International Law Office

April 4 2023

New proposal to strengthen regulations for financial institutions in Sweden

Wigge & Partners | **Banking & Financial Services - Sweden**

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A new proposal to strengthen regulations for financial institutions in Sweden is under way. This article explains the current law and the proposed changes.

Current regulations

Any person intending to conduct specific financial activities in Sweden that a credit institution may conduct within the framework of its license for banking or financing operations may be required to apply for registration as a financial institution with the Swedish Financial Supervision Authority (SFSA). Examples of this are:

- extending or intermediating loans; and
- providing financing in the form of factoring or leasing.

This follows from the Swedish Currency Exchange and Other Financial Activities Act (the CEFA Act). The main purpose of the CEFA Act is to prevent money laundering and terrorism financing. As such, registered financial institutions must:

- carry out risk assessments of their products, services and customers;
- take customer awareness measures;
- monitor ongoing business relationships;
- assess individual transactions; and
- report suspected money laundering.

In addition, the SFSA must check whether the registered financial institutions comply with the anti-money laundering legislation and intervene in the event of violations.

The registration requirement applies if such financial activities are conducted on a professional basis (eg, commercial, independent and durable) and constitutes the core of the person's business. However, banks, insurance companies, securities companies and certain other persons subject to other financial legislation (and, thus, anti-money laundering legislation (AML)) are exempt from the registration requirement.

According to the CEFA Act, the SFSA must approve the application for registration as a financial institution if:

- there are reasons to assume that the applicant's operations will be conducted in compliance with the AML legislation; and
- the requirements on the ownership and management of the applicant are met.

For instance, previous material breaches of obligations in business activities or serious crimes (either by the applicant itself or any owner or officer of the applicant) may disqualify a person from registration.

Any unregistered person conducting financial activities requiring registration must be ordered by the SFSA to apply for registration. If the order is not complied with or the registration is refused, the SFSA must order the person to cease the relevant activities (which may be combined with a fine).

Proposed amendments: key aspects

To further prevent money laundering and terrorism financing in the businesses of financial institutions, the Swedish council of legislation will consider a recent draft proposal regarding certain amendments of the CEFA Act. One of these amendments is that registration may be required, even if the relevant financial activities are not the core business. The rationale is that the current threshold entails demarcation difficulties and that it is in practice usually up to the person intending to carry out the financial activities to decide on whether the business is subject to registration – an arrangement that is not satisfactory. However, should the business require registration, it is only the relevant financial activities that will be subject to the requirements set out in the CEFA Act and AML legislation. Conversely, the requirements do not cover other activities within the business. This means, for instance, that know-your-customer procedure would still not be required in respect of these activities.

When it concerns financing in connection with provision of services that are offered or goods that are produced or sold, the draft proposal states the following. The obligation to register according to the CEFA Act does not apply to, among other things, credit institutions and consumer credit institutions. These are instead subject to a license requirement according to the Swedish Banking and Financing Act and the Certain Consumer Credit Activities Act. Pursuant to these rules, companies that provide financing in connection with the provision of services offered or goods produced or sold by the company are exempt from the license requirement. The fact that such businesses are exempt from the license requirement does, however, not mean that the registration obligation applies to them

according to the CEFA Act. Consequently, a removal of the "core business" requisite for registration pursuant to the CEFA Act does not affect these types of services.

Other proposed amendments impose:

- obligations on financial institutions to report changes in circumstances stated in their registration applications (including business descriptions); and
- an extended appropriateness requirement on the management of financial institutions as owners with qualifying holdings (ie, direct or indirect ownership representing at least 10% of the share capital or votes in the financial institution or otherwise having a material influence over the financial institution's management).

In addition to the current requirements referred to above, this provision also takes general law-abidance, experience and judgment into consideration.

The proposal also includes an express provision that the SFSA should ensure that financial institutions comply with AML legislation.

Additional aspects

The following are important additional aspects regarding the provisions.

Status, effective date and transitional provisions
The draft proposal was prepared after comments from the consulting bodies, including the SFSA. The amendments are proposed to enter into force as soon as possible, which the draft proposal estimates to be on 1 January 2024. As to the transitional provisions, existing businesses that are not covered by the current rules, but become subject to the amended legislation, should be allowed to continue with their operations until 31 March 2024. If an application for registration is submitted to the SFSA before 31 March 2024, the operations should then be allowed to continue, provided that the SFSA will have assessed the application.

SFSA's comments
The SFSA has commented that the proposed amendments may increase the possibilities to conduct an efficient and appropriate supervision of currency traders and other persons conducting financial activities. The SFSA further propose that, to ensure compliance with the new appropriateness requirement, which imposes significantly higher demands on the owners and management of the financial institutions in comparison with the current legislation, financial institutions registered for currency trading should be required to re-register with the SFSA. The SFSA highlights the extensive risks of money laundering deemed within currency trading, and that checking the appropriateness of already registered financial institutions within the scope of the SFSA's supervision would mean great practical difficulties in terms of the supervisory tools and resources available to the SFSA. It would also counteract the competitive advantages that registered financial institutions otherwise could achieve by not submitting to the appropriateness test that new financial institutions must undergo.

Additional comments
In contrast with other legislation in the financial sector, the CEFA Act lacks express provisions on its territorial application. The Swedish Bar Association believe this causes uncertainty as to whom is covered by the registration obligation, especially for foreign persons whose financial activities are aimed at the Swedish market but are exclusively conducted from abroad. As a response to that comment, the draft proposal state that the CEFA Act is not limited to operations conducted by Swedish persons but also covers foreign persons operating the relevant financial activities through branches in Sweden. It further states that cross-border operations to Sweden by a person that is domiciled in another jurisdiction (and does not have a branch in Sweden) are not covered by the CEFA Act. Their operations are instead subject to the rules that apply in the jurisdiction where such person is domiciled. A different order would likely involve practical difficulties – for instance, in supervision or collection of claims regarding penalty fees. Corresponding territorial demarcation applies to the fourth EU directive on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, whose provisions are implemented, among other things, through the CEFA Act.

Comment

The proposed amendments are motivated by a desire to mitigate the risks for money laundering and terrorism financing for financial institutions, especially in respect of currency traders. However, attention should be paid to the fact that, when it comes to the obligation for a business to register as a financial institution, the amendments will not only affect currency traders but also persons conducting other financial activities. If the proposed amendments are implemented, the registration obligation will be extended so that any natural or legal person conducting any of the relevant financial activities will, unless exempted, be obliged to register as a financial institution with the SFSA. This will be irrespective of the size of the business or whether their financial activities are the core or only a part of their business operations. The overall objective is thus to make more businesses subject to the AML legislation.

This draft proposal confirms that the amendments will increase the administrative burden and costs of financial institutions, but that this cost is proportionate in relation to the socio-economic benefits of preventing money laundering and terrorism financing. For instance, the appropriateness requirement may decrease the number of criminals operating the businesses concerned. The effects of not amending the CEFA Act would be that these operations continue to be used for money laundering and financing of terrorism to the same extent as currently.

It is also clear from the draft proposal and the SFSA's comments that amendments of the CEFA Act are necessary and should be made. However, what is not as clear is whether the amendments will be implemented as currently proposed or the actual effects the amendments will have on the parties concerned. This remains to be seen.

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