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Financial Information Authority

Palazzo San Carlo
00120 Vatican City

Tel.: (+39) 06 698 71 522
Fax.: (+39) 06 698 84 497
e-mail: aif@aif.va

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INTRODUCTION

Further strengthening of the supervisory system and fostering of international cooperation.

These are the strategic guidelines leading the activities of the Financial Information Authority (“AIF”) in 2016.

In the field of prudential supervision of entities carrying out financial activities on a professional basis (“supervised entities”), the regulatory framework¹ has been further strengthened with the promulgation, *inter alia*, of three Circulars in key areas.

The Circular on *Annual accounts and consolidated accounts of entities carrying out financial activities on a professional basis* (15 December 2016) transposed international accounting standards (“IAS/IFRS”), consistently with the uniqueness of supervised entities, establishing clear accounting principles applicable to entities carrying out financial activities on a professional basis.

In the same way, the Circular on *Monetary and financial statistics of entities carrying out financial activities on a professional basis* (29 December 2016) and the Circular on *Interest rate applied by entities carrying out financial activities on a professional basis* (29 December 2016) established clear statistical reporting requirements for supervised entities with a view to a closer monitoring of their financial stability.

The three Circulars have been issued also to comply with the commitment undertaken by the Holy See with the *Monetary Agreement between the European Union and Vatican City State* (17 December 2009)² and the *Ad-hoc Arrangement* of the Joint Committee established by the same Convention.

Alongside these regulatory efforts, always for prudential purposes, AIF devoted specific attention to the monitoring of the respect of capital requirements and criteria for equity allocation, also in view of addressing the medium-term risks still present in the global financial system³.

In the field of supervision for the prevention and countering of Money-Laundering and the Financing of Terrorism (“AML/CFT”), AIF has pursued its constant monitoring activities to ensure the consistent implementation of the risk-based approach, in particular in the execution of the procedures and measures for customer due diligence and international wire transfer, finding an overall compliance with the requirements established by the regulatory framework in place.

Within this context, AIF intensified its cooperation with supervisory authorities of countries where the supervised entities have closer relationships, for the exchange of information on supervisory activities.

The reporting system of potential suspicious activities and connected analytical and financial intelligence mechanisms have been further consolidated.

The number of suspicious activity reports (“SARs”) by different reporting subjects decreased in comparison to 2015, when a peak has been registered (207 in 2016, 544 in 2015; *see* § 3.2.1.). The stabilization is due to several inter-connected factors, including the conclusion of the “remediation process” of all customer relationships carried out by the Institute for the Works of Religion (“IOR”) – implying reports on enhanced due diligence and the closure of a number of current accounts – and in general the adoption of more efficient controls by the same Institute. The number of SARs was still higher than in the years before 2015, indicating an ever-increasing and effective implementation of reporting requirements by supervised entities.

¹ Based on Title III of Law n. XVIII (8 October 2013) and AIF Regulation on “*Prudential supervision of entities carrying out financial activities on a professional basis*” n. 1 (13 January 2015).

² Doc. 2010/C 28/05.

³ See International Monetary Fund, *Global Financial Stability Report*, October 2016.

In parallel, SARs show a constant improvement in terms of quality. And it is also worth mentioning that the trend relates also to SARs filed by competent Authorities of the Holy See and Vatican City State, in the direction of a close cooperation between domestic Authorities.

The improved quality of SARs led to the increase of reports disseminated by AIF to the Office of the Promoter of Justice at the Tribunal of Vatican City State (22 in 2016, 17 in 2015; *see* § 3.2.5.) as well as the international cooperation with foreign counterparts.

In 2016, AIF signed Memoranda of Understanding with the Supervisory Authorities of Brazil (*Conselho de Controle de Atividades Financeiras*), Italy (*Banca d'Italia*) and Poland (*Komisja Nadzoru Finansowego*) (*see* § 3.1.3.) and with the Financial Intelligence Units (“FIUs”) of Austria, Brazil, Canada, Panama and Russia (*see* § 3.2.4.).

While there has been a relative stability of cases of cooperation with foreign Supervisory Authorities (11 in 2016, 12 in 2015; *see* § 3.1.3.), in 2016 there has been a significant increase in cases of cooperation with foreign FIUs (837 in 2016, 380 in 2015; *see* § 3.2.4.), mainly by the initiative of AIF (721 cases out of a total of 837, *see* 3.2.4.), due to the fact the cases often involve a multitude of foreign subjects and jurisdictions.

Within this context AIF adopted more sophisticated analytical methodologies and systems. To this end, the IT and cyber security infrastructures have been revised and a formal relationship has been activated with the *United Nations Office on Drugs and Crimes* (“UNODC”) for use of the *goAML* software.

Finally, AIF is constantly engaged within the Financial Security Committee (“CoSiFi”) of the Holy See as member and coordinator of the General Risk Assessment for the protection of the jurisdiction, carried out with the methodology provided by the World Bank.

The limited financial sector established in Vatican City has a unique feature: providing essential services primarily to support the institutional activity of the Holy See and the Catholic Church in the world. By its nature, it has an international projection, including those critical areas and regions sometimes in which the Church, for various reasons, is present with its pastoral and humanitarian activities.

While retaining its own uniqueness, it therefore shares the inherent challenges and complexities of the current international scenario.

Within these trajectories, AIF is committed to protect and promote the integrity and sustainability of the financial sector under its supervision, favoring its activity and ultimately its major mission.

TOMMASO DI RUZZA
Director

PART I

INSTITUTIONAL FUNCTIONS AND ROLE
WITHIN THE FRAMEWORK OF THE HOLY SEE
AND VATICAN CITY STATE

1. LEGAL, ECONOMIC AND FINANCIAL FRAMEWORK.

1.1. LEGAL FRAMEWORK REGARDING FINANCIAL INTELLIGENCE AND SUPERVISION OF ENTITIES CARRYING OUT FINANCIAL ACTIVITIES ON A PROFESSIONAL BASIS.

The legal basis for supervision and regulation of entities carrying out financial activities on a professional basis and the financial intelligence is found in the Apostolic Letter issued “*Motu Proprio*” by Pope Francis “*for the prevention and countering of money laundering, the financing of terrorism and the proliferation of weapons of mass destruction*” of 8 August 2013, and in the Law “*on transparency, supervision and financial intelligence*”, n. XVIII of 8 October 2013 (“Law n. XVIII”).

The supervisory and regulatory framework is defined in Titles II and III of Law n. XVIII, dedicated to the prevention and countering of money laundering and the financing of terrorism, and prudential supervision respectively.

In order to implement Title III of Law n. XVIII, on 25 September 2014, the Board of Directors of the Financial Information Authority (“AIF”) adopted Regulation n. 1 on “*the prudential supervision of entities carrying out financial activities on a professional basis*” (“Regulation n. 1”), which came into force on 13 January 2015.

Financial intelligence activities are regulated under Chapter VIII of Title II of Law n. XVIII.

1.2. ECONOMIC AND FINANCIAL FRAMEWORK OF VATICAN CITY STATE.

By virtue of Law n. V of 7 June 1929, a public regime was established in Vatican City State for economic, commercial and professional sectors, including the financial sector.

Therefore, in Vatican City State, there is neither free market in place nor any private sector.

In particular, a limited financial sector is established in the State, namely the sector including the entities carrying out financial activities on a professional basis supervised by the Financial Information Authority.

The financial sector of the Vatican City State is public in nature and *de facto* closed. Within the State:

- (a) there is neither a financial market [i.e. regulated market, multilateral trading facilities (“MTFs”) nor organized trading facilities (“OTFs”)];
- (b) currently there is no issue of public debt instruments, capital instruments, securities or associated instruments;
- (c) no insurance companies, electronic money institutions, trust companies or securities firm have been established;
- (d) no foreign financial entity has branches or subsidiaries and/or offices within the Vatican City State.

1.3. GENERAL ASSESSMENT OF MONEY LAUNDERING AND TERRORISM FINANCING RISKS (“GENERAL RISK ASSESSMENT”).

In 2015, the Financial Security Committee (“CoSiFi”) launched a risk assessment project dedicated to money laundering and terrorism financing (“*Risk Assessment*”) for the Holy See and Vatican City State, relying on World Bank methodology and technical support.

During the year 2016, the relevant Authorities and bodies of the Holy See and Vatican City State were involved, including meetings and discussion on the process, its trends and results.

AIF, as member of CoSiFi, is in charge of the coordination of the project.

General Risk Assessment

The General Risk Assessment (“GRA”) on the prevention of Money Laundering (“ML”) and the Financing of Terrorism (“FT”) is a process aimed at identifying and analyzing the potential risk sources and factors in connection to ML/FT based on the methodology provided by the World Bank: the “National Money Laundering and Terrorist Financing Risk Assessment Tool”.

The GRA process is based on “two pillars”:

- (a) identification and assessment of “ML/FT Threats”;
- (b) identification and assessment of “ML/FT vulnerabilities”.

Aim.

The end of the process is twofold:

- (a) identifying and analyzing the main risk sources and factors in connection to ML/TF, in order to design an Action Plan for a more effective resource allocation to prevent, mitigate and eliminate potential risks;
- (b) providing guidance for the risk assessment of the financial sector and the operational risk assessment for the entities carrying out financial activities on a professional basis.

Scope.

The scope of the GRA process is limited to the activities and entities that fall legally within the direct jurisdiction of the Holy See and State of the Vatican City.

Competent Authority.

The Financial Security Committee (“CoSiFi”) is the competent authority for the establishment of criteria and procedures and for the approval of the “general risk assessment” on the prevention and countering of ML/FT and its regular updating.

2. INSTITUTIONAL FUNCTIONS.

2.1. INSTITUTIONAL FUNCTIONS AND STATUTE.

The Financial Information Authority (“AIF”) was established by Pope Benedict XVI with the Apostolic Letter issued “*Motu Proprio*” “*for the prevention and countering of illegal activities in the area of monetary and financial dealings*” of 30 December 2010. This was reformed and corroborated by Pope Francis on 15 November 2013 with Apostolic Letter, issued “*Motu Proprio*”, with which the Pontiff “*approved the Statute of the Financial Information Authority*”.

Under Art. 2 of the Statute, AIF performs the following functions, in full autonomy and independence:

- (a) supervision and regulation of entities carrying out financial activities on a professional basis, aimed at preventing and countering money laundering and the financing of terrorism, as well as for prudential purposes;
- (b) financial intelligence.

AIF has the *status* of an “Institution connected to the Holy See”, pursuant to Art. 186 *et seq.* of the Apostolic Constitution “*Pastor Bonus*” of 28 June 1988 [Art. 1 (1) of the Statute], it is endowed with public legal personality under Canon Law and its headquarters are located in Vatican City State [Art. 1 (2) of the Statute].

2.2. ORGANIZATION.

The organization of AIF is defined in the Statute approved by Pope Francis with His “*Motu Proprio*” of 15 November 2013.

Under Art. 3 (1), AIF’s governing bodies are:

- (a) the Board of Directors, which defines the Authority’s general policy guidelines and fundamental strategies;
- (b) the President, who chairs the Board of Directors, its legal representative and has the authority to sign on its behalf;
- (c) the Director, who guides, organizes and supervises the Authority’s activity, participates in the meetings of the Financial Security Committee (“CoSiFi”), and is a member of Holy See delegations to international bodies that are responsible for countering money laundering and the financing of terrorism.

The Board of Directors is composed of the following Members: Ms Maria Bianca Farina (Italy), Mr. Marc Odendall (Switzerland), Mr. Joseph Yuvaray Pillay (Singapore) and Mr. Juan C. Zarate (USA).

The President is Mr. René Brülhart (Switzerland).

The Director is Mr. Tommaso Di Ruzza (Italy).

Under Art. 3 (2) of the Statutes, AIF’s internal structure is subdivided into two Offices:

- (a) the Office of Supervision and Regulation;
- (b) the Office of Financial Intelligence.

The separation between the two Offices, provided for in Art. 3 (3) of the Statute, is meant to keep supervision and regulation formally and functionally separate from financial intelligence, since they also entail different channels for international cooperation and information exchange. Both Offices report to the Director in order to ensure effective internal operation and coordination.

Office of Supervision and Regulation

Competent Office for the implementation of the duties established by Articles 46 and 65 of Law n. XVIII and Article 2 (a) (b) of the Statute.

The Office of Supervision and Regulation is in charge of the:

- (a) prudential supervision and regulation (supervision with regard to the prudential regime established by Title III of Law n. XVIII, Regulation n. 1 on “*the prudential supervision of entities carrying out financial activities on a professional basis*” and other legal instruments issued by the competent Authorities and AIF; carrying out of off-site and on-site inspections on the supervised entities; regulatory activities within the prudential framework; cooperation with foreign Supervision Authorities);
- (b) supervision and regulation aimed at preventing and countering money laundering and the financing of terrorism (supervision with regard to the AML/CTF regime established by Title II of Law n. XVIII and other legal instruments issued by the competent Authorities and AIF; carrying out of off-site and on-site inspections on the supervised entities; regulatory activities within the AML/CTF framework; cooperation with foreign Supervision Authorities).

Office of Financial Intelligence

Competent Office for the implementation of the duties established by Article 48 of Law n. XVIII and Article 2 (c) of the Statute.

The Office of Financial Intelligence:

- (a) receives suspicious activity reports from the supervised entities and from the public Authorities of the Holy See and Vatican City State, as well as declarations of cross-border transportation of currency;
- (b) requests documents, data and information relevant to the purposes of preventing and countering money laundering and the financing of terrorism;
- (c) conducts strategic and operational analysis of the suspicious activity reports, documents, data and information received, cooperating when necessary with domestic and foreign counterparts;
- (d) elaborates reports, documents, data and information in view of a potential dissemination to the Promoter of Justice if there is a reasonable ground to suspect an activity of money-laundering or financing of terrorism.

2.3. SUPERVISED ENTITIES.

According to the “Motu Proprio” issued by Pope Francis on 8 August 2013 (*supra* 1.3), by way of principle, all Dicasteries of the Roman Curia and other bodies and entities that depend on the Holy See, as well as non-profit organizations having legal personality under Canon Law and their headquarters in the Vatican, must abide by State law concerning:

- (a) measures to prevent and counter money laundering and terrorism financing;
- (b) measures against subjects who threaten international peace and security;
- (c) prudential supervision of entities carrying out financial activities on a professional basis.

Title III of Law n. XVIII and Regulation n. 1 introduce formal requirements for entities to be authorized to carry out financial activities on a professional basis by the AIF.

In 2016, the only entity that was supervised by AIF was the Institute for the Works of Religion (IOR).

2.3.1. *Institute for the Works of Religion (IOR).*

IOR is a public canon law foundation⁴, whose purpose is “to provide for the custody and administration of movable and immovable property transferred or assigned to the Institute by natural or legal persons and intended to works of religion and charity”⁵.

According to the customer policy adopted by the Board of Superintendence, IOR is not open to the general public and currently provides its financial services to the following categories of natural and legal persons: Clerics and members of Institutes of Consecrated Life and Societies of Apostolic Life; Legal entities registered within Vatican City State; Institutes of Consecrated Life and Societies of Apostolic Life; Dioceses, parishes and other entities of the Catholic Church; Diplomatic missions accredited to the Holy See; Causes of Beatification and Canonization; Legates; Organs and entities of the Holy See and Vatican City State and connected institutions, including Apostolic Nunciatures and Delegations; Employees (and retired persons) of the Holy See and Vatican City State; Diplomats accredited at the Holy See.

IOR does not have branches or offices in foreign jurisdictions or territories, and it does not carry out financial activities in foreign jurisdictions or territories, including the promotion of its financial services.

IOR is subject to full and exclusive supervision by AIF.

⁴ See “*Chirographus in civitate vaticana institutum caritatis religionisque operibus tutandis conditur*” by Pope Pius XII of 27 June 1942.

⁵ See Art. 2 of “*Chirographus providing a new status to the Institute of Works of Religion*” by Pope John Paul II of 1 March 1990.

2.4. COOPERATION AND EXCHANGE OF INFORMATION AT DOMESTIC AND INTERNATIONAL LEVEL.

Under Art. 69 (a) (b) of Law n. XVIII, AIF works and exchanges information with Holy See and State Authorities (which provide AIF with relevant documents, data and information) and, on the basis of memoranda of understanding, with its foreign counterparts.

As a Supervisory Authority, AIF established bilateral relationships with counterparts of the relevant foreign jurisdiction for the Holy See. Given the geographical situation of the State of the Vatican City and the uniqueness of its financial system, contacts were established with relevant Supervisory Authorities in several countries, also in view of formalizing cooperation based on reciprocity and in line with shared international standards.

As Financial Intelligence Unit, AIF established significant relationships at bilateral as well as at multilateral level, given the universal projection of the activities of the supervised entity and its exposure to international treaties. At the multilateral level, AIF has been playing an increasingly active role within the *Egmont Group*⁶ since its admission in 2013.

⁶ The *Egmont Group* is united body of 152 Financial Intelligence Units (FIUs) providing a platform for the secure exchange of expertise and financial intelligence to combat money laundering and terrorist financing.

3. MAIN ACTIVITIES.

3.1. SUPERVISION AND REGULATION OF ENTITIES CARRYING OUT FINANCIAL ACTIVITIES ON A PROFESSIONAL BASIS.

The year 2016 was characterized by a continuous increase in supervisory and regulatory activities, especially in the field of prudential supervision.

Regulation n. 1 became law on 13 January 2015 and established a tailor-made supervisory system for the financial sector of Vatican City State and granted a transitional period of 365 days to the supervised entity for the fulfillment of all the requirements provided.

On 13 January 2016, in accordance with Article 121 (3) of Regulation n. 1, the transitional period to implement the requirements established by the new regulatory framework ended.

During 2016, in fulfilling the duties established by Article 65 of Law n. XVIII and Art. 2 (a) of the Statute, the activities of the Office of Supervision and Regulation has been characterized by five main drivers:

- (a) strengthening the stability of the financial sector;
- (b) strengthening the integrity of the financial sector;
- (c) establishing detailed accounting rules for the financial sector;
- (d) supervising the competence and honorability requirements;
- (e) strengthening the statistical reporting requirements for the financial sector.

In the same year, in fulfilling the duties established by Art. 46 of Law n. XVIII and Art. 2 (b) of the Statute, the activities of the Office of Supervision and Regulation have been mainly devoted to monitor the relationships among the supervised entity and foreign financial institutions.

3.1.1. *Prudential Supervision.*

In 2016, the prudential supervision was focused on the following main areas.

(a) Stability of the financial sector.

The Vatican prudential regulatory framework establishes strong regulatory capital requirements for the entities carrying out financial activities on a professional basis, such as the equivalence between common equity (composed by capital and supplemental capital)⁷ and regulatory capital⁸, as well as the reliable proportionality between regulatory capital and financial activities carried out, and their potential risks⁹.

⁷ See Art. 3 (12) of Regulation n. 1.

⁸ See Art. 3 (54) of Regulation n. 1.

⁹ See Art. 57 (1) of Regulation n. 1.

Considering the nature and the mission of the supervised entity and in view of strengthening the stability of the financial sector reducing the possible risks, AIF provided indications on the criteria to be followed for the allocation of the common equity, in order to ensure the full application of the provision established in Regulation n. 1.

In particular, in addition to the provision that the funding capital of the supervised entity be completely paid and cannot be reduced or distributed (except in the case of cessation or liquidation of the supervised entity), AIF prescribed that all the capital shall be invested only in liquidity and investment-grade bonds issued by super-national entities and foreign Governments.

(b) Integrity of the financial sector.

As part of its responsibilities, AIF examines whether a financial activity requires authorization under the laws whose observance it is responsible for supervising¹⁰. Entities already authorized to carry out certain financial activities on a professional basis within Vatican City State may only carry out additional financial activities if they have the necessary formal authorization.

Regulation n. 1 provides the general framework for the authorization requirements, as well as for the organizational and prudential criteria, to carry out a financial activity on a professional basis.

At the same time, some financial activities need particular scrutiny, especially when connected with collective portfolio management schemes and which are increasingly widespread in the financial markets in response to the increasing demand of the investors.

For these reasons, AIF devoted particular attention to the more common and requested investment instruments and, on 5 February 2016, issued the Circular on “*provision of collective asset management services through pension funds established within entities carrying out financial activities on a professional basis*”.

In 2016, AIF received no requests of authorization for collective asset management services through pension funds.

(c) Accounting rules for the financial sector.

In line with the *Ad hoc* regime adopted on 19 December 2014 by the Joint Committee for the implementation of the Monetary Agreement of 17 December 2009 between the European Union and Vatican City State, AIF issued the Circular on “*annual accounts and consolidated accounts of entities carrying out financial activities on a professional basis*” of 15 December 2016.

The Circular transposes the relevant and applicable provisions of the Council Directive 86/635/EEC of 8 December 1986 on “*the annual accounts and consolidated accounts of banks and other financial institutions*” as amended and the Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on “*the annual financial statements, consolidated financial statements and related reports of certain types of undertakings*”, as well as the relevant and applicable provisions established by the European legal sources on International Accounting Standards (“IAS”) and International Financial Reporting Standards (“IFRS”).

¹⁰ See Art. 54 of Law n. XVIII and Artt. 4-7 of Regulation n. 1.

The Circular, that establishes a comprehensive set of accounting rules for the entities carrying out financial activities on a professional basis within Vatican City State for the first time, became legally effective and will be fully applied in the 2016 financial statements of the supervised entity.

(d) Supervision on competence and honorability requirements.

As part of its responsibilities, AIF verifies whether subjects proposed for high positions (Senior management and Management) and relevant functions hold the necessary competence and honorability requirements¹¹.

During the year 2016, AIF carried out the required assessments, in line with the provisions of Artt. 18-20 of Regulation n. 1 for the relevant positions and functions within the supervised entity.

(e) Statistical reporting requirements.

According to the provisions of the prudential framework, the entities carrying out financial activities on a professional basis is obliged to communicate to AIF, on periodical basis, data on capital adequacy (i.e. the amount of regulatory capital) and liquidity ratios (i.e. the liquidity coverage ratio and the net stable funding ratio)¹².

In line with the *Ad hoc* regime adopted on 19 December 2014 by the Joint Committee for the implementation of the Monetary Agreement of 17 December 2009 between the European Union and Vatican City State, AIF issued the following two Circulars:

(i) Circular on “*monetary and financial statistics of entities carrying out financial activities on a professional basis*” of 29 December 2016.

The Circular transposes the relevant and applicable provisions of the Guideline ECB/2013/24 of the European Central Bank of 25 July 2013 on “*the statistical reporting requirements of the European Central Bank in the field of quarterly financial accounts*” as amended, the Regulation (EU) n. 1071/2013 of the European Central Bank of 24 September 2013 “*concerning the balance sheet of the monetary financial institutions sector*” and the Guideline ECB/2014/15 of the European Central Bank of 4 April 2014 on “*monetary and financial statistics*”.

(ii) Circular on “*interest rate applied by entities carrying out financial activities on a professional basis*” of 29 December 2016.

The Circular transposes the relevant and applicable provisions of the Regulation (EU) n. 1072/2013 of the European Central Bank of 24 September 2013 “*concerning statistics on interest rates applied by monetary financial institutions*” and the Guideline ECB/2014/15 of the European Central Bank of 4 April 2014 on “*monetary and financial statistics*”.

The first statistical report is expected for the end of the first quarter of the year 2017.

¹¹ See Art. 61 of Law n. XVIII and Artt. 18-20 of Regulation n. 1.

¹² See Art. 62 and Art. 115 of Regulation n. 1.

3.1.2. *Supervision for the Prevention and Countering of Money Laundering and the Financing of Terrorism.*

In 2016, the supervision for the prevention and countering of money laundering and the financing of terrorism was mainly focused on the following areas:

(a) Risk based approach.

Art. 22 of the Law n. XVIII establishes the “risk based approach” principle for the entities carrying out financial activities on a professional basis.

Supervised entities shall fulfill the customer due diligence requirements in a manner proportionate to the risks connected to the category and to the country or geographical area of the counterpart and to the typology of relationship, product or service, operation or transaction, or channel of distribution.

(b) Supervision on the relationships among the supervised entities and foreign financial institutions.

The unique geographical situation of Vatican City State and the activities carried out by the supervised entity implies the necessity to establish relations with foreign financial intermediaries.

AIF monitored these relations in order to guarantee their full compliance with the Vatican regulatory framework that imposes upon the supervised entity the obligation to gather sufficient information on the foreign financial institution in order to understand fully the nature of its activities and to determine its reputation and the quality of its supervision, as well as to evaluate the controls relating to the prevention and countering of money-laundering and financing of terrorism applied.

3.1.3. *Domestic and International Cooperation and Information Exchange.*

AIF cooperates and exchanges information with the Holy See and Vatican City State Authorities, and, on the basis of memoranda of understanding, with its foreign counterparts.

In 2016 AIF signed Memoranda of Understanding (“MoUs”) with the Supervisory Authorities of Brazil (“*Conselho de Controle de Atividades Financeiras*”), Italy (“*Banca d’Italia*”) and Poland (“*Komisja Nadzoru Finansowego*”).

Currently, AIF entered into formal relations with the Supervisory Authorities of 6 countries: namely, Brazil, Germany, Italy, Luxembourg, Poland and United States of America.

In 2016 AIF had 11 international information exchanges.

The degree of cooperation provided by foreign counterparts has been positive.

3.2. FINANCIAL INTELLIGENCE.

AIF's financial intelligence activities can be broken down into three fundamental steps:

- (i) receiving Suspicious Activity Reports (SARs);
- (ii) carrying out analysis of the reports received at operational and strategic level;
- (iii) dissemination of Reports to the Office of the Promoter of Justice in the Tribunal of Vatican City State in cases where there are grounds to suspect that money laundering or terrorism financing are taking place.

3.2.1. *Receiving Suspicious Activity Reports.*

The mainstay of financial intelligence activity is receiving SARs.

Under Art. 40 (1) of Law n. XVIII, supervised entities file a SAR to AIF:

- (i) whenever they suspect, or have reasonable grounds to suspect, that funds or other economic resources are proceeds of criminal activities or are related or connected to terrorism financing or are destined to be used for acts of terrorism or by terrorist organizations or individuals who finance terrorism;
- (ii) in case of activities, operations or transactions, which, due to their nature, are likely, to be connected or related to money laundering or terrorism financing or terrorist organizations or individuals who finance terrorism.

Furthermore, Art. 40 (2) of Law n. XVIII provides for a duty to files SARs to AIF also for competent Authorities of the Holy See and the State of the Vatican City in the cases envisaged under the same Art. 40 (1).

The number of the SARs received in 2016 is 207 (in comparison with 544 in 2015): 192 from supervised entities, 8 from Authorities of the Holy See and State of the Vatican City and 7 from other entities.

The number SARs by different reporting subjects decreased in comparison to 2015, when a peak has been registered. But the number of SARs was still higher than in the years before 2015, indicating an ever-increasing and effective implementation of reporting requirements by supervised entities.

3.2.2. Report Analysis.

Reports are analyzed at two levels:

- (i) operational level (using available or obtainable documents, data and information in order to identify specific targets, track down operations and transactions and establish links between the above-mentioned targets and possible proceeds of criminal activities);
- (ii) strategic level (using available and obtainable documents, data and information for more general purposes, also related to the identification of money laundering and terrorism financing trends).

Under Art. 50 (a) (b) of Law n. XVIII, for analytical purposes, AIF has the power to gain full access, in a timely manner, to all financial, administrative and investigative nature to the purpose of preventing and countering money laundering and the financing of terrorism, including all information possessed by the reporting subjects and the legal persons with their legal seat in the State of the Vatican City of registered in the register held by the State.

On the background of SARs filed by supervised subjects in 2016 an increasing complexity of potential money laundering schemes has been registered, requiring a deeper and wider analysis and cooperation with foreign counterparties.

Within this context, AIF enhanced its IT structures and cyber security systems in order to ensure the integrity, security and confidentiality of information and data processed and stored.

Furthermore, AIF entered into a formal relationship with the *United Nations Office on Drugs and Crimes* (UNODC) for the use of the *goAML* software.

3.2.3. Preventive Measures.

Under Art. 48 of Law n. XVIII, AIF:

- (a) “suspends the execution, for up to five working days, of transactions and operations suspected of money laundering or the financing of terrorism, as well as any other linked operation or transaction, where this does not obstruct investigative or judicial activity” [Art. 48 (j)];
- (b) “adopts the preventive freezing of accounts, funds and other assets, up to five working days, in the case of suspect of money laundering or financing of terrorism, where this does not obstruct investigative or judicial activity” [Art. 48 (k)].

In 2016, AIF ordered 4 suspensions of transactions and operations (for a total of 2,113,838.55 Euro) and preventive freezing in 1 instance (for a total of 1,550,199.45 Euro).

3.2.4. *Activities to Prevent and Counter the Financing of Terrorism.*

Under Art. 71 (1) of Law n. XVIII, the President of the Governorate, having obtained the opinion of the Secretariat of State, issued an order to approve and update an *ad-hoc* list of natural and legal persons for whom there are reasonable grounds to assume that they are a threat to international peace and security.

In drawing up this list, the President of the Governorate examined input coming from relevant agencies of the United Nations Security Council, the European Union and other States.

In this domain, AIF has the responsibility to forward such lists and their updates to entities carrying out financial activities on a professional basis [Art. 71 (3)], and to inform them about proposals to add or delete names from the list published by the President of the Governorate of the Vatican City State [Arts. 72 (3) and 73 (2)], as well as the adoption of precautionary measures [Art. 76 (1) (2)].

Furthermore, under Art. 75 (2) of Law n. XVIII, AIF has the power to order supervised entities to freeze, for preventive purposes:

- (a) funds and other assets owned, held, controlled or detained, exclusively or jointly, directly or indirectly, by subjects included in the list;
- (b) benefits and profits generated by funds and other assets referred to in letter a);
- (c) funds and other assets held or controlled by other subjects, natural persons or entities, in the name or in behalf or in favour of subjects included on the list.

During 2016 the President of the Governorate issued 29 Orders for updating the list of subjects who threaten international peace and security, also based on relevant Resolutions issued by the United Nations Security Council.

Concurrently AIF published the list of Orders on its website, forwarding it to supervised entities, and ordering the freezing of assets and economic resources that could be traced back to subjects included on the list.

3.2.5. *Dissemination of Reports to the Office of the Promoter of Justice in the Tribunal of the Vatican City State.*

If there are grounds to suspect that money laundering or terrorism financing are taking place, AIF disseminates reports to the Office of the Promoter of Justice in the Tribunal of Vatican City State.

In 2016, AIF disseminated 22 reports on potential ML cases to the Office of the Promoter of Justice (out of 207 SARs received) in comparison with 17 reports disseminated during 2015 (out of 544 SARs received). The main potential predicate offences identified are fraud, including serious tax evasion, misappropriation and corruption. The vast majority of potential offences involve conducts taken by foreign citizens in foreign jurisdictions.

3.2.6. *Domestic and International Cooperation and Information Exchange.*

Pursuant to Art. 69 (a) (b) of Law n. XVIII, AIF cooperates and exchanges information with Authorities of the Holy See and the State of the Vatican City State, as well as with its foreign counterparts, based on reciprocity and memoranda of understanding.

At the domestic level, in 2016 AIF exchanged information in 72 cases with other competent Authorities of the Holy See and the State of the Vatican City.

At the international level, in 2016 AIF signed 5 Memoranda of Understanding with the following counterparties: Austria-FIU, Brazil-COAF, Canada-FINTRAC, Panama-UAF and Russia-FSFM for a total number of 32 Memoranda of Understanding signed between 2011 and 2016¹³.

Additionally, AIF's membership in the *Egmont Group*, allows AIF to interact with financial intelligence units of 152 countries and jurisdictions.

More specifically, in 2016 AIF had 837 international information exchanges, of which 721 were upon AIF's request and 116 following requests made by its foreign counterparts (with an increase of 220% of the international information exchange).

The main driver of the increase of the figures relating to the international cooperation and exchange of information is, on the one hand, the preventive and proactive approach taken by AIF at the international level and, on the other hand, the increase of counterparts, and lastly the sophisticated feature of cases under strategic and operational analysis, involving several subjects and foreign jurisdictions.

3.3. ADDITIONAL DOMESTIC AND INTERNATIONAL FUNCTIONS.

3.3.1. *Collecting and Analyzing Declarations of Cross-Border Transportation Cash.*

Under Art. 81 of Law n. XVIII, anyone carrying cash across the border (or equivalent movable assets), from and to the State, for an amount equivalent to or greater than 10,000 Euro, must provide a written declaration to the offices of the Corps of the Gendarmerie or to offices authorized by AIF. A copy of the declaration shall be forwarded to AIF within 24 hours.

In 2016, 380 incoming declarations for a total of 9,642,657.58 Euro were collected (in comparison with 367 declarations for a total of 9,697,570.61 Euro in 2015) and 1,357 outgoing declarations were collected for a total of 23,956,122.58 Euro (in comparison with 1,196 declarations for a total of 24,155,840.76 Euro in 2015).

Data confirm a progressive decrease and stabilization of cross-border transportation of cash, both incoming and outgoing. The situation confirms the trend recorded in 2013-2015, following the strengthening of the State's institutional and legal framework and enhancing border controls and monitoring of cash flow.

¹³ In alphabetic order: Albania, Argentina, Australia, Austria, Belgium, Brazil, Canada, Cuba, Cyprus, France, Germany, Hungary, Italy, Liechtenstein, Luxemburg, Malta, Netherlands Norway, Panama, Paraguay, Peru, Poland, Principality of Monaco, Romania, Russian Federation, San Marino, Slovenia, South Africa, Spain, Switzerland, United Kingdom, United States of America.

3.3.2. *Tax Compliance Activities.*

On June 10, 2015, an Agreement between the Holy See and the United States of America was signed for the purpose of compliance and exchange of tax information in accordance with the “Foreign Account Tax Compliance Act” (“FATCA”).

In this context, AIF and the Secretariat for the Economy (which was identified as the Authority that is responsible for implementing the activities included in the aforementioned Agreement) signed a Memorandum of Understanding on 10 November 2015, whereby AIF was tasked to monitor the process adopted by the supervised entity to collect and assess the data and information requested to comply with FATCA.

In 2016, AIF monitored the compliance of the supervised entity within the requirements established by the Secretariat for the Economy, without detecting any critical issue.

3.3.3. *Other International Activities.*

AIF participated in the “*Egmont Group Meetings*” that were held in the Principality of Monaco (January 31-5 February 2016) and in the “*International Exchange Working Groups Meetings*” of Financial Intelligence Units, that were held in Paris (20-21 October 2016).

AIF was part of the Delegation of the Holy See to the 50th meeting (12-15 April 2016), 51st meeting (27-29 September 2016) and 52nd meeting (6-9 December 2016) of the *Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism* (“MONEYVAL”) at the Council of Europe.

PART II

STATISTICS

1. SUPERVISION AND REGULATION.

International Cooperation	2011	2012	2013	2014	2015	2016
Requests <i>to</i> foreign Authorities	0	0	0	2	10	11
Requests <i>from</i> foreign Authorities	0	0	0	2	2	0
Total				4	12	11

2. FINANCIAL INTELLIGENCE.

Suspicious Activity Reports	2011	2012	2013	2014	2015	2016
Number of Reports	1	6	202	147	544	207
Supervised Subjects	1	5	193	141	537	192
Authorities of the HS/VCS		1	5	4	6	8
Other Entities			4	2	1	7

Preventive Measures	2014 Number of measures	2014 Total amount	2015 Number of measures	2015 Total amount	2016 Number of measures	2016 Total amount
Suspension of transactions and operations	3	€ 561,574.89	8	€ 8,262,565.42 \$ 1,714,800.00	4	€ 2,113,838.55
Freezing of accounts, funds and other assets			4	€ 7,051,422.42 \$ 654,800.00	1	€ 1,550,199.45

Domestic Cooperation	2011	2012	2013	2014	2015	2016
Requests <i>to</i> domestic Authorities	1	2	11	41	108	72

Reports to the Office of the Promoter of Justice	2011	2012	2013	2014	2015	2016
	0	2	8	7	17	22

International Cooperation	2011	2012	2013	2014	2015	2016
Requests <i>to</i> foreign Authorities	1	1	28	20	199	721
Requests <i>from</i> foreign Authorities	7	3	53	93	181	116
Total	8	4	81	113	380	837

3. COLLECTION AND ANALYSIS OF DECLARATIONS OF CROSS-BORDER CASH TRANSPORTATION.

Declarations	2011	2012	2013	2014	2015	2016
	<i>(April)</i>					
Number of <i>incoming</i> declarations	658	598	550	429	367	380
Number of <i>outgoing</i> declarations	1,894	1,782	1,557	1,111	1,196	1,357
Total	2,552	2,380	2,107	1,540	1,563	1,737



