



Liechtenstein moves toward modernizing its anti-money laundering regime

Along with Monaco and Andorra, the European principality of Liechtenstein is one of the last three countries listed on the Organization for Economic Cooperation and Development (OECD) list of un-cooperative tax havens for not implementing best-practice standards to prevent illegal tax evasion. Liechtenstein, like the other two black-listed countries, is known for its refusal to cooperate in bilateral tax information exchanges and to meet international transparency standards by enacting bank secrecy laws. Due to its tax haven status Liechtenstein, a tiny country sandwiched between Austria and Switzerland, remains a paradise for all sorts of proceeds of crime. And now it has been drawn to the heart of one of Europe's largest tax evasion scandals.

The current Liechtenstein Tax Scandal involves a stolen CD with hundreds of client files from LGT Treuhand AG, the asset management arm of the LGT Group, owned by the ruling House of Liechtenstein. According to media reports, up to 4 billion euros that should have gone to the German Ministry of Finance as tax revenue have found their way to safe havens in Liechtenstein. The Liechtenstein Tax Scandal has, since the arrest of Klaus Zumwinkel, CEO of the German postal service company Post AG,

spread across Europe like wildfire. The client files reportedly relate to European tax evaders and to U.S. citizens. Organized crime groups operating on the fringes of and outside the European Union are also suspected of being listed on the CD.

Germany, where the case started to unravel, has taken a no-nonsense approach, and its chancellor, Angela Merkel, has been involved in heated discussions with Liechtenstein Crown Prince Alois. Merkel has asked that Liechtenstein sign an agreement with the EU similar to the transparency agreement between Liechtenstein and the United States, whereby Liechtenstein automatically sends U.S. authorities details of funds deposited in the country by U.S. citizens. Germany and other EU countries have strenuously appealed to Liechtenstein to bring its legislation and bank secrecy law in line with OECD best practice guidelines and help combat financial crime on an international level. (The other European countries that, like Liechtenstein, are not obliged to disclose details of funds deposited by foreign nationals to the financial authorities of the depositors' homelands are Switzerland, Luxembourg and Belgium.)

For Germany, this is not the first time Liechtenstein has been implicated in large-scale tax evasion scandals. In 2000

a similar case was uncovered, involving trusts managed by the Liechtenstein fiduciary firm Herbert Batliner, and resulted in a sweeping tax-evasion investigation and high profile convictions, including football star Franz Beckenbauer, the father of the tennis champion Steffi Graf, tennis star Boris Becker, singer Patrick Lindner, and show jumper Paul Schockemöhle.

The current Liechtenstein Tax Scandal involves some classic money laundering red flags, such as offshore trust structures and gatekeepers. In Germany, as in many EU countries, tax evasion is a predicate crime, and issues attached to money laundering have also featured tangentially in media coverage of the investigations. But the definition of predicate crimes for purposes of deciding whether money laundering has occurred varies from country to country. Prosecution for money laundering in this case could be particularly difficult due to "double criminality" requirements, whereby the predicate crimes must not only constitute an offense under the law of the country where the offense was carried out, but also under the law of the state where the proceeds were laundered. In this instance, from a double criminality perspective, tax evasion is not a predicate crime for money laundering in Liechtenstein or Switzerland, as it is where

the investigations are being conducted, such as Germany, the United Kingdom and the U.S.

Liechtenstein and money laundering

Liechtenstein is not a member of the EU and therefore not directly obliged to implement the Third EU Anti-Money Laundering Directive. However, as of January 28, 2008, Liechtenstein joined the Single Euro Payments Area (SEPA), which includes all EU countries and the members of the European Free Trade Association (EFTA), namely Iceland, Norway, Liechtenstein and Switzerland. As a result, Liechtenstein is obliged to implement the Third Directive. Discussions regarding the Directive and its implementation are currently ongoing in Liechtenstein. It should be noted that although the implementation deadline for the Third Directive was December 2007, Germany has, like most EU members,

combating the financing of terrorism (CFT) efforts and concluded that it had introduced legal standards in line with international requirements.

- The legislation is not only in place but has been an effective catalyst for further investigations:
 - Suspicious Transaction Report (STR) filed in Liechtenstein, which was followed up by its Financial Intelligence Unit (FIU), allegedly triggered a large-scale corruption investigation against Siemens AG in 2007.
 - The Spanish media, in response to media coverage related to the German Tax Scandal, reported that four of Spain's largest organized crime groups had used trust structures set up in Liechtenstein to launder funds.
 - Colombian drug cartels also had used accounts set up in Liechtenstein to fund shipments of

As reported on Liechtenstein's FIU web site, the Second EU Anti-Money Laundering Directive (dated December 2001), was implemented in November 2004 under the so-called Sorgfaltspflichtgesetz (SPG) which effectively means 'Duty of Care' or 'Due Diligence' law. The aim of the legislation was to combat money laundering, organized crime and terrorist financing, as outlined in the country's criminal law. Given the international pressures facing Liechtenstein it is likely that the Third EU Anti-Money Laundering Directive will be implemented in the near future.

In March 2007, Liechtenstein ratified the 1988 UN Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances (the Vienna Convention). It has also signed but not yet ratified the UN Convention against Transnational Organized Crime (the Palermo Convention).

On March 5, 2008 MONEYVAL published its *Third Round Detailed Assessment Report* on Liechtenstein focused on its AML and CTF efforts. A review of the report prepared by the International Monetary Fund's Legal Department identified Liechtenstein as largely compliant with the Financial Action Task Force (FATF) 40+9 recommendations and the second EU Directive. However, it was noted that a lack of convictions and prosecutions made it difficult to assess the effectiveness of the legal framework (See table 1 outlining the statistics on money laundering offenses under Article 165.) Furthermore, money laundering-related actions are initiated largely by mutual legal assistance requests and FIU reports. The percentage of investigations triggered by FIU reports is however, "rather low."

Some areas of concern relevant to the current Liechtenstein Tax Scandal mentioned earlier were highlighted in the report, among them:

- Money laundering and terrorism financing are broadly criminalized, in line with international best-practice requirements. However, there is no criminal liability of corporate entities, and Liechtenstein has not yet developed its own case law on money laundering.
- As to the definition of predicate crimes, a number of issues were highlighted. At the time of the assessment, no offenses involving environmental crimes, smuggling, forgery and market manipulation were defined as predicate offenses for money laundering. The law does not criminalize self-laundering in relation to converting, using or transferring criminal proceeds. Prosecution

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yet to implement the directive through national legislation, and is believed unlikely to pass implementing legislation before the summer.

The Third EU Directive broadens the scope of those professions that fall under the directive to include "gatekeepers" (lawyers, accountants, tax advisors, etc.) With money laundering as well as with tax evasion and other predicate crimes, gatekeepers have been instrumental in disguising financial crimes by giving criminals a veil of legitimacy. Furthermore, the obligation of these professionals to determine the beneficial owners of funds should also play a key role in improving the attempts to combat money laundering and other crimes.

As for its anti-money laundering (AML) efforts, Liechtenstein has taken significant steps by introducing best-practice legislation. Some of the steps include:

- The FATF Annual Report 2006-2007 announced that Liechtenstein was among the 23 countries¹ to be removed from the FATF's Non-Cooperative Countries List due to "significant progress" in strengthening their AML and counter-terrorist financing (CTF) systems.
- In 2003 the OECD reported on its assessment of Liechtenstein's AML and

cocaine from Colombia to Spain.

- Liechtenstein had also been involved in the Marbella Corruption Scandal in 2006 when billions of euros were paid as bribes to local politicians to secure construction licenses in southern Spain.

The head of Liechtenstein's FIU, René Brüllhart, is reported to have cooperated closely with German authorities, in relation not only to the Siemens scandal but to other monies laundered by the German Democratic Republic.

In sum, it would appear that Liechtenstein has been more effective in implementing and enforcing an AML regime than in enacting legislation to prevent tax evasion.

AML Legislation – Status Quo

Liechtenstein inaugurated an AML legislative framework in 1996 when it implemented the first EU Anti-Money Laundering Directive. Liechtenstein's Criminal Code is modeled on Austria's, and money laundering is criminalized through Article 165. It was last amended in 2000 when self-laundering was included in Article 1.1 and, in 2003, when Article 1.6 was added and terrorism financing became a predicate offence for money laundering.

Table 1

	2003	2004	2005	2006
Investigations	25	34	33	36
Prosecutions	0	0	1	1
Convictions	0	0	0	0
Transfer of proceedings to another jurisdiction	1	3	4	3

for money laundering is not possible in cases where the offender has been convicted for the predicate offense. Association or conspiracy of two persons to commit money laundering is not criminalized.

- In relation to customer due diligence², the report was critical of Liechtenstein's excessive discretion in identifying high-risk customers often as low- to medium-risk customers, and further criticized the lack of a specific requirement for enhanced due diligence. Most of Liechtenstein's financial business would be identified as high risk under the FATF risk-model, since more than 90 percent of the country's financial services would be defined as cross-border private banking, or private insurance or asset management services. Furthermore, the high number of non-resident customers, private banking, legal persons or arrangements such as trusts that are personal asset-holding vehicles, and companies that have nominee shareholders or shares in bearer form, would also be defined as high-risk. Those interviewed for the assessment cited only politically prominent persons (PEPs) and Eastern Europe as high-risk variables.
- The Liechtenstein DDA and DDO (see footnote 2) do not explicitly require verification of beneficial ownership information. Although in practice, trust service providers verify beneficial ownership to some degree, due to a requirement to determine the economic background and origin of assets, the legal obligations as defined in the DDA and DDO fall short of requiring that beneficial ownership be verified in all cases.

As for customer due diligence, the report concluded more attention should be paid to identifying beneficial ownership. The legislation does not reflect the definition of beneficial owner as set out in the FATF Recommendations, since it covers only persons who hold the economic rights to the legal entity's

assets, not those who hold control rights or interests, such as protectors/curators, nominee directors, or others who might manage a legal entity. It is also unclear whether in a trust arrangement, the trustee, as legal owner, or the beneficiary, as the beneficial owner, or both would be considered to hold economic rights to the trust assets. Article 10.4 requires identifying such persons, but applies only to trusts that have

Liechtenstein has not yet developed its own case law on money laundering


no or only one class of designated beneficiaries. Issues relating to the potential misuse of bearer shares were also highlighted.

Furthermore, the obligation to obtain beneficial ownership information, without assuming that the contracting party is the beneficial owner, covers only legal entities that are not commercially active in the domiciliary state and does not extend to commercially-active companies elsewhere.

- It is thought that the automatic freezing of assets for five days following reporting is counterproductive and reduces the inclination to file suspicious activity reports (SARs.)
- Furthermore, contrary to international standards, tipping-off³ is allowed 20 days from receipt of the report by the FIU. At the time of the 2002 OFC assessment of Liechtenstein, tipping-off was limited to only 10 days. Following recommendations made by the IMF, Liechtenstein extended the tipping-off prohibition to 20 days, so the situation remains noncompliant with the FATF standard. Liechtenstein authorities reportedly have committed to addressing the recommendations for removal of the time limit on tipping-off.

- As to information regarding cross-border wire transfers, the report recommended bringing requirements into line with the international standard. Liechtenstein's threshold for exemption is above the USD/EUR1,000 limit. Information requirements for international transactions were viewed as insufficient. Operations with Switzerland are considered domestic transfers. Furthermore, banks can avoid giving information for so-called legitimate reasons, and are not required to maintain information being transmitted through the payment chain. The authorities stated that improvements are anticipated.
- The report found that appropriate legal means for tracing criminal assets or proceeds are in place, but it was critical of the "soft-approach" to confiscation and forfeiture, which risks to undermine the deterrent effect of the measure.

Although confiscation of laundered assets is not formally covered, confiscation of direct and indirect criminal proceeds, the product of crime, the instrumentalities, and equivalent value are broadly covered. Also, confiscation of (intended) instrumentalities is seriously restricted by the condition that these objects can be forfeited only when they have a "dangerous nature" or are apt to be used in other crimes.

In summary, beyond the problems related to the different legal frameworks of individual states, both within the EU and beyond, and the difficulties that arise from "double criminality" requirements, a number of other nuts need to be tightened within Liechtenstein's AML framework. International bodies have praised the progress that Liechtenstein has made, but criticize the loopholes that continue to make it an attractive country for managing criminal proceeds. Given Liechtenstein's current discussions on implementing the third EU directive, further progress in closing some of these loopholes should be expected. 

Jennifer Hanley, CAMS, managing director, Business Risk Research, Berlin, Germany, jennifer.hanley@business-risk-research.com