Failure to prevent the criminal facilitation of tax evasion

Guidance for the financial services sector on the corporate criminal offences within the Criminal Finances Act 2017

Contents

1. Introduction

The Criminal Finances Act 2017 (the 'Act') creates two new criminal offences committed when a relevant body fails to prevent the criminal facilitation of tax evasion by its associated persons. The rationale for the corporate offences is to make a business, including regulated businesses, such as banks, building societies, insurance companies, solicitors and accountants accountable for failing to prevent the criminal acts of their employees and other associated persons who intentionally facilitate tax evasion whilst providing a service for or on its behalf.

The Act itself is modelled in large part on the Bribery Act 2010, and many elements will be familiar to those involved with those provisions. However, there are also a number of important differences.

In the event of a tax evasion facilitation offence taking place, it is a defence for a relevant body to show that either reasonable prevention procedures were in place to prevent the facilitation by the associated person, or that it was not reasonable to expect such procedures to be in place at the time the facilitation offence was committed. The Act does not prescribe reasonable prevention procedures that must be put in place but it does require the Chancellor to publish 'guidance about procedures that relevant bodies can put in place to prevent persons acting in the capacity of an associated person from committing UK tax evasion facilitation offences or foreign tax evasion facilitation offences'. HMRC's guidance sets out six guiding principles (the 'Principles') and illustrates good practice examples rather than prescriptive standards.

Section 47(7) of the Act also allows the Chancellor to approve guidance prepared and published by another person on the same topic. This guidance has been prepared on that basis.

This guidance was approved by the Chancellor on 8 January 2018. The Chancellor considers that this guidance is consistent with the guidance published by the Chancellor entitled "Tackling tax evasion: Government guidance for the corporate offences of failure to prevent the criminal facilitation of tax evasion" on 30 September 2017. As noted below, the approval of the guidance does not extend to the examples that accompany it, which the Chancellor does not approve.

Examples in this document

Note that some of the examples in this guidance reference specific countries for illustration purposes. Those examples are not intended to indicate that those countries are themselves higher risk for the purposes of reasonable prevention procedures under the Act.

This document contains formal guidance and also examples. Examples are included in this document only to assist with the illustration and interpretation of certain parts of the guidance. The examples are not part of the guidance, but have been discussed with HMRC.

The new offences came into force on 30 September 2017. The prevention procedures that might reasonably be expected to be in place on this date will not be the same as those which might be expected to be put in place over time. For example, changes to a global system might take some time to implement. If a relevant body fails to prevent an associated person from committing a tax evasion facilitation offence the question will be whether that relevant body had in place at that time prevention procedures which were in all the circumstances reasonable – refer to section 8.1.

Reliance on existing controls

Many organisations will already have existing internal policies, processes and controls which either directly or indirectly address risks of tax evasion, tax evasion facilitation, and other financial crimes. A risk assessment might lead to the conclusion that such controls provide sufficient comfort that risks related to criminal facilitation of tax evasion by employees and other associated persons are already appropriately mitigated. Section 7 of this guidance contains further detail which may be of interest to those in regulated industries.

The role of guidance

There is no requirement for financial institutions -to specifically consider this guidance in determining their own approach to either addressing the offences or establishing reasonable prevention procedures.

This guidance is intended principally to guide the financial services sector (and its legal advisors or representatives) in their understanding and interpretation of the Act and to highlight the potential actions that it may be proportionate to take given their individual circumstances and risk profile to avoid committing the new offences created by the Act. It is intended to consider how the offences apply to the financial services sector and comment on various matters of relevance to determining a reasonable compliance approach which could be adopted by some organisations. The guidance is given solely in the context of the Act and does not set out in extensive detail either minimum standards or best practice.

The guidance should not be regarded as law or as a substitute for HMRC's own guidance or as additional HMRC requirements: it should be read in conjunction with the Act and other relevant guidance issued by HMRC. Following the approach suggested in this guidance does not, of itself, mean that procedures will be reasonable, as this can only be decided by a court, though it may be considered a strong indication.

HMRC's guidance for all sectors can be found here (link).

Acknowledgements

This guidance was prepared by the following industry bodies: Association of British Insurers (ABI), Association for Financial Markets in Europe (AFME), Association of Foreign Banks (AFB), Alternative Investment Management Association (AIMA), Building Societies Association (BSA), British Venture Capital Association (BVCA), Investment Association (IA), Personal Investment Management & Financial Advice Association (PIMFA), Tax Incentivised Savings Association (TISA), and UK Finance (formerly the British Bankers' Association (BBA)).

London & International Insurance Brokers' Association (LIIBA) have produced their own guidance on this topic, which is available on their website.

2. Key terms

The offences

- the "Act" refers to Part 3 of the Criminal Finances Act 2017.
- the "corporate offences" – refers to the "failure to prevent the facilitation of tax evasion" offences created by s.45 and s.46 of the Act.
- the "facilitation offence" – refers to the "UK tax evasion facilitation offence" under s.45(5) and the foreign tax evasion facilitation offence under s.46(6), referring to the act of facilitation by the associated person.
- the "underlying offence" – refers to the act of tax evasion itself.
- the "foreign tax corporate offence" - refers to the corporate offence under s.46.
- "tax" is used to refer to all types of taxes, duties and National Insurance Contributions. Note however the comments in section 5.4 in respect of the requirements of dual criminality.

Other terms

- "entity" – refers to a relevant body under s.44(2), meaning a body corporate or partnership (wherever incorporated or formed).
- "financial institution" is used as a general term to mean any entity in scope for the corporate offences which is carrying on a financial services business.
- "reasonable prevention procedures" is used to describe the controls, procedures and processes which a financial institution would use to establish a control framework to avoid committing the offences, as described as 'prevention procedures' in s.45(3) and s.46(4). This includes scenarios where *"it was not reasonable in all the circumstances to expect an entity to have any prevention procedures in place"* as described in the legislation.
- "Chapter" is used to refer to an element of this guidance.
- "s." is used to refer to a section of the legislation.
- "paragraph" is used to refer to a section of HMRC's guidance or any other third party guidance.

3. Interaction with other regimes

There is a significant body of law and practice which already exists in relation to tax evasion by taxpayers, and there is a substantial obligation on financial institutions already created by anti-money laundering and counter-terrorist financing (AML/CTF) requirements.

Although the corporate criminal offence is distinct from existing requirements, recognising and leveraging existing controls allows all financial institutions to deploy resources in a way that complements existing controls rather than running compliance processes in parallel.

Where possible, the approach to developing this guidance has been to map the requirements of the corporate offence as it applies to the financial services sector to complementary legislation and regulation, and the resulting systems and controls which exist in the financial services sector.

In particular, this guidance cross refers to the guidance of the Joint Money Laundering Steering Group (JMLSG) titled 'Prevention of money laundering and combating terrorist financing'.

That guidance is itself due to be updated by JMLSG to reflect the changes in the financial crime area, including developments under the 4th Anti-Money Laundering Directive, Fund Transfer Regulations and other consequential changes as a result of the Criminal Finances Act 2017. This guidance will be updated to reflect any consequential changes.

3.1. JMLSG Guidance (link)

Guidance issued by the JMLSG sets out specific anti-money laundering guidance for financial institutions in terms of meeting their responsibilities under the Proceeds of Crime Act 2002 and the Terrorism Act 2006. This guidance is agreed with HMT.

Businesses that are already subject to the legal and regulatory framework for anti-money laundering and terrorist financing will, by definition, already be under an obligation to identify risks related to handling the proceeds of tax evasion on a risk based approach *("handling the benefit of acquisitive crimes such as theft, fraud and tax evasion"*).

JMLSG guidance notes that:

> *"guidance sets out what is expected of firms and their staff in relation to the prevention of money laundering and terrorist financing, but allows them some discretion as to how they apply the requirements of the UK AML/CTF regime in the particular circumstances of the firm, and its products, services, transactions and customers."*

The procedures which are established by regulated companies will therefore vary. Whilst procedures established for AML/CTF purposes may provide a starting point for, and assist in the development of, prevention procedures, some further work is likely to be needed to ensure that the prevention procedures in place adequately meet the tax evasion facilitation risks identified. Companies will need to consider the extent to which their existing compliance efforts suffice to meet the risks identified by their risk assessment. Ultimately it will be for a court to decide whether prevention procedures are reasonable.

However, the procedures which are established for AML/CTF purposes may assist with creating reasonable prevention procedures in compliance with the new corporate offences.

Employees in financial services will already be aware of their legal obligations to report any suspicion of criminal activity (JMLSG part 1, 7.18-7.19).). Financial institutions filed 95 per cent of all suspicious activity reports (SAR) for money laundering purposes in 2015[1]. SARs are an important part of an organisation's approach to the prevention of financial crime, and in general, the completion of a full and accurate SAR to report suspicions of tax evasion is an indicator that a financial institution understands the risks relating to the laundering of the proceeds of tax evasion within its client base and has at least some of the appropriate controls that could be leveraged to build the control environment. However, it should be noted that SARs predominantly address risks related to the handling of funds after tax evasion rather than identifying acts that will facilitate future evasion.

The extent to which this is true will depend on the effectiveness of reporting mechanisms, the natures of SARs submitted and adequacy of processes to identify when the proceeds of tax evasion are being handled (The SARs regime is under review, and changes to the above may be needed as a result).

Where is JMLSG Guidance relevant?

The below shows the key areas in which the JMLSG Guidance will provide a starting point when considering reasonable prevention procedures.

Principle	**JMLSG Guidance – useful provisions**
Proportionate procedures	**Chapter 4**: Risk-based approach – governance, procedures and internal controls 4.1-4.17
Top-level commitment	**Chapter 1**: Senior management responsibility, **Chapter 4**: Risk-based approach, 4.5-4.17
Risk assessment	**Chapter 4**: Risk-based approach - Identifying and assessing the risks, 4.18-4.41 NB. Although the risk assessment is focusing on associated persons, not customers, the high level principles of identifying risk are equivalent.
Due diligence on associated persons	-
Communication and training	**Chapter 7**: Staff awareness, training and alertness
Monitoring and review	**Chapter 4**: Risk-based approach - monitor and improve the effective operation of the firm's controls, 4.58-4.60

[1] http://www.nationalcrimeagency.gov.uk/publications/677-sars-annual-report-2015/file

3.2. Guidance on Anti-Bribery and Corruption

The Ministry of Justice has produced guidance on the scope of the Bribery Act 2010. The BBA (the predecessor body of UK Finance) has also published detailed guidance for banks to provide more detail on the principles and procedures which may be used to comply with the provisions of the Bribery Act 2010.

3.3. Common Reporting Standard and other tax transparency measures

The Financial Services industry has recently implemented new measures to improve tax transparency, in particular with the implementation of the US Foreign Account Tax Compliance Act (FATCA) programme and the OECD Common Reporting Standard (CRS). Both regimes impose new standards on financial institutions in the identification of customers and reporting of non-residents to tax authorities to support tax compliance efforts.

As with suspicious activity reporting, in general, robust controls over due diligence and reporting of a customer or client under CRS or FATCA may be a strong indicator that a financial institution has some level of control in place to ensure prevent the customer from committing tax evasion using that account. The extent to which these are proportionate on their own will depend on the entity's risk assessment and the due diligence underpinning their controls. These regimes are reliant on information provided by a customer to a financial institution, and therefore the absence of a report does not necessarily mean that appropriate reporting procedures are not in place.

The mere fact that there has been a failure to comply with obligations under CRS would not necessarily mean that an entity did not have in place reasonable prevention procedures. Each case will depend on its own facts and a court will be the final arbiter of whether prevention procedures are reasonable.

4. The offences – an overview

4.1. Overview

Given the regulatory environment in which financial institutions operate, existing procedures should already be in place relating to identifying the risk that customers may engage in tax evasion, such as AML reporting obligations. It should also be noted that many firms may already have procedures in place which look to deal with employee conduct more generally. Those procedures could assist with the assessment and design of the reasonable procedures to prevent the facilitation offence under the Act.

One of the first steps to devising reasonable prevention procedures is to conduct a risk assessment to determine the risks faced by the entity of an associated person criminally facilitating tax evasion. This process of assessing the risks of events happening in the future is necessarily different in nature to the exercise conducted by those investigating a suspected offence. A criminal investigation into a suspected offence looks back at events that are suspected to have occurred. A criminal investigation will look at the suspected crystallisation of risks that the risk assessment will hopefully have addressed.

Financial institutions designing procedures to demonstrate compliance with the new offences may deem having a thorough understanding of the customer tax laws of a particular country as disproportionate to the risk identified in its risk assessment. Such a level of understanding is not generally expected to be a necessary part of reasonable prevention procedures. Instead, financial institutions will likely focus on more general risks that a particular business line could be used to facilitate tax evasion, as detailed in later chapters.

To comply with the Act, financial institutions are not required to examine the tax affairs of their customers, beyond what is already required of them under the existing law.

Where there is a risk that a financial institution's client is involved in tax evasion, the financial institution will need to consider the issues raised in terms of the regimes under the money laundering regulations and the Act. It may be sensible to deal with the AML and tax evasion facilitation issues in tandem under an integrated set of procedures designed to meet the needs of both regimes.

The focus of prevention procedures should be the prevention of the facilitation offence by associated persons. The guidance in this chapter is to support financial institutions in identifying risks of both tax evasion and facilitation but should not be interpreted as requiring financial institutions to conduct any additional investigations into the tax affairs of their customers, nor for staff and associated persons to become experts in tax matters. However, relevant staff within a financial institution should be aware at an appropriate level of how their products and services could be used to evade taxes and it would be reasonable for financial institutions to deploy their existing tax knowledge when devising prevention procedures.

HMRC guidance recognises that risks of an associated person criminally facilitating tax evasion will inform the extent of prevention procedures that are reasonably required. Likewise, the degree of control that the relevant body has over an associated person will affect what prevention procedures can be reasonably expected. This approach allows all organisations to adopt a proportionate approach to the corporate offence, and recognises that it may depend on a number of factors (e.g. the size of the organisation, the type of business engaged in etc.).

The application of a risk-based approach and the scope of reasonable prevention procedures required by financial institutions is considered in Chapters 7-13 below.

4.2. The two offences under the Criminal Finances Act 2017

The legislation creates two corporate offences; one in relation to the failure to prevent the criminal facilitation of UK tax evasion, and a second which creates the equivalent offence for foreign taxes. Both offences have a legislative framework under which a number of elements are required; two predicate criminal offences and consideration of a possible defence.

4.3. Where the tax evaded is UK tax ('the corporate offence' related to UK tax)

1	A taxpayer (either an individual or an entity) has criminally evaded UK tax	*'Underlying offence' - Chapter 4.5*
2	That evasion was criminally facilitated by a third party	*'Facilitation offence' - Chapter 4.6*
3	That third party is an associated person of the financial institution	*'Associated person' - Chapter 6*
	That financial institution has failed to prevent the criminal act of facilitation, but may show in its defence that…	
4	It had in place reasonable prevention procedures to prevent the facilitation	*'Reasonable prevention procedures' – Chapters 7-13*

4.4. Where the tax evaded is not UK tax ('the foreign tax corporate offence')

1	A taxpayer (either an individual or an entity) has criminally evaded non-UK tax	*'Underlying offence' - Chapter 4.5*
2	The dual criminality test is met	*'Dual criminality' – Chapter 5*
3	That evasion was criminally facilitated by a third party and that facilitation also meets the dual criminality test	*'Facilitation offence' - Chapter 4.6*
4	The financial institution has a UK connection	*Geographical scope - Chapter 5*
5	That third party is an associated person of the financial institution	*'Associated person' - Chapter 6*
	The financial institution has failed to prevent the criminal act of facilitation, but may show in its defence that…	
6	It had in place reasonable prevention procedures to prevent the facilitation	*'Reasonable prevention procedures' – Chapters 7-13*

4.5. Criminal tax evasion ("the underlying offence")

'Tax evasion' refers to a number of specific criminal offences created by legislation as well as the common law offence of 'cheating the public revenue'. Because it is a common law offence, its scope is determined as the result of case law, and a substantial body of case law defining the offence which is beyond the scope of this guidance. The offence may best be summarised as any form of fraudulent conduct which seeks to divert money from the public revenue, depriving it of money to which it is entitled. Similarly, various statutory offences can be committed by a person who is knowingly concerned in, or takes steps with a view to, the fraudulent evasion of a tax.

Tax planning which is entered into with an honest belief that it is a legal method of legitimately reducing a tax liability is not tax evasion, even if that planning is later shown to be ineffective.

Tax evasion is characterised by dishonesty, typically either by:

- a dishonest positive act - such as submitting false or misleading information or the deliberate concealment of assets or income, or
- by a dishonest omission - such as failing to declare income on which tax is due, or failing to declare the sale of an asset which would be subject to capital gains tax.

Tax evasion requires fraudulent or dishonest behaviour; the Government guidance recognises that *"Non-compliance, falling short of fraud, at the taxpayer level will not result in the corporate offence being committed"* (see paragraph 1.3).

Note that for a relevant body to be criminally liable there is no requirement for there to have been a conviction for the underlying tax evasion offence. It will, however, need to be proved by the prosecution to the criminal standard as part of a prosecution for the corporate offence.

Examples of underlying tax evasion in financial services

- An individual dishonestly fails to declare income from an offshore investment held in a fund to the UK tax authorities in order to evade tax (failure to declare offshore income on various financial products is likely to be one of the most common forms of tax evasion encountered by all financial institutions).
- A sole trader requests payment in cash from customers. That trader makes substantial cash deposits into a UK bank account and deliberately does not declare the income for tax purposes in order to dishonestly hide revenue from HMRC.
- A customer creates a shell company in an offshore country and dishonestly claims that money belongs to that company. In reality, they treat the accounts of the company as their personal accounts without any reference to the company law requirements in using such accounts.
- An investor deliberately falsifies an annual statement of their investments to report a lower amount of income to the tax authorities in order to pay less tax.
- A small business sets up an offshore account and regularly pays amounts of money from their UK bank account to that offshore account. In their tax return they claim that these are legitimate expenses of running the business and are therefore tax deductible, when in fact the 'expenses' are wholly fraudulent.

*Examples of what is **not** tax evasion*

- A wealth manager refers a customer to a tax advisor (in circumstances which make them an associated person for these purposes). That tax advisor recommends a tax avoidance scheme to the customer despite knowing that the taxpayer is not entitled to the tax advantages of that scheme but does not disclose this to the customer. Instead they provide false documents indicating that HMRC have approved the scheme. The customer honestly believes that the scheme is legitimate and demonstrates that no tax evasion offence has been committed by them as they had no knowledge or intent to commit fraud. The customer is not guilty of tax evasion as their actions have not been dishonest. However, the tax advisor will have committed a tax evasion offence.

- Due to confusion in relation to scope of the Personal Savings Allowance, a customer believes that an income payment is not taxable when in fact it should have been declared and subject to tax. The customer has made a genuine honest mistake, and therefore no tax evasion offence has been committed.

- Merely moving an account to a country which has not adopted the Common Reporting Standard (including the US) of itself. It should however be noted that where an account is moved to avoid detection of a revenue authority and the client intends not to declare their taxable income or gains where such an obligation exists then this would amount to a tax fraud.

- A transparent fund requires the recognition by a UK investor that they have received income in the year. However, the fund does not provide tax reporting to investors (which is also not required by law). An investor does not realise that they should include the income in their tax return. The investor has not committed an evasion offence because they made an honest mistake. However, if they subsequently become aware of the mistake and do not correct the tax position, they may then commit an evasion offence.

- Establishing a fund in a low or zero tax jurisdiction is not, of itself, an indicator of evasion. There may be other relevant facts and circumstances to consider.

4.6. The facilitation of tax evasion ("the facilitation offence")

The facilitation offence relies in part on existing principles, in particular related to being knowingly concerned in or taking steps with a view to the evasion of tax owed by another, and the criminal aiding and abetting of an underlying tax offence. As with the underlying offence, this means that there is an established body of law which will inform HMRC's approach to the offence.

Although the term "aiding and abetting" is in common usage, its legal meaning may not always be understood, and financial institutions may not find it useful to use these terms in procedures.

In practice, an associated person will commit the facilitation offence where they knowingly and dishonestly encourage or assist the commission of a tax evasion offence. It is not a crime to innocently assist the crime of another (i.e. where the underlying offence has taken place and an associated person was innocently involved and unaware of the crime).

The facilitation offence must be proven to a criminal standard and it can be committed by positive action, failure to act when required to do so, or by wilful blindness.

Once the tax evasion facilitation offence has been committed by a person acting in the capacity of a person associated with the relevant body, there is no further requirement for senior management of the relevant body to have known anything about the underlying offence in order for that relevant body to be

criminally liable. Likewise, the relevant body will be criminally liable even if it does not gain any benefit from the criminal facilitation.

Accident, mistake and unknowingly being used by a customer for evasion

The facilitation offence requires dishonesty on the part of the associated person; it cannot be committed by accident or by mistake. HMRC's guidance recognises that the facilitation offence cannot be committed "*accidentally, ignorantly or even negligently*" (see paragraph 1.3). This will include an honest mistake where someone genuinely fails to spot a risk.

Financial institutions provide many services which could be misused by taxpayers seeking to evade tax without the financial institution, its employees or and any other associated persons being aware of that offence being committed. Criminal facilitation has not taken place where the associated person had neither the necessary knowledge nor the intent to facilitate the tax evasion offence.

Failure to act where there is a legal duty to act

The facilitation offence can be committed by omitting to act in certain circumstances where there is a duty to act.

The facilitation offence will only be committed through an omission where an associated person has a duty to act, and then fail to do so. This could apply, for example, where an employee (or other associated person) deliberately and knowingly facilitates tax evasion by: failing to record adequate due diligence on a customer's file to ensure that certain facts are not disclosed, fails to file a suspicious activity report when they have knowledge that tax is going to be evaded, or otherwise fails to make a mandatory report to a tax authority knowing that the customer is committing tax evasion. Criminal liability will not arise where a failure to act was not dishonest (whether due to either negligence on the part of the associated person or deceit by the person evading their tax liability only).

Examples of criminal facilitation in financial services

- An employee knowingly advises a customer to invest funds into an offshore account, and to not tell HMRC about the income in order to evade a tax liability.
- Following a meeting with a client, a relationship manager deliberately changes that client's electronic records to supress reporting to tax authorities under the Common Reporting Standard in the knowledge that doing so will assist the client to evade their tax liability.
- A law firm is appointed by a bank to assist with a high net worth customer's tax matters. Whilst acting its capacity as an associated person, the law firm knowingly assists that customer to evade tax by entering into a fraudulent evasion scheme.
- An employee of a UK investment manager of an offshore fund, assisting that fund with FATCA compliance, knowingly accepts without a challenge a FATCA self-certification form which they know to include a false classification in relation to the reportable controlling persons of a trust, knowing that it is to avoid reporting to the US.
- During the completion of due diligence an employee becomes aware that a customer is engaging in ongoing tax evasion and the employee fails to file a suspicious activity report because they do not want to lose the associated commission.

- A third-party product distributor sells, in its capacity as an associated person, a product on behalf of a UK financial institution in the knowledge that it will be used to facilitate tax evasion.
- An investment management firm knowingly designs or facilitates a product thats purpose is to generate a tax evasion opportunity.

*Examples of what is **not** criminal facilitation*

- A UK client tells his relationship manager that he wishes to invest in an offshore product to legally minimise his UK tax liability. The relationship manager makes it clear that he can refer the client to the Jersey office, but that details related to his account may be reported to the UK under the Common Reporting Standard and that the bank will not help the customer evade tax. The relationship manager does not suspect that the client is engaging in criminal activity.
- An employee conducting a due diligence review on a customer mistakenly fails to ask a question about tax transparency. That customer subsequently evades tax using the financial institution's services. The employee did not intend to facilitate the evasion of tax and made the error honestly.
- A customer withdraws £19,500 in cash from a bank account. The customer usually withdraws small amounts via an ATM. The cashier does not know the purposes of the withdrawal and is not required to ask any questions about the purpose. It transpires that the money is to be used to evade VAT on a payment to a house builder. The cashier has not committed a facilitation offence by providing the money, or by not asking any further questions about the purpose of the withdrawal, because the cashier was unaware of the evasion and did not act dishonestly. However, AML matters would require separate consideration.
- During the completion of due diligence an employee becomes suspicious that a customer is engaging in tax evasion. The employee follows internal procedures which results in a suspicious activity report being filed in accordance with existing legal obligations the account is not closed to avoid 'tipping off' the customer.
- A customer instructs a financial institution to make a payment on maturity of an investment to a bank account in a different country, through which the customer intends to evade a tax liability. There is no legal requirement in that country to determine why money is remitted to a third country. A facilitation offence has not been committed solely following the customer's instructions or by paying the money or failing to ask further questions, provided the payment had not created any suspicion of evasion and is made honestly.
- A transparent fund requires the recognition by a UK investor that they have received income in the year. However, the fund does not provide tax reporting to investors (which is also not required by law). An investor does not realise that they should include the income in their tax return. The fund and its associated persons have not committed the facilitation offence by failing to provide full tax reporting to a customer.

4.7. The 'failure to prevent…' offence

Where both the taxpayer has committed the underlying offence and an associated person has committed the facilitation offence, an organisation is liable for failing to prevent the criminal facilitation of tax evasion unless it can demonstrate that it had established, at the time at which the facilitation offence occurred, reasonable prevention procedures to prevent that facilitation.

For the avoidance of doubt, the offence requires that both the underlying offence and the facilitation offence must be criminal acts. As noted above, both offences require an element of dishonesty or fraud in their commission. The requirements of the offence are not fulfilled if an associated person unknowingly and honestly provides services that are subsequently abused to evade a tax liability.

The organisation is responsible for the actions of associated persons who perform a service for or on its behalf, even if management of the organisation was not aware of the specific actions of the associated person.

The focus of organisations will be to demonstrate that reasonable prevention procedures have been established, this is covered in more detail in Chapters 7-13 of this guidance.

5. Geographical scope

5.1. Overview

The legislation creates two corporate criminal offences: one in relation to the failure to prevent facilitation of the evasion of UK taxes, and the second in relation to the failure to prevent facilitation of evasion of non-UK taxes. As a result, an offence may be committed:

- Where any entity (regardless of where it is based) fails to prevent its associated persons from criminally facilitating UK tax evasion *(s.45).*
- Where an entity with a UK connection fails to prevent its associated persons from criminally facilitating non-UK tax evasion, provided there is dual criminality *(s.46).*

5.2. Facilitating the evasion of UK tax

A corporate offence is committed where an entity anywhere in the world has failed to prevent the criminal facilitation of UK tax evasion by its associated persons. The offence applies to all entities regardless of their location.

Both the risks of tax evasion and the scope of reasonable prevention procedures may vary based on the location in which the relevant body undertakes business due to nature of services and the client base served in different locations. A financial institution in the UK might conclude it is reasonable to apply controls to all of its operations whereas a financial institution outside of the UK may decide to focus primarily on ensuring compliance with elements where they provide service to UK taxpayers or with some other UK connection (although those factors may also be relevant to the approach of a UK financial institution).

Having conducted the risk assessment there are no particular prevention procedures that are mandated, the requirement is that reasonable prevention procedures be put in place. Factors that may influence what is reasonably required by way of prevention procedures will include anything relevant to the risk that an associated person may criminally facilitate tax evasion. This may include the financial institution's location and the location of the customer, client or taxpayer, and the nature of services being provided or products being sold.

5.3. Facilitating the evasion of non-UK tax

Where the tax evaded is not UK tax, the corporate offence can only be committed by a financial institution with a UK connection. A UK connection will be established where:

1. The financial institution is incorporated under the law of the UK,
2. The financial institution conducts part of its business in the UK, or
3. Any aspect of the facilitation offence occurs in the UK.

With regard to the third condition, this will include situations where an associated person such as a relationship manager meets with a taxpayer in the UK, even if neither is normally based in the UK.

The facilitation offence will not be considered to take place in the UK solely because;

- a transaction is conducted in sterling.

- a contract references English law, or recognises the jurisdiction of English courts. These are common contractual arrangements used globally and not an indication that any activity took place in the UK.
- money passes through a UK bank account (although if the bank was incorporated under the law of the UK or conducts part of its business in the UK then it would have a UK connection on this basis regardless of where the criminal act of facilitation occurs).
- It is performed by an individual who is a UK citizen or an individual who has a right of residence in the UK, where the activity is performed outside of the UK.

5.4. Dual criminality

Where the financial institution has a UK connection, the failure to prevent the facilitation of non-UK tax evasion will be an offence under s.46 of the Act.

However, recognising that different countries approach the criminalisation of taxpayer non-compliance differently, the offence will only be committed where it meets a requirement of dual criminality:

1. The underlying offence is a criminal offence in the country where it is committed (s.46(5)(a)) and would be regarded as the fraudulent evasion of tax in the UK (s.46(5)(c)); and,
2. The facilitation offence is a criminal offence in the country where it is committed (s.46(6)(a)) and would, if the foreign tax evasion offence were a UK tax evasion offence, amount to a UK tax evasion facilitation offence (s.46(6)(c)).

When considering procedures to prevent the facilitation of tax evasion, financial institutions are likely to find it easier to ask the question 'had all elements of the transaction been undertaken in the UK, would it have been a criminal offence under UK criminal law?' Acts that would not be criminal under UK law will not lead to the non-UK tax evasion offence being committed regardless of the other country's criminal law.

The concept of dual criminality exists under existing AML/CTF rules, and financial institutions may find it useful to reflect on how existing procedures approach this issue.

Prosecution of the overseas offences
Any prosecution for the foreign tax offence (s46) would require the personal consent of the DPP, DPPNI or Director of SFO (s49). Such consent would only be given where prosecution was in the public interest. In determining whether a prosecution was in the public interest a wide range of factors would need to be considered, including any compliance response that had taken place in the other countries. HMRC noted in their 2015 response to consultation that *"the preference will always be for the jurisdiction suffering the tax loss to take the criminal or civil response that it feels most appropriate"* (para 3.94). These considerations would also inform the decision whether or not to criminally investigate and prosecute an individual for offences of facilitation.

5.5. Application to multinational groups and branches

Banks and insurers are likely to operate through permanent establishments and representative offices.

The consequence of the business operating by having various branches of one single Financial Institution, rather than subsidiaries with separate legal personality, is that the offences created by the Act apply to the Financial Institution and not its individual branches. It is the company that commits the

new offence if a person acting in the capacity of a person associated with it criminally facilitates tax evasion, and it is the company that will be within scope of the foreign tax offence if it conducts part of its business from the UK, for example via a permanent establishment. Financial institutions cannot claim that the offence was committed "by the branch" when than branch has no separate legal personality and is part of the Financial Institution. Meanwhile, where a Financial Institution does operate through subsidiaries then these subsidiaries are themselves "relevant bodies" and thus capable of committing the new corporate offences (depending on the facts a subsidiary may also be an associated person of its parent company).

The result is that the application of the Act to financial institutions is likely to have a broad geographical scope. Chapter 5.3 - 5.5 illustrate the geographic scope.

Definition of terms

- *'Permanent Establishment'* means the operations of an entity in a country other than the one in which it is tax resident, where those operations give rise to a taxable presence in that other country. Permanent Establishments are commonly known as 'branches'. It is part of the same legal entity as the head office; however, it may be regulated separately in the country in which the PE is situated.

- *'Subsidiary'* means a separate legal entity from its holding/parent company. Joint Ventures which are created as separate legal entities will be treated the same way as subsidiaries (see chapter 6 for more detail).

Treatment of Permanent Establishments and Representative Offices

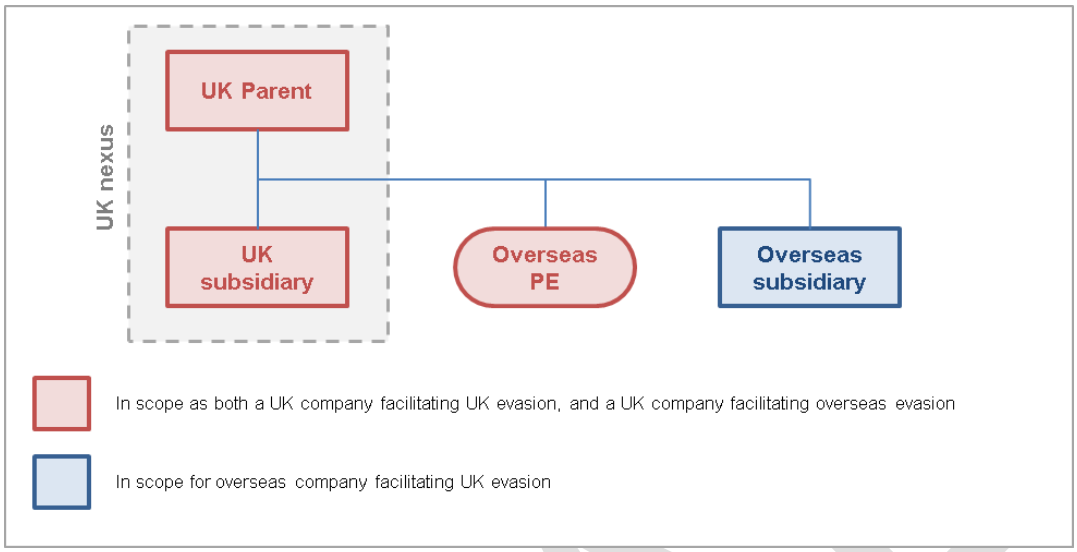
The main office and the branches are a single legal entity in law. The new offence applies to and can be committed by the Financial Institution rather than an individual office or branch. It is the Financial Institution, not the main office nor any of its branches, that is held liable under the criminal law. If an associated person criminally facilitates tax evasion through one of the financial institution's branches, the new offence will be committed by the financial institution.

For the purposes of putting in place reasonable procedures it will fall to the financial institution to consider which part of its organisation is best placed to lead on putting in place these procedures for the entity. It may be reasonable for these procedures to be controlled and directed by the head office, but equally it may be reasonable for the relevant body to choose to have one of its branches undertake this task on behalf of the whole organisation.

Financial institutions will typically view their permanent establishments as having a high degree of autonomy from their 'parent'. For the purposes of the following examples we have illustrated the permanent establishment separately but note that this is for illustration purposes only.

Note that the Act will apply where an organisation "carries on a business or part of a business in the United Kingdom". That will cover a number of scenarios in which there is a presence in the UK which does not amount to a permanent establishment.

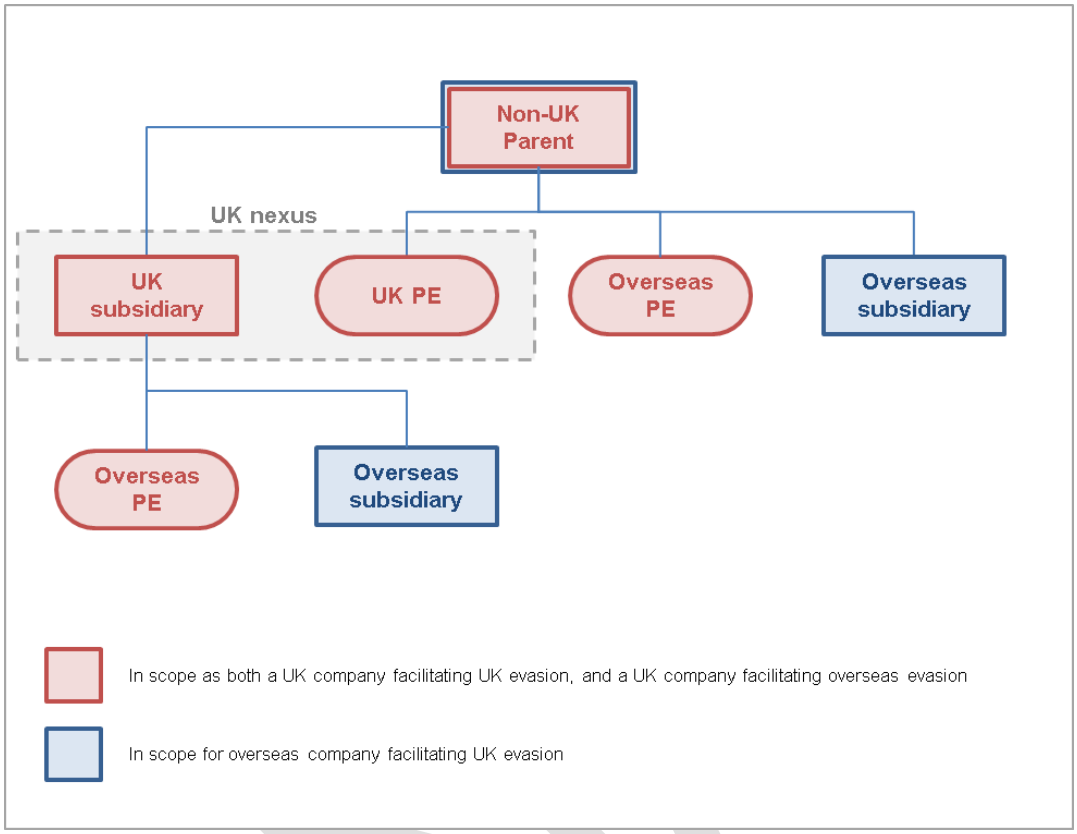
5.6. Example 1: For UK headquartered groups



A UK headquartered financial institution has a UK subsidiary, and both an overseas permanent establishment (PE) and an overseas subsidiary.

- *The UK parent and UK subsidiary are both incorporated under the law of the UK and are within the definition of UK based relevant bodies – therefore they are in scope for the foreign tax corporate offence (the UK tax offence also applies to all relevant bodies wherever incorporated).*
- *The overseas subsidiary is not incorporated under UK law, nor does it conduct any part of its business in the UK, and for the sake of this example assume it does not act as an associated party to the UK entities. Accordingly, it is in scope for the corporate offence related to foreign tax only if the criminal act of facilitation by an associated person takes place in the UK. However, the UK offence can be committed by any relevant body wherever formed.*
- *The overseas PE is part of the single legal entity comprising the UK parent. The whole legal body, including the overseas PE, is within scope for both the corporate offence related to UK tax and the foreign tax corporate offence.*
- *If similar activities were carried out in an overseas subsidiary, rather than a permanent establishment, then that overseas subsidiary would only be in scope of the foreign tax offence if carrying out part of its business in the UK or if the criminal act of facilitation by an associated person occurred in the UK.*

5.7. Example 2: For non-UK headquartered groups



A non-UK headquartered financial institution has a UK subsidiary and UK PE, and both an overseas PE and an overseas subsidiary.

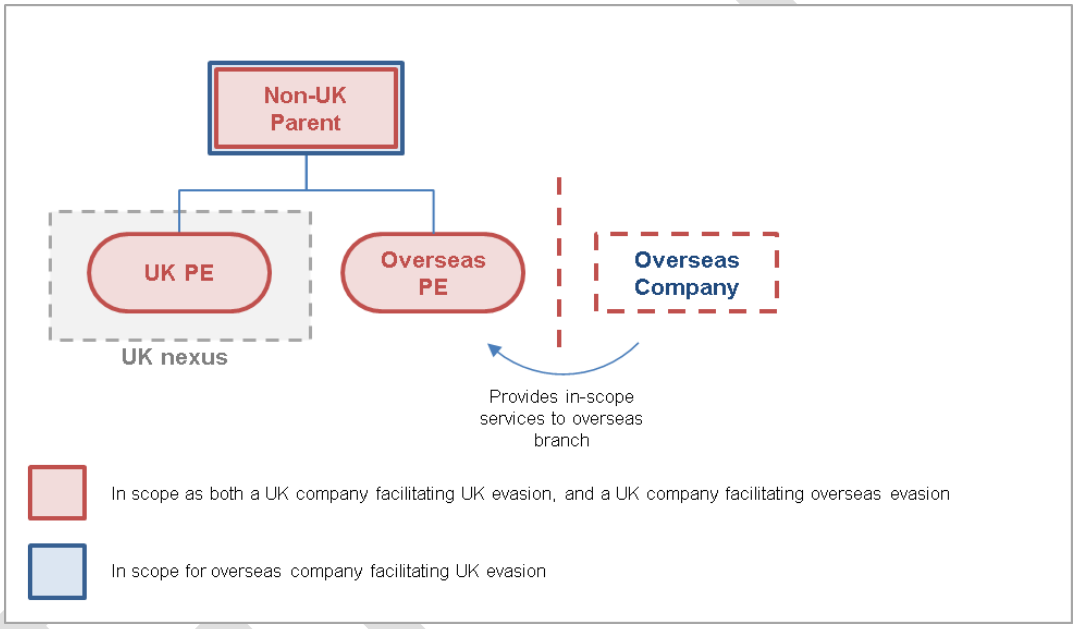
- *The UK PE and UK subsidiary are both incorporated under the law of the UK therefore both legal entities are in scope for the foreign tax corporate offence. The UK offence applies to all relevant bodies.*
- *Neither of the overseas subsidiaries is incorporated under the law of the UK, nor do they conduct any business in the UK, and assume for the sake of this example that they do not act as an associated person to the UK entities. Accordingly, they are in scope for the corporate offence related to foreign tax only if the associated person's criminal act of facilitation takes place in the UK. However, any relevant body can commit the offence in relation to UK tax.*
- *Because the non-UK parent carries out part of its business in the UK through its UK PE, the whole legal body, including the overseas PE, is within scope for the foreign tax corporate offence. The UK tax offence can be committed by any relevant body.*
- *The overseas PE of the UK subsidiary is also in scope of the foreign tax offence by virtue of being part of the UK subsidiary that is within scope in line with the example above.*
- *The non-UK parent is in scope for the foreign tax corporate offence. Note if the non-UK parent had no UK PE and did not otherwise carry on any part of its business in the UK, it would only be in scope of the foreign tax offence if the criminal act of facilitation occurred in the UK. However, the UK tax offence applies to all relevant bodies.*

For example, a US headquartered bank has permanent establishments in the UK and in the Netherlands. The actions of the banks employees working in the Netherlands permanent establishment can render the bank guilty of the foreign tax offence should they criminally facilitate the evasion of French income tax. The bank is a single legal entity within scope of the foreign tax offence by virtue of conducting part of its business in the UK (via its UK permanent

establishment). Such a prosecution would require the personal consent of the DPP or Director of the Serious Fraud Office. This would only be given where the prosecution was in the interests of justice. This would require consideration of various factors, including the compliance response of the authorities in the US, France and Holland, and whether there was a risk of the bank being subjected to "double jeopardy".

Note that assuming the same fact pattern above, if all operations were performed by subsidiaries, only UK subsidiaries would be in scope for the foreign tax corporate offence. An overseas company would only be within scope of the foreign tax offence if part of its business was conducted in the UK or if the criminal act of facilitation occurred in the UK.

5.8. Example 3: Interaction with associated persons rules



A non-UK headquartered financial institution has a UK PE and an overseas PE. Through the overseas permanent establishment, the financial institution uses a third party company to provide services to its customers.

- *The UK tax offence applies to all relevant bodies wherever incorporated and thus applies to the non-UK parent. The non-UK parent conducts part of its business from the UK (via its UK PE) and thus it is also within scope of the foreign tax offence. The UK and overseas PE are part of the non-UK parent company, even though they may act with a degree of autonomy.*
- *The UK PE is part of the single legal entity comprising the UK Parent. The whole legal entity, including the UK PE, is within scope of the foreign tax offence as it conducts part of its business within the UK (moreover the UK tax offence applies to all relevant bodies).*
- *The overseas PE is part of the single legal entity comprising the UK parent. The whole legal body, including the overseas PE, is within scope for the foreign tax corporate offence even though it acts autonomously. The UK tax offence applies to all relevant bodies.*
- *The non-UK Parent is in scope for the foreign tax corporate offence (the UK offence applies to all relevant bodies).*
- *The non-UK parent can be guilty of failing to prevent criminal facilitation by the overseas company as the overseas company is an associated person of the non-UK parent by virtue of providing services for or on its behalf (through its overseas PE).*

In this scenario, there would be a requirement for the financial institution to ensure that the overseas company did not facilitate UK tax evasion under s.45 of the Act. In addition, because of the UK PE, the bank as a single legal entity would need to consider whether there is a need to impose reasonable prevention procedures to prevent facilitation by the overseas company, even though there is no UK element to any offence committed other than the fact the legal entity is carrying on a business in the UK.

As with the previous example under 5.7, this would mean that the actions of a Netherlands branch (the overseas PE), of a US headquartered bank (the non-UK parent), using a German law firm (the overseas company) which failed to prevent the facilitation of the evasion of French tax in the course of acting as an associated person on non-UK Parent could be subject to prosecution because the US headquartered bank has a UK permanent establishment.

However, such a prosecution would need the consent of the DPP or Director of the SFO, which would only be given if the prosecution was in the interests of justice. One factor informing this decision would be what response to the wrongdoing had occurred in other jurisdictions whether any prosecution would expose the defendant relevant body to a risk of "double jeopardy". This could be in addition to any prosecutions by the authorities in each jurisdiction under their own laws. HMRC noted in their 2015 response to consultation that *"the preference will always be for the jurisdiction suffering the tax loss to take the criminal or civil response that it feels most appropriate"* (para 3.94).

5.9. The application of the offences outside of the UK – examples

Example 1: Red Ltd is a Netherlands headquartered insurer. Employees of the insurer based in Netherlands fraudulently assist clients to evade UK tax

- The corporate offence related to UK tax applies to all entities wherever incorporated.
- Netherlands based staff are employees of Red Ltd. Under s.44(5), the employees are associated persons of Red Ltd.
- Since its Netherlands based employees are associated persons Red has potentially committed the corporate offence related to UK tax.
- Where the tax evaded was non-UK tax, the foreign tax corporate offence would not be committed by Red unless there was some UK connection to the facilitation offence, for example if a meeting to arrange the facilitation had taken place in London or Red was a UK registered company, or the branch of a UK registered company, or carrying out a business or part of a business in the UK.

Example 2: Blue Plc is a UK headquartered insurer with a branch in Netherlands. Employees of the insurer based in the Netherlands Branch fraudulently assist clients to evade both UK and French tax

- The corporate offence in relation to UK tax applies to all entities wherever incorporated.
- As the Netherlands based staff are employees working in a branch they are associated persons of Blue Plc.
- Potentially Blue has committed the UK corporate offence in relation to the failure to prevent the facilitation of tax evasion of UK tax.
- The foreign tax corporate offence applies to Blue because it is incorporated in the UK.
- There has been a facilitation of evasion of French tax by persons associated with Blue (the employees based in Blue's Netherlands branch). But Blue Plc will only have committed the foreign tax corporate offence if the French facilitation and evasion offences would also be criminal offences under UK law and so there is dual criminality.

Example 3: Yellow SA is a French headquartered bank with branches in London and Netherlands. The bank is one legal entity. Employees of the bank based in the Netherlands Branch fraudulently assist clients to evade French tax, without the knowledge of anyone at the UK branch or the French head office.

- As employees of Yellow SA, Netherlands based staff are associated persons of Yellow SA.
- The tax evaded is French tax so the foreign tax corporate offence is relevant.
- As Yellow SA carries on part of its business in the UK (through the UK branch), then Yellow SA is in scope for the foreign tax corporate offence. The fact that the UK branch was unaware of the activity does not matter - the simple fact that Yellow SA conducts part of its business in the UK (in this case it has a UK PE) is sufficient to bring Yellow SA including all of its branches globally into the scope of the foreign tax offence.
- The French tax evasion will only create a potential foreign tax corporate offence if the facilitation and evasion offences would also be criminal offences under UK law.

Example 4: Green Inc. is a US headquartered bank which has a single branch in Netherlands. The bank is one legal entity. Employees of the bank based in the Netherlands Branch fraudulently assist clients to evade French tax.

- As employees of Green Inc. Netherlands based staff are associated persons of Green Inc.
- The tax evaded is French tax so the foreign tax corporate offence is relevant.
  Green Inc. is neither incorporated nor carrying on business in the UK nor does the fraudulent activity take place in the UK, therefore Green Inc. does not automatically commit the UK or foreign tax corporate offence.
- Because the corporate offence in relation to UK tax evasion (s.45) applies to all entities wherever incorporated, if the tax evaded had been UK tax liability, the corporate offence could be applied to Green Inc.
- However, if the criminal facilitation act had taken place in the UK, the offence would have a connection to the UK even when the evasion does not relate to a UK tax liability. This might include for example, a meeting in the UK between a client and an employee.

Example 5: XYZ Ltd is a UK Insurance Company with both a branch and a Maltese incorporated subsidiary, ABC, in Malta. The Maltese subsidiary is an EU regulated Independent adviser which refers its client to XYZ among other insurers.

In practice, it is likely that financial institutions will have a range of relationships to consider in determining the application of these rules. The example below shows the potential complexity in determining the application of these rules

ABC introduces business to the Malta branch of XYZ in respect of a high net worth individual, Person I, who is resident in Spain. An employee of ABC, despite knowing that Person I is resident in Spain, accepts a Maltese address and declaration of Maltese tax residency on Person I's application for a product to be sold by the Maltese Branch of XYZ Limited. In doing so the employee is acting contrary to ABC's internal rules and procedures.

ABC Ltd confirms to XYZ Ltd, via their AML Customer Due Diligence (CDD) reliance agreement, that they had verified the customers' AML CDD evidence and that there were no concerns in respect of their self-declarations of tax residency status.

A member of XYZ's front office staff notices common (Maltese) addresses being used for multiple and seemingly unconnected customers. She becomes suspicious that there may be tax evasion occurring and submits a Suspicious Activity Report to XYZ's MLRO.

Investigations by the MLRO reveal that, among others, Person I has deliberately falsified his tax residency declarations and used a correspondence addresses in Malta to appear to be Maltese resident in order to evade Spanish tax.

ABC is not in scope of the Act because it is only the subsidiary of XYZ ltd and the facilitation offence did not take place in the UK.

However, on these facts, the Maltese branch of XYZ has the necessary UK nexus (being a branch of a UK company) and is therefore potentially in scope for the offence of failing to prevent evasion of foreign tax and will potentially have committed this offence if the employee of ABC who facilitates the offence acts in the capacity of an 'associated person'. Therefore, the question is whether, in facilitating the tax evasion offence, the employee of ABC was providing services for, or on behalf of XYZ Limited.

6. Associated persons

An entity will have committed the offence where a person acting in the capacity of a person associated with it has criminally facilitated the evasion of tax, unless that entity can prove that it had in place reasonable prevention procedures to prevent that person's criminal conduct.

6.1. Who is an associated person?

A person acts in the capacity of a person associated with a relevant body if that person is an employee acting in the capacity of employee, agent acting in the capacity of agent, or other person that provides services for or on behalf of a relevant body acting in the capacity of such a person. The corporate tax facilitation offences can only take place if the person facilitates the fraudulent evasion of tax whilst acting in the capacity of a person associated with the relevant body. Facilitation that takes place outside of this capacity, for example in the persons' private life, does not give rise to corporate liability.

'Agent' is defined by UK law and typically includes anyone with authority to enter into contracts on behalf of the entity. It will apply only where the agent is acting in their capacity as an agent for that entity, so for example, an agent who acts on behalf of multiple entities will only be an associated person of Company A where they facilitate tax evasion whilst acting as agent of Company A, and not for any activities they conduct on behalf of other companies.

This means that anybody permitted to offer products or provide services on behalf of the entity may be a person associated with the entity and thus capable of rendering the entity guilty of the new offences if they criminally facilitate tax evasion when offering those products or services.

The definition is intended to be broad in scope. Dependent on the facts of the case it is capable of covering a whole range of persons who might facilitate tax evasion.

It is not possible to exclude a third party as an associated person through contractual terms. The determination of who is an associated person will always necessitate looking past the contractual form to the substantive reality, considering all the relevant factors, including contractual proximity and control. However, despite not determining who is an associated person, contractual terms may still be relevant as evidence of the company's prevention procedures and its commitment to preventing its associated persons from facilitating tax evasion.

It is not the case that where A is an associated person of B, that B is automatically an associated person of A. In all circumstances it will depend on the relationship between the parties, and who is doing what for whom.

Financial institutions will want to consider how the six principles can be applied to third party associated persons. There is a requirement to perform due diligence on third parties, but companies will also want to consider how communication, monitoring and controls can be applied to associated third parties.

Chapters 6.2 to 6.6 consider the application of these rules in relation to specific groups of associated persons.

6.2. Employees and persons acting in a similar capacity

Employees acting in the capacity of employees are associated persons of their employer. Temporary contractors and secondees, acting in that capacity, are associated persons of the entity for which they

are working. Where an employee acting in the capacity of employee criminally facilitates tax evasion, the employer will be liable for failing to prevent that facilitation (subject to raising the reasonable prevention procedures defence). Note that employees employed by one entity within a group structure, such as a service company, may be associated persons of other entities in that group.

However, employees may commit facilitation offences which are outside of their capacity as an employee. HMRC guidance refers to this as an employee acting on a "frolic of their own".

Example 1 – employee not acting in the capacity of an associated person

An employee who, completely unrelated to their employment, encourages a member of their rugby club to commit a tax evasion offence. In such a case it will be very unlikely indeed that the employee would be held have criminally facilitated tax evasion when acting in the capacity of an employee, even if in the course of his facilitation he used knowledge or information he acquired at work. However, if the employee encouraged a member of their rugby club to commit a tax offence whilst acting in their capacity as an employee (for example, as the rugby club's relationship manager for banking services) then they would likely be considered to have criminally facilitated tax evasion whilst acting in the capacity of an employee.

Example 2 – employee not acting in the capacity of an associated person

An employee of Purple Insurance Company is a client relationship manager. Outside of work, he assists his friend, who is not a client of Purple Insurance Company, with establishing an offshore account with a bank, knowing that his friend intends to evade tax and instructs him to make false declarations at account opening in order to avoid tax reporting.

The employee has facilitated a tax evasion offence. However, that facilitation is not performed while acting for or on behalf of Purple Insurance Company, and therefore the employee has not criminally facilitated tax evasion whilst acting in the capacity of an associated person of Purple Insurance for these purposes.

However, if the employee, in the course of his work for Purple Insurance, assists his friend in obtaining Purple Insurance's products (such as an investment product held offshore) in order to evade tax in his capacity as a client relationship manager, he would criminally facilitate tax evasion whilst acting in the capacity of an employee.

More complex situations will arise where the employee does something his employer has not permitted or perhaps has prohibited him from doing. Take for example an employee who is not allowed to communicate directly with a firm's clients but nonetheless does so, and helps a client falsify documents to aid the evasion of tax. In such a case it may well be determined that the employee was acting in the capacity of an employee, and so the employer will only be able to avoid criminal liability if it can establish a reasonable prevention procedures defence.

Example 3 – employee acting in the capacity of an associated person

An employee who maintains the email servers for Violet Bank accesses a customer data system and changes the coding of a payment of £1,000 from 'Interest' to 'Transfer' for her client, knowing that as a result the payment will not be reported to HMRC and the client will not declare any income to HMRC.

Although the employee has acted outside the normal role which she is employed to perform, she was only able to do so because she was an employee of the bank, and therefore is likely treated as acting in the capacity of an employee.

HMRC are of the view that the employees of entities who are associated persons may also be treated as associated persons. In that context, chapter 12.7 related to rules applicable to chains of suppliers may be useful in considering the reasonable prevention procedures which may be applied.

6.3. Subsidiaries and other group companies

Subsidiaries, parent companies and other group companies should not be treated as associated persons *solely* as a consequence of being in the same group as a relevant body. The issue is whether they are providing services for, or on behalf of, that entity.

In particular, ownership of a subsidiary (including entitlement to profits or other distributions) does not automatically mean that a subsidiary is an associated person, nor does the fact that a parent controls a subsidiary either as a director in its own right or through shared board members.

It is common for multinational financial institutions to have regional management, and in the case of non-EU headquartered groups, the EU management is often based in the UK. The fact that regional management is employed by a UK entity and has management responsibility and oversight of foreign operations is not enough on its own to make those overseas subsidiaries associated persons of the UK entity. Therefore, where a UK office has an oversight and governance role over an overseas subsidiary that overseas subsidiary is not necessarily an associated person.

In summary, a subsidiary will only be a person associated with the parent company where it acts as agent or provides services for or on behalf of the parent. In this respect, subsidiaries are like any other third party.

Note that subsidiaries are relevant bodies and also have to comply with the Act on their own account. Subsidiaries will be liable if their associated persons criminally facilitate the evasion of UK tax under s.45 of the Act. A subsidiary may also be liable for the foreign tax offence under s.46 if it is incorporated under the law of the UK, conducts part of its business in the UK, or if any aspect of the facilitation offence takes place in the UK. This is covered in Chapter 5.

6.4. Joint ventures

Joint ventures are forms of arrangement which enable different entities to partner and work together to achieve a common goal; they may be created either as separate legal entities or as a result of purely contractual arrangements.

Where a separate legal entity exists, the same approach will apply as for subsidiaries (see chapter 6.3 above). The legal entity will be a relevant body capable of committing the offences under the Act. The existence of a separate legal entity which is a joint venture will not of itself necessarily mean that it is 'associated' with any of its members, or that any of the members are associated with each other. It will depend whether the entity performs services for or on behalf of its members.

The situation will be different where the joint venture is a contractual arrangement. A contractual arrangement does not per se result in there being an associated person relationship. It will be necessary to consider a particular person (individual or legal entity) which is a member of the joint venture and whether that person is or is not performing '…*services for or on behalf of*…' the entity

whose conduct is being assessed, which may mean another joint venture partner. The degree of control that a participant in a joint venture has over that arrangement is likely to be one of the relevant factors that would be taken into account in deciding whether a third party is an associated person.

6.5. Suppliers

A third party will be treated as an associated person where they provide services "for or on behalf" of an entity.
An example of this will be where the financial institution sub-contracts the provision of a service to a third party. That third party, performing services for or on behalf of the financial institution will be an associated person of the financial institution.

Where the third party solely provides services to the financial institution as its customer the third party is unlikely to be an associated person. For example, a catering company providing food and drink to the financial institution is unlikely to be an associated person of the financial institution. The catering company provides services to the financial institution as its customer but does not provide services for or on the financial institutions behalf.

However, some suppliers may be providing services both to and for the financial institution. For example, external suppliers of payroll services provide a service to a financial institution but the service that they provide is to do something for or on their behalf (e.g. payroll). If, in the capacity of providing payroll on their behalf, the supplier criminally facilitates income tax evasion by staff then the employer would commit the new offence (subject to having the reasonable prevention procedures defence).

There is no single test to determine whether or not services are provided 'for' or 'to' a financial institution, or both. However, in practical terms, where a relevant body is a customer of another entity, and acts solely as a consumer in its own right, the supplier is unlikely to be associated. This would mean that where services provided are not provided directly or indirectly to the customers, clients staff or counterparties of a financial institution or to any other third parties, it is likely that services are provided 'to' the financial institutions and that the suppliers of such services will not be providing services "for or on behalf of" the financial institution. They are thus less likely to be associated persons.

Were a contractor to engage in the evasion of their own tax that should not normally render a financial institution guilty of the new offences: the contractor evading their own tax will be acting as part of a private frolic and not be committing a criminal act of facilitation when acting in the capacity of a person performing services for or on behalf of the financial institution. The Government guidance gives a specific example of tax evasion and facilitation which may affect contractors which requires knowledge and dishonest activity by someone within the organisation.

Consideration will need to be given to the actual arrangements in place and not the shorthand label applied to the third person. For example, consider a 'supplier' to an investment manager who provides document management services. At the request of a client of the investment manager, who is preparing an information pack for a tax authority, the supplier alters some figures which have the effect of reducing the client's tax liability. In such a case the supplier would be regarded as a person associated with the investment manager because the supplier is sending the information to the client on behalf of the investment manager.

Note that were an associated person to assist a supplier to evade their taxes that could also be within the scope of the offences.

6.6. Referrals

There is considerable focus for many financial services businesses on the circumstances in which a referral could result in a third party being treated as an associated person. A third party will be an associated person where it provides services for or on behalf of the financial institution. As such, sub-contractors and agents are likely to be associated persons.

There is not a simple answer of where a referral will create an associated person relationship. HMRC's guidance, at paragraph 3.5 sets out HMRC's view of the circumstances, along with examples in 6.8 and a number of key scenarios are included in the overview at chapter 6.9 below.

Example: A law firm, which is recommended by a bank to assist with a high net worth customer's tax matters, helps that customer to evade tax by entering into a fraudulent evasion scheme. Due diligence as conducted on the law firm and the employee of the bank made the referral in good faith believing the law firm to be in good standing. The bank does not have any ongoing role in the provision of the specific services (such as oversight or direction) made by the law firm. The men and women providing services are doing so for or on behalf of the law firm, not for or on behalf of the bank. Here, the bank's employees have not committed any criminal act of facilitation. The referral was made honestly and in good faith. The criminal act of facilitation was performed by employees of the law firm. These persons were not performing services for or on behalf of the bank, as this was a case of mere referral not an example of sub-contracting. Whilst the law firm has failed to prevent its employees from criminally facilitated tax evasion, the bank is unlikely to have committed the new offences.

6.7. Application to Financial Advisors (FA)

This guidance considers the issues that arise for entities when dealing with financial advisors. Financial advisors should consider these issues as they apply to their own fact pattern and contact their own representatives as necessary.

Financial advisors as "relevant bodies"

FAs who are constituted as a body corporate or a partnership will be relevant bodies and therefore capable of committing the corporate offences. As such, they will, themselves, be required to comply with the legal obligations, and may wish to take suitable account of the Guidance.

Where the relationship between the financial advisor and with a provider, such as a wealth management firm or insurer, is such that the provider is providing services for or behalf of the FA the provider will be an associated person of the FA and as such the FA will need to have "*reasonable procedures*" to prevent the provider from criminally facilitating tax evasion during the course of that firm providing services for or on behalf of the FA.

FAs, paid by the customer to provide services on their behalf, may act as intermediaries for the provision of services and products to the customer by insurers and other providers. There may be circumstances in which they could also be providing services for, and on behalf of the provider and therefore be an associated person of the provider. More details are in the section below.

Example 1. Wealth Management Firm ('WMF')

WMF does a lot of its business through intermediaries, such as third party financial advisers. WMF takes the view that the clients are clients of the intermediary not of WMF and historically the intermediary has performed all AML/KYC and held resulting data.

Following the introduction of RDR and AEOI, for more recently acquired business WMF now also maintains AML/KYC information on the underlying clients. For tax purposes (such as FATCA/CRS) generally the clients are regarded as clients of WMF. Intermediaries are largely UK based, but may also be offshore.

WMF provides all its services via the intermediary to the client and all communication with the client is via the intermediary. WMF should be controlling the provision of services to the client via the intermediary – however given the communication structure; there is scope for the intermediary to influence the service provision.

In the circumstances it is possible that the WMF is an associated person of the intermediary rather than the intermediary being an associated person of the WMF, where the WMF provides services to the client on behalf of the intermediary. However, the WMF should put in place all relevant due diligence processes in respect of the intermediary as it would for other associated persons.

Reasonable procedures

WMF should satisfy itself that its intermediaries have appropriate processes and procedures in place to prevent the facilitation of tax evasion, as they would for any other person associated with them.

The Financial Advisor as an associated person

When an FA acts as an intermediary for a provider of financial products, e.g. an insurer or a fund manager, the relationship rests between the customer and the FA, with the Customer Due Diligence process often carried out by the FA. The provider may have little knowledge of the customer other than that detailed on application documentation and required to comply with other regulatory requirements.

However the fact that an FA is paid by, and acting on behalf of its customer does not automatically rule out the possibility that it might also be providing services for, and on behalf of, the provider and for those services it could be considered as an associated person.

In its risk assessment the provider needs to consider the potential for FAs to be an associated person and what would be reasonable prevention procedures given the level of risk that the FA, in the capacity of person associated with the FI, criminally facilitates tax evasion.

The existence of a contractual arrangement does not, of itself, make the FA an associated person. In the case of a Fund Management Company 'FMC' the contractual relationship will formalise the dealing side of the relationship. All the facts should be considered including any contractual arrangements and the nature of the relationship between the FA and the provider.

Similarly for other providers, such as insurers, the extent to which the FA is tied to selling the provider's products is significant. A complete tie is likely to indicate that the FA is an associated person and reasonable prevention procedures may be akin to those required for employees. Where an FA sells products for more than one provider, they can only be an acting in the capacity of an associated person in relation to a provider (Provider A) where they are providing services for or on half of that provider (for example selling the products of Provider A).

Example 2. The sale of a standard product by a Financial Advisor

An individual with a pension pot accrued in one insurer A asks an independent FA for advice as to what to do with the pot on retirement. The FA advises the individuals to purchase a standard annuity product and after discussion with the customer about a number of providers and their products the customer chooses an annuity product offered by Insurer B. The FA is not remunerated by Insurer B.

The FA facilitates that purchase carrying out the Customer Due Diligence both in terms of local AML requirements and the client's reasoning for purchasing the product.

In this example, the FA is independent and acting as an agent of the customer when approaching Insurer B. The FA is not acting as a provider of services for or on behalf of Insurer B, as indeed the FA recommends to clients offers a range of products and services from various different insurance companies.

6.8. Relevant facts and circumstances

The next subchapters contain a range of examples of common third party relationships which financial institutions enter into. Those are divided into three groups –

i. Third parties more likely to be treated as associated persons
ii. Third parties which may be treated as associated person
iii. Third parties less likely to be treated as associated persons

In all cases, there is a need to consider all of the facts and circumstances of the relationship to determine whether the person is an associated person.

Note: HMRC's guidance states that where an associated person knows a referral is made to a third party who is "dishonest and made the referral knowing it would help evade tax", the referral could constitute the facilitation offence itself, even if the third party to whom the customer is referred is not in fact an associated person. In this case, the bank is liable as a result of its employee's criminal act of facilitation in making the dishonest referral.

Examples – when do referrals create associated persons relationships?

Example 1 Referral

Andrew is a client of Orange Bank and has been for many years. Andrew would like a service that Orange Bank does not provide. Instead, Orange Bank provide in good faith, a contact for a law firm who, on the basis of due diligence conducted by the bank, they believe to be reputable and to provide a good quality service.

Andrew enters into a contractual relationship with the law firm for the provision of on-going services. However, Orange Bank and the law firm are not in contact about the provision of services to Andrew.

The law firm will not be treated as an associated person of Orange Bank because it is not providing a service for or on behalf of Orange Bank

Example 2 Ongoing relationship

Andrew is a client of Orange Bank and has been for many years. Andrew would like a service that Orange Bank does not provide. Instead, they provide in good faith, a contact for a law firm who, on the basis of due diligence conducted by the bank, they believe to be reputable and to provide a good quality service.

Andrew asks Orange Bank to make the arrangements on his behalf. Orange Bank does not want to lose Andrew as a valued customer and are keen to help him. The bank contacts the law firm to arrange for the services that Andrew wants to benefit from, and agree that they will manage the relationship with the law firm going forward. Andrew's involvement is limited to signing the contract and paying for the services. On paper there exists a contractual relationship with Andrew and Orange Bank and a separate contractual relationship with Andrew and the law firm. However, the on-going service provided by the law firm is being directed by Orange Bank.

In this case Orange Bank is exercising control over the provision of services from the law firm to Andrew and the law firm will be seen to be acting as an associated person.

6.9. Examples – associated persons

The below examples illustrate where a common service provided by a third party for or on behalf of a financial institution may give rise to an associated person relationship.

Fact pattern *(and examples)*	
Offshore centres – a controlled subsidiary or offshore operation of the financial institution provides core services for or on behalf of the financial institution, which it would otherwise have provided itself *Examples: customer due diligence, transaction monitoring, tax reporting, IT which are outside of the legal entity but in the same group*	
Outsourced services - a third party provides outsourced services which a financial institution would otherwise have provided itself to a customer. Services to the customer are provided under the original contract between the customer and bank, and there is a separate contract with the third person *Examples: Bank trust company outsources the creation of trusts to a third person, Bank provides tax return or advice to a customer which are provided by an accounting firm.*	
Tri-partite agreements - a third party is person to a contract with both the financial institution and the customer to provide some or all of the services required under the contract. *Example: Wealth management agreement through which bank has custody of assets and investment manager advises on investments, sales and disposals.*	
Third party distributors remunerated for introduction and ongoing servicing – a third party distributor and fund management company have an agreement that the distributor will recommend investment in the management company's funds by its clients, and will be remunerated by way of fee or retrocession. The distributor's name (or its nominee) is recorded on the fund register and the fund relies on the distributor's AML/ABC checks performed on the clients. *Example* *Whether or not a distributor (B) will be an associated person of a fund management company (A) is a question of fact, depending on the specific arrangements. HMRC will look beyond legal contracts to what is happening in substance. The relationship between B and the end-client should also be considered:* *"Execution only" agreement between A and a fund platform – there would be no advisory services provided by the platform on behalf of A, therefore there is less likely to be an associated person relationship. This would be low risk.* *Financial planning agreement by an independent financial adviser – trustee type services likely to be provided. The full range of services provided to the end client may not be visible to A. This would be higher risk of being an associated person.* *Fund management companies should consider that distributors will only act on behalf of their clients where they have been paid to do. Where B is not being paid to conduct an element of their activity by an investor, then it is not likely that they are acting on behalf of the investor and may be acting on behalf of the fund management company. In all cases, it is important to consider the likelihood and impact of risks, as set out above.*	

Co-branding - where services are knowingly offered to customers under the brands of both the bank and a third person, even if the ultimate contract is only with the third person. Could include 'white-labelled' services. *Example: Insurance products which are sold by a bank but originated by an insurance company will result in the bank being an associated person of the insurance company.*	
Third parties acting as sales people – Financial advisors (FAs) or others who are contracted to sell products or services and where they only work for one financial institution, and are effectively treated as part of the sales force. *Examples: Financial advisors, mortgage brokers who work exclusively for that bank* Third parties who recommend a wide of products and treat the taxpayer as their own customer are not expected to be associated persons unless there are other factors which establish a closer connection. *Example: Financial advisers and mortgage brokers who provide a panel of various financial institutions and do not recommend particular institutions are unlikely to be considered an associated person.*	
Joint commercial approaches – use of third parties in the provision of services to clients, arranged and initiated by the bank. *Example: the use of a tax advisor in the arrangement of a syndicated loan, lease or other structured financing* *Lawyers, accountants and tax advisors involved in the development of services (scope largely limited to wholesale markets)*	
'Ongoing referral' a referral by an employee to a third party on whom due diligence has been conducted, and to whom ongoing services are provided by the bank to the customer, or to corporate structures which are created. Whether this is in scope will depend on the level of involvement of the bank in providing the services. *Example: a third-party tax advisor recommends the creation of a trust, and the bank provides a bank account to the trust. The tax advisor and the trust are highly unlikely to be considered associated persons of the bank in this case.* *Example: an employee recommends a third-party tax advisor on the basis they can assist the customer with the creation of a trust with the intention that the bank will act as trustees of the trust once it has been created. Both the tax advisor and the trust might be considered associated persons in this case as the facts potentially indicate the intention to act together to provide a service to the customer. Note this would not apply if the bank made a referral, and subsequently happened to provide services to the trust but without any intervening steps or intention to act together with the tax advisor.*	
Use of bank's infrastructure by other regulated bodies – banks may provide infrastructure to other regulated bodies to provide services to their underlying customers. The bank cannot typically access information on underlying customers for regulatory/data protection purposes. *Examples – provision of undesignated accounts and accounting software to solicitors for client money, provision of account infrastructure to accounts managed by third parties, omnibus accounts for client assets in the name of a nominee.*	

Third parties with authority over an account – accounts may give authority to a third party to deal on the account, who may also be signatories to contracts, but there is no other relationship between the bank and that third party. *Examples: Power of Attorney, investment advisors with dealing authority, segregated mandates of asset managers held for underlying customers.*	
Third parties referring customers – FAs who refer customers and where there is a normal commercial contract governing the referral which the FA has with more than one bank (for example governing the payments made to the IFA). All customer contracts are subject to normal due diligence, which may include 'permission to rely' on KYC checks performed by the FA.	
Third parties recommending your products – Financial advisors (FAs), corporate formation agents, etc. who recommend products to customers. The bank may be aware of the referral but contracts directly with the customer, subject to normal due diligence rules.	
'Vanilla' referral – a referral by an employee to a third party made in good faith. The third party and the customer contract directly, no ongoing relationship is created between the bank and the third party and the bank has no involvement in ongoing services. *Examples: referrals to solicitors, accountants or tax advisors where all that is provided is the contact details.*	
Banking services – ordinary banking services provided to third parties, where the bank does not know and is not required to know what the third party does as a result. *Examples: correspondent banking, fx spot transactions (a third party uses the bank to convert currency on behalf of underlying customers), letters of credit*	

	Third parties thought highly likely to be treated as associated persons
	Third parties which may be treated as associated person depending on facts and circumstances
	Third parties which are thought highly unlikely to be treated as associated persons absent any other factors which could create an associated person relationship

7. The six principles

7.1. Reasonable prevention procedures: the six principles

HMRC has identified six key principles (the 'principles') that organisations wishing to prevent the criminal facilitation of tax evasion by associated persons should consider when establishing reasonable prevention procedures.

- Risk assessment
- Proportionality of risk-based prevention procedures
- Top level commitment
- Due diligence
- Communication (including training)
- Monitoring and review

The six principles are necessarily flexible to allow each organisation to tailor its policies and procedures so they are proportionate to the risks of associated persons criminally facilitating tax evasion faced by the financial institution, and to recognise that existing controls and policies may already address many of these risks.

7.2. Applying the six principles

The following chapters provide further detail on the application of the six principles to financial services businesses, and include examples of actions and procedures which may assist a financial institution with the creation of reasonable prevention procedures to prevent the facilitation offence from taking place.

No part of the following chapters should be viewed as prescribing the precise form of prevention procedures to be implemented by a financial institution, which should be assessed based on the needs of an individual financial institution and the risks that it faces. The reasonableness of the procedures put in place in any case can only be definitively determined by the court. However, there are certain steps, such as conducting a risk assessment and retaining a record of its findings that a financial institution might need to have completed to have a realistic prospect of raising the reasonable prevention procedures defence. This guidance can only offer illustrations of how the 6 principles might be implemented by a financial institution.

A financial institution may find that after conducting its risk assessment and considering its existing procedures its risks are sufficiently mitigated. In such circumstances the financial institution should document the rationale for that conclusion. The conclusion will also need to be kept under review to ensure that the procedures in place from time to time are reasonable in relation to the risk it faces at that time.

Some of the content in the following chapters mentions a number of possibilities in relation to particular matters in connection with developing and applying reasonable prevention procedures, or sets out general comments on a possible approach. It is expressly not the purpose of this guidance to prescribe the precise form of specific action that must be adopted in relation to a particular matter, even in those cases where an organisation determines that higher risk factors are present, or it is a large or complex financial institution (that said, certain steps, such as conducting a risk assessment, might be thought almost essential for an financial institution to raise the reasonable prevention procedures defence). Equally, if a specific action is not mentioned in this guidance it may nonetheless form an appropriate

part of reasonable prevention procedures for a given financial institution and may be an appropriate alternative to those approaches and specific items mentioned in this guidance. In all cases, the prevention procedures that it is reasonable to put in place will depend on the risks faced by an entity and what is reasonable will ultimately be for the courts to determine.

The approach should be targeted to the business affected. Different parts of a business or group may have higher risks than in other parts of the same group or business entity, in which case the use of different and deeper procedures in those relatively higher risk areas would be merited.

7.3. Reliance on existing work and controls

Many organisations will have internal policies and controls which either directly or indirectly address tax evasion risks. Many will relate to AML controls but they may also reflect a financial institution's own proactive efforts to address tax evasion risks or broader requirements in relation to staff conduct. Those internal policies and controls are likely to be a critical part of any prevention procedures under the Act in so far as they relate to the facilitation risk.

Some organisations will have proactively sought to address these risks and may build on, or rely on, existing controls to demonstrate reasonable prevention procedures. That may also mean that a financial institution may find alternative ways of ensuring compliance which are not included in this guidance and adopting alternative approaches should not be viewed as unreasonable solely on the basis that an approach is not considered or included as an alternative approach in this guidance.

Reliance on existing risk assessments

The Government guidance indicates that institutions should (a) conduct a risk assessment; and (b) maintain a record of that assessment. Such a risk assessment is vital to inform what prevention procedures need to be put in place. It is essential to document both the risk assessment and the justification for not introducing new procedures.

Financial institutions may already have conducted risk assessments or other reviews which address all or part of the risk of criminal facilitation of tax evasion.

In such cases, it may be reasonable to perform a review of those existing risk assessments to determine the extent to which they sufficiently address the necessary considerations for the purposes of the Act (see chapter 9). This 'top-down' approach may be combined with either further risk assessment to address risks which are not adequately assessed, or a longer-term plan to combine risk assessments for the facilitation of tax evasion into other assessments conducted on a business as usual basis.

A financial institution is not however, required to undertake this activity in preference to other means of completing the necessary assessment of the risks that an associated person may criminally facilitate tax evasion.

A review of other risk assessments should consider whether the particular risks under the Act have been appropriately addressed. In particular, risks which may not have previously been considered might include:

- Risks of criminal facilitation by associated persons (other than employees)
- Facilitation risks in general, including the ability for facilitators to deliberately bypass controls
- Tax specific risks related to the facilitation of tax evasion

8. Implementation

8.1. Day one compliance

The corporate offences will apply from 30 September 2017. This means that where the underlying offence and the facilitation offence take place after that date, the entity will be potentially liable and will need to demonstrate that the facilitation offence took place despite the entity having in place reasonable prevention procedures at the time the criminal act of facilitation occurred.

Note that the facilitation offence can be committed by the continuation of criminal facilitation that began prior to 30 September 2017. Any criminal facilitation that takes place after the effective date will be within the scope of the Act.

The Criminal Finances Act 2017 was passed in April 2017 and the offences came into force on 30 September 2017. After this date there is no further transition or implementation period . Instead, entities will need to rely on a defence that they had reasonable prevention procedures in place to prevent the facilitation. The standard of what is 'reasonable' will evolve over time.

HMRC has confirmed that reasonable prevention procedures on day 1 will differ from what would be considered reasonable in the longer term. Even where an entity intends to amend or roll out new global systems and processes in the longer term, it may not be possible to do so by day 1.

In particular, Government guidance noted that, at the very least, the following items should be in place on day 1:

- demonstration of a clear commitment to compliance, which might include initial implementation steps (possibly including either high level or detailed risk assessments depending on the organisation).
- securing a top-level commitment and initial communication plan.
- an implementation plan for managing the risk in a proportionate and timely manner going forward.

Note that Government Guidance indicates that HMRC *"expects there to be rapid implementation, focusing on the major risks and priorities, with a clear timeframe and implementation plan on entry into force"* (paragraph 1.4).

8.2. Implementation plans

For day 1, the risk assessment should be supplemented by an implementation plan to implement further reasonable prevention procedures. The implementation is likely to include:

1. An analysis of existing controls that aim to mitigate the identified risks and their effectiveness,
2. A gap analysis of those risks or elements of the risks that are not addressed by existing controls (incorporating ethical standards, zero tolerance, organisational risk appetite, transparency standards, governance arrangements and senior management responsibility).
3. New controls or the enhancement of existing controls to meet requisite standards including post-implementation governance, and documentation of the relevance of existing controls where neither of the foregoing is needed.
4. A staff training needs assessment, including senior and middle management.
5. An incident management policy which could include whistle-blowing.
6. Securing budget for implementation and ongoing costs.
7. Where appropriate and proportionate, post-implementation review and monitoring.

The implementation plan may consider whether procedures are required in certain key areas such as:

- senior management accountability and oversight
- risk assessment
- policy, procedures and internal governance
- communication and training
- implementation approach
- decision making including delegation of authority, separation of function and conflicts of interest
- due diligence for existing and prospective associated persons
- contracts and governance of business relationships with associated persons
- disclosures and transparency, reporting and whistle-blowing
- monitoring and review, including management information

Whilst the Act creates new criminal offences, the approach above is similar to that required for compliance with other financial crime legislation, including the Bribery Act. Many good practices in the compliance, human resources, anti-money laundering and operational risk areas have relevance here.

9. Risk Assessment

9.1. Conducting a risk assessment

A risk assessment of the business will be the first step for financial institutions to put in place reasonable prevention procedures. Risk assessments are a fundamental part of many other compliance requirements, and financial institutions are therefore likely to have their own methodologies and approaches to conducting a risk assessment. These may be used as a starting point when developing a risk assessment for the purposes of the Act. What is most important is the outcome – an accurate assessment of the risk that usefully informs the development of prevention procedures – not the precise method used to achieve this outcome.

Whilst firms may have either existing methodologies or existing risk assessments they will wish to use when designing a risk assessment procedure for this Act, the following guidelines are still likely to be useful as a comparison to existing materials. This is particularly true for ensuring that the risk assessment adequately identifies the risks associated with the facilitation offence, which is separate and distinct from customer tax evasion.

In all cases, financial institutions should document their assessment of risks, the evaluation of any controls, and any conclusions which are drawn as a result.

9.2. Proportionate

The scale and detail of the risk assessment should be proportionate to the level of risk within the business. Understanding the risk within a business may require a staged approach.

Some level of risk assessment is likely to be needed in all circumstances, even for lower risk businesses. Having a regularly reviewed/updated risk assessment (reflecting the nature of your business and underlying risk) will prove an invaluable tool to demonstrate that the business understands the risks, and thus the reasons for your reasonable prevention procedures. It is likely that a financial institution would struggle to identify the reasonable prevention procedures without an up to date assessment of the risks that it faced: absent such an assessment a relevant body would have no means of showing why certain procedures were implemented and considered reasonable and other steps were considered unnecessary. The prevention procedures adopted need to be reasonable in light of the risk of criminal facilitation of tax evasion.

Risk assessment methodologies commonly require a consideration of the possible impact of a risk should it materialise and the likelihood of it materialising. More will need to be done to control an area considered to be high impact/high likelihood than will be needed for an area judged to be low impact/ low likelihood.

Some risk assessment methodologies require numerical/ quantitative inputs. It is important that the risk assessment method used assists in the exercise of proper judgment about the facilitation risks the firm faces and the prevention procedures these risks necessitate. A complicated method and accompanying paperwork may be unnecessary for a small business with only a few domestic lines of business. In some cases, lower risk businesses may conclude that a desktop review, appropriately documented, is reasonable in the circumstances.

A large and complicated firm, operating over a number of product and services lines, markets, and geographical areas, will inevitably require a more substantial process to properly assess and document the diverse risks that are posed by the business's complexity in order to be able to establish that a suitable and sufficient risk assessment has been undertaken.

All organisations may wish to start with a high-level risk assessment looking at business units across the financial institution, before conducting more detailed reviews in the areas where it is needed. In all cases the person conducting the risk assessment is likely to need to place him or herself in the position of an employee, agent or other person who provides services for or on behalf of the financial institution and pose the question "what would motivate me to criminally facilitate tax evasion and if I were doing so, how would I go about doing it and what would make succeeding more difficult?"

Organisations can leverage existing risk assessments to include an assessment around tax evasion facilitation risk.

In addition, organisations may already have conducted risk assessments for the facilitation of tax evasion which effectively meet the reasonableness test established by HMRC for these purposes. In those circumstances, relying on that risk assessment would be consistent with these requirements.

A number of factors used when undertaking AML/CTF risk assessments may also be useful in the identification of situations which pose greater risk of tax evasion by an underlying tax payer and may be useful for businesses in assessing the risks of facilitation associated with particular businesses. However, HMRC have indicated that it is unlikely to be sufficient to merely apply AML/CTF considerations without any further thought to the bespoke, unique, or different facilitation risks that may exist. This guidance includes the relevant chapters of the JMLSG Guidance at the end of this chapter.

9.3. Application to lower risk businesses

Once a business has completed its risk assessment it should consider to what extent existing 'controls' are in place to address that risk.

In circumstances where both the facilitation risk is considered to be low and existing controls are appropriate, additional requirements may be limited to:

- Documenting the assessment of risk for the purposes of the Act with appropriate review or approval.
- Top-level commitment to the prevention of facilitation.
- Monitoring and controls for changes to risk levels.
- Ensuring that existing procedures that are being relied upon are effective in addressing the identified risks when considered against the six principles.

9.4. Other key features of a risk assessment

Level of detail

There is not a single approach to determine the level of granularity, and financial institutions may wish to consider country, business units, products or customer segmentation when determining the right approach for them.

As the risk assessment will determine the need for controls to manage risks identified, financial institutions may wish to follow their internal business structures to best align risks, and resulting actions to the owners of those actions within the business itself.

Ownership

Ownership of the risk assessment is likely to be an important consideration both during initial compliance with the rules and in terms of longer term business as usual.

Documentation

It is critical that the risk assessment, the conclusions and any actions which result are clearly documented. In the event that both the underlying and facilitation offences happen in the future, the financial institution will need to be able to demonstrate that its approach to compliance with the offences was reasonable, and the risk assessment will be the first step in that process.

Review and integration

Risk assessments will need to be refreshed or validated on a periodic basis. The frequency of review is likely to be linked to the inherent facilitation of tax evasion risk within the business.

It is likely that the initial risk assessments undertaken by the firm where needed, may be performed 'off-cycle' compared to ongoing reviews.

It is anticipated that in the longer term some organisations, in particular those who are lower risk, may want to integrate the risk assessment for tax with those required in other areas.

Reviews may also be required where new information is discovered which was not considered as part of the previous risk assessment. For example, the discovery that an employee has been routinely circumventing controls may trigger a review of the business and control environment. Other triggers for review may be any significant changes in legislation or business activity including development of new products, new services or propositions. Consideration should be given to making tax evasion and tax evasion facilitation risk assessments an integral part of the product or business development sign-off process.

Financial institutions may wish to consider whether additional independent review, which may be by an internal audit or other compliance function, of the risk assessment is helpful.

9.5. Requirement for tax knowledge

One of the key elements of the predicate offences of tax evasion and facilitating tax evasion are that there is dishonest or deceptive conduct involved. This is an offence about fraud rather than non-compliance with technicalities of the tax code. This aspect of the risk assessment does not necessarily require acquiring specialist tax knowledge.

It is not expected that risk assessments (or any controls which are required) will be reliant on a detailed knowledge of tax law. The new offences relate to the criminal facilitation of tax evasion, that is fraudulent or dishonest conduct; they are not about ensuring compliance with technical aspects of tax law.

However it is expected that firms will know the specifics of their own product/services, how these are offered and use that knowledge to determine the risks of a tax evasion facilitation offence being committed.

The Government's Bribery Guidance states that those tasked with the risk assessment must have the necessary internal authority, resources, skills, knowledge of the business and objectivity to perform the task competently. A similar requirement might be expected in respect of these offences.

Beyond that, financial institutions should consider whether it is reasonable to conduct risk assessments without tax resources given the scale and complexity of their business. The availability of tax resources may itself be a factor in the consideration of reasonableness. Businesses would be prudent in deploying

and making use of their resources when conducting their risk assessment, including any in-house tax resource at their disposal.

Businesses which are not clearly low risk may require some level of tax knowledge in defining the risk assessment and the involvement of individuals with specialist tax knowledge may well assist in the risk assessment process. The risks to be identified are the risks of dishonest behaviour where the dishonest conduct is the facilitation of tax evasion. Therefore, while specialist tax knowledge will be a useful input to the process it is not expected to be the only input into the design of the risk assessment process. Where tax specialists are involved, and/or for organisations with tax specialised functions, the involvement of tax resources at the scoping phase (assist in defining) and the sign-off phase (participating in the review of the results of the risk assessment) may be a relevant factor in determining whether the procedures put in place are reasonable.

Tax knowledge and non-UK tax evasion

As noted in chapter 4 above, the offence described in chapter 3 will be committed where the tax evasion offence is a criminal offence in both the country whose tax is evaded, and would also be criminal if it took place in the UK.

When considering the risks for the evasion of non-UK tax, institutions based in the UK are likely to find it easier to focus on the UK element of the offence, and ask the question 'if the offence had occurred in the UK or had it involved the evasion of a UK tax liability, would it have been a criminal offence under UK law?' If the conduct would not be criminal if conducted in the UK then the foreign tax corporate offence will not be committed. Very broadly, the essential ingredient to all of the relevant tax evasion offences under UK law is the deliberate and dishonest behaviour on the part of the facilitator and taxpayer. If there is no dishonest behaviour, it is unlikely that the UK element of the offence would be met.

That approach should allow a consistent standard to be applied to the risk assessment and controls needed under the offence.

9.6. Conducting a risk assessment –indicative approach

There is no single way to conduct a risk assessment, and as noted above, financial institutions may have their own tailored approaches which are suitable for their businesses, or may already have conducted risk assessments with address facilitation of tax evasion risks. Where that is not the case, one proposed approach is indicated below.

Example of an approach:

1 **Define approach** - Establish the basic mechanism to perform the risk assessment to ensure it is practical, manageable, consistent and fit for purpose across the whole organisation. Document this process, obtain senior management approval and communicate the requirements.

2 **Evaluate inherent risk** - an audit or 'deep dive review' of the business to determine the scope and risk profile of the business in question, internal and external relationships, etc. *(see the end of this chapter for inherent risks identified as part of existing risk assessments)*

3 **Assess the control environment** - an evaluation of the extent to which existing controls to prevent other financial crime adequately address risks. Consider whether the controls are working as designed (operating effectiveness) and whether the design is right to reduce the risk of facilitation of tax evasion to an acceptable level (design effectiveness)?

4 **Determine the residual risk** – Determine the extent to which the existing control environment eliminates the inherent risk. Whatever remains is the residual risk, and the extent of that residual risk will determine the next steps.

Is any residual facilitation risk sufficiently low for no new controls to be necessary?

Yes

5 **No further action required –** The Government guidance recognises that it may be reasonable for no additional controls to be implemented in low risk businesses, or where existing controls effectively address identified risks *Note that this would be unusual for financial institutions.*

No

Action planning - Develop action plan/s to mitigate any gaps identified related to residual risk.
This could include actions planned to address gaps, prioritisation, budget and resource requirements, owners and delivery dates

6 **Sign-off** – the risk assessment and action plan should be approved by an accountable executive within the business in question. Consideration may be given to additional review by a senior manager with sufficient skill and experience to challenge the findings if necessary. The ownership of the risk should be agreed at this stage.

7 **Review** – Timetable an appropriate date for reviewing the risk assessment based on Inherent and Residual risk ratings. Higher risk areas may be subject to more frequent revalidation or review than low risk businesses but even the highest risk business will not need more than an annual risk assessment review requirement. It may be necessary to revise the risk assessment if a risk event occurs or there some other material change in circumstances.

9.7. Interaction with Risk assessments under Bribery Act 2010

The Government's Bribery Act 2010 Guidance identifies five key risks in determining the inherent risk of an offence which are specifically referenced in HMRC's guidance.

Country risk – Certain countries are likely to be considered higher risk than others, both in terms of the location of the underlying party who may commit the predicate offence, and the location of any associated person. Financial institutions may wish to use tax transparency ratings or lists of high risk tax jurisdictions, which might include lists published by the OECD or transparency NGOs which are kept updated. Financial institutions may wish to consider, amongst others – black lists issued by the OECD, countries named by FATF, IMF Offshore Financial Centres List, and countries who have not adopted the Common Reporting Standard.

Sectoral risk – Risk assessments may consider high and low risk factors which apply to the specific sector or service being provided – identifying both lower risk businesses (for example, retail banking, execution only share dealing, pension business) and higher risks (for example, banking trust services).

Transaction risk – Transaction risks will be a factor in the determination of risk of an associated person facilitating tax evasion, but will have a different character and influence on risk than those under the Bribery Act or Money Laundering Regulations in that transaction risk is focused on the risk that an associated person will be able to utilise a transaction to facilitate the underlying tax evasion offence.

Business opportunity risk – such risks might arise in high value projects or with projects involving many parties, jurisdictions or intermediaries.

Business partnership risk – This would apply to the services provided by associated persons, as some services will be inherently higher risk than others.

9.8. Other risks to consider

In addition, the following risks may be important considerations.

Note that these risks are potential 'lenses' though which the overall risk for a financial institution may be considered during the risk assessment. Some risks may be more or less relevant to a business's activities and many overlap. It may be more useful to focus extensively only on those most relevant to the business. Some examples of this approach are included in chapter 9.11 below.

Cultural risk – Whether there are specific internal factors which increase risk – which could include bonus culture, excessive risk taking, an absence of tone from the top, lack of clarity and controls. For example, are associated persons including employees inadvertently or deliberately incentivised to facilitate tax evasion?

Customer risk – As most organisations are customer-focused, a factor to be considered in the risk assessment is the risk inherent in the interaction of associated persons with customers. There are likely two connected elements; the risk that the customer will commit a tax evasion offence and the risk that the evasion offence will be criminally facilitated by an associated person.

Tax Risk – Different taxes may be at a greater risk of evasion for each particular business. A business might face significant risks in respect of some taxes (for example income tax and VAT) but less risk in respect of other taxes (such as landfill tax or aggregate levy). The prevention procedures that are reasonable in respect of the criminal facilitation of the evasion of one tax might to different to those in respect of another tax. Businesses should focus their prevention procedures on the risks relevant to their activity.

Product risk – HMRC's guidance identifies product risk, as certain products and services may have a higher risk of misuse by either clients or associated persons. For FIsFIs, this is likely to be covered by an assessment of sectoral risk.

Risk arising from the level of involvement – Businesses which have a greater level of involvement with a person would be at a greater risk of being able to facilitate tax evasion.

For example, a business that merely provides current accounts to retail customers on standard terms would be a lower risk than a business which provides bespoke wealth management services and is involved in assisting a customer in organising their financial affairs.

Further factors

The Government's Bribery Act Guidance also identifies key internal risks in determining the inherent risk of an offence, some of which are likely to be key risks indicating the risks of facilitation of tax evasion:

- deficiencies in employee training, skills and knowledge.
- bonus culture that rewards excessive risk taking.
- lack of clarity in the organisation's policies on, and procedures for reporting incidences of tax evasion or facilitation of evasion.
- lack of clear financial controls.
- lack of a clear anti-evasion facilitation message from the top-level management.

9.9. Businesses likely to be low risk

There are no fixed rules for which businesses will be low risk. Instead, there are a number of key considerations which may be relevant to the determination of the risk. The list below is not exhaustive, nor is it determinative – a financial institution may identify one or more factors below and still determine that it is higher risk if other factors exist. The below is not a substitute for conducting a risk assessment specifically for the financial institution.

There are likely to be inherent risks within the financial service sector which do not exist elsewhere. References to low or lower risk within this guidance are intended to mean low risk within the financial services sector, and mirror the terminology used in other areas such as the JMLSG guidance.

Although the offences relate to the risk of the criminal facilitation of tax evasion by associated persons, consideration of the following underlying aspects of the business may assist financial institutions with their risk assessment:

Lower risk indicators –customers:

- Customers who are within scope of a financial institution's FATCA/CRS reporting requirements (and the firm reports these to the relevant authority) to the extent that that would address particular risks of tax evasion.
- Customers who are subject to public disclosure, with particular focus on financial affairs (i.e. listed companies, regulated financial institutions government bodies on the basis that both the risk of tax evasion by those entities, or the facilitation of evasion by associated persons are low.

Lower risk indicators – products:

- Retail banking products (current accounts, saving accounts, mortgages, personal loans, ISAs etc.) provided on standard terms.
- Personal Insurance and Pensions.
- Execution only share dealing.
- Standardised and/or listed products (when compared to bespoke products).
- UCITS and UCITS-like funds.

Lower risk indicators – How is the relationship managed?

- Customers who purchase products or services remotely (e.g. online products) who have little or no contact with associated persons.
- Customer deals directly with the financial institution, and all products/services are offered by the financial institution because the financial institution has more control over the provision of the service which it will consider during the risk assessment.
- Dealing with customers for whom there is little or no possibility to criminally facilitate tax evasion, for example because the customer does not earn enough to pay tax or would be subject to audit.

Applying these lower risk indicators, the following businesses in particular may be lower risk:

- UK retail banking on standard terms where there is little or no bespoke customer contact.
- Financial services provided to companies within a publicly listed group which are provided on standard terms.
- Financial services, such as buying and selling of investments, custody of assets, etc., for customers which are institutional investors, widely held investment funds, or which are managed by publicly listed investment management groups.
- General off the shelf insurance and pensions businesses.

9.10. Businesses likely to be higher risk

As with lower risk factors, there are no fixed rules for which businesses will be higher risk. Instead, there are a number of key considerations which may be relevant to the determination of risk. The list below is not exhaustive, nor is it determinative - a financial institution may identify one or more factors below and still determine that it is lower risk if other mitigating factors exist.

To describe an activity as "higher risk" is not intended to suggest that the activity should not be conducted, it merely stresses the need for appropriate prevention procedures to ensure that the risk is suitably managed.

Although the risk assessment relates to the risk of the criminal facilitation of tax evasion by associated persons, consideration of the following underlying aspects of the business may assist financial institutions with their risk assessment.

Higher risk indicators – customers:

- Complex structures with deliberately opaque ownership/control, involving multiple layers and multiple jurisdictions.
- Customers who are the subject of negative media regarding their tax affairs (but note that customers may have been subject to adverse media coverage in respect of legitimate tax planning and this is not evidence of tax evasion issues). This could include reference to HMRC's own list of deliberate defaulters published here:

  https://www.gov.uk/government/publications/publishing-details-of-deliberate-tax-defaulters-pddd

- Customers who have had historic tax evasion issues (being investigations and/or settlements) with adverse results.
- Customers who reside in High Risk countries, whilst retaining a significant nexus with other countries. without reasonable explanation
- Customers with complicated or opaque financial arrangements, in particular where it is not apparent that the customer is advised by a member of a professional body.
- The customer does not conduct any business activities or operate in the country where it is incorporated or formed; or the account is to be opened or relationship is to be established.
- Customers with a high desire for secrecy in their personal affairs (even if safety issues are cited as the rationale).

- Customers who fail to claim repayment or reduction of material withholding taxes, to which they would otherwise be entitled as legitimate tax payers.

Higher risk indicators – products:

- Bespoke products or services rather than standardised off the shelf products.
- Wealth Management
- Creation of Trusts/companies and fiduciary services
- Provision of nominee companies with directors/trustees
- Wealth/Private banking business, particularly where investment and tax planning advice are either part of the service provided, or referrals to third parties for such advice are made.

Higher risk indicators – associated persons and how the relationship is managed:

- The relationship is managed by an employee of the firm, but lacks meaningful oversight by the firm
- Employees are incentivised to sell products/services to customers regardless of the suitability of the product or the risk potentially posed for encouraging facilitation
- When combined with other factors, controls are largely manual and could be easily bypassed by staff
- Relationship, or part of it, is managed via a third party on behalf of the firm
- A third party of the firm responsible for managing/introducing the relationship is from a high risk third country

9.11. Application of risk assessment to particular businesses

Retail banking and building societies - Retail products on standard terms are likely to be at the lower end of the spectrum for this higher risk sector as there is limited scope for the underlying offence to take place through the use of products themselves and limited opportunities for an associated person (likely an employee in the case of a retail business) to facilitate tax evasion. This will particularly be the case for cash savings and current accounts, mortgages and credit cards. However, many retail businesses will offer a wide range of products and will need to evaluate whether any product offered is higher risk of being used for tax evasion, and how its 'associated persons' deliver these higher risk products. Retail businesses should also consider whether engagement with particular customer segments increases the risk.

Large Corporate Banking - Businesses who deal solely with listed companies, or regulated financial institutions may also consider that they are lower risk, as the risk of those customers committing a tax evasion offence is constrained, including by the fact that these companies are often audited by reputable professionals. However, the products offered in such circumstances are generally more sophisticated than in retail banking and should therefore still be risk assessed in detail, as there may be a higher risk of associated persons criminally facilitating any evasion that may take place. It is also

noted that that such firms may be exposed to customers from high risk countries, which may increase the risk exposure faced by firms.

Insurance and Pensions businesses - businesses which only offer general insurance, those who offer non-investment life insurance and pensions business are likely to be lower risk as there is both limited scope for the underlying offence to be committed and low risk of facilitation by associated persons. However, many insurers offer a diverse range of products to a wide range of customers and will need to assess whether this increases the risk within their business.

Banks who provide limited services to corporate customers – banks which are direct-to-market and so do not rely on anyone other than their own employees to deliver their products and services. They do not have any retail customers, and do not provide any current account banking or transactional services for customers. They do not offer any over-the-counter branch-based services, or any cash withdrawal services, direct debit or credit arrangements, or credit or debit cards. The bank predominantly undertakes funding activities in the exchange-traded market for the bank's own account.

They may offer some limited products to corporate customers (such as lending or deposit-taking) but, not with any associated transactional services such as cash withdrawal, direct debits or credits, debit or credit cards, etc. Consequently, their activities would be expected to be lower risk overall with their main risk exposure arising from dishonest activities by employees. As most risks would also give rise to AML or other legal breaches, existing controls will likely be an important part of establishing reasonable prevention procedures.

Assuming that no other associated persons are identified the bank would also, therefore, not consider itself to have any persons delivering its products or services for or on its behalf and would, therefore, consider its associated persons to be limited to its employees.

Banks dealing with small businesses and sole traders – businesses who deal primarily with smaller businesses (for example those who are not subject to an audit), sole traders, or other businesses which deal primarily in cash transactions may consider that the inherent risk related to the customer committing a tax evasion offence is higher than for other customers. Having conducted a risk assessment, the bank would need to implement prevention procedures mitigating the risk that an associated person could facilitate tax evasion. The prevention procedures required will vary depending on the services provided and the proximity between the associated persons and the business

Issues that may be specifically relevant to the fund management sector

The factors a particular business should consider in performing and implementing the risk assessment and adopting reasonable prevention procedures will depend upon the nature of its operations. Each business should analyse its position by reference to its specific facts and circumstances.

These issues may be specifically relevant to businesses in the fund management sector:

- Risks relating to investors - shares or interests in funds may be open to general subscription or to purchase by any qualifying investors, or only by a closed group of investors for whom the fund is established. Investors represent the ultimate source of fund capital.
- Risks relating to investing structures used by investors.
- Risks relating to the nature of investments.
- Investment jurisdiction risk.
- FIN48/ASC740-related risk involving the investment manager as the associated person of the fund.
- Business culture and product risk in connection with fund entities, especially relevance (if any) to funds established in common no/low tax fund domiciles.
- The different types of fund marketing involving third parties, including which types of marketer or distributor are or are not associated persons of the fund.
- Bonus structures for associated persons, such as marketing or distribution teams.

9.12. Reasonable procedures for relevant bodies when dealing with Financial Advisors

When conducting their risk assessment, relevant bodies may wish to consider the following types of risk.

The type of product being sold and the degree of interaction between the FA and the provider

If the product being sold is a standard, off-the-shelf product with no tailoring for the FA's business model then it will normally be lower risk.

Products which are not investment products, for example general insurance policies, do not have a cash value and do not give rise to taxable receipts outside of a trading context. There will be a lower risk of such products being used to facilitate evasion by the customer.

If the product is bespoke or the FA is a sole distributor then there is an increased risk that the FA will be acting as an associated person. For the provider reasonable prevention procedures should include ensuring that it carries out appropriate due diligence processes on the FA to establish their commitment to maintaining appropriate controls to counter facilitation of tax evasion. This should be supported by regular reviews of the relationship to ensure that the FA is meeting this commitment.

Geographic locations of the FA and / or customers

UK intra-jurisdiction services present a lower risk of being used to a facilitate tax evasion because the products are sold to UK residents only and they are subject to regular reporting to HMRC in the normal course of business.

Where a client emigrates since purchasing a product and this presents an increased risk of non-compliance the risk will be in part mitigated by FATCA and AEOI reporting in relation to relevant clients.

However, it is possible for there to be greater risk of the facilitation of tax evasion where products are being packaged and sold offshore. Non-domestic locations may indicate an increased risk of products being used to evade UK or foreign tax obligations. This increased risk will need to be considered when carrying out the risk assessment and determining what is the appropriate level of due diligence applicable to the FA to mitigate any such risks. Some locations are higher risk than others (see JMLSG guidance).

Target Market

If the FA proposes to target high net worth customers specifically then, alongside any potential Politically Exposed Persons (PEP) risks, the firm should consider the potential that its products or services could be used to assist in creating complex or opaque structures to be used to evade tax. In such circumstances the sale of the product might amount to the criminal facilitation of tax evasion.

Relevant bodies will need to put in place procedures to address this risk. The firm may, for example, consider applying enhanced customer due diligence requirements for individual investments. For very high-risk transactions, this might include requiring independent tax advice regarding the transaction and the client's tax status. In addition, regular monitoring of the usage of the service (perhaps in conjunction with AML monitoring) is advisable.

On the following pages, relevant extracts of the JMLSG Guidance have been reproduced. Whether these extracts are relevant to a particular financial institution will depend on the approach they are taking to compliance. These chapters are therefore for information only.

JMLSG Guidance – assessment of risk (4.32)

Underlined entries indicate areas which are likely to be of most use in determining whether a business is at risk for the criminal facilitation of tax evasion

What risk is posed by the firm's customers? For example:

- Complex business ownership structures, which can make it easier to conceal underlying beneficiaries, where there is no legitimate commercial rationale.
- An individual meeting the definition of a PEP.
- Customers (not necessarily PEPs) based in, or conducting business in or through, a high-risk jurisdiction, or a jurisdiction with known higher levels of corruption or organised crime, or drug production/distribution.
- Customers engaged in a business which involves significant amounts of cash, or which are associated with higher levels of corruption.
- Customers engaged in industries that might relate to proliferation activities.

What risk is posed by a customer's behaviour? For example:

- Where there is no commercial rationale for the customer buying the product.
- Requests for a complex or unusually large transaction which has no apparent economic or lawful purpose.
- Requests to associate undue levels of secrecy with a transaction.
- Situations where the origin of wealth and/or source of funds cannot be easily verified or where the audit trail has been deliberately broken and/or unnecessarily layered, and
- The unwillingness of customers who are not private individuals to give the names of their real owners and controllers.

How does the way the customer comes to the firm affect the risk? For example:

- Occasional transactions v business relationships.
- Introduced business, depending on the effectiveness of the due diligence carried out by the introducer.

What risk is posed by the products/services the customer is using? For example:

- Can the product features be used for money laundering or terrorist financing, or to fund other crime?
- Do the products allow/facilitate payments to third parties?
- Is the main risk that of inappropriate assets being placed with, or moving from, or through, the firm?
- Does a customer migrating from one product to another within the firm carry a risk?

JMLSG Guidance – low-risk factors (4.37-4.41)

Customer risk factors

- Other regulated firms and other bodies, where they are subject to requirements to combat money laundering and terrorist financing consistent with the FATF Recommendations, have effectively implemented these requirements, and are effectively supervised or monitored to ensure compliance with those requirements.
- Public companies listed on a stock exchange and subject to disclosure requirements which impose requirements to ensure adequate transparency of beneficial ownership.
- Public administrations or enterprises.

Country or geographic risk factors

- Countries identified by credible sources as having effective AML/CTF systems.
- Countries identified by credible sources as having a low level of corruption or criminal activity.

Product, service, transaction or delivery channel risk factors

- Life assurance policies where the premium is low.
- Insurance policies for pension schemes if there is no early surrender option and the policy cannot be used as collateral.
- A pension, superannuation or similar scheme that provides retirement benefits to employees, where contributions are made by way of deduction from wages, and the scheme rules do not permit the assignment of a member's interest under the scheme.
- Financial products or services that provide appropriately defined and limited services to certain types of customers, so as to increase access for financial inclusion purposes.

JMLSG Guidance – high-risk factors (4.34-4.36)

Customer risk factors

- The business relationship is conducted in unusual circumstances.
- Non-resident customers.
- Legal persons or arrangements that are personal asset holding vehicles.
- Companies that have nominee shareholders or shares in bearer form.
- Business that are cash intensive.
- The ownership structure of the company appears unusual or excessively complex.

Country or geographic risk factors

- Countries identified by credible sources as not having adequate AML/CTF approaches.
- Countries subject to sanctions, embargoes, or similar measures issued by, for example, the UN.
- Countries identified by credible sources as providing support for terrorist activities, or that have designated terrorist organisations operating within their country.

Product, service, transaction or delivery channel risk factors

- Private banking.
- Anonymous transactions (which may include cash).
- Non face-to-face business relationships or transactions.
- Payment received from unknown or un-associated third parties.

Firms should examine, as far as reasonably possible, the background and purpose of all complex, unusual large transactions, and all unusual patterns of transactions which have no apparent economic or lawful purpose.

10. Proportionality

10.1. Overview

A financial institution's procedures to prevent the criminal facilitation of tax evasion by persons associated with it should be proportionate to the risks it faces and to the nature, scale and complexity of the organisation's activities. The procedures should also be clear, practicable, accessible, and effectively implemented and enforced.

The requirement for proportionality in procedures means that a risk assessment, as discussed in Chapter 9, is important, informed by the size of the financial institution, its structure, the scope and nature of its activities and its associated persons.

Where the risk assessment identified no significant new risks existing procedures may not need to be enhanced if they adequately address the risk of criminal facilitation of tax evasion. In addition, there is no requirement for new or standalone procedures to be established. Instead, depending on risk appetite, senior management may decide to otherwise apply resource to, for example, enhancing prevention procedures in existing arrangements; prevention procedures may be specifically developed or integrated into existing arrangements.

10.2. The meaning of 'reasonable'

The Act provides no definition of 'reasonable' in the context of procedures to prevent the criminal facilitation of tax evasion and HMRC guidance in this area accepts that there is no single 'one size fits all' solution. It sets out that there will likely be a considerable variation in what reasonable looks like across financial institutions depending on the size, nature and risk profile of the business concerned and the risks it faces.

Prevention procedures adopted should be proportionate to the risk that an associated person may criminally facilitate tax evasion, a risk that should have been identified through its risk assessment procedures. In addition to these considerations, the organisational structure will influence the approach taken to the implementation of procedures and their level of sophistication.

'Reasonable prevention procedures' will therefore be unique to each business, although they are also likely to take account of any specific market or industry thematic risk, when identified from information on prosecutions or regulatory activity which is in the public domain. The Risk Assessment conducted by the business will be key to determine and justify the proportionality of any procedures to the risks identified. The rationale for any decisions should be appropriately documented.

10.3. HMRC's view of the risk based approach

HMRC's guidance indicates that reasonable prevention procedures *"…will depend on the nature, scale and complexity of the relevant body's activities. The new offences do not require relevant bodies to undertake excessive due diligence but does demand more than mere lip-service to preventing the facilitation of tax evasion. "*

HMRC's guidance also indicates that *"the new offences do not require relevant bodies to undertake excessively burdensome procedures in order to eradicate all risk, but they do demand more than mere lip-service to preventing the criminal facilitation of tax evasion.".*

With HMRC's guidance in mind, an organisation's procedures to prevent the criminal facilitation of tax evasion should be proportionate to the risks it faces and to the nature, scale and complexity of the organisation's activities.

In particular, this would apply in the situation where an organisation has implemented a system of controls that identifies and mitigates its risks associated with the facilitation of tax evasion but an instance of such facilitation takes place notwithstanding those controls. If the controls implemented are proportionate to the identified risks, then the firm will be well placed to make out the defence.

HMRC's own guidance states that:

> *"The Government recognises that any regime that is risk-based and proportionate cannot also be a zero-failure regime. If a relevant body can demonstrate that it has put in place a system of reasonable prevention procedures that identifies and mitigates its tax evasion facilitation risks, then prosecution is unlikely as it will be able to raise a defence."* (paragraph 1.1)

In considering what is proportionate to the risks identified, financial institutions may also consider practicality, including: the amount of resource spent in terms of time, people, and money. What is reasonable will be determined not only the risk faced by an organisation but also what can practically be achieved to manage this risk. Achieving the impossible is not something that can be reasonably required.

10.4. Application to lower risk businesses

For lower risk businesses, the application of proportionality considerations will interact with the controls, policies and procedures already in place. See Chapter 7 for more details.

10.5. Proportionality and third parties

Proportionality is of particular relevance when dealing with third parties who are associated persons.

It is important to recognise that many associated persons are third parties who by definition operate to some extent independently of any financial institution on whose behalf they may provide services.

Associated persons may also be outside the UK, and particularly in the case of the foreign tax corporate offence this could pose the UK entity challenges in implementing reasonable prevention procedures in respect of the offence. However, these cases will still need to be addressed.

In these cases, practicality is likely to be an important part of any considerations on proportionality; financial institutions will need to consider what procedures may reasonably be applied to associated persons who operate independently. HMRC's guidance specifically includes consideration of the proximity between entities and third parties as part of the consideration of reasonable controls. Such procedures are included within the due diligence on associated persons in chapter 12 below.

11. Top-Level Commitment

11.1. Top-level commitment

In its guidance on the new corporate offences, HMRC defines 'top-level commitment' as:

> *'The top-level management of a corporation are committed to preventing persons associated with the corporation from engaging in criminal facilitation of tax evasion. They foster a culture within the corporation in which activity to facilitate tax evasion is never acceptable.'*

In the context of money laundering, Paragraphs 1.41-1.45 of the JMLSG Guidance set out a clear requirement for regulated firms to establish a *"formal policy in relation to financial crime prevention"* and goes on to state that *"senior management must be fully engaged in the decision making processes, and must take ownership of the risk-based approach, since they will be held accountable if the approach is inadequate"*. This is similar to the requirements under the Bribery Act and HMRC expects senior management to take a similar approach to the new corporate offences.

As such, top-level commitment could be an extension of these existing policies and procedures, particularly as the commitment to prevent financial crime already includes identifying the risks of handling the proceeds of tax evasion. Even where risks of tax evasion facilitation are low, tone from the top is essential to fostering the correct culture and awareness of the offences amongst associated persons. However, it is more likely in the case of lower risk businesses that existing statements made by senior management about financial crime generally may suffice without any need for a statement expressly referencing tax evasion facilitation.

A new or revised top-level commitment may not be needed in all cases. For some organisations, it may be proportionate to ensure that top-level commitment already includes a commitment to the prevention of financial crime including tax evasion. Other organisations may already have considered and issued appropriate statements which address facilitation of tax evasion risks.

For most organisations, it is expected that the top-level commitment could best be enacted and documented as an extension to existing commitments made under the anti-money laundering processes, the prevention of other financial crime and or commitments to ethics and culture.

A firm's preferred approach should make clear who is accountable and responsible for identifying and responding to the risks of the criminal facilitation of tax evasion. The accountable and responsible persons should also have the authority and access to information and resource, necessary to discharge their responsibilities.

The FCA has increasingly taken a view that 'tone from the top' alone will in itself be insufficient for improving ethical and behaviour standards, and in addition the FCA will increasingly be looking towards '**tone in the middle'** as a way of translating tone into actions which are observable on the ground.[2]

[2] FCA chairman, John Griffith-Jones speaking at the annual meeting of the Chartered Institute for Securities and Investment, 3rd July 2013

Similarly, HMRC has indicated the importance of making sure that tone from the top is delivered in practice out in the business. In line with the FCA's approach to conduct risk generally, HMRC's guidance states that:

> *"Communication should be from all levels within an organisation, i.e. it is not enough for the senior management to say that staff should not commit fraud, if middle management then actively ignore this and encourage junior members to circumvent the relevant body's prevention procedures"* (considered in Chapter 13)

11.2. Tone from the top

Senior management are ultimately responsible for fostering a culture with zero tolerance for the criminal facilitation of tax evasion by employees and setting the example in terms of integrity, stewardship and appropriate behaviours (i.e. 'tone from the top').

Senior managers may wish to issue a statement of commitment to the countering of tax evasion risks and the prevention of the criminal facilitation of tax evasion within the organisation. Alternatively, whilst the new corporate offences may initially attract specific attention (e.g. senior management issuing a communication announcing new procedures to comply with the new corporate offence), it may form part of the general senior commitment to preventing financial crime and other wrongdoing.

Such a statement should clearly define and communicate the zero-tolerance approach; the culture and attitude; the penalties and disciplinary processes in place for non-compliance and the support mechanisms and whistleblowing procedures that the organisation will provide in order to achieve these objectives.

Consideration may be given to making these policies, statements and training resources available to business partners where applicable, and this may be an important part of communicating the financial institutions approach to associated persons. Senior managers may consider whether this statement could be made public or communicated to other third parties which may include regulators or employee representatives such as trade unions.

The responsibilities of all staff from senior management (including non-executive directors), to general staff and associated persons should be clearly explained and communicated.

11.3. Application to lower risk businesses

Top-level commitment and tone from the top may not differ substantially for lower risk businesses. Even where risks of tax evasion facilitation are low, tone from the top is essential to fostering the correct culture and awareness of the offences amongst associated persons.

However, it is more likely in the case of lower-risk businesses that existing statements made by senior management about financial crime generally may be deemed sufficient to address any risks identified. This may be because controls that are proportionate to the risk exposure of the firm are already in place. It may also be because of the modest proportion of exposure that tax evasion facilitation presents when considered with the controls that are in place for financial crime more generally and due to its lower risk profile compared to the other financial crime exposures of the firm.

11.4. Governance structure

An organisation should have clear accountability for the management of risk within it. In practice to support the 'tone from the top' and 'tone from the middle' which financial institutions may use their existing oversight structures, including committees and audit functions, so as to drive forward their programmes via appropriate, regular review.

In large organizations, responsibilities of the board will be delegated and therefore, having tax evasion and the facilitation of tax evasion by associated persons "on the agenda" may mean that is the focus of appropriate senior management reporting to the board, rather than the board itself.

A clearly-defined governance structure may incorporate the following:

- Clearly-defined ownership and accountability within senior management.
- A code of ethics and a code of conduct.
- A risk assessment – for the organisation as a whole, its businesses, the jurisdictions in which it operates and the types of its associated persons (see Chapter 9 on Risk Assessment).
- Resourcing levels appropriate to the organisation's risk appetite.
- Appropriate policies and procedures.
- Governance arrangements with regards to relationships with associated persons.
- Recognition that management of risks should be embedded in all activities of the business.
- The interaction of different support functions and how they are coordinated.
- An analysis of how the group interacts with UK and overseas subsidiaries and branches and how much autonomy is devolved to local management.
- Suspicious activity reporting, insomuch as the firm could detect the deliberate failure of an employee to report suspicious activity in order to facilitate an underlying tax evasion offence.
- A system that encourages the transparency of transactions and interactions that may encourage associated persons to criminally facilitate tax evasion.
- A system for how incidents and risks are escalated, recorded, investigated, reported and managed.
- Training, including targeted training where individuals are involved in providing tax advice or related services.
- Speaking up/whistle-blowing procedures and protection of whistle-blowers.
- Review processes, including assurance, audit and management information.

11.5. Practical case studies

The case studies below may be useful in considering the 'tone from the top' where they are appropriate to the risk and scale of the organisation, but other approaches will be equally valid and the below should not be viewed as minimum standards.

Have champions

In practice, the appointment of one person or putting reliance solely on the board may not be the most efficient way to drive tone from the top. This is particularly true for larger global institutions. To overcome these hurdles some banks have introduced business line champions, for example Nominated Senior Managers who are responsible for recognising facilitation risks in their business.

Champions could be:

- Individuals who are sponsored by Board members or Managing Directors.
- Individuals with sufficient seniority to carry out the role.
- Individuals formally nominated or appointed to the role.

Governance: equipping senior management

Consideration may include support which enhances senior management's ability to fulfil their role, and may include:

- Senior management face-to-face training and induction sessions.
- Incorporating responsibility and accountability for compliance with the corporate criminal offence into the job description and objectives of senior management.
- Board members and senior staff openly discussing the consequences of not taking appropriate action, using forums such as: annual conferences, training events, listening events i.e. breakfast meetings and listening lunches.
- Induction sessions.

Setting the correct tone from the middle:

- Division- or country-wide communications issued by senior management / the board.
- Endorsing training sessions and ensuring that there are consequences for non-completion of the course.
- Supporting the exiting of relationships with associated persons deemed to present unacceptable tax evasion risk.
- Securing appropriate resource to manage tax evasion risk.
- Ensuring that commitment to new controls are included in annual plans or employee scorecards where appropriate.
- Promoting whistleblowing mechanisms.
- Communicating repercussions for non-compliance.

12. Due diligence on Associated Persons

12.1. Identifying associated persons who are not employees

As the offences relate to the facilitation of tax evasion by associated persons, financial institutionswill need to ensure they have controls in place that enable the identification, risk assessment and mitigation of risks posed by associated persons.

Chapter 6 (above) sets out the key criteria for determining whether someone is or is not an associated person. This chapter focuses on the due diligence and other controls which can be applied to those persons identified as associated persons.

12.2. Risk assessment and due diligence on associated persons who are not employees

The potentially large numbers of associated person relationships and the wide range of services they provide for a financial institution will likely necessitate a risk-based approach to mitigating and managing the tax facilitation risk. This approach is in line with World Economic Forum guidelines on conducting due diligence on associated parties which states *"the key to effective third party due diligence is knowing which third parties pose the most risk to the organization and targeting them for thoughtful review"*.[3]

A risk-assessment mechanism, similar to that of the customer risk assessment, may assist with the assessment of risks of associated persons new to the firm. Overall levels of due diligence conducted on associated persons will vary according to certain risk factors. In some cases, a 'bucket' approach to classifying third party relationships (where relationships are classified as high, medium or low risk) has been viewed as a proportionate approach.

The level of risk associated with a third party relationship will vary according to certain factors including but not limited to:

- The proposed role of the associated person and the nature of the service being provided.
- The country or location of the associated person or intended transaction and whether or not cross-border activities are anticipated and are in line with expectations.
- Existing knowledge of the associated person.
- The amount of proposed consideration or payment to the associated person and whether it is proportionate to the tasks required and/or in line with market rates.
- Whether there are lower or higher risk indicators (considered below).
- The transparency and reputation of the associated person, including their relationship with regulators.
- The presence of a potential conflict of interest e.g. a party involved may be friend or relative of an employee who facilitates or advises on a transaction.

[3] World Economic Forum 'Good Practice Guidelines on Conducting Third Party Due Diligence' 2013.

Proportionality and proximity are key considerations in considering the application of these rules to third parties. See Chapter 10.5 for discussion of the interaction between the proportionality requirement and due diligence on associated persons.

Lowerrisk indicators

Save where an associated person might be (or previously has been) linked to adverse publicity with regards to tax evasion or a nexus with economic crime, some fact patterns may suggest that an associated person is lower risk, including:

- Where the associated person is a legal entity falling within the definition of a "relevant body". It is therefore required to comply with the Act. This may apply in particular for associated persons who are financial institutions in the UK, or are specifically covered by similar industry specific guidance in respect of the Act
- Where the associated persons are overseen by a regulatory authority, who would view engagement in tax evasion as grounds for disciplinary or removal action
- Where all of the activities being undertaken by the associated person, or the customers with who they engage, would fall into the lower risk categories identified in 9.9 above provided their activities are controlled so that they cannot act outside of their role.

Higher risk indicators

Some fact patterns may cause an associated person to be viewed as higher risk, including where one or more of the following example considerations are encountered:

- The associated person insists on operating in anonymity or through its actions indirectly creates anonymity though the use of a complex corporate structure which hinders the completion of due diligence (note – the existence of a 'complex' corporate structure is not of itself necessarily an indication of higher risk where the structure is fully explained and does not give rise to anonymity).
- Due diligence identifies significant past allegations or incidents of fraud, corruption, tax non-compliance or illegality, including money laundering or an offence under either s.45 or s.46 of the Act itself.
- The associated person has used the services of a number of advisers in the past some of whom have been involved in instances of non-compliance and illegality.
- The associated person objects to reasonable clauses in the contract regarding compliance with tax evasion or facilitation laws or other applicable laws.
- The associated person does not reside or have a significant business presence in the country where the customer is located and there is no reasonable commercial explanation for the relationship.
- Where the activities being undertaken by the associated person, or the customers with who they engage, would fall into the higher risk categories identified in chapter 10.10 above.
- The associated person does not operate via clear lines of defence, to mitigate risk in internal controls where, by comparison, its peers utilise such a defence model.

- Regulatory censure against an associated person (or member of its management team) indicating a weakness in the associated person's tax evasion governance and/or other internal governance.

- A conflict of interest (e.g. an employee with a nexus / relationship with an associated person, or a member of the associated person's team involved in a transaction).

12.3. Application to lower risk businesses

For businesses that are a lower risk for tax evasion facilitation purposes, associated persons should still be considered as part of the risk assessment. Without a risk assessment of its associated persons, the decision to apply no or minimal additional prevention procedures cannot be justified, even when the business itself is assessed as low risk. Further prevention procedures should be determined on a risk-based approach and should be kept under regular review.

Where a business falls within the scope of the Act, already has financial crime procedures in place, is assessed as lower risk for facilitating tax evasion, and its associated persons are likewise assessed as lower risk, it may not be necessary to implement any further prevention procedures. Monitoring and regular review of the risks should however still be conducted.

12.4. Associated persons outside of the UK

The fact than an associated person is based outside of the UK should not automatically result in their treatment as higher or lower risk.

Regardless of where an associated person operates, there is a need to consider how associated persons might facilitate tax evasion given the activities which are performed on behalf of the financial institution.

For example, an associated person outside the UK who provides tax-related services on behalf of a UK financial institution to UK taxpayers may be higher risk, and therefore subject to higher due diligence requirements.

On the other hand, an associated person outside the UK who does not deal with UK residents providing services for a financial institution which is also outside the UK, and does not provide services which have an impact on tax may require fewer controls, or indeed no additional controls, to be proportionate to identifiable risk.

Financial institutions may need to give particular consideration to the interaction of these rules with the offence under s.46 of the Act.

12.5. Risk mitigation activities

Once associated persons have been identified, and the inherent risk has been assessed, financial institutions may wish to consider what further due diligence actions, if any, are proportionate to mitigate the risks.

Common risk mitigation activities may include the following where they are appropriate:

- Obtaining certifications, or contractual representations from the associated person in relation to compliance.

- Introducing restrictions on what activities can be performed.

- Approval processes for the distribution of relevant marketing material (i.e. with respect to co-branded products/services, or those offered on behalf of the financial institution).

Where heightened risk factors are present additional due diligence may include:

- Requesting a statement of compliance from the associated persons, which confirms that they have conducted their own risk assessment and, if necessary, implemented or will implement any enhancements to controls as a result. In the absence of any specific reason to doubt a statement that a risk assessment had been conducted and controls put in place, it may well be reasonable for a financial institution to rely on such a statement.

- Performing supplementary background and screening searches on the associated person / the key controllers in charge of its strategy and day-to-day operation.

- The right to review or monitor relevant activities undertaken by the associated person, or the right access to relevant records.

- Obtaining the associated person's policy statement on tax evasion or their statement/procedures for preventing the facilitation of tax evasion.

- Provision of a mechanism for associated persons to raise concerns (e.g. whistleblowing hotline available to external parties) subject to their own privacy requirements.

- Conducting enquiries or specific reviews with associated persons on their management of risks.

- Specific senior management approval/acceptance processes for engaging with persons who pose a higher risk.

- Validating direct requests for information (i.e. references from other firms that the third party has worked for), verifying information through official sources and obtaining independent verification of information obtained.

- Ascertaining the financial standing and credibility of the associated person and determining whether the associated person has a clear and proven track record in their area of service provision.

- Seeking clarification in respect of the associated person's own anti- tax evasion controls and policies, ideally obtaining copies of such policies or requiring a statement of compliance.

- Ongoing due diligence performed by the financial institution which may include periodic checks regarding activities performed and fees paid, with a particular focus on changes of scope.

The assessment of proportionate controls to be applied to an associated person may also include an assessment of the level of control which a financial institution is able to exert over an associated person and therefore the level of risk mitigation which might be proposed.

In addition to considering the assessed level of risk attributed to a particular associated person (or to a class of associated persons), the extent and frequency of due diligence undertaken may differ, between the outset of a relationship and in-life.

The depth of on-going oversight or interaction may be influenced, inter-alia, by:

- Contract or Service Level Agreements entered into with an associated person (e.g. whether the associated person provides management information on completeness of tax evasion training provided to their staff/agents).
- Materiality of a relationship with a particular associated person (e.g. it is likely that a significant or material relationship will involve a relatively higher volume of transactions than, say, a lower volume or lower impact relationship).

12.6. Contractual arrangements

In the case of associated persons who are identified as higher risk, it may be appropriate for written contracts to contain provisions in respect of adherence to the Act and, in some cases, conditions regarding the associated person's policies and procedures.

Changes to contracts are likely to be more appropriate where there are bespoke agreements between a financial institution and the associated person. For higher risk associated persons in particular, financial institutions may wish to consider whether specific training, review and monitoring requirements may be included in contractual terms, or periodic certifications of compliance.

The following are suggested provisions which organisations may consider including in their contracts with associated persons where appropriate:

- A warranty that neither the associated person, nor its employees or agents, has been convicted of, nor entered a settlement with an enforcement agency for an offence involving the facilitation of tax evasion, and is also not listed by any government agency or regulator as debarred.
- A requirement that the associated person will advise of any improper actions known by them in connection with the relationship and will assist in investigating any such allegations and remedying any violations.
- A requirement that the associated person will exercise due diligence in selecting employees or agents in connection with the assignment, will provide appropriate training on them and will monitor their activities.
- A requirement that the associated person will require compliance with restriction of the facilitation of tax evasion from any subcontractors or other entities/individuals who might be regarded as associated persons to the organisation.
- The ability to withhold payment and/or terminate the contract if the financial institution has reasonable grounds to believe that the associated person has violated any of the facilitation of tax evasion provisions.

Where contractual changes may not be proportionate

Changes to contracts will not be proportionate in all circumstances. For example, they are less likely to be proportionate for those which are not commonly subject to negotiation and those where there is a low risk that an associated person may facilitate tax evasion.

In addition, depending on the extent of the risk, it is less likely to be proportionate to make changes to pre-existing contracts, and it may be more appropriate for changes to be made when contracts are renegotiated.

As with the Bribery Act, there may be cases where an associated person outside of the UK is prevented under local law from agreeing contractual clauses which are related to the laws of another country. Alternative approaches, such as a statement of compliance could be used.

12.7. Chains of suppliers

Where a supply chain involves several entities, or a project is to be performed by a prime contractor with a series of subcontractors, a financial institution is likely to only exercise any degree of direct control over its contractual counterparty. Indeed, the organisation may only know the identity of its contractual counterparty. This will make it more difficult to review compliance, impose contractual clauses etc. on entities that are contractually distanced from the financial institution.

The principal way in which financial institutions may address these facilitation risks is by employing the types of procedures referred to elsewhere in this guidance in the relationship with their contractual counterparty, and by requiring so far as is practicable and proportionate that counterparty to adopt an appropriate approach with the next party in the chain, thereby exercising as much control as their limited contractual proximity permits

12.8. Associated persons who are employees

For employees a risk-based approach will be required to identifying employees at risk of facilitating evasion, delivering appropriate training to employees and establishing control systems. Chapters in this guidance related to communications and training, and monitoring and controls are likely to be relevant when considering the application of reasonable and proportionate controls for employees.

12.9. Associated persons who are financial advisors

The following examples may be useful in considering the application of these rules to associated persons who are financial advisors:

Example 1: Single premium Bonds sold via an Offshore Wealth Manager

A significant tranche of single premium investments is sold by an insurer to an offshore Wealth Manager that has indicated that it will distribute those bonds to individual clients. The particular facts of this arrangement means that the offshore Wealth Manager will be an associated person of the insurer.

The clients are not UK based nor are they based in countries that automatically share taxpayer information with the UK (i.e. they are not signed up for CRS). The transaction therefore carries a higher risk due to lack of availability of information of their clients to tax authorities.

The insurer will be provided with clients' names and addresses but the bulk of the KYC for the client is retained by the Wealth Manager to comply with local privacy legislation. The Wealth Manager certifies AML compliance to the Insurer and this is reinforced by compliance monitoring of the documentation underpinning the certification.

To address the identified risk of the single premium investments being used by the wealth management firm to facilitate tax evasion by the client the provider may wish take the following steps:

- Close analysis of the Wealth Manager's business rationale for the distribution of single premium investments, including how the product will be marketed, its target clients and their purported objectives in purchasing the investments (particularly any element of using the product to assist with tax planning),
- Checking the bona fides of the Wealth Manager including in relation to any allegations of assisting tax evasion in the past.
- Checking the Wealth Manager's own internal procedures for ensuring that it does not facilitate tax evasion (possibly as part of a review of its wider AML processes).
- Contractual clause in the agreement between the Insurer and the Wealth Manager where the Wealth Manager undertakes to ensure that it will not facilitate tax evasion.
- Ongoing monitoring of AML compliance to ensure that the process appears to be operated as stated by the Wealth Manager.
- Ongoing monitoring of the client base as the individual policies within the overall tranche of business are sold to identify any concentration risk from a tax evasion perspective.

Example 2 – **non-standard Protection Insurance:**

Property insurance is usually low risk from a facilitation of tax evasion perspective due to the nature of the contract with the client, the need for a specific loss event to occur prior to payment and scrutiny of unusual claims. However, there can be outliers that might need additional consideration. For example:

A property protection policy arrangement has been set up with an UK based FA that services a small group of High Net Worth (HNW) clients, resident in Middle East but with UK property and exposure to UK Inheritance Tax (IHT). The arrangement involves high value assured protection policies to be issued to assist with UK IHT planning for these clients.

The Insurer may wish to consider the following due diligence and other control initiatives that might be considered reasonable steps to prevent the facilitation of tax evasion:

- Checking the reputation of the FA and particularly its experience in this market to identify any regulatory action or censures and allegations of tax evasion.
- Checking that the FA has effective AML and anti-tax evasion policies and controls.
- Contractual clause in the agreement between the Insurer and the FA where the FA undertakes to ensure that it will not facilitate tax evasion.
- Seeking local expert advice that the arrangements do not infringe local tax laws.
- Ensuring that clients are provided with information regarding UK tax obligations.
- Ongoing monitoring of the client base as the individual policies within the overall tranche of business are sold to identify any concentration risk from a tax evasion perspective.

- Ongoing monitoring of policies to identify any unusual or suspicious behaviour that might suggest tax evasion is occurring.

Example 3 – FA receiving some payment from FMC:A third-party financial adviser acts for its clients (investors) while receiving some compensation (commission, retrocession) from the Fund Management Company, as is still often the case outside the UK.

The FA is only an associated person of the FMC with regard to those activities where it is acting for or on behalf of the Company. A risk based approach can be applied once the FMC has identified the activities that the intermediary carries out on its behalf. Having identified any third parties who perform services for or on their behalf (e.g. transfer agents, joint ventures, financial advisers); and the circumstances in which those associated parties may, in acting on their behalf, facilitate tax evasion; the FMC must put in place such prevention procedures as are reasonable.

These may include:

- contractual terms setting out the relationship between the Company and the third party;
- requiring them to have adequate training, education and whistleblowing policies, to prevent their staff facilitating tax evasion;
- permitting the Company to include this issue in their regular assurance program.

13. Training & communication

13.1. Overview

Communication within a financial institution is likely to begin with top-level commitment and the 'tone from the top' as described in Chapter 11 above.

Communication across the organisation may be required to ensure the policies and procedures are implemented in a timely manner and that they are relevant, practical and effective. A demonstrable output should include a good level of understanding and commitment; senior management own and understand the risk and are advocates of the regime; relevant employees are sensitive to risks and therefore monitor them effectively; and invoking the relevant incident management procedures when appropriate (including whistleblowing).

Internal communications should make clear the financial institution's zero tolerance policy towards the provision of illegal services, including the facilitation of tax evasion, by its representatives and the consequences for anyone found to be complicit in illegal activity.

HMRC also note that *"an important aspect of internal communication is an established and confidential means for representatives of the relevant body to raise concerns about the provision of services to facilitate tax fraud. It should be clear to those providing services on behalf of the relevant body whom they should contact within if they have questions or concerns about the services they are providing."*

These internal communications ideally should be issued in the name of, and with full buy-in from, the firm's senior management.

13.2. Application to employees and contractors

Financial institutions will be in a position to apply a higher level of control over employees and those in similar roles than they can over other associated persons.

Staff and employees should be able to access materials which inform them of the financial institution's approach to the Act and reinforce the tone from the top together with an introduction to the Act which is understandable for persons from the non-legal profession (employees at all levels).

Financial institutions may also wish to consider updates to codes of conduct, employee handbooks, job descriptions or performance objectives.

Appropriate training is likely to be a key control which can be applied by a financial institution for its employees and contractors and should be considered as part of the implementation of new or revised procedures under the Act, for future inductions and refresher training.

Training procedures should be proportionate to the identified risks.

It is not necessarily proportionate to provide specific training to all staff on the two offences contained in Part III of the Criminal Finances Act itself, and it may be reasonable to include general references to the risk of tax evasion or the facilitation of tax evasion as part of more general training provided on anti-money laundering, anti-fraud or more general financial crime. Detailed training could be provided for those in higher risk posts/AML teams, including procedures for escalation and investigation, and reporting to the MLRO.

Rather than focus on the details of the offence, it may be appropriate in lower-risk cases for the key message to be that it is not acceptable to deliberately facilitate fraud (including tax fraud); and that faced with such dishonest behaviour, a report should be made via the appropriate channels and business should not merely continue as normal.

However, a financial institution should be able to evidence that appropriate training has been both provided to, and understood and remembered by, relevant staff.

13.3. Application for other associated persons

Communication with external associated persons is likely to be a key part of the due diligence procedures, as discussed in the previous chapter, where appropriate on a risk assessed basis.

Examples of communication with associated persons (outside of contractual language) may include the issuance of a best practices letter or code of conduct, update calls and requirements for periodic certifications.

However, conducting training for a third party is not necessarily expected to be the norm, and may often be impractical or disproportionate. However, there will be cases where the risks are such that it is reasonable. For example, where there is a high risk attached to the associated person, a close connection between them and the financial institution, or where there is a compelling reason why they cannot put their own training programme into place.

13.4. External Communication

Recognising the importance placed on adequately communicating policies and procedures financial institutions may consider the types of material that could be usefully communicated to stakeholders such as:

- Third parties who carry out or promote business on the financial institution's behalf including associated persons.
- Third parties who place reliance on the financial institution to carry out or promote business on their behalf.
- Certain customer groups.
- Other entities for whom the financial institution is an associated person.

In such circumstances financial institutions may wish to consider providing the following information:

- Information setting out the financial institution's stance on tax evasion matters and its facilitation.
- Statements of compliance.

It is not expected that any external documents would contain detailed information of a financial institution's own compliance procedures.

13.5. Application to lower risk businesses

Training and communication requirements should still be considered by lower risk businesses to ensure associated parties are aware of the organisation's approach to facilitation of tax evasion, and the controls put in place by the firm to comply with the requirements of the Act.

It is more likely that a lower risk business may conclude that broader training on financial crime provided to employees that includes references to tax evasion is sufficient for these purposes, or that references to the corporate offences should only be included when the training is next updated.

14. Monitoring and review

14.1. Assessment of controls and monitoring

Monitoring and review is required to ensure policies and procedures are and continue to be appropriate and effective as the environment and organisation develops and that they are complied with.

This is consistent with JMLSG Guidance (paragraph 3.28) which, in the context of anti-money laundering, states that *"A firm is required to carry out regular assessments of the adequacy of its systems and controls to ensure that they manage the money laundering risk effectively"*

Internal audit may be able to integrate independent testing within their existing role. Independent assurance may focus not only on the processes but also the culture of compliance within the financial institution, focusing on aspects such as senior management oversight, training, and the 'tone from the top'.

It is a critical part of compliance that policies and procedures designed to establish reasonable prevention procedures are in fact adhered to and followed.

Financial institutions may consider:

- Describing the set of high-level controls it expects to see within the organisation.
- Documenting those controls and how they operate.
- Specifying the management information (MI) it seeks to obtain to ensure its programme is operating effectively, as well as which senior managers review that MI and how any emerging issues are addressed.
- Having a new business/third-person acquisition approval and review process that identifies the inherent risk with regards to the criminal facilitation of tax evasion.
- Monitoring changes in the business (e.g. new client segment, jurisdiction, business) which may trigger a re-review of the business.
- Compliance monitoring and internal audit reviews may challenge not only whether the internal processes to mitigate the identified risks of the facilitation of tax evasion have been followed but also the effectiveness of the processes themselves. However, organisations may also choose to rely on other tests of effectiveness which are already performed.

It is recognised that some financial institutions treat financial crime risks including predicate offences such as tax evasion as a combined function and/or may leverage similar procedures and controls to mitigate these risks (e.g. anti-money laundering, sanctions and anti-bribery). In such circumstances, it is may be appropriate for review and monitoring procedures to follow established practice.

Monitoring should be appropriate to the risks identified – if the risk assessment has revealed that a particular business unit, jurisdiction or class of associated person is presenting higher risks, then additional monitoring may be appropriate.

14.2. Internal incident management and reporting

By their nature, incidents are difficult to predict so any procedure for incident management should not be overly prescriptive. However, specifying structure and governance for investigation resource can help to ensure: rapid mobilization; organisation-specific know-how; best practice is already recorded and readily accessible; and having policy/procedures in place can improve training and help support the investigation.

The availability of whistle-blowing procedures to all associated persons should also be considered.

All organisations will have in place policies and procedures for responding to staff suspected of misconduct which may include reporting to regulators and/or law enforcement depending on the circumstances. Consideration will therefore need to be given as to whether existing procedures are sufficient to deal with situations where there is potential liability arising to the financial institution from the facilitation of evasion by members of staff.

Whilst it is recognised that a proportionate risk-based regime cannot be a zero-failure regime, it is imperative that where failure occurs the lessons from that failure are considered and processes reviewed to ensure improved performance going forwards

14.3. Application to lower risk businesses

Where a business faces lower risks it might be reasonable to conduct reviews of the effectiveness of the prevention procedures that are in place less frequently than a similar business facing a higher risk.

However, risk assessments should be kept up to date and the level of tax evasion facilitation risk in the business, and the adequacy of controls in place to mitigate any risks, should be monitored on a continuing basis. A business that continues to be lower risk and faces no change in circumstance might reasonably choose to conduct reviews of existing procedures less frequently than annually, in line with other compliance requirements but it should have a clear schedule for revisiting its procedures.