

**LAPSE OF
TIME**

SM/22/182
Correction 1

July 26, 2022

To: Members of the Executive Board
From: The Acting Secretary
Subject: **Republic of Lithuania—Selected Issues**

Board Action: The attached corrections to SM/22/182 (7/12/22) have been provided by the staff:

Evident Ambiguity **Pages 27 (para. 29, line 3) and 29 (para. 33, lines 1, 2, and 5)**

Factual Errors Not Affecting the Presentation of Staff's Analysis or Views **Pages 22, 27 (para. 29, line 2), 29 (para. 33, line 4)**

Questions: Mr. Gracia, EUR (ext. 36085)
Mr. Cevik, EUR (ext. 36695)
Mr. Markevych, LEG (ext. 37018)

management function in an FI. The assessors also noted that the BoL has some strong elements of risk-based supervision and is moving towards both a comprehensive risk-based approach and an amount of supervision commensurate with risks. Although the level of sanctions applied by the BoL has generally been commensurate with its supervisory findings, its sanctioning regime was not fully effective and dissuasive at that time. The assessment also concluded that a shortage of staff resources has had a negative impact on the overall effectiveness of the risk-based approach to supervision.

15. The BoL has made substantial progress in strengthening its AML/CFT supervision since the 2018 MONEYVAL assessment, conducting detailed off-site monitoring of ML/TF risks. In December 2020, the BoL has adopted the AML/CFT Supervision Policy and the ML/TF Risk Scoring Methodology—important steps in strengthening BoL’s risk-based approach to AML/CFT supervision. The policy envisages that the frequency and scope of inspections should be based on risk and proportionality and that allocation of resources should be based on the risks of specific FI or a sector. The new methodology for ML/TF risk assessment envisages FI-specific ML/TF risk scoring, which is based on data collection and risk evaluation. Data is gathered on various risk indicators related to the FI’s customer base, products/services offered, and countries of operations to generate the inherent ML/TF risk of an FI. In order to calculate the residual risk, the inherent risk ratings are combined with a score representing the strength of the FI’s ML/TF systems and controls, which reflects the supervisory judgement based on the qualitative assessment of the existing controls, mitigating measures, and other factors (e.g., adverse media revelations or negative information from another authority). Based on the progress in developing risk-based approach to supervision, MONEYVAL re-rated Lithuania’s level of compliance with the FATF recommendation on regulation and supervision of FIs from “partially compliant” to “largely compliant.”

16. The BoL should develop its understanding of higher-risk countries taking into account Lithuania-specific ML/TF risk factors. The BoL collects detailed statistics on the FIs’ cross-border activities, with disaggregation on the individual country level, but for risk scoring of the FIs’ country risk relies exclusively on the jurisdictions listed by the FATF, the European Commission and the Ministry of Finance of Lithuania.²³ Leveraging its offsite monitoring and ~~semi-annual~~ quarterly data collection from EMI/PI, the BoL is able to react dynamically to external events and analyze ML/TF risks facing supervised entities emanating from business relationships with certain countries. Considering the criticality of cross-border activity, the BoL should develop its understanding of higher ML/TF risk countries considering the Lithuania-specific foreign ML/TF threats, potentially based on the enhanced NRA methodology as outlined above. The blanket treatment of all transactions from and to the EU, which accounts for majority of the transactions in Lithuania, as lower ML/TF risk can be nuanced to account for differences in the risk profiles of the EU countries. The BoL AML/CFT supervision may usefully distinguish between higher risk countries that provide non-transparent corporate vehicles (part of customer risk factor) and countries posing higher risk of laundering the foreign proceeds of economic crimes in or via Lithuania, or of facilitating the laundering of proceeds of crime that originate in Lithuania (part of geographical risk).

²³ This sentence refers to the jurisdictions under the [FATF increased monitoring](#), EU high-risk third countries, and the Ministry of Finance targeted territories.

- Strengthen BoL's understanding of ML/TF higher-risk countries and incorporate it in the institutional risk scoring matrixes, inspection activities and other elements of risk-based supervision
- Conduct thematic review of FIs' exposures to the identified higher-risk countries
- Integrate delivery channels and value and volume of conducted cross-border payments directly as a separate risk factor in risk scoring of EMIs and PIs
- Expand customer risk grouping to focus on the specific categories of clients that pose high ML/TF risk, such as VASPs
- Strengthen the coverage of all supervised FIs with data collection and risk scoring

E. Regulation and AML/CFT Supervision of VASPs

28. A high number of VASPs has registered over the last year in Lithuania, with VASP sector becoming a source of emerging ML/TF risk. The 2019 NRA determined the level of ML/TF risk, threat, and vulnerability of VASPs being the highest among all assessed sectors and products. Based on the NRA findings, Lithuania amended its AML/CFT law in December 2019, introducing requirements, including AML/CFT-related such as customer due diligence, transaction monitoring, for VA/VASPs, and re-allocated Lithuanian FIU resources to VASP supervision. Lithuania experienced strong influx of VASPs registering in Lithuania since October 2021, bringing the current number to high 407 registered VASPs. Reportedly, the entry of some VASPs to Lithuania was prompted by strengthening legislative and regulatory requirement for VASPs in other EU countries. The Lithuanian FIU estimates that only 25 VASPs are fully operational at the moment, noting that at least 6 months are required to fully launch VASP operations. As a result, Lithuanian VASP sector's activity may increase substantially in the short-term, with corresponding increase in associated ML/TF risks.

29. Current registration regime for VASPs imposes light requirements for VASP sector entry, however, Parliament while the authorities are developing has adopted the amendments to strengthen AML/CFT legislation for VASPs. Under the former regime, VASPs could start operating in Lithuania after registering with the Register of Legal Entities administered by the State Enterprise Centre of Registers, providing contact information of their money laundering reporting officer and attestation of understanding and compliance with AML/CFT requirements for VASPs. Considering the national understanding that VASP activity poses the highest ML/TF risk, Lithuania should strengthen VASP market entry controls. Particularly, a stronger emphasis on fitness and propriety tests appears warranted as currently only a person convicted of economic crimes cannot own or control a VASP. The Lithuanian FIU (or other VASP supervisor in the future) should examine the integrity, reputation and competence of owners and senior management of registering VASPs, including to prevent criminals from holding significant or controlling interest or a management function in a VASP. This recommendation applies to both current registration regime that allows VASPs to start operations when the required documents are submitted and to a licensing regime that the authorities may wish to consider for the largest or riskiest types of VASPs. Lithuania should also assess ML/TF risks of VASPs that are being registered, including from their client base, products and services provided and geography of operations, as well as quality of their AML/CFT systems and controls. Recommended strengthening of the VASPs sector entry controls appears to require changes to the AML/CFT law to support expanded function

ML/TF risks of VASP activity, its customer base, type of VA used and quality of AML/CFT controls. Considering current light registration regime under which a significant number of new VASPs have entered Lithuania and improving understanding of ML/TF risks from individual VASPs, the Lithuanian FIU should be granted powers to cancel registration of VASPs with fundamental deficiencies in AML/CFT controls or that face unacceptably high level of ML/TF risk.

Recommendations:

- Strengthen VASPs market entry controls with a strong emphasis on fitness and propriety tests
- Develop institutional risk assessment methodology and tools for offsite monitoring with a focus on ML/TF risks of VASP activity and VA type based on the sectoral risk assessment results
- Grant the supervisor powers to revoke VASP registration and bring the AML/CFT framework in full compliance with the FATF Standards as related to VA and VASPs.

F. AML/CFT Controls for CENTROLINK

32. CENTROLINK is a retail payment system operated by the BoL, which represents another emerging area of ML/TF risk. The risk profiles of CENTROLINK customers and cross-border reach of its payments pose elevated ML/TF risk that is not adequately mitigated by BoL's AML/CFT systems and controls.

33. BoL opens accounts and provides ~~direct~~ access to Euro payment infrastructures to various EEA³²-licensed payment service providers to conduct SEPA³³ ~~national and cross-border~~ payments. The access is granted via CENTROLINK—a retail payment system launched in 2015 and operated by the BoL, which provides access to SEPA ~~and TARGET2~~ to various payment service providers (PSPs), banks, credit unions, EMI and PI licensed in the EEA. After connecting to CENTROLINK, they ~~may~~ receive access to full range of SEPA services: instant payments, credit transfers, and direct debit services. The BoL also facilitates reception of SWIFT Business Identifier Code and IBAN account numbers for the PSPs and its clients.

34. CENTROLINK played an important role in establishment of the Lithuanian fintech hub, providing easier access for EMI and PI to SEPA payments. Access to SEPA payments via CENTROLINK was promoted as one of the advantages to conduct business in Lithuania and is a component of the fintech hub's Newcomer Programme facilitating entry of fintechs to Lithuania. CENTROLINK is part of the BoL strategic direction towards fostering innovation in the financial sector and development of a FinTech-conducive regulatory and supervisory ecosystem. One of the CENTROLINK's objectives is also to promote competition in the financial sector through pricing of access and transaction fees that is lower/competitive with the same services provided by the

³² European Economic Area

³³ Single Euro Payments Area