7
Criminalising Money Laundering

7.1 Scope of the Criminal Offence of Money Laundering

Criminalising money laundering must be the starting point of any credible anti-money laundering strategy and it is now generally accepted that the international standard for a money laundering offence is one based on serious crimes

FATF Recommendations 1–3 require that:

(i) Countries should criminalise money laundering on the basis of the Vienna and Palermo Conventions.

(ii) Countries should apply the crime of money laundering to all serious offences with a view to including the widest range of predicate offences, for example taking a threshold approach to all offences carrying a sentence of one year or more or which are punishable by a minimum penalty of six months of more.

(iii) As a minimum, a range of offences within each of the following designated categories of offences should be included:

- Participation in an organised criminal group and racketeering;
- Terrorism, including terrorist financing;
- Trafficking in human beings and migrant smuggling;
- Sexual exploitation, including sexual exploitation of children;
- Illicit trafficking in narcotic drugs and psychotropic substances;
- Illicit arms trafficking;
- Illicit trafficking in stolen and other goods;
- Corruption and bribery;
- Fraud;
- Counterfeiting currency;
- Counterfeiting and piracy of products;
- Environmental crime;
- Murder or grievous bodily injury;

- Kidnapping, illegal restraint and hostage-taking;
- Robbery or theft;
- Smuggling;
- Extortion;
- Forgery;
- Piracy; and
- Insider trading and market manipulation.

(iv) Predicate offences for money laundering should at least extend to offences committed in another country which constitutes an offence in that country and which would have constituted an offence if committed domestically.

(v) Criminal liability and/or civil or administrative liability should apply to legal persons as well as to individuals.

(vi) Legislative measures should include the power to identify, trace, freeze, seize and confiscate criminally obtained or laundered property.

7.2 The Elements of the Vienna Convention

The elements of the Vienna Convention laundering offence, together with illustrations of some of the forms they might take in practice, are set out below.

- **Conversion** – this would include the exchange of one currency for another or the exchange of cash for travellers cheques or other negotiable instruments or securities. It would cover the trading of securities. It could be taken to include the acceptance of cash or cheques for deposit in an account – converting the money into an accounting record.
- **Transfer** – this would cover any form of money transmission service, including wire transfer.
- **Concealment** – this might be taken to cover acceptance of deposits, and also activities such as the establishment of trusts or companies to hold assets.
- **Disguising the true nature, source, location, disposition, movement, rights with respect to, and/or ownership** – this is very similar to concealment, and would particularly include offshore trust and company formation activities.
- **Acquisition** – this might include the receipt of funds through correspondent accounts with other financial institutions, or acceptance as a trustee.

- **Possession** – again, this might cover holding funds on behalf of another party, particularly when there is a degree of discretion over the disposition of the funds.
- **Use** – this might cover discretionary investment of funds held for a client.
- **Participation, association, conspiracy, attempting, aiding, abetting, facilitating and/or counselling** – this might cover a wide range of advisory services, including investment advice and brokerage services.

7.3 The Elements of the Palermo Convention

The Palermo Convention established the requirement to combat four distinct areas of activity which are commonly used in support of transnational organised crime.

Under Article 5 participating in the activities of an 'organised criminal group' and 'organising, directing, aiding, abetting, facilitating or counselling' serious crimes involving organised criminal groups must be made offences.

Under Article 6 activities relating to 'money laundering' must be criminalised. This extends not only to cash but to any form of property which is the proceeds of crime, and includes any form of transfer or conversion of the property for the purpose of concealing its true origin. Simple acquisition or possession is also included if the person in possession knows that the property is the proceeds of crime.

Under Article 8 corruption must be criminalised where there is a link to transnational organised crime. These include offering, giving, soliciting and accepting any form of bribe, undue advantage or other inducement, where the proposed recipient is a public official and the purpose of the bribe relates to his or her official functions.

Under Article 23 participating states are required to criminalise any form of obstruction of justice, including the use of corrupt means (e.g. bribery or physical coercion) to influence testimony, other evidence or the actions of any law enforcement or other justice official.

Article 2 defines an 'organised criminal group' as one having:

- At least three members;
- The intention of taking action in concert for the purpose of committing a serious crime to derive a financial or other benefit;
- Some internal organisation or structure;
- Existed for some period of time before or after the actual commission of the offences involved.

Three protocols cover the specific crimes of:

- Trafficking in persons;

- Smuggling of migrants;
- Smuggling or illicit manufacture of firearms.

The provisions of the Convention which deal with extradition and mutual legal assistance are similar to provisions already in place in many regional or bilateral agreements. However, their significance is that the Convention is expected to be ratified by a large number of countries making legal assistance and extradition more widely available than previously.

Article 24 requires participating states to adopt appropriate measures to protect witnesses from potential intimidation or retaliation.

Articles 29 and 30 encourage the development of domestic training programmes and the provision of technical assistance to other less developed countries.

7.4 The Commonwealth Model Law

To assist Commonwealth countries to develop their national legislation, the Commonwealth Secretariat has produced a model law for the Prohibition of Money Laundering (known as 'the Model Law'). The Model Law is intended for use by common law countries and covers all of the issues addressed by the FATF Recommendations. An 'all serious crimes' money laundering offence was included.

Heads of Government, at their meeting in Auckland in November 1995, agreed that a common legislative approach would facilitate international co-operation and invited member states to draw benefit from the Model Law. The Model Law has been updated during 2003 to reflect the developing international standards.

7.5 The Inclusion of Economic Crimes within Money Laundering Offences

A number of countries have deregulated their economies in order to improve the efficiency of production and use of resources. However, the trend towards financial and economic deregulation has both a positive and a negative impact on the problems of economic crime. On the positive side, by removing the regulations and restrictions that are subject to abuse, certain forms of economic crime automatically fall away. For instance, it is impossible to have a crime of exchange control evasion if there are no exchange controls.

At the same time, deregulation brings freedoms that can be abused by criminals, particularly those involved in other forms of activity that remain as economic crimes, such as tax evasion and corruption. Many countries suffer from high levels of economic crime which hinder their efforts to achieve sustainable economic growth.

It is important therefore to consider:

- How any approaches to tackling money laundering can additionally be used to combat the laundering of the proceeds of economic crime; and
- What steps can be taken to monitor large inflows and outflows of capital/currency once regulations and restrictions are removed.

7.5.1 Tax Evasion

The inclusion of tax evasion within the predicate offences for the criminalisation of money laundering is clouded by the perception that tax evasion is a domestic crime as opposed to an internationally recognised serious crime such as drug trafficking.

Public attitudes towards tax evasion are complicated by the generally held view that the payment of tax is something to be avoided whenever possible. This view generates an ever-growing 'tax planning' industry, serving corporations and individuals (particularly wealthy individuals) and advising them on how to minimise their tax liabilities. This often involves running as close as possible to the line that separates what is legal – tax minimisation – from what is illegal – tax evasion.

While countries that include all serious crimes within the definition of money laundering do not place tax-related offences in a special category from other serious crimes, many countries have taken the decision specifically to exclude tax-related offences from their money laundering legislation. In some countries, tax offences are still subject to the money laundering legislation, but information that might relate to the laundering of the proceeds of fiscal offences is not passed to the revenue authorities until another criminal offence is proved. Other countries, however, have involved their revenue authorities directly in their anti-money laundering regimes, and can effectively offset some or all of the costs of their operations against recovered tax revenues as well as against the confiscated proceeds of other crimes.

Evidence shows that where tax evasion has become a normal activity within a particular country, the inclusion of tax evasion within the activities constituting serious crime can significantly improve government finances through increased levels of tax recovery.

Tax Evasion as a Smokescreen

The lack of consistency in the treatment of tax evasion has provided an additional opportunity for the criminals. Money launderers involved in other crimes such as drug trafficking have frequently used tax reasons as a smokescreen for their unusual or abnormal transactions or instructions. In recognition of this growing practice. The interpretative note to FATF Recommendation 13 states that:

> *In implementing Recommendation 13, suspicious transactions should be reported by financial institutions regardless of whether they are also thought to involve tax matters. Countries should take into account that, in order to deter financial institutions from reporting*

suspicious transactions, money launderers may seek to state inter alia that their transactions are related to tax matters.

In addition FATF Recommendation 40 concerning international co-operation provides that:

Exchanges (of information) should be permitted without unduly restrictive conditions. In particular:

a) Competent authorities should not refuse a request for assistance on the sole ground that the request is also considered to involve fiscal matters.

7.6 Bribery and Corruption

Bribery and corruption raise problems of definition and ethics. In many countries the practice of offering bribes in order to obtain a contract or other advantage has become a normal part of business life. Likewise, public sector corruption, i.e. the abuse of public office for private gain has become endemic in some countries. Corruption damages development and the possibility of laundering the proceeds of corruption through the world's financial systems allows it to grow to a massively larger scale than would otherwise be possible. Significant international initiatives are now in place to tackle the problems of bribery and corruption.

7.6.1 The OECD Bribery Convention

One of the major international achievements has been the conclusion of the OECD Convention on the bribery of foreign public officials in the course of international business transactions (the OECD Bribery Convention). Specifically, the Convention provides that the making or receiving of a bribe should be made a criminal offence and provides for the seizure of the bribe or the proceeds of the bribe.

7.6.2 Grand Corruption

Corruption has been defined by the world bank as 'the abuse of public office for private gain'. Transparency International defines it as 'the abuse of entrusted power for private gain'. Whatever the definition, corruption invariably taints reputations and practices, infects political processes and economic stability, and generally deprives one person or group of persons to the benefit of another person or interest.

Corruption is not only a major disincentive to healthy economies growth, but it is also a major disincentive to outside investment and long term aid.[4]

The corrupt diversion of government funds and international aid money has become a significant problem for some Commonwealth countries and for many countries steps to combat corruption have become a prerequisite for contained international support. Corrupt government officials generally wish to place the proceeds form their corrupt acts

beyond the sight and reach of their own home jurisdictions. The illegally diverted funds concerned are generally laundered through bank accounts, companies or trusts set up in other countries or offshore financial centres. Most financial institutions do not willingly seek to acquire such funds, and many are increasingly refusing to accept them if they are identifiable. The criminal and civil liabilities for banks and others who knowingly or unwittingly launder the proceeds can be significant in addition to the reputational risks.

Financial institutions that know their customers and the sources of their wealth and income can usually be expected to recognise abnormal financial flows and could be expected to become suspicious of the large financial flows generated by corrupt payments. Those funds can then be reported to the relevant authorities and the process of returning them can commence. However, difficulties arise in practice when the financial institution does not know that a foreign customer is a public sector official with potential access to substantial government funds. While there may be no doubt in relation to heads of state and other very prominent individuals, many will not be recognisable as such.

Commonwealth countries that are vulnerable to high levels of corruption or diverted aid funds may therefore consider maintaining a list of individuals who fall in this category. This could then be made available to international banks through their supervisory bodies and would permit all banks to monitor the accounts of political customers or family members and assist in the reporting of transactions that might be linked to corruption.

7.7 Secrecy versus Confidentiality

Banking confidentiality is widely recognised as playing a legitimate role in protecting the confidentiality of the financial affairs of individuals and legal entities.

This right derives from the general principle of privacy and the concept that the relationship between a banker and his customer obliges a bank to treat all its customers' affairs as confidential. All countries provide, to a greater or lesser extent, the authority and obligation for banks to refuse to disclose customer information to ordinary third parties.

In common law countries, the circumstances when the common law duty of confidentiality between a financial institution and its customers may be breached are set out in the Tournier decision (*Tournier v National Provincial and Union Bank of England 1924*). The three most important of these circumstances in the context of money laundering are:

- when the bank is required by law to breach confidence;
- when breach of confidence is necessary in the bank's own interests; and
- when breach of confidence is in the legitimate public interest.

Money laundering legislation normally defines circumstances under which a financial

institution is required to disclose information to a designated authority and the financial institution is therefore protected from suit for breach of confidentiality by the need to disclose under compulsion of law.

Where banking confidentiality is enshrined in statute, it may be necessary to ensure that money laundering legislation provides adequate gateways (with appropriate checks and balances) through the confidentiality provisions to permit the disclosure of suspicions. Most confidentiality legislation permits financial institutions to pass on knowledge of criminal activity to the authorities coupled with explicit statutory protection from breach of customer confidentiality.

However, some Commonwealth countries extend customer confidentiality beyond the common law right, to the statutory right to secrecy. In these cases, legislation will usually provide that banks and other financial institutions must keep information concerning their affairs secret. Any person who discloses information relating to the identity, assets, liabilities, transactions and accounts of a customer will commit a criminal offence.

To be effective, money laundering legislation must allow financial institutions to pass on their knowledge and their suspicions of money laundering to the relevant authorities. The continued existence of banking secrecy legislation, rather than merely a customer's right to confidentiality, will prohibit the development of an effective anti-money laundering strategy.

Commonwealth countries should also be aware that if banking secrecy legislation prohibits disclosure of customer information in response to a Foreign Court Order or a US subpoena in respect of a criminal investigation, that country will be officially classified by the FATF as a non co-operative jurisdiction (see Chapter 4, section 4.4).

7.8 Implementing a Requirement to Report Knowledge/Suspicion of Money Laundering

In order for a national strategy to succeed, it is essential that financial institutions and professional firms (and within them, individual members of staff) are required, by statute, to report any knowledge or suspicion of money laundering.

7.8.1 Determining Reporting Requirements

The FATF Recommendations recognise two different approaches to the task of reporting.

Firstly, institutions should be required to report knowledge or suspicion of money laundering related to specific customer or transactions; this is known as suspicious transaction or suspicious activity reporting. FATF Recommendation 13 states:

If a financial institution suspects or has reasonable grounds to suspect that funds are the

proceeds of criminal activity or are related to terrorist financing, it should be required directly by law or regulation to report promptly its suspicions to the Financial Intelligence Unit (FIU).

The inclusion of the words 'or has reasonable grounds to suspect' introduces into Recommendation 13 a new objective test of suspicion. This enhanced requirement is discussed in greater detail in Chapter 12.

Secondly, institutions can be required to undertake routine reporting of transactions above a specified threshold; this is known as currency transaction reporting. FATF Recommendation 19b states:

Countries should consider the feasibility and utility of a system, where banks and other financial institutions and intermediaries would report all domestic and international currency transactions above a fixed amount to a national central agency with a computerised data base, available to competent authorities for use in money laundering or terrorist financing cases, subject to strict safeguards to ensure proper use of information.

7.8.2 Suspicious Transaction/Activity Reporting

The idea that financial institutions should spontaneously report to the authorities, transactions that they have conducted merely because they are suspicious of those transactions or consider them to be unusual is perhaps the most radical element of the approach to combat money laundering. It often runs counter to other legislative/contractual commitments and counter to the natural instincts of most financial institutions, which place very strong emphasis on customer confidentiality.

Why Should Financial Institutions Report Suspicious Transactions or Activity?

Where Recommendation 13 has been adopted, financial institutions, professional firms and other designated businesses will commit an offence if they do not report their suspicions of money laundering. However, there are two other reasons why financial institutions should co-operate in combating money laundering by disclosing details of suspicious transactions.

The first, is essentially a moral one. Regulated financial institutions and professional firms in particular are expected to be 'good citizens' who have a duty to uphold the law, and this duty may at times override the duty of confidentiality that they owe to their customers, if there is legitimate suspicion of wrong-doing. This issue of confidentiality is discussed in more detail below.

The second reason, for any financial or non-financial business to report suspicious transactions is that of simple self-interest – protecting themselves from fraud and protecting their reputation. The basis of trust on which the financial and professional systems operate can easily be undermined by the involvement of financial institutions or professional firms in criminal activity, even if the involvement was unintentional.

Any financial institution or professional firm that discovers it is holding criminal proceeds may be subject to criminal penalties under the common law (as an aider or abettor) or to a civil suit for constructive trust, even in the absence of money laundering legislation. By disclosing its situation to the authorities, a financial institution will to put itself in a safer position.

The options for establishing a central agency to receive and evaluate the suspicion reports is set out in section 9.1.

7.8.3 Protection for the Reporting Institution

While the legal situation protects reporting institutions from civil action by clients or criminal liability for breach of confidence, it does not protect staff from reprisals if the fact that a disclosure has been made becomes known to the customer. This possibly becomes significantly more acute if the report is made direct to the law enforcement agencies from the member of staff who is handling the transaction.

In some countries, legislation requires the identification of a senior manager within the institution who will be given responsibility for considering all 'suspicions', deciding if they should be passed to the authorities, and generally controlling the institution's reporting procedures. This role is often referred to as 'the Money Laundering Officer'.

7.8.4 Currency Transaction Reporting

Under a CTR regime, financial institutions report any transaction or transfer of funds above a fixed threshold to a central agency. This information is then put on a database and made available to investigators.

CTR regimes can impose significant compliance costs on financial institutions and their customers and, if the reporting threshold is set at an inappropriate level, can lead to the agency to which the reports are being sent being overloaded with information. This in turn will prevent the ability to analyses the information such that the money laundering transactions can be identified. However, from the government viewpoint, a well-run CTR system can potentially cover its costs. If resources and expertise were available to establish and maintain a computer-based CTR system, and the data was made available to revenue authorities to use to pursue tax evasion, this might be an attractive option for some Commonwealth governments.

A CTR system is often deemed to prove helpful in three situations:

- Where it is considered that the quality and educational standards of many staff, or the standard of the systems, within financial institutions are insufficient to exercise and apply the judgement necessary in a suspicion-based reporting regime. This may be considered a short-term phenomenon, and implementing a routine CTR system may be an expedient starting point (legislation permitting);
- As a first step in monitoring and reporting. With money laundering, one of the choke

«points is at the point of conversion of notes into instruments (cheques, money transfer orders, etc.), with the most likely being the conversion of convertible currencies. Therefore, in the early stages of a strategy, the routine reporting of convertible currency transactions (thus excluding the more numerous domestic currency transactions) may be an effective option;

- The application of money laundering legislation to tax evasion and other forms of economic crime has the potential to improve government finances through increased levels of tax recovery. Where the fiscal benefits are potentially very high, there is scope for the introduction of a CTR system.

Often the most effective anti-money laundering regimes require both CTR and suspicion-based reporting, but CTR alone has been found to be ineffective.

7.8.5 Reporting International Capital/Currency Movements

While deregulation and liberalisation of the financial system requires the removal of controls and restrictions over the 'free' flow of currency and capital, many jurisdictions maintain or implement a reporting procedure to permit the ongoing monitoring of such movements. Financial institutions may be requested to report to the central bank all movements of capital/currency, over a specified financial threshold, in to and out of the country. Such a reporting procedure serves two purposes:

- It provides the central bank with essential statistics and information in respect of the balance of payments, etc.; and
- It provides the central bank with the opportunity to recognise any unusual flows of capital/currency (by size, source or destination) which may be suspicious and warrant further enquiry.