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INTRODUCTION

In 2019, the *Autorità di Informazione Finanziaria* (AIF) intensified its action in every branch of activity, while consolidating forms of collaboration with other States and jurisdictions. At the system-wide level, also thanks to the Vatican authorities' strong commitment to fighting money laundering and the financing of terrorism, there was further progress towards a better functioning and international recognition of the jurisdiction.

AIF is responsible for setting the regulatory framework in the fields of its competence. In this context, several instructions were approved in 2019, both on prudential supervision and the countering of money laundering and terrorism financing.

As regards supervision, two onsite inspections were carried out at the IOR. The first, in June, aimed at assessing the technical compliance with the legal and regulatory framework for payment services, and at verifying the existence of all the requirements for inclusion of the Institute into the SEPA payment scheme. The second, in August, consisted in a general compliance assessment in the fields of money laundering and the financing of terrorism, including the effectiveness of the measures and controls put in place.

On several occasions AIF exchanged information with foreign supervisory authorities. This led to concrete results, because it enabled the analysis of complex financial schemes involving various jurisdictions, and the reporting of potential violations and illegitimate conducts. With some counterparts, given the greater integration with the respective jurisdictions, the collaboration and exchange of information took place on a regular basis and was not confined to the prevention of potential violations and illegal conduct but covered the financial activities as a whole, thus including prudential supervision.

As regards financial intelligence, AIF received 64 suspicious activity reports (SARs), of which 55 from supervised entities and 4 from other HS/VCS authorities. It enacted 4 preventive measures, including the freezing of a bank account. Moreover, it forwarded 15 reports to the Promoter of Justice, which confirms the rising trend in the ratio between reports to the Promoter of Justice and SARs. Overall, the tendency towards higher quality SARs is strengthening, thanks to the guidelines on more specific anomaly indicators which was provided and a more conscious implementation of a risk-based approach.

Also in this domain, international cooperation proved effective – more than 370 subjects were involved in the information exchanges with other FIUs – making it possible to analyze complex financial schemes involving several jurisdictions. This allowed for the transmission of useful information to the Promoter of Justice and to foreign counterparts. Four new MoUs were signed with foreign FIUs (Finland, Cook Islands, Czech Republic and Serbia), for a total of 60 MoUs signed since 2012.

As concerns the cross-border transfer of cash, the number and the size of the declarations confirms the tendency, already observed in previous years, of a progressive reduction in the use of cash. This trend also reflects better fund transfer systems now available at the IOR, assuring higher levels of security and traceability. The analyses of the declarations carried out by AIF did not reveal significant anomalies or indicators of risk.

Most of the potential financial crimes involve foreign subjects or conduct carried out in, or connected to, foreign jurisdictions. The main alleged crimes are international fraud, including fiscal fraud, and embezzlement. Finally, in 2019 AIF participated in the plenary sessions of the Egmont Group (Hague, the Netherlands, 1-5 July) and was part of the Holy See's delegation to the 58th and 59th Plenary Assembly (15-19 July and 2-6 December, respectively) of the Council of Europe's Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism (MONEYVAL).

GIUSEPPE SCHLITZER
Director

PART I

GENERAL FRAMEWORK,

INSTITUTIONAL FUNCTIONS AND

MAIN ACTIVITIES

1. GENERAL FRAMEWORK

1.1. LEGAL FRAMEWORK

The foundations of the legal framework for supervision, regulation and financial intelligence activities were laid with 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 Law No. XVIII of 8 October 2013 on *transparency, supervision and financial intelligence*. The latter legislation, under Titles II and III, regulates supervision for the prevention and combating of money laundering and terrorist financing, prudential supervision of entities that carry out financial activities on a professional basis and financial intelligence.

The Financial Information Authority (AIF) is responsible for establishing the regulatory framework for the purposes of both prudential supervision and prevention and countering of money laundering and terrorist financing, through the adoption of regulations, instructions and guidelines, also taking into account the commitments undertaken by the Holy See with the 2009 Monetary Agreement between the European Union and the Vatican City State. During 2019, the regulatory framework was supplemented with several new Instructions.

Prudential Supervision

In 2019, the regulatory activity focused mainly on two issues:

The first focused on the actions necessary to ensure that the entities that carry out financial activities on a professional basis entered the SEPA circuit and that they efficiently perform payment service activities within the circuit. With this in mind, the following instructions were promulgated:

a) Instruction No. 2 of 30 April 2019 *on reporting requirements for statistical information on fraud related to means of payment*, concerning the transmission of the statistical information referred to in Article 62 (3) of Regulation No. 3 of 23 May 2018;

b) Instruction No. 3 of 29 May 2019 *on claim procedures to the Financial Information Authority for the settlement of disputes related to the provision of payment services by entities carrying out financial activities on a professional basis*, concerning disputes arising from the conclusion, performance or interpretation of contracts relating to payment services; and

(c) Instruction No. 4 of 29 May 2019 *on measures for the management of operational and security risks related to payment services and connected reporting duties*, which addresses: (i) the requirements for the establishment, implementation and monitoring of the security measures that payment service providers must take, in accordance with Article 61(1) of Regulation No. 3, to manage the operational and security risks relating to the payment services they provide; and (ii) the criteria for the classification of major operational or security incidents by payment service providers, as well as the format and procedures they shall follow to notify such incidents to the Financial Information Authority, as laid down in Article 62 (1) of Regulation No. 3.

The second issue focused on strengthening the regulatory framework for the external audit of the accounts of entities carrying out financial activities on a professional basis. In this regard, the Circular of 4 July 2019 *on auditing standards for the annual and consolidated accounts of entities carrying out financial activities on a professional basis,* concerning the statutory audit of the financial statements of such entities, carried out by an external auditor, was promulgated.

Prevention and Countering of Money Laundering and Terrorist Financing

The measures required for customer due diligence have been strengthened. To this end, the following Instructions were promulgated:

1) Instruction No. 5 of 29 May 2019, *regarding the list of functions that within the Holy See and the Vatican City State are qualified as politically exposed persons*. A list of names is then regularly updated and sent to the entities that carry out financial activities on a professional basis.

2) Instruction No. 6 of 19 September 2019, *on the monitoring of the lists of designated entities* issued by the competent bodies of the Security Council of the United Nations and the European Union, in order to strengthen the procedures and measures regarding counterpart due diligence and suspicious activity reporting and, in particular, in the context of preventing and countering the financing of terrorism.

Furthermore, over the course of 2019, three updates were made (25 February 2019, 26 June 2019 and 21 October 2019) to the Annex to Instruction No. 1, *which publishes the list of high-risk states with strategic deficiencies in their systems for preventing and combating money laundering and terrorist financing*, taking into account the updates of the lists published by the Financial Action Task Force (FATF).

The main sources of legislation making up the current regulatory framework are, therefore, the following:

(a) Regulation No. 1 *on Prudential supervision of entities carrying out financial activities on a professional basis* (entered into force on 13 January 2015, as amended and supplemented on 19 September 2018);

(b) Regulation No. 2 *establishing the information and data accompanying transfers of funds, and the technical requirements for credit transfers and direct debits in euro* (of 12 December 2017, as amended and supplemented on 19 June 2018);

(c) Regulation No. 3 *governing the payment services provided by entities carrying out financial activities on a professional basis* (of 23 May 2018);

(d) Regulation No. 4 *relating to customer due diligence of entities carrying out financial activities on a professional basis* (of 19 September 2018);

(e) Regulation No. 5 *on suspicious activity reports* (of 19 September 2018);

(f) Instruction No. 1 *publishing the list of high-risk States, with strategic deficiencies in their systems for preventing and combating money laundering and terrorist financing* (of 23 October 2017);

(g) Instruction No. 2 *on reporting requirements for statistical information on fraud related to means of payment* (of 30 April 2019);

(h) Instruction No. 3 *on claim procedures to the Financial Information Authority for the settlement of disputes related to the provision of payment services by entities carrying out financial activities on a professional basis* (of 29 May 2019);

(i) Instruction No. 4 *on measures for the management of operational and security risks related to payment services and connected reporting duties* (of 29 May 2019);

(j) Instruction No. 5 *publishing the list of functions that within the Holy See and the Vatican City State are qualified as politically exposed persons* (of 29 May 2019);

(k) Instruction No. 6 *on monitoring of the lists of designated entities* (of 19 September 2019);

(l) Circular *on the drafting of annual and consolidated accounts of entities carrying out financial activities on a professional basis* (of 15 December 2016, as amended and supplemented on 31 October 2017);

(m) Circular *on monetary and financial statistics of entities carrying out financial activities on a professional basis* (of 29 December 2016);

(n) Circular *on interest rates applied by entities carrying out financial activities on a professional basis* (of 29 December 2016);

(o) Circular *on auditing standards for the annual and consolidated accounts of entities carrying out financial activities on a professional basis* (of 4 July 2019).

Memoranda of Understanding with Domestic Authorities

The collaboration and exchange of information between the Authorities of the Holy See and the Vatican City State are a fundamental prerequisite and guarantee for preventing and combating illegal activities, as well as for promoting transparency and integrity in financial activities.

Within this framework, on 9 May 2019, AIF and the Office of the General Auditor, in its capacity as an anti-corruption authority, signed a memorandum of understanding concerning collaboration and the exchange of information related to the prevention and combating of money laundering, terrorist financing, and corruption.

Furthermore, on 11 December 2019, AIF entered into a memorandum of understanding with the Office of the Promoter of Justice to strengthen the procedures and measures that guarantee the confidentiality, adequate processing and appropriate storage of data, documents and information received from foreign Financial Intelligence Units in the event of an exceptional search and seizure ordered by the Judicial Authority pursuant to Article 51 of Law No. XVIII, aligning such procedures to the Principles established by the *Egmont Group.*[1]

[1] "*Principles for Information Exchange among and between Financial Intelligence Units*", No. 8, 14, 20, 25, 26, 28, 29, 31, 32, 33, 36, adopted in 2013 by the *Egmont Group*.

1.2. ECONOMIC AND FINANCIAL FRAMEWORK

By virtue of Law No. V of 7 June 1929 *on the economic, commercial and professional sectors*, a public regime was established in the Vatican City State, and there are no financial markets or private financial actors:

(a) regulated markets, multilateral trading facilities and organized trading facilities are not established;

(b) public debt instruments, capital instruments, securities and associated instruments are not issued;

(c) insurance companies, electronic money institutions, trust companies and securities firms are not established;

(d) branches or subsidiaries of foreign financial institutions are not established.

Pursuant to the prudential regulatory framework in force, the carrying out of one or more financial activities on a professional basis is subject to the prior authorization of AIF.

Currently, the only entity authorized to carry out financial activities on a professional basis is the Institute for the Works of Religion (IOR).

1.2.1. Single Euro Payments Area (SEPA)

In November 2018, the *European Payment Council* (EPC) approved the entry of the Holy See/Vatican City State in the geographical scope of the *Single Euro Payments Area* (SEPA), with a favourable opinion of the European Commission.[2] In November 2019, once compliance with all the regulatory and technical requirements was completed and verified, the Vatican's International Bank Account Number (IBAN) became active. This number can be used to uniquely identify payment accounts opened with financial institutions in the jurisdiction.[3]

[2] See *Release of the Press Office of the Holy See of 30.11.2018 [B0885]* (https://press.vatican.va/content/salastampa/it/bollettino/pubblico/2018/11/30/0885/01934.html).
[3] See *IBAN Registry, Release 81 – December 2018*, p. 80.

2. INSTITUTIONAL FUNCTIONS

2.1. STATUTE AND INSTITUTIONAL FUNCTIONS

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.
AIF's mandate was consolidated by Pope Francis with the Apostolic Letter issued "Motu Proprio" *approving the Statute of the Financial Information Authority* of 15 November 2013.

Pursuant to Article 1 of the Statute, AIF has the status of an "institution connected to the Holy See", is endowed with public legal personality under Canon Law, and has its registered office in the Vatican City State.

Pursuant to Article 2 of the Statute, AIF carries out the following institutional functions in full autonomy and independence:

(a) prudential and AML/CFT supervision;

(b) financial intelligence;

(c) cooperation and exchange of information at the domestic and international levels.

2.2. STRUCTURE AND ORGANIZATION

The structure and organization of AIF are defined by the Statute (see § 2.1).

Pursuant to Article 3 (1), AIF's Statutory bodies are:

(a) the Board of Directors, which sets the policies and strategies;

(b) the President, who is the legal representative of AIF, chairs the Board of Directors and oversees the proper performance of activities and compliance with statutory provisions;

(c) the Director, who is in charge of the operational activity of AIF, is a Member of the Financial Security Committee (CoSiFi) and takes part in the Holy See's Delegation to international bodies responsible for countering money laundering and the financing of terrorism.

As at 31 December 2019, the Board of Directors was composed of the following members: Ms Maria Bianca Farina (Italy) and Mr Joseph Yuvaray Pillay (Singapore).

Pursuant to Article 3 (2) of the Statute, AIF's organisation is subdivided into two units:

(a) Supervision and Regulation Unit;

(b) Financial Intelligence Unit.

The Statute ensures the functional separation between supervisory and the financial intelligence activities. At the same time, and considering the uniqueness of the jurisdiction, the coexistence of the two units

within the same institutional framework ensures effective coordination and constitutes an added value for the effectiveness of the AML/CFT system as a whole.

Supervision and Regulation Unit

Competent for prudential and AML/CFT supervision, including the cooperation and exchange of information with the authorities of the Holy See and the Vatican City State, and foreign supervisory authorities, pursuant to Article 2 (a) (b) of the Statute and Articles 46, 65 and 69 of Law No. XVIII.

Financial Intelligence Unit

Competent for financial intelligence activities, including the cooperation and exchange of information with the authorities of the Holy See and the Vatican City State and foreign Financial Intelligence Units (FIUs), under Article 2 (c) of the Statute and Articles 48 and 69 of Law No. XVIII.

2.3. SUPERVISED SUBJECTS

According to the "Motu Proprio" of 8 August 2013 (see 1.1), all dicasteries of the Roman Curia and other bodies and entities that depend on the Holy See, as well as non-profit organizations (NPOs) having legal personality pursuant to Canon Law and having their registered offices in the Vatican City, fall under the scope of application of the legislation concerning:

(a) measures to prevent and counter money laundering and terrorist financing (AML/CFT);

(b) measures against subjects who threaten international peace and security;

(c) prudential supervision of entities carrying out financial activities on a professional basis.

The effects of the legislation depend on the institutional and legal status of the entities.

Article 2 of Law No. XVIII (see 1.1.) indicates the categories of subjects falling under AIF's supervision, and includes entities carrying out financial activities on a professional basis.

Pursuant to Article 4 of Law No. XVIII (see 1.1.), AIF publishes and updates the list of supervised subjects. The list includes one entity carrying out financial activities on a professional basis, the IOR.

2.3.1. Institute for the Works of Religion (IOR)

IOR is a public canon law foundation.[4] Pursuant to Article 2 of the Statute approved by Pope Francis with the *Chirograph providing for a new status to the Institute for the Works of Religion* of 8 August 2019, the mission of the IOR consists in: "the custody and administration of movable and immovable property transferred or assigned to the Institute by natural or legal persons, and intended for works of religion and charity".

According to the policy adopted by the Board of Superintendence, the 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 the 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; and diplomats accredited to the Holy See.

The IOR does not have branches or subsidiaries in foreign Jurisdictions.[5]

[4] See Article 1, paragraph 1, of the *Chirograph* whereby Pope Francis *approved the new Statute of the Institute for the Works of Religion*, of 8 August 2019.

[5] See Article 1, paragraph 2, of the *Chirograph whereby Pope Francis approved the new Statute of the Institute for the Works of Religion*, of 8 August 2019.

3. MAIN ACTIVITIES

3.1. GENERAL RISK ASSESSMENT AND RISK-BASED APPROACH

In 2017, the Financial Security Committee (CoSiFi) adopted the first General Risk Assessment (GRA) for the Holy See and the Vatican City State, with a view towards identifying and assessing potential risks of money laundering and terrorist financing, as required by Law No. XVIII[6] and in line with the recommendations of the *Financial Action Task Force* (FATF).[7]

The GRA was carried out using the World Bank's *National Money-Laundering and Terrorist Financing Risk Assessment Tool*, and involved all the competent Authorities of the Holy See and the Vatican City State. It had as its main object the limited financial activity carried out on a professional basis in the Vatican City State. At the same time, the GRA focused on the AML/CFT system as a whole, including the safeguard of the governmental financial activities, the donations, and the non-profit organizations (NPOs) registered in the Vatican City, as a consequence of a comprehensive risk-based approach.

Among the initial outcomes of the GRA is Law No. CCXI of 22 November 2017 *on the registration and supervision of non-profit entities*, which introduces the obligation to report suspicious activities on the part of non-profit organisations registered in the Vatican City State, as well as Instruction No. 1 of 23 October 2017.

In 2019, CoSiFi produced a second update of the GRA, which confirms a medium-low level of ML risk and a low level of FT risk, with no significant domestic threats. The main risks identified relate to international and/or cross-border activities. However, some areas can be further strengthened for a more effective AML/CFT system as a whole, such as donations, non-profit entities, public administrations and public procurement contracts.

This second update made it possible to adopt measures to mitigate the risks identified in the first GRA update of 2018. With regard to AIF, it is worth noting that, among other things, it carried out a general on-site inspection at the IOR for AML/CFT purposes, and adopted Instructions No. 5 and 6.

In the GRA update, additional measures were recommended to promote ever-growing awareness of potential risks in the AML/CFT area, including strengthening domestic prevention mechanisms and the supervision of public administrations and non-profit organisations registered in the Vatican City State; and refresher training sessions for the Holy See and Vatican City State offices active in relevant sectors, as well as for the entities carrying out financial activities on a professional basis.

[6] See article 9 (1) (b) of Law no. XVIII.

[7] See Recommendation no. 1 (Assessing risks and applying a risk-based approach), and Recommendation no. 2 (National cooperation and coordination).
FATF, International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation, The FATF Recommendations, February 2018.

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

Over the course of 2019, AIF continued its supervision of financial activities carried out on a professional basis in the Vatican City State.

The regulatory framework was further consolidated through new Instructions, also bearing in mind the commitments made by the Holy See with the *Monetary Agreement between the European Union and the Vatican City State* of 2009, and the *Ad hoc* Arrangement adopted on 19 December 2014 by the Joint Committee for the implementation of the same Agreement. The transposition of the relevant and applicable European Union legal sources has been carried out, consistent with the unique economic and financial framework of the jurisdiction (see § 1.2).

3.2.1. Prudential Supervision and Regulation

Prudential supervision was mainly focused on compliance with the legislative and regulatory framework in force regarding the payment services offered to users and on assessing its efficiency, with a special focus on the SEPA circuit. To this end, in June 2019 AIF conducted a targeted *on-site* inspection at the IOR.

(a) Strengthened Communication on Payment Services

Considerable progress was made in recent years in the integration of payment systems at international and, in particular, European level. This integration was also possible thanks to the definition of an appropriate set of common regulatory, technical, and operational rules.

Entry into the SEPA geographical scope required, *inter alia*, the preparation and adoption of an adequate and efficient regulatory framework for payment services, which was then further strengthened during the year.

Indeed, under the new provisions, payment service providers are required to regularly transmit to AIF the relevant data and information concerning, *inter alia*, the following:

(i) any fraud related to different means of payment initiated and executed, included those initiated by a payment order service provider; and

(ii) activities, operations and transactions related to the various means of payment, attempted and not executed, reported pursuant to Article 40 (1) of Law No. XIII of 8 October 2013.

(b) Definition of Standards on the Settlement of Disputes Arising from the Provision of Payment Services

Instruction No. 3 (see § 1.1) allowed for the introduction in the regulatory framework of standards on the settlement of disputes arising from the provision of payment services, aimed at establishing transparent and effective claim procedures to protect users.

The claim procedure may be activated for disputes related to the conclusion, execution or interpretation of contracts related to payment services concerning, *inter alia*:

(i) the ascertainment of rights, obligations and powers, without regard to the value of the service to which they refer; and
(ii) the payment of a sum of money within the limit of 100,000 euro, which in case of a currency other than the euro is calculated using the average reference exchange rate published by the European Central Bank for the relevant period.

To further facilitate the activation of such procedures, a form for claims has been prepared and made available on the AIF's website, and a dedicated e-mail address has been activated as well.

(c) Strengthened Measures for the Management of Operational and Security Risks Related to Payment Services

The publication of Instruction No. 4 introduced, *inter alia*:

(i) requirements for the establishment, implementation and monitoring of the security measures that payment service providers shall take to manage the operational and security risks relating to the payment services they offer, pursuant to Article 61 (1) of Regulation No. 3; and

(ii) the criteria for the classification of major operational or security incidents by payment service providers, as well as the format and procedures they shall follow to notify such incidents to the Financial Information Authority, as laid down in Article 62 (1) of Regulation No. 3.

In order to further facilitate the relevant fulfilments, a reporting template of major operational or security incidents has been prepared and made available on the AIF's website. Payment service providers are required to fill in this form in order to keep AIF informed throughout the incident.

(d) Onsite Inspection of Payment Services and Conformity with SEPA Requirements

In June 2019, AIF conducted a targeted on-site inspection at the IOR for the purpose of verifying compliance with the current legislative and regulatory framework for payment services, including the fulfilment of all the necessary requirements for the IOR to join the SEPA schemes, as well as the "effectiveness" of the payment systems.

In particular, the inspection focused on:

(i) transparency of conditions and information requirements for payment services, as laid down in Title II of Regulation No. 3 *governing payment services provided by entities carrying out financial activities on a professional basis*;

(ii) rights and obligations in relation to the provision and use of payment services, as laid down in Title III of Regulation No. 3;

(iii) comprehensiveness and adequacy of compliance schemes with the provisions of Instruction No. 2 *on reporting requirements for statistical information on fraud related to means of payment*, and of Instruction No. 4 *on measures for the management of operational and security risks related to payment services and connected reporting duties*; and

(iv) comprehensiveness and adequacy of technical requirements to ensure indirect adherence to SEPA schemes, including the clearing and regulatory mechanisms that will be implemented.

The inspection – which had a substantially positive outcome – verified the fulfilment of the necessary requirements for the IOR to join the relevant SEPA schemes. The technical and operational activities related to SEPA (adequacy of services provided, effective functioning of internal procedures, etc.) began to be concretely carried out by the IOR once the entry process was successfully completed.

3.2.2. Supervision and Regulation of the Prevention and Countering of Money Laundering and the Financing of Terrorism

AML/CFT supervision was mainly focussed on verifying the implementation of a risk-based approach, compliance with the legislative and regulatory framework in force in the State - including AIF instructions and guidelines - and the concrete effectiveness of the policies, procedures and measures adopted by the supervised entities.

Starting in August 2019, AIF carried out the second general on-site inspection at the IOR on the prevention and combating of money laundering and terrorist financing, including the effective functioning of the measures and safeguards adopted.

(a) List of Politically Exposed Persons

Instruction No. 5 provides for the publication of the list of functions that within the Holy See and the Vatican City State are qualified as politically exposed persons, pursuant to Article 1 (14) (h) of Law No. XVIII of 8 October 2013. Entities carrying out financial activities on a professional basis shall adopt enhanced customer due diligence measures in the event of relationships, or activities, operations or transactions, even occasional, in the name, on behalf or in favour of politically exposed persons. The qualification of a PEP – or of a family member or person with close links to a PEP – involves the acquisition of additional information when carrying out due diligence (e.g. the amount and origin of the counterpart's total assets).

Taking into account the updates of the Pontifical Yearbook, AIF periodically provides a list with the names of politically exposed persons to the entities that carry out financial activities on a professional basis.

(b) List of Designated Subjects

With a view towards strengthening procedures and measures for the prevention and countering of terrorist financing, and implementing a risk-based approach, Instruction No. 6 was published on the monitoring of the lists of designated subjects issued by the competent bodies of the UN Security Council and the European Union.

The aforementioned Instruction is part of an effort aimed at strengthening the provisions of Title VI of Law No. XVIII, "*Measures against subjects threatening international peace and security*". It establishes that, in carrying out activities of counterpart due diligence and identification and reporting of potential suspicious activities, the supervised entities shall monitor lists of designated entities issued by the competent bodies of the United Nations and the European Union, in addition to those issued by the President of the Governorate of the Vatican City State.

In the event of a potential involvement with subjects included in the list, the supervised entities shall send, in a timely manner, a suspicious activity report to the Financial Information Authority indicating, among other things:

(i) data and information concerning relationships, activities, operations or transactions, as well as

any available data related to the designated subjects; and

(ii) data or information concerning any attempted activities, operations or transactions based on funds or other assets economically relevant for the designated subjects.

(c) Update of the List of High-Risk States

The integrity of financial activities is seriously threatened by States with strategic deficiencies in their anti-money laundering and terrorist financing systems. Instruction No. 1 of 23 October 2017[8] has established an *ad hoc* reporting system, instrumental also in the protection of humanitarian and charitable activities in high-risk or unstable environments, where the Holy See and its instrumentalities are particularly active to meet the requirements of the civil population.

The annex to the Instruction was updated three times in the course of 2019: on 25 February 2019,[9] on 26 June 2019,[10] and on 21 October 2019.[11]

(d) AML/CFT On-Site Inspection

Starting in August 2019, AIF conducted its second onsite general inspection at the IOR, to check and verify the Institute's technical compliance with the existing legal and regulatory framework on the prevention and countering of money-laundering and terrorist financing (AML/CFT), as well as the effectiveness of the measures and safeguards in place.

The general inspection – which followed the first general inspection of 2014, and the four targeted inspections held over the years 2015-2018[12] – is part and parcel of the AML/CFT supervision process, as established by AIF following a risk-based approach, pursuant to Article 7 (2) of Law No. XVIII, and relevant domestic policies.

The Inspection in question was aimed at evaluating the pathway the IOR had gone through in the previous 5 years, and to this end the following profiles were analysed: (i) risk assessment; (ii) internal audits; (iii) due diligence; (iv) transfer of funds; (v) safeguards on cash- or cheque-based transactions, and on the safety box service; (vi) suspicious activity reporting, and (vii) implementation of obligations for the transmission of declarations for cross-border transportation of currency.

The inspection was subdivided into two phases:

(i) a first remote phase, characterised by the review and analysis of all policies, procedures and measures adopted over the years 2015-2019;

[8] See *Public Statement* and *Improving Global AML/CFT Compliance: On-going Process*, as made public by the FATF on 23 October 2017.

[9] See *Public Statement* and *Improving Global AML/CFT Compliance: On-going Process,* as made public by the FATF on 22 February 2019.

[10] See *Public Statement* and *Improving Global AML/CFT Compliance: On-going Process,* as made public by the FATF on 21 June 2019.

[11] See *Public Statement* and *Improving Global AML/CFT Compliance: On-going Process,* as made public by the FATF on 18 October 2019.

[12] These are in particular the inspections serving the following purposes:
1) to verify the actual segregation between the investment activities carried out by the Institute on its own behalf, and the investment activity carried out on behalf of its customers;
2) to verify compliance of some specific provisions on the transfer of funds with the legal and regulatory framework in force;
3) to verify compliance of the existing legal and regulatory framework for the management of "non-autonomous pious foundations" or "legates";
4) to verify compliance of the way in which transfers of funds are carried out with the existing legal and regulatory framework.

(ii) a second on-site phase carried out through meetings with the relevant IOR functions and personnel, support in the execution of ordinary processes, and examination of a sample of relevant documents and data.

The outcome of the inspection highlighted a high level of technical compliance with the existing AML/CFT legal and regulatory framework, and an adequate level of effectiveness of the relevant measures and safeguards adopted. There was also some room for improvement, against which an action plan was drawn up to implement appropriate mitigation measures.

3.2.3. *International Cooperation and Exchange of Information*[13]

AIF exchanged information with foreign supervisory authorities in 18 cases (16 requests *to* foreign authorities and 2 requests *from* foreign authorities). International cooperation produced concrete results and in some cases allowed for the analysis of complex financial schemes with connections with several jurisdictions, leading to the reporting of potential breaches and misconducts. With some counterparts, since the respective jurisdictions have closer financial interactions, the cooperation and exchange of information was carried out on a regular basis, and its scope was not limited to the prevention of potential breaches and misconducts, but covered the overall integrity and sustainability of the financial activities, also from the perspective of prudential supervision.

[13] Pursuant to Article 69 (b) of Law No. XVIII, AIF: "cooperates and exchanges information with equivalent authorities of other States, on the condition of reciprocity and on the basis of memoranda of understanding. The Secretariat of State is informed of such memoranda being entered into."

3.3. FINANCIAL INTELLIGENCE

Financial intelligence activities consist of following main activities:

(a) the receipt of suspicious activity reports (SARs) from supervised entities, authorities of the Holy See and the Vatican City State, non-profit organisations (NPOs) and other subjects;

(b) operational analysis of the SARs, which includes accessing documents, data and information, the outcome of which may result in one of the following:

  (i) the adoption of preventive measures;

  (ii) the transmission of reports, documents, data and information to the Office of the Promoter of Justice;

(c) strategic analysis, carried out annually, and based on aggregate data from SARs;

(d) domestic and international cooperation and exchange of information.

3.3.1. Suspicious Activity Reports

In 2019, AIF received 64 Reports, 55 of which from supervised subjects, 4 from authorities of the Holy See and Vatican City State and 5 from other subjects (see § 4.2.1).

The SARs submitted by reporting entities confirmed the same trend already observed in 2017 and 2018[14] towards better quality reports, also fostered by the provision of more detailed anomaly indicators and a more aware implementation of a risk-based approach (§ 3.1). The trend was also linked to the stabilization and normalization of the reporting system and the intensification of the preventive measures taken by the IOR itself.

Within the framework of its analytical activities, in 2019 AIF ordered 4 preventive measures – 3 transactions were suspended pursuant to Article 48 (j) of Law No. XVIII for a total of 240,000 euro, and one account was frozen pursuant to Article 48 (k) of Law No. XVIII for a total 178,970.65 euro[15] – thus confirming the consolidation of a rigorous preventive approach in identifying potential suspicious activities (see § 4.2.2).

[14] See Financial Information Authority, *Annual Report 2018*, § 3.3.1, p. 15.

[15] Pursuant to Article 48 (j) (k) of Law No. XVIII, AIF: "suspends the execution, for up to five working days, of transactions and operations suspected of money laundering or financing of terrorism, as well as any other linked operation or transaction, where this does not obstruct investigative or judicial activity; 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".

Box 1 – Example case

A company based in a foreign state has signed a contract with the Vatican City State.
The company is owned by a foreign citizen and businessman holding a personal account with a financial institution based in the Vatican City State
The businessman requests that the fees for the services rendered to the Vatican entity be paid into the account with the financial institution on which he is delegated to operate. The businessman then withdraws these sums in cash.
Owing to the large cash withdrawals, the Vatican financial institution sends a suspicious activity report to Financial Information Authority.
AIF, after having activated several channels of both domestic and international cooperation and exchange of information, sends a report to the Office of the Promoter of Justice, finding in the conduct of the businessman potential crimes of tax evasion and fraudulent tax declaration in his State of origin.
The Office of the Promoter of Justice opens a file for further investigative activities. Subsequently, the businessman is sentenced and convicted for the crime of self-laundering in the Vatican City State, and the sums deposited into the Vatican financial institution are seized.

IT structures (hardware and software) and cyber-security systems have been further strengthened to ensure the highest level of integrity, security and confidentiality of data storage and processing.

An assessment of the security of the infrastructure in use at the Authority was carried out during the year. The purpose of this assessment was to identify security issues and subsequent vulnerabilities that may affect servers and data processing applications.

The assessment methodology adopted includes review processes structured on the basis of recognized "best-in-class" practices, defined by methodologies such as ISECOM's Open Source Security Manual Testing Methodology, the Open Web Application Security (OWASP) project and the ISO 27001 information security standard.

In particular, the following tests were carried out:

(i) *Penetration Test*, which simulates a realistic attack from outside the network through a web portal exposed to the world, in order to attain a very precise goal; and

(ii) *Vulnerability Assessment*, a type of test specifically designed to discover and validate as many vulnerabilities as possible, and then identify which of them have the greatest impact on the Authority.

Both the tests listed above generated medium and low results. The final report of the assessment process illustrated in detail all issues relevant to vulnerabilities and possible ways that could be used by possible malicious persons to undermine and gain unauthorised access to sensitive information and data.

In 2019, a statistical software was also developed internally to support AIF's strategic and operational analysis activities.

3.3.2. Reports to the Office of the Promoter of Justice

In 2019, AIF filed 15 Reports to the Office of the Promoter of Justice (see § 4.2.3), thus confirming an increasing trend in the proportion between the Reports sent and the SARs received over the years, which also proves a steady increase in the quality of the SARs filed by the reporting entities.

The majority of the potential financial crimes involve foreign subjects or conduct undertaken in, or in connection with, foreign jurisdictions. The main potential predicate offences are: international fraud, including tax fraud, and embezzlement.

3.3.3. Combating the Financing of Terrorism

Against the current global backdrop, the fight against the financing of terrorism is still a priority.

In 2019, AIF received only one SAR potentially connected, directly or indirectly, to terrorist financing; however, after the analysis carried out it proved to be free of the subjective and objective elements that might suggest there may be terrorist financing activities behind the operation concerned.

In this regard, it is worth noting that the 2019 update to the GRA confirmed a low level of FT risk.

At the same time, AIF has maintained a preventive and proactive approach, ensuring its international cooperation and providing steady support to the Financial Intelligence Units (FIUs) of the jurisdictions more exposed to the risk of terrorist attacks.

Within this framework, as laid down in Article 71 (1) of Law No. XVIII, the President of the Governorate of the Vatican City State periodically issues ordinances updating the list of subjects threatening international peace and security, incorporating the indications of the UN Security Council and the European Union, as well as any indications provided by AIF or competent law enforcement authorities. In 2019, the President of the Governorate issued 15 ordinances of this kind.

In forwarding the lists to the IOR, AIF requests enhanced monitoring and the adoption of potential preventive measures, including: the freezing of potential funds and other assets owned, held, controlled or detained, exclusively or jointly, directly or indirectly, by subjects included in the lists; potential benefits and profits generated by the aforementioned funds and assets; and potential funds and other assets held or controlled by other subjects, natural persons or entities, in the name or on behalf of or in favour of subjects included in the lists.[16]

The analyses and subsequent monitoring activities did not show links between the designated subjects and the jurisdiction.

With a view towards promoting the highest level of awareness of the potential risks among the authorities of the Holy See and the Vatican City State and the NPOs registered in the Vatican City, the lists are published in AIF's website[17].

[16] See Article 75 (2) and Article 76 (1) (2) of Law No. XVIII.
[17] See Article 71 (3) of Law No. XVIII.

3.3.4. *Domestic and International Cooperation and Exchange of Information*[18]

Domestic cooperation with the competent authorities of the Holy See and the Vatican City State is intense and led to 24 requests for information and concerned 423 subjects (see § 4.2.4). A marked increase in exchanges with the authorities of the Holy See and Vatican City State was observed as compared with the previous year, which confirms the trend of greater domestic cooperation and exchange of information, as well as greater involvement of Holy See and Vatican City State authorities in countering money-laundering and the financing of terrorism.

In particular, the cooperation with law enforcement authorities, namely the Office of the Promoter of Justice and the Corps of the Gendarmerie, is an important component of the activity of the AIF, producing concrete results in the use of financial intelligence. Furthermore, with a view towards ensuring the appropriate coordination of the relevant operational activities, again in 2019 regular meetings were held between AIF, the economic and financial crimes section of the Office of the Promoter of Justice and the Economic and Financial Police Unit of the Gendarmerie Corps. Following the amendment to Law No. XVIII (see § 1.1), and in particular the introduction of Article 48 (n), since 2018 AIF has received feedback from the competent authorities, including the Office of the Promoter of Justice and the Gendarmerie Corps, on the use of the information provided and on the outcome of the investigations or inspections carried out on the basis of that information. This is an important development for the effective functioning and coordination of the domestic system.

Box 2 – Example case

A financial institution registered in the Vatican City State sends a suspicious activity report to AIF concerning a customer of the institution which, according to press reports, is under investigation in a foreign jurisdiction.
Analyses carried out by AIF highlight the possibility that the amounts transited on the person's current account may represent the proceeds of potential misconduct carried out in the foreign jurisdiction.
AIF, after having activated, *inter alia,* the channels of cooperation and exchange of information with the Financial Intelligence Unit of the country concerned, sends a report to the Office of the Promoter of Justice who initiates criminal proceedings for further investigative activities, while requesting international legal assistance by means of an international letter rogatory.
Following the report transmitted by AIF, the Office of the Promoter of Justice issued a freezing order on the accounts held by the person with Vatican financial institution.

AIF exchanged 66 requests for information with foreign FIUs concerning 373 subjects (see § 4.2.5). International cooperation resulted in the transmission of relevant financial intelligence to the Office of the Promoter of Justice and to foreign counterparts.

In 2019, AIF signed new memoranda of understanding with the FIUs of 4 foreign jurisdictions, such as: Finland, the Cook Islands, the Czech Republic and Serbia, amounting to a total 60 Memoranda of understanding that have been signed since 2012 (see § 4.2.6).[19]

[18] Pursuant to Article 69 (a) (b) of Law No. XVIII, AIF: "cooperates and exchanges information with other authorities of the Holy See and the Vatican City State, which provide the Financial Intelligence Authority with the relevant documents, data and information; cooperates and exchanges information with equivalent authorities of other States, on the condition of reciprocity and on the basis of memoranda of understanding. The Secretariat of State is informed of the memoranda entered into".
[19] In alphabetical order: Albania, Andorra, Argentina, Armenia, Aruba, Australia, Austria, Belgium, Brazil, Bulgaria, Cape Verde, Canada, Chile, Colombia, Cuba, Cyprus, Czech Republic, Ecuador, Estonia, Finland, France, Germany, Ghana, Gibraltar, Greece, Guernsey, Honduras, India, Isle of Man, Cook Islands, Jersey, Italy, Latvia, Liechtenstein, Luxembourg, Malta, Mexico, Moldova, Monaco, New Zealand,

3.4. ADDITIONAL ACTIVITIES

3.4.1. Declarations of Cross-Border Transportation of Currency

Article 81 of Law No. XVIII establishes the duty to declare the cross-border transportation of currency (cash and bearer negotiable instruments) for an amount equivalent to, or greater than, 10,000 euro. The declaration must be presented to the Corps of the Gendarmerie, namely the competent customs Authority, or to the offices authorized by AIF.

In 2019, there were 270 incoming declarations, amounting to a total of 5,849,652.71 euro, and 851 outgoing declarations, amounting to a total of 15,781,160.28 euro. The number and amount of cross-border declarations confirm the trend already observed in previous years of a progressive decrease in the use of cash (see § 4.3.1). The trend is also due to the availability of other systems of funds transfer carried out by the IOR (including the possibility of making a funds transfer through the SEPA circuit, which became avaible in 2019), thus ensuring a better standard of security and traceability.

In 2019, the analysis of the declarations carried out by AIF did not show significant anomalies or risk indicators.

3.4.2. Tax Compliance

Within the Vatican City State there are no productive economic activities (see § 1.2) and a structured domestic tax system is not in place.

At the same time, the Holy See is strongly commitment to ensuring international cooperation and the exchange of information for the prevention of tax evasion and the promotion of the fulfilment of fiscal requirements by foreign citizens and legal entities having an account at the IOR.

To this end, the Holy See signed two international treaties on fiscal matters: the *Convention between the Holy See (acting also in the name and on behalf of the Vatican City State) and the Government of the Italian Republic in fiscal matters* of 1 April 2015, and the *Agreement between the Holy See (acting also in the name and on behalf of the Vatican City State) and the United States of America to improve international tax compliance and exchange of tax information in view of the US Foreign Account Tax Compliance Act (FATCA Agreement)* of 10 June 2015.

As far as the FATCA Agreement is concerned, AIF and the Secretariat for the Economy (identified by the signatory parties as the competent authority of the Holy See for the transmission of data) signed an MOU on 10 November 2015 allowing AIF to monitor the implementation of the procedures adopted by the IOR for the fulfilment of the requirements established by the Agreement.

The checks and controls carried out by AIF in 2019 showed that the implementation of the procedures adopted by the IOR is effective. Furthermore, the overall monitoring activities did not show significant anomalies and risk indicators, and this is also a concrete result of the constant review of the adherence by the customers of the IOR to the voluntary tax compliance programmes launched by their respective jurisdictions, object of specific instructions issued by AIF,[20] in line with the indications provided by the FATF in view of preventing voluntary tax compliance programmes from being abused to

Norway, Netherlands, Panama, Paraguay, Peru, Poland, Portugal, United Kingdom, Romania, Russia, San Marino, Serbia, Slovenia, United States of America, South Africa, Spain, Switzerland, Taiwan (Republic of China), Hungary, Uruguay.

[20] See AIF, *Annual Report*, Year IV-2015, p. 14, Vatican City 2016.

circumvent AML/CFT policies.[21]

3.4.3. Other International Activities

In 2019, AIF actively participated in the meetings of the working groups of the *Egmont Group* (the Hague, Netherlands, 1-5 July 2019).

AIF was also part of the delegation of the Holy See to the 58th and 59th Plenary Assembly (respectively 15-19 July, and 2-6 December, 2019) *Committee of Experts on the Evaluation of Anti-Money Laundering and Combating the Financing of Terrorism Measures* (MONEYVAL) at the Council of Europe.

[21] FATF, Best Practices Paper, *Managing the Anti-Money Laundering and Counter-Terrorist Financing Policy Implications of Voluntary Programmes*, October 2012.

PART II

STATISTICS

4. STATISTICS

4.1. SUPERVISION AND REGULATION

4.1.1. International Cooperation

	2015	2016	2017	2018	2019
Total	***12***	***11***	***14***	***15***	***18***
Requests to foreign supervisory authorities	***10***	***11***	***11***	***13***	***16***
Requests from foreign supervisory authorities	***2***	***0***	***3***	***2***	***2***

4.1.2. Memoranda of Understanding with foreign Supervisory Authorities

	2015	2016	2017	2018	2019
Total	***0***	***3***	***1***	***1***	***0***

4.2. FINANCIAL INTELLIGENCE

4.2.1. Suspicious Activity Reports

	2015	2016	2017	2018	2019
Total	***544***	***207***	***150***	***54***	***64***
Supervised entities	***537***	***192***	***136***	***48***	***55***
Authorities of the Holy See /Vatican City State	***6***	***8***	***9***	***4***	***4***
Non-Profit Organisations	***0***	***0***	***0***	***0***	***0***
Other subjects	***1***	***7***	***5***	***2***	***5***

4.2.2. Preventive Measures

	2015		2016		2017		2018		2019	
	Number	**Amount**	**Number**	**Amount**	**Number**	**Amount**	**Number**	**Amount**	**Number**	**Amount**
Suspension of transactions and operations	8	€8.262.565,42 $ 1.714.800	4	€2.113.838,55	0	-	3	€422.077,00	3	€ 240.000,00
Freezing of accounts, funds and other assets	4	€7.051.422,42 $ 654.800	1	€1.550.199,45	1	€175.740,40	2	€2.362.725,53	1	€ 178.970,65

4.2.3. Reports to the Office of the Promoter of Justice

	2015	2016	2017	2018	2019
Total	*22*	*24*	*8*	*11*	*15*

4.2.4. Domestic Cooperation

	2015	2016	2017	2018	2019
Total	*117*	*72*	*91*	*234*	*423*
Subjects involved in requests to Authorities of the Holy See/Vatican City State	108	67	86	230	**413**
Subjects involved in requests from Authorities of the Holy See/ Vatican City State	9	5	5	4	**10**

4.2.5. International Cooperation

	2015	2016	2017	2018	2019
Total	*380*	*837*	*268*	*473*	*373*
Subjects involved in requests to foreign FIUs	199	721	88	231	**313**
Subjects involved in requests from foreign FIUs	181	116	180	242	**60**

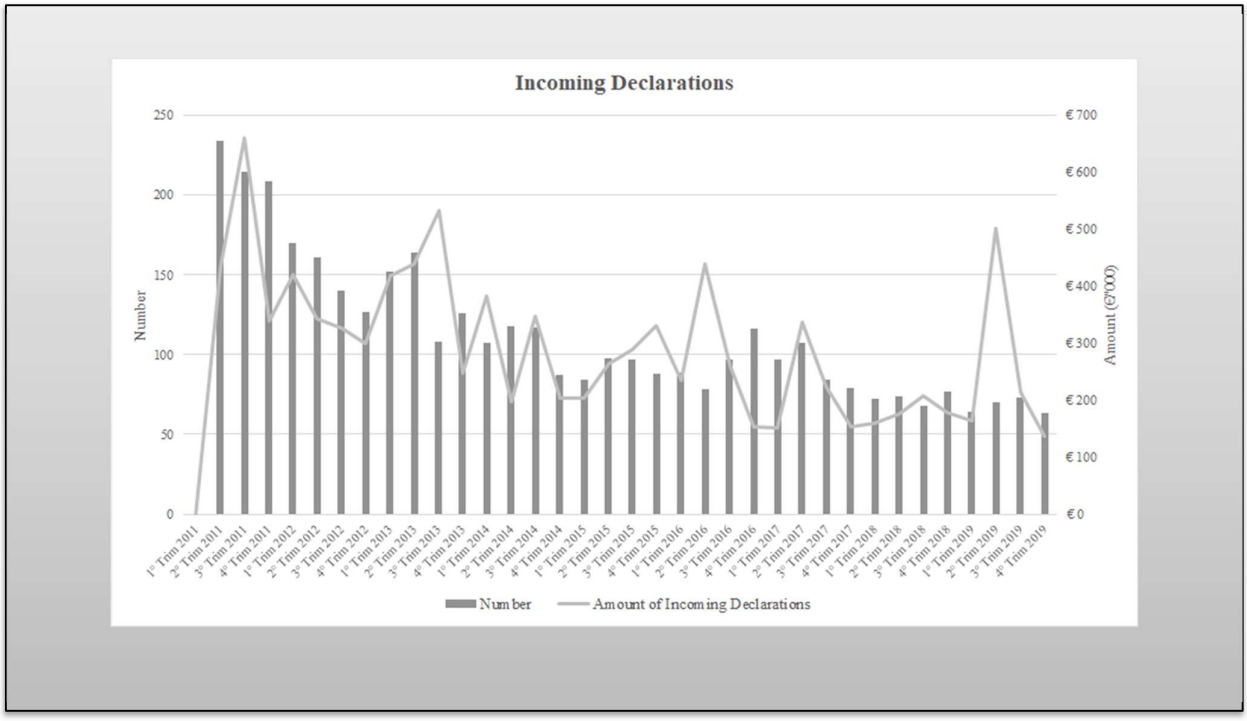
4.2.6. Memoranda of Understanding with Foreign Financial Intelligence Units

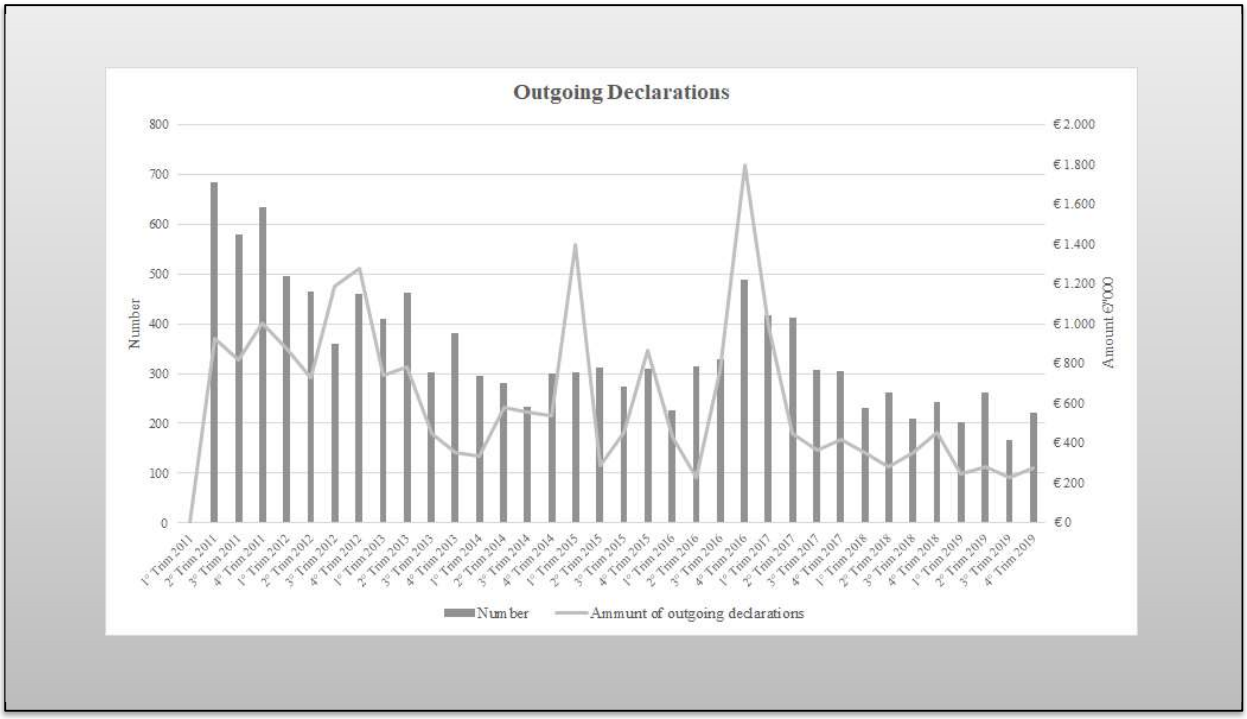
	2015	2016	2017	2018	2019
Total	*6*	*5*	*18*	*6*	*4*

4.3. DECLARATIONS OF CROSS-BORDER TRANSPORTATION OF CURRENCY

4.3.1. Number and Amount of Declarations

	2015	2016	2017	2018	2019
Total Number Total Amount	***1.563 €33.853.411,37***	***1.737 €33.598.780,16***	***1.806 €32.630.799,91***	**1.239 *€26.085.386,73***	**1121 € 21.630.812,99**
Incoming Declarations					
Number	367	380	367	291	270
Amount	€9.697.570,61	€ 9.642.657,58	€9.222.729,22	€7.416.789,14	€ 5.849.652,71
Outgoing Declarations					
Number	1.196	1.357	1.439	948	851
Amount	€24.155.840,76	€23.956.122,58	€23.408.070,69	€18.668.597,59	€ 15.781.160,28




Outgoing Declarations
Number
Amount €'000
800
700
600
500
400
300
200
100
0
€ 2.000
€ 1.800
€ 1.600
€ 1.400
€ 1.200
€ 1.000
€ 800
€ 600
€ 400
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3° Trim 2019
4° Trim 2019
Number
Ammunt of outgoing declarations

GLOSSARY/ACRONYMS

AIF, Financial Information Authority (*Autorità di Informazione Finanziaria)*

CoSiFi, Committee of Financial Security *(Comitato di Sicurezza Finanziaria)*

AML/CFT, Anti-Money Laundering and Countering the Financing of Terrorism

FATCA, Foreign Account Tax Compliance Act of the United States of America

FATF, Financial Action Task Force

EGMONT GROUP, a global body of Financial Intelligence Units (FIUs)

IOR, Institute for the Works of Religion *(Istituto per le Opere di Religione)*

MONEYVAL, Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism of the Council of Europe

NPO, Non-Profit Organisation

SAR, Suspicious Activity Report

FIU, Financial Intelligence Unit

GRA, General Risk Assessment