What does a risk based approach mean for tax practitioners?

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The AML risk based approach

What will we be talking about today?

- What do we mean by the risk based approach?
- What risks and red flags do tax advisers come across?
- Practical ways to manage and mitigate risk
- Practice and client risk assessment

What is risk?

RISK ....

is generally viewed as the possibility or chance of loss, danger or injury

What is money laundering and terrorist financing MLTF risk?

MLTF RISK ….

is generally viewed as the possibility or chance of money laundering or terrorist financing taking place in the circumstances in question.

Businesses are required to analyse the risks THEY face and make proportionate responses to them.

What is the MLTF risk based approach?

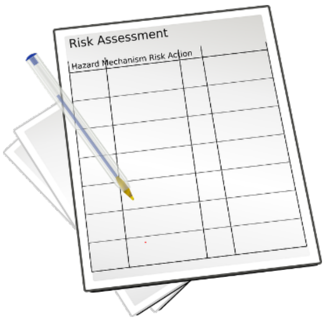
Key legislative requirements are:

"18.—(1) A relevant person must take appropriate steps to identify and assess the risks of money laundering and terrorist financing to which its business is subject.

(3) In deciding what steps are appropriate under paragraph (1), the relevant person must take into account the size and nature of its business".

What is the MLTF risk based approach?

What is the point of assessing risk?



Once a firm has assessed risk the regulations state

“19.—(1) A relevant person must—

(a) establish and maintain policies, controls and procedures to mitigate and manage effectively the risks of money laundering and terrorist financing identified in any risk assessment undertaken by the relevant person under regulation 18(1);”

What is the MLTF risk based approach?

A risk based approach means:

- You have considered the risks for **your business** .
- The approach taken to do this should be appropriate for your size of business.
- Evidence based decision making enables you to better target risks. Once you have identified the risks you can focus energy and resources on dealing with those risks and put appropriate policies and procedures in place to do that.
- Senior management must be involved.
- Risk needs to be kept under review

Overall your approach has to be tailored to the risks your business has identified

What risks should be considered?

The regulations set out categories of risk as follows:

- Clients
- Countries or geographic areas in which it operates;
- Products or services;
- Transactions; and
- Delivery channels

And also require supervised firms to refer to the risk assessment prepared by their AML supervisor and the National Risk Assessment (NRA).

Common areas for tax advisers - what risks should be considered?

The risks in each category need to be considered for your firm

Further information on high risks and low risks in each category are set out in the Money Laundering Regulations (reproduced in appendix D of AMLGAS)

Firms should also consider the NRA and supervisory risk assessment prepared by the CIOT and ATT:

https://www.tax.org.uk/professional-standards/consultations-articles/aml-guidance-%E2%80%93-supervisory-risk-assessment

https://www.att.org.uk/attciot-supervisory-risk-assessment-money-laundering-terrorist-financing-mltf

Common risk areas for tax advisers – case studies

Case Study A

A new client approaches you and from an initial discussion you find out:

a. They are a self-employed individual
b. 40% of takings are from cash
c. They have recently bought a holiday home in the Algarve
d. They can't come into the office because of COVID restrictions
e. They want their accounts and tax return dealt with by the end of next week

What red flags and risk factors can you spot here?

Common risk areas for tax advisers – case studies

Case Study A – continued

Assess risk and put in place appropriate policies and procedures to manage and mitigate risk:

- What are your CDD procedures and how do you manage and mitigate risks where you cannot meet clients?
- What CDD do you do in relation to transactions to ensure you identify proceeds of crime and can make a suspicious activity report if you need to?
- What procedures are there for cash businesses to ensure that cash is recorded accurately and income is not understated?
- How do the staff know what to do on which businesses and how to make an internal report?

Common risk areas for tax advisers – case studies

Case Study B

Your client runs a successful garden centre business.

- They have decided to diversify and have set up a company to produce PPE. This company has a complex ownership structure and wants to claim COVID 19 government support.
- They have also set up a hand car wash behind the garden centre
- The client also wants you to start doing payroll work. They have a huge number of people working different shifts but everyone appears to be paid the same.

What red flags and risk factors can you spot here?

Common risk areas for tax advisers – case studies

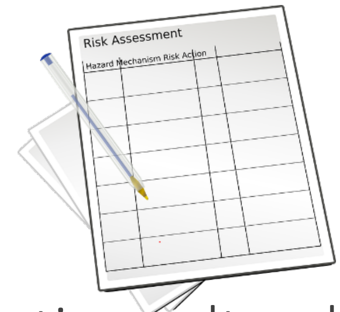
Case Study B continued

A risk based approach includes:

- A consideration of what type of work you will take on because of the risks of undertaking work you are not familiar with.
- Undertaking CDD to understand why clients want a particular company structure.
- Having payroll procedures to ensure you ask appropriate questions where there might be any red flags for human trafficking or modern slavery.
- Putting in place a high risk rating and undertaking further monitoring where COVID 19 government support schemes might be abused.

Common risk areas for tax advisers – case studies

Case Study C



A client who was born in one of the FATF high risk jurisdictions has decided to set up a new trade importing cultural artefacts from the country of his birth and neighbouring countries.

A google search indicates he is the brother of a government minister in that country. The brother has approached you because he wants to purchase property in Mayfair and would like you to set up his company and provide ongoing compliance services.

What red flags and risk factors can you spot here?

Common risk areas for tax advisers – case studies

Case Study C continued

A risk based approach includes:

- A knowledge of the high risk factors in the legislation relating to the importing of cultural artefacts.
- Checking the high risk third country lists, financial sanctions lists and PEP details as part of CDD.
- Ensuring appropriate due diligence is undertaken for clients based overseas.
- Being alert to the risks of overseas individuals purchasing UK property.
- Are you used to dealing with work of this nature or is it outside your normal expertise?

Risk factors - clients

We've looked at a mixture of risk factors in the case studies but client risk factors include clients:

Seeking anonymity or undue secrecy

Those outside normal client base

Frequent changes of professional adviser

Emerging sectors

High Net Worth individuals – particularly PEP or high profile

Resident in a high risk jurisdiction

Complex structure, nominee shareholders etc

A criminal history

Cash based businesses

Risk factors – clients (cont)

The risk factors highlight the need to look out for MLTF but do not mean the client is automatically involved. You need to consider red flags in relation to the risks eg.

Property transactions with no clear source of funds

Cash businesses with unexplained weeks of no income

Rapid rates of turnover (trades for a short time then closes down and starts up again)

Risk factors - geographical

Concerned here with clients or other parties to a transaction based in certain countries:

Countries that do not have effective MLTF controls (FATF lists)

Countries with significant levels of corruption (transparency international lists)

Countries with organisations etc subject to sanctions (OFSI lists)

Risk factors – product or service risks

The accountancy sector is used by criminals to give a veneer of legitimacy to businesses involved in money laundering including:

Trust and company services

Aggressive tax schemes

Investment business

Government support schemes

Legitimising books and records

Insolvency services

Tax investigations

Payroll services

Risk factors – transaction or delivery channel risks

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Factors here include:

Clients' money bank accounts

Transactions involving certain products

Clients not met (if certain safeguards are not in place)

New ways of delivering services to clients and new technology

Practical ways to manage and mitigate risk

The starting point is always……

Identifying the risks in relation to your own clients and your own practice. It will be exceptionally rare for firms to have no clients with inherent risks even if:

- All clients are local
- Clients have been on the books for years
- Work is comfortably within your area of expertise.

Be alert and maintain professional scepticism

Practical ways to manage and mitigate risk

Once the risk is identified…

Document those risks in your practice wide risk assessment

Ensure policies and procedures are in place to manage and mitigate those risks and document those as well

Review risk regularly and update policies and procedures as required

The written practice risk assessment

- Remember that a written risk assessment and written policies and procedures document are required even for sole practitioners with no staff.
- As supervisors the CIOT and ATT will expect to see what risks you have identified so make sure you have backing information.
- The CIOT and ATT have a pro forma document available and a number of training providers also have these. They MUST be tailored to your practice.

The written practice risk assessment (cont)

- Depending on the set up of the firm and services provided risks may be different in different parts of the business. Consideration then needs to be given to how to manage the client across the business.

- Risk assessment can take into account the business's experience and knowledge. For example if the business has no experience of a particular country it might rate associated work as high or medium risk although another firm may rate it as low risk.

Risk assessment of individual clients

- Remember to assess the risk in relation to each client at the time you take them on and make sure you document this.

- Review the risk assessment as part of ongoing monitoring. The firm changes, clients change, services change and therefore risks may change.

Policies and procedures to manage risk

The aim of all the practice policies and procedures is to manage and mitigate risk and ultimately to report matters where MLTF is identified.

It should not be a tick box approach. Make sure all the policies and procedures you have are tailored to the risks in relation to your firm and clients (the risk based approach):

- Client due diligence (CDD)
- Risk assessment
- Ongoing monitoring of CDD and risk
- Record keeping and destruction of documents
- AML Training
- Suspicious Activity Reporting

Policies and procedures to manage risk – areas relevant to tax advisers

We will now have a look at some of the ways firms adopt a risk based policies and procedures where they deal with:

Cash based businesses

Complex business structures

Overseas clients/High net worth clients and those who cannot be met face to face

Remember it is not a tick box exercise

Policies and procedures to manage risk – cash based businesses

- Knowing the client and their business is key.
- Consider visiting and see how cash is managed.
- Set out expectations at the start that all income has to be declared.
- Make it clear in the firm's records that client is medium/high risk so all staff dealing with the client are reminded to be vigilant
- Staff training should cover the additional risks and red flags and firm's procedures for dealing with these businesses.

Policies and procedures to manage risk – cash based businesses (cont)

- Spreadsheet pro forma provided
- Cloud accounting
- Getting records sent in more regularly
- Reconciling to till receipts and making sure till rolls are used
- Ensuring trained accountancy staff are on site doing spot checks on what happens with cash
- Monitoring gross margins/gaps in records lifestyle changes
- Continue to review and ask appropriate questions each year
- Ensure staff are clear about internal suspicious reporting procedures where they have concerns

Policies and procedures to manage risk – complex ownership structures

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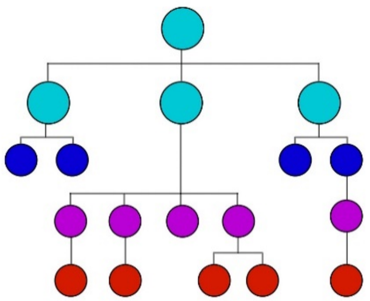
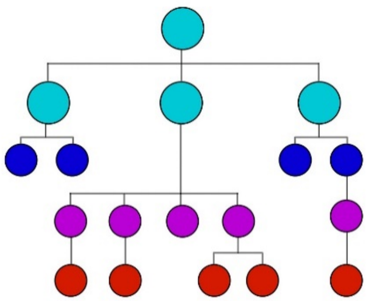


- Knowing the client and their business is key
- Work through the structure and ensure the beneficial ownership is understood (do not rely on Companies House PSC register)
- Make sure you understand the reasons behind the structure and where the initial funding/wealth came from
- Is the structure being used to hide assets and wealth?

Policies and procedures to manage risk – complex ownership (cont)



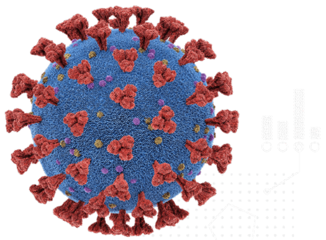
- Are there commercial reasons why the structure is being used?
- Is it an area of work and a structure you are familiar with – working outside your area of expertise increases the risks?
- Do you know the other advisers involved with the client and how does that impact on the risk?
- Ensure risk assessments, staff training etc cover this area

Policies and procedures to manage risk – overseas clients and HNW, plus those not met

- Where you cannot meet consider how CDD will be done including:
  - Electronic checks
  - Certified documents
  - Post office id certification service
  - Financial sanctions checks
  - Additional documentation
  - ZOOM calls etc
  - Make sure you know about the source of wealth and source of funds. Risks on HNW clients can vary widely.

COVID 19 Risks

Ensure your risk assessment takes into
Account emerging COVID risks:

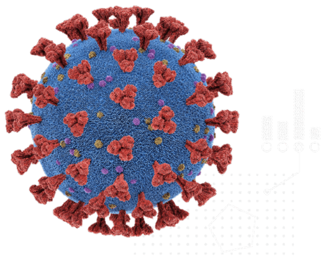


- The set up of companies at short notice particularly where they have COVID, PPE or tracking in the name as there are instances of such companies being used for abuse of government support schemes.

- Unexplained deposits into accounts particularly where there has been reduced trading

COVID 19 Risks (cont)

- Businesses claiming under the furlough scheme whilst employees continue to work



- Changes in client business to now provide PPE and hand sanitizer where not previously part of their business – has there been a genuine change of trade?

Further COVID 19 Professional Standards guidance is available on the website:

https://www.tax.org.uk/professional-standards/consultations-articles/some-professional-standards-matters-consider-result

Summary - what is the MLTF risk based approach?

We have looked at a number of risks and red flags and considered what firms can do to manage and mitigate risks

A risk based approach means identifying risks for your firm and using that information to inform your policies and procedures to manage and mitigate risk.

Money Laundering Risk Areas
Further information

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- Government information – National Risk Assessment (NRA) – watch this space
- Supervisory information - Supervisors supplement the findings in the NRA with their own detailed assessments of risks in their own sectors.
- AML Guidance for the Accountancy Sector
- NCA website

Money Laundering Risk Areas
Further information

Further guidance on AML is available via the professional standards sections of the CIOT and ATT websites:

http://www.tax.org.uk/professional-standards

https://www.att.org.uk/professional-standards

If you have any queries or want to talk through potential suspicious activity reports where we are AML supervisors please email standards@ciot.org.uk or standards@att.org.uk

Tax advisers and the risk based approach

Any questions?