Commission de Surveillance du Secteur Financier

ML/TF Sub-sector Risk Assessment

Collective Investment Sector (Update 2022)

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1. Foreword

This update of the Collective Investment Sub-Sector Risk Assessment ("SSRA") published in 2020 illustrates the effectiveness of the efforts made by the CSSF and the private and public sectors to mitigate the risk of money laundering and terrorist financing in the Collective Investment Sector.

This follow-up exercise has enabled us to update our comprehensive and shared understanding of the inherent risks faced by the Collective Investment Sector, the strengths of the current AML/CFT regime, and areas where mitigating measures should be developed further. It has been a joint and coordinated effort, led by the CSSF and with input from stakeholders across the Collective Investment and public sector.

The inherent risk for the Collective Investment Sector remains **high** as detailed in the National Risk Assessment ("NRA") updated in 2020[1].

The present assessment does not repeat general messages which were detailed in the 2020 SSRA but rather focuses on the evolutions to highlight several ML/TF threats and vulnerabilities that are increasingly important for the fund industry in Luxembourg.

This risk assessment is a valuable tool for all stakeholders to better understand the ML/TF risks associated with the Collective Investment Sector and the measures necessary to mitigate them. Supervised entities should use this risk assessment to strengthen their understanding of ML/TF threats and vulnerabilities and to implement proportionate and effective controls. To this end, the assessment details observed best practices, common findings from supervision, and targeted recommendations which the private sector should adopt. The CSSF will monitor the entities' adherence to these recommendations as part of its supervisory activities.

I would like to thank all of those who have participated in this exercise for their valuable contribution, in particular the members of the Expert Working Group on AML in the Collective Investment Sector. This SSRA should help financial actors to further strengthen their AML/CFT efforts so as to ensure that the AML/CFT framework is and remains effective and that Luxembourg remains a place where the Collective Investment Sector can thrive.

Marco Zwick, Director, CSSF

[1] https://mj.gouvernement.lu/dam-assets/dossiers/blanchiment/Brochure-import-version-04082021-002-.pdf

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2. Disclaimer

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. It shall therefore neither be interpreted for instance that all Chapter 15 ManCos present a High Inherent Risk, nor that all Luxembourg Registered AIFMs have a Medium-Low Residual Risk of ML/TF.

The reader is furthermore reminded that while the assessments and outcomes presented in the 2022 SSRA should be embedded by supervised entities in their ML/TF risk assessments as required pursuant to article 2-2 of the AML Law, it does not exempt those entities to perform their own ML/TF risk assessments taking into consideration their own risk factors, including those relating to their customers, countries or geographic areas, products, services, transactions or delivery channels.

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, geopolitical crisis must be taken into consideration in the ML/TF risk assessment of supervised entities depending on their exposure to involved markets/entities.

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3. Purpose and scope of the document

In January 2020, the CSSF published its first Sub-Sector Risk Assessment (SSRA) on ML/TF risks faced by the Collective Investment Sector.[2] The conclusions drawn in this assessment were based on quantitative data collected through different initiatives, in particular the annual AML/CFT 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 2020 risk assessment using quantitative and qualitative data related to the years 2020 and 2021.

Table 1: Overview of Luxembourg NRA – sub-sector risks

Sector		Inherent risk	Sub-sectors	Inherent risk (sub-sector)
1	Banks	High	Retail & business banks	4.0
			Wholesale, corporate & investment banks	3.9
			Private banking	4.4
			Custodians and sub-custodians (incl. CSDs)	3.7
2	Investment sector	High	Wealth and asset managers	3.6
			Brokers and broker-dealers (non-banks)	3.6
			Traders / market-makers	2.7
			Collective investments	4.1
			Regulated securitisation vehicles	2.9
			CSSF-supervised pension funds	2.0

In the Luxembourg National Risk Assessment published in September 2020[3], **the sub-sector of Collective Investments has been assessed as inherently High Risk** in relation to money laundering and terrorist financing.

The scope of this assessment encompasses all Luxembourg regulated undertakings for collective investments. **It focuses on Investment Fund Managers (IFM),** considering their specific AML/CFT roles and responsibilities.

[2] https://www.cssf.lu/en/Document/ml-tf-sub-sector-risk-assessment-2020/

[3] https://mj.gouvernement.lu/dam-assets/dossiers/blanchiment/Brochure-import-version-04082021-002-.pdf

Similar to its previous sub-sector risk assessment, the CSSF would like to stress that this document does not include unregulated investments vehicles nor pension funds. It does, however, include some indications regarding authorised securitisation vehicles.

The present document is aimed for public distribution and aims at fulfilling several objectives:

- To serve as a source for the investment fund industry when performing their own ML/TF risk assessments;
- To promote the understanding of ML/TF risks and AML/CFT obligations in the fund industry;
- To support public-private interaction;
- To reflect CSSF's own understanding of particular ML/TF risks in the sub-sector;
- To further improve CSSF's supervisory activities and sub-sector specific supervision strategy, where relevant; and
- To serve as an input for CSSF's risk assessments.

This document does not repeat the general messages of the initial SSRA on the Luxembourg Collective Investment Sector which have not changed since 2020, rather it focuses on the evolutions which have an impact on the ML/TF risks. Consequently, this document should be seen as an updated supplement to the 2020 SSRA.

The figures provided in the 2020 SSRA related to 2018 year-end, whereas the figures provided in the 2022 SSRA relate to 2020 year-end. Therefore, the assessment provided therein is based on the latest available full AML/CFT supervisory exercise performed by the CSSF throughout the year 2021 (based on data as of 31/12/2020). For information purposes only and where available, this document also provides in brackets, figures related to data as of 31/12/2021.

4. Introduction

This section provides an overview of the evolution of the Collective Investment Sector since 2020. The overview of the landscape and its main participants is not repeated as it has not changed since the 2020 SSRA.

4.1 Evolution of the Collective Investment Sector since January 2020 (product side)

Luxembourg offers a wide range of Undertakings for Collective Investments (UCI). These products take a variety of forms, depending on their category, regime and structure, as detailed in the 2020 SSRA.

The type of product offering for regulated UCIs has not changed since the 2020 SSRA and the two following main categories of collective investments therefore remain available in Luxembourg, with distinctive investment policies and investor bases:

- UCITS (Undertakings for Collective Investments in Transferable Securities), introduced in 1985 with the objective to create a single European market for open-ended investment funds investing in transferable securities and aimed towards retail investors;

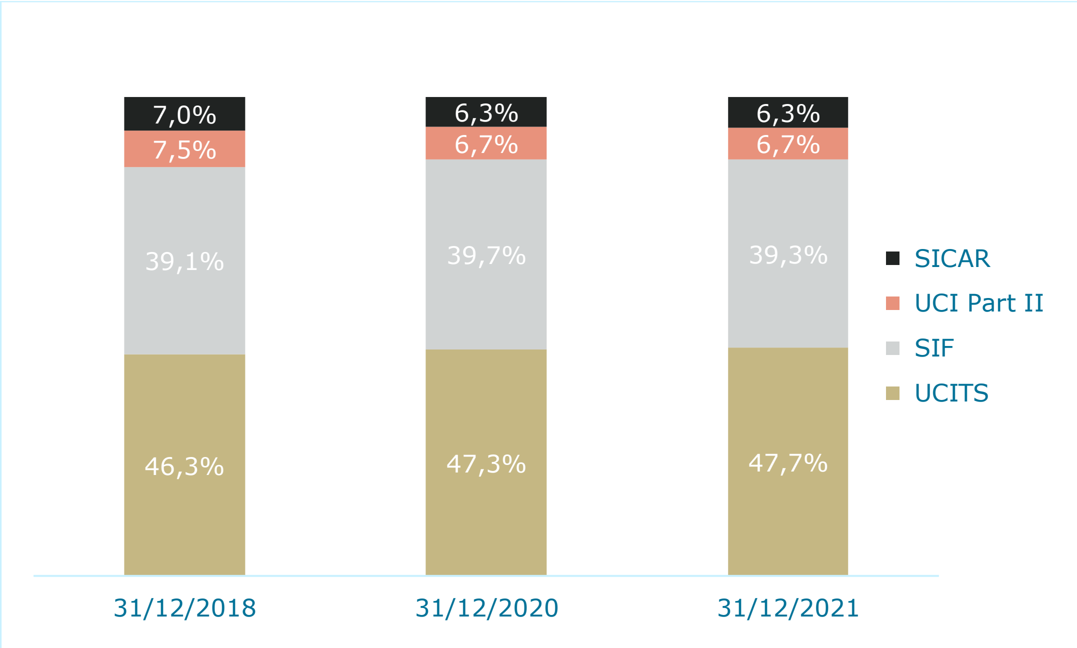
- AIF (Alternative Investment Funds), collective investments not covered by the UCITS Directive (e.g. hedge funds, venture capital, private equity or real estate) which are reserved to well-informed investors.

The aggregated total net assets (TNA) of Luxembourg funds regulated for AML/CFT purposes have progressed noticeably from EUR 4.065bn as per 31/12/2018[4] to EUR 4.974bn as per 31/12/2020[5] (EUR 5.859bn as of 31/12/2021), although the overall number of AML/CFT supervised investment funds has decreased from 3.908 to 3.611 (3.492 as of 31/12/2021).

[4] *2018 CSSF annual report (page 85)*

[5] *2020 CSSF annual report (page 75)*

Figure 1: Proportion of fund schemes per fund regime



Considering the above, the overall landscape of CSSF supervised UCIs has not considerably changed since the 2020 SSRA and the descriptions and explanations provided therein relating to the landscape, the UCI forms, categories, regimes and structures remain appropriate. Indeed, since the 2020 SSRA, the types of investment fund regimes per sectoral law remained unchanged and the scope of the AML/CFT supervision on investment funds has consequently not been widened.

4.2 Regulated securitisation undertaking issuing fiduciary notes

Regulated securitisation vehicles are governed by the law of 22 March 2004 on securitisation that issue securities to the public on a continuous basis (more than three issues per year).

Based on the aforementioned law, such entities are permitted to issue notes on a fiduciary basis pursuant to the Luxembourg Law of 27 July 2003 relating to trust and fiduciary contracts. The fiduciary arrangements underlying such fiduciary notes qualify for registration as per articles 13(1) and 1(5) and (6) of the Luxembourg Law of 10 July 2020 establishing a register of fiducies and trusts.

Regulated securitisation undertakings issuing such fiduciary notes are consequently acting as "a fiduciaire in a fiducie" within the meaning of article 1(8)(d) of the Luxembourg Law of 12 November 2004, as amended, on the fight against money laundering and terrorist financing ("AML Law") and are therefore considered as providing trust and company service activities as per article 2(1)6b of the AML Law.

As of December 2020, 29 regulated securitisation undertakings exist in Luxembourg (28 as of 31/12/2021), but only 2 of these entities issue fiduciary notes and are thereby regarded as providing trust and company service activities as per article 2(1)6b of the AML Law (3 as of 31/12/2021).

The CSSF has performed specific and targeted AML/CFT supervisory measures on the aforementioned entities throughout the year 2021, the extent and content of which will not be discussed in the updated SSRA considering the very limited number of regulated securitisation undertakings issuing fiduciary notes.

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4.3 Evolution of the Collective Investment Sector since January 2020 (Investment Fund Managers side)

Three main categories[6] of Investment Fund Managers ("IFMs") are active in Luxembourg, based on the type of UCI they manage[7]:

- Management Companies for UCITS (UCITS ManCo)[8];
- Alternative Investment Fund Managers for AIF (AIFM)[9]; and
- Self or internally-managed UCI.

Multiple regimes are available to IFMs based on the UCI they manage and their country of origin. These aspects have been explained in the 2020 SSRA and, given that the types of IFM categories and regimes remain unchanged, shall not be discussed any further in the updated SSRA.

As of 31/12/2021, the number of Luxembourg based Investment Fund Managers managing Luxembourg regulated products has decreased since the 2020 SSRA (cca -19%), however their assets under management have significantly increased (cca +40%). As of 31/12/2021, these entities manage cca. 79% of Luxembourg regulated assets under management.

As of 31/12/2021, the number of foreign based Investment Fund Managers managing Luxembourg regulated products has decreased since the 2020 SSRA (cca -11%), however their assets under management have significantly increased (cca +72%). As of 31/12/2021, these entities manage cca. 19% of Luxembourg regulated assets under management.

[6] *For the purpose of the updated SSRA, IFMs with multiple licences will be included in the most stringent regime (e.g. "Super ManCo" with Chapter 15 and authorised AIFM licences will be treated as a Chapter 15 ManCo).*

[7] *Note that managers may combine several regimes, e.g. "Super ManCo", being managers with both Luxembourg Chapter 15 and AIFM licences.*

[8] *This cluster is composed of Luxembourg Chapter 15 Management companies and EU/EEA UCITS Management companies.*

[9] *This cluster is composed of Luxembourg authorised and registered AIFMs as well as Luxembourg Chapter 16 Management companies and EU/EEA and non-EU/EAA AIFMs.*

As of 31/12/2021, the number of Luxembourg funds which have not appointed an Investment Fund Manager has decreased since the 2020 SSRA (cca -34%), however their assets under management remained equivalent. As of 31/12/2021, these entities represent cca. 2% of Luxembourg regulated assets under management.

5. Methodology

This section describes the approach used to update the assessment of ML/TF risks in the Collective Investment Sector.

5.1 Stakeholders & process

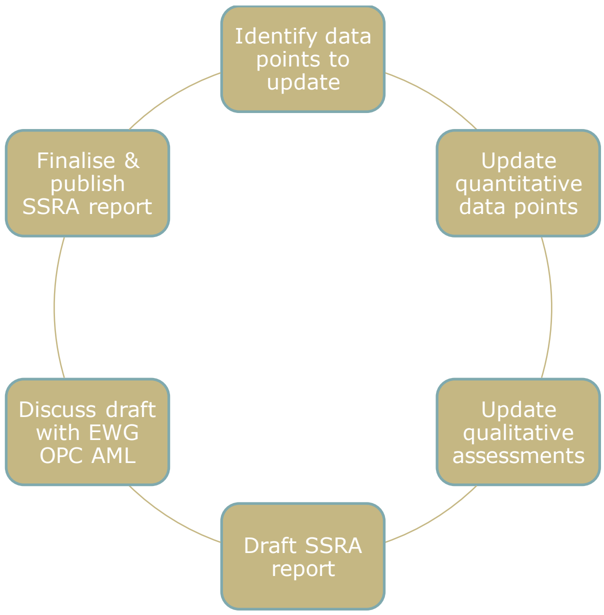
For comparability purposes, the stakeholders and process to update the SSRA remained comparable to the 2020 exercise.

The report was prepared by the CSSF and discussed with the Expert Working Group OPC 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) and the Luxembourg Barreau (Ordre des Avocats du Barreau de Luxembourg), as well as the ABBL Depositary Banking cluster and the Financial Intelligence Unit.

Since 2020, new members have joined the Group, in particular the Luxembourg Institute of Internal Auditors and the Administration de l'Enregistrement et des Domaines.

The process includes six different iterative steps which are illustrated below.

Figure 2: SSRA updating process



5.2 Scope and taxonomy

For comparability purposes, the scope and taxonomy of the present document mirrors the 2020 SSRA.

Therefore, the inherent risks and quality of mitigation measures are reviewed for the following three main clusters aiming at regrouping elements with similar characteristics and risk profiles into a manageable number of classes[10], in order to assess their relative ML/TF risk:

1. UCITS ManCo (including Super ManCo);
2. AIFM; and
3. Self or internally-managed UCI.

[10] *Each class is mutually exclusive, and all classes taken together cover the full spectrum of regulated collective investments in Luxembourg for ML/TF purposes.*

6. Inherent Risk – Threat Assessment Evolution

For the sake of clarity, the mainstream threats which were detailed in the 2020 SSRA are not mentioned in this document and remain accurate. The present report focuses on emerging threats which arose or significantly increased since January 2020.

The 2020 SSRA was published shortly before the global Covid-19 outbreak; Covid-19 also gave rise to new ML/TF threats for the Collective Investment Sector; as outlined in the CSSF publication "AML/CFT supervision in the Collective Investment Sector during the Covid-19 situation[11]".

A) Cybercrime

Criminal offences associated with *cybercrime* are predicate offences under the Luxembourg AML/CFT framework.

The lockdown and the subsequent waves of Covid-19 infections made homeworking, either complete or partial, a new way of working. This entailed potentially a difficulty in terms of communication and controls which resulted in an increase of CEO scams and other social engineering attacks on businesses and individuals[12]. According to INTERPOL Secretary General Jürgen Stock, "*Cybercriminals are developing and boosting their attacks at an alarming pace, exploiting the fear and uncertainty caused by the unstable social and economic situation created by COVID-19".* An assessment performed by INTERPOL on the impact of COVID-19 revealed that cybercrime has shown a *"significant target shift from individuals and small businesses to major corporations, governments and critical infrastructure."*[13]

In addition, as highlighted in a recent FATF publication, geopolitical crisis can increase the threat of cybercrimes faced by supervised entities[14].

[11] https://www.cssf.lu/wp-content/uploads/C_AML_CFT_supervision_collective_investment_covid19_040520_annexe.pdf

[12] Please see Circular CSSF 20/740 on Financial crime and AML/CFT implications during the Covid-19 pandemic for an in-depth analysis (Circular CSSF 20/740 – CSSF) and relevant publications by CRF

[13] https://www.interpol.int/en/News-and-Events/News/2020/INTERPOL-report-shows-alarming-rate-of-cyberattacks-during-COVID-19

[14] https://www.fatf-gafi.org/fr/publications/gafiengeneral/documents/ukraine-2022.html

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B) Purchases of businesses by organised criminal groups

Due to the Covid-19, some businesses lost significant turnover, in particular, in the hospitality sector. Organised criminal groups have been reported to exploit this situation to buy equity of businesses on the verge of bankruptcy in exchange of loans financed by funds arising out of predicate offences of money laundering[15]. These equity stakes in new business lines, in particular in the hospitality sector pose a new threat for the Collective Investment Sector, in particular for Private Equity and Real Estate investment strategies. In its latest amendment of its Regulation 12-02, the CSSF highlighted in article 34 the importance of performing AML/CFT due diligence on assets when performing investment operations.

C) Abuse of virtual assets

The year 2021 was marked by a very sharp increase in total market capitalisation of cryptocurrencies and trading volumes of virtual assets such as non-fungible tokens. On 29 November 2021, the CSSF published an FAQ on virtual assets notably to address questions raised by the Collective Investment Sector and updated it on 4 January 2022.

The underlying technology used for by virtual assets can provide a level of anonymity which can be abused by criminals. In addition, the volatility of these assets may be perceived as an opportunity of a higher return of investments by money launderers and terrorist financiers.

Since the publication of the 2020 SSRA, the CSSF has observed a slight rise in interest from Luxembourg Investment Fund Managers to manage investment funds directly or indirectly exposed to virtual assets in their portfolios.

D) Geopolitical crisis

The beginning of the year 2022 was marked by a geopolitical crisis which impacted the financial world on a global scale, notably through the implementation of targeted financial sanctions on designated persons, entities and bodies. For investment funds, these events can have consequences both on the investors and investments sides and thus, must be taken into consideration by CSSF supervised entities. There are several negative outcomes pertaining to such events on which the CSSF wishes to draw the attention upon:

[15] *Link to an illustrative press article : https://edition.cnn.com/2020/04/19/europe/italy-mafia-exploiting-coronavirus-crisis-aid-intl/index.html*

- Aggressive de-risking leading to financial exclusion: Some professionals may be tempted to extend the targeted financial sanctions to a larger population/geographical scope (for instance, based on nationality). While the CSSF does not interfere with entities' risk appetites, it reminds the professionals subject to its supervision of the risk of financial exclusion that could be the outcome of such practices and may be seen as an inadequate application of the Risk Based Approach [16].

- Increase in human-centred predicate offences of money laundering: Geopolitical crisis often involve massive refugees' flows that can be exploited by organised criminal groups[17]. The CSSF therefore stresses the necessity to perform specific due diligence on origin of funds and on transactions that would be located in, or close to, the jurisdiction concerned by the crisis, notably in case of unusual financial flows.

[16] *http://www.fatf-gafi.org/publications/financialinclusionandnpoissues/documents/unintended-consequences-project.html*

[17] *https://www.cssf.lu/en/2022/04/restrictive-measures-of-the-eu-in-response-to-the-current-situation-in-ukraine-and-anti-money-laundering-and-counter-terrorist-financing-measures/*

7. Inherent Risk – Vulnerability Assessment Evolution

This section assesses the evolution of the ML/TF vulnerabilities for each cluster used pursuant to the methodology, namely UCITS ManCo, AIFM and self or internally-managed UCI, as of 31/12/2020.

Considering the stability of the Collective Investment Sector, and for the purpose of comparability, the factors and underlying indicators used in this assessment remain identical to those used in the 2020 SSRA.

***Reminder**: The vulnerability assessment considers five main risk factors: (1) Intermediaries; (2) Clients/Investors and geography; (3) Market structure; (4) Products, services and transactions; and (5) Channels of distribution. It analyses how these five risk factors influence the ML/TF risk in each cluster and each class.*

Table 2 below provides an overview of the overall inherent vulnerabilities for each cluster and each class of elements in the updated SSRA.

Table 2: Inherent vulnerabilities for each cluster and elements of cluster – 2022 SSRA

<table>
<tr><th>Cluster</th><th>Inherent Risk (IR) 2022 SSRA</th><th>Element</th><th>Inherent Risk (IR) 2022 SSRA</th></tr>
<tr><td rowspan="2">UCITS ManCo (incl. SuperManCo)</td><td rowspan="2">High Risk</td><td>Lux Chap 15 ManCo</td><td>High Risk</td></tr>
<tr><td>EU/EEA UCITS ManCo</td><td>High Risk</td></tr>
<tr><td rowspan="5">AIFM</td><td rowspan="5">Medium-High Risk</td><td>Lux authorised AIFM</td><td>Medium-High Risk</td></tr>
<tr><td>Lux registered AIFM</td><td>Medium-High Risk</td></tr>
<tr><td>Lux Chap 16 ManCo</td><td>Medium-Low Risk</td></tr>
<tr><td>EU/EEA AIFM</td><td>Medium-Low Risk</td></tr>
<tr><td>Non-EU/EEA AIFM</td><td>Medium-Low Risk</td></tr>
<tr><td rowspan="2">Self or internally-managed UCI</td><td rowspan="2">Medium-High Risk</td><td>SIAG</td><td>Low Risk</td></tr>
<tr><td>FIAAG</td><td>Medium-High Risk</td></tr>
</table>

Note: the coloured circle in the Inherent Risk 2022 SSRA column provides information on the Inherent Risk Scoring in the 2020 SSRA and helps to identify the changes.

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Consequently, in the updated SSRA, the Luxembourg collective investments' largest inherent vulnerabilities arise from UCITS ManCos.

Similar to the 2020 SSRA, within the UCITS ManCo category, the Lux Chapter 15 ManCos present the highest inherent risk, primarily because of the volume of managed assets and because of the cross-border distribution of UCITS.

7.1 UCITS ManCo (including Super ManCos)

Within this cluster, **Luxembourg Chapter 15 ManCos** present a high inherent risk which is identical to the 2020 SSRA rating. This element of the cluster includes an important number of entities which manage the vast majority of assets in the Luxembourg Collective Investment Sector which is characterised by a high degree of concentration. This element of the cluster also has the largest number of branches and subsidiaries, both, in absolute and relative terms, across all clusters and most entities holding a license for discretionary portfolio management are Chapter 15 ManCos.

Luxembourg Chapter 15 ManCos use cross-border distribution networks to market their UCIs across Europe and in a number of non-EU jurisdictions and have a number of distributors which are not supervised for AML/CFT purposes by national competent authorities or self-regulatory bodies, although this number has decreased since the 2020 SSRA.

As already pointed out in the 2020 SSRA, the high inherent risk presented by this category is also explained by the volume of Assets under Management ("AuM") and the inclusion of entities benefitting from a double license (CH15 and AIFM) in this category. Therefore, the AIFM component of this cluster increases the inherent risk notably because of the types of investments made by AIFs.

The inherent risk scoring of **UCITS ManCos (including SuperManCos)** remains identical to 2020 SSRA (high risk).

EU/EEA UCITS ManCos are primarily located in France and, to a lesser extent, in Ireland, Spain and Germany and their numbers and AuM have increased significantly since the 2020 SSRA.

Therefore, the inherent risk scoring of **EU/EEA UCITS ManCos** increases since the 2020 SSRA (medium-high risk) to high risk.

7.2 AIFM

In line with the findings of the 2020 SSRA, **Lux authorised AIFMs**[18] are generally of moderate size with most Luxembourg AIFs initiated in France, Germany and the United States of America. The sector is characterised by a certain degree of concentration, with the top 10 entities representing more than half of total assets attributed to this element of the cluster.

AIFMs manage a diverse set of UCIs, across different regimes, generally subject to less rules and diversification requirements than UCITS, which increases the risk of investing in higher ML/TF risk assets.

The geographical reach of Luxembourg authorised AIFMs facilitated by EU/EEA passporting agreements may increase ML/TF vulnerability. However, the CSSF has noted a decrease of distributors marketing funds managed by these AIFMs which are not supervised by NCAs or self-regulated bodies for AML/CFT purposes.

The inherent risk scoring of **Lux authorised AIFMs** remains identical to the 2020 SSRA (medium-high risk).

Lux registered AIFMs only account for a small portion of all AuM which is mostly due to regulatory thresholds which limit AuM at EUR 100 million or EUR 500 million for unleveraged AIFs.

Investments from this element of the cluster are typically longer term which, to some extent, prevents some ML/TF typologies requiring a quick exit to gain access to the laundered funds.

It is however to be noted that the investment strategies of these IFMs are higher risk. The CSSF has notably identified several IFMs of that cluster managing funds investing in virtual asset strategies.

The inherent risk scoring of **Lux registered AIFM** remains identical to the 2020 SSRA (medium-high risk).

[18] Please note that AIFM with a CH15 license as well (Super ManCo) are counted in the Chapter 15 ManCo section of this report.

Lux Chap 16 ManCos represent a very small portion of Luxembourg based Investment Fund Managers. The number of entities in this element of the cluster has decreased since the 2020 SSRA but their AuM have slightly increased. This category represents only a very small share of the AuM in the Luxembourg Collective Investments Sector.

The inherent risk scoring of **Lux Chap 16 ManCos** remains identical to the 2020 SSRA (medium-low risk).

EU/EEA AIFMs act as designated AIFMs of Luxembourg investment vehicles and are primarily located and supervised in five countries: UK[19], France, Ireland and, to a lesser extent, the Netherlands and Sweden.

EU-EEA AIFM regimes have seen a reduction in terms of AuM between 31/12/2018 and 31/12/2020 which explains the slight decrease in inherent risk. The cross-border dimension remains a key ML/TF risk driver for that category.

The inherent risk scoring of **EU/EEA AIFMs** decreased from medium-high risk to medium-low risk since the 2020 SSRA.

Non-EU/EEA AIFMs also act as designated AIFM of Luxembourg investment vehicles, but are supervised by non-EU/EEA National Competent Authorities.

Non-EU-EEA AIFM regimes have seen a reduction in their AuM between 31/12/2018 and 31/12/2020. The cross-border dimension remains a key ML/TF risk driver to consider for that category.

The inherent risk scoring of **Non-EU/EEA AIFM** remains identical to the 2020 SSRA (medium-low risk).

[19] As the reference period for the updated SSRA is 31/12/2020, the United Kingdom is included in the EU / EEA category considering that the United Kingdom retained EEA rights during the transition period of the "Brexit" which ended on 31/12/2020.

7.3 Self-Managed UCIs ("SIAG", "FIAAG")

SIAGs are self-managed UCITS investment companies, which present lower ML/TF vulnerabilities due to the nature of their investments and regulatory restrictions. In their capacity as UCITS, SIAGs invest in traded securities such as bonds and equities, the transparency of which and liquidity requirements reduce the risk of abuse or misuse for ML/TF purposes.

Luxembourg only has a very limited number of **SIAGs** with a relatively low level of AuM and, as of 31/12/2020, the market is very concentrated around one particular SIAG which manages the near totality of all assets managed by Luxembourg SIAGs.

The inherent risk of **SIAG** remains identical to 2020 (low risk).

The second element of the cluster, **FIAAGs,** consists of:

1- SIFs and SICARs which qualify as AIFs which have not designated an Investment Fund Manager and therefore are often referred to as "self-managed AIFs". Similar to the findings of the 2020 SSRA, those funds appear to primarily invest in traded securities (e.g. bonds and equities), therefore reducing their ML/TF risk exposure on assets. FIAAGs are reserved to well-informed investors which may, however, include HNWIs and complex corporate structures with less transparent beneficial ownership chains which may in turn increase the ML/TF risk.
2- SIFs and SICARs which do not qualify as AIFs and which have not designated an Investment Fund Manager are often referred to as "self-managed Non-AIFs". For these entities, the risk regarding the liability side is often considered by these entities as low as in several cases the sole investor is the initiator. Regarding the assets side however, these funds have a wide array of strategies which can be complex or lack transparency and may therefore potentially be abused by money launderers or terrorist financiers. Nonetheless, this element of the cluster represents a very small portion of the Luxembourg AuM.

The inherent risk of **FIAAGs** remains identical to the 2020 SSRA (medium-high risk).

8. Evolution of mitigating factors and residual risk assessment

Similar to the 2020 SSRA, this section assesses risk mitigating factors, both supervisory measures and controls at entity level, and resulting residual risk for the different clusters.

The methodology for the assessment of risk mitigation remains identical to the 2020 SSRA for comparability purposes.

***Reminder**: It is based on four mitigating factors: Risk Based Approach, AML/CFT Supervision, Ongoing Monitoring and Procedures & Trainings.*

Table 3: Residual vulnerabilities for each cluster – 2022 SSRA

Cluster	Inherent Risk (IR) 2022 SSRA		Residual Risk (RR) 2022 SSRA
UCITS ManCo (incl. Super ManCo)	**High Risk**	Impact of mitigating factors	**Medium-Low Risk**
AIFM	**Medium-High Risk**	Impact of mitigating factors	**Medium-Low Risk**
Self or internally-managed UCI	**Medium-High Risk**	Impact of mitigating factors	**Medium-Low Risk**

Note: the coloured circle in the Residual Risk 2022 SSRA column provides information on the Residual Risk Scoring in the 2020 SSRA and helps to identify the evolution.

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8.1 UCITS ManCos (including Super ManCos)

For **Lux Chap 15 ManCos**[20], the CSSF noted an improvement in terms of the implementation of a Risk Based Approach both on the UCI's liability and asset side.

The overall level of mitigation measures implemented by this cluster has improved, in particular when it comes to the oversight on third parties performing AML/CFT controls on behalf of the IFM. The due diligence processes have been more precise and better documented but, in some cases were still lacking an in-depth analysis and remediation of identified shortcomings.

The content and frequency of AML trainings have improved, which contributed to the overall improvement of the quality of mitigation measures.

The conclusions of external and internal control functions (Internal Audit and Statutory Auditor) remained similar to those of 2020.

For **EU/EEA UCITS ManCos**, the quality of the mitigation measures implemented by these IFMs was assessed mostly through the results of the international cooperation performed by the CSSF with other European National Control Authorities, like in 2020. No particular deviation was noted since the 2020 SSRA.

8.2 AIFM

For **Lux authorised IFMs**, the CSSF did not identify any significant change regarding the implementation of a Risk Based Approach, however it noted a moderate modification of the results of the work performed by the external and internal control functions which identified more shortcomings in the AML/CFT framework of these entities. A change of compliance rating from "Compliant" to "Largely Compliant" by these control functions was observed in this cluster, which is in line with the CSSF's own observations.

Nevertheless, the CSSF noted significant improvements in the due diligence performed on assets, screening of Targeted Financial Sanctions and oversight on distributors (when applicable).

Similar to Lux Chapter 15 ManCos, the content and frequency of AML trainings have improved, which contributed to the overall improvement of the quality of mitigation measures.

[20] *Including « Super ManCos »*

Lux Registered AIFMs had been identified as a class needing significant improvements in the 2020 SSRA. They have demonstrated some improvements in terms of their AML/CFT framework, notably through the set-up of tailor-made AML/CFT procedures and policies and the registration with the GoAML platform used by the Financial Intelligence Unit, but also and more importantly, through a major review of their understanding of their exposure to the risks of ML/TF both on the UCI's liability and assets side. The CSSF also noted an improvement in terms of ongoing monitoring of third parties performing AML/CFT controls on their behalf, in particular Registrar and Transfer Agents.

Similar to Lux registered AIFMs, **Lux Chap 16 ManCos** have improved the quality of their mitigation measures notably through a better understanding of their exposure to the risks of ML/TF. This class has also improved its ongoing monitoring of third parties performing AML/CFT controls on their behalf, in particular investment advisors and distributors.

Comparable to EU/EEA UCITS ManCos, the quality of the mitigation measures implemented by **EU/EEA AIFMs and Non-EU/EEA AIFMs** was assessed mostly through the results of the international cooperation performed by the CSSF with other European National Control Authorities.

8.3 Self-Managed UCIs

SIAGs already had a strong AML/CFT framework in place at the time of the 2020 SSRA and it remained stable. The CSSF did not identify significant shortcomings in its ongoing offsite AML/CFT supervision.

Similar to the 2020 SRRA, with regards to **FIAAGs**, the CSSF observed similar mitigation quality trends as with the Lux registered AIFM cluster.

9. Outcome of this report

The outcome of the analysis performed by the CSSF for the drafting of this Sub Sector Risk Assessment is unequivocally an overall improvement of the quality of the mitigation measures implemented by the entities in scope. The CSSF sees this positive evolution as the result of (i) the increased involvement in the AML/CFT framework of the Senior Management and control functions of these entities, (ii) the result of the work performed by the professional associations to provide guidance to their members, (iii) the continued guidance provided by the CSSF to the supervised entities, and (iv) the strengthening of the cooperation between the CSSF and these professional associations to bring further clarity to issues identified by the market participants.

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10. Areas for further improvement

Despite the overall decrease in terms of Residual Risk of the Collective Investment Sector, notably through an increase of the quality of mitigation measures, the CSSF wishes to draw the attention of the market participants to the fact that there are still areas which require further improvement.

In addition, the CSSF wishes to remind the importance of the data provided in the annual AML survey which constitute key sources of information to prepare this SSRA. While the data quality has increased, the CSSF still identifies cases where erroneous data has a significant impact on the scoring of the entity and the related risk measures implemented by the entity.

10.1 CSSF recommendations to the private sector

Recommendations	*How IFMs may show compliance (examples)*
For cross-border intermediaries consider information such as the type/ geographical origin of the underlying investors as part of the risk assessment criteria.	Consider adding a relevant clause to obtain typological information on underlying investors.
Improve the AML/CFT due diligence performed on assets, especially for alternative non-UCITS-like strategies.	For Funds of Funds, take into consideration the ML/TF risk of the underlying assets of the target fund (for instance by considering the work performed by the target fund on its own assets) on a risk-based approach.
When outsourcing the screening of Targeted Financial Sanctions to non-European entities, ensure that the Luxembourg applicable, notably European, Sanction lists are screened.	Add a detailed clause in the outsourcing agreement requiring that the Luxembourg applicable Sanction lists are screened; if not, this task must be performed by the Luxembourg professional.

Review the IT components of AML/CFT systems.	Ensure that proper access rights are in place. Review the matching thresholds or transaction monitoring rules in case too few or too many alerts are being generated.
Improve the quality of RC reports.	Consider the requirements laid out in Circular CSSF 18/698 as a minimum requirement. In case the entity is not within scope of this circular, consider the requirements laid down as best practice. Use the guidelines given by the CSSF during conferences or in FAQs or leverage guidance prepared by Luxembourg professional associations.

10.2 CSSF initiatives

Similar to the engagements taken in the SSRA 2020, the CSSF will continue to:

- Promote the understanding of AML/CFT obligations and ML/TF risks. The CSSF actively supports the efforts made by the fund industry to improve their understanding of AML/CFT obligations and ML/TF risks. To achieve this, the CSSF will continue several existing initiatives, including regular meetings of the AML/CFT Expert Working Group with the private sector, the organisation of additional AML/CFT conferences with the private sector and the issuance of additional guidance, where relevant.

- Further enhance the effectiveness of AML/CFT supervision within the Collective Investment Sector. For instance, the CSSF has implemented as of 31.12.2021 a new AML/CFT external report as per the newly issued Circular CSSF 21/788. The analysis of this report, the methodology of which has been designed by the CSSF, will further improve the identification of shortcomings at a more micro level and will help to identify areas where further guidance may be needed.

In addition, the CSSF will continue to play an active role at an international level, notably through the participation and lead of several AML/CFT Colleges as set out by the EBA guidelines of December 2019.

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