



Association of Accounting Technicians response to the Department for International Trade consultation on Freeports

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1. Introduction

- 1.1. The Association of Accounting Technicians (AAT) is pleased to respond to the Department for International Trade's consultation on Freeports, published on 10 February 2020.
- 1.2. AAT is submitting this response on behalf of our membership and for the wider public benefit.

2. Executive summary

- 2.1. **Association of Accounting Technicians (AAT) understands and supports the desire to increase investment and promote economic growth, especially post-Brexit. However, the proposed introduction of Freeports as a means of achieving this, raises serious concerns from an anti-money laundering (AML) perspective.**
Freeports are vulnerable to illicit activity in part because by providing preferential treatment, they resemble offshore financial centres, offering both high security and discretion to users, allowing transactions to be made without attracting the attention of regulators. This does not sit well with the importance of establishing and maintaining a consistent and robust AML supervisory regime in the UK.
- 2.2. **AAT believes that regulatory requirements are only meaningful when effectively enforced.**
The recent transposition of the 5th Money laundering directive (5MLD) on 10 January 2020 placed a greater emphasis on regulated entities in relation to the client due diligence process. However, the creation of Freeports endangers the effective implementation of the directive by reducing the due diligence burden for goods in Freeports.
- 2.3. **The Luxembourg Freeport example indicates it may be possible for the UK to introduce Freeports whilst simultaneously requiring them to meet all necessary AML requirements.**
Please see below at 1.14 and 1.15 for further information.

3. AAT response to the consultation paper

Q47: In your view, what is the level of risk of illicit activity in Freeports? Please explain your answer

- 3.1 AAT considers the level of risk of illicit activity in Freeports to be high because they lack regulation, which makes them conducive to secrecy. Introducing 'special economic zones', which have been highlighted by FATF as presenting a unique money laundering and terrorist financing threat¹ sits uneasily alongside the UK's wider efforts to fight economic crime.
- 3.2 Ultimately, for all their purported economic benefits, Freeports are not without significant drawbacks. The relative secrecy and lax regulation associated with Freeports make them no different from offshore financial centres that risk becoming havens for money laundering and tax evasion. AAT is concerned that this suspension of fiscal responsibilities may lead to an oversight of customs' security functions, who are obligated to report any suspicious transactions they encounter to a national financial intelligence unit. Instead, goods will be entering and leaving Freeports with little or no safeguards regarding the legitimacy of the cargo. As such, AAT also considers Freeports to pose a serious risk with regard to counterfeiting, as they allow counterfeiters to land consignments, adapt or otherwise tamper with loads or associated paperwork, and then re-export products without customs intervention, enabling the disguise of both the nature of the goods and the original supplier.

¹ Financial Action Task Force report, Money laundering vulnerabilities of free trade zones, March 2010:
<https://www.fatf-gafi.org/media/fatf/documents/reports/ML%20vulnerabilities%20of%20Free%20Trade%20Zones.pdf>

- 3.3 Moreover, because Freeports rely on self-declarations of the value of any export, there is no insight into whether goods have been assigned a false value as part of a trade-based money laundering scheme. Therefore, illegal transactions can be easily disguised as legal, using trade-based money laundering schemes that are notoriously difficult to detect.
- 3.4 As precise information on the Ultimate Beneficial Owners (UBO) is not required, it is relatively simple to hide the UBO's identity behind another layer of secrecy, such as an offshore firm, a trust, a lawyer or a combination of both. Likewise, as Freeport operators are not financial institutions, they are not obliged to provide bulk data regarding their clients to tax authorities unless upon request. This will undoubtedly only make them more attractive to those looking to facilitate money laundering. Such a lack of transparency ultimately permits unsourced goods to be bought and sold with cash.
- 3.5 AAT therefore considers Freeports to be structurally problematic when it comes to preventing abuse of the financial system. Freeports give those who are looking to commit wrongdoing the secrecy that they require. This leads AAT to question how the obligations of existing AML legislation can effectively be met where the operation of Freeports is based on the premise of limited oversight.
- 3.6 AAT acknowledges that the Government appears aware of the level of risk in relation to tax evasion created by Freeports, and that HMRC is involved in their design with a view to limiting this. However, AAT is not reassured that AML aspects are being given the same degree of consideration. This concern has been increased by recent comments from Treasury Minister Steve Barclay, who whilst acknowledging tax concerns, completely ignored the significance of money laundering considerations when given the opportunity to do so.²

Q48: What additional measures should be implemented to mitigate such activities?

- 3.7 Regulatory requirements are only meaningful when backed up by enforcement. AAT believes that under current proposals the success of the AML framework will largely depend on the good faith of Freeport operators and their willingness to act as AML gatekeepers by reporting suspicions. Even with 5MLD in force, AAT considers the likelihood of exchanges of information between tax authorities and regulators will be low because of the limited access to AML data kept by non-financial obliged entities such as Freeports.
- 3.8 As such, if the Government insists on the creation of Freeports, AAT believes there should be consideration given to establishing an overarching governance body to monitor them. To reduce the risk of illicit finance, the government could consider requiring Freeport administrators to take on supervisory duties. Ideally, customs officials and administrators should be required to share information and customs security checks should be standardised and frequent.
- 3.9 There should also be consideration given to an extension of other types of goods subject to 5MLD oversight. For example, if there is believed to be a danger associated with the use of Freeports for the storage of artworks, because they are the type of asset that might attract a money launderer, then it seems logical to capture other high-value goods over €10,000. AAT believes that such AML obligations must be extended to other types of goods if Freeports are to be effectively protected from criminals.

Q49: Please provide any other comments you have on the issue of preventing illicit activity within Freeports.

- 3.10 AAT recognises that information sharing plays a vital role in fighting money laundering and terrorist financing measures. The fifth EU Directive on Administrative Cooperation (DAC5) provides for tax authorities to have access to UBO information and other information collected by obliged entities under the 5MLD.

² Steve Barclay MP, 4 March 2020:

<https://www.parliament.uk/business/publications/written-questions-answers-statements/written-question/Commons/2020-02-27/22013/>

- 3.11 The use of Freeports under current proposals presents many challenges from an information sharing perspective. It is unclear how declaration requirements, as proposed in this consultation, when moving goods into Freeports, would work in practice in with anti-money laundering legislation. This raises questions regarding the circumstances under which tax authorities can access UBO information held by obliged entities, such as Freeport operators.
- 3.12 Despite sharing common features with financial institutions, Freeports are considered non-financial obliged entities. As such, income generated by art or other moveable property in Freeports does not currently fall within any automatic exchange category of information between tax authorities. Therefore, bringing operators such as auction houses and dealers under the 5MLD will pose tremendous challenges for tax authorities, but also for supervisors. Even if national legislation required UBO information to be kept on record, the question remains as to what extent that information is accessible for other authorities and to what extent it could be shared with tax administrations in other countries. However, 'fishing' in the data held by non-financial obliged entities is not allowed other than via 'access upon request'. Tax authorities must know who and what they are looking for before requiring access to UBO information.
- 3.13 Under these proposed Freeport conditions, AML legislation cannot be said to function as a strong deterrent against money laundering. As a result, AAT considers that the introduction of Freeports, without imposing some form of AML requirements, would result in the UK system working in parallel and separate ways, which will ultimately place a further burden on law enforcement agencies.
- 3.14 Luxembourg makes for a good case study of a potential way forward. This Freeport, established in 2014, was very quickly recognised as presenting AML risks and so within a year (and five years ahead of 5MLD requirements) the Luxembourg government imposed the same AML obligations on it as are in place for its real estate agents and others. In fact, they went further. For example, requiring customs officers to be present during operating hours.
- 3.15 The Luxembourg Freeport requires the identification of the ultimate beneficiary of goods. To some, this may be seen as a competitive disadvantage compared to Freeports in the likes of Geneva or Singapore where registering only those who bring goods in is required. Indeed, the Freeport did lose some customers as a result of these changes, but this may not necessarily be a bad outcome given it raises questions about what those customers might have been doing. The Luxembourg example indicates it may be possible for the UK to introduce Freeports whilst simultaneously requiring them to meet all necessary AML requirements.

4 About AAT

- 4.1 AAT is a professional accountancy body with approximately 50,000 full and fellow members and over 80,000 student and affiliate members worldwide. Of the full and fellow members, there are over 4,250 licensed accountants who provide accountancy and taxation services to individuals, not-for-profit organisations and the full range of business types.
- 4.2 AAT is a registered charity whose objectives are to advance public education and promote the study of the practice, theory and techniques of accountancy and the prevention of crime and promotion of the sound administration of the law.

5 Further information

If you have any questions or would like to discuss any of the points in more detail then please contact Adam Williamson, AAT Head of Professional Standards, at:

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