

Risk-Based Approach and Risk-Based Supervision

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Summary

This week, the Financial Action Task Force (FATF) Learning and Development Forum (LDF) brought together more than 100 dedicated professionals from around the world committed to combating financial crime, with the aim of strengthening implementation of the risk-based approach, and in particular risk-based supervision.

Financial supervisors, financial intelligence units (FIUs), law enforcement agencies (LEAs) and policy makers from the FATF Global Network came together with the Wolfsberg Group members and other major international banks that operate globally in the largest and higher risk financial markets. By working interactively through practical case studies, participants looked to understand the global challenges and solutions in this area. This summary highlights some of the many insights gained.

Key insights

- The FATF's focus on the risk-based approach and the effectiveness of systems to combat financial crime and protect the integrity of financial systems is the right one, but we **need greater focus on effectiveness to reduce the harms caused by money laundering and terrorist financing**. Participants acknowledged that over the past years, the approach has been refined but we now need to pivot more toward ensuring all relevant authorities and the private sector are allocating resources according to a shared view of risks. This will **sharpen the focus on the highest risks to deter criminal activity** more effectively and efficiently, while **at the same time reducing friction on innocent customers**.
- The **FATF plays a critical role** - through its convening power, as the global standard setter and in undertaking holistic country-level evaluations of effectiveness - to support and encourage countries to apply the risk-based approach more effectively through clearer communication of expectations, tackling barriers, sharing best practice and training and capacity building.
- A central theme was that **trust is foundational to effective risk-based supervision**. Continuous communication enables proportionality by building understanding and confidence. There is a need to shift away from a culture of zero-failure, and on the need for public and private sectors to better focus resource towards higher risk and reducing low value activity. Supervisory attention should focus on measures that will have the greatest impact on preventing and detecting crime.



Elisa de Anda Madrazo
FATF President

"Risk based supervision ensures that we're agile and dynamic, just like the risks. It's about changing the core question from 'are the rules being followed?' to 'are the highest risks being addressed?'"



Giles Thomson
FATF Vice-President

"By bringing together people from across the world from different fields, we have been able to better understand and build the trust that is required to make progress."



Emma Molvidson
Wolfsberg Group Co-Chair

"Tech is moving fast, criminals are moving fast and we have no choice but to join forces and focus on the real risks."



Sarah Paquet
Director & CEO, FINTRAC Canada

"Risk-based supervision ensures that we are saving victims faster, and that we are preventing other victims from falling into the nets of criminals."

Challenges and opportunities for enhancing our response to financial crime

- The understanding of a risk-based approach and an effective system can vary depending on the viewpoint of the stakeholder, and in some instances there is a lack of alignment on the needs and priorities across the system. Participants highlighted that an AML/CFT regime is most effective and focused when **relevant government agencies specifically define a set of national priorities** for financial institutions to focus on, and when regulators are supervising in line with national priorities - crucial to **give financial institutions the confidence to allocate resources in line with risks and priorities**. That means shifting resource to high value activity and stopping or doing less low value activity.
- Considering the constantly evolving threat picture, in many jurisdictions the understanding of risks has moved from cyclical risk assessments to a more dynamic and collaborative approach to identifying the risks and partnering with the private sector to address them, including through public-private partnerships (PPPs). This involves **proactively and openly engaging with the private sector as a trusted and critical partner in addressing illicit finance**.
- Participants also highlighted the role of PPPs in sharing operational intelligence to produce higher value reporting to FIUs and LEAs and, therefore, better disruption of criminals - as well as **the potential for PPPs to play a greater role in not just detecting but preventing financial crime**, as they already do in some jurisdictions. To reinforce their efforts, the private sector and supervisors could use the information from PPPs as a proactive risk management tool.
- **Supervisory techniques are evolving and our understanding of what constitutes effective supervision must also adapt**. In line with this, a **focus on 'function over form'** to achieving effectiveness will give supervisors confidence to use new technologies to support and focus their activities and resources - for example, in some countries much of what used to occur in 'onsite' inspections now occurs 'offsite' thanks to enhanced technological capabilities. Embracing new tools and models of supervision can focus the activities of supervisors on the risks present, make better use of various sources of information available and ensure that their activities are sustainable and relevant. **Supervisors also have an important role in enabling and incentivising innovative and more effective approaches by the private sector.**

The road ahead

The LDF will support FATF's development of a roadmap to improve global implementation of the risk-based approach and risk-based supervision. Participants put forward number of proposals including:

- Initiatives to develop **greater alignment on what the risk-based approach means in practice** between key stakeholders including the private (including different sectors), supervisors, FIUs and LEAs keeping in mind regional specificities.
- Developing opportunities for **regular exchanges of experiences and practices** among supervisors, FIUs, LEAs and other stakeholders to refine the implementation of the risk-based approach.
- Ensuring that FATF's evaluation of countries **give credit for innovative and forward-leaning approaches** to attain effectiveness and building a better evidence base on different supervision models and their impact.
- Encourage and **support the use of technology and information sharing mechanisms** to enable public and private authorities to **stay abreast of the evolving risk landscape** and better manage risks.



Stevenson Munro
Wolfsberg Group Co-Chair

"It's all about proportionality, prioritisation, and focusing on effectiveness - all in service of managing the risk to protect communities that we're all collectively trying to serve."



Brendan Thomas
CEO AUSTRAC

"We've heard common challenges like over-reporting, defensive reporting, a lack of collaboration between government agencies, and the need to be clear about what our priorities are."