

## CHAPTER 4

# MONEY LAUNDERING

## CONTENTS

1. INTRODUCTION TO MONEY LAUNDERING
2. THE ESSENTIAL ELEMENTS OF MONEY LAUNDERING
3. THE MOST COMMON METHODS OF MONEY LAUNDERING
4. INTERNATIONAL STANDARDS FOR PREVENTION AND CRIMINALIZATION OF MONEY LAUNDERING
5. STATE-LEVEL AML REGIMES: US, UK AND CANADA
6. EVALUATING THE EFFECTIVENESS OF AML REGIMES

### 1. INTRODUCTION TO MONEY LAUNDERING

The term “money laundering” describes a range of practices used to disguise the source of illicit profits and integrate them into the legitimate economy. Simply put, money laundering means ‘washing’ dirty money so that it appears clean. Corrupt officials and other criminals use money laundering techniques to hide the true sources of their income. This allows them to avoid detection by law enforcement and to spend their profits freely. Money laundering in some form is an essential part of most illicit enterprises, although methods vary widely. Large drug-trafficking organizations and corrupt public officials use complex, multi-jurisdictional layering schemes; small-time criminals use simpler strategies.

As Baker points out in a 2013 article, all the illicit funds in the global economy flow through similar channels. Drug smugglers, tax evaders and corrupt officials use their money for different ends and acquire it by different means. Nonetheless, Baker notes:

All three forms of illicit money – corrupt, criminal, and commercial – use this structure, originally developed in the West originally for the purpose of moving flight capital and tax evading money across borders. In the 1960s and 1970s drug dealers stepped into these same channels to move their illicit money across borders. In the 1980s and 1990s, seeing how easy it was for the drug dealers to do it, other kinds of racketeers stepped into these same structures to move their illicit money across borders. In the 1990s and in the early years of this new century, again seeing how easy it was for drug dealers and racketeers, terrorist financiers also stepped into these same channels to move their illicit money across borders. Drug dealers, criminal syndicate heads, and terrorist masterminds have not invented any new ways of shifting illicit money across borders. They merely utilize the

mechanisms we originally created to move corrupt and commercially tax evading money across borders.<sup>1</sup>

Therefore, suppressing money laundering through a variety of anti-money-laundering (AML) schemes is essential to combating terrorist financing, organized crime and corruption. What Baker calls the “global shadow financial system” is integral to a broad range of corrupt and criminal activities worldwide.<sup>2</sup> Indeed, as Beare notes, while the 1931 arrest, conviction and downfall of Al Capone is often dismissed as being “merely for tax evasion,” his undoing was in fact due to a failure to launder illicit money adequately.<sup>3</sup>

Because the purpose of money laundering is to conceal the source of illicit funds, it is inherently difficult to measure its global scope. In a recent article, McCarthy summarizes some of the more common estimates:<sup>4</sup>

The IMF and the World Bank, for example, have estimated that some 2-4 per cent of the world’s GDP stems from illicit sources. Agarwal and Agarwal (2004; 2006), using regression analysis and forecasts, suggest an even higher level of 5-6 per cent. At this rate somewhere between \$2.0-2.5 trillion should flow through the money laundering market on an annual basis. Walker (1999, 2004, 2007) however, claims that this is too low a figure and, using input-output and gravity models, proposes that the true amount is more like \$3 trillion per annum. Each estimate is subject to some criticism (cf. Reuter 2007), and are variously said to be overblown – either by media hype, or measurement errors – by as much as +/- 20 per cent (Schneider, 2008). Despite all this the consensus remains that the market for money laundering is a significant one. [footnotes omitted]

Despite the wide range of estimates, there is a degree of consensus among researchers. No one has an accurate estimate, but everyone agrees that a large amount of money is being laundered every year.

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<sup>1</sup> Raymond W Baker, “The Scale of the Global Financial Structure Facilitating Money Laundering” in Brigitte Unger & Daan van der Linde, eds, *Research Handbook on Money Laundering* (Edward Elgar, 2013) 190 at 191.

<sup>2</sup> *Ibid* at 190.

<sup>3</sup> Margaret Beare, *Criminal Conspiracies - Organized Crime in Canada*, (Oxford University Press, 2015) at 208.

<sup>4</sup> Killian J McCarthy, “Why Do Some States Tolerate Money Laundering? On the Competition for Illegal Money” in Unger & van der Linde, eds, (2013) 127 at 129.

## 2. THE ESSENTIAL ELEMENTS OF MONEY LAUNDERING

There are many ways to launder money. Most scholars break laundering schemes into three stages to make it easier to compare, contrast and analyze different methods. These three stages are:

1. **Placement:** illicit funds are used to make a purchase in the legitimate economy;
2. **Layering:** through repeated transactions, the source of the funds is concealed; and
3. **Integration:** the funds are fully and untraceably integrated into the economy.

Regardless of how a money laundering scheme works, it can be broken into these three stages. The “layering” stage, in which the source of the funds is concealed, is where most of the activity occurs in any given scheme. In small-scale schemes, the layering process may be quite simple. In large, complex laundering schemes, it may involve hundreds of transactions in multiple jurisdictions.

A useful and easily readable description of the basic concepts of money laundering and its prevention can be found in the Global Organization of Parliamentarians Against Corruption (GOPAC)’s 2011 guide, the *Anti-Money Laundering Action Guide for Parliamentarians*.<sup>5</sup> GOPAC is a non-profit organization made up of current or former legislators from around the globe. The organization is dedicated to promoting accountability and good governance in national parliaments in order to combat corruption.

## 3. THE MOST COMMON METHODS OF MONEY LAUNDERING

As noted above, the term “money laundering” encompasses a wide variety of different schemes used by everyone from small-time drug dealers to corrupt heads of state. As Beare notes, “[i]t is impossible to identify all the laundering possibilities - from cults to marathons and beyond,” noting in the 1990s the Solar Templar doomsday cult was accused of being a front for laundering, and the Los Angeles Marathon Corporation was convicted of money laundering. Methods of money laundering can be as simple as small businesses dealing in cash using illicit cash to generate greater profits or as complex as international schemes using methods of concealing funds including offshore laundering havens, shell companies and wire transfers.<sup>6</sup> Beare identifies four typologies of money laundering schemes. *Simple-limited* schemes launder relatively small volumes of illicit proceeds through small cash-based businesses such as bars and vending machine companies. *Simple-unlimited* schemes can launder large amounts of money with few transactions utilizing big-budget companies with unclear resources, materials and service costs. *Serial-domestic* schemes use numerous

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<sup>5</sup> Global Organization of Parliamentarians Against Corruption, *Anti-Money Laundering Action Guide for Parliamentarians* (GOPAC, 2011), online:

<[http://www.gopacnetwork.org/Docs/GOPAC\\_AML\\_ActionGuide\\_EN.pdf](http://www.gopacnetwork.org/Docs/GOPAC_AML_ActionGuide_EN.pdf)>.

<sup>6</sup> Beare (2015) at 243-44.

financial transactions, moving funds through a network of transactions that involve multiple banks. *Serial-international* schemes use multiple transactions and international services, often returning funds into big banks in North America and Europe. Both *serial domestic* and *serial-international* schemes can use professionals such as lawyers and accountants.<sup>7</sup> The Liberty Reserve Global takedown demonstrates complex schemes used by money launderers. Liberty Reserve offered a digital currency service based in Costa Rica. The DOJ created a diagram of the complexity of the investigation, which involved 17 countries and 36 mutual legal assistance treaty (MLAT) requests in 15 countries for execution of search warrants, wiretap authorizations, freezing or seizing assets, all of which culminated in 5 arrests.<sup>8</sup>

This chapter focuses on money laundering in the context of corruption. While a great deal of global AML efforts are directed towards controlling organized crime and preventing terrorist financing, those topics are beyond the scope of this book. The following excerpt from “Laundering the Proceeds of Corruption,” a 2011 report produced by the Financial Action Task Force (FATF), describes the most common money-laundering methods used by corrupt officials.<sup>9</sup> The FATF is an inter-governmental policy group composed of 34 nations, including the US, the UK and Canada, which sets standards in the form of the FATF 40 Recommendations, promotes procedures for combatting money laundering and evaluates member states’ performance.

BEGINNING OF EXCERPT

**An Analysis of the Most Common Methods Used to Launder the Proceeds of Grand Corruption**

40. Laundering of corruption proceeds can take a variety of forms, depending on the nature of the corrupt act. In the grand corruption context, the most prevalent forms of proceeds are those arising from 1) bribe-taking or kickbacks; 2) extortion; 3) self-dealing and conflict of interest; and 4) embezzlement from the country’s treasury by a variety of fraudulent means. Understanding the typical methods by which PEPs [“politically exposed persons” – a technical term for public officials in the AML context] unlawfully obtain proceeds assists in understanding how those funds could be laundered.

41. In bribery, money flows from a private entity, generally speaking, to a PEP or associate in exchange for the grant of some sort of government concession: a contract for goods or services, for example, or the right to extract resources from the state. The

<sup>7</sup> *Ibid* at 215-16.

<sup>8</sup> United States, Department of Justice, “The Liberty Reserve Global Takedown”, online: <<https://www.justice.gov/sites/default/files/usao-sdny/legacy/2013/05/30/visual.pdf>>.

<sup>9</sup> Financial Action Task Force, “Laundering the Proceeds of Corruption: FATF Report” (FATF, July 2011), online: <[http://www.fatf-gafi.org/media/fatf/documents/reports/Laundering\\_the\\_Proceeds\\_of\\_Corruption.pdf](http://www.fatf-gafi.org/media/fatf/documents/reports/Laundering_the_Proceeds_of_Corruption.pdf)>.

proceeds of the bribery flow from the bribe giver to the corrupt PEP or an associate, possibly through a shell company or trust in which the PEP is the beneficial owner; it may never touch the home country of the corrupt PEP. A good example of this is found in the Bangkok film festival case, in which two promoters were able to bribe certain Thai officials to obtain the rights to sponsor and manage a government-funded film festival in Thailand.<sup>10</sup> The bribes were paid simply by means of the wire transfer of funds from US-based accounts, where the promoters were located, into offshore accounts in third countries maintained by family members of the PEP. The bribes never passed through Thailand, although that was the locus of the corrupt activity.

42. However, as noted later in the section on the use of cash, sometimes funds are retained in the country where the corruption takes place. For example, Joseph Estrada, then the President of the Philippines, often received cash or check payments from gambling operators in exchange for their protection from arrest or law enforcement activities. This money was simply deposited into domestic accounts in the name of a fictional person or in corporate vehicles established by Estrada's attorney, and then used for a variety of expenses.<sup>11</sup> Likewise, in the case of the bribery of US Congressman Randall Cunningham, who was a senior legislator with significant control over military expenditures, a military contractor bribed him both by checks to a corporation controlled by Cunningham, but also by agreeing to purchase real estate owned by Cunningham at a vastly inflated price.<sup>12</sup>

43. Proceeds are also generated through extortion schemes. In such schemes, funds are passed from the victim to the PEP. This can be done within the country or elsewhere. Pavel Lazarenko, former Prime Minister of Ukraine, regularly required entities that wished to do business in Ukraine to split equally the profits of the enterprise with him in exchange for his influence in making the business successful. These businesses would transfer a share of ownership to Lazarenko associates or family members, and money would be wired from the victim companies to offshore accounts controlled by Lazarenko.<sup>13</sup>

44. Self-dealing occurs when a PEP has a financial interest in an entity which does business with the state. The PEP is able to use his official position to ensure that the state does business with the entity, thereby enriching the PEP. A US Senate report noted a situation in which one West African PEP was responsible for selling the right to harvest timber from public lands, while at the same time owning the same company

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<sup>10</sup> [39] *United States v. Green, et al*, (2010) court documents. Kickbacks and bribes generally have no legal distinction. In ordinary parlance, a kickback typically refers to the payment of a percentage of a specific contract, while bribery is simply the unrestricted payment of money.

<sup>11</sup> [40] *People of the Philippines v. Estrada* (2007), court decision.

<sup>12</sup> [41] *United States v. Cunningham* (2006), court documents.

<sup>13</sup> [42] *United States v. Lazarenko* (2006), court decision.

that had been awarded those rights.<sup>14</sup> In such situations, money would flow from the affected country's accounts or central bank to accounts owned by the corporation or entity owned or controlled by the PEP.

45. Finally, embezzlement schemes are used in a number of corruption cases. Money flows can occur in a number of ways, using a variety of methods. In the case involving former governor of Plateau state in Nigeria, Joshua Dariye, for example, a grant for environmental contracts was made from the federal government to the State, and the money was deposited into a bank account established by the State. Dariye used his influence to cause the bank to issue a bank draft creditable to an account at a different Nigerian bank that Dariye had established under an alias about ten months previously.<sup>15</sup> In the case involving Sani Abacha, then the President of Nigeria, Abacha directed his national security advisor to create and present false funding requests, which Abacha authorised. Cash "in truckloads" was taken out of the central bank to settle some of these requests. The national security advisor then laundered the proceeds through domestic banks or Nigerian and foreign businessmen to offshore accounts held by family members.<sup>16</sup>

46. Thus, it would appear that all stages of the money laundering process – placement, layering, and integration – are present in the laundering of proceeds regardless of the manner of corruption. The specific methods by which the funds are actually laundered are discussed below.

END OF EXCERPT

### 3.1 Use of Corporate Vehicles and Trusts

BEGINNING OF EXCERPT

47. The project team's review of the case studies showed that every examined case featured the use of corporate vehicles, trusts, or non-profit entities of some type. That this is the case should perhaps not be surprising; corporate vehicles and trusts have long been identified by FATF as posing a risk for money laundering generally, and

<sup>14</sup> [43] Permanent Subcommittee on Investigations (2010), pp. 24-25.

<sup>15</sup> [44] *Federal Republic of Nigeria v. Joshua Chibi Dariye* (2007) (UK) court documents.

<sup>16</sup> [45] Okonjo-Iweala, *The Nigerian Experience* (2007) unpublished World Bank case study.

are addressed in Recommendations 33 and 34.<sup>17</sup> WGTYP [Working Group on Typologies] long ago noted in its 1996-1997 Report on Money Laundering Typologies of the common use of shell corporations, and the advantages they provide in concealing the identity of the beneficial owner and the difficulty for law enforcement to access records.

48. WGTYP issued a report detailing the risks of misuse of corporate vehicles and trusts in October 2006.<sup>18</sup> The intervening ten years changed little. As that report noted, “[o]f particular concern is the ease with which corporate vehicles can be created and dissolved in some jurisdictions, which allows these vehicles to be...misused by those involved in financial crime to conceal the sources of funds and their ownership of the corporate vehicles.” This point was again made more recently in FATF’s 2010 typology, *Money Laundering Using Trust and Company Service Providers*.<sup>19</sup>

49. These typologies, as well as other publically available information, set forth the money laundering risks that corporate vehicles and trusts present, regardless of the predicate crime. Features of corporate vehicles that enhance the risk of money laundering include:

- the ease with which corporate vehicles can be created and dissolved in some jurisdictions;
- that a vehicle can be created as part of a series of multi-jurisdictional structures, in which a corporation in one jurisdiction is owned by one or more other corporations or trusts in other jurisdictions;
- the use of specialised intermediaries and professionals to conceal true ownership;
- the ease in which nominees may be used to disguise ownership, and corporations;
- and other vehicles whose only purpose is to disguise the beneficial owner of the underlying asset.<sup>20</sup>

50. Moreover, each jurisdiction has its own set of requirements regarding identification of the beneficial owner and the circumstances under which that information may be accessed. As discussions within the FATF regarding clarification

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<sup>17</sup> [46] In preparation for the fourth round of mutual evaluations, the FATF has recently started a review of some key components of the Recommendations, including transparency of legal persons and arrangements. In February 2012, the FATF plenary will consider the WGEI [Working Group on Evaluations and Implementation] recommendation on amending the standards related to the transparency of legal persons and arrangements.

<sup>18</sup> [47] FATF (2006).

<sup>19</sup> [48] FATF (2010b).

<sup>20</sup> [49] See, e.g., United States Government Accountability Office (2006).



of the standards related to beneficial ownership have demonstrated, few jurisdictions collect beneficial ownership information at the time of company formation, increasing the challenges of international cooperation. Each of these features has the effect of making it more difficult for financial institutions, regulators, and law enforcement to obtain information that would allow for an accurate understanding of the ownership and control of the assets involved and the purposes for which specific financial transactions are conducted. Some vehicles are even designed to protect against asset confiscation; certain trusts, for example, require the trustee to transfer assets upon receiving notice of a law enforcement or regulatory inquiry.<sup>21</sup>

51. The ease by which an individual can obtain a corporate vehicle is highlighted by J.C. Sharman's recently-published foray into purchasing shell corporations. Sharman, a professor at Griffith University in Brisbane, Australia, noted that of 45 service providers he was able to contact, 17 of them were willing to form the company with only a credit card and mailing address (to receive the documents).<sup>22</sup> Sharman acknowledged that the relatively small sample size of his study "necessitates a degree of modesty about the findings," and that obtaining a bank account for the corporations without divulging an identity would be more difficult. Nevertheless, as he notes, "If one law-abiding individual with a modest budget can establish anonymous companies and bank accounts via the Internet using relatively high-profile corporate service providers, how much simpler is it likely to be for criminals, who are not bound by any of these restrictions, to replicate this feat?"

52. In the corruption context, it is easy to understand why a corrupt PEP may wish to use a corporate vehicle. In some jurisdictions, PEPs are subject to public asset disclosure requirements, rules regarding engaging in outside transactions to prevent self-dealing and conflicts of interest, and a host of other codes of conduct, and ethical prohibitions.<sup>23</sup> Specific investigative bodies and watchdog groups may exist to guard against corruption, and in many countries a robust media is able to publicise missteps by public officials. Some countries have effectively implemented FATF Recommendation 6 [now Recommendation 12], and require financial institutions to conduct enhanced due diligence for those customers who are foreign PEPs. PEPs have their career and reputation at stake if found to be in possession of unexplained wealth. In this environment, corrupt PEPs have a greater need than others to ensure that specific criminal assets cannot be identified with or traced back to them. Corporate

<sup>21</sup> [50] Baker, R.W. (2005), p. 37.

<sup>22</sup> [51] Sharman, J.C. (2010).

<sup>23</sup> [52] Many of these are obligations of member states under the UNCAC. A good description of the available legislative and regulatory schemes employed by some countries is described in the UNODC's UN Anti-corruption Toolkit (2004), found at [updated link: <<http://www.pogar.org/publications/finances/anticor/anticorruptiontoolkit.pdf>>].

vehicles thus provide one of the most effective ways to separate the origin of the illegal funds from the fact that the PEP controls it.

53. One example of this comes from the case of Augusto Pinochet, the former President of Chile. Pinochet was assisted by his US-based bank (and its U.K. branch) in setting up corporate vehicles in order to both hide his assets and shield them from the reach of asset freezing and confiscation or civil recovery orders. Specifically, Pinochet was able to set up offshore shell corporations and a trust in 1996 and 1998, even after a Spanish magistrate had filed a detailed indictment against Pinochet for crimes against humanity and issued world-wide freezing orders.<sup>24</sup> These corporations, established in jurisdictions that at the time had weak AML controls, were listed as the nominal owners of the US bank accounts and other investment vehicles that benefited Pinochet and his family. The bank's KYC documentation listed only the corporations, not Pinochet, as the owners of the accounts, despite the fact that the bank knew that Pinochet was the beneficial owner (since the bank itself had set up the corporations). The bank has since been convicted of AML-related criminal charges.

54. According to the case study of Vladimiro Montesinos, Peruvian President Fujimori's security advisor, he used shell corporations very effectively to disguise and move money illegally obtained through defence contracts with the Peruvian government.<sup>25</sup> Such a scheme, involving several corporate vehicles in a number of jurisdictions with each vehicle holding bank accounts in yet other jurisdictions, is designed to frustrate any financial institution, regulator or government investigator attempting to unravel the scheme.

END OF EXCERPT

### 3.2 Use of Gatekeepers

BEGINNING OF EXCERPT

55. Gatekeepers were significantly represented in the cases within the project team inventory. "Gatekeepers are, essentially, individuals that 'protect the gates to the financial system' through which potential users of the system, including launderers, must pass in order to be successful."<sup>26</sup> The issue of gatekeepers has been addressed

<sup>24</sup> [53] Permanent Subcommittee on Investigations (2004).

<sup>25</sup> [54] ADB/OECD (2007b); UNODC and World Bank (2007).

<sup>26</sup> [55] FATF (2010c).

by FATF on several occasions, including WGTYP's 2003- 2004 Report, which concluded:

Increasingly, money launderers seek out the advice or services of specialised professionals to help facilitate their financial operations. This trend toward the involvement of various legal and financial experts, or gatekeepers, in money laundering schemes has been documented previously by the FATF and appears to continue today. The work undertaken during this year's exercise confirmed and expanded the FATF's understanding of specific characteristics of this sector and what makes it vulnerable to money laundering. The most significant cases each involve schemes of notable sophistication, which were possible only as a result of the assistance of skilled professionals to set up corporate structures to disguise the source and ownership of the money.

56. In 2010, FATF published its Global Money Laundering and Terrorist Financing Threat Assessment, which described gatekeepers as a "common element" in complex money laundering schemes. The report noted that gatekeepers' skills are important in creating legal structures that could be used to launder money and for their ability to manage and perform transactions efficiently and to avoid detection. Recommendation 12 [now Recommendation 22] acknowledges the role that such gatekeepers can play by recommending that such individuals engage in due diligence and record keeping when engaged in certain activities.

57. The review of the cases illustrates the variety of ways in which gatekeepers, in particular lawyers, are used to launder the proceeds of corruption. They have been used to create corporate vehicles, open bank accounts, transfer proceeds, purchase property, courier cash, and take other means to bypass AML controls. In addition, lawyers have subsequently used rules of attorney-client privilege to shield the identity of corrupt PEPs.

58. West African PEPs: In four separate case studies of West African PEPs and their families, the US Senate discovered that lawyers were used to create corporate vehicles, open bank accounts and purchase property with the express purpose of bypassing AML controls set up to screen for PEPs.<sup>27</sup> For example, the son of the President of one West African nation, who himself was a minister within the government, wished to purchase real estate and aircraft within the United States. To do so, a lawyer for the PEP opened bank accounts there. However, because of US banking rules requiring enhanced level of due diligence for funds moving through those accounts, several US banks closed the accounts on the belief that they were being used to conduct

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<sup>27</sup> [56] Permanent Subcommittee on Investigations (2010).

suspicious transactions. In response, the lawyers for the PEP would deposit incoming funds into attorney-client or law office accounts, and then transfer the money into newly-created accounts for the PEP. Due to the fact that the lawyer's accounts were not subject to the same enhanced due diligence as the PEP, the lawyer was able to circumvent the enhanced AML/CFT measures. Ultimately, at least two banks were able to identify the fact that the attorney's accounts were being utilised in this manner and closed the attorney accounts, but not before hundreds of thousands of dollars had passed through.

59. Duvalier case: Haitian government assets diverted by Jean-Claude Duvalier were likewise disguised by the use of lawyers as intermediaries, who would hold accounts for the Duvalier family. This, according to the UK court that examined the matter, had the added advantage of the use of professional secrecy to avoid identifying the client.<sup>28</sup> The court opinion identified numerous accounts held by law firms for Duvalier and his family, both in the UK and in Jersey. The use of professional secrecy was used to attempt to prevent an inquiry into the nature of the funds.

60. Chiluba case: Similarly, in a civil recovery suit instituted in the UK against the former President of Zambia, the court, in its factual findings, described in great detail the use of certain lawyers and law firms to distribute and disguise money embezzled from the coffers of the Zambian government.<sup>29</sup> Special corporate vehicles had been set up, purportedly for use by the country's security services, and government funds were transferred to accounts held by those entities. Thereafter, millions of dollars were transferred to the client accounts of certain law firms, from which the lawyers would then make certain disbursements upon instructions from complicit PEPs. These disbursements were to other accounts located both in Zambia and in other countries, as well as payments for personal expenses and asset acquisitions for the government officials and their families. As the Court noted in its opinion, "There is no reason for his client account to be used for any genuine currency transactions. This is ... money which has been traced back to [the Zambian Ministry of Finance]. It is a classic example of washing money through [the attorney's] client account to hide its origins and to clothe it with an aura of respectability."

61. The court also noted an instance in which the PEP's lawyer withdrew GBP 30 000 – an amount that vastly exceeded the President's annual salary – and delivered it personally to the President. Moving the money through the lawyer's accounts disguised the fact that the money originated from government accounts, and further hampered the ability to trace the proceeds. The court noted that the lawyers involved did not make any efforts to determine the source or the purpose of the money: "Yet [the lawyer] made no enquiry as to how the President could simply take such a large

<sup>28</sup> [57] *Republic of Haiti v. Duvalier*, 1990 UK.

<sup>29</sup> [58] *Attorney General of Zambia v. Meer Cares, et al*, UK court opinion (2007).

amount of money. An honest solicitor would not participate in such a transaction without a full understanding of its nature so that he could be satisfied it was lawful. [The lawyer] did not so satisfy himself because he was unwilling to ask the question because he was afraid of the answer.” Additionally, the lawyers involved formed foreign shell corporations, which were then used to purchase properties with government money for the benefit of corrupt officials.

END OF EXCERPT

### 3.3 Use of Domestic Financial Institutions

BEGINNING OF EXCERPT

62. Much of the focus on PEPs to date has been to ensure that foreign PEPs are subject to enhanced due diligence regarding the source of funds deposited into financial institutions – in other words, measures to prevent corrupt PEPs from laundering their proceeds in foreign bank accounts. For example, the Third EU Directive requires enhanced due diligence only for foreign PEPs. The UNCAC, however, does not distinguish between foreign PEPs and those prominent political figures within the institution’s own country. The World Bank policy paper on PEPs notes that many financial institutions do not distinguish between foreign and domestic PEPs.<sup>30</sup>

63. The Interpretive Note to Recommendation 6 encourages jurisdictions to extend its EDD requirements to domestic PEPs as well. Recently the FATF has discussed the degree to which domestic PEPs should be subject to enhanced due diligence, and in addressing the issue, has recommended that domestic PEPs continue to be considered on a risk-based approach, and that foreign PEPs continue to receive enhanced due diligence.<sup>31</sup>

64. Some typology exercises the project team reviewed have concluded that domestic PEPs may present a significant risk for corruption-related money laundering. Professor Jason Sharman, in summarizing the ADB/OECD paper on PEPs, characterised the notion that domestic PEPs do not present a threat of money laundering as a “myth.”<sup>32</sup> The project team’s analysis of the case study inventory found that PEPs are not only using foreign financial institutions to transfer and hide

<sup>30</sup> [59] Greenberg, T.S. et al. (2009).

<sup>31</sup> [60] This is the situation as at the publication of this report (July 2011).

<sup>32</sup> [61] Sharman, J.C., (2009).

the proceeds of corruption. PEPs are also using domestic financial institutions to launder funds.

65. Perhaps the most obvious example of this involves President Joseph Estrada of the Philippines, who was convicted in his country of the crime of plunder. The court's ruling in that case noted that a significant portion of the money that Estrada collected as a result of kickbacks from illegal gambling and tobacco excise taxes ultimately ended up at a bank account in the Philippines in the name of an alias, Jose Velarde. The court noted that Estrada used the account and would simply sign Velarde's name to deposit slips, oftentimes in the presence of bank personnel. Money that went through that account was used for various asset purchases, including real estate for the benefit of Estrada.<sup>33</sup>

66. The US Senate, in its 2010 investigation of the use of US banks to launder corruption proceeds, described in two different reports the banking and asset purchase activities of the President of a West African oil producing country as well as that of his son, who was also a high-level government official. The son, for example, in purchasing in cash a house in the United States for USD 30 million, wire transferred money, in six different USD 6 million tranches, from a personal bank account he held in his own country, through an account in France and then to the United States. The son had an official government monthly salary of approximately USD 6 000.

67. The case involving assets stolen by Joshua Chibi Dariye also highlight the use of domestic accounts in at least the initial stages of a more complex scheme. Dariye, the Governor of Plateau State in the Federal Republic of Nigeria from May 1999 through May 2007, embezzled money belonging to the state in several ways. Checks issued from the central bank of Nigeria to Plateau State for ecological works were received by Dariye and, rather than being deposited into a government account, were instead diverted to an account in Nigeria Dariye had established using an alias. The money was then transferred to accounts held in Dariye's own name in the UK. Likewise, Dariye purchased real estate by diverting money destined for a Plateau State account into an account in Nigeria in the name of a corporation he controlled. That corporation, in turn, transferred money to UK accounts in the corporation's name to effectuate the real estate purchase.<sup>34</sup>

68. Raul Salinas, the brother of the President of Mexico, likewise was able to move money out of his home country by using the Mexican branch of a US-based international bank. A US-based bank official introduced Salinas' then-fiancée to a bank official at the Mexico City branch of the bank. The fiancée, using an alias, would

<sup>33</sup> [62] *People of the Philippines v. Joseph Estrada* court opinion.

<sup>34</sup> [63] *Federal Republic of Nigeria v. Joshua Chibi Dariye* (2007) (UK).

deliver cashier's checks to the branch, where they were converted to dollars and wired to US accounts.<sup>35</sup>

69. PEPs need accounts in their own country in which to fund their lifestyles, and there have been examples in which the PEP, after secreting money overseas, then moved the money back to his home country. The US Senate, in its 2004 investigation of corruption-related money laundering, provided one such example. Augusto Pinochet of Chile, notwithstanding a modest official government salary, was able to secret millions of dollars in UK and US accounts, often through the use of aliases and family members. In 1998 a Spanish investigating magistrate instituted worldwide asset freeze orders as a result of an investigation into Pinochet's role in human rights abuses and other crimes and was subsequently facing charges in Spain and Chile. Pinochet was able however, to purchase USD 1.9 million in cashier's checks (in USD 50 000 increments) from his account in the US, which he was thus able to cash using banks in Chile.<sup>36</sup>

70. That corrupt PEPs would seek to move money outside of their home jurisdiction is at the root of Recommendation 6, requiring enhanced due diligence for foreign PEPs. An examination of the corruption case studies revealed that in nearly every case foreign bank accounts were being used in part of the scheme. Beginning with one of the earliest cases, Marcos of the Philippines, through the significant and egregious activity of Sani Abacha and a number of Nigerian governors, and most recently with the US Senate's study of three West African heads of state, corrupt PEPs nearly universally attempt to move their money outside of their home country. This money is typically moved from developing countries to financial institutions in developed countries or those with a stable climate for investment.

71. Of course, corruption is not restricted to developing countries. The project team analyzed the Nino Rovelli judicial corruption matter, for example.<sup>37</sup> There, approximately USD 575 million was paid out to individuals as a result of bribes paid to judicial officials in Italy. The money ultimately was moved and disguised in a series of financial transactions involving accounts and corporate vehicles in the United States, British Virgin Islands, Singapore, Cook Islands and Costa Rica. Likewise, the developing world's financial systems may well be used to hide money. In the Titan Corporation bribery case for example, bribes from a US corporation to the President of Benin, intended to secure government contracts in telecommunications, was moved, in cash, directly to Benin.<sup>38</sup>

<sup>35</sup> [64] Permanent Subcommittee on Investigations (1999).

<sup>36</sup> [65] Permanent Subcommittee on Investigations (2004).

<sup>37</sup> [66] *United States v. Proceeds of Crime Transferred to Certain Domestic Financial Accounts* (2007), court filings.

<sup>38</sup> [67] *United States v. Titan Corporation (US)* (2005), court filings.

72. The reason for this preference is obvious. Foreign accounts hold the advantage of being harder to investigate for the victim country, are perceived of as more stable and safer, and are more easily accessed than accounts held in the PEPs home country. Moreover, a PEP can “stack” foreign jurisdictions: a bank account in one country could be owned by a corporation in another jurisdiction, which is in turn owned by a trust in a third jurisdiction. Each additional country multiplies the complexity of the investigation, reduces the chances of a successful result, and extends the time needed to complete the investigation.

END OF EXCERPT

### 3.4 Use of Nominees

BEGINNING OF EXCERPT

73. The use of associates or nominees – trusted associates or family members, but not necessarily the lawyers and accountants described in the gatekeepers section – to assist the PEP in disguising and moving the proceeds of corruption was common in the inventory of cases. FATF has documented the use of such nominees previously. The WGTYP annual report for 2003-2004 noted at paragraph 78:

PEPs, given the often high visibility of their office both inside and outside their country, very frequently use middlemen or other intermediaries to conduct financial business on their behalf. It is not unusual therefore for close associates, friends and family of a PEP to conduct individual transactions or else hold or move assets in their own name on behalf the PEP. This use of middlemen is not necessarily an indicator by itself of illegal activity, as frequently such intermediaries are also used when the business or proceeds of the PEP are entirely legitimate. In any case, however, the use of middlemen to shelter or insulate the PEP from unwanted attention can also serve as an obstacle to customer due diligence that should be performed for every customer. A further obstacle may be involved when the person acting on behalf of the PEP or the PEP him or herself has some sort of special status such as, for example, diplomatic immunity.

74. A typical use of nominees can be found in the case of Arnaldo Aleman. Aleman was able to siphon government funds through a non-profit institution known as the Nicaraguan Democratic Foundation (FDN), an entity incorporated by Aleman’s wife in Panama. In addition, Aleman and his wife set up both front companies and non-



profit organisations to funnel money through. Lastly, Aleman was able to defraud the government in the sale of telecommunications frequency to a private entity, using companies set up by advisors to Aleman. Aleman was also assisted in his efforts to steal and subsequently move money through the active participation of Byron Jerez, the country's tax commissioner at the time.<sup>39</sup>

75. The scheme set up by a high level PEP in a Central American country likewise depended on the assistance of both family members as well as other associates to succeed. The PEP would divert money that was intended to be paid to the country's treasury through a series of financial transactions, which would then ultimately end up in foreign bank accounts in the name of the PEP's former wife and daughter.<sup>40</sup>

END OF EXCERPT

### 3.5 Use of Cash

BEGINNING OF EXCERPT

76. The use of cash, and its placement into the financial system, has long been identified as a method for the laundering of proceeds of crime. Indeed, when the FATF 40 Recommendations were first issued in 1990, the focus of many of its preventative measures was on detecting money laundering at the cash proceeds stage. The anonymous nature of cash, with its lack of paper trail, is attractive and may outweigh other negatives. Some of the predicate crimes, such as drug trafficking, are historically cash businesses. Indeed, even for crimes that do not generate cash requiring placement into the financial system, WGTYP has noted (Report on Money Laundering Typologies, 2000-2001) some laundering schemes in which the proceeds are converted back to cash in order to break the paper trail.

77. While smaller-scale, endemic corruption (in which money is provided to lower- or mid-level government officials in order to act or refrain from acting in their official capacity), would be expected to generate cash in need of placement, the grand corruption cases would not be expected to have significant amounts of cash. A cash payment to a PEP would break the chain of bank records, of course, but it would require the PEP to run the gauntlet of AML/CFT controls designed to combat placement of illegally-derived cash into the system. This would include the possibility that the PEP's transactions (as well as those for his family and close associates) are subject to enhanced due diligence in accordance with Recommendation 6. In each case

<sup>39</sup> [68] *United States v. \$125,938 (US)* (2008) court filings.

<sup>40</sup> [69] *United States v. Alfonso Portillo (US)* (2009) court documents.

in which the PEP receives the cash, he must engage in a calculus to determine whether the risks associated with placement – including the possibility of EDD as a result of his PEP status – outweigh the benefits of having broken the chain. It appears that in a significant number of cases, the corrupt PEP wants the cash and, moreover, is able to place the cash without attracting undue attention.

78. The US Senate's investigation of corruption-related money laundering identified the President of one oil rich West African country, for which a US bank accepted nearly USD 13 million in cash deposits over a three-year period into accounts controlled by the President or his wife. The report noted that some of these deposits were for a million dollars at a time, and the currency was in shrink-wrap packaging. The report could identify no legitimate source for such currency. This same bank also provided USD 1.9 million in cashier checks to a PEP from a South American country, using the maiden name of the wife of the PEP as the payee. These cashiers' checks were ultimately cashed in the PEP's home country. The bank involved was fined and criminally prosecuted for these violations and ultimately was closed as a result.<sup>41</sup>

79. The Zambian asset recovery lawsuit, noted above, also highlights the use of cash. As part of the scheme, the president of Zambia directed his UK-based lawyer to withdraw GBP 30 000 in cash from accounts containing diverted government money and deliver it to him personally. There were also other significant cash payments, including a USD 250 000 payment made from a diverted account to the Zambian Ambassador to the United States, which he then took in a suitcase to Switzerland and gave to the head of the Zambian security service, and hundreds of thousands of dollars in cash used to purchase property in the UK and elsewhere. The court found that there was no legitimate purpose for the large cash withdrawals.<sup>42</sup>

80. Other case studies have shown the presence of significant amounts of unexplained cash. Diepreye Alamiyeseigha, for example, was found to have over GBP 1 000 000 in his apartment in the UK at the time of his arrest, notwithstanding the fact that as governor of Bayelsa State in Nigeria, his salary was a fraction of that. Another governor of a Nigerian state around that time, Joshua Chibi Dariye, previously discussed, was found to have deposited into his UK accounts in excess of GBP 480 000 during a four and a half year period. According to a US Senate report on the matter, immediately after Sani Abacha's death in 1998, his wife was stopped at a Lagos airport with 38 suitcases full of cash, and his son was found with USD 100 million in cash. According to the World Bank study he was able to place significant amounts of cash in the financial system by using associates. Lastly, Montesinos used cash couriers to transfer funds from Switzerland to Mexico and Bolivia.

<sup>41</sup> [70] Permanent Subcommittee on Investigations (2004).

<sup>42</sup> [71] *Attorney General of Zambia v. Meer Cares, et al*, (UK)(2007) court opinion.

81. PEPs have an advantage not usually available to the general public: the use (and abuse) of the so-called “diplomatic pouch.” Intended to protect free communication between diplomats and their foreign missions, a diplomatic bag is protected from search or seizure by the *1961 Convention on Diplomatic Relations*.<sup>43</sup> A diplomatic bag may only be used for official materials and, while the Convention protects it from search, it does not relieve the carrier of adherence to the laws of the host nation, including cross-border currency reporting requirements.

82. Such was the situation that the US Senate uncovered in its report on the financial affairs of one West African PEP. His daughter, who was in graduate school in the United States, asked her US bank to count certain cash she had stored in her safe deposit box. The bank found USD 1 million in cash, in USD 100 bills, wrapped in plastic. When asked about the source of the money, the daughter replied that her father, the PEP, provided her the cash when he came into the United States, and that he often brought cash into the United States. The PEP had never declared his transport of the cash, as he was required to do by US law.<sup>44</sup>

END OF EXCERPT

## 4. INTERNATIONAL STANDARDS FOR PREVENTION AND CRIMINALIZATION OF MONEY LAUNDERING

### 4.1 UNCAC

As discussed in previous chapters, UNCAC is the most extensive and most widely ratified international convention addressing corruption. In addition to prohibiting bribery and other forms of corruption, the drafters of UNCAC recognized that effective anti-money laundering strategies are an important factor in preventing and detecting large-scale corruption. Like other forms of corruption, the transnational nature of money laundering necessitates international cooperation and consistent standards in anti-money laundering efforts. UNCAC therefore addresses money laundering in both Chapter II (Preventative Measures) and in Chapter III (Criminalization and Law Enforcement). Article 14 sets out standards for State Parties to follow in developing anti-money laundering measures, while Article 23 of UNCAC criminalizes the laundering of the proceeds of corruption. A more comprehensive overview of the anti-money laundering provisions of UNCAC can be found in Carr and Goldby’s paper, “The UN Anti-Corruption Convention and Money Laundering.”<sup>45</sup>

<sup>43</sup> [72] [http://untreaty.un.org/ilc/texts/instruments/english/conventions/9\\_1\\_1961.pdf](http://untreaty.un.org/ilc/texts/instruments/english/conventions/9_1_1961.pdf).

<sup>44</sup> [73] Permanent Subcommittee on Investigations (2010).

<sup>45</sup> Indira Carr & Miriam Goldby, “The United Nations Anti-Corruption Convention and Money Laundering” (2009) Working Paper, online: <<http://ssrn.com/abstract=1409628>>.

#### 4.1.1 Article 23 – Criminalization of Money Laundering

Article 23 is ambitious in scope. It criminalizes the actions of those involved in money laundering in a number of different capacities. Unlike some of the other criminalization provisions of UNCAC, the criminalization of money laundering under Article 23 is mandatory, although the provision may be adapted if necessary to conform to the “fundamental principles” of the State Party’s domestic law. Article 23 provides as follows:

##### Article 23. Laundering of proceeds of crime

1. Each State Party shall adopt, in accordance with fundamental principles of its domestic law, such legislative and other measures as may be necessary to establish as criminal offences, when committed intentionally:
  - (a)
    - (i) The conversion or transfer of property, knowing that such property is the proceeds of crime, for the purpose of concealing or disguising the illicit origin of the property or of helping any person who is involved in the commission of the predicate offence to evade the legal consequences of his or her action;
    - (ii) The concealment or disguise of the true nature, source, location, disposition, movement or ownership of or rights with respect to property, knowing that such property is the proceeds of crime;
  - (b) Subject to the basic concepts of its legal system:
    - (i) The acquisition, possession or use of property, knowing, at the time of receipt, that such property is the proceeds of crime;
    - (ii) Participation in, association with or conspiracy to commit, attempts to commit and aiding, abetting, facilitating and counselling the commission of any of the offences established in accordance with this article.

The following excerpt from the *Legislative Guide for the Implementation of the United Nations Convention against Corruption* provides guidance on Article 23 to legislators tasked with incorporating Article 23 into a state’s domestic legislation:

## BEGINNING OF EXCERPT

**(e) Money-laundering**

220. Article 23 requires the establishment of offences related to the laundering of proceeds of crime, in accordance with fundamental principles of domestic law. The related Convention articles addressing measures aimed at the prevention of money-laundering were discussed in the previous chapter.

221. In the context of globalization, criminals take advantage of easier capital movement, advances in technology and increases in the mobility of people and commodities, as well as the significant diversity of legal provisions in various jurisdictions. As a result, assets can be transferred instantly from place to place through both formal and informal channels. Through exploitation of existing legal asymmetries, funds may appear finally as legitimate assets available in any part of the world.

222. Confronting corruption effectively requires measures aimed at eliminating the financial or other benefits that motivate public officials to act improperly. Beyond this, combating money-laundering also helps to preserve the integrity of financial institutions, both formal and informal, and to protect the smooth operation of the international financial system as a whole.

223. As noted in the previous chapter, this goal can only be achieved through international and cooperative efforts. It is essential that States and regions try to make their approaches, standards and legal systems related to this offence compatible, so that they can cooperate with one another in controlling the international laundering of criminal proceeds. Jurisdictions with weak or no control mechanisms render the work of money launderers easier. Thus, the Convention against Corruption seeks to provide a minimum standard for all States.

224. The Convention against Corruption specifically recognizes the link between corrupt practices and money-laundering and builds on earlier and parallel national, regional and international initiatives in that regard. Those initiatives addressed the issue through a combination of repressive and preventive measures and the Convention follows the same pattern (see also chap. II of the present guide).

225. One of the most important of the previous initiatives related to the Organized Crime Convention, which mandated the establishment of the offence of money-laundering for additional predicate offences, including corruption of public officials, and encouraged States to widen the range of predicate offences beyond the minimum requirements.

226. "Predicate offence" is defined as "any offence as a result of which proceeds have been generated that may become the subject of an offence as defined in article 23 of this Convention" (art. 2, subpara. (h)).

227. As a result of all these initiatives, many States already have money laundering laws. Nevertheless, such laws may be limited in scope and may not cover a wide range of predicate offences. Article 23 requires that the list of predicate offences include the widest possible range and at a minimum the offences established in accordance with the Convention against Corruption.

228. The provisions of the Convention against Corruption addressing the seizure, freezing and confiscation of proceeds (see art. 31) and the recovery of assets (see chap. V of the Convention and, especially, art. 57) include important related measures. States should review the provisions they already have in place to counter money-laundering in order to ensure compliance with these articles and those dealing with international cooperation (chap. IV). States undertaking such a review may wish to use the opportunity to implement the obligations they assume under other regional or international instruments and initiatives currently in place.

229. Article 23 requires that States parties establish the four offences related to money-laundering described in the following paragraphs:

**(f) Conversion or transfer of proceeds of crime**

230. The first offence is the conversion or transfer of property, knowing that such property is the proceeds of crime, for the purpose of concealing or disguising the illicit origin of the property or of helping any person who is involved in the commission of the predicate offence to evade the legal consequences of his or her action (art. 23, para. 1 (a) (i)).

231. The term "conversion or transfer" includes instances in which financial assets are converted from one form or type to another, for example, by using illicitly generated cash to purchase precious metals or real estate or the sale of illicitly acquired real estate, as well as instances in which the same assets are moved from one place or jurisdiction to another or from one bank account to another.

232. The term "proceeds of crime" means "any property derived from or obtained, directly or indirectly, through the commission of an offence" (art. 2, subpara. (e)).

233. With respect to the mental or subjective elements required, the conversion or transfer must be intentional, the accused must have knowledge at the time of conversion or transfer that the assets are criminal proceeds and the act or acts must be done for the purpose of either concealing or disguising their criminal origin, for

example by helping to prevent their discovery, or helping a person evade criminal liability for the crime that generated the proceeds.

234. As noted in article 28 of the Convention against Corruption, knowledge, intent or purpose may be inferred from objective factual circumstances.

**(g) Concealment or disguise of proceeds of crime**

235. The second money-laundering offence is the concealment or disguise of the nature, source, location, disposition, movement or ownership of or rights with respect to property, knowing that such property is the proceeds of crime (art. 23, para. 1 (a) (ii)).

236. The elements of this offence are quite broad, including the concealment or disguise of almost any aspect of or information about property.

237. Here, with respect to the mental or subjective elements required, the concealment or disguise must be intentional and the accused must have knowledge that the property constitutes the proceeds of crime at the time of the act. This mental state is less stringent than for the offence set forth in article 23, subparagraph 1 (a) (i). Accordingly, drafters should not require proof that the purpose of the concealment or disguise is to frustrate the tracing of the asset or to conceal its true origin.

238. The next two offences related to money-laundering are mandatory, subject to the basic concepts of the legal system of each State party.

**(h) Acquisition, possession or use of proceeds of crime**

239. The third offence is the acquisition, possession or use of proceeds of crime knowing, at the time of receipt, that such property is the proceeds of crime (art. 23, para. 1 (b) (i)).

240. This is the mirror image of the offences under article 23, paragraph 1 (a)(i) and (ii), in that, while those provisions impose liability on the providers of illicit proceeds, this paragraph imposes liability on recipients who acquire, possess or use the property.

241. The mental or subjective elements are the same as for the offence under article 23, paragraph 1 (a) (ii): there must be intent to acquire, possess or use, and the accused must have knowledge, at the time this occurred, that the property was the proceeds of crime. No particular purpose for the acts is required.

**(i) Participation in, association with or conspiracy to commit, attempts to commit and aiding, abetting, facilitating and counselling the commission of any of the foregoing offences**

242. The fourth set of offences involves the participation in, association with or conspiracy to commit, attempts to commit and aiding, abetting, facilitating and counselling the commission of any of the offences mandated by the article (art. 23, para. 1 (b) (ii)).

243. These terms are not defined in the Convention against Corruption, allowing for certain flexibility in domestic legislation. States parties should refer to the manner in which such ancillary offences are otherwise structured in their domestic system and ensure that they apply to the other offences established pursuant to article 23.

[Note – see Chapter 3, Sections 3 and 4, for a discussion on inchoate crimes and secondary liability.]

244. The knowledge, intent or purpose, as required for these offences, may be inferred from objective factual circumstances (art. 28). National drafters could see that their evidentiary provisions enable such inference with respect to the mental state, rather than requiring direct evidence, such as a confession, before the mental state is deemed proven.

245. Under article 23, States parties must apply these offences to proceeds generated by “the widest range of predicate offences” (art. 23, para. 2 (a)).

246. At a minimum, these must include a “comprehensive range of criminal offences established in accordance with this Convention” (art. 23, para. 2 (b)). For this purpose, “predicate offences shall include offences committed both within and outside the jurisdiction of the State party in question. However, offences committed outside the jurisdiction of a State party shall constitute predicate offences only when the relevant conduct is a criminal offence under the domestic law of the State where it is committed and would be a criminal offence under the domestic law of the State party implementing or applying this article had it been committed there” (art. 23, para. 2 (c)). So, dual criminality is necessary for offences committed in a different national jurisdiction to be considered as predicate offences.

247. Many States already have laws on money-laundering, but there are many variations in the definition of predicate offences. Some States limit the predicate offences to trafficking in drugs or to trafficking in drugs and a few other crimes. Other States have an exhaustive list of predicate offences set forth in their legislation. Still other States define predicate offences generically as including all crimes, or all serious crimes, or all crimes subject to a defined penalty threshold.



248. An interpretative note for the Convention against Corruption states that “money-laundering offences established in accordance with this article are understood to be independent and autonomous offences and that a prior conviction for the predicate offence is not necessary to establish the illicit nature or origin of the assets laundered. The illicit nature or origin of the assets and, in accordance with article 28, any knowledge, intent or purpose may be established during the course of the money-laundering prosecution and may be inferred from objective factual circumstances” (A/58/422/Add.1, para. 32).

249. The constitutions or fundamental legal principles of some States do not permit the prosecution and punishment of an offender for both the predicate offence and the laundering of proceeds from that offence. The Convention acknowledges this issue and, only in such cases, allows for the non-application of the money-laundering offences to those who committed the predicate offence (art. 23, para. 2 (e)).<sup>46</sup>

END OF EXCERPT

#### 4.1.2 Article 14 – Measures to Prevent Money-Laundering

As mentioned above, in addition to mandating the criminalization of money laundering, UNCAC also requires state parties to take measures to establish a regulatory regime intended to prevent money laundering. The relevant article is Article 14, which is reproduced below:

##### Article 14. Measures to prevent money-laundering

1. Each State Party shall:
  - (a) Institute a comprehensive domestic regulatory and supervisory regime for banks and non-bank financial institutions, including natural or legal persons that provide formal or informal services for the transmission of money or value and, where appropriate, other bodies particularly susceptible to money-laundering, within its competence, in order to deter and detect all forms of money-laundering, which regime shall emphasize requirements for customer and, where appropriate, beneficial owner identification, record-keeping and the reporting of suspicious transactions;

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<sup>46</sup> United Nations Office on Drugs and Crime, *Legislative Guide for the Implementation of the United Nations Convention against Corruption* [UN Legislative Guide (2012)], 2nd ed (New York: United Nations, 2012) at 46–74, paras 220-249, online: <[https://www.unodc.org/documents/treaties/UNCAC/Publications/LegislativeGuide/UNCAC\\_Legislative\\_Guide\\_E.pdf](https://www.unodc.org/documents/treaties/UNCAC/Publications/LegislativeGuide/UNCAC_Legislative_Guide_E.pdf)>. Reprinted with the permission of the United Nations.

- (b) Without prejudice to article 46 of this Convention, ensure that administrative, regulatory, law enforcement and other authorities dedicated to combating money-laundering (including, where appropriate under domestic law, judicial authorities) have the ability to cooperate and exchange information at the national and international levels within the conditions prescribed by its domestic law and, to that end, shall consider the establishment of a financial intelligence unit to serve as a national centre for the collection, analysis and dissemination of information regarding potential money-laundering.
2. States Parties shall consider implementing feasible measures to detect and monitor the movement of cash and appropriate negotiable instruments across their borders, subject to safeguards to ensure proper use of information and without impeding in any way the movement of legitimate capital. Such measures may include a requirement that individuals and businesses report the cross-border transfer of substantial quantities of cash and appropriate negotiable instruments.
3. States Parties shall consider implementing appropriate and feasible measures to require financial institutions, including money remitters:
  - (a) To include on forms for the electronic transfer of funds and related messages accurate and meaningful information on the originator;
  - (b) To maintain such information throughout the payment chain; and
  - (c) To apply enhanced scrutiny to transfers of funds that do not contain complete information on the originator.
4. In establishing a domestic regulatory and supervisory regime under the terms of this article, and without prejudice to any other article of this Convention, States Parties are called upon to use as a guideline the relevant initiatives of regional, interregional and multilateral organizations against money-laundering.
5. States Parties shall endeavour to develop and promote global, regional, subregional and bilateral cooperation among judicial, law enforcement and financial regulatory authorities in order to combat money-laundering.

Carr and Goldby note that Article 14(1) requires states to implement a regulatory and supervisory regime that monitors both formal and informal methods of transferring money in order to combat money laundering.<sup>47</sup> They state that “[t]he system known as *Hawala* (in India) or *Fie Ch’ieu* (in China) is typically used by migrant workers to transfer small amounts of money to relatives in villages lacking bank accounts or access to banks, but can also be

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<sup>47</sup> Carr & Goldby (2009).

abused by criminals.”<sup>48</sup> Although Carr and Goldby welcome this inclusion of informal networks of money transfer into supervisory regimes, they argue that “much research still needs to be done in order to design an effective regime for the regulation and supervision of such informal networks.”<sup>49</sup>

Article 14 of UNCAC also requires states to develop comprehensive anti-money laundering regimes. Although not expressly mandated, there is a strong suggestion by UNCAC that states look to international standard setting bodies, such as the FATF, when designing anti-money laundering frameworks. Therefore, although the FATF recommendations are not themselves binding international law, in addition to their independent ability to set standards through peer pressure, they are given some degree of legal recognition under UNCAC.

The following excerpt from the UNCAC *Legislative Guide* summarizes and explains the various mandated and recommended actions that, pursuant to Article 14, State Parties are to follow:

BEGINNING OF EXCERPT

**Summary of Main Requirements**

138. Article 14 contains two mandatory requirements:

- (a) To establish a comprehensive domestic regulatory and supervisory regime to deter money-laundering (para. 1 (a));
- (b) To ensure that agencies involved in combating money-laundering have the ability to cooperate and exchange information at the national and international levels (para. 1 (b)).

139. In addition, pursuant to article 14 States must consider:

- (a) Establishing an FIU (para. 1 (b));
- (b) Implementing measures to monitor cash movements across their borders (para. 2);
- (c) Implementing measures to require financial institutions to collect information on originators of electronic fund transfers, maintain information on the entire payment chain and scrutinize fund transfers with incomplete information on the originator (para. 3);
- (d) Developing and promoting global, regional and bilateral cooperation among relevant agencies to combat money-laundering (para. 5).

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<sup>48</sup> *Ibid* at 8.

<sup>49</sup> *Ibid* at 8-9.

**Mandatory requirements: obligation to take legislative or other measures****(a) Regulatory and supervisory regime**

140. Article 14, paragraph 1 (a), requires that States parties establish a regulatory and supervisory regime within their competence in order to prevent and detect money-laundering activities. This regime must be comprehensive, but the precise nature and particular elements of the regime are left to States, provided that they require, at a minimum, banks and non-bank financial institutions to ensure:

- (a) Effective customer identification;
- (b) Accurate record-keeping;
- (c) A mechanism for the reporting of suspicious transactions.

141. The requirements extend to banks, non-bank financial institutions (e.g. insurance companies and securities firms) and, where appropriate, other bodies that are especially susceptible to money-laundering (art. 14, para. 1 (a)). The interpretative notes add that other bodies may be understood to include intermediaries, which in some jurisdictions may include stockbroking firms, other securities dealers, currency exchange bureaux or currency brokers (A/58/422/Add.1, para. 18). An addition to the equivalent provisions in the Organized Crime Convention is that financial institutions include “natural or legal persons that provide formal or informal services for the transmission of money or value” (art. 14, para. 1 (a)). This is a reference to concerns about both formal remitters and informal value-transfer systems, such as the *hawala* networks that originated in South Asia and have become global in recent decades. These channels offer valuable services to expatriates and their families, but are also vulnerable to abuse by criminals, including corrupt public officials.

142. Thus, this regime should apply not only to banking institutions, but also to areas of commerce where high turnover and large volumes make money-laundering likely. Previous experience shows that money-laundering activities have taken place in the real estate sector and in the trade of commodities, such as gold, precious stones and tobacco.

143. In many forums, the list of institutions is being expanded beyond financial institutions to include businesses and professions related to real estate and commodities. For example, recommendation 12 of the FATF Forty Recommendations extends, when certain conditions are met, the requirements of customer due diligence and record-keeping to casinos, real estate agents, dealers in precious metals and stones, lawyers, notaries, other independent legal professionals and accountants and trust and company service providers. Similar requirements are set forth in article 1 of Directive 2005/60/EC adopted by the European Parliament and the Council of the European Union on 26 October 2005.

144. More recently, increased attention has been focused on money service businesses and informal value-transfer systems, such as *hawala* and *hundi*. In a growing number of jurisdictions, these are also subject to a regulatory regime for the purposes of detecting money-laundering, terrorist financing or other offences.

145. Customer identification entails requirements that holders of accounts in financial institutions and all parties to financial transactions be identified and documented. Records should contain sufficient information to identify all parties and the nature of the transaction, identify specific assets and the amounts or values involved, and permit the tracing of the source and destination of all funds or other assets.

146. The requirement for record-keeping means that client and transaction records should be kept for a specified minimum period of time. For example, under the FATF Forty Recommendations, at least five years is recommended, while for States parties to the International Convention for the Suppression of the Financing of Terrorism, retention of records for five years is mandatory.

147. Suspicious transactions are to be notified to the FIU or other designated agency. Criteria for identifying suspicious transactions should be developed and periodically reviewed in consultation with experts knowledgeable about new methods or networks used by money launderers.

148. The interpretative notes indicate that the words “suspicious transactions” may be understood to include unusual transactions that, by reason of their amount, characteristics and frequency, are inconsistent with the customer’s business activity, exceed the normally accepted parameters of the market or have no clear legal basis and could constitute or be connected with unlawful activities in general (A/58/422/Add.1, para. 19). The International Convention for the Suppression of the Financing of Terrorism defines suspicious transactions as all complex, unusually large transactions and unusual patterns of transactions, which have no apparent economic or obviously lawful purpose (General Assembly resolution 54/109, annex, art. 18, para. 1 (b) (iii)).

149. The powers to be granted to regulators and staff of the FIU to inspect records and to compel the assistance of record keepers in locating the records must also be defined. As some of these records may be covered by confidentiality requirements and banking secrecy laws that prohibit their disclosure, provisions freeing financial institutions from complying with such requirements and laws may be considered. Drafters should also ensure that the inspection and disclosure requirements are written in such a way as to protect financial institutions against civil and other claims for disclosing client records to regulators and FIUs.

150. The implementation of such measures is likely to require legislation. In particular, the requirement that financial institutions must disclose suspicious transactions and the protection of those who make disclosures in good faith will require legislation to override banking secrecy laws (see also paras. 1-3 of art. 52, on the prevention and detection of transfers of proceeds of crime).

**(b) Domestic and international cooperation**

151. Coordination of efforts and international cooperation is as central to the problem of money-laundering as it is to the other offences covered by the Convention against Corruption. Beyond the general measures and processes such as extradition, mutual legal assistance, joint investigations and asset recovery (which are covered in detail in the sections on international cooperation in chapter IV and asset recovery in chapter V, below), the Convention seeks to strengthen such coordination and cooperation.

152. Article 14, paragraph 1 (b), requires that administrative, regulatory, law enforcement and other domestic authorities in charge of the efforts against money-laundering are able to cooperate at both the national and international level. This includes the exchange of information within the conditions prescribed by their domestic law. This must be done without limiting or detracting from (or in the words of the Convention, “without prejudice to”) the requirements generated by article 46 (Mutual legal assistance).

153. In order for cooperation to be possible, domestic capabilities must be developed for the identification, collection and interpretation of all relevant information. Essentially, three types of entity may be part of a strategy to combat money-laundering and could, thus, be considered by States:

- (a) Regulatory agencies responsible for the oversight of financial institutions, such as banks or insurance entities, with powers to inspect financial institutions and enforce regulatory requirements through the imposition of regulatory or administrative remedies or sanctions;
- (b) Law enforcement agencies responsible for conducting criminal investigations, with investigative powers and powers to arrest and detain suspected offenders and that are subject to judicial or other safeguards;
- (c) FIUs, which are not required under the Convention, whose powers are usually limited to receiving reports of suspicious transactions, analysing them and disseminating information to prosecution agencies, although some such units have wider powers (see more on FIUs in sect. V.E, below).

154. The authority of each entity to cooperate with national bodies and with other similar agencies in other States is usually specified in the relevant legislation. If States do have such entities, legislation may be needed to amend existing mandates and the

division of labour among these entities, in accordance with each State's constitutional or other principles and the specificities of its financial services sector.

155. Some of these measures may constitute a strong challenge for countries in which the financial sector is not heavily regulated and the necessary legislation and administrative infrastructure may have to be created. It is essential to note, however, that the relevance and utility of these arrangements are not limited to the control of money-laundering, but also to corruption. They also strengthen confidence in the financial infrastructure, which is instrumental to sustainable social and economic development.

156. The remaining provisions of this article are also closely connected to domestic and international cooperation, and are examined below, as they are not mandatory under the Convention.

#### **Optional requirements: obligation to consider**

##### **(a) Financial intelligence units**

157. Article 14, paragraph 1 (b), requires States parties to consider the establishment of FIUs to serve as a national centre for the collection, analysis and dissemination of information regarding potential money-laundering. Since the 1990s, many States have established such units as part of their regulatory police or other authorities. There is a wide range of structure, responsibilities, functions and departmental affiliation or independence for such units. According to the interpretative notes, the call for the establishment of an FIU is intended for cases where such a mechanism does not yet exist (A/58/422/Add.1, para. 20).

158. The Egmont Group (an informal association of FIUs) has defined such units as a central, national agency responsible for receiving (and, as permitted, requesting), analysing and disseminating to the competent authorities, disclosures of financial information (a) concerning suspected proceeds of crime; or (b) required by national legislation or regulation; in order to counter money laundering.<sup>50</sup>

159. The Convention does not require that an FIU be established by law, but legislation may still be required to institute the obligation to report suspicious transactions to such a unit and to protect financial institutions that disclose such information in good faith (see also art. 58, on FIUs). In practice, the vast majority of FIUs are established by law. If it is decided to draft such legislation, States may wish to consider including the following elements:

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<sup>50</sup> [31] The website for the Egmont group is <http://www.egmontgroup.org/>, which, inter alia, provides links to FIUs on all continents.

- (a) Specification of the institutions that are subject to the obligation to report suspicious transactions and definition of the information to be reported to the unit;
- (b) Legislation defining the powers under which the unit can compel the assistance of reporting institutions to follow up on incomplete or inadequate reports;
- (c) Authorization for the unit to disseminate information to law enforcement agencies when it has evidence warranting prosecution and authority for the unit to communicate financial intelligence information to foreign agencies, under certain conditions;
- (d) Protection of the confidentiality of information received by the unit, establishing limits on the uses to which it may be put and shielding the unit from further disclosure;
- (e) Definition of the reporting arrangements for the unit and its relationship with other Government agencies, including law enforcement agencies and financial regulators. States may already have money-laundering controls in place that can be expanded or modified to conform to the requirements of article 14 relating to money-laundering and those of article 31 relating to freezing, confiscation, seizure, disposal of proceeds, as well as provisions on asset recovery, as necessary.

160. It is worth noting that actions taken to conform to article 14 may also bring States into conformity with other conventions and initiatives, such as Security Council resolution 1373 (2001), the International Convention for the Suppression of the Financing of Terrorism, the Organized Crime Convention and the FATF Nine Special Recommendations on Terrorist Financing.

161. Further information about various options that can be included in laws, regulations and procedures to combat money-laundering can be obtained from the Anti-Money-Laundering Unit of the United Nations Office on Drugs and Crime.

**(b) Other measures**

162. As part of the effort to develop the capacity to provide effective international cooperation, States are required to consider the introduction of feasible measures aimed at monitoring the cross-border movement of cash and other monetary instruments (art. 14, para. 2). The goal of such measures would be to allow States to detect and monitor the movement of cash and appropriate negotiable instruments across their borders, subject to safeguards to ensure proper use of information and without impeding in any way the movement of legitimate capital. Such measures may include a requirement that individuals and businesses report the cross-border transfer of substantial quantities of cash appropriate negotiable instruments. Generally, structures based on monitoring or surveillance will require legal powers giving



inspectors or investigators access to information on cross-border transactions, in particular in cases where criminal behaviour is suspected.<sup>51</sup>

163. Article 14, paragraph 3, contains provisions going beyond the Organized Crime Convention. It requires that States consider the implementation of measures obliging financial institutions, including money remitters:

- (a) To include on forms for the electronic transfer of funds and related messages accurate and meaningful information on the originator;
- (b) To maintain such information throughout the payment chain; and
- (c) To apply enhanced scrutiny to transfers of funds that do not contain complete information on the originator.

164. The concern is essentially about the identification of remitters and beneficiaries on the one hand and the traceability of the transaction on the other. There are no exact estimates on the extent of funds transferred across national borders, especially with respect to informal remitters, who are popular in many countries. Given that they range in the tens of billions of United States dollars, however, it is an area of regulatory concern.

165. As mentioned above, the Convention against Corruption builds on parallel international initiatives to combat money-laundering. In establishing a domestic regulatory and supervisory regime, States parties are called upon to use as a guideline the relevant initiatives of regional, interregional and multilateral organizations against money-laundering (art. 14, para. 4). An interpretative note states that during the negotiations, the words “relevant initiatives of regional, interregional and multilateral organizations” were understood to refer in particular to the Forty Recommendations and the Eight<sup>52</sup> Special Recommendations of the FATF, as revised in 2003 and 2001, respectively, and, in addition, to other existing initiatives of regional, interregional and multilateral organizations against money-laundering, such as the Caribbean Financial Action Task Force, the Commonwealth, the Council of Europe, the Eastern and Southern African Anti-Money-Laundering Group, the European Union, the Financial Action Task Force of South America against Money Laundering and the Organization of American States” (A/58/422/Add.1, para. 21).

166. Ultimately, States are free to determine the best way to implement article 14. However, the development of a relationship with one of the organizations working to combat money-laundering would be important for effective implementation.

167. In implementing article 14, paragraph 4, States may wish to consider some specific elements relative to the measures that the comprehensive regulatory regime must include. The Forty Recommendations are useful in this regard, as are model regulations that have been prepared by the United Nations Office on Drugs and Crime

and the Organization of American States (see sect. II.G (Information resources) at the end of this chapter of the guide).

168. Furthermore, paragraph 5 of article 14 requires that States endeavour to develop and promote global, regional, subregional and bilateral cooperation among judicial, law enforcement and financial regulatory authorities in order to combat money-laundering.<sup>53</sup>

END OF EXCERPT

## 4.2 OECD Anti-Bribery Convention

The OECD Convention does not deal extensively with money laundering, but it does touch on the issue in articles 7 and 8, which are reproduced below:

### Article 7: Money Laundering

Each Party which has made bribery of its own public official a predicate offence for the purpose of the application of its money laundering legislation shall do so on the same terms for the bribery of a foreign public official, without regard to the place where the bribery occurred.

### Article 8: Accounting

In order to combat bribery of foreign public officials effectively, each Party shall take such measures as may be necessary, within the framework of its laws and regulations regarding the maintenance of books and records, financial statement disclosures, and accounting and auditing standards, to prohibit the establishment of off-the-books accounts, the making of off-the-books or inadequately identified transactions, the recording of non-existent expenditures, the entry of liabilities with incorrect identification of their object, as well as the use of false documents, by companies subject to those laws and regulations, for the purpose of bribing foreign public officials or of hiding such bribery.

Each Party shall provide effective, proportionate and dissuasive civil, administrative or criminal penalties for such omissions and falsifications in respect of the books, records, accounts and financial statements of such companies.

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<sup>51</sup> [32] See the website of the Financial Action Task Force on Money Laundering at [updated link: <http://www.fatf-gafi.org/>].

<sup>52</sup> [33] In October 2004, the FATF adopted a ninth Special Recommendation on Terrorist Financing.

<sup>53</sup> UN Legislative Guide (2012) at 46–53, paras 138–168. Reprinted with the permission of the United Nations.

The OECD website notes that “The Financial Action Task Force (FATF) is the international standard setter in the development and promotion of national and international policies to **combat money laundering and terrorist financing**” [emphasis in original] and that “[t]he OECD’s work on tax crime and money laundering is designed to complement that carried out by FATF.”<sup>54</sup> The FATF recommendations, which are covered in the following section, provide a more comprehensive treatment of money laundering and the measures that states can take to combat it.

### 4.3 FATF Recommendations

As already noted, the Financial Action Task Force (FATF) is a governmental policy group composed of 34 nations including the US, UK and Canada. The latest version of the FATF Recommendations was released in 2012. There are 40 recommendations in this new version, which merged the original 40 recommendations (issued in 1996) with nine additional 2003 recommendations (on countering terrorism financing). The recommendations can be found at: <<http://www.fatf-gafi.org/topics/fatfrecommendations/documents/fatf-recommendations.html>>. The Recommendations also include interpretive notes. The following excerpt from Paul Allan Schott’s *Reference Guide to Anti-Money Laundering and Combating the Financing of Terrorism*, 2<sup>nd</sup> ed (World Bank, 2006) provides a general introduction to the FATF and the Recommendations. This excerpt is based on the 2003 version of the *Forty Recommendations*, but this does not affect the validity of the general comments set out below.

#### BEGINNING OF EXCERPT

[Chapter III: International Standard Setters, pp. III-7 to III-12]

Formed in 1989 by the G-7 countries,<sup>55</sup> the Financial Action Task Force on Money Laundering (FATF) is an intergovernmental body whose purpose is to develop and promote an international response to combat money laundering.<sup>56</sup> In October of 2001, FATF expanded its mission to include combating the financing of terrorism.<sup>57</sup>

FATF is a policy-making body, which brings together legal, financial and law enforcement experts to achieve national legislation and regulatory AML and CFT reforms. Currently, its membership consists of 31 [now 34] countries and territories

<sup>54</sup> OECD CleanGovBiz, “Money Laundering”, online:

<<http://www.oecd.org/cleangovbiz/toolkit/moneylaundering.htm>>.

<sup>55</sup> [30] *Id.* The G-7 countries are Canada, France, Germany, Italy, Japan, United Kingdom, and United States.

<sup>56</sup> [31] About FATF, and Terrorist Financing at <http://www.fatf-gafi.org/>.

<sup>57</sup> [32] *Id.* at Terrorist Financing.

and two regional organizations.<sup>58</sup> In addition, FATF works in collaboration with a number of international bodies<sup>59</sup> and organizations.<sup>60</sup> These entities have observer status with FATF, which does not entitle them to vote, but otherwise permits full participation in plenary sessions and working groups.

FATF's three primary functions with regard to money laundering are:

1. monitoring members' progress in implementing anti-money laundering measures;
2. reviewing and reporting on laundering trends, techniques and counter-measures; and
3. promoting the adoption and implementation of FATF anti-money laundering standards globally.

### **1. *The Forty Recommendations***

FATF has adopted a set of 40 recommendations, *The Forty Recommendations on Money Laundering (The Forty Recommendations)*, which constitute a comprehensive framework for AML and are designed for universal application by countries throughout the

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<sup>58</sup> [33] The 31 member countries and territories are: Argentina, Australia, Austria, Belgium, Brazil, Canada, Denmark, Finland, France, Germany, Greece, Hong Kong-China, Iceland, Ireland, Italy, Japan, Luxemburg, Mexico, Kingdom of the Netherlands, New Zealand, Norway, Portugal, Russia, Singapore, South Africa, Spain, Sweden, Switzerland, Turkey, United Kingdom, and United States. The two regional organizations are the European Commission and the Gulf Co-operation Council.

<sup>59</sup> [34] The international bodies are regional FATF-style regional bodies (FSRBs) that have similar form and functions to those of FATF. Some FATF members also participate in the FSRBs. These bodies are: Asia/Pacific Group on Money Laundering (APG), Caribbean Financial Action Task Force (CFATF), Council of Europe MONEYVAL (previously PC-R-EV) Committee, Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG) and Financial Action Task Force on Money Laundering in South America (GAFISUD). For a discussion of these organizations, See Chapter IV, Regional Bodies and Relevant Groups, FATF- Style Regional Bodies. FATF also works with the Egmont Group.

<sup>60</sup> [35] Each of the international organizations, which have, among other functions, a specific anti-money laundering mission or function, are: African Development Bank, Asia Development Bank, The Commonwealth Secretariat, European Bank for Reconstruction and Development, European Central Bank (ECB), Europol, Inter-American Development Bank (IDB), Intergovernmental Action Group Against Money-Laundering in Africa (GIABA), International Association of Insurance Supervisors (IAIS), International Monetary Fund (IMF), Interpol, International Organization of Securities Commissions (IOSCO), Organization of American States/Inter-American Committee Against Terrorism (OAS/CICTE), Organization of American States/Inter-American Drug Abuse Control Commission (OAS/CICAD), Organization for Economic Co-operation and Development (OECD), Offshore Group of Banking Supervisors (OGBS), United Nations Office on Drugs and Crime (UNODC), World Bank and World Customs Organization (WCO).

world.<sup>61</sup> The Forty Recommendations set out principles for action; they permit a country flexibility in implementing the principles according to the country's own particular circumstances and constitutional requirements. Although not binding as law upon a country, *The Forty Recommendations* have been widely endorsed by the international community and relevant organizations as the international standard for AML.

*The Forty Recommendations* are actually mandates for action by a country if that country wants to be viewed by the international community as meeting international standards. The individual recommendations are discussed in detail throughout this Reference Guide and, particularly in Chapters V, VI, VII, and VIII.

*The Forty Recommendations* were initially issued in 1990 and have been revised in 1996 and 2003 to take account of new developments in money laundering and to reflect developing best practices internationally. [The current version of the *Forty Recommendations* was revised in 2012.]

## 2. Monitoring Members Progress

Monitoring the progress of members to comply with the requirements of *The Forty Recommendations* is facilitated by a two-stage process: self assessments and mutual evaluations. In the self-assessment stage, each member responds to a standard questionnaire, on an annual basis, regarding its implementation of *The Forty Recommendations*. In the mutual evaluation stage, each member is examined and assessed by experts from other member countries.

In the event that a country is unwilling to take appropriate steps to achieve compliance with *The Forty Recommendations*, FATF recommends that all financial institutions give special attention to business relations and transactions with persons, including companies and financial institutions, from such non-compliant countries and, where appropriate, report questionable transactions, i.e., those that have no apparent economic or visible lawful purpose, to competent authorities.<sup>62</sup> Ultimately, if a member country does not take steps to achieve compliance, membership in the organization can be suspended. There is, however, the process of peer pressure before these sanctions are enforced.

## 3. Reporting on Money Laundering Trends and Techniques

One of FATF's functions is to review and report on money laundering trends, techniques and methods (also referred to as typologies). To accomplish this aspect of

<sup>61</sup> [36] *The Forty Recommendations*, [updated link: <http://www.fatf-gafi.org/media/fatf/documents/FATF%20Standards%20-%2040%20Recommendations%20rc.pdf>].

<sup>62</sup> [37] *Id.*, Rec. 21.

its mission, FATF issues annual reports on developments in money laundering through its Typologies Report.<sup>63</sup> These reports are very useful for all countries, not just FATF members, to keep current with new techniques or trends to launder money and for other developments in this area.

#### 4. The NCCT List

One of FATF's objectives is to promote the adoption of international AML/CFT standards for all countries. Thus, its mission extends beyond its own membership, although FATF can only sanction its member countries and territories. Thus, in order to encourage all countries to adopt measures to prevent, detect and prosecute money launderers, i.e., to implement The Forty Recommendations, FATF has adopted a process of identifying those jurisdictions that serve as obstacles to international cooperation in this area. The process uses 25 criteria, which are consistent with *The Forty Recommendations*, to identify such non-cooperative countries and territories (NCCT's) and place them on a publicly available list.<sup>64</sup>

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[In response to criticisms levied against the use of the NCCT list, the last country on the NCCT list was removed in 2006, and no new states have been reviewed by the FATF under the NCCT criteria since 2001. Many felt that the NCCT focused attention unfairly on smaller, less powerful nations while ignoring the failings of more powerful countries such as the United States. Since it is no longer relevant, the remainder of the section on the NCCT list has not been included in this excerpt. However, the FATF has continued to issue public statements on high-risk and non-compliant countries. This list presently includes Iran, the Democratic People's Republic of Korea and Algeria. It is available at: <http://www.fatf-gafi.org/topics/high-riskandnon-cooperativejurisdictions/>]

#### 5. Terrorist Financing

FATF also focuses its expertise on the world-wide effort to combat terrorist financing. To accomplish this expanded mission FATF has adopted nine *Special Recommendations on Terrorist Financing (Special Recommendations)*.<sup>65</sup> As part of this effort, FATF members use a self-assessment questionnaire of their country's actions to come into compliance

<sup>63</sup> [38] See FATF Documents, Money Laundering Trends and Techniques at [http://www.fatf-gafi.org/pdf/TY2004\\_en.PDF](http://www.fatf-gafi.org/pdf/TY2004_en.PDF).

<sup>64</sup> [39] NCCT Initiative, [http://www.fatf-gafi.org/NCCT\\_en.htm](http://www.fatf-gafi.org/NCCT_en.htm).

<sup>65</sup> [42] See *Special Recommendations*. These Special Recommendations are set out in Annex V, [http://www.fatf-gafi.org/pdf/SRecTF\\_en.pdf](http://www.fatf-gafi.org/pdf/SRecTF_en.pdf).

with the *Special Recommendations*.<sup>66</sup> FATF is continuing to develop guidance on techniques and mechanisms used in the financing of terrorism.

END OF EXCERPT

The FATF prepares guidance and best practices documents to assist states in implementing the Recommendations. Seven such documents have been published since the latest version of the Recommendations was released in 2012. They are available on the FATF website: <http://www.fatf-gafi.org/documents/guidance/>.

## 5. STATE-LEVEL AML REGIMES: US, UK AND CANADA

### 5.1 Introduction to the Essential Elements of AML Regimes

While the FATF Recommendations provide a global standard for AML measures, these recommendations must be put into place at the state level to be effective. The global effectiveness of the AML regime depends on a degree of standardization, but each state must also create a regime that fits within its domestic legal framework and policy goals. As a result, despite many shared elements, there is significant variation between different state-level AML regimes.

The overall goal of state-level AML regimes is to allow centralized monitoring of the financial sector. The set of laws and policies contained in the FATF Recommendations is intended to enable sweeping state surveillance and intelligence gathering across the financial sector. Data concerning suspicious transactions is transmitted to a central organization for analysis and selected information is then passed to law enforcement agencies for investigation. In general, the goal is to create a system in which suspicious transactions or patterns of transactions are promptly detected and thoroughly investigated, preventing the abuse of financial institutions by organized crime and corrupt officials.

There are three principal elements in a state-level AML regime, each of which is dealt with in a separate section below. The first element is a Financial Intelligence Unit (FIU). FIUs are central, national-level organizations that collect and analyze information concerning suspicious transactions reported by financial institutions. They pass selected information along to the appropriate law enforcement agencies for investigation.

The second element of a state-level AML regime is sweeping regulation of the financial sector, which requires financial institutions to report information to the FIU. There are three basic aspects of this regulatory framework. The first is customer due diligence measures (CDD), which require financial institutions to collect identifying information from each of

<sup>66</sup> [43] [http://www.fatf-gafi.org/SAOTF\\_en.htm](http://www.fatf-gafi.org/SAOTF_en.htm).

their customers. The second is record keeping requirements, which require financial institutions to retain all information collected for at least five years. The final aspect is transaction reporting requirements, which require financial institutions to report certain transactions to their respective FIUs.

The third element of a state-level AML regime is the creation of tools that law enforcement agencies can use to effectively prosecute money launderers once their activities are detected. These include the creation of stand-alone criminal offences for money laundering to enable prosecution of launderers. In theory, the three elements discussed above should create a state-level regime in which money laundering can be effectively combated through cooperation between the financial sector, the FIU and law enforcement agencies.

While the three elements described above are present in all state-level AML regimes that conform to the FATF recommendations, how each is put into place varies considerably from country to country. The following section surveys the state-level AML regimes in the US, Canada and the UK, comparing and contrasting the different approaches taken in each jurisdiction. Each subsection begins by reproducing the appropriate FATF recommendation, and then briefly discusses how the recommendation has been enacted by each of the three governments.<sup>67</sup>

## 5.2 Financial Intelligence Units

### 5.2.1 FATF Recommendations

Recommendation 29 of the FATF requires that each member state create a financial intelligence unit (FIU) as part of its AML regime. These FIUs cooperate internationally through their membership in the Egmont Group, an informal network whose membership currently includes 139 state-level FIUs. The Egmont Group's website, <<http://www.egmontgroup.org/>>, provides a library of research reports produced by the organization as well as sanitized cases from member FIUs.

The full text of Recommendation 29 is reproduced below:

#### **29. Financial intelligence units**

Countries should establish a financial intelligence unit (FIU) that serves as a national centre for the receipt and analysis of: (a) suspicious transaction reports; and (b) other information relevant to money laundering, associated predicate offences and terrorist financing, and for the dissemination of the results of that analysis. The FIU should be able to obtain additional information from reporting entities, and should have access on a timely

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<sup>67</sup> Only selected FATF recommendations are reproduced here. The full text can be found online: <<http://www.fatf-gafi.org/topics/fatfrecommendations/documents/fatf-recommendations.html>>.



basis to the financial, administrative and law enforcement information that it requires to undertake its functions properly.

There is considerable scope available to states in implementing this recommendation. All that is strictly required is the creation of a central organization that collects and analyzes reports of suspicious transactions and “other information.” Some states have chosen to create FIUs with a broad range of powers, while others have taken a more minimal approach. Furthermore, there is nothing in the recommendation to indicate how the FIU should relate to other government agencies, or who it should report to. States have made different choices in this regard as well. The following section briefly discusses and compares the FIUs created by the UK, the US and Canada respectively.

The US FIU is known as the Financial Crimes Enforcement Network (FinCEN).<sup>68</sup> Canada, displaying US influence, chose the name Financial Transactions and Reports Analysis Centre of Canada (FINTRAC).<sup>69</sup> The UK, taking a more prosaic approach, named its FIU the UK Financial Intelligence Unit (UKFIU).<sup>70</sup> FinCEN and FINTRAC are independent organizations that report through the financial arms of their respective states. FinCEN reports to the Secretary of the Treasury<sup>71</sup> and FINTRAC to the Minister of Finance.<sup>72</sup> In contrast, UKFIU is situated within the law enforcement apparatus of the UK (in an indication of this embedded role, the organization does not have its own website). It forms part of the National Crime Agency (NCA). The NCA website describes its function as follows:

The NCA has a wide remit. We tackle serious and organised crime, strengthen our borders, fight fraud and cyber crime, and protect children and young people from sexual abuse and exploitation. We provide leadership in these areas through our organised crime, border policing, economic crime and CEOP commands, the National Cyber Crime Unit and specialist capability teams. The NCA works closely with partners to deliver operational results. We have an international role to cut serious and organised crime impacting on the UK through our network of international liaison officers.<sup>73</sup>

Had the US and Canada taken a similar approach, their FIUs would have been created as specialist bodies within the Federal Bureau of Investigation (FBI) and Royal Canadian Mounted Police (RCMP). Instead, FINCEN and FINTRAC have considerably more autonomy from law enforcement than UKFIU, as well as broader powers.

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<sup>68</sup> For more information, see: <<http://www.fincen.gov/>>.

<sup>69</sup> For more information, see: <<http://www.fintrac-canafe.gc.ca/intro-eng.asp>>.

<sup>70</sup> For more information, see: <<http://www.nationalcrimeagency.gov.uk/about-us/what-we-do/economic-crime/ukfiu>>.

<sup>71</sup> FINCEN, “What We Do”, online: <<https://www.fincen.gov/what-we-do>>.

<sup>72</sup> FINTRAC, “Who We Are”, online: <<http://www.fintrac-canafe.gc.ca/fintrac-canafe/1-eng.asp>>.

<sup>73</sup> NCA, “What We Do”, online: <<http://www.nationalcrimeagency.gov.uk/about-us/what-we-do>>.

### 5.2.2 US

Established under the *Bank Secrecy Act*, FINCEN performs a variety of functions, covering data gathering, regulation, research and analysis. Its website describes the organization's powers as follows:

Congress has given FinCEN certain duties and responsibilities for the central collection, analysis, and dissemination of data reported under FinCEN's regulations and other related data in support of government and financial industry partners at the Federal, State, local, and international levels. To fulfill its responsibilities toward the detection and deterrence of financial crime, FinCEN:

- Issues and interprets regulations authorized by statute;
- Supports and enforces compliance with those regulations;
- Supports, coordinates, and analyzes data regarding compliance examination functions delegated to other Federal regulators;
- Manages the collection, processing, storage, dissemination, and protection of data filed under FinCEN's reporting requirements;
- Maintains a government-wide access service to FinCEN's data, and networks users with overlapping interests;
- Supports law enforcement investigations and prosecutions;
- Synthesizes data to recommend internal and external allocation of resources to areas of greatest financial crime risk;
- Shares information and coordinates with foreign financial intelligence unit (FIU) counterparts on AML/CFT efforts; and
- Conducts analysis to support policymakers; law enforcement, regulatory, and intelligence agencies; FIUs; and the financial industry.<sup>74</sup>

Under the *Bank Secrecy Act (BSA)*, FinCEN can bring enforcement actions for *BSA* violations.<sup>75</sup> For example, in May 2015, a FinCEN enforcement action led to the imposition of a \$700,000 fine on a virtual currency exchange company that lacked an AML program.<sup>76</sup> In June 2015, FinCEN fined a casino in the Northern Mariana Islands \$75 million for its failure to institute an AML program, hire compliance staff and create procedures for

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<sup>74</sup> FINCEN, "What We Do", online: <<https://www.fincen.gov/what-we-do>>.

<sup>75</sup> For a list of FinCEN enforcement actions, see: <[http://www.fincen.gov/news\\_room/ea/](http://www.fincen.gov/news_room/ea/)>.

<sup>76</sup> Richard L Cassin, "Ripple Labs Becomes First Virtual Money Exchange Fined by FinCEN", *The FCPA Blog* (7 May 2015), online: <<http://www.fcpablog.com/blog/2015/5/7/ripple-labs-becomes-first-virtual-money-exchange-fined-by-fi.html>>.

detecting suspicious transactions.<sup>77</sup> In July 2015, FinCEN imposed “special measure five” on Tanzania-based FBME Bank Ltd, meaning US financial institutions are barred from “opening or maintaining correspondent accounts or payable through accounts for or on behalf of FBME.”<sup>78</sup> FinCEN alleges that FBME is being used to facilitate money laundering and that high-risk shell companies are among its customers.<sup>79</sup> The bank expressed outrage at the ban and claimed it did not receive adequate notice, although FinCEN issued a notice in July 2014 warning that FBME was a primary money laundering concern and could be subject to a final ban.<sup>80</sup> For a full list of FinCEN enforcement actions see: <<https://www.fincen.gov/news-room/enforcement-actions>>.

### 5.2.3 UK

The UK’s FIU responsibilities were transferred from the Serious Organized Crime Agency to the National Crime Agency (NCA) in 2013 with the passing of the *Crime and Courts Act*. In contrast to FinCEN, the UKFIU page on the NCA website states simply: “The UK Financial Intelligence Unit (UKFIU) receives, analyses and distributes financial intelligence gathered from Suspicious Activity Reports (SARs).”<sup>81</sup> While FinCEN and FINTRAC also handle SARs, which will be discussed in more detail in the following section, they also do a great deal more. UKFIUs mandate is narrower, likely due to its integration within the state’s law enforcement apparatus. FinCEN and FINTRAC have broader mandates and greater organizational independence.

### 5.2.4 Canada

Similarly to its US counterpart, FINTRAC’s description of its function is comprehensive, covering data gathering, analysis and research. The organization’s website states that:

Our mandate is to facilitate the detection, prevention and deterrence of money laundering and the financing of terrorist activities, while ensuring the protection of personal information under our control. We fulfill our mandate through the following activities:

- Receiving financial transaction reports and voluntary information on money laundering and terrorist financing in accordance with

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<sup>77</sup> Richard L Cassin, “FinCEN Fines Pacific Island Casino \$75 Million for ‘Egregious’ Anti-Money Laundering Offenses”, *The FCPA Blog* (4 June 2015), online: <<http://www.fcpablog.com/blog/2015/6/4/fincen-fines-pacific-island-casino-75-million-for-egregious.html>>.

<sup>78</sup> Richard L Cassin, “Tanzania Bank is ‘Shocked’ after ‘Unexplained’ FinCEN Ban”, *The FCPA Blog* (27 July 2015), online: <<http://www.fcpablog.com/blog/2015/7/27/tanzania-bank-is-shocked-after-unexplained-fincen-ban.html>>.

<sup>79</sup> *Ibid.*

<sup>80</sup> *Ibid.*

<sup>81</sup> NCA, “UK Financial Intelligence Unit”, online: <<http://www.nationalcrimeagency.gov.uk/about-us/what-we-do/economic-crime/ukfiu>>.

the legislation and regulations and safeguarding personal information under our control;

- Ensuring compliance of reporting entities with the legislation and regulations;
- Producing financial intelligence relevant to money laundering, terrorist activity financing and threats to the security of Canada investigations;
- Researching and analyzing data from a variety of information sources that shed light on trends and patterns in money laundering and terrorist financing;
- Maintaining a registry of money services businesses in Canada;
- Enhancing public awareness and understanding of money laundering and terrorist activity financing.<sup>82</sup>

FINTRAC is authorized by legislation to provide information to foreign FIUs, and also receives information from FIUs and law enforcement agencies in other jurisdictions (23-34).<sup>83</sup>

FINTRAC has broad powers to search without warrant, investigate and report to police authorities. Normal criminal law protections do not apply. For example, FINTRAC can enter any premises without a warrant unless the premises are a dwelling.<sup>84</sup> Terence D. Hall notes that “[t]here is a tension between the values placed on privacy and the protection of personal information and the public policy goals of deterring criminal activity and the financing of terrorism by requiring the collection and disclosure of personal and proprietary information.”<sup>85</sup> In 2013, Canada’s Privacy Commissioner audited FINTRAC, reporting that FINTRAC “continues to receive and retain personal information not directly related to its mandate.”<sup>86</sup>

## 5.3 Regulation of Financial Institutions and Professionals

### 5.3.1 Customer Due Diligence

FATF Recommendation 10 deals with customer due diligence (CDD) measures. The essence of CDD is requiring financial institutions to ascertain whom they are dealing with for each major transaction. The full text of the recommendation is reproduced below.

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<sup>82</sup> FINTRAC, “Who We Are”, online: <<http://www.fintrac-canafe.gc.ca/fintrac-canafe/1-eng.asp>>.

FINTRAC has reorganized all its very detailed guidelines in respect to the *PCMLTFA*, and these can be found on FINTRAC’s website at: <<http://www.fintrac.gc.ca/guidance-directives/1-eng.asp>>.

<sup>83</sup> Terence D Hall, *A Guide to Canadian Money Laundering Legislation*, 4<sup>th</sup> ed (LexisNexis, 2015) at 23.

<sup>84</sup> *Ibid* at 147–48.

<sup>85</sup> *Ibid* at 18.

<sup>86</sup> *Ibid* at 19.

BEGINNING OF EXCERPT

## 10. Customer due diligence

Financial institutions should be prohibited from keeping anonymous accounts or accounts in obviously fictitious names.

Financial institutions should be required to undertake customer due diligence (CDD) measures when:

- (i) establishing business relations;
- (ii) carrying out occasional transactions: (i) above the applicable designated threshold (USD/EUR 15,000); or (ii) that are wire transfers in the circumstances covered by the Interpretive Note to Recommendation 16;
- (iii) there is a suspicion of money laundering or terrorist financing; or
- (iv) the financial institution has doubts about the veracity or adequacy of previously obtained customer identification data.

The principle that financial institutions should conduct CDD should be set out in law. Each country may determine how it imposes specific CDD obligations, either through law or enforceable means.

The CDD measures to be taken are as follows:

- (a) Identifying the customer and verifying that customer's identity using reliable, independent source documents, data or information.
- (b) Identifying the beneficial owner, and taking reasonable measures to verify the identity of the beneficial owner, such that the financial institution is satisfied that it knows who the beneficial owner is. For legal persons and arrangements this should include financial institutions understanding the ownership and control structure of the customer.
- (c) Understanding and, as appropriate, obtaining information on the purpose and intended nature of the business relationship.
- (d) Conducting ongoing due diligence on the business relationship and scrutiny of transactions undertaken throughout the course of that relationship to ensure that the transactions being conducted are consistent with the institution's knowledge of the customer, their business and risk profile, including, where necessary, the source of funds.

Financial institutions should be required to apply each of the CDD measures under (a) to (d) above, but should determine the extent of such measures using a risk-based approach (RBA) in accordance with the Interpretive Notes to this Recommendation and to Recommendation 1.

Financial institutions should be required to verify the identity of the customer and beneficial owner before or during the course of establishing a business relationship or conducting transactions for occasional customers. Countries may permit financial institutions to complete the verification as soon as reasonably practicable following the establishment of the relationship, where the money laundering and terrorist financing risks are effectively managed and where this is essential not to interrupt the normal conduct of business.

Where the financial institution is unable to comply with the applicable requirements under paragraphs (a) to (d) above (subject to appropriate modification of the extent of the measures on a risk-based approach), it should be required not to open the account, commence business relations or perform the transaction; or should be required to terminate the business relationship; and should consider making a suspicious transactions report in relation to the customer.

These requirements should apply to all new customers, although financial institutions should also apply this Recommendation to existing customers on the basis of materiality and risk, and should conduct due diligence on such existing relationships at appropriate times.

END OF EXCERPT

As discussed in the first section of this chapter, PEPs launder large amounts of misappropriated government funds and bribes every year. Because of the particular risks associated with PEPs, FATF Recommendation 12, set out below, requires enhanced due diligence when dealing with them as customers:

BEGINNING OF EXCERPT

## **12. Politically exposed persons**

Financial institutions should be required, in relation to foreign politically exposed persons (PEPs) (whether as customer or beneficial owner), in addition to performing normal customer due diligence measures, to:

- (a) have appropriate risk-management systems to determine whether the customer or the beneficial owner is a politically exposed person;
- (b) obtain senior management approval for establishing (or continuing, for existing customers) such business relationships;
- (c) take reasonable measures to establish the source of wealth and source of funds; and
- (d) conduct enhanced ongoing monitoring of the business relationship.

Financial institutions should be required to take reasonable measures to determine whether a customer or beneficial owner is a domestic PEP or a person who is or has been entrusted with a prominent function by an international organisation. In cases of a higher risk business relationship with such persons, financial institutions should be required to apply the measures referred to in paragraphs (b), (c) and (d).

END OF EXCERPT

Both the UK and Canada have created comprehensive regulatory frameworks to implement the above recommendations.<sup>87</sup> Both countries require financial institutions to collect and record personal information about their customers. As suggested by the FATF, both also require banks to conduct ongoing monitoring of the customer relationship and to take steps to identify the beneficial owners of customers that are organizations. Finally, both Canada and the UK require financial institutions to take steps to determine if their customers are PEPs and require enhanced due diligence in such cases.<sup>88</sup> The PEP concept has been criticized by some for its vagueness. Different definitions are used internationally, and challenges arise in determining who fits each definition. Financial institutions must choose where to draw the line, which is often far from clear cut.<sup>89</sup>

At present, the US CDD regime is somewhat weaker. US regulations require financial institutions to set up a Customer Identification Program (CIP) to determine the identity of each customer.<sup>90</sup> However, there are no specific requirements to identify beneficial ownership or conduct ongoing monitoring of the customer relationship. FINCEN is moving to address these weaknesses in the near future. A proposal for new regulations incorporating

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<sup>87</sup> In the UK, see the *Proceeds of Crime Act 2002* and the *Money Laundering Regulations 2007*, SI 2007/2157. The Financial Conduct Authority (FCA) is the authority responsible for supervising compliance with the *Money Laundering Regulations* by most financial firms and organisations. For more detail, see the resources available at the FCA website: <<http://www.fca.org.uk/>>. See also William Rees et al, *Blackstone's Guide to the Proceeds of Crime Act*, 4<sup>th</sup> ed (Oxford University Press, 2011). In Canada, see the *Proceeds of Crime (Money Laundering) and Terrorist Financing Act (PCMLTFA)*, SC 2000, c 17 and the *PCMLTF Regulations* SOR/2002-184 and four subsequent Regulations. See the Financial Transactions and Reports Analysis Centre of Canada (FINTRAC) website for detailed information on the various regulations related to the enforcement of *PCMLTFA*: <<http://www.fintrac-canafe.gc.ca/>>. See also Hall, (2015), and Peter M German, *Proceeds of Crime: The Criminal Law, Related Statutes, Regulations and Agreements* (Carswell, 1998) (loose-leaf updated 2013), ch 3, 16.

<sup>88</sup> UK: *The Money Laundering Regulations 2007*, SI 2007/2157, ss 7, 14(4); Canada: *The Proceeds of Crime (Money Laundering) and Terrorist Financing Regulations*, SOR/2002-184, ss 53-67.2.

<sup>89</sup> Louis de Koker, "Applying Anti-Money Laundering Laws to Fight Corruption" in Adam Graycar & Russell G Smith, eds, *Handbook of Global Research and Practice in Corruption* (Edward Elgar, 2011) 340 at 344-47.

<sup>90</sup> 31 CFR § 103.121.

these elements was released in 2014.<sup>91</sup> The US does require enhanced CDD in the case of correspondent accounts created by US banks for non-US persons. These measures include a requirement to determine beneficial ownership of any organizations involved and to determine whether the account holder is a Senior Foreign Political Figure (the US statutory language, roughly equivalent to PEP).<sup>92</sup>

### 5.3.2 Transaction Reporting

FATF Recommendation 20 requires states to create legal requirements for financial institutions to report any suspicious transactions to their respective FIUs:

#### 20. Reporting of suspicious transactions

If a financial institution suspects or has reasonable grounds to suspect that funds are the proceeds of a criminal activity, or are related to terrorist financing, it should be required, by law, to report promptly its suspicions to the financial intelligence unit (FIU).

Canada, the US and the UK follow this recommendation, requiring that all suspicious transactions be reported to their FIUs by financial institutions. However, there are some significant variations between the different reporting regimes. The UK only requires that all *suspicious* transactions be reported to UKFIU.<sup>93</sup> The US and Canada have similar requirements,<sup>94</sup> but both countries also require that *all* transactions over \$10,000 be reported to their respective FIUs.<sup>95</sup> Canada requires anyone, including members of the public, who imports or exports cash or monetary instruments with a value of \$10,000 or more to report the transaction to a customs officer. Reports are then passed on to FINTRAC.<sup>96</sup> The UK has taken a strict risk-based approach to transaction reporting, while Canada and the US have supplemented this with threshold-based reporting requirements. However, this should not be taken to mean that the UK's regime is weaker. Their reporting requirements are backed up with harsh sanctions for failure to report suspicious transactions.<sup>97</sup> Failure to disclose can result in up to five years imprisonment or a fine, or both. While the UK has taken a slightly different approach, it is not a more lenient one, and this "fear factor" has led to a dramatic

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<sup>91</sup> Fed Reg, Vol 79 No 149 (4 August 2014) online: <[http://www.fincen.gov/statutes\\_regs/files/CDD-NPRM-Final.pdf](http://www.fincen.gov/statutes_regs/files/CDD-NPRM-Final.pdf)>.

<sup>92</sup> Fed Reg, Vol 72 No 153 (9 August 2007) online: <[http://www.fincen.gov/statutes\\_regs/frn/pdf/31\\_CFR\\_Part\\_103\\_312\\_EDD\\_Rule.pdf](http://www.fincen.gov/statutes_regs/frn/pdf/31_CFR_Part_103_312_EDD_Rule.pdf)>.

<sup>93</sup> *Proceeds of Crime Act 2002* (UK), c 29, ss 330-331.

<sup>94</sup> US: 12 CFR §§ 21.11; Canada: *Proceeds of Crime (Money Laundering) and Terrorist Financing Act*, RSC 2000, c 17, s 7.

<sup>95</sup> US: 31 CFR Ch X § 1010.311; Canada: *The Proceeds of Crime (Money Laundering) and Terrorist Financing Regulations*, SOR/2002-184, s 12(1).

<sup>96</sup> Hall (2015) at 74.

<sup>97</sup> *Proceeds of Crime Act 2002* (UK), c 29, ss 330-332.



increase in SAR submissions. However, critics claim that the high cost of compliance with the UK's SAR regime is disproportionate to its effectiveness.<sup>98</sup>

### 5.3.3 Record-Keeping

The final piece of the regulatory regime proposed by the FATF Recommendations is the requirement for financial institutions to retain transaction records and customer information for at least five years. This requirement is set out in Recommendation 11:

#### 11. Record-keeping

Financial institutions should be required to maintain, for at least five years, all necessary records on transactions, both domestic and international, to enable them to comply swiftly with information requests from the competent authorities. Such records must be sufficient to permit reconstruction of individual transactions (including the amounts and types of currency involved, if any) so as to provide, if necessary, evidence for prosecution of criminal activity.

Financial institutions should be required to keep all records obtained through CDD measures (e.g. copies or records of official identification documents like passports, identity cards, driving licences or similar documents), account files and business correspondence, including the results of any analysis undertaken (e.g. inquiries to establish the background and purpose of complex, unusual large transactions), for at least five years after the business relationship is ended, or after the date of the occasional transaction.

Financial institutions should be required by law to maintain records on transactions and information obtained through the CDD measures.

The CDD information and the transaction records should be available to domestic competent authorities upon appropriate authority.

The US, UK and Canada all require financial institutions to store records for five years in accordance with Recommendation 11.<sup>99</sup> While the information stored in these records will vary slightly based on differences in their respective CDD regimes, there are no significant variations with regard to the record-keeping requirements themselves.

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<sup>98</sup> Karen Harrison & Nicholas Ryder, *The Law Relating to Financial Crime in the United Kingdom* (Farnham, England: Ashgate, 2013) at 32.

<sup>99</sup> Canada: *The Proceeds of Crime (Money Laundering) and Terrorist Financing Regulations*, SOR/2002-184, s 69; UK: *The Money Laundering Regulations 2007*, SI 2007/2157, s 19; US: 31 CFR § 103.121(3).

## 5.4 Money Laundering Offences

### 5.4.1 FATF Recommendations and UNCAC

FATF Recommendation 3 requires states to create offences to directly criminalize money laundering. The recommendation is reproduced below, along with an interpretive note. FATF Recommendation 3 on money laundering was produced in the original 2003 FATF Forty Recommendations. Recommendation 3 was drafted on the basis of two existing UN Conventions: the 1998 Narcotic Drugs and Psychotropic Substances Convention and the 2000 Transnational Organized Crime Convention. The money laundering provisions in those two conventions are now consolidated in the money laundering provisions in UNCAC. FATF Recommendation 3 provides:

#### 3. Money laundering offence

Countries should criminalise money laundering on the basis of the Vienna Convention and the Palermo Convention. Countries should apply the crime of money laundering to all serious offences, with a view to including the widest range of predicate offences.

#### Interpretive Note to Recommendation 3 (Money Laundering Offence)

1. Countries should criminalise money laundering on the basis of the United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, 1988 (the Vienna Convention) and the United Nations Convention against Transnational Organized Crime, 2000 (the Palermo Convention) [and now in accordance with Articles 14 and 23 of UNCAC (2005), which are discussed in detail in Sections 4.1.1 and 4.1.2 of this Chapter].
2. Countries should apply the crime of money laundering to all serious offences, with a view to including the widest range of predicate offences. Predicate offences may be described by reference to all offences; or to a threshold linked either to a category of serious offences; or to the penalty of imprisonment applicable to the predicate offence (threshold approach); or to a list of predicate offences; or a combination of these approaches.
- ...
5. Predicate offences for money laundering should extend to conduct that occurred in another country, which constitutes an offence in that country, and which would have constituted a predicate offence had it occurred domestically. Countries may provide that the only prerequisite is that the conduct would have constituted a predicate offence, had it occurred domestically.

6. Countries may provide that the offence of money laundering does not apply to persons who committed the predicate offence, where this is required by fundamental principles of their domestic law.

The US, the UK and Canada all have money laundering offences that generally comply with FATF and UNCAC requirements. However, there are significant differences between the three countries' provisions. Canada and the US define money laundering as the use of the proceeds of a list of specified offences ("predicate offences"). The UK takes a more inclusive approach. Under its regime, virtually all profit-driven crime can lead to money laundering charges.

### 5.4.2 US

In the United States, money laundering is primarily enforced at the federal level. Thirty-six states have money laundering offences. Where money laundering is criminalized at the state level, federal and state authorities work closely together. Approximately 2,500 natural and legal persons are charged with federal money laundering offences each year, resulting in over 1,200 convictions. In 2014, a total of 3,369 money laundering charges were laid and 1,967 convictions registered (the greater number of charges accounted for by the fact that a person may be charged with multiple counts of various money laundering offences).<sup>100</sup>

The two primary money laundering offences are 18 USC 1956: Money Laundering (proceeds laundering) and 18 USC 1957: Money Laundering (transactional). Respectively, charges for these offences were laid 1,895 and 517 times in 2014, accounting for 72% of all money laundering charges in United States. Other money laundering related charges are USC 1952: Interstate & foreign travel/transportation, including of proceeds, in aid of racketeering enterprises, 18 USC 1962: Receiving or deriving income from racketeering activities (RICO) and 31 USC 5332: Bulk cash smuggling.<sup>101</sup>

The relevant provisions of 18 USC 1956 and 18 USC 1957 are reproduced below:

#### 18 U.S. Code s.1956 – Laundering of monetary instruments

- (a) (1) *Whoever, knowing that the property involved in a financial transaction represents the proceeds of some form of unlawful activity, conducts or attempts to conduct such a financial transaction which in fact involves the proceeds of specified unlawful activity—*
  - (A) (i) *with the intent to promote the carrying on of specified unlawful activity; or*

<sup>100</sup> Financial Action Task Force, "Anti-Money Laundering and Counter-Terrorist Financing Measures - United States Mutual Evaluation Report" [US Mutual Evaluation Report (2016)] (FATF, 2016) at 64-65, online: <<http://www.fatf-gafi.org/media/fatf/documents/reports/mer4/MER-United-States-2016.pdf>>.

<sup>101</sup> *Ibid* at 64-65.

- (ii) with intent to engage in conduct constituting a violation of section 7201 or 7206 of the Internal Revenue Code of 1986; or
- (B) *knowing that the transaction is designed in whole or in part—*
  - (i) *to conceal or disguise the nature, the location, the source, the ownership, or the control of the proceeds of specified unlawful activity; or*
  - (ii) *to avoid a transaction reporting requirement under State or Federal law,*

shall be sentenced to a fine of not more than \$500,000 or twice the value of the property involved in the transaction, whichever is greater, or imprisonment for not more than twenty years, or both. For purposes of this paragraph, a financial transaction shall be considered to be one involving the proceeds of specified unlawful activity if it is part of a set of parallel or dependent transactions, any one of which involves the proceeds of specified unlawful activity, and all of which are part of a single plan or arrangement.

- (2) Whoever *transports, transmits, or transfers, or attempts to transport, transmit, or transfer a monetary instrument or funds from a place in the United States to or through a place outside the United States or to a place in the United States from or through a place outside the United States—*
  - (A) *with the intent to promote the carrying on of specified unlawful activity; or*
  - (B) *knowing that the monetary instrument or funds involved in the transportation, transmission, or transfer represent the proceeds of some form of unlawful activity and knowing that such transportation, transmission, or transfer is designed in whole or in part—*
    - (i) *to conceal or disguise the nature, the location, the source, the ownership, or the control of the proceeds of specified unlawful activity; or*
    - (ii) *to avoid a transaction reporting requirement under State or Federal law,*

shall be sentenced to a fine of not more than \$500,000 or twice the value of the monetary instrument or funds involved in the transportation, transmission, or transfer, whichever is greater, or imprisonment for not more than twenty years, or both. For the purpose of the offense described in subparagraph (B), the defendant's knowledge may be established by proof that a law enforcement officer represented the matter specified in subparagraph (B) as true, and the defendant's subsequent

statements or actions indicate that the defendant believed such representations to be true.

- (3) Whoever, with the intent—
- (A) to promote the carrying on of specified unlawful activity;
  - (B) to conceal or disguise the nature, location, source, ownership, or control of property believed to be the proceeds of specified unlawful activity; or
  - (C) to avoid a transaction reporting requirement under State or Federal law,

*conducts or attempts to conduct a financial transaction involving property represented to be the proceeds of specified unlawful activity, or property used to conduct or facilitate specified unlawful activity, shall be fined under this title or imprisoned for not more than 20 years, or both. For purposes of this paragraph and paragraph (2), the term “represented” means any representation made by a law enforcement officer or by another person at the direction of, or with the approval of, a Federal official authorized to investigate or prosecute violations of this section. [Emphasis added. The remainder of the section has not been included.]*

18 U.S. Code s.1957 – Engaging in monetary transactions in property derived from specified unlawful activity

- (a) Whoever, in any of the circumstances set forth in subsection (d), knowingly engages or attempts to engage in a monetary transaction in criminally derived property of a value greater than \$10,000 and is derived from specified unlawful activity, shall be punished as provided in subsection (b).
- (b)
  - (1) Except as provided in paragraph (2), the punishment for an offense under
    - this section is a fine under title 18, United States Code, or imprisonment for not more than ten years or both. If the offense involves a pre-retail medical product (as defined in section 670) the punishment for the offense shall be the same as the punishment for an offense under section 670 unless the punishment under this subsection is greater.
  - (2) The court may impose an alternate fine to that imposable under paragraph (1) of not more than twice the amount of the criminally derived property involved in the transaction.
- (c) In a prosecution for an offense under this section, the Government is not required to prove the defendant knew that the offense from

which the criminally derived property was derived was specified unlawful activity.

- (d) The circumstances referred to in subsection (a) are—
  - (1) that the offense under this section takes place in the United States or in the special maritime and territorial jurisdiction of the United States; or
  - (2) that the offense under this section takes place outside the United States and such special jurisdiction, but the defendant is a United States person (as defined in section 3077 of this title, but excluding the class described in paragraph (2)(D) of such section).
- (e) Violations of this section may be investigated by such components of the Department of Justice as the Attorney General may direct, and by such components of the Department of the Treasury as the Secretary of the Treasury may direct, as appropriate, and, with respect to offenses over which the Department of Homeland Security has jurisdiction, by such components of the Department of Homeland Security as the Secretary of Homeland Security may direct, and, with respect to offenses over which the United States Postal Service has jurisdiction, by the Postal Service. Such authority of the Secretary of the Treasury, the Secretary of Homeland Security, and the Postal Service shall be exercised in accordance with an agreement which shall be entered into by the Secretary of the Treasury, the Secretary of Homeland Security, the Postal Service, and the Attorney General.
- (f) As used in this section—
  - (1) the term “monetary transaction” means the deposit, withdrawal, transfer, or exchange, in or affecting interstate or foreign commerce, of funds or a monetary instrument (as defined in section 1956 of this title) by, through, or to a financial institution (as defined in section 1956 of this title), including any transaction that would be a financial transaction under section 1956 of this title, but such term does not include any transaction necessary to preserve a person’s right to representation as guaranteed by the sixth amendment to the Constitution;
  - (2) the term “criminally derived property” means any property constituting, or derived from, proceeds obtained from a criminal offense; and
  - (3) the terms “specified unlawful activity” and “proceeds” shall have the meaning given those terms in section 1956 of this title. [Emphasis added]

While the US statutory provisions are longer and more complex than their Canadian equivalents (discussed below), their overall effect is similar. Only the proceeds of certain crimes (“specified unlawful activity”) can give rise to a money laundering charge. The term “specified unlawful activity” is defined in 18 USC 1956(c)(7), and provides a long list of offenses that encompasses most serious crimes and includes violations of the *Foreign Corrupt Practices Act*. To be convicted, the accused must have known that the property in question was derived from unlawful activity of some kind. The two US provisions excerpted above include a variety of different uses that can give rise to a money laundering conviction, including attempting to avoid transaction reporting requirements and promoting the carrying on of a specified unlawful activity (funding further crimes). However, the overall effect is that money laundering consists of using the proceeds of certain defined crimes in certain defined ways.

Sentences for money laundering offenses are often lengthy and can reach a life term. From 2010-2015, prison sentences greater than 61 months (5 years) were imposed in 40% of convictions, while non-custodial sentences were used in only 15% of convictions. The table below outlines the sentences given in US federal money laundering cases from 2010-2014.

**Table 4.1** Sentencing for Money Laundering Convictions (FY2010-FY2014)

Offense	# of Defendants	Not imprisoned	1-12 Months	13-14 Months	25-36 Months	37-60 Months	61+ Months	Life
18 USC 1956	5076	784	341	520	456	823	2106	46
18 USC 1957	1253	174	81	145	112	249	486	6

Source: US Mutual Evaluation Report (FATF, 2016) at 74.

### Further Reading

For lawyers prosecuting or defending money laundering charges, the above provisions raise a host of issues. For a detailed analysis of the US money laundering provisions, including elements of the offences, possible defenses and sanctions, see Carolyn Hart, “Money Laundering” (Fall 2014) 51 Am Crim L Rev 1449.

Charles Doyle, “Money Laundering: An Overview of 18 U.S.C. 1956 and Related Federal Criminal Law” (Congressional Research Service, 2012), online: [www.crs.gov](http://www.crs.gov); *United States Code Annotated*, Title 18, ss1956 and 1957.

### 5.4.3 UK

In the UK, money laundering is criminalized by sections 327-329 of the *Proceeds of Crime Act, 2002* (POCA). Those provisions provide as follows:

327 Concealing etc

- 1) A person commits an offence if he—
  - (a) conceals criminal property;
  - (b) disguises criminal property;
  - (c) converts criminal property;
  - (d) transfers criminal property;
  - (e) removes criminal property from England and Wales or from Scotland or from Northern Ireland.
- 2) But a person does not commit such an offence if—
  - (a) he makes an authorised disclosure under section 338 and (if the disclosure is made before he does the act mentioned in subsection (1)) he has the appropriate consent;
  - (b) he intended to make such a disclosure but had a reasonable excuse for not doing so;
  - (c) the act he does is done in carrying out a function he has relating to the enforcement of any provision of this Act or of any other enactment relating to criminal conduct or benefit from criminal conduct.
- 3) Concealing or disguising criminal property includes concealing or disguising its nature, source, location, disposition, movement or ownership or any rights with respect to it.

328 Arrangements

- 1) A person commits an offence if he enters into or becomes concerned in an arrangement which he knows or suspects facilitates (by whatever means) the acquisition, retention, use or control of criminal property by or on behalf of another person.
- 2) But a person does not commit such an offence if—
  - (a) he makes an authorised disclosure under section 338 and (if the disclosure is made before he does the act mentioned in subsection (1)) he has the appropriate consent;
  - (b) he intended to make such a disclosure but had a reasonable excuse for not doing so;
  - (c) the act he does is done in carrying out a function he has relating to the enforcement of any provision of this Act or of any other enactment relating to criminal conduct or benefit from criminal conduct.

[The meaning of “suspicion” in section 328 has been the subject of some debate due to its subjectivity. The case law has indicated a preference for the



“more than fanciful possibility” test. It should also be noted that “arrangement” does not include legal proceedings.<sup>102]</sup>

### 329 Acquisition, use and possession

- 1) A person commits an offence if he—
  - (a) acquires criminal property;
  - (b) uses criminal property;
  - (c) has possession of criminal property.
- 2) But a person does not commit such an offence if—
  - (a) he makes an authorised disclosure under section 338 and (if the disclosure is made before he does the act mentioned in subsection (1)) he has the appropriate consent;
  - (b) he intended to make such a disclosure but had a reasonable excuse for not doing so;
  - (c) he acquired or used or had possession of the property for adequate consideration;
  - (d) the act he does is done in carrying out a function he has relating to the enforcement of any provision of this Act or of any other enactment relating to criminal conduct or benefit from criminal conduct.
- 3) For the purposes of this section—
  - (a) a person acquires property for inadequate consideration if the value of the consideration is significantly less than the value of the property;
  - (b) a person uses or has possession of property for inadequate consideration if the value of the consideration is significantly less than the value of the use or possession;
  - (c) the provision by a person of goods or services which he knows or suspects may help another to carry out criminal conduct is not consideration.

As the above provisions make clear, the UK’s domestic AML offences encompass a considerably larger range of acts than their equivalents in the US and Canada.

Section 340(3) of the *POCA* defines criminal property broadly. Property is criminal property if:

- (a) it constitutes a person’s benefit from criminal conduct or it represents such a benefit (in whole or part and whether directly or indirectly), and

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<sup>102</sup> Karen Harrison & Nicholas Ryder, *The Law Relating to Financial Crime in the United Kingdom* (Ashgate, 2013) at 14-15.

- (b) the alleged offender knows or suspects that it constitutes or represents such a benefit.

The person benefitting from criminal conduct need not commit the criminal act. The definition also includes property from anywhere in the world.

In the UK, unlike Canada and the US, there is no defined set of predicate offences for money laundering. There is also no need, under some of the provisions above, for any intent to conceal the source of the funds. The use or possession of the proceeds of any crime whatsoever can be prosecuted as money laundering. Under this regime, stealing and selling bicycles can give rise to money laundering charges. There is a requirement that the accused know that the proceeds in question were derived from criminal activity and a statutory defence if the accused reported the act as a suspicious transaction. Nonetheless, far more criminal activity is captured by this regime than in either the US or Canada.

Section 333 of the *POCA* also creates an offence of “tipping off.” The offence is committed where a person in the regulated sector tells a customer or third person that a money laundering investigation is underway or under consideration and where this disclosure is likely to be prejudicial.<sup>103</sup>

Sentencing guidelines for money laundering offences came into force October 1, 2014. For more information see Chapter 7, Section 5.

### **Further Reading**

For a detailed analysis of the provisions of the *Proceeds of Crime Act 2002*, see Edward Rees, QC, Richard Fisher & Richard Thomas, *Blackstone’s Guide to the Proceeds of Crime Act 2002*, 4<sup>th</sup> ed (Oxford University Press, 2011).

For a critical look at the success of the UK’s money laundering laws, see Peter Allan Sproat, “An Evaluation of the UK’s Money Laundering and Asset Recovery Regime” (2007) 47:3 *Crime, L & Soc Change* 169.

For more on the UK’s anti-money laundering regime and its weaknesses, see Karen Harrison & Nicholas Ryder, *The Law Relating to Financial Crime in the United Kingdom* (Ashgate, 2013) 9-37.

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<sup>103</sup> Stuart H Deming, *Anti-Bribery Laws in Common Law Jurisdictions* (Oxford University Press, 2014) at 166.

#### 5.4.4 Canada

Money laundering laws in Canada were first enacted in 1989 and were subsequently amended in 1997, 2001 and 2005.<sup>104</sup> The current money laundering offences are set out in sections 462.31(1) and 354(1) of the *Criminal Code*, which state:

Laundering proceeds of crime

**462.31** (1) Every one commits an offence who *uses, transfers the possession of, sends or delivers to any person or place, transports, transmits, alters, disposes of or otherwise deals with, in any manner and by any means, any property or any proceeds of any property with intent to conceal or convert that property or those proceeds, knowing or believing that all or a part of that property or of those proceeds was obtained or derived directly or indirectly as a result of*

- (a) the commission in Canada of a *designated offence*; or
- (b) an act or omission anywhere that, if it had occurred in Canada, would have constituted a designated offence.

Possession of property obtained by crime

**354.** (1) Every one commits an offence who has in his *possession* any property or thing or any proceeds of any property or thing *knowing* that all or part of the property or thing or of the proceeds was obtained by or derived directly or indirectly from

- (a) the commission in Canada of an *offence punishable by indictment*; or
- (b) an act or omission anywhere that, if it had occurred in Canada, would have constituted an offence punishable by indictment [Emphasis added].

There are three important aspects to section 462.31. First, it applies only to the proceeds of “designated offences.” The term “designated offence” is defined in section 462.3 of the *Criminal Code* as an offence that may be prosecuted as an indictable offence under Canadian legislation, unless is it expressly excluded by regulation. This means violations of the *Corruption of Foreign Public Officials Act* or bribery offences in the *Criminal Code* are included as designated offences. Second, while the range of actions that can constitute the *actus reus* of the offence is broad, there must be intent to conceal on the part of the accused. Finally, the accused must know or believe that the property or proceeds were derived from the commission of an indictable offence. An offence under section 462.31 is punishable by up to ten years imprisonment. Section 354(1) does not require any intent to conceal the source of

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<sup>104</sup> For a brief history of the development of money laundering laws in Canada, see Standing Senate Committee on Banking Trade and Commerce, “Follow the Money: Is Canada Making Progress in Combatting Money Laundering and Terrorist Financing? Not Really” (Ottawa: Senate Reports, March 2013), online: <<http://www.parl.gc.ca/Content/SEN/Committee/411/BANC/rep/rep10mar13-e.pdf>>.

the property or proceeds, but it requires specific knowledge that the property was derived from an indictable offence. Therefore, only certain uses of the proceeds of relatively serious crimes will be caught by these provisions.

Money laundering charges are typically laid along with a predicate offence such as bribery or drug trafficking. From 2010 to 2014, 1,800 money laundering charges were laid in 1,027 cases involving one or more counts of money laundering along with other offences. Prosecuting the money laundering is typically not prioritized in these circumstances. The tables below, reproduced from FATF’s 2016 mutual evaluation of Canada, show that while the conviction rate for these cases was 59.6%, the money laundering charge led to a conviction only 9.4% of the time.<sup>105</sup> Conversely, the money laundering charge was stayed 14.6% of the time and withdrawn 72.7% of the time. In FATF’s mutual evaluation of Canada, discussed in greater detail in Section 6.3.3 of this chapter, it is explained that insufficient evidence, avoidance of over-charging, plea bargaining, and length of proceedings in money laundering cases were some of the reasons why this is done.<sup>106</sup> Given the principle of totality in sentencing, pursuing a money laundering charge when there is already a conviction for the predicate offence may not greatly increase the sentence, and therefore prosecutors may believe their resources are better directed at crafting a plea bargain or focusing on the predicate offence.

**Table 4.2** Results of ML-Related Cases

	2010	2011	2012	2013	2014	Total	%
Guilty	82	108	140	136	146	612	59.6%
Acquitted	2	0	0	4	7	13	1.3%
Stayed	8	12	15	26	18	79	7.7%
Withdrawn	49	63	74	64	53	303	29.5%
Other Decisions	0	0	12	4	4	20	1.9%
<b>Total</b>	<b>141</b>	<b>183</b>	<b>241</b>	<b>234</b>	<b>228</b>	<b>1027</b>	<b>100%</b>

Source: Statistics Canada’s Integrated Criminal Court Survey (ICCS) as cited in Canada Mutual Evaluation Report (FATF, 2016) at 52.

<sup>105</sup> Financial Action Task Force, “Anti-Money Laundering and Counter-Terrorist Financing Measures - Canada Mutual Evaluation Report” [Canada Mutual Evaluation Report (2016)] (FATF, 2016) at 54, online: <<http://www.fatf-gafi.org/publications/mutualevaluations/documents/mer-canada-2016.html>>.

<sup>106</sup> *Ibid.*

**Table 4.3** Results of ML-Charges

	2010	2011	2012	2013	2014	Total	%
Guilty	38	21	35	31	44	169	9.4%
Acquitted	5	1	8	6	9	29	1.6%
Stayed	17	26	144	45	31	263	14.6%
Withdrawn	132	190	366	327	294	1309	72.7%
Other Decisions	2	2	14	7	5	30	1.7%
<b>Total</b>	<b>194</b>	<b>240</b>	<b>567</b>	<b>416</b>	<b>383</b>	<b>1800</b>	<b>100%</b>

Source: Statistics Canada's Integrated Criminal Court Survey (ICCS) as cited in Canada Mutual Evaluation Report (FATF, 2016) at 52.

Conviction rates for money laundering were higher in cases where that is the only charge laid. In a limited sample size of 35 single-charge money laundering cases from 2010 to 2014, 12 resulted in convictions, a 34.3% rate. Stays were imposed 14.3% of the time, a comparable proportion as when money laundering is charged with other offences, while withdrawals were far less frequent, occurring 40% of the time, compared to 72.7% when money laundering is charged alongside other offences.

Sentencing for money laundering ranges from non-custodial sentences to penitentiary terms. FATF suggests sanctions imposed in Canada for money launderers are low and not dissuasive enough. In 145 sentencing cases where money laundering was the most serious offence, nearly half received no prison time, and only 11% received over 2 years' incarceration.<sup>107</sup>

**Table 4.4** Sanctions in ML Cases where ML was the Most Serious Offence, from 2010 to 2014

	Number	Percentage
<b>Custodial Sentence</b>	<b>80</b>	<b>55.2%</b>
• Less than 12 months	47	32.4%
• 12 to 24 months	17	11.7%
• More than 24 months	16	11.0%
<b>Conditional sentence, probation, fine, restitution</b>	<b>65</b>	<b>44.8%</b>
<b>Total</b>	<b>145</b>	<b>100.0%</b>

*Note.* There are other undisclosed cases where the ML offence runs concurrently with another MSO. Source: Canada Mutual Evaluation Report (FATF, 2016) at 54.

### Further Reading

For a detailed legal analysis of Canada's money laundering offences see Terence D Hall, *A Guide To Canadian Money Laundering Legislation*, 4<sup>th</sup> ed (Lexis Nexis, 2015); Peter

<sup>107</sup> *Ibid* at 54.

M German, *Proceeds of Crime: The Criminal Law, Related Statutes, Regulations and Agreements* (Carswell, 1998) (loose-leaf, updated quarterly) ch. 5 and 6; *Anti-Money Laundering Law*, BC CLE Course Materials (BC CLE, May 2011); and Margaret Beare, *Criminal Conspiracies – Organized Crime in Canada*, (Oxford University Press, 2015), ch 6.

For a good critical analysis of money laundering in Canada and a claim as to its dubious benefits, see Margaret E Beare & Stephen Schneider, *Money Laundering in Canada: Chasing Dirty and Dangerous Dollars* (University of Toronto Press, 2007).

## 5.5 The Role of Legal Professionals

### 5.5.1 FATF Recommendations

FATF Recommendations 22 and 23 state that lawyers should be required to engage in CDD measures when performing transactions for clients and to report suspicious transactions. Many members of the legal profession and legal organizations such as the Canadian Bar Association have strongly opposed the inclusion of lawyers in these reporting regulations.<sup>108</sup> The interpretive note to Recommendation 23, reproduced below, modifies FATF's position somewhat:

Interpretive Note to Recommendation 23 (DNFBPS [designated non-financial businesses and professions] – Other Measures)

1. Lawyers, notaries, other independent legal professionals, and accountants acting as independent legal professionals, are not required to report suspicious transactions if the relevant information was obtained in circumstances where they are subject to professional secrecy or legal professional privilege.
2. It is for each country to determine the matters that would fall under legal professional privilege or professional secrecy. This would normally cover information lawyers, notaries or other independent legal professionals receive from or obtain through one of their clients: (a) in the course of ascertaining the legal position of their client, or (b) in performing their task of defending or representing that client in, or

<sup>108</sup> John A Kelley, "International Anti-Money Laundering and Professional Ethics" (2006) 40:2 Intl Lawyer 433. For an explanation of lawyer opposition to reporting requirements, see Kent Roach et al, "Sentries or Facilitators?: Law and Ethics in Trusting Lawyers with Money Laundering Prevention" (2004) 49 Crim LQ 34. For a comparative analysis of responses to the FATF recommendations in various jurisdictions (EU, UK, US, Canada, Australia and New Zealand) and an examination of the effects of gatekeeper obligations on the solicitor-client relationship, see Maria Italia, "Lawyers and Accountants as 'Gatekeepers' to Combat Money Laundering: An International Comparison" (2013) 42:2 Austl Tax L Rev 116.

concerning judicial, administrative, arbitration or mediation proceedings.

3. Countries may allow lawyers, notaries, other independent legal professionals and accountants to send their STR [suspicious transaction report] to their appropriate self-regulatory organisations, provided that there are appropriate forms of cooperation between these organisations and the FIU.
4. Where lawyers, notaries, other independent legal professionals and accountants acting as independent legal professionals seek to dissuade a client from engaging in illegal activity, this does not amount to tipping-off.

In this interpretive note, the FATF clarifies that its recommendations are tempered by the requirements of legal privilege and confidentiality, and leaves it in the hands of member states to decide how to implement an AML regime that respects those duties. Lawyers in the US, the UK and Canada are subject to different degrees of regulation. This variation is a function of a number of factors, principally legislative policy, the power of the bar and the constitutional structure of the country in question. For instance, after the government of Canada attempted to impose stringent regulations on the legal profession, the Federation of Law Societies successfully challenged these measures on constitutional grounds (further discussed at Section 5.5.4). In the UK, on the other hand, lawyers have been less successful in staving off state regulation of their practice.

There are two principal ways that lawyers must deal with state-level AML regimes. The first is regulation. Similarly to financial institutions, lawyers in some countries are subject to reporting, record-keeping and CDD requirements. The second is direct criminal liability. In some countries, AML laws are drafted in such a way that lawyers must be extremely careful to avoid prosecution for careless handling of funds or lack of due diligence in the ordinary course of their practice.

### 5.5.2 US

To date, the US has not taken serious steps to regulate lawyers as part of their AML regime. According to an article on the International Bar Association's Anti-Money-Laundering Forum:

the American legal system regards legal professional privilege as fundamental to the lawyer-client relationship. Therefore, it is disinclined towards modifying its current anti-money laundering legislation to include professionals such as lawyers. Trust and confidence are considered as keystone principles to the legal professional relationship. They would be eroded indefinitely, if lawyers were required to reveal information relating to the client to third parties, based upon mere suspicions. A client must feel

free to seek legal assistance and be able to communicate with his legal representative fully and frankly.<sup>109</sup>

US lawyers are not subject to any mandatory reporting requirements, with one exception. They are required to report any cash transaction greater than \$10,000 to the IRS.<sup>110</sup> Other than that, their work is outside the US AML regime.

US lawyers are also not likely to be caught by the country's anti-money laundering offenses in the ordinary course of their work. As discussed in Section 5.4, the US money-laundering offenses require that the accused have actual knowledge that the funds in question were derived from criminal activity. While some courts have held that willful blindness is sufficient to make out this element of the offence, it is still unlikely that a lawyer who was not knowingly complicit in a money laundering scheme could be successfully prosecuted.<sup>111</sup>

### 5.5.3 UK

Lawyers in the UK are in an unenviable position relative to their North American colleagues. They face significant potential criminal liability under section 328 of the *POCA*, even in the ordinary course of their practice. Section 328 targets those who assist in the layering and integration stages of the money laundering process. The Crown is required to establish that the accused entered into or became concerned in an arrangement that they knew or suspected "facilitates (by whatever means) the acquisition, retention, use or control of criminal property by or on behalf of another person." This provision is intended to catch financial advisors, accountants, lawyers and other professionals who assist in a money laundering scheme.

Section 328 is broad enough that even careless lawyers can be prosecuted. For example, in *R v Duff*, a solicitor was sentenced to six months imprisonment because he suspected that his client's funds had been criminally derived, but did not report his suspicions.<sup>112</sup> This came to light some years later when his client was arrested for cocaine smuggling.<sup>113</sup> There are statutory defences to a section 328 charge, but they require the accused either to have reported their suspicions or to have a reasonable excuse for their failure to do so. This regime forces lawyers to report any suspicions or face criminal charges.

The UK courts have limited the scope of section 328 somewhat. In the 2005 case of *Bowman v Fels*, the English Court of Appeal held that section 328 does not apply to lawyers involved in ordinary litigation or other dispute resolution processes who, as a result of the privileged

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<sup>109</sup> "Lawyers and Money Laundering", International Bar Association Money Laundering Forum, online: <[http://www.anti-moneylaundering.org/Lawyers\\_and\\_Money\\_Laundering.aspx](http://www.anti-moneylaundering.org/Lawyers_and_Money_Laundering.aspx)>.

<sup>110</sup> 26 USC s 6050I. This provision was unsuccessfully challenged in *United States v W Ritchie & Pc*, 15 F (3d) 592 (1994), 73 AFTR 2d 94-994, online: <<http://openjurist.org/15/f3d/592>>.

<sup>111</sup> Carolyn Hart, "Money Laundering" (2014) *Am Crim L Rev* 1449 at 1460.

<sup>112</sup> *R v Duff*, [2003] 1 Cr App R (S) 466.

<sup>113</sup> Edward Rees, QC, Richard Fisher & Richard Thomas, *Blackstone's Guide to the Proceeds of Crime Act 2002*, 4th ed (: Oxford University Press, 2011) at 130.



information they receive, come to suspect that the property at issue is criminal property.<sup>114</sup> The case involved a family law dispute. The claimant, Ms. Bowman, sought recognition of a proprietary interest in the defendant's home based on the doctrine of constructive trust. The claimant and the defendant had previously both lived in the house together in a common-law relationship. During the course of preparing for litigation, the claimant's solicitors began to suspect that the house may have been criminal property and became concerned that if they did not disclose their suspicions to the authorities that they would be held liable under section 328 for participating in an arrangement to aid their client in acquiring an interest in criminal property. The Court in *Bowman* clarified that the solicitors were in no such danger. Section 328 does not override the concept of legal privilege and therefore would not have applied to the acts of the solicitors of the claimant or the defendant.

However, the Court in *Bowman* did not address the position of lawyers who assist clients in matters not involving litigation. Therefore, the potential liability of lawyers acting in a transactional context remains uncertain.<sup>115</sup>

#### Further Reading

For further information on legal privilege in the context of UK anti-money laundering law see: The Law Society, "Chapter 6: Legal Professional Privilege" in *Practice Notes: Anti-Money Laundering*, online:

<<http://www.lawsociety.org.uk/advice/practice-notes/aml/legal-professional-privilege/>>.

#### 5.5.4 Canada

The Canadian government has tried unsuccessfully to subject lawyers to reporting and CDD requirements much like those imposed on financial institutions. When they were promulgated, the *Proceeds of Crime (Money Laundering) and Terrorist Financing Act and Regulations* applied to lawyers. They imposed reporting and CDD requirements and allowed searches of law offices and seizure of evidence. The application of the *Act* and *Regulations* to lawyers was challenged by the Federation of Law Societies on constitutional grounds. In a 2015 ruling, the Supreme Court upheld the Federation's position and read down the relevant

<sup>114</sup> *Bowman v Fels*, [2005] EWCA Civ 226.

<sup>115</sup> Edward Powles, "All that Glisters Is Not Gold: Laundering the UK Money Laundering Regime" (2006) 42 Cambridge LJ 40 at 42.

provisions to effectively exclude lawyers from the *Act* and *Regulations*.<sup>116</sup> The Federation has created model rules to deal with money laundering, which have been adopted by the provincial law societies.<sup>117</sup> The Federation's model rule on cash transactions states that "[a] lawyer shall not receive or accept from a person, cash in an aggregate amount of \$7,500 or more Canadian dollars in respect of any one client matter or transaction."<sup>118</sup> The B.C. Law Society Rule 3-59 also adopts the \$7,500 cash rule.<sup>119</sup> However, these rules are less comprehensive and generally impose less stringent requirements than the government's *Regulations*. The federal legislation and regulations require that financial institutions and other professionals, such as accountants or investment brokers, report all transactions of \$10,000 or more to FINTRAC. On the other hand, lawyers need not report cash transactions to anyone. The law societies take the position that when a cheque or electronic bank transfer of \$10,000 or more is received by a law firm, that money has already been subjected to the automatic FINTRAC reporting requirement (for \$10,000 or more) at the point of deposit of that money with a financial institution.

As in the US, Canadian lawyers are unlikely to be prosecuted for money laundering offences unless they deliberately facilitate a money laundering scheme. As discussed in Section 5.4.4, the Canadian offences require that the accused have actual knowledge that the funds in question were obtained through the commission of an indictable offence. Willful blindness,

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<sup>116</sup> *Canada (Attorney General) v Federation of Law Societies of Canada*, 2015 SCC 7. The SCC articulated a new principle of fundamental justice under section 7 of the *Canadian Charter of Rights and Freedoms*. The SCC held that it is a principle of fundamental justice that the state cannot impose duties on lawyers that undermine their duty of commitment to their clients' causes. The SCC stated that this duty is a basic tenet of the Canadian legal system, a distinct element of a lawyer's broad common law duty of loyalty and a fundamental part of the solicitor-client relationship. The Court noted that the lawyer's duty of commitment to the client's cause is essential to maintain confidence in the integrity of the administration of justice. Under the impugned regulations, lawyers must create and preserve records not required for client representation and the solicitor-client confidences contained in these records are not adequately protected against the sweeping warrantless searches authorized by sections 62-64 of the *PCMLTFA*, which violate section 8 *Charter* rights against search and seizure in law offices as set out in *Lavallee, Rackel & Heintz v Canada (Attorney General)*, 2002 SCC 61.

<sup>117</sup> The FLSC Model Code is available online: <<http://www.flsc.ca/en/federation-model-code-of-professional-conduct/>>. Rule 3.2-7 prohibits lawyers from "knowingly assist[ing] in or encourage[ing] any dishonesty, fraud, crime or illegal conduct, or instruct[ing] the client on how to violate the law and avoid punishment," including money laundering. The same prohibition is also found in Rule 3.2-7 of the BC Law Society *Code of Professional Conduct for BC*, online: <<https://www.lawsociety.bc.ca/page.cfm?cid=2638&t=Chapter-3---Relationship-to-Clients#3.2-7>>. For a useful description of the Law Society of B.C. rules, see Barbara Buchanan, "BC Lawyers and Professional Responsibility" in *Anti-Money Laundering Law* (Materials for CLE BC Seminar on *Anti-Money Laundering Law*, May 27, 2011), online: <<http://www.cle.bc.ca/>>.

<sup>118</sup> Federation of Law Societies of Canada, *Model Rule on Cash Transactions* (adopted by Council of the Federation of Law Societies of Canada as of July 2004), online: <<http://flsc.ca/wp-content/uploads/2014/10/terror1.pdf>>.

<sup>119</sup> Law Society of BC, *Law Society Rules 2015*, Rule 3-59, online: <<https://www.lawsociety.bc.ca/page.cfm?cid=4089&t=Law-Society-Rules-2015>>.

but not subjective recklessness, will normally suffice as actual knowledge.<sup>120</sup> Section 462.31(1) of the *Criminal Code* also requires some intent to conceal the source of the funds. Mere careless conduct on the part of a lawyer is unlikely to make out the offence.

### Further Reading

For a practical guide to lawyers' legal and ethical obligations regarding money laundering, see International Bar Association, American Bar Association & Council of Bars and Law Societies of Europe, *A Lawyer's Guide to Detecting and Preventing Money Laundering* (October 2014), online: <<http://www.lawsociety.org.uk/support-services/advice/articles/new-global-aml-guidance/>>.

For a comparative review of money laundering regimes in Canada and the US, see Ronan Reinart, "Laundering Around the World: Legislative Responses to Money Laundering in Canada, the US and Bermuda" (2004) 4 *Asper Rev Intl Bus & Trade L* 131 and Nicholas Ryder, *Money Laundering: An Endless Cycle? A Comparative Analysis of the Anti-Money Laundering Policies in the United States, the United Kingdom, Australia and Canada* (Routledge, 2012).

For a summary of various US and international AML developments, see Mikhail Reider-Gordon, "US and International Anti-Money Laundering Developments" (2011) Spring 2011 *Intl Lawyer* 365.

## 6. EVALUATING THE EFFECTIVENESS OF AML REGIMES

### 6.1 Introduction

This section discusses tools for evaluating the success or failure of state-level AML regimes and introduces the two most common international evaluators, the Basel Institute on Governance and the FATF. It describes both the Basel AML Index and the FATF mutual evaluation process and briefly summarizes how the US, the UK and Canada performed on each of these evaluations. It then excerpts a critical evaluation from the Canadian Senate and discusses some of the systemic barriers to creating effective state-level AML regimes.

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<sup>120</sup> See G Ferguson et al, *Canadian Criminal Jury Instructions* (Vancouver: CLE BC, 2017) at 6.60, user note before para 13.

## 6.2 The Basel AML Index

Since 2012, the Basel Institute on Governance has produced an annual index on anti-money laundering.<sup>121</sup> The Basel AML Index provides a useful tool for assessing and comparing *the risk* of money laundering in different countries worldwide and for observing over time changes to that risk within a given country.

The index is a composite weighting of the average of 14 indicators, relying on data provided by groups such as FATF, Transparency International and the World Bank.<sup>122</sup> For the 2016 report, data was available for 149 countries who were given a score from 0 (lowest risk) to 10 (highest risk).<sup>123</sup>

Factors weighed in the total score are:

- 65% - Money Laundering/Terrorist Financing Risk
- 15% - Financial Transparency & Standards
- 10% - Corruption Risk
- 5% - Public Transparency & Accountability
- 5% - Political Risk<sup>124</sup>

**Table 4.5** A sample of 20 countries and their scores and rankings from the 2016 Basel Index.

Country	Overall Score (0-10)	Rank (1-149)
Iran	8.61	1
Afghanistan	8.51	2
Panama	7.09	25
Nigeria	6.97	32
Brazil	6.23	56
Russia	6.22	58
Guatemala	5.97	66
Luxembourg	5.89	70

<sup>121</sup> As it describes itself, the Basel Institute is an “independent not-for-profit competence centre specialised in corruption prevention and public governance, corporate governance and compliance, anti-money laundering, criminal law enforcement and the recovery of stolen assets”: “Basel Institute on Governance”, online: <<http://index.baselgovernance.org/index/about>>.

<sup>122</sup> Basel Institute on Governance, “Basel AML Index 2016” (2016) at 12, online: <[https://index.baselgovernance.org/sites/index/documents/Basel\\_AML\\_Index\\_Report\\_2016.pdf](https://index.baselgovernance.org/sites/index/documents/Basel_AML_Index_Report_2016.pdf)>.

<sup>123</sup> To be included in the public version of the report, data must be available on 8 or more indicators including all three indicators assessing the money laundering/terrorist financing risk. An overview of 203 countries is available in an Expert Edition of the report, available free of charge to academics, public and supervisory institutions and NPO’s and for a fee to commercial institutions.

<sup>124</sup> These factors are determined by a number of sub-factors. For example, the money laundering/terrorist financing risk stems from FATF Recommendations (30%), TJN - Finance Secrecy Index (25%) and UN INCSR - Volume II on Money Laundering (20%). One exception is Corruption Risk, where the entire score stems from the TI CPI - Perception of Public Corruption.

Country	Overall Score (0-10)	Rank (1-149)
Japan	5.76	76
India	5.69	78
Switzerland	5.46	88
Italy	5.36	90
Germany	5.33	92
United States	5.17	97
Taiwan, China	5.12	99
France	5.03	103
Canada	5.00	105
South Africa	4.86	117
United Kingdom	4.77	121
Finland	3.05	149

It is important to note that the Index measures *risk* of money laundering and terrorist financing. In practice, factors relating to a country's financial sector and economy are important considerations for money launderers and can contribute significantly to the volume of laundering in any given country. For example, the US ranks 97<sup>th</sup> of 149 countries, meaning there are approximately 50 countries which have a lower risk for money laundering. However, that US ranking does not mean that all the countries which were ranked as lower money laundering risks are doing more, or are more effective, in trying to control and prevent money laundering. In practice, the majority of international money launderers choose not to operate in small, isolated economies. One study found that nearly half of the world's money laundering originates in the US, due in part to the dominance of US dollars in global markets and transactions.<sup>125</sup>

### 6.3 FATF Mutual Evaluations

FATF assesses compliance with its AML recommendations through a process of mutual evaluation. For the first three rounds of evaluation, countries were assessed on their technical compliance with the FATF recommendations. However, a new methodology was developed in 2013 to evaluate the *effectiveness* of AML regimes. This methodology is used in the ongoing fourth round of FATF evaluations, which began in mid-2014. So far, only Australia, Belgium, Ethiopia, Norway and Spain have undergone this revised evaluation process. The calendar of fourth round evaluations can be seen at: <http://www.fatf-gafi.org/media/fatf/documents/assessments/Global-assessment-calendar.pdf>.

Evaluations are carried out by teams of experts, described by FATF as follows:

An assessment team will usually consist of 4 expert assessors (comprising at least one legal, financial and law enforcement expert), principally drawn

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<sup>125</sup> Killian J McCarthy, "Why Do Some States Tolerate Money Laundering? On the Competition for Illegal Money" in Unger & van der Linde, eds., (2013) 127 at 138.

from FATF members, and will also include members of the FATF secretariat. Depending on the country and the money laundering and terrorist financing risks, additional assessors or assessors with specific expertise may also be required.<sup>126</sup>

Prior to 2014, countries were assigned a rating for compliance with each FATF recommendation. Possible ratings were C (compliant), LC (largely compliant), PC (partially compliant) or NC (non-compliant). After an evaluation, a country may be required to report back to the FATF at intervals to describe its progress in addressing any shortcomings identified by the evaluation team.

The US, UK and Canada have not yet undergone evaluations under the 2013 methodology and the third round of evaluations ended before the new FATF recommendations were released in 2012. Only Canada has undergone a follow-up report since 2012. Care must be exercised in using the FATF evaluations as a basis for comparing AML regimes in the US, UK, Canada and elsewhere. Also, the process for conducting mutual evaluations and the FATF Recommendations themselves have changed significantly over the past ten years. The mutual evaluations and follow-up reports on each member state were prepared at different times, and may not be directly comparable. The mutual evaluations are intended as a tool to assist countries to improve their AML regimes and to allow the FATF to exert peer pressure on reluctant countries. The evaluations are not a global comparative survey for scholarly analysis.

Nonetheless, the FATF mutual evaluation process provides the best primary data on global AML efforts and is an important source for surveys by other organisations, including the Basel Institute. The following sections summarize the most recent evaluations of the AML regimes in the US, the UK and Canada, focusing on any key weaknesses identified.

### 6.3.1 US

The United States had a FATF mutual evaluation in 2016, which like the previous evaluation in 2006 was generally positive. The United States has significant exposure to potential money laundering due to the global dominance of the US dollar. The US was one of the first countries to place significant focus on money laundering and has a developed anti-money laundering system.<sup>127</sup>

Of FATF's 40 recommendations, the US was found compliant with 11, largely compliant with 20, partially compliant with 6 and non-compliant with 3. The non-compliances related

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<sup>126</sup> "Procedures for the FATF Fourth Round of AML/CFT Mutual Evaluations" (FATF, 2014) at 6, online: <<http://www.fatf-gafi.org/media/fatf/documents/methodology/FATF-4th-Round-Procedures.pdf>>.

<sup>127</sup> US Mutual Evaluation Report (2016) at 5, 23.

to lacking trans-parency of beneficial ownership and the regulation of designated non-financial businesses and professions including lawyers, accountants and real estate agents.<sup>128</sup>

Mutual legal assistance from the US was positive. From 2009 to 2014, the US received 1,541 requests from MLA relating to money laundering, terrorist financing or asset forfeiture and recovery and granted the request in 1,062 of those cases.

**Table 4.6** Response to Incoming MLA Requests

Response to incoming MLA requests	ML	TF	Asset Forfeiture
Granted	568	53	501
Denied (grounds include lack of evidence, assistance not legally available, and other process reasons)	64	3	72
ML and asset forfeiture cases: Other reasons for not executing request (includes unable to locate evidence, withdrawn, and other non-process reasons)	150	N/A	102
TF cases: Other reasons for not executing request (includes no response from requestor, unable to locate evidence, and withdrawn)	N/A	14	N/A
Inexecutable under U.S. law	4	0	10
Total number of MLA requests related to ML, TF & asset forfeiture	786	70	685

Source: US Mutual Evaluation Report (FATF, 2016) at 164.

In the same years, 21 requests to extradite a money laundering suspect were made, resulting in 10 extraditions. Contested extraditions took an average of one year to resolve.

**Table 4.7** Response to Incoming Extradition Requests

Response to incoming extradition requests	ML	TF
Granted	10	0
Denied	3	0
Other (Includes cases withdrawn, fugitive not located, fugitive located in another country or fugitive arrested in requesting country)	6	0
Inexecutable under U.S. law	2	0
Total number of extradition requests related to ML & TF	21	0

Source: US Mutual Evaluation Report (FATF, 2016), at 165.

<sup>128</sup> *Ibid* at 255-259.

One beneficial aspect of the US system is the assigning of an attorney to US embassies in specific countries to assist in mutual legal assistance and extradition requests.<sup>129</sup>

Recommendations made in the FATF mutual evaluation include ensuring beneficial ownership information is required to be obtained at the federal level<sup>130</sup> as well as assessing and addressing exposure to the risk of money laundering by non-financial businesses and professions such as lawyers, accountants and real estate agents.<sup>131</sup>

### 6.3.2 UK

The last mutual evaluation of the UK took place in 2007. Overall, the assessment team concluded that the country's AML regime was effective. As the executive summary notes:

The UK has a comprehensive legal structure to combat money laundering and terrorist financing. The money laundering offence is broad, fully covering the elements of the Vienna and Palermo Conventions, and the number of prosecutions and convictions is increasing. The terrorist financing offence is also broad. The introduction of the *Proceeds of Crime Act 2002* (POCA) has had a significant and positive impact on the UK's ability to restrain, confiscate and recover proceeds of crime. The UK has also established an effective terrorist asset freezing regime. Overall, the UK FIU appears to be a generally effective FIU. The UK has designated a number of competent authorities to investigate and prosecute money laundering offences. Measures for domestic and international co-operation are generally comprehensive as well.<sup>132</sup>

However, the report noted that a key weakness in the regime was its failure to comply fully with Recommendation 5 (customer due diligence, which is now Recommendation 10 in the 2012 Recommendations).<sup>133</sup>

A follow-up report produced in 2009 describes the steps the UK had taken to address the deficiencies identified in the 2007 report. It concludes that:

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<sup>129</sup> *Ibid* at 167.

<sup>130</sup> *Ibid* at 38, 118, 154.

<sup>131</sup> *Ibid* at 135.

<sup>132</sup> Financial Action Task Force, "Summary of the Third Mutual Evaluation Report on Anti-Money Laundering and Combating the Financing of Terrorism: United Kingdom of Great Britain and Northern Ireland" (FATF, 2007) at 1, online: <<http://www.fatf-gafi.org/topics/mutualevaluations/documents/mutualevaluationofunitedkingdomofgreatbritainandnorthernireland.html>>.

<sup>133</sup> *Ibid* at 10-11. For a detailed breakdown of UK compliance with each FATF Recommendation at the time of the report, see the Mutual Evaluation Report Executive Summary at 10-15, online: <<http://www.fatf-gafi.org/media/fatf/documents/reports/mer/MER%20UK%20ES.pdf>>.



The UK has taken substantive action towards improving compliance with Recommendation 5, and nearly all of the deficiencies identified in the MER [mutual evaluation report] relating to the customer due diligence (CDD) framework have been addressed by the Money Laundering Regulations 2007. Although a few shortcomings remain, the UK has taken sufficient action to bring its compliance to a level essentially equivalent to LC [largely compliant].<sup>134</sup>

The full 2009 follow-up report is available online:

<<http://www.fatf-gafi.org/media/fatf/documents/reports/mer/FoR UK.pdf>>.

The UK has recently introduced a beneficial ownership law that requires disclosure in a publicly accessible registry of the beneficial ownership of companies and trusts. That law will greatly aid in the identification of money launderers. Mandatory disclosure of beneficial ownership is discussed more fully in Chapter 5, Section 5.2.2.

### 6.3.3 Canada

Canada had a FATF mutual evaluation in 2016, and that evaluation noted significant progress since the previous evaluation in 2007. The FATF report noted overall that “Canada has a strong framework to fight ML and TF, which relies on a comprehensive set of laws and regulations, as well as a range of competent authorities.”<sup>135</sup> Of the 40 FATF recommendations, Canada was found compliant with 11, largely compliant with 18, partially compliant with 6 and non-compliant with 5.<sup>136</sup> The non-compliant ratings resulted from the anti-money laundering legal obligations being inoperative in respect to lawyers, inadequate beneficial ownership laws (discussed in Chapter 5, Section 5.2.2 of this book) and failing to meet the standards for foreign politically exposed persons.<sup>137</sup> The latter concern was addressed through amended regulations to the *Proceeds of Crime (Money Laundering) and Terrorist Financing Act* in July 2016.

The evaluation states that most high-risk areas are governed by Canada’s AML/CTF framework, but finds that the exemption of legal counsel, law firms and Quebec notaries is a “significant loophole” in Canada’s framework.<sup>138</sup> This has a trickle-down effect throughout the AML/CTF regime. As the evaluation notes “[i]n light of these professionals’ key gatekeeper role, in particular in high-risk sectors and activities such as real-estate

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<sup>134</sup> Financial Action Task Force, “Mutual Evaluation Fourth Follow-Up Report: Anti-Money Laundering and Combating the Financing of Terrorism, United Kingdom” (FATF, 2009) at 4, online: <<http://www.fatf-gafi.org/media/fatf/documents/reports/mer/FoR UK.pdf>>.

<sup>135</sup> Canada Mutual Evaluation Report (2016) at para 12.

<sup>136</sup> *Ibid* at 205-209.

<sup>137</sup> *Ibid* at 205-209.

<sup>138</sup> *Ibid* at 31.

transactions and the formation of corporations and trusts, this constitutes a serious impediment to Canada's efforts to fight ML."<sup>139</sup>

The evaluation suggests that law enforcement results are not commensurate with Canada's money laundering risk and that asset recovery appears low. The report notes that some provinces appear more effective in asset recovery, citing Quebec as an example.<sup>140</sup> As discussed in Chapter 6, Section 3.1.2, Quebec is the only province to have a dedicated, multi-governmental anti-corruption agency.

As discussed in Section 5.4.4 of this chapter, the evaluation is also critical of the prosecution of money laundering cases, finding that there is a high percentage of withdrawals and stays of proceedings and that sanctions in money laundering cases are not sufficiently dissuasive.<sup>141</sup>

The evaluation commended Canada's mutual legal assistance system. From 2008 to 2015, Canada received 383 mutual legal assistance requests for money laundering offences. Canada provided assistance in 253 of these requests, while 17 were withdrawn, 36 abandoned and 7 refused. Feedback from 46 countries found that assistance provided by Canada is of good quality.<sup>142</sup>

Canada is also cooperative with extradition requests, although the process can be lengthy. From 2008 to 2015, Canada received 92 requests for extradition in money laundering cases, 77 of which came from the US. These resulted in 48 persons being extradited and 13 subject to other measures such as deportation or voluntary return.<sup>143</sup> As noted in Section 6.3.1 of this chapter, contested extradition from the US in money laundering cases is resolved in one year on average. The extradition process from Canada is lengthier, with 53% of cases taking 18 months to 5 years to complete, 28% from 3 to 5 years and 4% over 5 years.<sup>144</sup>

Recommendations stemming from the mutual evaluation included mitigating the risks posed by the exclusion of lawyers, law firms and Quebec notaries from the *MLTF Act*, engaging prosecutors at earlier stages in money laundering cases and ensuring asset recovery is pursued as a policy objective.<sup>145</sup>

## 6.4 Other Evaluations

As the previous two sections demonstrate, both the FATF and the Basel Institute are relatively positive about the performance of the US, the UK and Canada. However, in the case of the Basel Index this is a relative measure – it simply shows that many other countries

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<sup>139</sup> *Ibid* at 7.

<sup>140</sup> *Ibid* at 6.

<sup>141</sup> *Ibid* at 36.

<sup>142</sup> *Ibid* at 108-09.

<sup>143</sup> *Ibid* at 110.

<sup>144</sup> *Ibid* at 110.

<sup>145</sup> *Ibid* at 31, 37, 77, 87, 101.

in the world are doing worse in reducing or controlling their risk of money laundering. In the case of the FATF mutual evaluations, most of the focus is on implementation of the Recommendations. However, in some cases, even complete compliance with the FATF Recommendations may not produce an effective AML regime in practice. Some commentators have produced more critical reviews of the AML regimes discussed above.<sup>146</sup>

The excerpt below is from a 2013 Canadian Senate report entitled “Follow the Money: Is Canada Making Progress in Combatting Money Laundering and Terrorist Financing? Not Really.”<sup>147</sup> This Report was completed pursuant to section 72 of the *PCMLTFA*, which mandates that a Parliamentary Committee review the act every five years. As the title of the report suggests, the Senate committee found that there is little evidence that the *PCMLTFA*, FINTRAC and the rest of Canada’s anti-money laundering regime is effective at reducing or prosecuting money laundering. The Report goes on to suggest eighteen recommendations for reform. The following excerpt (pages 5-7) provides an overview of the Committee’s findings and recommendations:

BEGINNING OF EXCERPT

**B. The Impact**

Recognizing that Canada’s anti-money laundering and anti-terrorist financing legislation has had incremental changes over the past 11 years, the Committee believes that it is appropriate to examine the extent to which Canada’s Regime is effective in detecting and deterring the laundering of money and the financing of terrorist activities, and contributes to the successful investigation and prosecution of those who are involved in these criminal activities. The Committee is interested in the responses to several questions:

- Have the scope and magnitude of money laundering and terrorist financing in Canada diminished over time?
- Are the time, money and other resources dedicated to addressing these activities having sufficient “results?” and
- What changes are needed to bring about better “results?”

Throughout the hearings, the Committee questioned witnesses about the scope and magnitude of money laundering and terrorist financing in Canada. While the

<sup>146</sup> For example, Louis de Koker calls for an evaluation of FATF itself due to its power and lack of transparency in decision-making: Louis de Koker, “Applying Anti-Money Laundering Laws to Fight Corruption” in Graycar & Smith, eds, (2011) 340 at 356.

<sup>147</sup> Standing Senate Committee on Banking Trade and Commerce, “Follow the Money: Is Canada Making Progress in Combatting Money Laundering and Terrorist Financing? Not Really” (Ottawa: Senate Reports, March 2013), online:

<<http://www.parl.gc.ca/Content/SEN/Committee/411/BANC/rep/rep10mar13-e.pdf>>.

Committee learned that FINTRAC has a solid reputation internationally, witnesses shared only limited and imprecise information about the extent to which the Regime meets its objective of detecting and deterring money laundering and terrorist financing. The Committee believes that there continues to be a clear need for legislation to combat money laundering and terrorist financing in Canada.

The Committee feels that there is a lack of clear and compelling evidence that Canada's Regime is leading to the detection and deterrence of money laundering and terrorist financing, as well as contributing to law enforcement investigations and a significant rate of successful prosecutions. It is possible that some witnesses were unable to share confidential information in a public meeting. It is also possible that information about the success or failure of the Regime is not being collected. In any event, the Committee feels that the current Regime is not working as effectively as it should, given the time, money and other resources that are being committed by reporting entities, a variety of federal departments and agencies, other partners and taxpayers.

Given that multinational financial institutions have recently been implicated in money laundering and terrorist financing, the Committee is concerned about non-compliance with the Act by reporting entities. While the majority of non-compliance charges laid in Canada are in relation to cross-border reporting offences, the Committee is aware of the July 2012 report by the United States (U.S.) Senate Permanent Subcommittee on Investigations of the U.S. Senate Committee on Homeland Security and Governmental Affairs, entitled *U.S. Vulnerabilities to Money Laundering, Drugs, and Terrorist Financing: HSBC Case History*, in relation to HSBC and money laundering using international wire transfers. [In 2013, HSBC paid \$1.9 billion to settle money laundering charges filed by the US Department of Justice.<sup>148</sup>] The U.S. Senate Committee made several recommendations designed to strengthen anti-money laundering and anti-terrorist financing controls, particularly in relation to large, multinational financial institutions with affiliates in jurisdictions that are considered to be at high risk of being targeted by money launderers and those who finance terrorism. As financial institutions play a critical role in preventing illicit money from entering the financial system, the Committee feels that FINTRAC must be vigilant in ensuring that Canada's reporting entities comply with their obligations under the Act.

The Committee believes that an approach involving incremental legislative and regulatory changes must end. Consequently, ongoing efforts are needed to ensure that the resources committed to detecting, deterring, investigating and prosecuting money laundering and terrorist financing offences have the best "results" in the least costly,

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<sup>148</sup> "HSBC's \$1.9B Money Laundering Settlement Approved by Judge", *CBC News* (3 July 2013), online: <<http://www.cbc.ca/news/business/hsbc-s-1-9b-money-laundering-settlement-approved-by-judge-1.1377272>>.

burdensome and intrusive manner. While it is virtually impossible to eliminate the illegal activities that lead to the need to launder money, a continuation of the current incremental approach – which appears to involve changes to fill gaps by adding reporting entities and to meet evolving FATF recommendations that may or may not have relevance for Canada – is not the solution that Canada needs at this time.

Having conducted a comprehensive study, the Committee’s view is that the Act should be amended to address three issues:

- the existence of a structure for Canada’s Regime that leads to increased performance in relation to the detection, deterrence, investigation and prosecution of money laundering and terrorist financing;
- the existence of information-sharing arrangements that ensure that suitable information is being collected and shared with the right people at the appropriate time, bearing in mind the need to protect the personal information of Canadians; and
- the existence of a scope and focus for the Regime that is properly directed to ensuring that individuals and businesses report the required information to the appropriate entity in an expedient manner.

The time for incremental change to the Regime has ended. The time for examination of fundamental issues has arrived.

END OF EXCERPT

Some commentators criticize the high costs of AML measures for businesses and society and question whether these costs are worth the potentially negligible benefits of AML regimes.<sup>149</sup> See, for example, Michael Levi & Peter Reuter, “Money Laundering” (2006) 32:1 *Crime and Justice* 289.

### Further Reading

For a detailed cost-benefit analysis of AML laws in a hypothetical EU country, see Joras Ferwerda, “Cost-benefit analysis” in Brigitte Unger et al., eds, *The Economic and Legal Effectiveness of the European Union’s Anti-Money Laundering Policy* (Edward Elgar Publishing, 2014) 205.

<sup>149</sup> The UK has embarked on a review of the country’s AML regime with the goal of making the system more efficient and less costly for businesses. See: Department of Business, Innovation and Skills, Press Release, “Financial Red Tape Targeted in New Review” (28 August 2015), online: <<https://www.gov.uk/government/news/financial-red-tape-targeted-in-new-review>>.

For a detailed analysis of money laundering regulation in 80 countries with the aim of determining which regulations are most effective in curtailing money laundering and predicate offences, see Alberto Chong & Fernando Lopez-de-Silanes, "Money Laundering and its Regulation" (March 2015) 27:1 Economics and Politics 78.

## 6.5 Barriers to Creating Effective AML Measures

There are a variety of reasons why it is difficult to create effective AML measures. First, there are the difficulties posed by the lack of information available to legislators at the national and international level. There is no accurate estimate of the global scope of money laundering or its extent in any particular country. This makes it difficult to evaluate the success of any particular AML measure, since we cannot accurately measure the impact of any such measure. The secrecy surrounding government and FIU information also poses a challenge to those researching the effectiveness of AML measures.<sup>150</sup>

Investigation of money laundering also presents many problems, such as the morass of data and the length of time between a corrupt act and its discovery.<sup>151</sup> A further difficulty is that a successful AML regime relies heavily on the cooperation of the financial sector, which may have much more money to gain by facilitating money laundering than stopping it. As Beare and Schneider note in their 2007 book *Money Laundering in Canada*:

The rhetoric of financial institutions come across as if all of the objectives of the banks are equal: profit, risk management, customer satisfaction, *and* a sense of societal/corporate responsibility towards the reduction of money laundering. In reality, these goals are often seen to be contradictory and are not given equal attention. As we have noted, a focus on profitability runs throughout the banking sector. Picking up on the 'what gets measured and gets rewarded, gets done' line of reasoning (Bogach and Gordon, 2000), it is important to consider the reward system within those institutions that have claimed to implement sound voluntary codes, especially where those codes might work against other rewarded objectives. During the US Senate's 1999 review of the operations of private banking, one bank official stated that 'no-one took the "know-your-customer" policies seriously until bonuses were threatened.' The internal study of bank defalcations [failure to repay loans] within Canadian financial institutions revealed a maze of individual, departmental, and branch incentives that were offered based on performance. These individual and group rewards were so coveted that they were seen to be partially responsible for overzealous banking decisions

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<sup>150</sup> de Koker (2011) 340 at 354.

<sup>151</sup> Charles Monteith, "Case and Investigation Strategy" in Gretta Fenner Zinkernagel, Charles Monteith & Pedro Gomes Pereira, eds, *Emerging Trends in Asset Recovery* (Peter Lang AG, International Academic Publishers, 2013) 183.

(e.g., unwise loans and credit lines). Peer pressure from group incentives was particularly powerful. Hence any policy that resulted in the loss of customers – especially customers with large amounts of money – operated against the current reward structure. Banks are organized around the concept of attracting funds, and few banks reward those who turn money away.<sup>152</sup>

Gordon further criticizes this reliance on the private sector to report transactions and keep records. He calls for a greater role for the public sector and FIUs in AML efforts.<sup>153</sup> The recent movement to require public disclosure of the beneficial owners of shell companies and trusts is discussed in Chapter 5, Section 5.2.2 of this book.

Fletcher and Hermann outline several other challenges for AML regimes.<sup>154</sup> Political immunity of high-level politicians may block prosecution of money laundering offences. Corrupt officials may also use AML measures to freeze funds of their opponents and can frustrate the efforts of law enforcement in other countries to gather evidence against themselves or their government. Bank secrecy laws continue to pose a challenge to AML efforts, although strict secrecy has been relaxed due to FATF blacklisting and increased international pressure since September 11, 2001. Finally, Fletcher and Hermann note that the creation of FIUs is expensive for developing countries, and the effectiveness of FIUs has been questioned in less advanced, cash-oriented economies.

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<sup>152</sup> Margaret E Beare & Stephen Schneider, *Money Laundering in Canada: Chasing Dirty and Dangerous Dollars* (University of Toronto Press, 2007) at 214–216.

<sup>153</sup> Richard K Gordon, “Losing the War against Dirty Money: Rethinking Global Standards on Preventing Money Laundering and Terrorism Financing” (Spring 2011) 21:3 *Duke J Comp & Intl L* 503.

<sup>154</sup> Clare Fletcher and Daniela Herrmann, *The Internationalisation of Corruption* (, 2012) at 177-179.