

FATF



BEST PRACTICES PAPER

MANAGING THE ANTI-MONEY LAUNDERING AND COUNTER-TERRORIST FINANCING POLICY IMPLICATIONS OF VOLUNTARY TAX COMPLIANCE PROGRAMMES

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FINANCIAL ACTION TASK FORCE

The Financial Action Task Force (FATF) is an independent inter-governmental body that develops and promotes policies to protect the global financial system against money laundering, terrorist financing and the financing of proliferation of weapons of mass destruction. The FATF Recommendations are recognised as the global anti-money laundering (AML) and counter-terrorist financing (CFT) standard.

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BEST PRACTICES

MANAGING THE ANTI-MONEY LAUNDERING AND COUNTER-TERRORIST FINANCING POLICY IMPLICATIONS OF VOLUNTARY TAX COMPLIANCE PROGRAMMES

I. INTRODUCTION

1. Voluntary tax compliance (VTC) programme refers to any programme that is designed to facilitate legalisation of the taxpayer's situation vis-à-vis funds or other assets that were previously unreported or incorrectly reported. Countries¹ may introduce VTC programmes for a variety of purposes including: raising tax revenue; increasing tax honesty and compliance; and/or facilitating asset repatriation for the purpose of economic policies, especially when the country is in an economic crisis. Such programmes come in a variety of forms and may involve voluntary disclosure mechanisms, tax amnesty incentives and/or asset repatriation. In many cases, VTC programmes are introduced by a highly political decision reacting to the immediate economic or fiscal situation of the country. In such circumstances, the programme may be introduced on short notice (e.g. in response to a serious financial crisis).

2. The Financial Action Task Force (FATF) recognises the potential for VTC programmes to be abused by criminals for the purpose of moving funds. The level of potential money laundering (ML) and terrorist financing (FT) risk varies greatly, depending on the characteristics of the particular VTC programme being implemented. In general, a programme that is being used solely for the purpose of allowing taxpayers to voluntarily correct tax reporting information would not seem to carry a significant ML/FT risk. However, the ML/FT risk is greater when the programme fully or partially incorporates elements of tax amnesty or asset repatriation.

3. Tax amnesty incentives and asset repatriation may increase the potential ML/FT risks for the following reasons. First, both tax amnesty and asset repatriation incentives encourage taxpayers to bring forward funds or other assets that were previously undeclared. This may result in large volumes of funds or other assets, which were previously held outside of the formal financial system or held in another country, being deposited into financial institutions throughout the duration of the programme. This may result in excessively large volumes of transactions that overwhelm the capacity of financial institutions to apply anti-money laundering (AML) and counter-terrorist financing (CFT) measures effectively, particularly if it is burdensome for financial institutions to distinguish ordinary transactions from those related to the programme. Second, financial institutions may believe that the legitimacy of funds or other assets being deposited under such a programme has been officially endorsed by the authorities. Third, where funds or other assets are being repatriated, information on the funds or other assets and the taxpayer may be held in

¹ All references to *country* or *countries* apply equally to territories or jurisdictions.

different countries, making it more difficult for financial institutions and the authorities to verify the legitimacy of the funds or other assets.

II. STATEMENT OF THE PROBLEM

4. An issue of particular concern which has come to the attention of the FATF is that some VTC programmes, explicitly or in practice, exempt full or partial application of AML/CFT measures. For example, some programmes exempt financial institutions from the requirements to conduct full customer due diligence (CDD) on taxpayers and verify that the funds or other assets being declared or repatriated come from a legitimate source, or may grant the taxpayer immunity from investigation or prosecution for money laundering in relation to declared or repatriated funds or other assets.

5. To highlight the importance of ensuring that VTC programmes do not negatively impact the effectiveness of AML/CFT systems, the FATF has agreed four basic principles which underscore the importance of ensuring that countries address and mitigate the ML/FT risks of VTC programmes, and are able to effectively investigate and prosecute their abuse.

6. This paper sets out international best practices, based on the four basic principles, to assist countries in their implementation of VTC programmes, with a view to ensuring that such programmes do not impede the effective implementation of AML/CFT measures. It is important to note that the extent to which the following best practices are relevant will depend on the particular characteristics of the VTC programme, including whether it involves tax amnesty or asset repatriation.

III. DEFINITIONS

7. For the purpose of this paper, the following definitions apply:

- (a) The term *asset repatriation* refers to bringing (i.e. repatriating) funds or other assets from abroad to the home country.
- (b) The term *tax amnesty* refers to favourable tax treatment such as a full or partial reprieve from any tax, interest and penalties that would otherwise be due in relation to previously unreported (or incorrectly reported) taxable income, funds or other assets.
- (c) The term *voluntary disclosure* refers to the voluntary disclosure to the tax authorities of any previously unreported (or incorrectly reported) taxable income, funds or other assets.
- (d) The term *voluntary tax compliance programme* refers to any programme that is designed to facilitate legalisation of the taxpayer's situation *vis-à-vis* funds or other assets that were previously unreported or incorrectly reported.

IV. EFFECTIVE APPLICATION OF AML/CFT PREVENTATIVE MEASURES

Principle 1: The effective application of AML/CFT preventative measures is a prerequisite for addressing and mitigating the money laundering and terrorist financing risks associated with implementing any type of voluntary tax compliance programme.

8. Overall, the effective application of AML/CFT preventative measures is a prerequisite for mitigating the ML/FT risks associated with implementing any type of VTC programme.

9. This section describes elements, considered to be best practices, which countries may incorporate into a VTC programme to ensure that it does not pose an unreasonable ML/FT risk or seriously undermine the effectiveness of the AML/CFT regime:

- (a) Taxpayers are required to deposit repatriated assets with a financial institution(s) that is subject to AML/CFT measures.
- (b) The application of the programme takes into account the ML/FT risks of funds or other assets repatriated from countries that do not adequately apply the FATF Recommendations.
- (c) The authorities raise awareness among financial institutions on the potential for abuse and the ML/FT risks inherent in the VTC programme.
- (d) The authorities raise awareness among financial institutions that any documents or statements issued by the competent authorities in relation to the VTC programme are not official endorsements that the assets involved are of legitimate origin.

V. PROHIBITION OF EXEMPTING AML/CFT REQUIREMENTS

Principle 2: The FATF Recommendations do not allow for full or partial exemptions from AML/CFT requirements in the context of implementing a voluntary tax compliance programme. Therefore, when implementing a voluntary tax compliance programme, national authorities should ensure that its terms do not allow, in law or in practice, for full or partial exemptions from AML/CFT requirements as set out in the FATF Recommendations. Voluntary tax compliance programmes which do so are in breach of the FATF Recommendations.

10. It is important to note that the FATF Recommendations do not allow for full or partial exemptions from AML/CFT requirements in the context of implementing a VTC programme. Programmes purporting to do so are in breach of the FATF standards.²

11. It is best practice for countries to ensure that any VTC programme being implemented does not explicitly set out full or partial exemptions from AML/CFT requirements, or result in such exemptions in practice. This means ensuring that the VTC programme is consistent with the following AML/CFT requirements, as relevant:

- (a) Financial institutions are required to conduct CDD on taxpayers who are transferring, repatriating or depositing assets under the programme, as appropriate, based on an assessment of the applicable risks.
- (b) Financial institutions are required to identify the beneficial owner of the account into which the assets are being transferred, repatriated or deposited under the programme.
- (c) Financial institutions should, where necessary, take reasonable measures to establish the origin of the assets being transferred, repatriated or deposited, in accordance with applicable CDD requirements.
- (d) Financial institutions are prohibited from accepting deposits under the programme by way of wire transfers that are not accompanied by required originator information and required beneficiary information, as required by Recommendation 16.

² This footnote is intended to clarify the application of the four basic principles since February 2012 when the FATF made tax crimes (related to direct taxes and indirect taxes) predicate offences for money laundering. A VTC programme does not breach Principle 2 if the taxpayer is exempted from prosecution for previously not reporting (or incorrectly reporting) taxable income, funds or other assets, and for money laundering, insofar as it exclusively relates to the proceeds of this incorrect or non-reporting of taxable income, funds or other assets, provided that:

- (i) the funds or other assets are of lawful origin; and
- (ii) there are no exemptions from undertaking AML/CFT requirements (including CDD and reasonable measures, where necessary, to establish the origin of the funds or other assets); and
- (iii) in cases where the taxpayer's funds or other assets originate from other predicate offence(s), the taxpayer is subject to prosecution for these other predicate offence(s) and related money laundering.

- (e) The authorities advise financial institutions that AML/CFT measures are applied to the programme, and financial institutions are not exempted from reporting suspicious transactions to the financial intelligence unit (FIU), particularly in relation to: (i) declared/repatriated funds or other assets that are thought to have resulted exclusively from tax offences which are not punishable under the programme in accordance with the FATF Recommendations 20 and 21, and (ii) taxpayers who are reluctant or uncooperative in disclosing information concerning customer identification or the source of the funds or other assets being repatriated under the programme. Consideration should be given to require the systematic reporting to the FIU of all repatriated funds or other assets or by making such information directly available to the FIU in some other way.
- (f) Taxpayers are not exempt, by law or in practice, from investigation or prosecution for ML/FT in relation to repatriated funds or other assets (see also footnote 2).

VI. DOMESTIC CO-ORDINATION AND CO-OPERATION

Principle 3: When implementing a voluntary tax compliance programme, it should be ensured that all relevant domestic competent authorities be able to co-ordinate and co-operate, and exchange information, as appropriate, with a view to detecting, investigating and prosecuting any ML/FT abuse of the programme.

12. A VTC programme may impact on a number of authorities at the domestic level, including the tax authorities, the FIU, law enforcement, supervisory authorities, prosecutorial authorities and customs authorities. Consequently, it is important to ensure that all relevant domestic authorities are able to co-ordinate and co-operate, as appropriate, with a view to detecting, investigating and prosecuting any ML/FT abuse of the programme. The following best practices will help meet this objective:

- (a) Mechanisms are in place to enable the relevant authorities to co-ordinate, co-operate and share information, as appropriate, in preparation for the programme's implementation, throughout its duration, and after its expiration.
- (b) The tax authorities have the authority to conduct their own investigations into the origin of assets subject to the programme, or refer such investigations to other appropriate authorities who are authorised to conduct such investigations, in accordance with the role of the tax authorities and the terms of the VTC programme.
- (c) Mechanisms are in place which enable information related to the programme (*e.g.* on taxpayers and/or declared/repatriated funds or other assets) to be shared between competent authorities that hold such information and the FIU.
- (d) The authorities involved in the programme are adequately resourced to manage their roles in the programme, in addition to their normal functions.

VII. INTERNATIONAL CO-OPERATION

Principle 4: The widest possible range of mutual legal assistance and exchange of information in ML/FT investigations, prosecutions and related proceedings relating to the abuse of voluntary tax compliance programmes, including asset recovery investigations and proceedings, should be provided.

13. VTC programmes involving asset repatriation, by their nature, impact more than one country. In some circumstances, this may increase the potential ML/FT risks. The following best practices ensure that, where more than one country is impacted by a VTC programme, the authorities can provide the widest possible range of mutual legal assistance and exchange of information to mitigate these risks and ensure that any related ML/FT activity is effectively investigated and prosecuted:

- (a) The authorities of countries from which funds or other assets are likely to be repatriated provide the widest degree of co-operation to the authorities implementing the VTC programme.
- (b) Mechanisms, such as bilateral and multilateral treaties and other international arrangements, are in place to enable the country implementing the VTC programme to proactively share information and co-operate with the authorities of countries from which funds or other assets are being repatriated and other affected countries.
- (c) The repatriation of funds or other assets from countries that do not adequately apply the FATF Recommendations is subject to enhanced due diligence and scrutiny.