

**“Tax evasion as a predicate offence for money laundering”**

**A RESEARCH PAPER SUBMITTED TO THE FACULTY OF LAW OF THE  
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**“TRANSNATIONAL CRIMINAL JUSTICE AND CRIME PREVENTION:  
AN INTERNATIONAL AND AFRICAN PERSPECTIVE”**

**DECLARATION**

I declare that "Tax evasion as a predicate offence for money laundering" is my own work, that it has not been submitted before any degree or examination in any other university, and that all the sources I have used or quoted have been indicated and acknowledged as complete references.

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## KEY WORDS

Anti-Money Laundering

Financial Action Task Force (FATF) Recommendations

Implementation of the FATF Recommendations

Money Laundering

Offshore finance

Predicate crimes

Secrecy Jurisdictions

Tax crimes

Tax evasion

Tax Havens



## LIST OF ABBREVIATIONS AND ACRONYMS

AML	Anti-Money Laundering
CFT	Counter-Terrorist Financing
DNFBPs	Designated Non-Financial Business and Professions
ECJ	European Court of Justice
ESAAMLG	Eastern and Southern African Anti-Money Laundering Group
EU	European Union
FATF	Financial Action Task Force
GDP	Gross Domestic Product
GFI	Global Financial Integrity
GIABA	Inter-Governmental Action Group against Money Laundering in West Africa
G7/G8/G20	Group of 7/Group of 8/ Group of 20
IMF	International Monetary Fund
ML	Money Laundering
NCCTs	Non-cooperative Countries and Territories
NGO	Non-Governmental Organisation
OECD	Organisation for Economic Cooperation and Development
Palermo Convention	United Nations Convention against Transnational Organised Crime
SADC	Southern African Development Community
TI	Transparency International
TIEAs	Tax Information Exchange Agreements
TJN	Tax Justice Network

UK	United Kingdom
UN	United Nations
UNCAC	United Nations Convention Against Corruption
UNODC	United Nations Office on Drugs and Crime
UNSC	United Nations Security Council
US	United States
VTC	Voluntary Tax Compliance
VAT	Value Added Tax
Vienna Convention	United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances
WB	World Bank



## Table of Contents

CHAPTER 1 .....	1
INTRODUCTION.....	1
1 General background .....	1
1.1 The FATF Recommendations .....	1
1.2 Tax evasion and its global impact.....	4
1.3 Tax evasion and money laundering.....	6
1.4 The significance of the introduction of tax crimes in the FATF Recommendations	7
2 Hypothesis and scope.....	7
3 Methodology and significance.....	8
4 Structure of the paper.....	9
CHAPTER 2 .....	11
TAX EVASION AND MONEY LAUNDERING.....	11
1 Tax in the international arena.....	11
1.1 The international tax regime.....	11
1.2 (Harmful) Tax competition.....	12
1.3 The offshore world.....	15
1.4 International initiatives to tackle the abuse of the offshore world.....	18
2 Tax evasion, avoidance and mitigation.....	20
2.1 Definitions.....	20
2.2 Methods of evading tax.....	21
3 Criminalisation of tax evasion under ML.....	23
3.1 The rationale of AML.....	23
3.2 Elements of the crime.....	25
3.3 Tax evasion, ML and Human Rights.....	27
3.4 AML regulations applied to tax evasion cases.....	28
4 Conclusion.....	29
CHAPTER 3.....	32
INTERNATIONAL AML FRAMEWORK IN RELATION TO TAX CRIMES.....	32
1 Historical overview of the expansion of the scope of international AML regulation with respect to tax crimes.....	32
2 The revision process of the 2012 FATF Recommendations.....	39
2.1 The first round of public consultations.....	40
2.2 The second round of public consultations .....	42
2.3 The FATF's official response.....	42
3 Tax crimes as a predicate offence for ML under FATF Recommendation 3 .....	43
4 Impact of the Revised Recommendations of 2012 on regional groups.....	44
4.1 Implementation of the FATF regime in relation to tax crimes in Africa.....	44
4.2 Implementation of the FATF regime in relation to tax crimes in Europe.....	46
CHAPTER 4.....	48
A CASE STUDY: THE ITALIAN AML REGIME IN RELATION TO TAX CRIMES.....	48
1 Case study: Italy.....	49
1.1 ML in the Penal Code.....	49
1.2 AML regulations.....	51
1.3 Revenue offences.....	51
1.4 Is tax evasion a predicate crime for ML? .....	52
2 Conclusion.....	55
CHAPTER 5 .....	56
CONCLUSIONS AND RECOMMENDATIONS.....	56
BIBLIOGRAPHY .....	59

# CHAPTER 1

## INTRODUCTION

### 1 General background

This paper discusses the progress of international anti-money laundering (AML) law with regard to making tax evasion a predicate offence for the crime of money laundering (ML). This paper will focus particularly on the recent amendments that the Financial Action Task Force (FATF) made to its 40 + 9 Recommendations. The FATF Recommendations are recognised as the global AML standards.<sup>1</sup> The amendments to these have resulted in tax crimes being made designated offences for ML.<sup>2</sup> The aim of this paper is to reconstruct the rationale behind this change and to assess the implications of bringing fiscal crimes under the AML regime.

#### 1.1 The FATF Recommendations

The FATF is an “inter-governmental body that develops and promotes policies to protect the global financial system against money laundering, terrorist financing and the financing of proliferation of weapons of mass destruction”.<sup>3</sup> Currently the FATF consists of 36 member countries, eight associate members, the so-called FATF-Styled Regional Bodies, and 26 observers.<sup>4</sup> The FATF is housed within the Organisation for Economic Cooperation and Development (OECD), in Paris.

The FATF standards are a broad criminal law framework for combating ML. These standards lay down the criteria for criminalising particular types of conduct as conduct falling within the meaning of ML. In addition, they provide a framework which countries

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<sup>1</sup> 191 countries have been endorsed the FATF standards, according to the FATF Annual Report 2010-2011. “The FATF Recommendations are recognised as the global anti-money laundering (AML) and counter-terrorist financing (CFT) standard”; The FATF Recommendations (2012). This paper focuses on AML.

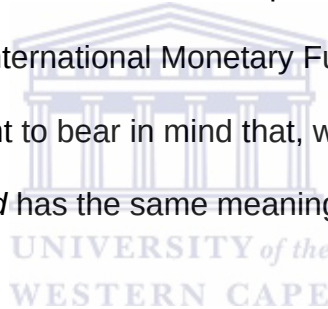
<sup>2</sup> The FATF Recommendations (2012: 112).

<sup>3</sup> The FATF Recommendations (2012: 1).

<sup>4</sup> FATF (2012d).

could implement to recover the proceeds of ML offences (assets recovery), and they also set out how countries can go about preventing the misuse of financial institutions and non-financial designated businesses and professions (e.g. law firms) for ML purposes. The standards are made up of the Recommendations themselves as well as the Interpretive Notes to each Recommendation and the applicable definitions in the Glossary.

The Recommendations are a source of soft law, which means that governments are not legally bounded to implement these measures. Yet, given the fact that soft law can be very influential, to the point that it can be very forceful, just like hard law, the FATF wields tremendous political binding power. The implementation of the Recommendations is, in fact, rigorously assessed through Mutual Evaluation processes, and through the assessments conducted by the International Monetary Fund (IMF) and the World Bank (WB). In this regard, it is important to bear in mind that, when assessing compliance with FATF standards," the word *should* has the same meaning as *must*".<sup>5</sup>



Non-member countries, i.e. those not belonging to the FATF, are assessed by FATF-styled Regional Bodies to see whether their laws and policies comply with those laid down by the FATF Recommendations. After such mutual evaluations are conducted, Mutual Evaluation Reports are compiled, and countries which are found to be non-compliant with the standards are called upon to address the deficiencies. A follow-up report is thereafter published, the idea being to keep the countries on their toes. Jurisdictions which are found to be clearly non-compliant could be sanctioned. Such sanctions take the form of expressions of concern, formal letters, public statements,<sup>6</sup> or a threat to suspend the

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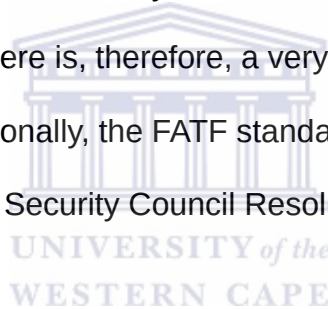
<sup>5</sup> The FATF Recommendations (2012: 120).

<sup>6</sup> Turkey was found clearly non-compliant in 1996. The OECD president sent a letter to the Turkish minister, afterwards a high level mission went to Ankara to call for urgent action, and a public statement was made referring to the possibility of sanctions. See Pieth (2004: 20).



country's membership.<sup>7</sup> Between the years 2000 and 2006, the FATF listed 23 Non-cooperative Countries and Territories (hereafter NCCTs) as lacking an effective anti-money laundering/combating the financing of terrorism (AML/CFT) system. Jurisdictions whose mutual evaluation reveals key deficiencies are referred to the International Co-operation Review Group for a preliminary review. If, notwithstanding the review process, jurisdictions are found to be non-compliant, the FATF calls upon its members to consider the risks arising from the deficiencies associated with each of the jurisdictions.<sup>8</sup>

The FATF's persuasiveness stems from the fact that it has the enormous ability to influence whether or not a country can be seen as a viable business partner or an investment destination. Being "blacklisted" by the FATF reduces the ability of a country of doing business internationally. There is, therefore, a very strong incentive to implement the FATF's Recommendations. Additionally, the FATF standards are hardened by the fact that they can be incorporated into UN Security Council Resolutions.<sup>9</sup>



However, the authority of the FATF to require compliance with its standards has been criticised because the FATF is not a treaty-based organisation, and therefore does not have a legal mandate.<sup>10</sup> Another point of criticism is that the review process in respect of non-member jurisdictions which did not accept the FATF's authority, lacks legitimacy.<sup>11</sup> Yet, it can be argued, that those countries have accepted membership in FATF-Style Regional Bodies, and through this, the FATF exercises its authority over them.

Despite facing criticism of lacking accountability and transparency,<sup>12</sup> the informality of the

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<sup>7</sup> Austria was found non-compliant in 1999. After years of inactivity of the Austrian government, the FATF threatened the country with suspension. See Pieth (2004: 20).

<sup>8</sup> FATF (2012a: 2).

<sup>9</sup> For example, the UNSC Resolution 1617 of 2005 urged the international community to implement the FATF Standards; Paragraph 7 S/RES/1617.

<sup>10</sup> Sharman (2008: 645).

<sup>11</sup> Bosworth-Davies (2006:358); Pieth (2011: 22).

<sup>12</sup> Blazejewski (2007: 1).

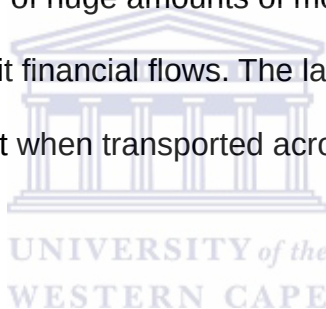
FATF is the key feature that gives it this flexibility, which allows the task force to respond quickly to the ever-evolving practices of money launderers. For this reason, this paper's main hypothesis is that tackling tax evasion under the umbrella of the FATF regulations can result in a more effective global fight against tax crimes, thanks to the FATF's power to influence national criminal laws and to press for the harmonization of AML regulations.

## **1.2 Tax evasion and its global impact**

This paper deals with tax evasion insofar as it affects the international community.

It focuses on "grand" tax evasion as committed by big corporations and high net-worth individuals and how this evasive conduct results in the depletion of national economies.

The focus is particularly on tax evasion that is committed through transnational transactions involving the transfer of huge amounts of money, a process which qualifies to be included in the category of illicit financial flows. The latter are proceeds of crimes or of legal activities which become illicit when transported across borders in violation of national laws, such as tax laws.<sup>13</sup>



High-level tax evasion affects both developing and industrialised countries. A study conducted by Baker in 2005 revealed that two-thirds of global cross-border movements of dirty money are related to funds generated from commercial activities, mostly linked to attempts to evade paying taxes.<sup>14</sup> In practice, the evasion of tax by companies results in developing countries losing up to US\$160 billion a year.<sup>15</sup> Because of tax evasion, West Africa, for example, has an estimated government revenue loss of 50% of potential

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<sup>13</sup> For a more comprehensive definition of "illicit financial flows" and methods of estimation, see GFI (2008: 1 et seq).

<sup>14</sup> Baker has estimated the cross-border flows of global dirty money as amounting to between US\$1 trillion and US\$ 1.6 trillion annually. This included US\$ 0.3 – US\$ 0.5 trillion emerging from criminal activities (drugs, counterfeit goods, smuggling, racketeering, etc), and US\$ 0.7 – US\$ 1 trillion arising from illegal commercial transactions, notably those violating national tax laws. See Baker (2005: 172), as cited also in UNODC (2011: 34).

<sup>15</sup> Christian Aid (2008: 2). "We predict that illegal, trade-related tax evasion alone will be responsible for some 5.6 million deaths of young children in the developing world between 2000 and 2015"; Christian Aid (2008: 1).

revenues.<sup>16</sup> Tax is the most sustainable revenue source for developing countries. This is why governments must be made accountable to the citizens, the taxpayers, rather than to the donors.<sup>17</sup> Money that should contribute to public spending but which is instead stashed away to benefit only a tiny minority of the population, contributes to poverty and impedes social and economic development.<sup>18</sup> It is for these reasons that aggressive tax avoidance<sup>19</sup> is seen as one of the causes of the financial crisis, as huge amounts of money are siphoned away from national revenues.<sup>20</sup>

The April G20 Summit of 2009 declared that the major causes of the financial crisis were failures in the financial sector and deregulation. In particular, secrecy has contributed to the crisis by making it impossible for financial institutions to make reliable estimates of the assets of other institutions, an information asymmetry which negatively affects transactions. The secrecy surrounding assets held offshore was heavily criticised at the 2009 G20 Summit,<sup>21</sup> so much that Switzerland, which is known for its strict bank secrecy laws, accepted that there was a need for it to “relax” its bank secrecy rules.<sup>22</sup>

The cost of tax evasion is, at the end of the day, borne by dutiful taxpayers, who end up assuming larger portion of costs of government. This increases the gap between poor and rich, and thus undermines the value of tax in a democratic society, which is the redistribution of resources.<sup>23</sup> Since illicit flows deriving from tax evasion are embedded in the globalised economy, the answer should also be an international one.

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<sup>16</sup> GIABA (2010:20). “Nigeria is the region’s biggest economy but taxes amount to a mere 6.1% of Nigeria’s GDP of about \$170 billion”; GIABA (2010: 19).

<sup>17</sup> Shaxson (2011: 200).

<sup>18</sup> “For example, former Nigerian dictator General Sani Abacha, was reported to have stashed away away \$ 4 billion by using banks in Switzerland and London. This money could have been used to provide sorely-needed social services and to alleviate poverty”. Otusanya & Lauwo (2012: 355).

<sup>19</sup> This paper supports the idea that aggressive tax avoidance should be legally treated as tax evasion; see Chapter 2.

<sup>20</sup> “Tax distortions are likely to have contributed to excessive leveraging and other financial market problems that came to the forefront during the crisis”; IMF (2009: 8).

<sup>21</sup> “The era of banking secrecy is over”; G20 (2009).

<sup>22</sup> Simonian (2009).

<sup>23</sup> Barker (2009: 239).

### **1.3 Tax evasion and money laundering**

Flows of ill-gotten money is facilitated by the existence of offshore finance and the misuse of financial tools. These structures allow also gains obtained through licit activities to be concealed from national revenue authorities for the purposes of evading the payment of taxes. In the end, these sums are repatriated and integrated into the economic circuit of the country from which they are whisked away. This cycle, in sum, constitutes money laundering. ML is a three-stage process which starts with the money coming from the crime first being placed somewhere to hide its link to the crime (placement). After it has been placed it is layered, which means its connection to the crime and the criminal is further disguised. This can be done, for example, by a series of transactions, a process which often involves the money being transferred through several banks abroad or being used to set up shell companies in tax havens (layering). After it has been layered successfully, the money (which can also be in the form of property) is then integrated into the lawful economy (integration). These three phases are not always clearly separated; sometimes the placement and the integration overlap. What is essential, is that the criminal must have the intention to conceal the provenance of the ill-gotten assets from the criminal justice authorities.

In the case of money deriving from tax evasion, there is a debate concerning the unlawfulness of the origin of those assets. Tax evasion is an economic crime which has no identifiable direct victims. It is also a white collar crime, meaning conduct in violation of criminal law, committed by persons of respectability and high social status. When corporate tax, which is payable by companies, is evaded, it is hard to identify the individuals responsible. Therefore, in practice, tax evasion can be perceived to be comparatively less criminal than say, organised crime, because the perpetrators wear a cloak of legitimacy, and because it often difficult to identify a victim, unless it is some

abstract construct like society or the economy.<sup>24</sup> This has raised, and will raise concerns at a national level, for states that do not yet regard tax crimes as predicate offences (i.e. offences which give rise to ML).

#### **1.4 The significance of the introduction of tax crimes in the FATF Recommendations**

The FATF Recommendations were revised in February 2012 in order to “strengthen global safeguards and further protect the integrity of the financial system by providing governments with stronger tools to take action against serious crime”.<sup>25</sup> Tax crimes have been included as predicate offences for ML, with the aim of contributing to better co-ordination between law enforcement, border and tax authorities, and removing potential obstacles to international cooperation regarding tax crimes.<sup>26</sup> The idea behind making tax crimes predicate offences of ML is that this should result in a higher deterrent effect on would-be tax evaders, since it brings fiscal crimes into the money laundering fold. High-level tax evasion is often committed through the help of professionals, such as lawyers, accounting firms, tax advisors, financial service providers; the fact that these actors may face charges of ML, can be a high deterrent. Financial institutions and non-financial designated businesses and professions have, in fact, an obligation to detect suspected tax-dodgers among their clients, and report suspicious transactions. But above all, the change in the FATF Recommendations will also involve the removal of some of the obstacles to co-operation between tax authorities among different countries.

## **2 Hypothesis and scope**

This paper aims at analysing the suitability of the AML regime, for the purpose of tackling tax evasion. The international soft law AML standards are set by the FATF. The latter expects states to implement these standards at a national level, and has created so-called

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<sup>24</sup> Goredema (2006: 123).

<sup>25</sup> FATF (2012c: 1).

<sup>26</sup> FATF (2012c: 2).

FATF-styled regional bodies to monitor how the standards are implemented by the various countries. Considering the fact that tax regimes are largely based on national law, the choice of limiting the scope to tax evasion is due to the fact that most countries criminalise tax evasion, for it is treated as tax crime.<sup>27</sup> Furthermore, the FATF limits the scope of the Recommendations to serious tax crimes, thus leaving out minor fiscal contraventions. The assumption on which the paper is based is, indeed, that tax evasion, associated with illicit financial flows and tax competition, is emerging as an issue requiring global attention.<sup>28</sup>

The analysis and argument will be informed by the theory that there must be a correlation and a proportionality between the mischief sought to be eradicated, which is tax evasion through the use of tax havens, and the economic benefit that accrues, which is the potential reduction in the sums of money that are diverted away from the legal economy. The overarching question will be: Is the AML regime a suitable framework to cope with tax crimes? Inherent in this question are the following sub-questions: How are tax crimes related to ML?; What was the rationale behind including tax crimes as a designated category of offences for ML in the revised FATF Recommendations?; What are the implications of this change on FATF member jurisdictions and members of regional-related bodies?; How can this change in the FATF standards contribute to solving debates about the advisability of considering tax crimes under the AML regime, at a national level?

### **3 Methodology and significance**

This paper fits in the general debate about the necessity of dealing with the fine line between the lawful and unlawful economy, the so-called “grey zone”. The “grey zone” is the space where profits are made in an illicit way but with the appearance of having been

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<sup>27</sup> There is a distinction in tax law between tax avoidance, which is often perceived as licit, and tax evasion which is, on the contrary, a crime. Both behaviours aim at saving tax. For further clarification of these two terms, see Chapter 2.

<sup>28</sup> Tax Justice Network (2005: 3).

made lawfully. The most used method to conceal the illicit origin of profit is through ML. This paper aims to contribute to the existing literature on international AML law. The originality of the work lies in the combined economic-legal analysis of tax crimes and in the approach of discussing ML and tax evasion as related phenomena.

In order to understand the context of this study better, the analysis of the law, both the hard and the soft law, will be aligned closely to the theoretical assumptions spelt out in the hypothesis above, and this will include looking into both the sociological and economic factors that play a role in arriving at a more balanced understanding of the issues at play here. This is a pure desktop study. This means that the research will be conducted using the standard primary sources on international AML standards, regional instruments and structures, and national laws.

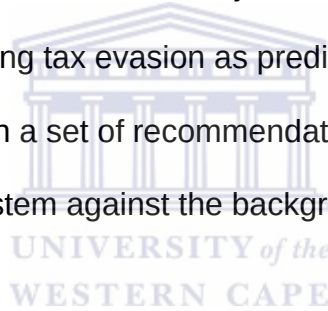
#### **4 Structure of the paper**

This paper contains four more chapters. Chapter 2 deals with the criminalisation of tax offences under the umbrella of the crime of ML. Firstly, the chapter gives an overview on the international tax regime; secondly, it discusses the concept of “tax competition” and analyses the international status of offshore jurisdictions. Secondly, the chapter defines tax evasion, in contrast to the concepts of tax mitigation and tax avoidance; thereafter the chapter approaches the idea of criminalising tax evasion as a predicate crime for ML, in line with the approach of “follow the money” to tackle crime. The paper seeks to understand whether tax evasion would fall into the category of predicate offences, according to the rationale of criminalisation of ML, or whether there would be other categories more suitable for the purpose, if any. By recalling the change in the FATF Recommendations, the chapter concludes with an analysis of the consequences for professionals, financial institutions, and law enforcement institutions, of including tax

evasion under the umbrella of ML, and the challenges that this will raise, and is already raising.

Chapter 3 deals with the current international AML framework. Firstly, it gives an overview of the historical process that has brought the FATF to revise the Recommendations and to include tax crimes as predicate offences for ML. Secondly, the chapter analyses and defines the scope and the impact, in terms of criminalisation of conducts and of preventive measures, of new FATF Recommendation 3. In conclusion, the chapter deals with the implementation of the FATF regime of regional groups, in Africa and in Europe.

Chapter 4 provides a closer analysis of a national jurisdiction, Italy, with the aim of assessing the suitability of including tax evasion as predicate offence for ML, in a domestic system. The paper concludes with a set of recommendations on how to sustain the working of the global financial system against the background of the phenomenon of tax evasion.





## CHAPTER 2

### TAX EVASION AND MONEY LAUNDERING

#### 1 Tax in the international arena

##### 1.1 The international tax regime

A tax is “a contribution to state revenue, compulsorily levied on people, business, property, income, commodities, transactions, etc”.<sup>29</sup> Tax serves four main purposes: collection of revenue by the state, redistribution of resources for the benefit of citizenry and the economy, political representation, and re-pricing economic alternatives.<sup>30</sup> At the beginning of the 20<sup>th</sup> century income and profit tax became the main source of governments' revenue. Tax was calculated either on source or residence basis,<sup>31</sup> according to national laws. Consequently, corporations and individuals, operating in different countries, complained about the imposition of double taxation on interstate business and transactions. Governments started concluding bilateral agreements to avoid double taxation and encourage investment. Bilateral agreements either allocated the right to collect tax to one of the states (residence or source state), or required one of the two states to grant double taxation relief. The League of Nations decided to tackle this issue and founded in 1929 a permanent Fiscal Committee of the League. This Committee drafted the concept that has become known as “the UN model”, as a basis for bilateral tax agreements, which differentiates itself from the “OECD model”. The first is a “source country” oriented model, which advantages host countries of investment, while the latter follows the “residence country” approach, which is preferable for capital-exporting countries.<sup>32</sup>

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<sup>29</sup> Oxford English Dictionary (2007: 3189).

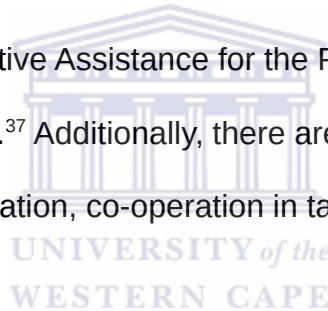
<sup>30</sup> Cobham (2005: 5).

<sup>31</sup> Profits on an investment can be taxed both in the host country of the investment (source country jurisdiction) and in the residence country of the investor (residence country jurisdiction); Lennard (2008: 23).

<sup>32</sup> For a detailed study on the differences between the two models, see Lennard (2008).

The OECD model was established in 1963 by the OECD's Fiscal Committee, which drafted the Double Taxation Convention on Income and on Capital, that has been updated and become the Model Tax Convention on Income and on Capital in July 2010. Both approaches aim at eliminating double taxation, to favour international investments. Currently, almost 3500 bilateral tax treaties are based on this instrument, or on the UN Model Tax Convention.<sup>33</sup>

Bilateral treaties, together with the the OECD and the UN Model Conventions and other transnational instruments, create the international tax regime. The other main tax related instruments are:<sup>34</sup> the Model Agreement on Exchange of Information on Tax Matters,<sup>35</sup> the Convention on Mutual Administrative Assistance in Tax Matters;<sup>36</sup> the International Convention on Mutual Administrative Assistance for the Prevention, Investigation and Repression of Customs Offences.<sup>37</sup> Additionally, there are regional treaties which deal with information exchange, double taxation, co-operation in tax matters, and mutual assistance.<sup>38</sup>



## 1.2 (Harmful) Tax competition

The challenged faced currently by the international tax regime is no longer that of double taxation, but rather that of “double non-taxation”.<sup>39</sup> By exploiting loopholes and

<sup>33</sup> OECD (2012b: 14).

<sup>34</sup> For a complete and updated catalogue of all instruments existing, see OECD (2012b).

<sup>35</sup> Released by the OECD in 2002. At the moment there are more than 600 bilateral Tax Information Exchange Agreements based on this model; OECD (2012b: 36).

<sup>36</sup> Developed in 1998 by the OECD and the Council of Europe. Currently 30 states have ratified the Protocol of 2010; OECD (2012b: 41).

<sup>37</sup> Adopted in Nairobi in 1977, under the auspices of the World Customs Organization, it entered into force in 1980. Currently, 28 Parties have acceded to the Convention; OECD (2012b: 69).

<sup>38</sup> Within the EU, the main instruments are the Council Directive 2011/16/EU on Administrative Cooperation in the Field of Taxation; the EU Council Regulation No. 904/2010 on Administrative Cooperation and Combating Fraud in the Field of Value Added Tax; and the Convention on Mutual Assistance and Cooperation Between Customs Administrations. Most relevant instruments in the African region are: The Convention A/P5/5/82 for Mutual Administrative Assistance in Customs Matters issued of the Economic Community of West African States; Annexure 3 of the SADC Protocol on Finance and Investment which focuses on Tax Coordination in the region to facilitate trade. The Tax Administration Forum, a OECD baked initiative, is a platform that facilitates tax co-operation between developing and industrialised countries.

<sup>39</sup> Shaxson (2011: 23); Rosenzweig (2012: 720).

opportunities of different tax regimes, corporations and individuals manage to pay very low or no tax on their income or profit.

This is seen as licit “tax competition” between states, in a free market economy.

Competition among tax regimes is considered to promote global economic efficiency.<sup>40</sup> The idea behind this is that citizens and corporations should be able to choose their own tax regime for their wealth and income; states, on the other hand, should be free to provide competitive fiscal regulations. This would punish less efficient countries with harsher fiscal regimes, and boost international business.<sup>41</sup>

Countries, in which foreign investors pay less tax than national companies, and much less than what they would pay in their home country, are known as offshore countries. States, especially those with small economies, have engaged in tax competition in order to attract foreign investment. They used the globalisation of capital movements as an opportunity for receiving economic resources and thus boost development. It has been demonstrated<sup>42</sup> that hosting offshore finance has been lucrative for small island economies, since the 1960s, as regards employment opportunities and the overall contribution to public revenues and GDP. In addition, offshore jurisdictions perform faster economic growth than do other countries, and are well-governed countries, although this seems inconsistent with their reputation.<sup>43</sup>

This paper, despite taking into consideration the reasons and the positive consequences of becoming an offshore jurisdiction, embraces the idea that fiscal competition leads to a “race to the bottom”,<sup>44</sup> and is hence harmful. This paper advocates a global tax

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<sup>40</sup> Shaxson (2011: 188); Christensen (2011: 190).

<sup>41</sup> Masciandaro (2006: 369).

<sup>42</sup> Hampton & Christensen (2010: 2).

<sup>43</sup> James & Hines (2010: 118; 121).

<sup>44</sup> Shaxson (2011: 184).

harmonisation, as a key factor for a more sustainable finance. There is no evidence, in fact, that tax competition improves the quality of trade, or the service for customers, or the free market. The offshore financial system, instead, has been proven to be one of the causes of the financial crisis, poverty, and in general, a system that redistributes wealth upwards and risks downwards.<sup>45</sup> Elites and corporations using offshore jurisdictions, while profiting from public services, social benefits, and domestic security, do not pay for any of them.<sup>46</sup>

Moreover, offshore finance is not a sustainable source of revenues. The banking crises of 2007 and 2008 have affected offshore jurisdictions, by reducing the value of deposits held. Particularly small economies, which based their GDP on foreign investments and are therefore dependent on offshore finance, are not ready to diversify the local economy, to combat the financial crisis. In fact, as these countries have a big part of the population employed in the financial sector, there is a lack of other professional skills.<sup>47</sup> Offshore finance affects developing countries negatively: Global Financial Integrity estimated that approximately US\$ 858 to US\$ 1 trillion flows annually from poorer countries as proceeds of corruption, state looting and tax evasion;<sup>48</sup> the main destinations are offshore jurisdictions in the developed world. Illicit flows from Africa, for example, flow mostly into the British offshore system.<sup>49</sup> In addition, offshore jurisdictions can easily attract criminal investment and terrorist financing transactions. The “anthropologic” argument, used often

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<sup>45</sup> Shaxson (2011: 148).

<sup>46</sup> Action Aid has observed that SAB Miller, the second largest brewery in the world, relies on services provided from the state, as much as citizens do: it owns property, thus benefits from the enforcement of the rule of law to keep its property rights; it uses public roads and ports; it relies on states to provide them educated workforce. All these benefits should come “with a quid pro quo: the tax that companies pay on their own income”. However, this company has paid no taxes in the last two years, thanks to aggressive tax avoidance practices, therefore it has profited from public services, without having contributed to them. See Action Aid (2012: 34).

<sup>47</sup> See the study case conducted on Jersey. However, other authors are less pessimistic with regard to the future of small offshore jurisdictions; Christensen & Hampton (2010: 14).

<sup>48</sup> Kar & Cartwright-Smith (2008: 22).

<sup>49</sup> Shaxson (2011: 18).

in support of tax competition, is that it is intrinsic in human nature to try to pay as little tax as possible; this, however, should not result in a race to the bottom, since tax payers will try to pay less tax even where tax rates are already very low.<sup>50</sup>

### **1.3 The offshore world**

“The offshore world is all around us”.<sup>51</sup> Offshore wealth amounted to US\$7.4 trillion in 2009, equivalent to 6.6% of globally held assets.<sup>52</sup> An estimated 50% of global commerce passes through offshore jurisdictions.<sup>53</sup>

Regulatory authorities and organisations adopt different definitions of “offshore”. Often, other terms are employed, such as tax havens, financial havens, secrecy jurisdictions, financial offshore centres, or offshore centres. All these notions refer to places that offer an escape from tax, provide secrecy and lax financial regulations, attract foreign investment through fiscal competition with other countries, and are reluctant to exchange tax information with other countries. Usually, these jurisdictions result in having financial services industry much larger than their local economy.<sup>54</sup> According to the different definitions, diverse lists of countries have been drafted.<sup>55</sup> Depending on the choice of definition, between 30 and 70 tax havens exist.

Attractive tax regimes can be modelled by providing very low tax rates on specific services. The Netherlands Antilles, for example, do not apply withholding tax on interest or royalties; Dutch holding companies are, thus, able to receive tax free dividends and capital gains originating from their subsidiaries, and at the same time are allowed to deduct expenses, including interest on loans. Usually, countries make use of offshore jurisdictions

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<sup>50</sup> Bridges (200: 161).

<sup>51</sup> Shaxson (2011: 8).

<sup>52</sup> UNODC (2011: 44).

<sup>53</sup> Baker (2005: 134).

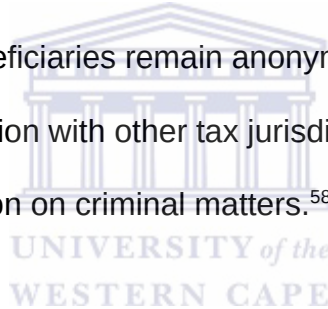
<sup>54</sup> Shaxson (2011: 9).

<sup>55</sup> For the most relevant lists, see IMF (2003: 26); OECD (2000); Tax Justice Network (2011).

which are located geographically close to them.

A defining aspect of these jurisdictions is the provision of conditions of secrecy, either through banking secrecy laws or through judicial arrangements and banking practices.<sup>56</sup>

Secrecy can be a risk factor: The anonymity of financial transactions and the opaqueness of offshore operations make these jurisdictions vulnerable to financial abuse. Banking secrecy was established in Switzerland in 1930. Violation of banking confidentiality was made a criminal offence, with the purpose of protecting Jewish money from the Nazi regime.<sup>57</sup> Currently, secrecy covers not only banking activities, but the whole range of financial transactions. Regulations that provide secrecy include laws that allow a low degree of transparency in the establishment and accounting by corporate entities, the creation of trusts whose real beneficiaries remain anonymous, zero or low tax rates and minimal exchange of tax information with other tax jurisdictions, banking secrecy, and barriers to exchange of information on criminal matters.<sup>58</sup>



Secrecy is a controversial topic. The right to privacy is a fundamental right of any individual,<sup>59</sup> and secrecy can, in fact, serve licit and valid purposes. Politically persecuted individuals can use secrecy to secure their assets from being confiscated by authoritarian regimes; and secrecy can also be in the interest of the family.<sup>60</sup>

Yet, secrecy should not be exploited for unlawful purposes, such as violations of national tax law. The veil of secrecy is a bar to investigations, thus a guarantee of impunity. This

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<sup>56</sup> Christensen (2011: 183); Leikvang (2012: 301).

<sup>57</sup> Although this view is commonly accepted, some authors state that the Swiss law was passed only after 8 days of Hitler's installation as imperial chancellor, and therefore did not directly aim at evading German Intelligence's control of Jewish assets. See Shaxson (2011: 51).

<sup>58</sup> Reed & Fontana (2011).

<sup>59</sup> Article 12 of the United Nations Declaration on Human rights.

<sup>60</sup> For example, the original purpose of trusts (financial tools which provide secrecy) was to promote the protection of spouses who are unable to look after their own affairs. See Christensen (2011: 183).

makes the concealing of financial transactions seductive for terrorists as much as organised criminal groups, tax evaders, and corrupt political elites who need to stash away huge amount of money. Secrecy has been used by corrupt dictators around the world to conceal stolen assets.<sup>61</sup> Secrecy mechanisms are complex and expensive, but “people will pay for secrecy because it costs less than disclosure”.<sup>62</sup> Banking secrecy had been used as a ground to refuse mutual legal assistance and co-operation in criminal matters, thus impeding or hindering criminal investigations or other legal proceedings. International consensus on the importance of preventing the use of banking secrecy, as an obstacle to provide assistance to requesting states, has been achieved after long negotiations.<sup>63</sup>

In order to tackle lack of transparency in the financial system, the international community has been concluding Tax Information Exchange Agreements (TIEAs), which are bilateral treaties that aim at allowing an easier exchange of information on tax matters. However, often these instruments require dual criminality for the exchange of information; this results in a bar to assistance especially when dealing with tax matters with offshore jurisdictions, which notably have lax fiscal legislations.<sup>64</sup> Sometimes TIEAs do not provide for automatic exchange of information, and may impose notification to the assets owner before a disclosure order is issued.<sup>65</sup>

The main problem remains the fact that these agreements, even though they might be efficient in tackling abuse of fiscal regimes between the two countries, are not comprehensive. There will always be an offshore jurisdiction which has no TIEA with a specific country, where tax-dodgers can shift their funds. Yet, according to the Financial

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<sup>61</sup> Baker (2005: 238).

<sup>62</sup> Alldridge (2003: 32).

<sup>63</sup> UNODC (2010: 319 et seq.).

<sup>64</sup> Leikvang (2012: 302).

<sup>65</sup> Leikvang (2012: 317).



Times, banking secrecy laws will probably be degraded to the point of being disabled within the course of the coming decade.<sup>66</sup>

#### **1.4 International initiatives to tackle the abuse of the offshore world**

In the last 15 years the fight against offshore jurisdictions has been promoted by the UN, the US, the EU, the G20, the OECD, the IMF and the WB. The first main step was undertaken by the G7 and the OECD, with the “Harmful Tax Competition” Initiative of 1998, which identified harmful tax practices and provided the definition of a “tax haven”,<sup>67</sup> thus allowing the OECD to publish a list of tax havens.<sup>68</sup> In 1999 the Financial Stability Forum was established by the G7 countries to promote financial stability by focusing on international cooperation regarding the exchange of information and overview of financial markets. In 2000, the Global Forum on Transparency and Exchange of Information on Tax Matters was established by the OECD, as a framework to monitor the implementation of globally endorsed tax transparency standard.<sup>69</sup> The Global Forum currently includes 92 countries and promotes tax information exchange agreements among them; yet most participants are from industrialised countries. In 2005, the EU Savings Tax Directive included associated and dependent territories,<sup>70</sup> which are often used as offshore systems by the protectorate state. However, the Directive had a loophole, in the regulation of trusts. A “beneficial owner”, under European law,<sup>71</sup> is only an individual; this has allowed limited companies to hold funds on deposit, without a duty to disclose.<sup>72</sup> In addition countries like Belgium, Luxembourg, Austria, and outside the EU, Guernsey, Jersey and the Isle of Man have objected to the Directive and excluded themselves from the obligation to furnish

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<sup>66</sup> Simonian (2009).

<sup>67</sup> OECD (1998: 21 et seq).

<sup>68</sup> OECD (2000: 17).

<sup>69</sup> OECD (2012a).

<sup>70</sup> Anguilla, Aruba, British Virgin Islands, Cayman Islands, Gibraltar, Guernsey, Jersey, Isle of Man, Montserrat, Netherlands Antilles, and the Turks and Caicos Islands. Other jurisdictions agreed to participate: Andorra, Liechtenstein, Monaco, San Marino and Switzerland.

<sup>71</sup> Article 2 of the Council Directive 2003/48/EC.

<sup>72</sup> Tax Justice Network (2008: 4).



information. A breakthrough judgement was handed down in 2006, by the European Court of Justice (ECJ), in the *Halifax* case.<sup>73</sup> The ECJ affirmed the principle of prohibition of abuse of EC law, by referring to the ongoing movement to combat and prevent avoidance and evasion. This will affect the principle of neutrality of VAT.

After the financial crisis of 2008/2009, initiatives to tackle the abuse of the offshore world have accelerated, because of domestic budgetary pressure. In 2009, at the London meeting, the G20 launched a new initiative to tackle tax havens, led by the OECD, which broadened the list, by including European countries, such as Switzerland, Austria, Luxembourg. In 2011, the US introduced the Stop Tax Haven Abuse Act, with the purpose of “restricting the use of offshore tax havens and abusive tax shelters”.<sup>74</sup>

Yet, this response to harmful tax competition also has controversial aspects. International organisations have identified offshore jurisdictions as “high risk” countries with regard to ML and terrorist financing threats. Often, the “war on terror” has been used to impose strict financial regulations on poor countries, without reasonable cost-effectiveness planning, thus resulting in an unbearable burden.<sup>75</sup> The systems of “blacklisting” and “naming and shaming” that are applied to point out jurisdictions that are not in line with international standards, have been proven to be harmful and not efficient to promote financial integrity.<sup>76</sup> In addition, the OECD, an organisation led mainly by industrialised countries, has been criticised for applying a double standard when listing major tax havens. For example, it has never mentioned the UK and the US.<sup>77</sup> The OECD has also been accused of financial imperialism, with the argument that no nation has the right to tell another sovereign entity

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<sup>73</sup> ECJ case C-255/02.

<sup>74</sup> Leikvang (2012: 320).

<sup>75</sup> Rahn (2008: 341); Bosworth-Davies (2008: 180); Sharman (2011: 55).

<sup>76</sup> Pieth (2004: 21); Sharman (2011: 50).

<sup>77</sup> Christensen & Hampton (2010: 8).

which fiscal policy to adopt. The OECD initiative to tackle tax havens has been criticised as an attempt by European countries to prevent their own citizens moving their assets to non-OECD countries with less punitive tax laws, by forcing the latter to raise tax rates and abolish financial privacy.<sup>78</sup>

Although unilateral and regional actions play an important role in the fight against harmful tax competition, there is need for collective action to find a unified international solution. However, tax is a matter of sovereignty, therefore it is particularly difficult to obtain consensus on the creation of any international organisation dealing with the matter, and which has power to influence national parliaments. The FATF, through the work of the regional bodies, can be the right authority to address this issue.

## **2 Tax evasion, avoidance and mitigation**

### **2.1 Definitions**

This paper focuses on tax evasion as one of many fiscal offences. Tax evasion is “any illegal action taken to avoid the lawful assessment of taxes; for example, by concealing or failing to declare income”.<sup>79</sup> The concept of tax evasion is often defined in opposition to tax avoidance and tax mitigation. Tax mitigation is the minimisation of taxes, with the approval and/or knowledge of the government. An example is the deduction of donations to charity. This behaviour is thus legal, in contrast to tax evasion.

“Tax avoidance” is a very controversial term.<sup>80</sup> Tax avoidance is “the lawful arrangement or planning of one's affairs so as to reduce liability to tax”.<sup>81</sup> Tax avoidance, thus, exploits the uncertainty that results from the incongruence between the literal interpretation of the law

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<sup>78</sup> Rahn (2002: 341).

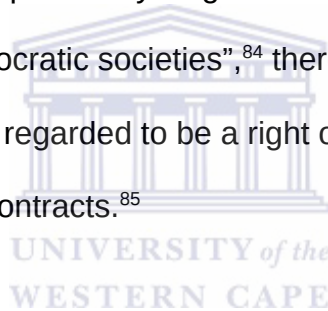
<sup>79</sup> Law (2006: 529).

<sup>80</sup> “The term tax avoidance does not have a limiting and definite meaning”; Barker (2009: 230).

<sup>81</sup> Law (2006: 527).

and the intent of the legislative power. What makes this concept disputable is that the tax advantages pursued by tax avoiders are unintended by lawmakers, despite being formally in accordance with the law. Tax avoidance and evasion are impelled by the same motivation, and they have the same result, which is the paying of less taxes. Yet, they are treated as different in nature.

Tax evasion is usually described as illegal, whereas tax avoidance is identified as legal. A better interpretation is offered by Barker who describes tax avoidance as “noncriminal behaviour”, not as “legal behaviour”.<sup>82</sup> Tax avoidance is not *contra legem*, but *extra legem*. National law might, indeed, provide a general anti-avoidance clause.<sup>83</sup> Although “tax avoidance is recognized today by practically all governments as a serious threat to the integrity of the tax system in democratic societies”,<sup>84</sup> there is still great support for avoidance. Tax avoidance is also regarded to be a right of the person to deal freely with property and to enter freely into contracts.<sup>85</sup>



Tax avoidance is a borderline conduct. This paper supports the view that aggressive tax avoidance should become a criminal offence, by expanding the scope of tax evasion, or of tax fraud. This chapter deals with both the effects of tax avoidance and tax evasion. In order to tackle abusive offshore practices, both concepts are, in fact, key. In the next chapter, the term “tax crimes” will be used, since the FATF Recommendations use a wide category which has to be limited according to domestic law.

## 2.2 Methods of evading tax

Tax can be evaded through different mechanisms and tools, such as transfer pricing, false

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<sup>82</sup> Barker (2009: 243).

<sup>83</sup> For example, Italian fiscal law (articolo 37bis, comma 8, del Dpr 600/1973); Section 245 of the Canadian Income Tax Act; Part IV A of the Australian Income tax Act; Section BB9 of the New Zealand Income Tax Act. Tax Law Review Committee (1997: 19; 23; 24).

<sup>84</sup> Barker (2009: 229).

<sup>85</sup> Barker (2009: 234).

documentation, dummy corporations, shell banks, kickbacks, wire transfers, numbered accounts, trusts, shell corporations, earnings stripping, or repatriation of dividends. Trusts are financial tools which have a primary lawful purpose. They allow, for example, holders of assets to put them in the hands of others to protect the interests of minor children or people who are unable to care for themselves. They are also used to transfer and hold assets for charitable purposes. Problems arise when trusts are used to conceal the origin and distribution of illegal funds, because the law of the offshore jurisdiction permits the obscuring of the identity of both the settlor and the beneficiary.

Fictitious pricing serves to implement tax evasion schemes between countries. It is called “mispricing” in unrelated-party transactions, and abusive transfer pricing in related-party transactions.<sup>86</sup> Also quantities, qualities, weights, measurements can be completely faked with money flowing for trade that never existed. Transfer pricing occurs between related companies, when trading with each other. Traded products are, in fact, not subjected to neutral market evaluation, instead, the group's accountants decide what price they should pay each other. International standards would require them to do this based on the arm's length price, which is the price that the company would be supposed to pay for a product when buying it from a non-related company. If the companies, instead, under-value or over-value commodities or services, with the sole aim of reducing their tax liability, this constitutes mispricing. This can amount to tax evasion, according to national law.

Multinational enterprises have been implicated in shifting income or profits from Africa through transfer pricing, with estimated revenue losses exceeding \$10 billion a year.<sup>87</sup>

Mispricing is a form of trade-based money laundering.<sup>88</sup> Trade-base ML is defined as “the

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<sup>86</sup> Baker (2005: 134).

<sup>87</sup> Tax Justice Network for Africa (2006: 3).

<sup>88</sup> Goredema (2011: 3).

process of disguising the proceeds of crime and moving value through the use of trade transactions in an attempt to legitimise their illicit origins. In practice, this can be achieved through the misrepresentation of the price, quantity or quality of imports or exports”.<sup>89</sup> In resource-rich countries, high amounts of taxes are evaded through the negotiation of contracts between the state and extracting companies, which result in very low taxes being paid by the latter. Revenue collection linked to extraction and export is seriously affected by corruption, as a result of low or no competition in the sector, and of the discretionary political control over the resources. Additionally, contracts are negotiated with subsidiaries incorporated in offshore jurisdictions, which afterwards proceeded with high-interest loans, in order to avoid taxes in the home country.<sup>90</sup> Underreporting production and underpricing minerals appear to be two major channels for tax evasion in the mining sector.<sup>91</sup>

### **3 Criminalisation of tax evasion under ML**

Following the discussion of the harmful consequences of fiscal competition, and the most common methods of tax evasion, this section aims at analysing whether criminalising tax evasion under the umbrella of the ML would be an effective and appropriate way of dealing with the issue. AML consists of two elements, one of criminal law, that is the criminalisation of the conduct, and one regulatory, which aims at preventing the abuse of the financial system for ML purposes.

#### **3.1 The rationale of AML**

“The primary reason for fighting ML is to enable law enforcement authorities to confiscate the proceeds of predicate criminal activities in those situations where confiscation might otherwise not be possible”.<sup>92</sup> The crime of ML was, in fact, invented, to “follow the money”

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<sup>89</sup> FATF (2006b).

<sup>90</sup> Le Billon (2011: 6).

<sup>91</sup> Le Billon (2011: 7).

<sup>92</sup> Stessens (2000: 85). However, against this opinion it can be argued that, once there is enough evidence to prove the serious predicate offence, states could attach a duty to proceed with assets forfeiture to the main offence, without needing the ML conviction. See Alldridge (2003: 65).

of criminal groups, since the imprisonment of even top ranking criminals did not result in a reduction of organised crime rates.<sup>93</sup> The underlying idea was to attack the criminals' economic wealth, through assets recovery mechanisms. This, it was believed, would improve the effectiveness of the fight against ML and criminal activities, such as drug trafficking.<sup>94</sup> Assets recovery has been recognised as a key element also in the fight against corruption, under UNCAC.<sup>95</sup> Additionally, since most high level criminals usually stay aloof from the commission of crimes, while enjoying the financial profits, ML can serve the purpose of gathering evidence against top criminals by tracking the movement of money.<sup>96</sup>

The crime of ML punishes conduct aimed at disguising and concealing the origin or the ownership of the proceeds of crime. In particular, when AML law allows the confiscation of the equivalent, this can result in an advantage for law enforcement, when proceeds of crimes have been intermingled with lawful assets, or are held by *bona fide* third parties. In the first case it should be still possible to confiscate the equivalent value of assets from the money launderer, and, in the second case, the object of confiscation will be any property deriving from the ML, even the profit made by the selling of the criminal assets to *bona fide* third parties. Financial gain is also what moves tax evaders. If the earnings resulting from tax evasion might be confiscated as proceeds of ML, this may become a deterrent for legal persons involved in fiscal crimes. The question, with regard to legitimacy under criminal laws, is this: Can tax evasion be the predicate offence which justifies the court in

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<sup>93</sup> In opposition, it has been demonstrated that when criminal assets remain untouched from law enforcement measures, and all effort is put on the imprisonment of criminals, criminal groups will expand their scope and scale of violence and corruption to public officials to protect themselves from prosecutions. This “paradox of expected punishment” shows that a functioning financial intelligence, co-operating with investigative authorities, which follows the “dirty money”, is essential to effectively combat organised crime. See Buscaglia (2008: 11).

<sup>94</sup> ML was, in fact, first regulated in the Vienna Convention, which deals with the criminalisation of dealing with illicit drugs and psychotropic substances in Article 3(1)b i and ii.

<sup>95</sup> Article 51 of UNCAC.

<sup>96</sup> Stessens (2000: 86).

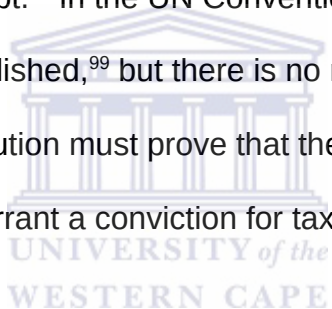
issuing a confiscation order?

### 3.2 Elements of the crime

ML is a derivative crime. The elements of the crime determining the *actus reus* are: The commission of a predicate offence and the presence of the proceeds of crime. The *mens rea* required is the intent to conceal the proceeds and the knowledge of unlawfulness.<sup>97</sup>

With regard to the scope of ML, it has been shown to be flexible, and has been, in fact, expanded since the Vienna Convention. Currently, the FATF Recommendations list twenty categories of designated offences. Among them there are serious tax crimes.

The standard of proof of the ML predicate offence can be lower than that for an ordinary crime. This means that the commission of the antecedent crime does not need to be proven beyond a reasonable doubt.<sup>98</sup> In the UN Conventions, the law requires that predicate offences must be established,<sup>99</sup> but there is no requirement of a previous conviction. Therefore, the prosecution must prove that the property generated through tax evasion is illegal but does not warrant a conviction for tax evasion.



Proceeds of crime are usually considered properties deriving from the commission of a criminal offence; for example, money obtained from drug smuggling is *ab initio* criminal. Monies deriving from tax evasion, are, instead, lawfully earned, but may become tainted, for example, when not declared or when retained due to fraudulent tax deductions.

This has raised criticism, on the basis that the proceeds of tax evasion are different in nature from profits of conventional criminality; yet, even though the underlying conduct which generates the proceeds may be legal, it is the retention of the money that should be

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<sup>97</sup> Article 28 of UNCAC.

<sup>98</sup> For example, in the UK, prosecution can prove that a property is a proceed of a crime, “by evidence of the circumstances in which the property is handled which is such as to give rise to the irresistible inference that it can only be derived from crime”, Court of Appeal in *Anwoir* (2008); see also McCluskey (2009: 719).

<sup>99</sup> Article 23 of UNCAC; Article 6 of the Palermo Convention.

paid over as tax which constitutes the criminal conduct.<sup>100</sup> It might be argued that proceeds of crime are monies “derived from or obtained, directly or indirectly, through the commission of an offence”,<sup>101</sup> and therefore monies retained are not included. However, it is the evasion of taxes that generates the illicit profits. It can be, thus, argued that those profits derive from an offence.

ML convictions should be followed by confiscation of criminal assets. With regard to tax evasion, problems arise because usually tainted money is intermingled with lawful money. It is, thus, difficult to identify the dirty amount. Furthermore, it might be difficult to find out the right amount of tax evaded. The quantity of the unpaid tax is the quantity of the benefit, and any part of the tax evader's property might be the object of assets recovery, once the *mens rea* is proved.<sup>102</sup>

Another controversial issue, in relation to fiscal offences, is whether they amount to a predicate offence if committed abroad. The traditional approach is, in fact, that countries are not supposed to enforce other countries' revenue laws. Some jurisdictions, therefore, do not consider tax offences predicate crimes if committed abroad.<sup>103</sup> Besides the sovereignty principle, there are also practical problems, since the suspected offence committed abroad must be a criminal offence in that country too. This assigns domestic prosecution a burden of collecting information about foreign legislation on tax matters. The tax evasion might be discovered by tax authorities only after some years. This might undermine the system of reporting of suspicious transactions by financial institutions, if they cannot access information about the lawfulness of the transaction under tax law. It should be clearer, for this purpose, to what extent a fiscal offence committed abroad can

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<sup>100</sup> Oliver (2009: 57).

<sup>101</sup> Article 2 of UNCAC.

<sup>102</sup> Alldridge (2001: 353).

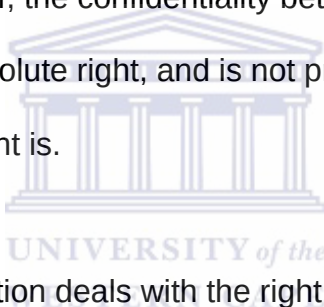
<sup>103</sup> Implementation Review Group of the United Nations Convention Against Corruption (2011: 7).



be considered a predicate crime, and there should be faster and easier ways of exchanging tax information between countries.

### **3.3 Tax evasion, ML and Human Rights**

Including tax evasion as an antecedent offence for ML charges may raise inconsistencies with human rights, particularly with Article 8 of the European Convention on Human Rights, which protects the right to private life. A person's financial affairs, the relation between client and accountant, and the confidentiality between the client and the professional advisor, are protected by this article. Therefore, compelling disclosure on fiscal management may, on the face of it, seem a breach of the individual's right to privacy,<sup>104</sup> and of the confidentiality principle.<sup>105</sup> Yet, tax evasion is not only a private matter, but affects the whole public. Moreover, the confidentiality between the client and the professional advisor is not an absolute right, and is not protected to the extent that privilege between lawyer and client is.



Article 6 of the European Convention deals with the right to a fair trial. The use of investigative powers of the revenue authorities to generate evidence for ML prosecutions might not be consistent with the provision. In addition, if even the proceeds of crime are considered subject to taxation, there is the danger that law enforcement will treat proceeds of drug trafficking, for example, as tax evasion, and choose to charge drug dealers with ML, just by proving the undeclared income.<sup>106</sup> The underlying claim seems to be that tax evasion liability can serve as a useful fallback for authorities who are unable to acquire sufficient evidence to secure a conviction for the main crime, as in the famous case of Al Capone, who was finally convicted for tax evasion by American authorities, because of their incapability of bringing charges of organised criminal activities against him. However,

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<sup>104</sup> Alldridge (2001: 354).

<sup>105</sup> Flight (2001: 324).

<sup>106</sup> Alldridge (2001: 354).

law enforcement, while aiming at fighting against crime, should not violate fundamental democratic principles, such as the principle of legality.<sup>107</sup>

Despite difficulties and controversies which may arise by including tax evasion under the umbrella of ML, the fact that the FATF Recommendations now list serious tax crimes as predicate offences might help to pressurise countries to harmonise their tax laws, which would make mutual legal assistance easier as far as tax matters are concerned.

Additionally, techniques used for tax dodging involve identical mechanisms and financial subterfuges as those used for ML. This means that the same means employed to obtain mutual legal assistance with regard to money laundering crimes, for example, by resorting to the use of Financial Intelligence Units, may be used for tax-related offences.

### **3.4 AML regulations applied to tax evasion cases**

The second element of the AML regime is the regulatory part. This has a preventive purpose, and imposes duties on the financial sector, on professionals, and on some designated non-financial businesses, to detect money launderers. Tax evasion is usually committed through the help of professionals, such as lawyers, accountants, corporate service providers and bankers. Accountants play a major role in providing schemes to save great amount of taxes.<sup>108</sup> The question whether lawyers accepting dirty money when dealing with criminals and knowing that the money might stem from illicit sources is an argument of current debate. With regard to tax evasion, when the professional adviser suspects tax evasion and the funds are clearly identifiable, but still enters into arrangements or provides advice, he/she will face prosecution for failing to disclose the suspicion.<sup>109</sup> Usually, tax authorities have difficulty in proving a conspiracy between a taxpayer and his professional adviser. The extension of ML legislation to tax evasion may

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<sup>107</sup> Alldridge (2001: 354).

<sup>108</sup> Tax Justice Network (2005: 30).

<sup>109</sup> Brandon (2000: 41).

make it easier to bring charges in relation to such transactions because the investigation does not have to prove the tax offence in regard to the professional.<sup>110</sup>

On the one hand, with respect to AML regulations dealing with financial institutions, it has to be noticed that it will be difficult to extend the Know Your Customer and the Customer Due Diligence requirements, since commercial crimes, such as tax evasion, might not raise suspicions of conventional dirty money. On the other hand, banks and other financial institutes may over-report suspicious transactions to the Financial Intelligence Unit, to avoid being regarded as being party to the ML scheme of their customer.<sup>111</sup>

#### **4 Conclusion**

ML has been criminalised in the majority of the countries in the world. This fortifies the AML regulatory regime. However, AML regulations have not reduced the number of money laundering offences committed, especially the predicate offences which give rise to the money laundering. In particular, AML standards have been criticised because when one compares the costs of implementation with the benefits obtained, the standards do not seem to be effective. Rules of prevention of ML impose high costs of compliance on the public and the private sector. This results in a great burden being imposed on small business enterprises and on countries with low government spending possibilities. There are therefore no apparent advantages. Countries continue to seek compliance with international AML standards because the cost of non-compliance is expensive, meaning that it results in their being boycotted by foreign investors. These considerations need to be borne in mind when tax evasion is made a predicate offence for ML

John Christensen has suggested that “grand” tax evasion be included under the label of

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<sup>110</sup> Bridges (1996: 169).

<sup>111</sup> Bridges (1996: 166).

corruption, in order to apply the UNCAC legal framework to the offence.<sup>112</sup> Other authors have also recognised UNCAC's potential for tackling illicit financial flows.<sup>113</sup> Corruption has been studied mainly from the demand point of view (e.g. the side of the corruptor). This means, for example, passive corruption of African political leaders and senior public officials. The Transparency International Corruption Perceptions Index classifies many African states as very corrupt countries and the industrialised world, such as Switzerland, as least corrupt.<sup>114</sup> Pointing fingers "at petty officials and ruling kleptomaniacs has resulted in insufficient attention being paid to the (largely) Western financial intermediaries who facilitate the laundering of the proceeds of corruption through offshore companies, trusts and similar subterfuges".<sup>115</sup> To make real efforts to stop illicit flows, it is necessary to tackle the abuse of banks and offshore jurisdictions. Eva Joly advocated for a shift of the corruption discourse to phase two, in which the role of bankers, lawyers and offshore financial centres in enabling corrupt practices comes under far greater scrutiny.<sup>116</sup> The legal framework provided by UNCAC, which requires, specifically, the criminalisation of private sector corruption, by supporting the establishment of corporate responsibility, for example, could be useful also to prosecute corporations engaged in high-level tax evasion. The fact that UNCAC sidesteps the requirement of dual criminality, which has traditionally constituted a major obstacle to effective cooperation, might also result in an advantage in the international co-operation against tax crimes. The system of seizure and recovery of assets, set as a fundamental principle in the Convention, under article 51, can be an essential tool to address grand tax evasion, too.

However, all States Parties must ratify any modification of the UN Convention before it

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<sup>112</sup> Christensen (2007: 11).

<sup>113</sup> Chene (2011: 3).

<sup>114</sup> Transparency International (2011).

<sup>115</sup> Christensen (2011: 186).

<sup>116</sup> Christensen (2011: 193).

can take effect. Trans-governmental bodies are more flexible and thus more suitable to tackle the rapid changes that take place in the financial system. For this reason, the fact that the FATF has introduced tax crimes as predicate offences for ML in the Recommendations may represent a breakthrough in international financial regulation.



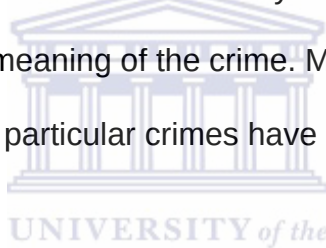
## CHAPTER 3

### INTERNATIONAL AML FRAMEWORK IN RELATION TO TAX CRIMES

Currently, the FATF Recommendations list tax crimes as a designated category of predicate offences for ML. The idea of including tax crimes under ML is the outcome of a long process, where international organisations and trans-governmental bodies have recognised the negative impact of fiscal offences, and have identified in the AML framework a suitable scheme to combat more effectively tax crimes.

#### **1 Historical overview of the expansion of the scope of international AML regulation with respect to tax crimes**

ML is a derivative crime. Its definition as a crime depends on the origin of the proceeds of crime involved. With time, the international community has broadened the range of predicate offences, and thus the meaning of the crime. Major changes in the definition have been on an *ad hoc* basis as particular crimes have come to public awareness.



The crime of ML was first regulated at an international level in the Vienna Convention of 1988.<sup>117</sup> However, the scope of this convention was limited to crimes related to drug trafficking. Tax crimes were not included as predicate offences. Since then, the scope of international AML law has been expanded, with tax evasion being a key area of dispute.<sup>118</sup>

In 1989 the FATF was formed by the G7 member States, the European Commission and eight other industrialised countries. The aim was to ensure a more efficient prevention of the use of financial institutions for the laundering of drugs proceeds. Although some parts aimed at cracking down on tax havens and generally on economic crimes,<sup>119</sup> a

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<sup>117</sup> Although this instrument does not use the term “money laundering”, article 3 of the Vienna Convention lists as an offence the conversion or transfer of property, knowing that such property is derived from offences, for the purpose of concealing or disguising the illicit origin, and the concealment or disguise of the true nature of property, knowing that such property derived from an offence.

<sup>118</sup> Levi (2002: 182).

<sup>119</sup> President Mitterand of France advocated such a direction in 1989 at the G7 Summit in Paris, where the FATF was founded; Pieth (2004: 8).

compromise had to be reached and tax matters were excluded from the scope of the task force.<sup>120</sup> In the same year, the Council of Europe expanded the definition of ML beyond the scope of drug trafficking to include the proceeds derived from any criminal activity, by adopting the Strasbourg Convention.<sup>121</sup> Despite two previous European Protocols on extradition<sup>122</sup> and mutual legal assistance,<sup>123</sup> which had provided that cooperation could not be refused solely on the ground that the predicate offence was considered a tax offence in the country, in the Strasbourg Convention, co-operation could be refused in case of a fiscal offence.<sup>124</sup>

In 1990, the FATF issued a report containing a set of Forty Recommendations. These were intended to provide a comprehensive plan of action needed to combat and prevent ML. In 1991 the European Council issued a Directive<sup>125</sup> with the goal of strengthening the implementation of the Vienna Convention and the FATF Recommendations of 1990. The category of ML offences extended beyond the scope of drug-related crimes; yet States Members were free to determine their own list. These steps, which were taken at a European level, stimulated the FATF process of expanding the scope of ML within the Recommendations.

In fact, in 1996 the FATF redrafted Recommendation 4 by including all serious offences as predicate crimes for ML, but leaving national jurisdictions free to define this category. The change was nevertheless crucial: ML was no longer seen as only a drugs-related offence

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<sup>120</sup> Switzerland, especially, agreed to join the task force only after having been assured that tax matters were not part of the negotiations; Pieth (2004: 9).

<sup>121</sup> Article 1(e) of the Warsaw Convention defines “predicate offence” as “any criminal offence as a result of which proceeds were generated that may become the subject of an offence as defined in Article 9 of this Convention”; Art. 9 describes the money laundering offences. According to the Warsaw Convention, any offence that originates proceeds may be a predicate offence.

<sup>122</sup> Second Additional Protocol to the European Convention on Extradition.

<sup>123</sup> Additional Protocol to the European Convention on Mutual Assistance in Criminal Matters.

<sup>124</sup> Article 18 of the Warsaw Convention.

<sup>125</sup> Directive 91/308/EEC.

which required a drugs-related countermeasure, but an offence which fed ill-gotten gains into the lawful economy and which therefore required an appropriate response. In June 1997, the European Council, in its Action Plan on Organised Crime, stated that “fiscal authorities should be subjected nationally to a similar reporting obligations for transactions connected with organised crime, at least for transactions relating to value added tax (VAT) and excise”,<sup>126</sup> and that tax fraud linked to organised crime should be treated as a form of organised crime. The European Council recognised that the major driving force behind organised crime is the pursuit of financial gain. It therefore saw the necessity of tackling any economic crime, including VAT and other fiscal frauds.

However, the European Banking Federation reported to the European Commission, in June 1998, that the creation of a fiscal offence under ML would be counterproductive. Firstly, because revenue offences were not seen as serious enough in comparison to organised criminal activities; secondly because tax fraud does not create an identifiable asset which can be detected for ML prevention; and thirdly because the report of all tax-related, suspicious transactions would violate the right to privacy, and because the extension of the scope of ML to revenue offences would alienate many countries otherwise committed to the fight against organised crime. Another argument raised had to do with the fact that some countries did not see anything wrong with money stemming from tax evasion.<sup>127</sup>

In 1998, the UN Office for Drug Control and Crime Prevention presented the results of its report called *Financial Havens, Banking Secrecy and Money-laundering*. The report concluded, among other things, that “one of the key remaining facilitators of crime has been the tax avoidance/evasion exemption in the laundering regulations of many

<sup>126</sup> Paragraph 26(e) of the European Council Action Plan on Organised Crime.

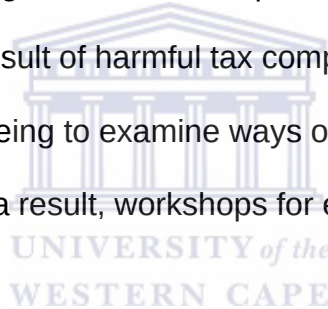
<sup>127</sup> Oliver (2009: 60).



countries".<sup>128</sup> The UNODC did not recommend the inclusion of tax-related crimes in AML regulation, but it warned about the fact that the secrecy veil on tax matters would hamper the combating of ML by leaving open the opportunity of evading conviction by representing transactions as tax-related.<sup>129</sup>

The G7 Finance Ministers, in May 1998, encouraged the tackling of tax-related crimes through the international AML system and through exchanging information on taxes.<sup>130</sup>

A significant move towards the international recognition of the necessity of dealing with tax crimes was made by the OECD's Committee on Fiscal Affairs with the publication of the report titled *Harmful Tax Competition: an emerging global issue*. This document provided defensive measures for restraining harmful tax competition.<sup>131</sup> The OECD work triggered a debate on revenue losses as a result of harmful tax competition. A dialogue between the FATF and the OECD came into being to examine ways of improving co-operation between tax and AML authorities, and as a result, workshops for experts were organised to share expertise in both fields.<sup>132</sup>



In 1999 the FATF adopted an Interpretative Note to Recommendation 15.<sup>133</sup> It dealt with suspicious transaction reports and provided that all reports on transactions concerning tax matters should be allowed to be reported. The idea behind this was that if a link with tax matters would stop suspicious reports, money launderers would always try to make tax

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<sup>128</sup> Blum Levi Naylor Williams (1988: 51).

<sup>129</sup> The link with tax matters was often used as a ground to refuse co-operation and information disclosure for purposes of AML.

<sup>130</sup> OECD (2012c).

<sup>131</sup> See Chapter 2.

<sup>132</sup> OECD (2012c).

<sup>133</sup> Recommendation 15: "If financial institutions suspect that funds stem from a criminal activity, they should be required to report their suspicions to the competent authorities." Interpretative note: In implementing Recommendation 15, suspicious transactions should be reported by financial institutions regardless of whether they are also thought to involve tax matters. Countries should take into account that, in order to deter financial institutions from reporting a suspicious transaction, money launderers may seek to state *inter alia* that their transactions relate to tax matters. See The FATF Recommendations (1996).

related transactions. In the same year the G8 expressed deep concern about the growth in illicit international financial transactions, including money laundering, as well as wide-scale tax evasion, emphasizing how the two phenomena were related to each other.<sup>134</sup> In the UN Convention against Transnational Organised Crime, which was adopted in 2000, the criminalisation of the laundering of the proceeds of crime had to be applied to the widest range of predicate offences.<sup>135</sup> In particular, states were required to include as predicate offences all serious crimes punishable with up to four years' imprisonment,<sup>136</sup> or offences associated with organised criminal groups. Tax crimes were not explicitly mentioned in the text of the Convention. Article 2 refers to "serious offences" (maximum prison sentences of at least four years), and since tax evasion, for instance, may be a criminal offence in one jurisdiction and an administrative offence in another, ML linked to tax offences is not covered by the Convention.<sup>137</sup> However, mutual legal assistance cannot be refused on the sole ground that the predicate offence involved a tax related matter.<sup>138</sup> At the IMF meeting in Washington, in April 2000, the UK's Chancellor of the Exchequer called for a strong response to offshore tax havens and to financial crimes, and raised the need to link ML to tax matters.<sup>139</sup>

After the 9/11 bombings in America, the 40 Recommendations were complemented with 9 special recommendations against the financing of terrorism. Yet, FATF member states were still far from agreeing on whether countries should be compelled to include tax offences as a predicate crime for ML.<sup>140</sup> In 2001, the European Second Money Laundering Directive<sup>141</sup> amended the first one by expanding the scope of the predicate offences to all

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<sup>134</sup> G7 (1999).

<sup>135</sup> Article 6 of the Palermo Convention.

<sup>136</sup> Article 2 of the Palermo Convention.

<sup>137</sup> UNODC (2011: 124).

<sup>138</sup> Article 18(22) of the Palermo Convention.

<sup>139</sup> Alldridge (2001: 350).

<sup>140</sup> Levi (2002: 186).

<sup>141</sup> Directive 2001/97/EC.

serious offences for which suspicious transaction reporting was now mandatory. The Directive also extended the reporting obligation to non-designated financial business and professions (hereafter DNFBPs).<sup>142</sup>

In 2003, the Recommendations were revised, and a common minimum definition of “serious offences” was established. Recommendation 1 left it open to states to choose in the list between the “threshold” or the “all offences” approach. The Glossary listed 20 areas that had to be included. Yet, tax related offences were not explicitly included.

However, the interpretative note to Recommendation 13 (Reporting of suspicious transactions and compliance) states that “suspicious transactions should be reported by financial institutions regardless of whether they are also thought to involve tax matters”.

The United Nations Convention against Corruption (UNCAC), which was signed in 2003, requires States Parties to criminalise the laundering of proceeds deriving from the widest range of predicate offences, as a minimum, from the criminal offences established in accordance with the Convention.<sup>143</sup> Although tax evasion is not mentioned, requests for extradition<sup>144</sup> and mutual legal assistance<sup>145</sup> cannot be refused solely on the ground that the offence involves fiscal matters.

In 2005 the Council of Europe adopted the Third Money Laundering Directive<sup>146</sup> with the aim of providing a common basis for implementing the revised international standards, and to tackle new risks and practices that came into being since Directive 2001/97/EC. Article 3(5) of this Third Directive sets out a range of “serious crimes”. Beyond the listed offences,

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<sup>142</sup> “Designated non-financial businesses and professions mean: Casinos; Real estate agents; Dealers in precious metals; Dealers in precious stones; Lawyers, notaries, other independent legal professionals and accountants” The FATF Recommendations (2012: 112).

<sup>143</sup> Article 23 of UNCAC.

<sup>144</sup> Article 44(16) of UNCAC.

<sup>145</sup> Article 46(22) of UNCAC.

<sup>146</sup> Directive 2005/60/EC.

Article 3(5)(f) takes a general approach with respect to all other offences which carry a punishment of imprisonment based on a mixture of maximum and minimum thresholds.<sup>147</sup> The threshold approach already allowed national jurisdictions to include tax offences, but this was not mandatory.

Nowhere in the Directive is the issue of tax evasion specifically exempted from the list of predicate offences, especially with regard to the obligation of professionals to report suspicious transactions. Tax advisers are not excluded from the duty; on the contrary, the Directive focused attention specifically on the professions.<sup>148</sup>

In 2010, the FATF produced a document in which AML policies were dealt with in conjunction with tax matters<sup>149</sup> in regard to voluntary tax compliance programmes (VTC). VTC programmes may consist of voluntary disclosure mechanisms, tax amnesty incentives or asset repatriation. They are introduced by states with the aim of raising tax revenue, increasing tax honesty and compliance, or facilitating assets repatriation for economic purposes. These programmes encourage taxpayers to declare previous undeclared assets which were held outside of the formal financial system or held in another jurisdiction. The effect would be to give such assets legitimacy. But the verification of repatriated assets is still difficult, given the fact that information on the assets and the taxpayer may be held in different jurisdiction. Furthermore, VTC programmes can exempt financial institutions from the duty to conduct full customer due diligence, and may grant the taxpayer immunity from investigation or prosecution for ML in relation to declared or repatriated assets. Having recognised the potential abuse of such programmes to move

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<sup>147</sup> Article 3 (5)(f). "All offences which are punishable by deprivation of liberty or a detention order for a maximum of more than one year or, as regards those States which have a minimum threshold for offences in their legal system, all offences punishable by deprivation of liberty or a detention order for a minimum of more than six months".

<sup>148</sup> Bridges (2010: 164).

<sup>149</sup> FATF (2010a).

illicit funds, the FATF set out international best practices to assist jurisdictions in their implementation of VTC programmes. The idea was to ensure that such programmes do not impede the effective implementation of AML measures. Although this document does not encompass tax related offences within the AML framework, it identifies the strong relationship between the two phenomena, and the risk of considering them separately. Until the recent revision of the FATF standards, states were never obliged to include tax-related crimes as a predicate offence for ML. Getting international consensus had been easier on issues linked to drug trafficking and terrorism than to environmental crimes and tax evasion.<sup>150</sup> However, a debate on the urgency of tackling large scale tax evasion had emerged. It was prompted by the OECD, the UN, the G20, and other regional organisations. This call to develop an awareness about this issue could not be ignored by the mainstream parties involved in the fight against ML. As a matter of fact, fundamental changes in the international AML framework are triggered by actions undertaken by the FATF.



The discussion now turns to focus on the implications of the FATF Recommendations of February 2012, which include serious tax crimes as a predicate offence for ML.

## **2 The revision process of the 2012 FATF Recommendations**

The FATF Recommendations are subject to periodic reviews. The reason for this is to monitor the relevance of the Recommendations, to keep them abreast of new developments, and to see what countries can learn from the outcomes of mutual evaluations. In preparation for the Fourth Round of Mutual Evaluations, the process of reviewing the Recommendations started already in 2009. In 2010 the first Round of Public Consultation with representatives of the financial sector, the DNFBPs, and non-governmental organisations, was undertaken to assess the first phase of the review. With

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<sup>150</sup> Levi (2002: 182).

regard to tax crimes, the FATF expressed, in a consultation paper, that it was “considering including tax crimes as a predicate offence for money laundering in the context of Recommendation 1”.<sup>151</sup>

## **2.1 The first round of public consultations**

Many stakeholders from the financial sector and from the DNFBPs raised their concerns about the inclusion of tax crimes as designated offences.<sup>152</sup> One of the reasons for these concerns was that small AML institutions find it hard to monitor violations due to lack of capacity, especially fiscal expertise. As to the cost-benefit relationship, the concern here was that the cost of monitoring tax offences is disproportionate to the expected outcome. Another reason for disquiet was that the new requirements would place an additional administrative burden on the financial industry, without taking into consideration time and budget constraints. Other opposing arguments raised were the following: the controversial distinction between tax avoidance and evasion, and legitimate tax planning; and the lack of an internationally accepted definition of tax crimes. In addition, stakeholders lamented the inconsistency of AML preventive measures with the legal framework on tax matters. STRs are effective if filed as soon as transactions are undertaken, but the time lapse between a tax payment and a verification of the correctness of it by national tax authorities, because of protracted court cases involving tax authorities and tax payers and the difficulty of gaining access to information during on-going court proceedings, could undermine the reporting of suspicions. Moreover, banks and other financial institutions would find it cumbersome and impracticable to obtain tax information on foreign customers and to acknowledge tax laws governing international clients. They would therefore have to file an STR each time a company is transacting with a low tax jurisdiction, which could result in over-reporting. The FATF therefore needs to assist financial institutions to identify STRs in

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<sup>151</sup> FATF (2010b).

<sup>152</sup> FATF (2011b; c; d).

relation to tax crimes.

It was observed that, as a matter of principle, financial intermediaries should be absolved from the duty to ensure that national taxes are paid. There were also concerns that to give prosecutors the choice to prosecute alternatively under an AML statute would undermine due process safeguards in the prosecution of tax cases. Some stakeholders suggested that a detailed analysis should be made of the impact of the new provision on national jurisdictions, and that it is necessary to clarify the distinction between avoidance and evasion. Insurance associations considered whether whether insurers and their intermediaries should be required to report taxpayers who have evaded insignificant amount of income or have claimed unsubstantiated tax deductions.

NGOs took also part in the consultation.<sup>153</sup> They observed that the inclusion of tax crimes in the list of designated offences would be a key change in relation to STRs, and that therefore the task force would need to specify the meaning of tax crimes in order to facilitate the work of financial institutions and DNFBPs.

By recognising that every citizen is a victim of tax evasion, some NGOs applauded the prospective change in the Recommendations. Yet, they advocated for a common definition of tax crimes, since leaving the matter to countries would undermine mutual legal assistance and international co-operation. With regard to financial institutions and the probable and understandable concern about the need of knowledge of foreign tax jurisdictions, NGOs stated that these institutions should not act as judges by deciding on their own whether conduct amounts to a fiscal crime, but that their authority should be limited to not more than filing a report on suspicious transactions.

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<sup>153</sup> FATF (2011e).



## 2.2 The second round of public consultations

Between 2010 and 2011 the FATF conducted a second round of public consultations with regard to reviewing the Recommendations. Responses from NGOs and individuals were partly positive, partly critical.<sup>154</sup> The introduction of tax offences was opposed by some respondents on the basis that taxes are specific to jurisdictions. Others supported it on the ground that the information gathering by fiscal authorities would benefit AML efforts and would further the goals of the OECD with respect to tax information exchange. NGOs called for strong collaboration and coordination between the FATF and the OECD to avoid the overlapping of regulations and efforts.

## 2.3 The FATF's official response

In 2012 the FATF published its official feedback to the more than 140 written comments that it had received during the public consultations. In particular, the document states that *"[t]he responses received from the private sector on the inclusion of tax crimes as predicate offences were mixed, with a number of financial representative bodies supporting the proposal in general, while many representative bodies, including DNFBPs' representative bodies, indicating concerns or rejecting the proposal. The concerns relate in particular to: (i) the scope of tax crimes, with a strong preference indicated that only serious tax crimes should be included; (ii) the lack in expertise and the inherent difficulty for the private sector in detecting tax crimes; and (iii) the need for a level playing field. The FATF had considered these concerns and the need to address the growing threat over the laundering of tax crimes proceeds. The change is thus calibrated to focus on the inclusion of serious tax crimes, and is similar to the approach that the FATF has taken consistently in defining the minimum range of predicate offences for money laundering as being serious offences. Countries would, therefore, have some flexibility with respect to the precise offences to be included in relation to its own circumstances"*.<sup>155</sup>

<sup>154</sup> FATF (2011g; h; i).

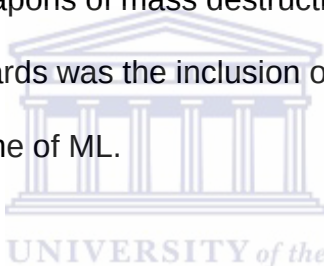
<sup>155</sup> FATF (2011f).



The FATF eventually expanded the scope of ML predicate offences to include serious tax crimes. In order to have a complete understanding of the content and significance of the new provision regarding tax crimes, Recommendation 3 needs to be read together with its Interpretative Note and the Glossary.

### **3 Tax crimes as a predicate offence for ML under FATF Recommendation 3**

The FATF revised standards were published on 16 February 2012. The revision of the Recommendations aimed at strengthening the protection of the integrity of the financial system by providing governments with stronger tools to take action against serious crime.<sup>156</sup> Their scope has been expanded to deal with new threats and priorities, such as corruption, the proliferation of weapons of mass destruction, and cooperation. One of the key changes to the FATF's standards was the inclusion of serious tax crimes in the list of the predicate offences for the crime of ML.



Current Recommendation 3 (which is a summary of Recommendations 1 and 2 of 2006) requires that “countries should criminalise money laundering on the basis of the Vienna Convention and the Palermo Convention”. Countries should apply the crime of money laundering to all serious offences with a view to including the widest range of predicate offences. This Recommendation needs to be read in conjunction with the interpretative note. The note leaves governments free to decide whether to adopt a comprehensive approach, a designated list-approach or a threshold-approach.<sup>157</sup> This freedom of choice is consistent with the fact that countries “have diverse legal, administrative and operational frameworks and different financial systems, and so cannot all take identical measures to

<sup>156</sup> FATF (2012c:2).

<sup>157</sup> Interpretative Note to Recommendation 3: “Countries should apply the crime of money laundering to all serious offences, with a view to including the widest range of predicate offences. Predicate offences may be described by reference to all offences; or to a threshold linked either to a category of serious offences; or to the penalty of imprisonment applicable to the predicate offence (threshold approach); or to a list of predicate offences; or a combination of these approaches”. The FATF Recommendations (2012: 34).

counter these threats, (...) countries should implement measures adapted to their particular circumstances".<sup>158</sup> Yet, whichever approach is adopted, each country should, at a minimum, include a range of offences within each of the designated categories of offences. The Glossary lists among the category of offences, tax crimes (related to direct taxes and indirect taxes)<sup>159</sup> and smuggling (including in relation to customs and excise duties and taxes). When deciding on the range of offences to be covered as predicate offences under each of the categories listed, each country may decide, in accordance with its domestic law, how it will define those offences and the nature of any particular elements of those offences that make them serious offences.<sup>160</sup>

States that do not have tax crimes as predicate offences for money laundering are requested to implement this new provision by extending the scope of money laundering to cover serious tax crimes. Tax crimes constitute a broad category, so national jurisdictions are free to choose which specific conduct to include in this broad category. But only serious tax crimes must be taken into consideration for the purposes of AML, and the seriousness of the tax crime has to be defined in accordance with domestic law.

#### **4 Impact of the Revised Recommendations of 2012 on regional groups**

##### **4.1 Implementation of the FATF regime in relation to tax crimes in Africa**

The two main regional groups in Africa which are required to implement the Recommendations as associate members, are the ESAAMLG (Eastern and Southern African Anti-Money Laundering Group)<sup>161</sup> and the GIABA (Inter-Governmental Action Group against Money Laundering in West Africa).<sup>162</sup>

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<sup>158</sup> Introduction to the FATF Recommendations.

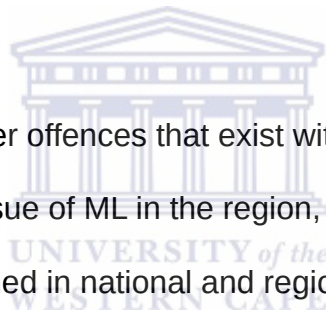
<sup>159</sup> Indirect taxes are, for example, VAT or excise duty. Direct taxes are income or corporation tax.

<sup>160</sup> FATF Recommendation 3.

<sup>161</sup> The ESAAMLG comprises Botswana, Kenya, Lesotho, Malawi, Mauritius, Mozambique, Namibia, Republic of South Africa, Seychelles, Swaziland, Tanzania, Uganda, Union of Comoros, Zambia and Zimbabwe.

<sup>162</sup> GIABA members are: Benin, Burkina Faso, Cape Verde, Côte d'Ivoire, Gambia, Ghana, Guinea Bissau, Guinea Conakry, Liberia, Mali, Niger, Nigeria, Senegal, Sierra Leone, and Togo.

GIABA countries already considered tax crimes as predicate offences for ML, before the FATF revised the Recommendations.<sup>163</sup> The size of the informal economy, the nature of tax evasion, and the problem of corruption make West Africa, in fact, a unique environment for ML and terrorist financing.<sup>164</sup> GIABA identifies the relation between tax evasion and ML as a crucial one for the West African region. In fact, tax evasion, together with smuggling, represents the major categories of predicate offences.<sup>165</sup> High-level tax evasion in this region is mainly committed by high-income earners and corporations, and they do this by withholding tax documentation, understating their revenue or diverting cash into hidden accounts or assets.<sup>166</sup> According to GIABA, the conducting of customer due diligence (CDD) is critically important for preventing the laundering of funds deriving from tax evasion.<sup>167</sup>



Tackling tax evasion, and the other offences that exist within the informal economy, is fundamental to addressing the issue of ML in the region, and therefore all countries need to ensure that tax evasion is defined in national and regional laws and standards, respectively, as a predicate crime for AML purposes.<sup>168</sup>

Until now, among the 12 countries comprising the SADC (Southern African Development Community) that committed themselves through the ESAAMLG, controversies persist on the range of predicate activities for ML. The ESAAMLG took notice of the change in the revised Recommendations, in relation to tax crimes and welcomed the step as an opportunity to facilitate co-operation between national authorities responsible for

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<sup>163</sup> "Tax evasion is a predicate offence for money laundering, as well as a significant weakness – most prominently in terms of budgetary revenues – for many states in West Africa"; GIABA (2010: 19).

<sup>164</sup> GIABA (2010: 5).

<sup>165</sup> GIABA (2010: 7).

<sup>166</sup> GIABA (2010: 20).

<sup>167</sup> GIABA (2010: 22).

<sup>168</sup> GIABA (2010: 31).

investigating and prosecuting tax crimes. Furthermore, the ESAAMLG appreciated the fact that, thanks to this new input in the fight against tax offences, governments will be able to have more public funds at their disposal to support policies and initiatives.<sup>169</sup>

#### **4.2 Implementation of the FATF regime in relation to tax crimes in Europe**

After the FATF Recommendations were revised in February 2012, the European Union committed itself to a rapid updating of the European Union's legal framework to make provision for the incorporation of the necessary changes.<sup>170</sup> Parallel to this process, the European Commission has also undertaken a review of the Third Money Laundering Directive with a view to addressing any identified shortcomings. This review comprises a study of the application of the Directive, and includes extensive contacts and consultations with private stakeholders and civil society organisations, as well as with representatives of EU Member States' regulatory and supervisory authorities. The Report on the application of the Third Directive published by the Commission in April 2012 states that the FATF has included tax crimes in the list of designated offences for ML. The Commission is considering whether the existing "all serious crimes" approach remains sufficient to cover tax crimes; whether tax crimes should be included as a specific category of "serious crimes" under Article 3(5); and whether a further definition of tax crimes is required.<sup>171</sup>

In July 2012, the European Commission published a Summary of Comments on the Report which were made by public authorities, civil society bodies, business federations and companies in several fields (including financial services, the gambling sector, the legal

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<sup>169</sup> FATF (2012b: 2).

<sup>170</sup> "The Commission needs to act fast to incorporate the new standards into existing EU law. To this end, the Commission has already launched a process to review the functioning of the relevant legislation, i.e. the 3rd AMLD, including the publication of an external application study and targeted consultations with private stakeholders and Member States. At the end of March, the Commission will adopt a report on the application of the Third Anti-Money Laundering Directive, following which work will begin on an impact assessment and the accompanying legislation, with the intention of adopting a legislative proposal, amending the 3<sup>rd</sup> AMLD, by end 2012". European Commission (2012b: 4).

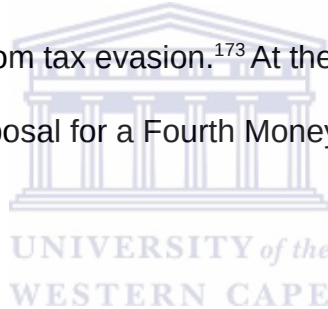
<sup>171</sup> European Commission (2012c: 4).

profession, the real estate sector, as well as trusts and company service providers).<sup>172</sup>

The highest number of responses were on the issue of extending the scope of the Third Directive to include tax crimes as predicate offences for money laundering.

The majority favoured the introduction of tax crimes, because of the necessity of tackling tax evasion under the umbrella of AML, and also because of the fact that national jurisdictions already adopted the "all crimes approach". But, contrastingly, few considered the existing provision to be sufficient, suggesting in the alternative that "serious" tax crimes be limited, possibly by applying a threshold. This, it was said, would exclude errors when filling in income tax returns and when undertaking legitimate tax planning activities.

Stakeholders asked, in addition, for a clear definition of tax crimes and precise guidance in distinguishing tax avoidance from tax evasion.<sup>173</sup> At the time of writing, the European Commission plans to table a proposal for a Fourth Money Laundering Directive in the autumn of 2012.<sup>174</sup>



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<sup>172</sup> European Commission (2012c).

<sup>173</sup> European Commission (2012c: 6).

<sup>174</sup> European Commission (2012a).

## CHAPTER 4

### A CASE STUDY: THE ITALIAN AML REGIME IN RELATION TO TAX CRIMES

The Council of Europe is drafting the Fourth Money Laundering Directive, which will align European law with the FATF revised standards, and will certainly expect EU member states to include serious tax crimes as a predicate offence for ML in their respective jurisdictions. Some countries already consider tax offences as crimes whose proceeds can be laundered. For example, in Austria, Belgium, Finland, France, Germany, Ireland, Italy, the Netherlands, Norway, Spain, Sweden, and the UK violations of tax laws are considered a predicate offence for ML.<sup>175</sup> Many countries, in fact, have adopted the “all crimes” approach.

The 2002 UK Proceeds of Crime Act, for instance, does not refer any longer to certain predicate offences, but to “property obtained through unlawful conduct”,<sup>176</sup> which is defined as property constituting the benefit from unlawful conduct, or which is represented by the person as such.<sup>177</sup> Criminal conduct is any violation of UK criminal law, even if committed abroad. The UK, therefore, has almost abolished the concept of a predicate offence.<sup>178</sup> In relation to foreign tax crimes, however, the prosecution still has to deal with the fact that in many jurisdictions tax crimes are not predicate offences yet.

This chapter, takes a closer look at one national jurisdiction, Italy, with the aim of assessing the suitability of the AML regime to tax crimes, both from a domestic criminal point of view and from the local regulatory perspective.

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<sup>175</sup> Spreutels & Gissels (2000: 12). However, the criminalisation of tax evasion is not homogeneous, for some countries include only tax fraud, some require a link to a criminal group, and in some country there is still a debate going on; Tax Justice Network (2007: 17).

<sup>176</sup> Chapter VII Money Laundering Offence, Proceeds of Crime Act.

<sup>177</sup> Section 242, Proceeds of Crime Act.

<sup>178</sup> Bell (2003: 138).

## 1 Case study: Italy

It has been estimated that in Italy the annual value of money laundered amounts to 150 billion Euro.<sup>179</sup> Italy is a country with a very significant informal economy<sup>180</sup> and a high incidence of organised criminal activities,<sup>181</sup> yet it is an industrialised nation, with one of the higher GDPs. Italy has one of the highest rates of successful ML prosecutions in Europe, with almost 600 cases leading to convictions every year.<sup>182</sup> However, only 5% of total detected ML transactions are prosecuted to a final judgement for ML.<sup>183</sup>

### 1.1 ML in the Penal Code

ML in Italy is currently regulated under Article 648*bis* of the Penal Code.<sup>184</sup> The provision criminalises the transformation or transfer of proceeds of crime, or the creation of obstacles to the identification of the origin of proceeds of crime, when the person did not commit or participate in the commission of the predicate offence (thus excluding self-laundering cases). The punishment is imprisonment between four and twelve years, or a sanction between €1.032 and €15.493. The punishment can be increased if the action is committed in the exercise of a professional activity. The punishment is decreased if the proceeds derive from a crime for which the maximum punishment is less than five years' imprisonment. Predicate offences can be any criminal offences if committed intentionally. The provision is applicable even if the author of the predicate offence is not indictable, or

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<sup>179</sup> Bank of Italy (2011).

<sup>180</sup> The value of the informal economy, which includes legal businesses that are not registered with the revenue authorities, was estimated by the National Statistics Agency in 2008 to have been between € 255 and 275 billion, which equated to between 16,3% and 17,5% of the GDP. ISTAT (2010: 1).

<sup>181</sup> The mafia turnover was estimated as € 100.000 million. Parlamento Italiano (2012: 2).

<sup>182</sup> FATF (2006a: 8).

<sup>183</sup> Argentiero, Bagella & Busato (2008: 342).

<sup>184</sup> Article 648*Bis* c.p. "Riciclaggio: Fuori dei casi di concorso nel reato, chiunque sostituisce o trasferisce denaro, beni o altre utilità provenienti da delitto non colposo, ovvero compie in relazione ad essi altre operazioni, in modo da ostacolare l'identificazione della loro provenienza delittuosa, è punito con la reclusione da quattro a dodici anni e con la multa da euro 1.032 a euro 15.493. La pena è aumentata quando il fatto è commesso nell'esercizio di un'attività professionale. La pena è diminuita se il denaro, i beni o le altre utilità provengono da delitto per il quale è stabilita la pena della reclusione inferiore nel massimo a cinque anni. Si applica l'ultimo comma dell'articolo 648. (Le disposizioni di questo articolo si applicano anche quando l'autore del delitto da cui il denaro o le cose provengono non è imputabile o non è punibile ovvero quando manchi una condizione di procedibilità riferita a tale delitto)".



not punishable, or when the proceeding for that offence is not admissible.<sup>185</sup> A peculiarity of the Italian legal framework is that self-money laundering is not included, because Article 648*bis* covers only the hypothetical situation of the money launderer who did not commit or participate in the predicate offence. The Legislature's intention was to respect the double jeopardy principle. However, this makes Italy a "legal paradise for self-money launderers",<sup>186</sup> and has been, in fact, questioned by the FATF in the Mutual Evaluation Report (MER) of 2006.<sup>187</sup>

ML is complemented by two other offences in respect of which the possession or acquisition of the proceeds crime or their use for economic or financial purposes is punishable.<sup>188</sup> The *mens rea* required is generic intent (which encompasses *dolus eventualis*). This also covers knowledge of unlawfulness which, in this case, means knowledge of the criminal origin of the assets, as well as the wilful impeding of the identification of the criminal provenance of the assets.<sup>189</sup> The Italian legal system does not provide for the criminal liability of companies, only for administrative sanctions.<sup>190</sup> Article 648*quater* requires the confiscation of the proceeds or the equivalent, without violation of the rights of *bona fide* third parties. The law allows for the prosecution of persons who assisted in the commission of the tax offence, without participating in the commission, for example, where the proceeds of the crime are transferred to the bank account of a family member or to that of a financial advisor. However, ML is punished more severely than tax offences.

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<sup>185</sup> Corte di Cassazione 11/05/2005 n° 23396. In this case the Supreme Court stated that even though the fiscal offences were remitted by a voluntary tax compliance law, the proceeding for ML was not affected.

<sup>186</sup> Razzante (2012: 8).

<sup>187</sup> FATF (2006a: 26).

<sup>188</sup> Articles 648 and 648ter c.p.

<sup>189</sup> Corte di Cassazione 30/01/2007 n° 6350; Corte di Cassazione 18/12/2007 n° 16980.

<sup>190</sup> Legislative Decree 231/2001.



## 1.2 AML regulations

With regard to the prevention of ML, the Italian AML regulations are found in the Legislative Decree number 231 of 2007, which domesticates the Third European Money Laundering Directive, and which is, in fact, more in line with the international AML standards. The definition of ML, particularly insofar as it refers to prevention, includes also a hypothesis of self-laundering, and concealing and disguising the proceeds of crime is punishable even where the aim is to conceal not only the origin of the property, but also its ownership.<sup>191</sup> Article 36 of the Decree allows the use of information collected in the fulfilment of AML preventive measures, for fiscal purposes. The preventive measures are based on those set out in the FATF's Recommendations. The FATF has found Italy compliant in respect of almost all the preventive measures, except for the regulation of DNFBPs, Politically Exposed Persons, and the absence of specific requirements for cross-border correspondent banking operations, with respect to gathering of information.<sup>192</sup>

## 1.3 Revenue offences

Tax evasion has a great impact on Italian economy.<sup>193</sup> Tackling tax evasion is a priority in relation to the current financial crisis, as the governor of the Bank of Italy affirmed in 2011.<sup>194</sup> The National Agency for statistics (ISTAT) calculated that the undeclared VAT in Italy in 2008 amounted to 9,8% of the GDP.<sup>195</sup>

Tax related offences are regulated under the Legislative Decree number 74 of 2000, as amended by the Law 148 of 2011. The following categories of conduct are criminalised: fraudulent or non-declaration of income or value added tax in excess of a prescribed amount; the issuing of false invoices; the concealing or destruction of financial accounting

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<sup>191</sup> Article 2(1)a; b of the Legislative Decree 231/2007.

<sup>192</sup> FATF (2006a: 101).

<sup>193</sup> FATF (2006a: 12).

<sup>194</sup> Bank for International Settlements (2011: 1).

<sup>195</sup> ISTAT (2010: 3).

books, or the failure to pay tax.

Tax avoidance is not criminalised under this law. However, the Supreme Court (*Corte di Cassazione*), in various decisions, has recognised the existence of a general principle of anti-avoidance, which can be inferred from Article 53 of the Constitution.<sup>196</sup> In particular, tax payers are not allowed to benefit fiscally from the abuse of loopholes existing in the law. Even though the conduct might not violate the law, if the person acts in fault of an economic reason that justifies the operation, different from mere tax saving, the conduct amounts to tax avoidance and is thus unlawful.<sup>197</sup>

#### **1.4 Is tax evasion a predicate crime for ML?**

The question whether tax offences can trigger a charge of ML has been long debated.

Arguments raised by those who disagree with the inclusion of tax offences under ML are linked to the nature of the criminal property, and to the fact that proceeds from tax evasion are usually intermingled with lawfully earned money. In particular, what derives from tax evasion is not a concrete profit, but a tax saving. By contrast, a predicate offence should generate new wealth, and not an undue advantage such as, say, the avoided impoverishment of the particular property.<sup>198</sup> The impossibility of identifying the actual proceeds of the criminal conduct in the pool of money deposited into and held in a bank account, brought the Italian Supreme Court to block the freezing of a bank account.<sup>199</sup> There is still a raging debate on whether the proceeds of tax evasion should be regarded as criminal property susceptible to ML. However, a judgement handed down by the Italian Supreme Court in 2009, confirmed that the concept “proceeds of crime” can refer to an economic gain, which is added to the assets of the accused.<sup>200</sup>

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<sup>196</sup> Article 53 states that everyone must contribute to public expenditure, according to their *capacità contributiva*.

<sup>197</sup> Corte di Cassazione 23/12/2008 n° 30055.

<sup>198</sup> Cosseddu (2011: 6).

<sup>199</sup> Corte di Cassazione 07/12/1992 n° 2206; Corte di Cassazione 20/09/2007 n° 38600.

<sup>200</sup> Corte di Cassazione 25/06/2009 n° 38691.

In a landmark decision in 2008 the Supreme Court held that the crime of ML, as regulated under Article 648*bis* of the Penal Code (as amended), which aligned national law to international standards, discharges the accused from being found guilty, too, of committing the predicate offence. The court went on to affirm that, currently, all criminal offences committed intentionally can trigger a ML conviction, and among them are not only the typical ones such as corruption, bankruptcy crimes, and corporate crimes, but also fiscal offences.<sup>201</sup>

Therefore, the unlawfulness of the origin of the money has to be interpreted not in a physical-materialistic way (as the entry of illegal monies into the property of the accused), but in an economic sense. The profit, in fact, would not accrue to the assets of the accused without the criminal conduct occurring. The rationale here is that the money passes from a legal to an illegal status.

Moreover, Article 1(143) of Law 244 of 2007 introduced a provision which allows for property to be confiscated to the value of its equivalent in the proceeds of the fiscal crime committed. By analogy, this provision could apply to ML cases as well.

The predicate offence, consisting in a tax crime, is relevant even if committed abroad, if the conduct is considered a crime under the domestic law of that country, too. This is what a sentence of the Supreme Court established in relation to a case of ML where the proceeds derived from a fiscal offence committed in Spain. After having requested mutual legal assistance from Spain, and after having issued assurances that the relevant conduct

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<sup>201</sup> "Il delitto di riciclaggio (...) è oggi svincolato dalla pregressa tassativa indicazione dei reati che potevano costituire il presupposto, esteso attualmente a tutti i delitti non colposi previsti dal codice penale (per cui il delitto di riciclaggio può presupporre come reato principale non solo delitti funzionalmente orientati alla creazione di capitali illeciti quali la corruzione, la concussione, i reati societari, i reati fallimentari, ma anche delitti che, secondo la visione più rigorosa e tradizionalmente ricevuta del fenomeno, vi erano estranei, come ad esempio i delitti fiscali e qualsiasi altro)" Corte di Cassazione, 27/11/2008 n° 1024.

constitutes a crime punishable with imprisonment under national law, the court proceeded with the ML charge.<sup>202</sup> In a judgement released on 24 February 2011, the Supreme Court confirmed the confiscation of assets, obtained through tax fraud, and considered these as laundered proceeds.<sup>203</sup> The persons accused were part of a criminal association. They did not participate in the commission of the tax offence and were therefore held liable for ML. The confiscation order aimed at the seizure of the equivalent value of the amount of proceeds deriving from the fiscal fraud and subsequently laundered. In a very recent case, the Court held in its reasoning concerning the lawfulness of a freezing order, that ML predicate offences, for which asset recovery can be undertaken, can be also tax-related crimes.<sup>204</sup>

In another recent judgement, the Court dismissed the charges for ML in respect of the proceeds of corporate tax evasion, despite recognising that the conduct did constitute a predicate offence, because the accused person participated in the commission of tax evasion, as a shareholder of the company.<sup>205</sup> In July 2012 the Court found an individual guilty under Article 648bis of the Penal Code, because he/she was involved in the concealing of assets derived also from tax fraud that was perpetrated by means of real estate transactions in Milan and through bank accounts held in the Principality of Monaco and in Switzerland. Notwithstanding the fact that the money was still traceable, because the person declared the dividends of those activities, the court asserted that the mere fact of having transformed them, in order to conceal the illicit origin, amounted to ML.<sup>206</sup> In this case, too, one of the predicate offences was a tax crime.

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<sup>202</sup> Corte di Cassazione, 17/11/2009 n° 49427.

<sup>203</sup> Corte di Cassazione, 24/02/2011 n° 11511.

<sup>204</sup> Corte di Cassazione, 14/02/2012 n° 10359.

<sup>205</sup> Corte di Cassazione, 15/06/2012 n° 36757.

<sup>206</sup> Corte di Cassazione, 13/07/2012 n° 32936.

## 2 Conclusion

From the discussion above we may conclude that in Italy tax evasion can be a predicate offence for ML. Yet the recognition of fiscal crimes as a source of criminal property is still controversial. The doctrine is still controversial. The process of implementing the revised Recommendations through the Fourth Money Laundering Directive should shed more light on some of the issues in dispute and would help to guarantee a uniform and coherent application of the standards. In Italy, controversies seem to arise mostly in relation to making fiscal crimes money laundering predicate offences. In other European countries, the reservations also concern the regulatory side. The Italian Financial Intelligence Unit (FIU) took notice of the fact that the revised version of the FATF Recommendations includes tax crimes among the designated offences.<sup>207</sup> The FIU observes that tax evasion and ML are two phenomena that are linked to each other, because often the first is used to create funds utilised for criminal purposes, and that money launderers and tax evaders use the same financial tools and subterfuges to get around the law; the effects of both forms of conduct are the distortion of economic competition and of the allocation of resources.

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<sup>207</sup> Banca d'Italia (2012: 1).

## CHAPTER 5

### CONCLUSIONS AND RECOMMENDATIONS

This paper has discussed the suitability of the anti-money laundering regime to tackle fiscal crimes. It concludes that tax crimes can and should be addressed as predicate offences for ML. The second chapter has debated the topic from a theoretical point of view, by analysing how the two phenomena of tax evasion and ML relate to each other. The third chapter has addressed the matter in relation to the negotiations that have been undertaken at an international level, between trans-governmental organisations and private stakeholders, and within regional groups. The fourth chapter has presented one national perspective, by looking at the local legal debate that comes to light between the doctrine and the jurisprudence. In summary, it can be said that the AML regime is appropriate for dealing with tax crimes, because it provides a very sophisticated prevention system that has not only the potential of discouraging would-be tax evaders, but can also be a deterrent for professionals involved in high-level tax-dodging practices. Furthermore, leaving fiscal crimes out of the AML regime would enable money launderers to exploit a “tax loophole” by suggesting that their transactions are driven by tax reasons and not by the intention to conceal criminal property.

The discussion has showed that the FATF Recommendations, in particular, are the right instrument to address fiscal crimes. Notwithstanding concerns relating to the fact that the FATF standards are not a conventional source of international public law, as a matter of fact, this instrument has proved to be very effective in influencing regional legal frameworks, and thus national AML policies. Despite the fact that many jurisdictions in the world already classify tax offences as predicate crimes for ML, the matter is still a topic of debate, and the dissimilarities between national regulations can undermine international

co-operation with regard to this matter. Therefore, the change in the Recommendations, which should result in a higher level of harmonisation, could tighten up the global combating of tax evasion.

At the time of writing, for example, 10 EU States are ready to adopt a unified financial transaction tax<sup>208</sup> for purposes of tackling the fragmented system of financial transactions tax. This is necessary in order to prevent distortions in competition and to avoid the risks of double-taxation and double non-taxation. It also diminishes the costs incurred by businesses to ensure that they remain compliant with the law.

States need to aim at reducing opportunities for people and companies to avoid paying tax. There is also a need to increase transparency in business dealings and to encourage the exchange of information between the state and the main role players in the economy, for this can contribute to the financial sector paying its proper share of the tax and not leaving the ordinary citizens burdened with onerous taxes.<sup>209</sup> Once the tax is approved, it will be important to guarantee co-operation between states. In particular, if the Fourth Money Laundering Directive will recognise tax crimes as predicate offences for ML, as set out in the revised FATF Recommendations, the application of these two provisions may result in a very effective action against the abuse of the financial system to the detriment of public revenues. Tax advisors, lawyers and accountants will have the duty to report transactions which might have a tax-dodging purpose. This, added to the new tax on financial transactions and the facility of exchanging information between states, will result in a strong disincentive for engaging in cross-border machinations aimed at tax

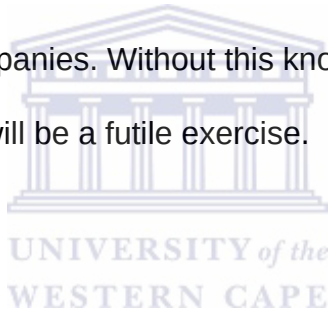
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<sup>208</sup> Austria, Belgium, France, Germany, Greece, Italy, Portugal, Slovakia, Slovenia, Spain, on the basis of European Commission proposal for a Directive on a financial transaction tax of September 2011, have asked the Commission to proceed through enhanced co-operation, to promote co-operation on a financial transaction tax among them; European Commission (2012b).

<sup>209</sup> European Commission (2012b).

avoidance or evasion.

The new FATF standards are a big step, indeed, in the direction of ensuring a more sustainable pool of public finance. However, there is still much to be done. Concerns have already been raised by some non-governmental organisations<sup>210</sup> about the missed chance of demanding more transparency in the financial system. What has been subject to most criticism is the fact that, without an obligation being imposed on states to publish a register of the ultimate beneficiaries of companies, shell companies will be still able to hide tax evaders. They will thus remain unpunished, notwithstanding the new severe regulation. As a result, the fight against tax crimes on a global scale could be undermined by the difficulty of gaining access to information about who are in fact the ultimate or beneficial owners of these anonymous companies. Without this knowledge, charging only the frontline actors with tax evasion will be a futile exercise.



(Word count: 18.301)

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<sup>210</sup> Global Financial integrity (2012); Financial Task Force (2012); Tax Justice Network (2012); Tax Research UK (2012).



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