiB Simbula – Universitetet i Bergen



# Innovation calls for AML overhaul...

- Great deal of regulatory changes/updates (far from being completed...)
- Much of the changes are justified by the challenges brought up by financial innovation, e.g. the (first) definition of crypto currency.



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# “Soft you go...”

- FATF (2014) *Virtual Currencies: Key Definitions and Potential AML/CFT Risks*
- FATF (2021), *Opportunities and Challenges of New Technologies for AML/CFT*, FATF, Paris, France
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- ESAs (2018) *Opinion on the use of innovative solutions by credit and financial institutions in the customer due diligence process*, January 2018
- ESMA, EBA, EIOPA (2018) *Joint Warning on Virtual Currencies*
- EBA (2021) *survey 2019 and 2020 on the use of financial innovation*
- EBA (2021) *Opinion of the European Banking Authority on the risks of money laundering and terrorist financing affecting the European Union’s financial sector*



# AML package

On 20 July 2021, the European Commission presented its proposal for the reform of the anti-money laundering and counter-terrorism system, which is articulated in a series of interventions, namely:

- i) the VI anti-money laundering directive;
- ii) the regulation establishing a European Anti-Money Laundering and Anti-Terrorist Financing Authority (AMLA);
- iii) the regulation containing certain directly applicable anti-money laundering and counter-terrorism rules, including those relating to customer due diligence and effective identity verification;
- iv) a revision of the 2015 regulation on funds transfers for the purpose of tracking cryptocurrency transactions.



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# AML package

The measures «refine the existing EU regulatory framework, adapting it to **new and emerging challenges related to technological innovation**, such as virtual currencies, the increased integration of financial flows in the single market and the global nature of terrorist organizations. These proposals will help create a much more coherent framework to facilitate compliance for operators subject to AML/CFT rules, in particular those operating across borders»



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# What about CBDC and AML??



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# CBDC and AML

CBDC is defined as a “*digital form of central bank money that is different from balances in traditional reserve or settlement accounts*” (The Committee on Payments and Market Infrastructures and Markets Committee).

There are three different types of CBDC that vary depending on who has access and on the technology used:

- a) digital central bank tokens that can be used by financial institutions (e.g. for interbank and securities settlements);
- b) accounts at the central bank for the general public, and
- c) digital “cash” that could be used by the general public in retail payments.



# DEFINITION OF VIRTUAL CURRENCY – IV AML DIRECTIVE

- Article 3 (1) (18) of Dir. 2015/849/EU, as amended by Dir. 2018/843/EU, refers to «a digital representation of value that is **not issued or guaranteed by a central bank** or a public authority, is not necessarily attached to a legally established currency and does not possess a legal status of currency or money, but is accepted by natural or legal persons as a means of exchange and which can be transferred, stored and traded electronically».

# The AML approach is in line with substantive financial law (MiCA Regulation)

CBDCs and crypto assets are like “apples” and “oranges”

Recital n. 7:

“Digital assets issued by central banks acting in their monetary authority capacity, including central bank money in digital form, or crypto-assets issued by other public authorities, including central, regional and local administration, **should not be subject to the Union framework covering crypto-assets, and neither should related services** - that are provided by such central banks when acting in their monetary authority capacity or other public authorities”.





# DEFINITIONS OF CRYPTO ASSETS || CASH

## PROPOSAL FOR AN EU REGULATION ON AML

- No “virtual currency”
- ‘crypto-asset’ means a crypto-asset as defined in Article 3(1), point (2) of Regulation [please insert reference – proposal for a Regulation on Markets in Crypto-assets, and amending Directive (EU) 2019/1937 - COM/2020/593 final] except when falling under the categories listed in Article 2(2) of that Regulation or not otherwise qualifying as funds;
- ‘cash’ means currency, bearer-negotiable instruments, commodities used as highly-liquid stores of value and prepaid cards, as defined in Article 2(1), points (c) to (f) of Regulation (EU) 2018/1672 of the European Parliament and of the Council



# CBDC and AML

- CBDCs escape the «virtual currencies» for the purposes of AMLD
- FATF Standards explicitly state that virtual assets «do not include digital representations of fiat currencies, securities and other financial assets that are already covered elsewhere in the FATF Recommendations». Thus. CBDCs are not «virtual assets» for FATF purposes
- Consequently, **CBDCs are treated – for AML purposes – as «cash»**



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# CBDC and AML

**Trade-off between «privacy» and «other EU policy objectives» (see Fabio Panetta, A digital euro that serves the needs of the public: striking the right balance, 30 March 2022)**

Full anonymity is not a viable option from an AML policy perspective.

**See art. 58 AML regulation (Proposal )**

«Credit institutions, financial institutions and crypto-asset service providers shall be prohibited from keeping anonymous accounts, anonymous passbooks, anonymous safe-deposit boxes or anonymous crypto-asset wallets as well as any account otherwise allowing for the anonymisation of the customer account holder»

This means that intermediaries of a digital euro will be prohibited from hosting anonymous accounts and/or wallet



# CBDC and application of the “travel rule”

- Furthermore, if we consider CBDC as «cash» also Regulation Regulation (EU) 2015/847 on information accompanying transfers of funds applies (the so-called “travel rule”)
- “This Regulation lays down rules on the information on payers and payees, accompanying transfers of funds, in any currency, for the purposes of preventing, detecting and investigating money laundering and terrorist financing, where at least one of the payment service providers involved in the transfer of funds is established in the Union” (see art. 1)
- Proposal to amend this regulation (part of the AML package 2021) projected at regulating so called virtual assets and virtual asset service providers, has provided new and similar obligations for virtual asset service providers, with the purpose to facilitate the traceability of transfers of virtual assets.



# CBDC and application of the “travel rule”

- Regulation (EU) 2015/847 currently only applies to **transfer of funds**
- The proposal aims to expand to crypto:
- «This Regulation shall apply to transfers of funds, in any currency, - or crypto-assets, - which are sent or received by a payment service provider - , a crypto-asset service provider, - or an intermediary payment service provider established in the Union»

# CBDC and application of the “travel rule”

- (8) ‘funds’ means funds as defined in ~~point (2515) of~~ Article 4, point (25), of Directive (EU) 2015/2366~~2007/64/EC~~
  
- (9) ‘transfer of funds’ means any transaction at least partially carried out by electronic means on behalf of a payer through a payment service provider, with a view to making funds available to a payee  
*‘funds’ means banknotes and coins, scriptural money or electronic money as defined in point (2) of Article 2 of Directive 2009/110/EC;* e of whether the payment service provider of the payer and that of the payee are one and the same, including:



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# CBDC and CUSTOMER DUE DILIGENCE (CDD)

«Once a CBDC is established, financial institutions, designated non-financial businesses and professions and VASPs that deal in the CBDC will have the same AML/CFT obligations as they do with fiat currencies or cash.

A customer transacting using a CBDC **will have the same customer due diligence obligations as if it was an electronic transaction using fiat currency**».

FATF, FATF Report to the G20 Finance Ministers and Central Bank Governors on so-called Stablecoins, June 2020, par. 94.

(see also U.S. DEPARTMENT OF THE TREASURY, Framework for International Engagement on Digital Assets, July 2022: «FATF standards apply to CBDCs similar to any other form of fiat currency issued by a central bank»)



# CBDC and AML

## CBDCs could present greater risks than cash

CBDCs could be made available to be used by the general public in retail payments or as accounts and, in theory, allow for anonymous peer-to-peer transactions. In this scenario, the CBDC would be acting as an instrument with the liquidity and anonymity of cash, but without the limitations on portability that come with physical cash.

OK, cash...

**But AML/CTF risks depend on the design of the CBDC**  
**Risk-Based Approach**

## CBDCs could present less risks than cash

A wholesale CBDC, for example, that can only be used among licensed financial institutions for interbank settlement may have lower risks than a retail instrument.



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# CBDC and AML

**The Risk- Based Approach is a general principle stated (WITH REFERENCE TO NEW TECHNOLOGIES) by the Financial Action Task Force**

Jurisdictions are required under the revised FATF Standards to **identify AML/CTF risks relating to new technologies and apply appropriate measures to mitigate those risks.**

Recommendation 15, FATF Recommendations.

Recommendation 1, FATF Recommendations.



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# CBDC and AML

Supervised intermediaries – which are the natural candidates for distributing a digital euro – are best placed to manage the onboarding process of clients

([https://www.ecb.europa.eu/pub/pdf/other/Report\\_on\\_a\\_digital\\_euro~4d7268b458.en.pdf](https://www.ecb.europa.eu/pub/pdf/other/Report_on_a_digital_euro~4d7268b458.en.pdf))

The risk-based approach could be the yardstick/parameter against which to adapt AML obligations to the (risks) connected to CBDCs

Example: Provision of different types of accounts/wallets where the transaction amounts could be limited in proportion to KYC/CDD measures.



# Wrapping up

- The AML regulatory regime is undergoing important «substantive» and «institutional» reforms
- AML reforms are – rightly so! – concerned with «crypto assets» (not with CBDCs)
- There is no explicit reference to CBDC neither in the current nor in the upcoming AML regulatory regimes
- CBDCs escape the Virtual Assets/Virtual assets categories since it is «currency»/cash
- Being captured by the AML net as currency - but with special features!- opens up certain critical questions..
- The application of AML will be guided by the risk-based approach, which will most likely be shaping the specific AML obligations (onboarding/CDD/KYC).

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Thank you!

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