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COVER NOTE

From: Mr Mario DRAGHI, President of the European Central Bank
date of receipt: 14 October 2016
To: Mr Jeppe TRANHOLM-MIKKELSEN, Secretary-General of the Council of the European Union

Subject: Opinion of the European Central Bank on a proposal for a directive of the European Parliament and of the Council amending Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing and amending Directive 2009/101/EC (CON/2016/49)

Delegations will find attached the above-mentioned Opinion.



EUROPEAN CENTRAL BANK
EUROSYSTEM

Mario DRAGHI
President

Frankfurt/Main, 12 October 2016

Mr Jeppe Tranholm-Mikkelsen
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Opinion of the European Central Bank on a proposal for a directive of the European Parliament and of the Council amending Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing and amending Directive 2009/101/EC (CON/2016/49)

Dear Mr Tranholm-Mikkelsen,

Please find attached, for your information, the Opinion of the European Central Bank on a proposal for a directive of the European Parliament and of the Council amending Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing and amending Directive 2009/101/EC (CON/2016/49).

Yours sincerely,

Encl.



OPINION OF THE EUROPEAN CENTRAL BANK

of 12 October 2016

on a proposal for a directive of the European Parliament and of the Council amending Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing and amending Directive 2009/101/EC

(CON/2016/49)

Introduction and legal basis

On 19 August 2016 and 23 September 2016, the European Central Bank (ECB) received requests from the Council and the European Parliament respectively for an opinion on a proposal for a directive amending Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing and amending Directive 2009/101/EC¹ (hereinafter the 'proposed directive').

The ECB's competence to deliver an opinion is based on Articles 127(4) and 282(5) of the Treaty on the Functioning of the European Union, since the proposed directive contains provisions falling within the ECB's fields of competence. In particular, the ECB's competence to deliver an opinion is based on Article 127(2) and (5) and Article 128(1) of the Treaty, as the proposed directive contains provisions which have implications for certain tasks of the European System of Central Banks (ESCB), including the promotion of the smooth operation of payment systems, contributing to the smooth conduct of policies pursued by the competent authorities relating to the stability of the financial system and authorising the issue of euro banknotes within the Union. In accordance with the first sentence of Article 17.5 of the Rules of Procedure of the European Central Bank, the Governing Council has adopted this opinion.

1. Observations

1.1. Regulation of virtual currency exchange platforms and custodian wallet providers

1.1.1 The proposed directive expands the list of obliged entities to which Directive (EU) 2015/849 of the European Parliament and of the Council² applies in order to include providers engaged primarily and professionally in exchange services between 'virtual currencies' and 'fiat currencies' (understood in the proposed directive to be currencies declared to be legal tender³) and wallet

1 COM (2016) 450 final.

2 Directive (EU) 2015/849 of the European Parliament and of the Council of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, amending Regulation (EU) No 648/2012 of the European Parliament and of the Council, and repealing Directive 2005/60/EC of the European Parliament and of the Council and Commission Directive 2006/70/EC (OJ L 141, 5.6.2015, p. 73).

3 See recital 6 of the proposed directive.

providers offering custodial services of credentials necessary to access virtual currencies (hereinafter 'custodial wallet providers')⁴. The proposed directive also requires Member States to ensure that providers of exchanging services between virtual currencies and fiat currencies and custodian wallet providers are licensed or registered⁵. The ECB strongly supports these provisions, which are in line with the Financial Action Task Force (FATF) Recommendations⁶, given that terrorists and other criminal groups are currently able to transfer money within virtual currency networks by concealing the transfers or by benefiting from a certain degree of anonymity on such exchange platforms. The use of virtual currencies also poses greater risks than traditional means of payment in the sense that the transferability of virtual currency relies on the internet and is limited only by the capacity of the particular virtual currency's underlying network of computers and IT infrastructure.

In this context, the ECB also mentions that digital currencies do not necessarily have to be exchanged into legally established currencies. They could also be used to purchase goods and services, without requiring an exchange into a legal currency or the use of a custodial wallet provider. Such transactions would not be covered by any of the control measures provided for in the proposal and could provide a means of financing illegal activities.

- 1.1.2 The ECB recognises that the technological advances relating to the distributed ledger technology underlying alternative means of payment, such as virtual currencies, may have the potential to increase the efficiency, reach and choice of payment and transfer methods. The Union legislative bodies should, however, take care not to appear to promote the use of privately established digital currencies, as such alternative means of payment are neither legally established as currencies, nor do they constitute legal tender issued by central banks and other public authorities⁷. The ECB has several concerns as regards the differences that exist between what the proposal refers to as 'fiat currencies' and 'virtual currencies', one of which is the volatility associated with virtual currencies, which is typically higher than with currencies issued by central banks or whose issue is otherwise authorised by central banks, as this volatility does not always appear to be related to economic or financial factors. Other concerns are that: (a) unlike the holders of legally established currencies, the holders of virtual currency units typically have no guarantee that they will be able to exchange their units for goods and services or legal currency in the future; and (b) the reliance of economic actors on virtual currency units, if substantially increased in the future, could in principle affect the central banks' control over the supply of money with potential risks to price stability, although under current practice this risk is limited. Thus, while it is appropriate for the Union legislative bodies,

⁴ See recital 6 and point (1) of Article 1 of the proposed directive.

⁵ See point (16) of Article 1 of the proposed directive.

⁶ See the ATF's 'International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation: The FATF Recommendations' (February 2012). See also the 'FATF Report Virtual Currencies Key Definitions and Potential AML/CFT Risks' (June 2014) and the FATF 'Guidance for a risk-based approach - Virtual Currencies' (June 2015). All documents are available on the FATF's website at: www.fatf-gafi.org.

⁷ See page 13 of the Explanatory Memorandum accompanying the proposed directive and recitals 6 and 7 of the proposed directive. See also the European Parliament Committee on Economic and Monetary Affairs' Draft report on virtual currencies (2016/2007 (INI)) of 23 February 2016.

consistent with the FATF's recommendations, to regulate virtual currencies from the anti-money laundering and counter-terrorist financing perspectives, they should not seek in this particular context to promote a wider use of virtual currencies.

- 1.1.3 The term 'virtual currencies' is defined under the proposed directive as meaning 'a digital representation of value that is neither issued by a central bank or a public authority, nor necessarily attached to a fiat currency, but is accepted by natural or legal persons as a means of payment and can be transferred, stored or traded electronically'⁸.

The ECB would like to make a number of specific comments regarding this definition.

First, 'virtual currencies' do not qualify as currencies from a Union perspective⁹. In accordance with the EU Treaties and the provisions of Council Regulation (EC) No 974/98, the euro is the single currency of the Union's economic and monetary union, i.e., of those Member States which have adopted the euro as their currency¹⁰. Consistent with the approach, which has either already been adopted, or is currently being considered, by other jurisdictions regulating virtual currency exchange platforms, including Canada, Japan and the United States, the ECB recommends defining virtual currencies more specifically, in a manner that explicitly clarifies that virtual currencies are not legal currencies or money¹¹.

Second, given that virtual currencies are not in fact currencies, it would be more accurate to regard them as a means of exchange, rather than as a means of payment. Additionally, the proposed directive's definition of 'virtual currencies' as a means of payment does not take into account that in some circumstances virtual currencies can be used for purposes other than that of a means of payment¹². As noted by the Bank for International Settlements (BIS), the distributed ledger technology underlying many digital currency schemes could have a much broader application beyond payments¹³. In this respect, the FATF has noted that non-payment uses of virtual

⁸ Point (2)(c) of Article 1 of the proposed directive. The definition appears to be based on that proposed in paragraph 19 of the European Banking Authority's (EBA) Opinion on virtual currencies of 4 July 2014 (EBA/Op/2014/08), available on the EBA's website at www.eba.europa.eu.

⁹ See the definition of 'currency' in Article 2(a) of Directive 2014/62/EU of the European Parliament and of the Council of 15 May 2014 on the protection of the euro and other currencies against counterfeiting by criminal law, and replacing Council Framework Decision 2000/383/JHA (OJ L 151, 21.5.2014, p.1). See also page 16 of the International Monetary Fund's (IMF) Staff Discussion Note on 'Virtual Currencies and Beyond: Initial Considerations' (January 2016), available on the IMF's website at www.imf.org.

¹⁰ See the Preamble and Article 3(4) of the Treaty on European Union; Article 119(2) of the Treaty on the Functioning of the European Union; and Article 2 of Council Regulation (EC) No 974/98 of 3 May 1998 on the introduction of the euro (OJ L 139, 11.5.1998, p. 1).

¹¹ See, for example, Articles 2 to 5 of the Japanese Payment Services Act, which define cyber-currency to exclude the Yen and foreign currencies, and Section 103(3) of the United States' National Conference of Commissioners on Uniform State Laws Draft Regulation of Virtual Currency Businesses Act of February 2 2016, which defines virtual currency to exclude money. For a broad analysis of the regulatory treatment of Bitcoin in 41 jurisdictions, see The Law Library of Congress' 'Report on the Regulation of Bitcoin in Selected Jurisdictions' (January 2014); see also the proceedings of the Canadian Parliament's Standing Senate Committee on Banking, Trade and Commerce of 26 March 2014, where the Canadian Department of Finance stated that 'virtual currency is not ... the official currency of the country; it is not the Canadian dollar'.

¹² See page 24 of the ECB's report 'Virtual Currency Schemes – a further analysis' (February 2015), available on the ECB's website at www.ecb.europa.eu.

¹³ See page 15 of the BIS' Committee on Payments and Market Infrastructures' report on 'Digital currencies' (November 2015), available at www.bis.org.

currencies may include store-of-value products for savings or investment purposes, such as derivatives, commodities, and securities products¹⁴. More recent digital currencies, which are based on more sophisticated distributed ledger and block chain technology, have a large array of uses that go beyond payment purposes¹⁵, including for example, online casinos. In the light of the above, the ECB suggests that the proposed directive also refers to other possible uses of virtual currencies in the proposed definition of that term.

The ECB suggests adapting the definition of virtual currencies under the proposed directive to take the above points into account.

1.2. Central registers of bank and payment accounts

1.3.1 Pursuant to the proposed directive, Member States are required to put in place centralised automated mechanisms or central electronic data retrieval systems, which would allow the identification, in a timely manner, of any natural or legal persons holding or controlling payment accounts and bank accounts held by a credit institution within their territory¹⁶. The explanatory memorandum accompanying the proposed directive clarifies in this respect that Member States are free to set up either a central banking registry, or a retrieval system, whichever best fits their own existing framework¹⁷. Member States are therefore free to designate their national central bank (NCB) as the administrator of the central register of bank (and payment) accounts. Moreover, under the proposed directive, such a central register would be open to access by the FIUs and other competent authorities.

1.3.2 The ECB has previously expressed its view that, for the purpose of assessing whether the Treaty prohibition on monetary financing is infringed, tasks entrusted to an NCB in the European System of Central Banks (ESCB) relating to the establishment of a central register of bank accounts are not to be considered central bank tasks, nor do they facilitate the enforcement of such tasks¹⁸. The ECB considers the task of establishing a central register pursuant to Article 30 of Directive (EU) 2015/849 to clearly be a government task since its purpose is to combat money laundering and the financing of terrorism. With a view to safeguarding the financial independence of the ESCB members and dispelling the monetary financing concerns associated with carrying out a government task, the ECB emphasises that, in taking up the task of operating a central register of accounts, the national legislation implementing the proposed directive should include a cost recovery mechanism with explicit procedures for monitoring, allocating and invoicing all costs

¹⁴ For instance, crypto-currencies like 'ethers', the currency unit of the 'ethereum block chain', are traded on exchanges for investment or speculative purposes, but do not always serve as a means of payment. See also page 4 of the FATF 'Guidance for a risk based approach - Virtual Currencies' (June 2015), available on the FATF's website at www.fatf-gafi.org.

¹⁵ See page 7 of the IMF Staff Discussion Note on 'Virtual Currencies and Beyond: Initial Considerations' (January 2016), available on the IMF's website at www.imf.org.

¹⁶ See point (12) of Article 1 of the proposed directive.

¹⁷ See page 7 of the Explanatory Memorandum accompanying the proposed directive.

¹⁸ See, for example, paragraph 2.1 of Opinion CON/2011/30; paragraph 2 of Opinion CON/2011/98; paragraphs 3.1 and 3.2 of Opinion CON/2015/46; and paragraphs 3.1 to 3.8 of Opinion CON/2016/35. All ECB opinions are available on the ECB's website at www.ecb.europa.eu.

incurred by the NCBs that are associated with operating and granting access to the central register.

2. Technical observations and drafting proposals

Where the ECB recommends that the proposed regulation is amended, specific drafting proposals are set out in a separate technical working document accompanied by an explanatory text. The technical working document is annexed to this Opinion and is available in English on the ECB's website.

Done at Frankfurt am Main, 12 October 2016.



The President of the ECB

Mario DRAGHI

Drafting proposals

Text proposed by the Commission	Amendments proposed by the ECB ¹
Amendment 1 Recital 7	
<p>(7) The credibility of virtual currencies will not rise if they are used for criminal purposes. In this context, anonymity will become more a hindrance than an asset for virtual currencies taking up and their potential benefits to spread. The inclusion of virtual exchange platforms and custodian wallet providers will not entirely address the issue of anonymity attached to virtual currency transactions, as a large part of the virtual currency environment will remain anonymous because users can also transact without exchange platforms or custodian wallet providers. To combat the risks related to the anonymity, national Financial Intelligence Units (FIUs) should be able to associate virtual currency addresses to the identity of the owner of virtual currencies. In addition, the possibility to allow users to self-declare to designated authorities on a voluntary basis should be further assessed.'</p>	<p>(7) The credibility of virtual currencies will not rise if they are used for criminal purposes. In this context, anonymity will become more a hindrance than an asset for virtual currencies taking up and their potential benefits to spread. The inclusion of virtual exchange platforms and custodian wallet providers will not entirely address the issue of anonymity attached to virtual currency transactions, as a large part of the virtual currency environment will remain anonymous because users can also transact without exchange platforms or custodian wallet providers. To combat the risks related to the anonymity, national Financial Intelligence Units (FIUs) should be able to associate virtual currency addresses to the identity of the owner of virtual currencies. In addition, the possibility to allow users to self-declare to designated authorities on a voluntary basis should be further assessed.'</p>
<u>Explanation</u> <i>See paragraph 1.1.2 of the Opinion.</i>	
Amendment 2 point (2)(c) of Article 1 (new point (18) of Article 3 of Directive (EU) 2015/849)	
<p>(18) "virtual currencies" means a digital representation of value that is neither issued by a central bank or a public authority, nor necessarily</p>	<p>(18) "virtual currencies" mean a digital representation of value that is neither issued by a central bank or a public authority, nor attached to a</p>

¹ Bold in the body of the text indicates where the ECB proposes inserting new text. Strikethrough in the body of the text indicates where the ECB proposes deleting text.

Text proposed by the Commission	Amendments proposed by the ECB ¹
attached to a fiat currency, but is accepted by natural or legal persons as a means of payment and can be transferred, stored or traded electronically.'	legally established fiat currency, which does not possess the legal status of currency or money, but is accepted by natural or legal persons, as a means of exchange and possibly also for other purposes, and which can be transferred, stored or traded electronically.'
<p style="text-align: center;"><u>Explanation</u></p> <p>See paragraph 1.1.3 of the Opinion.</p>	