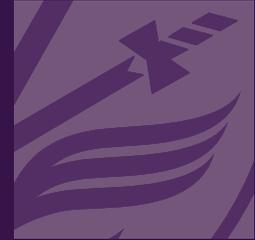




Royal United Services Institute  
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Conference Report

# Euro SIFMANet: European Sanctions and Illicit Finance Monitoring and Analysis Network Berlin Report



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RUSI Conference Report, December 2022



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SIFMANet is a collaborative network, led by the Centre for Financial Crime and Security Studies at RUSI, in collaboration with RUSI Europe, and supported by the National Endowment for Democracy. The network aims to bolster the response of EU member states to the national security threat posed by illicit finance to democracies and to provide viable policy recommendations.

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# Euro SIFMANet: European Sanctions and Illicit Finance Monitoring and Analysis Network: Berlin Report

IN LATE NOVEMBER 2022, the Centre for Financial Crime and Security Studies at RUSI convened a roundtable discussion (in partnership with the Jacques Delors Centre at the Hertie School) and a series of one-on-one meetings involving representatives from government ministries and agencies, and the private sector (such as banks, law firms and other organisations exposed to sanctions implementation) in Berlin as part of its ongoing study of EU sanctions implementation and wider responses to illicit finance (Euro SIFMANet) funded by the National Endowment for Democracy.

## Background

This roundtable discussion and series of one-on-one meetings was overshadowed by the August 2022 publication by the Financial Action Task Force (FATF) of its fourth-round Mutual Evaluation Report (MER) of Germany.<sup>1</sup> As a result, before turning to the roundtable and one-on-one meetings themselves, this report first provides a brief summary of the key points from the MER, as they featured repeatedly in the discussions held in Berlin during the RUSI visit.

The FATF noted many accomplishments in Germany's compliance with its standards on anti-money laundering and countering the financing of terrorism (AML/CFT) since its previous evaluation in 2010. In contrast to many jurisdictions, Germany did not complete its first national risk assessment until 2019, a delay that may well have set back the development of its understanding of national money-laundering risks. That same year, it also established a public-private partnership, the Anti-Financial Crime Alliance, progress that likewise lagged European peers. Over this period, the country also sought to improve cooperation and coordination between federal and state governments by increasing the human resources of the main financial-sector supervisor (BaFin) and the financial intelligence unit (FIU). Limitations – in the provisions for asset recovery, and in the offence of money-laundering – were removed, and a Transparency Register was introduced to improve access to information on beneficial ownership. Alongside these major changes to reinforce the fight against illicit finance, Germany also introduced non-

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1. Financial Action Task Force (FATF), 'Anti-Money Laundering and Counter-Terrorist Financing Measures – Germany', Fourth Round Mutual Evaluation Report, August 2022.

conviction-based asset-confiscation laws in 2017 and made asset confiscation a mandatory consideration for prosecutors in every case.

However, as is often the case in FATF evaluations, Germany's compliance with the FATF standards is stronger in the technical dimension than in implementation. For example, in its evaluation, the FATF observed a number of significant shortcomings, including the concerning observation that 'there is no clear policy or strategy for disrupting and sanctioning ML [money laundering] in a consistent and comprehensive manner' in the country. The reasons for this lack of effectiveness – elaborated further below – are explained by a series of challenges identified in the MER, challenges that Germany is now working to overcome in order to finally achieve an effective response to financial crime and illicit finance.

At the same time, increasing evidence is emerging of adversarial states seeking to weaponise finance against Western democracies, taking advantage of the kinds of vulnerabilities that exist in Germany. Not only do kleptocrats continue to sequester their money in the open and freely accessible markets in Europe, they also endeavour to use this money to buy influence in these same countries. More alarmingly, the US State Department has recently revealed that Russia has spent \$300 million seeking to exert influence over elections worldwide to undermine democracies at a time of widespread political instability.<sup>2</sup> This goal is enabled by weak regulations, legal loopholes and underpowered law enforcement responses in countries such as Germany. In this critical context, it is essential for all EU member states to have a strong regime to counter illicit finance and ensure that the sanctions regimes against Russia are comprehensively implemented.

With this background in mind, this report now turns to the substantive issues raised during the roundtable and one-on-one discussions.

## Germany's Challenges

In presentations and interventions at the roundtable, and discussions in one-on-one meetings, several key challenges in Germany's approach to sanctions enforcement and countering illicit finance were repeatedly highlighted. Participants specifically drew attention to a fragmented agency structure, a struggling FIU, inadequate staffing and resourcing, and – notwithstanding its success – limitations in the Transparency Register.

As participants noted, despite Germany's technical compliance with the FATF standards, outcomes – and thus effectiveness – fall short. For example, the overall number of money-laundering cases investigated and prosecuted in Germany is low, especially given the size of the country and its economy.<sup>3</sup> Germany is described in its MER as having a rather reactive approach

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2. Edward Wong, 'Russia Secretly Gave \$300 Million to Political Parties and Officials Worldwide, U.S. Says', *New York Times*, 13 September 2022.

3. The FATF did not count cases where ML and the predicate offence were successfully prosecuted (in most of these cases the ML charges were dropped because the predicate offence was the more serious offence).

to the identification of money laundering and lacking sufficient understanding of issues such as: money-laundering involving professional networks; cash smuggling; foreign predicate offences; complex money laundering; and cases involving legal persons. This was endorsed during the roundtable, with the added observation from several participants that the focus in the country currently relies on prosecuting predicate offences, often not pursuing money-laundering charges in cases where there is no clear link to a predicate offence. As a result, the number of convictions for money laundering rarely reaches 1,000 per year, with all but a fraction being domestically focused and against financial agents and money mules, concerning low-volume financial flows. Complex cases involving cross-border networks are rarely pursued.

Both public and private sector participants in the roundtable agreed that a major challenge that has led to this current state is the **fragmented agency structure** of the response against financial crime. Currently, the competent authorities include the Central Customs Authority, the Federal Criminal Police Office, 16 state criminal investigation offices and a number of large police headquarters throughout the country. Supervision of the formal banking sector is satisfactory, but a particularly concerning fact that exemplifies this fragmented – and ultimately ineffective – regime is the number of supervisory entities for Designated Non-Financial Businesses and Professionals (such as lawyers, accountants and insurance companies). At more than 300 agencies, the number of supervisory entities is larger than the actual number of staff members working within them.

The role of the FIU also represents a major challenge. In a significant structural reform in 2017, the FIU was transferred from the Federal Criminal Police Office (BKA) to the Central Customs Authority. Since then, non-government experts at the roundtable asserted that the FIU has been in a permanent state of crisis, a claim supported by media reporting.<sup>4</sup> The FIU has seen an increase in its capabilities and a rise in the dissemination of its output to law enforcement agencies has followed. However, despite the growing number of suspicious transaction reports (STRs) being filed, from 32,008 reports in 2016 to 144,005 reports in 2020, the FATF regards the level of usage of FIU intelligence to be very low, bringing into question the quality and relevance of the information gathered by the FIU.<sup>5</sup> In this regard, **staffing and resourcing** are seen as two major obstacles. Representatives in the roundtable from both the public and private sectors highlighted the shortage of financial investigators and insufficient access to data in financial investigations, compounded by issues with IT. Until as recently as February 2018, STRs were sent by fax to the FIU, and access to important databases such as the Electronic Account Retrieval System, the Customs database and the Transparency Register is still not automated in many cases.

While the introduction of the **Transparency Register** was noted by participants as an achievement in increasing transparency in the country – although as discussed below, this has been reversed

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4. Karin Matussek, 'German Finance Ministry Raided Over Anti-Money Laundering', *Bloomberg News*, 9 September 2021.

5. FATF, 'Anti-Money Laundering and Counter-Terrorist Financing Measures – Germany'.

by a recent ruling from the European Court of Justice (ECJ)<sup>6</sup> – a range of issues hinder its effectiveness. In its MER, the FATF highlights that, between 2017 and 2021, if information on a legal entity was previously registered on the Commercial Register, registration would not be required on the Transparency Register, even though the former did not contain beneficial ownership information in most cases.<sup>7</sup> This created the notion of a ‘fictitious’ beneficial owner, which, combined with a lack of systematic data review and no linkage to data from other key registries (notably land registers<sup>8</sup>), rendered the data in the Transparency Register unreliable.

## Germany’s Response

The roundtable also focused on how Germany has responded. Participants in the roundtable and the interviews addressed in detail the ongoing legislative developments in the country to strengthen the implementation of sanctions and reinforce the overall AML regime, with the passing of two Sanctions Enforcement Acts and a new AML architecture.

Structural reforms in the regime against financial crime were already underway in Germany, but the publication of the MER and the invasion of Ukraine have been catalysts for national efforts. EU restrictive measures against Russia range from asset freezes of listed individuals and travel bans, to restrictions on imports and exports. In May 2022, Germany passed the **Sanctions Enforcement Act I** (SEA I, Sanktionsdurchsetzungsgesetz I) to ensure the effective national implementation of sanctions. The rationale of this first act was to introduce measures that could be implemented in the short term, mainly aiming to enhance the capabilities of responsible authorities and their access to information. The act amended the Foreign Trade and Payments Act, the Money Laundering Act, the Banking Act, and the Securities Trading Act.<sup>9</sup> Alongside the existing authorities tasked with the enforcement of sanctions, including the Bundesbank, BaFin, the Central Financial Transactions Investigation Agency (Germany’s FIU), the Customs Criminological Office (ZKA) and the Federal Office for Economic Affairs and Export Control (BAFA), the states now also have administrative powers when it comes to detecting and, if necessary, sequestering sanctioned assets.

Government officials attending the roundtable explained that in seeking greater structural changes to facilitate a more effective implementation of sanctions, the Ministry of Finance and the Federal Ministry for Economic Affairs and Climate Action have put forward **Sanctions**

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6. European Court of Justice, Judgment of 22 November 2022 in joined cases C-37/20 and C-601/20, <<https://curia.europa.eu/juris/document/document.jsf?jsessionid=66B70588C0220A2067037C74990CFB53?text=&docid=268842&pageIndex=0&doclang=EN&mode=req&dir=&occ=first&part=1&cid=1093680>> , accessed 5 December 2022.

7. *Ibid.*

8. Land registers are also decentralised and operated by local district courts. There have been plans to create a centralised land register, but the slow pace of digitisation hinders its launch.

9. Außenwirtschaftsgesetz, Geldwäschegesetz, Kreditwesengesetz and Wertpapierhandelsgesetz.

**Enforcement Act II** (SEA II),<sup>10</sup> which was approved by the German Bundestag on 1 December 2022.<sup>11</sup> Participants acknowledged that SEA II presents a greater advance, with the establishment of a new Central Office for Sanctions Enforcement to be created by January 2023 within the General Directorate of Customs. The new Central Office will assume the administrative powers of the states and will manage asset freezes, coordinate sanctions implementation, investigate suspected sanctions-evasion cases and share intelligence with foreign counterparts. The new act is also set to:

- Create a register of assets of sanctioned persons and partnerships, as well as assets that cannot be clearly assigned.
- In the future, ban payments with cash, crypto-currencies and commodities such as precious metals and gemstones for the purchase of real estate.
- Link land registries and real estate data to the Transparency Register showing the true owners of real estate, and revealing where the true owners are unknown.
- Require foreign legal entities that own real estate in Germany to inform the beneficial ownership register.
- Achieve more transparency in the identity of the beneficial owner.
- Make ownership and control structure overviews available to authorities.

However, consistent with the broader lack of illicit finance supervisory and enforcement framework in Germany, the country required broader structural improvements that would allow for the truly effective implementation of the national AML regime, beyond the implementation of sanctions. The Ministry of Finance thus aims to combine relevant key competencies, ensure coordination and steer priorities under one roof via the creation of a Higher Federal Authority for Combating Financial Crime. With this, as announced by the German government<sup>12</sup> and reiterated by government officials at the roundtable, the fight against financial crime will be approached in a holistic manner, seeking to break siloes and enhance the expertise of staff. The focus will be placed on the maxim ‘follow the money’, to target criminal financial flows connected to criminal networks and other offences that harm social cohesion and justice. Under the Higher Federal Authority for Combating Financial Crime, the new AML framework will include:

- The new Federal Financial Criminal Office.

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10. German Federal Ministry of Finance, ‘Zweites Gesetz zur effektiveren Durchsetzung von Sanktionen (Sanktionsdurchsetzungsgesetz II)’, 21 November 2022, <[https://www.bundesfinanzministerium.de/Content/DE/Gesetzestexte/Gesetze\\_Gesetzesvorhaben/Abteilungen/Abteilung\\_IV/20\\_Legislaturperiode/2022-10-26-SanktionsdurchsetzungsgII/0-Gesetz.html](https://www.bundesfinanzministerium.de/Content/DE/Gesetzestexte/Gesetze_Gesetzesvorhaben/Abteilungen/Abteilung_IV/20_Legislaturperiode/2022-10-26-SanktionsdurchsetzungsgII/0-Gesetz.html)>, accessed 23 November 2022.

11. German Bundestag, ‘Initiative zur “effektiven Durchsetzung von Sanktionen” angenommen’, Dokumente, 1 December 2022, <<https://www.bundestag.de/dokumente/textarchiv/2022/kw48-de-sanktionsdurchsetzungsgesetz-923082>>, accessed 5 December 2022.

12. German Federal Ministry of Finance, ‘Stepping up the fight against financial crime’, 25 August 2022, <<https://www.bundesfinanzministerium.de/Content/EN/Standardartikel/Topics/Priority-Issues/Financial-Crime/fight-against-financial-crime.html>>, accessed 3 December 2022.

- The FIU, made more effective and partnered with the Federal Financial Criminal Office.
- A central office for coordinating money-laundering supervision in the non-financial sector.

As further detailed by roundtable participants, the next step would be to remove the Central Office for Sanctions Enforcement (as well as the FIU) from the General Directorate of Customs and transfer it to the future Higher Federal Authority for Combating Financial Crime. However, according to participants at the roundtable, this end state is in flux and thus the entire architecture might still be changed.

## Looking to the Future

The discussions also looked to the future. Participants spoke about the continuing need to prioritise the threat from illicit finance, the need to reallocate resources to ensure an effective response to changing circumstances, the key role of the private sector, and the need for greater transparency and access to accurate data.

With the new AML and sanctions reforms on track to be introduced in Germany, it was noted that some gaps and issues remain to be addressed. For example, the roundtable considered the interest of the general public in financial crime. It was widely accepted by roundtable participants that AML experts often do not phrase their statements in an accessible manner, yet the unjust advantage that non-compliance gives to businesses in breach of responsibilities and the impact of illicit financial flows in noticeable sectors, such as access to the purchase of real estate as a result of inflated prices, does lead to greater media attention and overall public concern. Regardless of the public attention these measures receive, the threats posed by illicit finance to a country's security and democracy should engender a **prioritisation** of this issue.

In light of the concerning weaknesses highlighted in Germany's MER, the need to enforce sanctions against Russia has galvanised efforts to reinforce the country's AML framework. Roundtable participants, particularly those from the private and non-government sectors, noted that this rising priority must be met with a **reallocation of resources** to ensure that responsible authorities have the necessary human resources and capabilities to fulfil their tasks effectively. This reflects a concern faced by authorities in many countries: the difficulty in retaining the talent of financial investigators in the public sector who are lured away by private sector salaries. Given the current geopolitical and security context, and the changing domestic political context following the 2021 election, there has been a noticeable and welcome increase in political will and support for remedial action in Germany's response to illicit finance as well as a clear focus on the importance of sanctions implementation. Another dimension where efforts should be dedicated is the introduction of effective technology to combat financial crime, a commendable priority under the recently concluded German presidency of the FATF. New technologies can be leveraged by the private sector and supervisors to implement AML/CFT measures more

efficiently, and by operational agencies to detect and investigate money-laundering or terrorist-financing cases, while allowing data pooling, collaborative analytics and data protection.<sup>13</sup>

The effective implementation of these measures and the successful rearrangement of the structural framework of Germany, for both illicit finance and sanctions implementation, is also dependent on the effective **involvement of the private sector**, given how central it is to the fight against illicit finance and the effective implementation of sanctions. Promoting engagement from the private sector should be led by the example of the state. On the sanctions side, banks are largely familiar with the requirements of sanctions-related asset freezes, and industrial companies exposed to export-control requirements and complex matters such as the manufacture of dual-use goods are likewise used to managing the required licensing and approval processes. However, sanctions have posed new and unique challenges for many industrial companies that are dealing with sanctions for the first time after the inclusion of new trade sectors under EU restrictive measures; many German industrial companies do not have the capacity or expertise to implement sanctions effectively in light of this inexperience. It is thus imperative that these private sector actors receive support from the public sector to ensure their correct understanding of sanctions and facilitate their implementation.

A common element to ensuring the effectiveness of any element included in this report is **data transparency and accessibility**, enabling the clear understanding of who owns particular companies and assets, and supporting the ability of the private sector and journalists/civil society to conduct their investigations. One participant also noted that there is currently little information published by the German government on the effectiveness of sanctions, such as the amount of funds that have been frozen. In contrast, the UK publishes the amounts that have been frozen,<sup>14</sup> which facilitates the monitoring of progress in a country's efforts to enforce sanctions. The publication of asset recovery data likewise enables measurement of the advancement of efforts to counter illicit finance. Roundtable participants also drew attention to the gaps – mentioned earlier in this report – in the Transparency Register, which act as core obstacles that should be addressed by Germany's planned structural reforms. Ensuring the veracity and completeness of the data included in the register must be prioritised to strengthen the country's ability to identify beneficial ownership. At the time of the roundtable, the ruling from the ECJ limiting the general public's access to information on beneficial ownership had not yet been made public. Since then, public access to the Transparency Register has been 'suspended until further notice', in line with the ECJ ruling.<sup>15</sup>

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13. FATF, 'Opportunities and Challenges of New Technologies for AML/CFT', July 2021, <<https://www.fatf-gafi.org/media/fatf/documents/reports/Opportunities-Challenges-of-New-Technologies-for-AML-CFT.pdf>>, accessed 2 December 2022.

14. HM Treasury, 'Financial Sanctions Targets: List of All Asset Freeze Targets', updated 11 November 2022, <<https://www.gov.uk/government/publications/financial-sanctions-consolidated-list-of-targets/consolidated-list-of-targets>>, accessed 23 November 2022.

15. Transparency Register, Bundesanzeiger Verlag, <<https://www.transparenzregister.de/treg/en/start;jsessionid=A1B106E1C24B02446147B1E54081403A.app12?0>>, accessed 2 December 2022.

Leveraging the experience of other jurisdictions such as Italy – a country that has strong experience of developing a centralised structure with enhanced powers – could also support Germany’s efforts to strengthen its ability to combat illicit finance. New tools to enhance the fight against illicit finance and sanctions evasion should also be considered. For example, Unexplained Wealth Orders in the UK and similar instruments in Ireland have demonstrated the possibilities (and pitfalls) of introducing instruments that aim to overcome some of the challenges faced by law enforcement in complex illicit finance cases by reversing the burden of proof in legal proceedings. The difficulty in implementing Suspicious Wealth Orders – as labelled by some in Germany<sup>16</sup> – was addressed in the roundtable, noting risks of contradicting basic constitutional law. Moreover, regulation requiring data collection, which would facilitate the investigation and prosecution of illicit finance offences, is often met with public reluctance. This matter continues to be an international challenge, although in an increasing number of countries, a balance has been found between data privacy and attaining sufficient information to effectively build a regime against illicit finance and facilitate the identification and prosecution of sanctions evasion.

## Conclusion

The discussions in Berlin reiterated a view widely held across the EU that although the Russian war in Ukraine has catalysed reform of illicit finance and sanctions legislation in many EU member states – Germany included – countries should not see these efforts merely as a response to the war; nor should they be confined to a box-ticking exercise seeking compliance with the FATF standards.

Efforts must be focused on achieving robust AML and sanctions-implementation regimes with the clear objective of combating illicit finance and sanctions evasion, not merely meeting compliance requirements, and, in doing so, reinforcing the rule of law and the security of democracy.

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16. Mohamad El-Ghazi, Kilian Wegner and Till Zimmermann, ‘Im Zweifel verdächtiges Vermögen einziehen’, Legal Tribune Online, April 2022, <<https://www.lto.de/recht/hintergruende/h/ussland-sanktionen-verdaechtiges-vermoegen-intransparenz-organisierte-kriminalitaet-geldwaesche-vorschlag-reform-suspicious-wealth-order/>>, accessed 29 November 2022.