



Anti-money laundering and counter-terrorist financing measures

Hungary

1st Enhanced Follow-up Report & Technical Compliance Re-Rating

December 2017

Follow-up report



The Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism - MONEYVAL is a permanent monitoring body of the Council of Europe entrusted with the task of assessing compliance with the principal international standards to counter money laundering and the financing of terrorism and the effectiveness of their implementation, as well as with the task of making recommendations to national authorities in respect of necessary improvements to their systems. Through a dynamic process of mutual evaluations, peer review and regular follow-up of its reports, MONEYVAL aims to improve the capacities of national authorities to fight money laundering and the financing of terrorism more effectively.

The 1st Enhanced Follow-up Report and Compliance Re-Rating on Hungary was adopted by the MONEYVAL Committee at its 55th Plenary Session (Strasbourg, 5 – 7 December 2017).

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Hungary: 1st Enhanced Follow-up Report and Technical Compliance Re-Rating

I. INTRODUCTION

1. The mutual evaluation report (MER) of Hungary was adopted in September 2016. This follow-up report analyses the progress of Hungary in addressing the technical compliance deficiencies identified in its MER. Re-ratings are given where sufficient progress has been made. This report also analyses progress made in implementing new requirements relating to FATF Recommendations which have changed since the MER was adopted: Recommendations 5 and 8. Overall, the expectation is that countries will have addressed most if not all technical compliance deficiencies by the end of the third year from the adoption of their MER. This report does not address what progress Hungary has made to improve its effectiveness. Progress on improving effectiveness will be analysed as part of a later follow-up assessment and, if found to be sufficient, may result in re-ratings of Immediate Outcomes at that time.

II. FINDINGS OF THE MUTUAL EVALUATION REPORT

2. The MER rated¹ Hungary as follows:

IO 1	IO 2	IO 3	IO 4	IO 5	IO 6	IO 7	IO 8	IO 9	IO 10	IO 11
LE	SE	ME	ME	LE	SE	LE	LE	ME	ME	ME

R 1	R 2	R 3	R 4	R 5	R 6	R 7	R 8	R 9	R 10
PC	PC	LC	C	PC	PC	PC	PC	C	PC
R 11	R 12	R 13	R 14	R 15	R 16	R 17	R 18	R 19	R 20
LC	PC	PC	LC	PC	PC	LC	PC	PC	C
R 21	R 22	R 23	R 24	R 25	R 26	R 27	R 28	R 29	R 30
LC	PC	PC	PC	PC	LC	LC	PC	C	C
R 31	R 32	R 33	R 34	R 35	R 36	R 37	R 38	R 39	R 40
LC	PC	PC	PC	PC	LC	LC	LC	LC	LC

3. Given these results, Hungary was placed in enhanced follow-up. The assessment of Hungary's request for technical compliance re-ratings and the preparation of this report were undertaken by the following Rapporteur teams (together with the MONEYVAL Secretariat):

- Armenia
- The United Kingdom Crown Dependency of Jersey

¹ There are four possible levels of technical compliance: compliant (C), largely compliant (LC), partially compliant (PC), and non-compliant (NC).

4. Section III of this report summarises the progress made to improve technical compliance. Section IV sets out the conclusion and a table showing which Recommendations have been re-rated.

III. OVERVIEW OF PROGRESS TO IMPROVE TECHNICAL COMPLIANCE

1. This section summarises the progress made by Hungary to improve its technical compliance by:

- a) Addressing the technical compliance deficiencies identified in the MER, and
- b) Implementing new requirements where the FATF Recommendations have changed since the MER was adopted (R.5 and R.8).

3.1. Progress to address technical compliance deficiencies identified in the MER

6. Hungary has made progress to address the technical compliance deficiencies identified in the MER. As a result of this progress, Hungary has been re-rated on Recommendations 1, 2, 6, 7, 10, 15, 16, 19, 22, 23, 25, 34 and 35.

Recommendation 1 (Originally rated PC)

7. In its 5th MER, Hungary was rated PC with R.1. The main factors underlying the technical rating related to the following findings of the evaluators: the NRA process did not demonstrate the characteristics of a comprehensive assessment, based on a robust methodology; the Hungarian authorities had not explored domestic and foreign ML/FT threats and ML/FT vulnerabilities related to certain products, customers and FIs/DNFBPs; following the adoption of the NRA, no coordinated measures had been adopted (a national AML/CFT strategy and an Action Plan) in order to address the risks identified; service providers were neither required to undertake their own risk assessment nor to incorporate the findings of the NRA into already existing assessments; FIs and DNFBPs were neither obliged to take enhanced measures to manage and mitigate the ML/FT risks identified at national level (when appropriate) nor to address the risks identified by their own risk assessments; conditions for the exemption from the application of the FATF Standards and for application of simplified and enhanced CDD requirements were not based on the results of the NRA.

8. A fresh and more comprehensive NRA process was conducted between November 2016 and August 2017, which has resulted in a 274-page detailed analytical assessment, based on a much more robust and clearly thought-out methodology than in 2015. The 2017 methodology recognises the different concepts of “threats”, “vulnerabilities”, “consequences” and “risks” within this process. It has followed more closely the methodology of the recent supranational risk assessment by the European Commission. As such, ML/FT risks are assessed bearing in mind each of these concepts, in respect of 43 separate activities, sectors, criminal activities and systemic problems which were considered to pose ML/TF risks. The working groups were broadly constituted (including security services on the law enforcement side and a wider variety of external reports and information drawn from MLA requests was exploited. The private sector has been involved both the risk identification and the risk assessment stage of the NRA, though not in the phase when risk-mitigating measures were determined.

9. A new AML/CFT Act came into force on 26 June 2017. Section 3 now defines national risk assessment as “the national-level assessment suitable for identifying, assessing, interpreting and continually reviewing the risks of ML and FT, as well as for establishing the national risk management procedures.”

10. Section 27 of the 2017 AML/CFT Act now creates an enforceable obligation on “service providers” to prepare internal risk assessments - proportionate to the nature and size of the service provider. Breaches of this obligation can be subject to dissuasive sanctions. The service provider is explicitly required to “identify and evaluate” the risk factors related to the nature and amount of the business relationships relationship or transaction order, the customer, the product, the service, the geographic area and the equipment used (delivery channels) in order to determine and evaluate the risks. The service provider is also explicitly obliged to record the risk assessment in writing, update it, to make it available to the competent authorities in the course of authorisation or supervision, to take into consideration the outcome of the NRA in preparing internal risk assessments and in order to mitigate and manage the risks. The internal risk assessments should form the basis of the internal rules of the service provider – which, under Section 65 of the 2017 AML Act, are subject to approval of the supervisor.

11. Section 28 of the Act also requires the supervisory body to prepare a supervisory risk assessment based on circumstances that are typical to the sector and the outcome of the NRA, and to monitor the changes in risk in the sector and update its own assessments accordingly.

12. Section 27 (4) of the Act allows a service provider not to prepare its own internal risk assessment where the relevant supervisory body provides an option for this in the guide it provides to service providers, which is based on its own sectoral risk assessment.

13. Sections 27 and 28 of the Act together with the *decree on the compulsory elements of the internal rules (21/2017 MNE Decree)* address most of the major deficiencies identified under R 1.

14. Hungary has developed an action plan to implement a risk based approach specifically tailored on the risks identified in the course of the recent NRA assessment. A government resolution mapping out the steps needed to be taken to implement the action plan is currently under inter-ministerial discussion. In addition, the Government issued Resolution 1688/2017 (IX.22). This contains a comprehensive 92-point 2-year action plan on the implementation of the 2016 MONEYVAL recommendations, including the provision of sector specific risk assessments by the MNB and other risk based supervisory procedures. Many of the necessary tasks identified by MONEYVAL for the improvement of ML prosecutorial results, which are endorsed and amplified in the recent NRA, are included in this action plan. Thus there is a process on which to build in developing the strategy addressing other risks identified by the NRA and for consideration of issues of resourcing.

15. **Most of the deficiencies identified in the MER have been addressed and only minor deficiencies remain. On that basis R.1 is re-rated to LC.**

Recommendation 2 (Originally rated PC)

16. The deficiencies were as follows: no initiatives have been adopted to transpose the risks and the vulnerabilities identified into (coordinated) national AML/CFT policies and strategies; no initiatives have been adopted to transfer the findings of the NRA into the activities of the competent authorities; the coordination and the cooperation among competent authorities for the development and implementation of AML/CFT policies and activities is marginal; and no coordination and cooperation mechanisms are in place for PF.

17. A coordinated Action Plan for the implementation of the AML recommendations formulated in Hungary's MER was adopted by Government in Resolution no. 1688/2017 (IX.22). Although the Action Plan will contribute to strengthening national cooperation and coordination, it does not appear to have been designed to mitigate ML/FT risks identified in the NRA. A Government Resolution specifically aimed at mitigating the NRA risks has been agreed upon and is currently under inter-ministerial discussion (see para. 14).

18. Various actions were undertaken to enhance cooperation and coordination on policymaking and operational levels: the role of the AML Sub-Committee has been reinforced (its mandate covers NRA and PF issues); Government Resolution of 1333/2017. (VI. 9.) establishes an action plan for updating the NRA, including coordinated actions by the relevant institutions; the development and implementation of the Action Plan on MONEYVAL recommendations have contributed to closer cooperation between relevant authorities at policy and operational level; there have been several high-level meetings on the prioritisation of the implementation of MONEYVAL recommendations; and Section 70 of the new AML/CFT Act emphasizes interagency coordination for the purposes of supervision.

19. Progress has also been achieved in reinforcing cooperation and coordination in relation to PF-issues. As noted, the Charter of the AML Sub-Committee now covers PF matters. Experts from the AML Sub-Committee and the informal Inter-ministerial Committee on Non-Proliferation have become permanent delegates in the other institution's meetings.

20. **Hungary has made progress in relation to C.2.1, C.2.3 and C.2.4. R.2 is re-rated to LC.**

Recommendation 6 (Originally rated PC)

21. In its 5th MER, Hungary was rated PC with R.6. The deficiencies related to: targeted financial sanctions of UNSCRs 1988 and 1989 were not applied without delay; there were no mechanisms for the application of freezing obligations under UNSCR 1373 in relation to EU internals; the mechanisms for the implementation of UNSCRs 1267, 1373 and 1988 did not cover all requirements.

22. According to the Action Plan (IV/F/1.) Hungary would develop a formal national listing mechanism in relation to uniform and comprehensive implementation of UNSCRs on TFS related to FT and PF. As indicated by the authorities, this mechanism would address deficiencies related to the identification of the competent authority responsible for proposing and designation of persons and

entities; identification of targets; application of evidentiary standards; information exchange on designations; de-listing and other matters. It seems that, after this mechanism is in force, the deficiency related to the application of the TFS measures to EU internals might be also resolved. Although the task was planned to be accomplished on 1 November 2017, the authorities informed that it is still on-going for the time being. Hence deficiencies identified in the MER under Criteria 6.1, 6.2 have not yet been remedied.

23. As an EU member state, Hungary applies targeted financial sanctions through the EU Council Regulations. It is noted that delays between the date of a designation by the UN and the date of its transposition into European law has recently been significantly shortened to 3-4 days.

24. More importantly, Hungary has implemented complementary domestic measures. A new Act on the Implementation of Financial and Asset-Related Restrictive Measures Ordered by the European Union and the UN Security Council (FRM Act LII) was adopted in 2017. The act introduces a requirement for service providers (including all FIs and DNFBPs) and public registries (real estate register, company register, vehicle register, register of vessels and navigation facilities, aircraft register, official register of cultural heritage) to monitor on an on-going basis new designations under the EU Regulations and UNSCRs on TFS. Where the service providers or the public registries identify data, facts or circumstances which suggest that they are in possession of funds or other assets related to a designated person, they are required to immediately submit a report to the HFIU and refrain from performing any transactions involving those funds or assets for 4 business days (Chapter 3 of the FRM Act LII). Within this timeframe, the HFIU is required to determine whether the funds or other assets are subject to freezing under the relevant EU Regulations or the UNSCRs. Where this is the case, an application is made to the court, which will order an attachment on the basis of an administrative procedure. Although the FRM Act does not extend its requirements to all natural and legal persons, it covers all reporting entities and public registries. The FRM Act LII has clarified the scope of the decisions to be made by the HFIU and the Regional Court when analysing and deciding upon application of the respective measures. These are now limited to the determination if the person or the assets fall under the TFS.

25. The Judicial Enforcement Act sets forth that the freezing order shall be terminated if the conditions under the Community Law no longer apply. However, the law has not been provided for the present analysis. There is no further information provided on measures taken to address other deficiencies identified with respect to implementation of the FATF recommendation as provided under the Criteria 6.3 and 6.5.

26. **Hungary has addressed the majority of issues identified in the MER; only some minor deficiencies remain. On that basis, R.6 is re-rated to LC.**

Recommendation 7 (Originally rated PC)

27. In its 5th MER, Hungary was rated PC with R.7. The deficiencies were that: targeted financial sanctions of UNSCRs relating to the prevention, suppression and disruption of proliferation of mass destruction and its financing were not applied without delay; and the mechanisms for the implementation of the relevant UNSCRs did not cover all the requirements.

28. The measures in place to ensure implementation of the EU and UN financial sanctions “without delay” and to ensure the freezing of funds and economic resources are described under the analysis of Recommendation 6.

29. **Hungary has addressed the majority of issues identified in the MER; only some minor deficiencies remain. On that basis, R.7 is re-rated to LC.**

Recommendation 10 (Originally rated PC)

30. In its 5th round MER Hungary was rated PC with regard to R.10. The main technical deficiencies were: the lack of direct prohibition to maintain anonymous accounts or accounts in fictitious names; the limited definition of the beneficial owner; lack of explicit requirement to verify the identity of the beneficial owner using the relevant data from a reliable source in all cases and understand the control structure of the legal entity; lack of requirements to obtain data on relevant persons having a senior management position within the legal person or arrangement and principal place of business (if different); deficiencies in the simplified due diligence regime, which includes blanket exemptions without consideration of specific risks; and the lack of a requirement to identify and take reasonable measures to verify the identity of the protector or potential beneficiary if the beneficiaries are not yet determined.

31. The concern that there are no legal provisions expressly prohibiting anonymous accounts or accounts in fictitious names has not been addressed. The amended definition of beneficial owner of legal person covers the natural person who controls a customer (legal person or natural person) through other means; however the deficiency identified in the 5th round MER with regard to beneficial owner of foundations still remains. The amended AML/CFT Act introduces procedures to verify the identity of the beneficial owner. Under the AML/CFT Act it is required to check the data relating to the identity of the beneficial owner based on the instrument (identification documents) presented to it, publicly accessible registries or other registries, from the operator of which the service provider is entitled to request data. Shortcomings related to the explicit requirements to understand the nature of the customer’s business and the control structure of the legal entity appear to be largely addressed as the amended AML/CFT Act requires to record information about the main activity of the legal person and/or organisation without legal personality, to disclose the data on the nature and extent of the ownership interest in the declaration. However, this provision does not require the understanding of the control structure of the legal person or organisations without legal personality (control other than by ownership).

32. Requirements to obtain data on relevant persons having a senior management position within the legal person or arrangement and principal place of business (if different) seem to be not included in the amended AML/CFT legislation.

33. The amended AML/CFT Act introduces a definition of beneficial owner which extends to settlor and the natural person who controls the managed assets (this would cover the protector). Section 13(7) of the amended AML/CFT Act requires trusts to record all information relating to any beneficiary not known at the time of the conclusion of the contract required for identification and

verification of the identity. In this case, the verification of the identity shall take place at the time of the payment, with or prior to the beneficiary enforcing its rights originating from the contract.

34. No information has been provided on the requirement for information about the beneficiary of a life policy to be taken into account when considering whether to apply enhanced CDD measures.

35. Enhanced due diligence should be conducted in the situations listed in the AML/CFT Law and or cases set out in the internal rules of the service providers.

36. Under the amended AML/CFT Act, financial institutions can apply simplified due diligence in the following circumstances: 1) when issuing e-money; and 2) if it is provided in the internal rules of the financial institution. In case of issuing e-money, the financial institution is required to monitor the business relationship and may record identification data and request necessary documents for the verification of the identity. In cases where simplified due diligence is conducted based on the internal rules of the financial institution, identification data should be recorded. However, verification is optional and may be avoided. There seems to be no explicit prohibition on the application of simplified measures where there is a high risk or suspicion of ML/FT.

37. Although there is no explicit requirement for the financial institutions to adopt risk management procedures concerning the conditions under which a customer may utilise the business relationship prior to verification, service providers may perform under the AML/CFT Act the verification of the identity of the customer and beneficial owner when establishing the business relationship, if this is necessary in order to avoid interruption of its regular operation and when the probability of money laundering and terrorist financing is low. In this case, the verification shall be completed before the first transaction is executed.

38. The financial institutions seem to be not permitted not to pursue the CDD process - and instead file an STR - in case they form a suspicion of ML or FT and the CDD process will tip-off the customer.

39. **Major deficiencies identified in the MER have been addressed; only some minor deficiencies remain. On that basis, R.10 is re-rated to LC.**

Recommendation 12 (Originally rated PC)

40. In its 5th round MER, Hungary was rated PC with R.12. The identified deficiencies related to the relevant legislation neither setting out preventive measures for domestic PEPs or persons with a prominent function by an international organisation, nor requirements related to “risk management systems”, “sources of wealth” and “enhanced on-going monitoring”. The definition of PEP limits the function to a period of one year preceding the application of CDD. Moreover, preventive measures in case of PEPs apply when the customer is identified as “(non-resident) PEP” and not when the beneficial owner is considered such.

41. The new AML/CFT Act requires enhanced CDD measures also in relation to national PEPs, as well as the heads of international organisations, their deputies and members of the managing bodies of such organisations. Such amendments also introduce new requirements to determine whether a customer or beneficial owner is a PEP. Before establishing business relationships with a PEP, senior management approval is required. The declaration by the customer that he/she or the beneficial owner is a PEP includes information to establish the source/origin of funds, but not the source of wealth (R.12.1(c)).

42. The provisions of the new AML/CFT Act shall also be applied in relation to life insurance policies (R.12.4).

43. Section 4 (1) AML/CFT Act continues to limit the definition of PEP to an individual holding such a function in the year preceding the application of CDD.

44. Hungary has addressed a number of deficiencies identified in the MER. However, moderate deficiencies remain. On that basis, R.12 remains PC.

Recommendation 13 (Originally rated PC)

45. In its 5th round MER Hungary was rated PC with R.13. The general provisions with respect to correspondent banking were considered substantially in line with the standards, but they were not applied with respect to respondent institutions within the EU.

46. The new amendments to the AML/CFT Act set out requirements in line with R.13. In relation to correspondent relationships with a service provider established in a Member State of the EU, financial institutions are required to apply these requirements on a risk-sensitive basis, where they determine that the correspondent relationship poses a higher risk.

47. While Hungary has introduced requirements which extend to respondent institutions within the EU, these relationships are only subject to enhanced CDD if determined by the service provider to pose a higher ML/FT risk. On that basis, R.13 remains PC.

Recommendation 15 (Originally rated PC)

48. In its 5th round MER Hungary was rated PC with R.15. The main technical deficiencies were: the lack of requirement for financial institutions to identify and assess the ML/FT risks that may arise in relation to the development and new business practices; the use of new or developing technologies while there is a lack of enforceable legal provisions requiring financial institutions to undertake the risk assessment prior to the launch or use of such products, practices and technologies and to take appropriate measures to manage and mitigate the risks.

49. Financial institutions are required to conduct an internal risk assessment – proportionate to the nature and size of the service provider – based on the nature and amount of the business relationship or transaction order and the circumstances of the customer, the product, the service and the equipment used. Furthermore, financial institutions are required to maintain internal

compliance procedures, known as the internal rules (Section 65(1) AML/CFT Act), which should include a list of cases giving rise to the application of enhanced CDD and the measures to be applied in relation thereto (Section 1(d) of the Decree on the compulsory elements of the internal rules). The cases and the measures to be applied shall be based on the factors related to higher risk listed in Annex 2 of the Decree (Section 6 of the Decree). Point 2.5 in Annex 2 refers to new products and new business practices, including (but not limited to) the use of new delivery mechanisms or new or developing technologies either for new or previously existing products. Taken together these provisions require financial institutions to consider the risks posed by all such products, practices and technologies before they are launched or used and apply enhanced due diligence measures to mitigate the risks. In addition, pursuant to Section 10(2)(c) of the MNB Decree, the establishment of a business relationship or the execution of a transaction involving such products, practices and technologies requires prior management approval.

50. The deficiencies identified in the MER have been addressed. On that basis, R.15 is re-rated to C.

Recommendation 16 (Originally rated PC)

51. The main deficiencies noted under R.16 pertained to the lack of obligations relating to beneficiary information and the limited requirements for intermediary financial institutions in EU Regulation no. 2006/1781, which affected almost all criteria.

52. EU Regulation no. 2015/847, directly applicable in Hungary since 26 June 2017, now requires that wire transfers should be accompanied by beneficiary information (Art.4-6); that intermediary financial institutions should ensure that originator and beneficiary information that accompanies a wire transfer is retained with it (Art.10); that beneficiary financial institutions should implement measures to detect whether originator or beneficiary information is missing (Art.7.2), verify the accuracy of beneficiary information for transfers above EUR 1,000 (Art.7.3), and maintain this information for five years (Art.16); and extends the scope of the record-keeping obligation to beneficiary information (Art.16).

53. The new Regulation has also broadened the scope of obligations on intermediary institutions (they should implement effective procedures to detect whether originator or beneficiary information is missing under Art.11-2; and establish risk-based procedures for determining whether to execute, reject or suspend a transfer lacking the required originator and beneficiary information and for taking appropriate follow-up action under Art.12-1).

54. EU Regulation no. 2015/847 also created an obligation for beneficiary financial institutions to implement effective risk-based procedures for determining whether to execute, reject or suspend a transfer of funds lacking the required originator and beneficiary information and for taking the appropriate follow-up action (Art.8-1).

55. The new Regulation no longer contains provisions on obligations for intermediary financial institutions in case of certain technical limitations, which makes their obligation to retain both originator and beneficiary absolute in that case (Art.10, 11 and 12). This is further clarified by the

guidelines of the Joint Committee of the three European Supervisory Authorities to prevent the abuse of funds transfers for TF and ML purposes: *“IPSPs should use only payment or messaging systems that permit the onward transfer of all information on the payer or the payee, irrespective of whether or not this information is required by Regulation (EU) 2015/847.5. Where this is not possible, for example because a domestic payment system restricts the data that can be entered into that system, IPSPs should put in place alternative mechanisms to pass on relevant information to the PSP of the payee. Such alternative mechanisms should be used only during a short transition period while domestic systems are being adjusted to comply with Regulation (EU) 2015/847 and these guidelines”.*

56. The new Regulation addresses most deficiencies noted in the MER, especially in relation to C.1-9, and C.11-15. R.16 is re-rated to LC.

Recommendation 18 (Originally rated PC)

57. In its 5th MER, Hungary was rated PC with regard to R.18. The main technical deficiencies were the lack of requirements for: FIs to appoint a compliance officer at a management level; to implement group-wide AML/CFT programmes; and to ensure that FIs’ foreign branches and majority-owned subsidiaries apply at least measures equivalent to the requirements of Hungary.

58. In relation to criterion 18.1, FIs must appoint one or more executive officers specified in their internal rule, which shall be responsible for the fulfilment of AML/CFT Act obligations (AML/CFT Act, Section 63 (5)). However, there are no requirements to have in place screening procedures when hiring employees. In relation to criterion 18.2, FIs are now required to adopt and implement group-wide AML/CFT policies for information-sharing regarding STRs (but not CDD and ML/FT risk management) and the protection of the personal data. However, these group-wide programmes do not include the measures set out in criterion 18.1 (provisions for the appointment of a compliance officer, employee screening, training, and independent auditing). In relation to criterion 18.3, FIs are now required to apply the higher standard where the requirements of Hungary and another country differ and apply measures in accordance with the guidelines developed by the European supervisory bodies and accepted by the European Commission. This criterion is therefore met.

59. All sub-criteria under C.18.1 are now met except for (b). This criterion may be considered to be at a level of ‘mostly met’. C.18.2 is only ‘partly met’ since there are no requirements for group wide programmes which include the measures set out in c.18.1 and no measures implementing c. 18.2(a) and (b). C. 18.3 is met. On that basis, R.18 remains PC.

Recommendation 19 (Originally rated PC)

60. In its 5th round MER, Hungary was rated PC with R.19. The identified deficiencies related to the fact that there was no requirement in the law or other enforceable means to apply enhanced due diligence proportionate to the risks, to business relationships and transactions with natural and legal persons (including financial institutions) from countries for which this is called for by the FATF. Moreover, there were no legal provisions enabling the application of countermeasures when decided so by the State authorities or to transpose a call for such measures by the FATF.

61. Section 16(1)(b) of the new AML/CFT Law requires that the service provider shall perform enhanced CDD measures if the customer is from a high-risk third country with strategic deficiencies. Although this provision does not explicitly state that such enhanced CDD must be proportionate to the risks (R.19.1), such obligation follows from the risk-based approach that service providers are required to apply under the AML/CFT Act. The term “high-risk third country with strategic deficiencies” refers to Commission Delegated EU Regulation 2016/1675 of 14 July 2016 which lists in its annex the FATF-identified high risks and non-cooperative jurisdictions. Decree No.19/2017.(VII.19.)MNB of the Governor of the Central Bank of Hungary obliges service providers to use specific measures when dealing with customers from such high-risk countries. Despite of this, there still does not appear to be an express legal basis to apply countermeasures.

62. Hungary has addressed most deficiencies identified in the MER, while minor deficiencies remain. On that basis, R.19 is re-rated to LC.

Recommendation 22 (Originally rated PC)

63. In its 5th MER, Hungary was rated PC with R.22. The main technical deficiencies were: not all trustees are covered by the AML/CFT framework; no requirements for casinos and card rooms to link the CDD information for a particular customer to the transactions that the customer conducts in the casino; the legal privilege for lawyers and notaries is not only limited to the reporting requirements as recommended by the FATF standards, but it goes beyond inhibiting the application of all the preventive measures, including CDD requirements; the circumstances under which legal professionals are required to carry out CDD measures in case of legal arrangements have not been extended as indicated by R.22.1 letter d), last bullet point, of the FATF Methodology; deficiencies in the legal and regulatory framework related to CDD requirements, PEPs and “new technologies” affect the compliance of DNFBPs on these matters.

64. Under the amended AML/CFT Act all trustees are now covered by the AML/CFT framework.

65. New provisions in the AML/CFT Act entitle service provider operating a casino or card room to record the image of a natural person and to record video footage of the activity thereof. However, it is not clear what the procedures are which are applied by casinos and card rooms to link CDD information for a particular customer with the transactions that the customer conducts in the casino.

66. It seems that the legal privilege for lawyers and notaries does no longer inhibit the application of all the preventive measures, including CDD requirements.

67. For further analysis on the regulatory framework related to CDD, see the relevant analysis above.

68. Most of the deficiencies identified in the MER have been addressed. Minor deficiencies remain. On that basis, R.22 is re-rated to LC.

Recommendation 23 (Originally rated PC)

69. In its 5th MER, Hungary was rated PC with R.23. The main technical deficiencies identified under Recommendations 18, 19 and 21 are also applicable to compliance with Recommendation 23. For further analysis on the regulatory framework related to R.18 and R.19, see the relevant analysis above.

70. **Most of the deficiencies identified in the MER have been addressed, while minor deficiencies remain. On that basis, R.23 is re-rated to LC.**

Recommendation 24 (Originally rated PC)

71. In its 5th MER, Hungary was rated PC with regard to R.24. The deficiencies were the following: there was no specific assessment of the risks associated with different categories of legal persons that can be created under Hungarian law; not all companies were required to notify the Register of changes of data (particularly as regards changes of ownership) and it was not clear if information was updated on a timely basis; there was no specific obligation for companies to cooperate with the competent authorities in determining the beneficial owner; there was no requirement for the companies to obtain and hold up-to-date information on the companies' beneficial ownership; beneficial ownership information was not required to be as accurate as possible; given that there was no prohibition to provide nominee director services, it was important to set up relevant mechanisms to ensure that they were not misused; no information on the monitoring of the quality of assistance the country received from other countries on beneficial ownership or locating beneficial owners residing abroad was provided by the authorities.

72. In order to ensure transparency of BO, Hungary set out certain measures in the Action Plan², considering the establishment of a Central Register of the Beneficial Ownership of Corporate and Other Legal Entities and Trusts (hereinafter Central Register) by January 1, 2019(IV/C/1.). In addition, in order to ensure accuracy and timeliness of basic information on legal persons, and to establish mechanisms to mitigate risks deriving from provision of nominee director services, Hungary planned certain steps to be taken as of the end of 2017 (I/A/1., III/B/1. and III/E/1.).

73. Hungary has conducted an assessment of ML/FT risks associated with different categories of legal persons. These risks were qualified as significant in the updated NRA. However, the risk assessment has not covered all types of the legal persons created in Hungary.

74. Section 9 of the amended AML/CFT Act stipulates that the representative of a customer (legal person or organisation without legal personality) shall – based on the accurate and up-to-date records kept by the customer – make a declaration regarding the beneficial owners. However, this provision does not cover adequately the requirement for the companies to obtain and hold up-to-date information on the companies' beneficial ownership.

² Action Plan on "Implementation of Anti-Money Laundering Recommendations for Hungary, Specified in the MONEYVAL Country Report of the Council of Europe" (hereinafter The Action Plan) was adopted by the Government Decision 1688/2017 (IX. 22.)

75. Since the company registry contains information only on legal ownership of companies, it is the service provider who is considered being the source of the beneficial ownership information for Hungary as stipulated by the AML/CFT Act. In line with Sections 9 and 12 of the amended AML/CFT Act, the service provider requests and checks data on beneficial owner of the customer, and ensures that the collected data is up-to-date. As set out in Section 25 of the amended AML/CFT Act, the service provider shall promptly transmit data on beneficial owner of customer to the Central Register³, which should be accessible for the FIU, LEAs, the Prosecutor's Office, courts and supervisory authorities. However, the definition of the beneficial owner as provided under the AML/CFT Act is not fully in line with the FATF standards (see also the analysis of R.10).

76. The customer shall notify the service provider regarding any changes in the beneficial owner within 5 business days after becoming aware. However, while Section 69 of the amended AML/CFT Act reflects on sanctions to be applied to the service providers for violation of the obligations, there are no measures set out for the customer.

77. In order to monitor the quality of international cooperation (not limited only to basic and beneficial ownership information exchange), the HFIU uses the Egmont Biennial Census Mechanism. There is no other mechanism for any formal assessment of the quality of assistance the Hungarian authorities receive from other countries.

78. Hungary has addressed some of the deficiencies identified in the MER, while other significant deficiencies remain. On that basis, R.24 remains PC.

Recommendation 25 (Originally rated PC)

79. In its 5th MER, Hungary was rated PC with R.25. The deficiencies were that: a) there was no requirement for non-professional trustees to disclose their status to financial institutions and DNFBPs; b) there were no provisions on providing information on the beneficial ownership of trusts and the assets to be managed to financial institutions and DNFBPs.

80. According to Section 1(1(m)) of the amended AML/CFT Act, the distinction between the trust performing trust activities on a commercial scale (professional) and the trust performing trust activities on a non-commercial scale (non-professional) is eliminated. Both types are now subject to AML/CFT requirements.

81. There is no requirement set out in the amended AML/CFT Act for trustees to disclose their status to financial institutions or DNFBPs. However, in case the non-professional trustee concludes a contract (agreement) of trust, this shall be drawn up as a notarial deed or a private document countersigned by an attorney-at-law. Thus the non-professional trustee discloses its status in this particular case⁴.

³ According to the Action Plan measure IV/C/1, the central register of the beneficial ownership of corporate and other legal entities and trusts should be established by 1 January 2019.

⁴ Section 37 of the Amendment to Act XV of 2014 on Trusts and on the Regulation of Trust Activities, adopted on 30 May 2017.

82. Section 3 (38(e)) of the amended AML/CFT Act provides a definition of the beneficial owners of the trust arrangements. Beneficial ownership information does not cover the basic information on other regulated agents of, and service providers to the trust, including investment advisors or managers, accountants, and tax advisors.⁵ According to Section 9 of the amended AML/CFT Act there are obligations set to make a written declaration regarding its beneficial owners for the representative of a customer (legal person or organisation without legal personality).

83. A trust company shall comply with the regulations set out for transparent organisations in the Act on National Assets (Act LXI of 2017 on Amending Certain Acts in order to Increase the Legal Competitiveness of Business Environment).⁶ Its structure of ownership and its beneficial owner defined by the Act on the Prevention and Combating of Money Laundering and Terrorist Financing may be identified.

84. There are no provisions on providing information on the assets to be managed by trustee to financial institutions and DNFbps.

85. Most of the deficiencies identified in the MER have been addressed and only minor deficiencies remain. On that basis, R.25 is re-rated to LC.

Recommendation 28 (Originally rated PC)

86. In its 5th MER, Hungary was rated PC with R.28. The deficiencies were that: there was a lack of legal requirements to avoid the presence of criminals and their associates among DNFbps (and prevent them from holding, being the beneficial owner of or managing a DNFbp); there was an absence of measures and widespread practices among supervisors on risk-basis AML/CFT supervision; legal gaps on the AML/CFT sanctions regime limited its dissuasiveness.

87. Hungary set out certain measures in the Action Plan (IV/B/1. and IV/B/2.) in order to introduce legal requirements on prevention of criminals and their associates from being a legal or beneficial owner of the precious metal dealers and real estate agents. However, as indicated in Criterion 28.4(b), there are no specific provisions which apply in case of law firms, accounting firms or auditing firms, where criminals might hide under the status of shareholders or managers. There are also no provisions insuring that Court of Registry information on criminal records provided by the DNFbps upon registration is further updated.

88. According to Section 28 of the amended AML/CFT Act there are new requirements introduced for all of the supervisory authorities to conduct a ML/FT risk assessment, monitor the risks, and prepare rules of procedure. In addition, relevant measures on the revision and development of risk-based supervision procedures are set out in the Action Plan (II/C/1. - II/C/3.)

⁵ Interpretive Note to FATF Recommendation 25, para. 1.

⁶ Established by: Subsection (2) of Section 2 of Act LXXXIV of 2012; in force from: 30 June 2012

for the NAV⁷, Gambling Supervision Board, the BFKH⁸, MNB⁹, Bar Association, Chamber of Notaries and the Chamber of Auditors.

89. Hungary revised the sanctions to be applied for failure to comply with AML/CFT requirements according to Section 69 of the amended AML/CFT Law. These measures now apply also to entities engaged in auditor activity, attorneys and notaries public (see also the analysis of R.35).

90. **Hungary has addressed some of the deficiencies identified in the MER, while other significant deficiencies remain. On that basis, R.28 remains PC.**

Recommendation 34 (Originally rated PC)

91. R. 34 was rated PC, with identified deficiencies relating to guidance and additional material provided by the competent authorities with regard to FT typologies. There was also insufficient guidance pertaining to understanding and application of a risk-based approach by financial institutions and DNFBPs.

92. Section 65 of the new AML/CFT Act establishes a new framework under which supervisory authorities have been authorised and empowered to establish further mandatory rules for the service providers. Hungary has provided information about a large number of finalised or nearly-finalised guidance, which also includes FT prevention and the application of the risk-based approach. This progress is to be commended and the Hungarian authorities are encouraged to finalise the guidance which is still underway.

93. **On that basis, R.34 can be re-rated as LC.**

Recommendation 35 (originally rated PC)

94. In its 5th MER, Hungary was rated PC with R.35. The main technical deficiencies were: sanctions for auditors, notaries public and lawyers under the sectorial legislation are not proportionate; sanctions are not available for managerial functions of DNFBPs.

95. According to the amendments under the Act on Auditors, these are now subject to sanctions under the AML/CFT Act. Thus the deficiencies with regard to the auditors have been addressed.

96. As for the notaries public and lawyers, the maximum amount of fines has been increased and is 1,128,000 Euros. This deficiency has been adequately addressed.

⁷ National Tax and Customs Administration.

⁸ Government Office of the Capital City Budapest proceeding within its scope of competence as trade authority.

⁹ Bank of Hungary.

97. According to the amended provisions of the Auditor Act there is the possibility to assess the personal responsibility of the executive officers and sanctions can be imposed on persons with managerial functions.

98. In case of accountants, tax consultants and tax advisors the registration/permission of the person or executive officer responsible for compliance to the AML/CFT act may be withdrawn.

99. The Gambling Supervision Board may sanction the operator of a casino or card room, a betting operator, or a distance gambling or online casino game operator, or their executive officer for any violation of the provisions of the AML/CFT Act, according to the Gambling Act.

100. Concerns remain for the time being in relation to the ability to sanction senior managers in the DNFBP categories of lawyers and notaries. However, the deficiency with regard to lawyers is addressed by new legislation entering into force on 1 January 2018, while the deficiency with regard to notaries - who do not exercise their functions in a hierarchy involving senior management - is not relevant.

101. **On that basis, R.35 can be re-rated as LC.**

3.2. Progress on Recommendations which have changed since adoption of the MER

102. Since the adoption of Hungary's MER, Recommendations 5 and 8 have been amended. This section considers Hungary's compliance with the new requirements.

Recommendation 5 (Originally rated PC)

103. In its 5th round MER, Hungary was rated PC with R.5. The identified deficiencies related to an undue merging of the financing of the "specific treaty terrorist activity" (Art. 2.1a FT Convention) with the generic FT offence (Art. 2.1b FT Convention) while requiring a specific purpose for both aspects of the offence; the non-criminalisation of the offences provided in Article 2 (a) and (c) of the "1988 Protocol for the suppression of unlawful acts against the safety of fixed platforms on the continental shelf"; the absence from the FT offence to criminalise the *collection* of funds to finance an individual terrorist or a terrorist organisation; as well as the absence of criminalisation of the financing of the travel of individuals to other States for perpetrating, planning of, or participation in, terrorist acts or for receiving or providing terrorist training.

104. Hungary has adopted amendments to its Criminal Code which are not yet in force at the time of the adoption of the follow-up report in December 2017, but which will do so shortly after in January 2018. These amendments are addressing a number of the above-mentioned deficiencies. A newly-introduced provision (Article 318/A of the Criminal Code) ensures that the financing of "terrorist-like criminal offences" is criminalised without requiring any specific purposive element. However, the list of such offences in paragraph 2 of the new provision does still not cover the offences in Article 2 (a) and (c) of the "1988 Protocol for the suppression of unlawful acts against the safety of fixed platforms on the continental shelf". Moreover, while the provision/collection of funds to individual terrorists and terrorist organisations will be criminalised by the newly-adopted

legislation with regard to the purpose-bound generic FT offence, the financing of the “terrorist-like criminal offences” will be criminalised with regard to the provision/collection of funds to individual terrorists only (i.e. not with regard to terrorist organisations). These now separately-regulated “terrorist-like criminal offences” will be punishable with imprisonment of a maximum of three years (while the purpose-bound generic FT offence provides for imprisonment between two and eight years), which may not be sufficiently dissuasive.

105. The criminalisation of the financing of the travels of foreign terrorist fighters, as required by R.5.2*bis*, is addressed by a newly-introduced Article 316/A of the Criminal Code. The article provides, *inter alia*, for imprisonment between two and eight years for the provision/collection of financial assets for the purpose of a person’s travelling in order to facilitate the commission of a terrorist attack or to join a terrorist group. This formulation is sufficiently broad to also include the providing or receiving of terrorist trainings. For reasons of coherence, the definition of “financial assets” as laid down in Article 318/B of the Criminal Code (“[f]or the purposes of Article 318 and Article 318/A, ‘financial assets’ shall mean ...”) would benefit from a direct reference also to the newly-introduced provision of Article 316/A.

106. **Hungary has addressed a number of concerns under R.5, including the elimination of the purposive element for “terrorist-like criminal offences” and the criminalisation of the financing of the travels of foreign terrorist fighters, as well as a wide criminalisation of the collection of funds for terrorist financing. Some minor deficiencies remain or have been newly-created by the legislative changes. However, this does not preclude the overall conclusion that – once the new legislation enters into force in January 2018 – the level of compliance with R.5 will have been brought to a level of LC. For the time being, a re-rating is prevented by the fact that the law is not yet in force at the time of the adoption of the follow-up report. On that basis, R.5 remains PC.**

Recommendation 8 (Originally rated PC)

107. In its 5th MER, Hungary was rated PC with R.8. The deficiencies were the following: no formal review of the NPO sector was conducted to assess the potential vulnerability of the sector to terrorist activities and reassess this information periodically; no specific outreach to the NPO sector concerning FT issues was conducted; there was not a holistic system for monitoring NGOs, except for the prosecutorial oversight in case of alleged violations of NGOs’ requirements (legality check). After the adoption of MER of Hungary, R.8 and its Interpretive Note were significantly revised.

108. Hungary has recently conducted a risk assessment of the overall NPO sector, and identified the types of the NPOs and specific characteristics of their activities, the nature of vulnerabilities and threats for terrorism financing.

109. In June 2017, the “Law on the Transparency of Organisations Receiving Support from Abroad” entered into force, which requires organisations receiving at least 7.2 million forints (approximately EUR 24,000) from foreign sources to register as organisations “receiving support from abroad” and provides for the possible dissolution of an organisation as a penalty for non-compliance. The law, which refers in its preamble to both transparency and the fight against ML/FT,

was not based on any risks identified in the above-mentioned risk assessment. In a letter in April 2017, MONEYVAL had expressed concern that the then draft law was not the result of the application of a risk-based approach. Once a possible upgrade to LC can be considered, the question of the proportionality within the meaning of R.8 will be assessed.

110. Hungary has taken steps to increase accountability of the NPOs revising financial reporting obligation of NPOs (Gov. Resolution 479/2016). In addition, after the adoption of the NRA, the Ministry for National Economy has initiated discussion of the risk assessment outcomes with the European Centre for Not-for-Profit Law. Hungary plans to examine and detect “how the adequate level of transparency of non-profit organisations can be ensured the best, and which mechanism or authority can best perform the continuous control over the assets managed by the NPOs” (Action Plan III/G/1.).

111. As previously indicated, sanctions for senior officers of NPOs are primarily tax violations-related, and do not appear to be dissuasive or proportionate – given the various types of violations that could be envisaged.

112. Although Hungary has recently conducted the NPO sector risk analysis, it has not identified those organisations that meet the FATF’s definition of NPO. Measures taken after the adoption of the MER do not emanate from the NRA outcomes. There are shortcomings related to the need for further outreach and encouragement of the use of regular financial channels, to the application of targeted risk-based measures, and to sanctions in place for senior officers of NGOs. The level of compliance with this Recommendation should therefore remain PC.

IV. CONCLUSION

113. Overall, Hungary has made very commendable progress during a very short time period in addressing the technical compliance deficiencies identified in its MER and has been re-rated on 13 Recommendations (13 upgrades).

114. As Hungary has addressed the deficiencies in respect of Recommendations R.1, 2, 6, 7, 10, 16, 19, 22, 23, 25, 34 and 35. These Recommendations are now re-rated as LC. R.15 has been re-rated as C.

115. Further steps have been taken to improve compliance with Recommendations 12, 13, 18, 24 and 28, but shortcomings (which are more than just minor ones) remain. Consequently, the ratings for these Recommendations remain PC.

116. For Recommendation 5, Hungary has adopted amendments to its Criminal Code, but these will be in force only in January 2018, i.e. after MONEYVAL’s 55th Plenary in December 2017. Consequently, its rating remains PC for the purposes of this report, with the possibility of a re-rating once the amendments have entered into force. For Recommendation 8, Hungary has taken some initial steps, but more is required to adequately implement that recommendation; consequently, the rating remains PC.

117. Overall, in light of the progress made by Hungary since its MER was adopted, its technical compliance with the FATF Recommendations has been re-rated as follows:

R 1	R 2	R 3	R 4	R 5	R 6	R 7	R 8	R 9	R 10
LC	LC	LC	C	PC	LC	LC	PC	C	LC
R 11	R 12	R 13	R 14	R 15	R 16	R 17	R 18	R 19	R 20
LC	PC	PC	LC	C	LC	LC	PC	LC	C
R 21	R 22	R 23	R 24	R 25	R 26	R 27	R 28	R 29	R 30
LC	LC	LC	PC	LC	LC	LC	PC	C	C
R 31	R 32	R 33	R 34	R 35	R 36	R 37	R 38	R 39	R 40
LC	PC	PC	LC	LC	LC	LC	LC	LC	LC

118. Hungary will remain in enhanced follow-up, and will continue to report back to MONEYVAL on progress to strengthen its implementation of AML/CFT measures.

GLOSSARY OF ACRONYMS

AML	Anti-money laundering
BO	Beneficial ownership
CDD	Customer due diligence
CFT	Countering the financing of terrorism
DNFBP	Designated non-financial business and professions
FI	Financial institutions
FT	Financing of terrorism
HFIU	Hungarian Financial Intelligence Unit
LC	Largely compliant
ML	Money laundering
NGOs	Non-governmental organisations
NPOs	Non-profit organisations
NRA	National risk assessment
PC	Partially compliant
PF	Proliferation financing
R	Recommendation
STR	Suspicious transaction report
TFS	Targeted financial sanctions
UNSCR	United Nations Security Council Resolutions

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December 2017

Anti-money laundering and counter-terrorist financing measures - **Hungary**

1st Enhanced Follow-up Report & Technical Compliance Re-Rating

This report analyses Hungary's progress in addressing the technical compliance deficiencies identified in the FSRB assessment of their measures to combat money laundering and terrorist financing of September 2016.

The report also looks at whether Hungary has implemented new measures to meet the requirements of FATF Recommendations that changed since the 2016 assessment.