ML/TF Sub-sector Risk Assessment

COLLECTIVE INVESTMENT SECTOR (UPDATE 2025)

Commission de Surveillance du Secteur Financier

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TABLE OF CONTENTS

1. Foreword

This update of the Sub-sector Risk Assessment (SSRA) – Collective Investment Sector (CIS), following the 2020 and 2022 reports, highlights the continued success of the efforts made by the private and public sectors in mitigating the risks of money laundering and terrorist financing (ML/TF) within the CIS.

We encourage readers to consider this update alongside previous reports, as it does not repeat general messages already covered, but instead focuses on recent developments, bringing attention to emerging ML/TF threats and vulnerabilities that are increasingly relevant to Luxembourg's fund industry.

This risk assessment serves as a valuable tool for all stakeholders, offering deeper insights into the ML/TF risks specific to the CIS and outlining effective measures to mitigate them. Supervised entities are encouraged to use this assessment to enhance their understanding of these risks and implement proportionate, effective controls. With a new presentation format designed for ease of use, the SSRA aims to guide professionals in adopting best practices, addressing common supervisory findings, and implementing targeted recommendations. The CSSF will continue to monitor adherence to these recommendations through its supervisory activities.

Following the adoption of the 4th Mutual Evaluation Report of Luxembourg by the Financial Action Task Force (FATF), I would like to extend my sincere thanks to all those who contributed to this exercise, especially the members of the Expert Working Group on AML with the private sector (which was transformed into a Public-Private Partnership in 2024). This enhanced SSRA should empower financial actors to further strengthen their AML/CFT efforts, ensuring that Luxembourg remains a robust and secure hub for the thriving CIS.

Marco Zwick, Director, CSSF

2. Caveats and reminders

Results shown in this report relate to a snapshot in time and are performed through computation at cluster level. Consequently, within the same cluster, entities may have different scorings.

The reader is furthermore reminded that the assessments and outcomes presented in the 2025 SSRA, along other risk assessments, shall be embedded by supervised entities in their ML/TF risk assessments pursuant to Article 2-2 of the Law of 12 November 2004 on the fight against money laundering and terrorist financing, as amended (AML Law).

The CSSF draws the attention of its supervised entities to the fact that on top of regular risk criteria, specific trigger events must be taken into consideration. For instance, especially with regard to financial sanctions and embargoes, geopolitical crisis must be taken into consideration in the ML/TF risk assessment of supervised entities depending on their exposure to involved markets/entities.

The CSSF has been contacted multiple times by entities seeking information to understand their AML/CFT risk scoring presented on eDesk in the General Information section of the AML/CFT external report (Circular CSSF 21/788). The CSSF therefore provides the following clarifications:

- The risk scoring that is mentioned on the eDesk platform for the AML/CFT external report is a residual risk scoring, as determined by the CSSF.
- It is calculated using the numerous data points relevant for AML/CFT purposes that have been provided by the entity to the CSSF in reports or survey, mostly the yearly Financial Crime Survey. This automatic scoring is then enriched with the conclusions of the offsite and onsite supervisory measures performed by the CSSF case officers during the year.
- The scoring also takes into account triggers, such as adverse media or presence of politically exposed persons (PEPs) in the structure of the entity.

3. Purpose and scope of the document

In January 2020, the CSSF published its initial SSRA on ML/TF risks faced by the CIS and updated it in 2022.

The conclusions drawn in these assessments were based on quantitative data collected through different initiatives, in particular the annual Financial Crime Survey, and qualitative assessments by the CSSF as part of its onsite and offsite AML/CFT supervision.

In line with its AML/CFT supervisory strategy, the CSSF hereby updates its 2022 CIS ML/TF risk assessment using quantitative and qualitative data related to the years 2022 and 2023.

In the European Supra-National Risk Assessment published in October 2022[1], the retail and institutional investment sector's vulnerabilities have been assessed as **Significant/Moderately Significant** in relation to the money laundering (ML) risk and the threats in relation to terrorist financing (TF) as **Non-Relevant**[2]. It is however important to note that this evaluation relates to the whole EU and not just Luxembourg.

In its "*Opinion on money laundering and terrorist financing risks affecting the EU's financial sector*" published in July 2023, the European Banking Authority (EBA) provided an overview on the ML/TF risks of the CIS assessed by the EU National Competent Authorities (NCAs). The majority of NCAs concluded to a **Moderately Significant** inherent and residual risks for the Investment Fund Managers[3].

While the scope of this assessment encompasses all Luxembourg regulated stakeholders of the investment sector, it **focuses on Investment Fund Managers (IFMs),** considering their specific AML/CFT roles and responsibilities.

The present document is designed for public dissemination[4] and fulfils the following three main objectives:

- Promote exchanges between the public and private sectors;
- Improve the CIS participants' understanding of ML/TF risks; and
- Strengthen CSSF AML/CFT supervision in the CIS.

[1] https://www.cssf.lu/wp-content/uploads/EN_Supranational_report_-2022_risk_assessment_MLTF.pdf

[2] https://www.cssf.lu/wp-content/uploads/EN_Annex_to_Supranational_report_-2022_risk_assessment_MLTF.pdf

[3] https://www.eba.europa.eu/sites/default/files/document_library/Publications/Opinions/2023/1058335/EBA%20Op%202023%2008%20Opinion%20on%20MLTF%20risks%20EBA%20REP%202023%2021.pdf

[4] The figures provided in this document are as of 31 December 2024.

4. Methodology

The present risk assessment methodology has been modified from the previous ones, following discussions with numerous stakeholders including at the level of AML/CFT Colleges.

Moreover, to simplify the understanding of the risks faced by supervised entities of the CIS and, in particular, the differences between ML and TF, the structure of the report has also been modified.

This translates into the design and computation of new risk and mitigation indicators considering the new data points available notably pursuant to the AML/CFT external reports (Circular CSSF 21/788).

Regarding the structure of this report, two separate sections have been created to distinguish between ML and TF risks.

4.1. Stakeholders & process

For comparability purposes, the stakeholders and the process to update the SSRA remained in line with the 2022 exercise. The report was prepared by the CSSF and discussed with the Public-Private Partnership on AML, which is composed of representatives of the Association of the Luxembourg Fund Industry (ALFI), the Luxembourg Private Equity and Venture Capital Association (LPEA), the Real Estate Association of Luxembourg (LuxReal), the *Association Luxembourgeoise des Compliance Officers* (ALCO), the *Institut des Réviseurs d'Entreprises* (IRE), the Luxembourg Bar (*Ordre des Avocats du Barreau de Luxembourg*), the Luxembourg Institute of Internal Auditors (IIA Luxembourg Chapter), as well as the ABBL Depositary Banking cluster, the *Administration de l'Enregistrement, des Domaines et de la TVA* (AED) and the Financial Intelligence Unit (FIU-LUX).

Since 2023, new members have joined the Expert Working Group on AML, namely the Luxembourg Institute of Administrators (ILA) and the Luxembourg Association for Risk Management (ALRiM).

4.2. Scope and taxonomy

For the sake of clarity and consistency with the National Risk Assessment (NRA), the risk scoring categories have been updated to align with the NRA's structure.

Therefore, the buckets used in this report are:

- Very High;
- High;
- Medium;
- Low; and
- Very Low.

Furthermore, to harmonise with the practices of other EU Member States, the taxonomy has been simplified to distinguish between two key categories: UCITS Management Companies (UCITS ManCos) and Alternative Investment Fund Managers (AIFMs). This revision provides for greater consistency and transparency to risk assessments across the board.

5. Evolution of the Luxembourg CIS landscape

5.1. General overview – IFMs & products

Since the publication of the 2022 SSRA, the landscape of Luxembourg CIS supervised by the CSSF has not significantly changed. It is dominated by UCITS in terms of assets under management (AuM), but it is evenly split between UCITS and alternative investment funds (AIFs) in terms of number of structures.

Luxembourg continues to offer a wide range of undertakings for collective investment (UCIs). These products take a variety of forms, depending on their category, regime and structure, as detailed in the initial SSRA. The type of product offering for regulated UCIs has not significantly changed since the initial SSRA.

CSSF supervised UCIs	**31/13/2021**	**31/12/2024**
TNA	€ 5,859 billion	€ 5,821 billion
Number	3,492	3,143

5.2. Supervision novelties since the 2022 SSRA

A number of Luxembourg investments funds have elected to appoint a foreign IFM in the European Union. Considering that the CSSF has no authority over the IFM located abroad, the CSSF has strengthened its AML/CFT supervision at the level of these investment funds, notably via the introduction of a mandatory AML/CFT section in the Separate Report of the Statutory Auditor as per Circular CSSF 21/790.

Furthermore, the CSSF introduced a new template for the Summary Report of the *Responsable du Contrôle* (SRRC) in Circular CSSF 24/854 of 29 February 2024. CSSF supervised funds, which have appointed a foreign IFM, have the obligation, since 31 December 2023, to provide the aforementioned report on eDesk. The CSSF will use the content of this report to identify potential shortcomings in the design and the effectiveness of the AML/CFT framework at the level of the product with a focus on the oversight of outsourced AML/CFT activities.

In parallel, the CSSF strengthened its cooperation with the NCAs of these IFMs via bilateral exchanges of information on a bi-annual basis.

6. ML risk assessment evolution since 2022 SSRA

6.1. Evolution of Money Laundering threats

The SSRA published in 2022 provided an overview of emerging ML threats for the Luxembourg CIS.

- Cybercrime
- Purchase of businesses by organised criminal groups
- Abuse of Crypto Assets
- Geopolitical crisis

The CSSF has not observed additional threats since the publication of the latest SSRA.

6.2. ML inherent risk evolution

This section presents the results of the inherent risk assessment conducted by the CSSF concerning: UCITS ManCos and AIFMs.

The assessment is based on data reported by these supervised entities to the CSSF, ensuring a detailed understanding of the risks involved.

The evaluation incorporates several critical risk criteria, including (1) the market structure, which assesses how the sector's organisation may impact exposure to risk; (2) geographical risk, focusing on regions where these entities operate (investors / investments); (3) customer risk, analysing the profiles of the investors involved; (4) the nature of products, services, and transactions offered by these entities; and (5) the channels of delivery, which include the methods used to distribute and manage financial products.

This holistic approach allows the CSSF to comprehensively evaluate the risk landscape in the CIS.

6.2.1. UCITS ManCos

Geographical Risks

The initiators of UCITS are primarily based in Germany, Switzerland, and Luxembourg, presenting a lower inherent risk of ML regarding the origin of the products managed by UCITS ManCos. Luxembourg is known for the cross-border distribution of UCIs, particularly UCITS, which are marketed globally. Based on CSSF data, the main countries for UCITS distribution, in terms of AuM, are Luxembourg, Germany, the UK and France, presenting a lower ML risk.

UCITS ManCos typically have branches and subsidiaries outside Luxembourg, with most of these being located within the European Union and used mainly for marketing activities.

Product/Service/Transaction Risks

The assets held by UCITS carry a Low inherent risk of ML, as they largely consist of securities admitted to trading on regulated markets and money market instruments. These assets inherently have high levels of transparency, reducing their exposure to financial crime risks, including ML.

The number of UCITS ManCos offering Discretionary Portfolio Management services has remained stable since the last SSRA. Additionally, there has been a decrease in the provision of Trust and Corporate Service Providers (TCSPs) services by UCITS ManCos to the funds they manage.

Customer Risks

The customers of UCITS are typically retail or institutional investors.

Distribution Risks

Luxembourg is characterised by its global cross-border distribution of UCITS, which is highly intermediated through fund platforms with remote subscription of units and shares. These platforms are primarily based in the European Union and act as gatekeepers for AML controls on underlying investors.

Considering the above-mentioned risk factors updated with data as of 31 December 2024, the CSSF concludes that UCITS ManCos present a **Medium** inherent risk of ML.

6.2.2. AIFMs

Geographical Risks

The initiators of AIFs are primarily located in Germany, Switzerland, and Luxembourg, which are considered lower-risk jurisdictions in terms of ML for the origin of the products managed by AIFMs.

However, some AIFs include assets that are not admitted to trading on a regulated market in countries that present a higher inherent risk of ML.

Product/Service/Transaction Risks

AIFMs manage a variety of AIFs in Luxembourg, such as SIFs and SICARs. AIFs are generally closed-ended and based on investor commitments where funds are called by AIFMs before being allocated to specific investments.

AIFs typically invest for the long term, which may limit certain ML or TF typologies that require quick exits to access laundered funds. However, AIF investments are diverse and often not admitted to trading on a regulated market, including assets such as Private Debt, Private Equity, Real Estate, Real Assets, and Crypto Assets. These investments inherently present a higher ML risk compared to securities admitted to trading on regulated markets.

Customer Risks

The investors in AIFs often exhibit higher ML risk characteristics than those in UCITS. AIF investors often participate through legal entities, which can be structured in ways that may qualify as complex. The CSSF has furthermore observed that most investors identified as PEPs are more frequently found in AIFs rather than UCITS, further increasing the inherent risk profile.

Distribution Risks

AIF distribution is more diverse compared to UCITS. While some AIFs are distributed through intermediaries, similar to UCITS products, there are other cases where AIFMs engage with investors during roadshows, adding a more direct approach to distribution.

Considering these risk factors and the updated data as of 31 December 2024, the CSSF concludes that AIFMs present a **Medium** inherent risk of ML. Nevertheless, AIFMs are more exposed to ML risks than UCITS ManCos in particular due to the assets they manage.

6.3. Mitigating factors and residual ML risk assessment

This section evaluates the risk mitigating factors, combining both supervisory measures and entity-level controls, and determines the resulting residual risk for UCITS ManCos and AIFMs, specifically from an AML perspective.

6.3.1. UCITS ManCos

For UCITS ManCos, the implementation of AML controls had already achieved a high level of maturity in the last SSRA. The CSSF observed minor improvements in the application of AML controls across the spectrum of professional obligations.

Additionally, the number of letters of observation issued by the offsite inspection team declined between 2021 and 2024.

Risk-based Approach and Risk Appetite

Risk Assessment and the Risk-based Approach are implemented across UCITS ManCos.

While UCITS ManCos receive Key Performance Indicators (KPIs) from their delegates, CSSF supervision revealed that not all of them make effective use of these KPIs. CSSF inspections revealed that the risk appetite of UCITS ManCos is generally Low and has been properly formalised.

The majority of UCITS ManCos have self-assessed their ML residual risk with a variance of no more than one category compared to the CSSF's evaluation of the CIS, demonstrating a strong understanding of their risks and the effectiveness of their mitigation measures.

AML due diligence

AML due diligence conducted by UCITS ManCos on their fund investors, who are often financial intermediaries, is frequently delegated to Registrar and Transfer Agents (RTAs). The CSSF has not detected significant weaknesses with respect to legal compliance with requirements, particularly in cases requiring enhanced due diligence on the relationship between the intermediary and the underlying investors. It was noted that UCITS ManCos typically engage with large financial institutions acting as RTAs.

UCITS ManCos are also responsible for the distribution channels of their funds. The distributors' due diligence processes reviewed by the CSSF's offsite supervision team uncovered only a few issues related to the formalisation of such due diligence, primarily in long-standing relationships. This was corroborated by sample testing performed by statutory auditors in the AML/CFT external reports.

The CSSF also identified some instances where the origin of funds was insufficiently formalised for UCITS ManCos offering Discretionary Portfolio Management services. Even though such occurrences were rare, the CSSF emphasises that establishing the origin of funds is a vital component of customer due diligence.

Ongoing Monitoring

Following its review of the investor due diligence process on AML service providers by UCITS ManCos, the CSSF noted that some KPIs related to name screening and transaction monitoring were outside peer ranges for certain UCITS ManCos, based on a peer comparison. However, the CSSF notes that the overall framework remains robust.

Procedures and Trainings

All UCITS ManCos have reported the implementation of up-to-date AML procedures, a fact confirmed by both CSSF inspections and statutory reviews in the AML/CFT external reports. UCITS ManCos also indicated that they conduct annual AML training and the CSSF confirmed this during its inspections.

However, the offsite supervision team observed a growing trend of UCITS ManCos opting for generic e-learning courses from third-party service providers. While these tools are useful, the CSSF encourages UCITS ManCos to supplement them with theoretical and practical case studies reflecting the UCITS Manco’s business and internal processes. This ensures the training is tailored to the entity's specific risk appetite and procedures, enhancing the overall effectiveness of staff preparedness.

Residual Risk Assessment

After evaluating both inherent risk and mitigation factors, the CSSF concludes that UCITS ManCos present a residual risk level of **Medium**. Indeed, following the application of mitigation measures, the residual risk scoring of UCITS ManCos decreases which reflects the quality of the mitigation measures implemented within this group and highlights the effectiveness of their risk management efforts.

6.3.2. AIFMs

AIFMs continue to be closely supervised by the CSSF due to the additional risks posed by the asset side. In line with this, the CSSF has conducted various sample tests on assets to evaluate the existence and adequacy of ML/TF risk assessments and related due diligence processes.

While the number of letters of observation issued by the offsite supervision team decreased between 2021 and 2024, it remains higher than for UCITS ManCos.

Risk-based Approach and Risk Appetite

The CSSF observed that the risk appetite for AIFMs was typically defined and that the risk assessments were performed by taking a granular approach, in particular due to the higher exposure to ML risks associated with the AIFMs' investment strategies.

However, with respect to registered AIFMs, these risk assessments often lacked formalism and depth. To address this, the CSSF introduced AML orientation meetings with newly registered AIFMs to emphasise the importance of formalising risk assessments and risk appetite statements. Since implementing this measure, the CSSF noticed a perceptible improvement in the formalism and quality of risk assessments.

AML due diligence

In addition to performing AML due diligence on investors, which is similar in design and effectiveness to UCITS ManCos, AIFMs are exposed to ML risks on the asset side as well. Given the higher ML risks posed by certain investment strategies, the CSSF placed particular emphasis on AML due diligence concerning assets. The CSSF found that AIFMs had implemented appropriate due diligence measures for their portfolios, as confirmed by AML/CFT external reports from statutory auditors.

Ongoing Monitoring

The CSSF noted that some AIFMs using medium to small service providers relied on their name screening and transaction monitoring systems. The CSSF reminded AIFMs that oversight of AML service providers includes reviewing the adequacy of these systems.

Furthermore, in several cases, where AIFMs delegated AML controls to sister or parent companies, due diligences were insufficient because group AML procedures were presumed to be in place. The CSSF reiterated that the existence of group AML procedures does not guarantee their effectiveness, and proper oversight is still required. Affected AIFMs have since implemented appropriate remediation plans.

Procedures and Training

The CSSF did not identify significant issues with the AML procedures of AIFMs but reminded them that these procedures should be updated if there is a change in investment strategies.

Unlike UCITS ManCos, some AIFMs conduct AML trainings less frequently, often every two years or less frequently. After interviewing these entities, the CSSF understood that this approach was taken because these AIFMs managed a limited number of closed-ended funds with long-term investments. However, the CSSF still recommends that AIFMs perform annual AML training to stay updated, amongst others, on new ML typologies.

Additionally, similar to UCITS ManCos, the CSSF noted an increasing trend of AIFMs using generic third-party e-learning platforms for AML training. The CSSF encourages AIFMs to supplement them with theoretical and practical case studies reflecting the AIFMs' business and internal processes as well as their specific risks, especially those related to their investment strategies.

Residual Risk Assessment

After assessing both, inherent risk and mitigation factors, the CSSF concludes that AIFMs present a residual risk level of **Medium**, similarly to UCITS ManCos. Following the application of mitigation measures, the residual risk score of AIFMs decreases albeit in a more nuanced trend. Despite both UCITS ManCos and AIFMs being in the same risk bucket, AIFMs presents additional ML risk factors notably in relation to the assets that are not admitted to trading on a regulated market they manage. Additionally, based on the outcome of the CSSF's supervision, the quality of mitigation measures of AIFMs remains generally less effective than those of their UCITS counterparts.

6.4. Red flags of ML in the CIS

- **Unusual Transaction Patterns**: Investors who frequently make large, unexplained transactions, or whose investment activities show a pattern inconsistent with their profile or financial situation, can be a red flag. For example, an investor with a moderate income suddenly making large-scale investments without a clear source of funding.

- **Overuse of Wire Transfers**: Frequent incoming or outgoing wire transfers, especially from or to countries known for higher risks of ML or TF, without clear business rationale or economic activity.

- **Use of Intermediaries to Obscure Identity**: Investments made through intermediaries, trusts, offshore companies set up as "shell" companies that serve to obscure the identity of the true beneficial owner can indicate an attempt to launder money.

- **Rapid Movement of Funds**: Quick turnover of investments, such as rapid buying and selling of securities without concern for gain or market conditions, can be indicative of an attempt to integrate/reintegrate illicit funds into the financial system.
- **Mismatch Between Investor Profile and Activity**: An investor's transactions that are inconsistent with their known legitimate business or personal investment behaviour, such as a retail investor suddenly engaging in complex derivative transactions typically reserved for sophisticated investors.

- **Complex or Unusual Structures**: The use of complex or unusual structures involving multiple layers of transactions, companies, or cross-border activities designed to obscure ownership, source of funds, or ultimate beneficiaries.

- **Reluctance to Provide Information**: Investors that are reluctant to provide complete information about the purpose of an investment, the source of funds/wealth, or the identities of the beneficial owners.

- **Adverse Media Reports**: Negative media reports or publicly available information suggesting criminal activity, corruption, or involvement in money laundering/circumvention of targeted financial sanctions (TFS) by the investor or entities associated with it.

- **High-risk Countries**: Investments connected to countries considered High risk for ML or TF, especially those without adequate anti-money laundering or counter-terrorism financing frameworks.

- **Evasive Behaviour Regarding Taxes**: Investors who express undue concern about tax evasion or seek advice on tax evasion strategies may be attempting to use the investment fund to launder money.

7. TF risk assessment in the Luxembourg CIS

7.1. Introduction

A dedicated vertical risk assessment on TF has been published in May 2022[5]. It exclusively focuses on TF risks in order to deepen the understanding of its drivers, following the approach outlined in the FATF TF Risk Assessment Guidance (2019) for assessing TF risks in jurisdictions with financial centres and low domestic terrorism risk[6], which is suitable for Luxembourg's particular situation.

TF encompasses the raising, movement and use of funds by terrorist actors and is considered as one of the most important threats to global security.[7] However, the risk of terrorist financing in collective investments is Low. As reported by the FATF, there has been "relatively little evidence of the securities industry being used to finance terrorism"[8].

Similarly, in the European Supra-National Risk Assessment published in October 2022[9], the retail and institutional investment sector has been assessed as **Low risk** in relation to TF.

The main TF risks for Luxembourg emanate from the threat that terrorists, terrorist organisations and their financiers might exploit the vulnerabilities of certain sectors, **essentially for moving funds**.

7.2. TF threats in the Luxembourg CIS

Both the 2020 NRA, as well as the 2022 dedicated vertical risk assessment on TF, assess the **residual TF risk in the CIS as being Low**, which is explained by several factors:

- Short-term and transitory cash flow requirements to move cash from one party to another (especially uncommon and unrelated parties) are less compatible with an industry generally focused on individual medium to long-term asset appreciation;
- Relying on transfer methods outside of the regulated banking system (e.g. Hawala, cash couriers) is incompatible with the custodian's obligations;
- Low value financing requirements do not match the common higher minimum subscriptions. The CIS's exposure to TF is more relevant for wealthy terrorism sponsors outside the EU than for lone actors or small terrorist cells operating within the EU. This is particularly true for discretionary management mandates which typically cater to High-Net-Worth Individuals; and
- Investment decisions are generally taken on a discretionary basis meaning that investment decisions are taken by the professional and not by the client itself.

Indeed, there is limited evidence that the CIS is misused for TF purposes, as reflected also by the very low number of TFARs and TFTRs[10] submitted to the CRF (FIU).

[5] https://mj.gouvernement.lu/dam-assets/dossiers/blanchiment/tf-vra-2022-en.pdf

[6] FATF, Terrorist Financing Risk Assessment Guidance, 2019, paragraph 39.

[7] FATF, International standards on combating money laundering and the financing of terrorism and proliferation – the FATF recommendations, 2012.

[8] FATF, Money Laundering and Terrorist Financing in the Securities Sector, 2009.

[9] https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52022SC0344

[10] https://justice.public.lu/dam-assets/fr/publications/rapport-activites-crf/rapport-crf-2021-2022.pdf (page 36)

7.3. TF vulnerabilities in the Luxembourg CIS

Notwithstanding the fact that the threats of TF are considered Low for the CIS in Luxembourg, some vulnerabilities are highlighted and need to be mitigated.

- The volume of AuM in the Luxembourg CIS makes it difficult to spot small transactions that could be linked to terrorist financing;
- The Luxembourg CIS is partly focused on illiquid assets such as real estate, real assets, private equity. When buying these assets, the funds may deal with persons acting as terrorist financiers;
- As mentioned in international literature[11], Sharia funds, some being incorporated in Luxembourg, may be abused by terrorist financiers or by rogue governments for the benefit of terrorist organisations;
- The Luxembourg CIS uses a significant number of financial intermediaries investing on behalf of underlying investors. This set-up commonly used worldwide in the fund industry may be abused by terrorist financiers;
- The investors in the Luxembourg CIS are mostly non-resident.

7.4. Specific work performed between 2021-2024 by the CSSF on TF in the CIS

In order to confirm the Low residual risk scoring for TF in the Luxembourg CIS, the CSSF has initiated several specific projects dedicated to CTF since the publication of the previous SSRA, as further elaborated in the following sections.

The objectives of these projects are to ensure that the risks identified are mitigated. In particular, regarding the following potential vulnerabilities of the sector:

- Illiquid assets in Luxembourg funds;
- Use of financial intermediaries in Luxembourg funds;
- Sharia funds; and
- Non-resident investors' base in Luxembourg funds.

7.4.1. Project Alpha

Objective

Assess the CIS' exposure to investors with nexuses to higher risk countries from a TF perspective.

Methodology

The CSSF reached out to the 10 largest registrar and transfer agents (based on the AuM of the funds to which they provide Transfer Agency services) and has requested a list of all investors in investment funds supervised by the CSSF as of 31 December 2022, along with unique identifiers, their countries of nationality and residence and the countries of their subscribing bank accounts.

A list of higher risk countries for terrorist financing factors was established internally by the CSSF, by taking into account international literature, based in particular on countries identified by reliable and independent sources as being state sponsors of terrorism or known to harbor terrorist organisations.

11 https://www.imf.org/external/pubs/ft/wp/2016/wp1642.pdf

After identification of the investors as being residents of, or having a bank account in, a higher TF risk jurisdiction, the OPC AML Team requested the holdings of all of them, to also assess how much AuM they represented.

Outcome

The data provided by the registrar and transfer agents was mapped against the above-mentioned list and the CSSF OPC AML team computed the number of investors who were residing in or having a bank account in such countries.

The sample of all investors collected represented over a third of the investors in CSSF-supervised Luxembourg funds.

The final calculation revealed that less than 0.05% of the investors in the sample were residents of, or had a bank account in, a higher TF risk jurisdiction.

7.4.2. Project Bravo

Objective

Assess the exposure of CSSF supervised funds to distribution in Palestine following the Hamas terrorist attacks of 7 October 2023 in Israel.

In case of identification of distribution in Palestine, the aim was to identify the investors and to perform specific due diligence in order to identify potential red flags of TF.

Methodology

The CSSF analysed the reports made by the CSSF supervised funds in which the countries of distribution were indicated.

The OPC AML team also used the data collected as part of Project Alpha to search for investors located in Palestine.

Outcome

No distribution in Palestine was identified at the time of the project (November 2023).

No investor national, resident of, or having a bank account in, Palestine was identified.

7.4.3. Project Charlie

Objective

Assess adequacy of AML/CFT framework of IFMs managing Sharia funds to specificities and typologies of Sharia funds and ensure that proper mitigations are in place to avoid Sharia funds of being abused by terrorist financiers or rogue governments for the benefit of terrorist organisations.

The CSSF conducted onsite inspections at 5 Luxembourg IFMs managing 16 Sharia funds. The onsite inspections comprised sample testing and focused on several facets of the mitigation framework relating to Sharia funds covering both, procedural and operational, aspects. As such, the CSSF OPC AML team checked, amongst others, the exhaustiveness and formalisation of ML/TF risk assessments and the coherence of the IFMs' AML/CFT risk appetite with the respective AML/CFT risk scores of the managed Sharia funds. Tests were also performed on the approval process for High-risk ML/TF relationships and on the management information received at Board and senior management levels with respect to Sharia funds. CSSF inquiries also focused on Sharia-specific AML/CFT trainings as well as on name screening aspects.

Outcome

The CSSF did not identify any major shortcomings. Certain findings of lesser importance and not relevant from a TF risk perspective were, however, identified and appropriate remedial action was taken.

7.4.4. Project Delta (financial intermediaries)

Objective

Assess whether terrorist financiers or individuals with known ties to terrorist organisations invest in CSSF supervised funds or funds managed by Luxembourg IFMs by investing via financial intermediaries.

Methodology

Between 2021 and 2024 year-ends, the CSSF has on a risk-based approach and in line with its supervisory planning, performed 38 supervisory measures related to distribution oversight, each composed of multiple samples. This specific type of supervisory measure consisted of reviewing the types of measures used by supervised entities to perform their AML/CFT due diligences on distributors (e.g. onsite visits, desk-based reviews of distributors' AML/CFT policies & procedures and name screening framework, sample testing, etc.) and on the formalisation and validation of the respective due diligence and oversight reports. On the other hand, this supervisory measure also focused on shortcomings identified by supervised entities as well as on the relevant corrective actions taken to remediate such shortcomings.

Outcome

Based on the reviewed sample, the CSSF has not identified any apparent shortcomings that would allow terrorist financiers or individuals with known ties to terrorist organisations to subscribe units and shares of CSSF supervised funds or funds managed by Luxembourg IFMs via financial intermediaries, nor has the CSSF OPC AML team identified instances where such subscriptions took place.

7.4.5. Project Echo (Assets)

Objective

Assess whether assets held by CSSF supervised funds may be linked to terrorist financing.

Methodology

Through offsite supervision, the CSSF performed sample testing of name screening on assets to assess the quality of the related due diligence files.

Between 2022 and 2024, a sample of nearly 200 due diligence files on assets was reviewed. The sample focused primarily on securities not admitted to trading on a regulated market.

A particular emphasis was given to assets located in jurisdictions presenting a higher TF risk.

Outcome

The main finding of the CSSF in that project was that in the sample of IFMs and related funds, almost no assets were located in a jurisdiction considered having a higher TF risk.

Out of the whole sample, the OPC AML team only identified a minority of cases (four) where the due diligence on assets was not commensurate with the risk attributed to said assets. Those instances gave rise to observation letters and the IFMs remediated those shortcomings.

The OPC AML team also identified that several IFMs had delegated the screening and due diligence on assets to their external portfolio managers. However, the CSSF noted that the KPIs provided by those delegates were often high level and did not provide sufficient details in particular regarding the results of the name screening against TFS lists (which include some entities related to terrorism). The CSSF also wishes to remind the fact that TFS screening is rule-based and not risk-based.

To mitigate the risk of TF on the assets side, the OPC AML team noted that the entities in the sample had chosen to have a very Low risk appetite when it came to TF risks and therefore refrained from investing in jurisdictions bearing a higher TF risk.

7.5. Red Flags of TF in the CIS

- **Transactions linked to High-risk Jurisdictions**: Investments or transactions involving countries known to have a High risk of terrorist activity, or that are subject to sanctions, embargoes, or other measures due to terrorism financing concerns.

- **Contributions in Kind:** contributions in kind which cannot be logically explained or that are inconsistent with the investor's profile or business activities.

- **Use of Third Parties Without Clear Reasons**: Use of intermediaries or third parties to conduct transactions when it does not seem to be based on a legitimate business purpose, especially if these parties are located in High-risk jurisdictions.

- **Rapid Movement of Funds**: Quick movement of funds in and out of accounts or between different financial institutions without clear business reasons, especially if these transactions involve High-risk jurisdictions.
- **Complex or Opaque Financial Structures**: Investments involving complex structures or transactions with no apparent legal or economic purpose, designed to obscure the origin, destination, or ownership of funds.

- **Anonymity or Use of Pseudonyms**: Attempts to invest or conduct transactions anonymously, or using pseudonyms, or other methods that prevent identification of the true beneficial owners.

- **Mismatch Between Activity and Customer Profile**: An investor's transactions are inconsistent with their known legitimate business, personal activities, or risk profile, especially if funds are directed towards known or suspected terrorist entities.

- **Frequent Changes in Account Details**: Frequent changes in account information, such as authorised signatories or beneficial owners, without a clear explanation.

- **Donations to NPOs with Ties to Terrorism**: Investments or transactions that include donations to NPOs, where there are indications that the NPOs may be a front for financing terrorism.

- **Evasive Behaviour**: Investors who are evasive or reluctant to provide additional information about transactions, or who seem to be attempting to evade reporting requirements or monitoring.

- **Adverse Media**: Negative news reports that link the investor or entities involved in the investment to terrorist activities, organisations, or individuals known to be associated with terrorism.

8. Concluding remarks

8.1. Anti-money laundering analysis

The data collected and analysed for the drafting of this updated report showed that the professionals of the Luxembourg CIS continue to adapt and strengthen their AML controls to mitigate ML everchanging threats.

8.2. Counter terrorism financing analysis

Multiple projects performed by the OPC AML team confirm the Low level of residual TF risk for the Luxembourg CIS.

Nevertheless, considering the size of the Luxembourg financial sector at large, both the CSSF and the supervised entities will need to continue to monitor this risk in the CIS, to ensure that it will be adequately mitigated should it increase.

	ML Residual risk	**TF Residual risk**
UCITS ManCos	Medium	Low
AIFMs	Medium	Low

9. Way forward

In line with the commitments made in the SSRA 2020 and the updated SSRA 2022, the CSSF will continue its proactive approach by:

Promoting the understanding of AML/CFT obligations and ML/TF risks, as well as the risks of circumventing TFS.

The CSSF actively supports the fund industry's efforts to enhance their comprehension of AML/CFT obligations and associated risks. To further develop this, the CSSF will maintain several ongoing initiatives, such as regular meetings of Public-Private Partnership.

Additionally, the CSSF will continue to organise AML/CFT conferences with the private sector and issue further guidance where relevant.

Enhancing the effectiveness of AML/CFT supervision within the CIS.

The CSSF recently provided the sector with a template for the SRRC on eDesk. This structured format aims to improve the CSSF's ability to analyse the report and identify weaknesses at both micro and macro levels, on which the CSSF will provide feedback.

Moreover, the CSSF will continue its active participation at international level, including leading several AML/CFT Colleges, as outlined by the EBA guidelines from December 2019.

The CSSF will also continue to engage in FATF, IOSCO, and EU AML/CFT forums, and contribute to workshops focused on the establishment of AMLA.