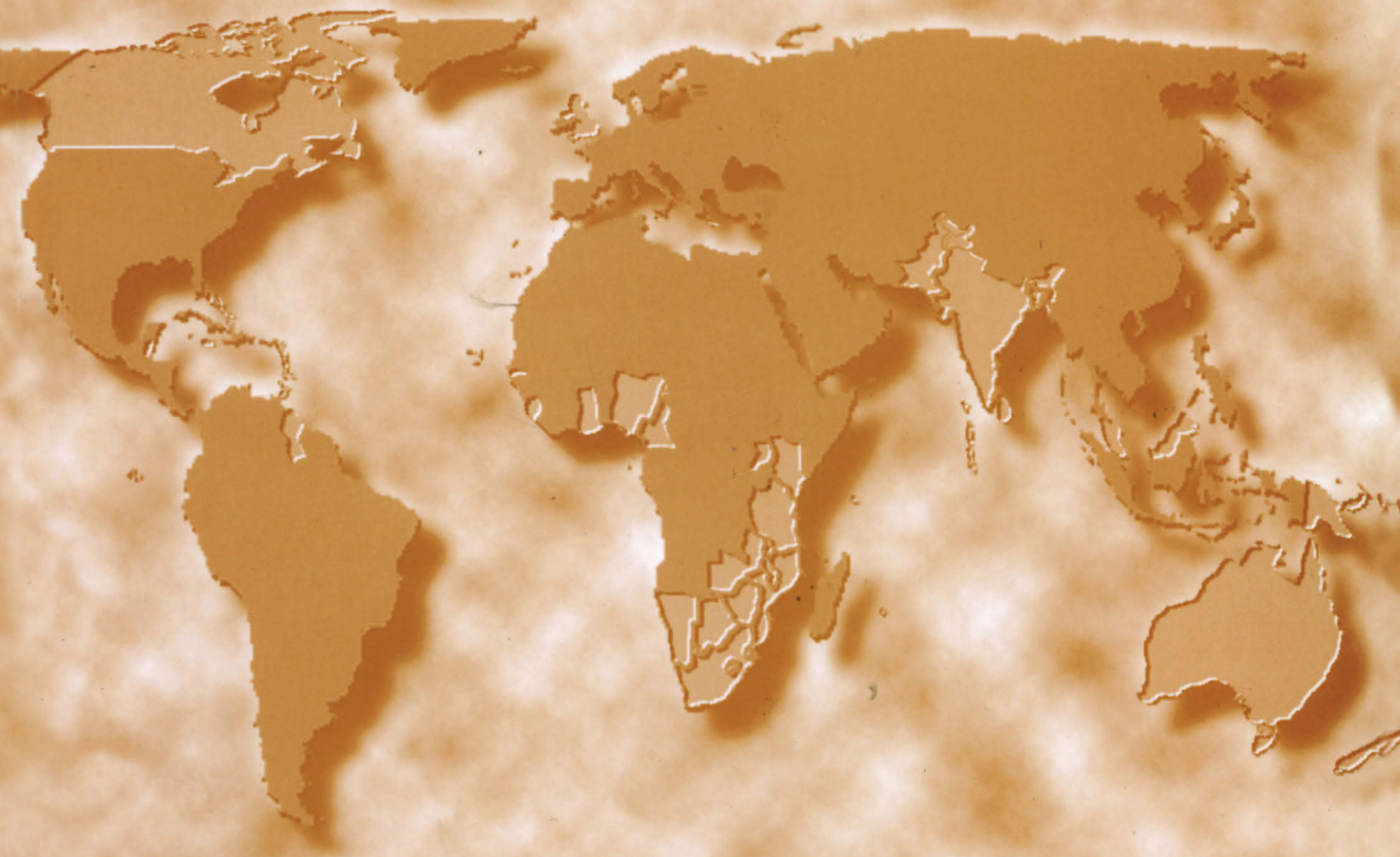
Money Laundering

Key Issues and Possible Action



COMMONWEALTH SECRETARIAT

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Foreword

Money laundering is a pervasive problem affecting countries large and small, rich and poor, as well as international financial centres. It poses a serious threat, not just to sound economic and financial development but to the political integrity and stability of nations. The Commonwealth has been in the forefront of international efforts to combat money laundering. Commonwealth Heads of Government have commended the recommendations of the Financial Action Task Force on Money Laundering (which was established by the G-7 Economic Summit in 1989) and urged steps for their early implementation. The Commonwealth Secretariat has taken a series of actions to meet this request in which it has followed a two-pronged approach. On the one hand it has developed a model law for the prohibition of money laundering. On the other, recognising that legislation alone is not enough, it has taken a number of steps to develop anti-money laundering strategies for the financial sector. These include regional workshops on the financial aspects of money laundering, the convening of meetings of Senior Finance Officials, initiating a process of self-evaluation of progress in the financial sector and developing a comprehensive and practical set of "guidance notes" for strengthening the capacity of financial sectors to track money laundering.

Commonwealth Finance Ministers, at their annual meeting in September 1996, agreed to level up minimum international standards across the Commonwealth for combating money laundering, endorsed the "guidance notes" and agreed to disseminate them widely among their financial institutions. They also agreed to set up multi-disciplinary national steering groups in order to design and implement effective national strategies to combat money laundering, and to support regional initiatives to enable Commonwealth countries to review progress in implementing anti-money laundering measures. They asked the Secretariat to initiate work on the parallel economy and its role in money laundering. This is a significant sector in several developing countries with implications for efforts to combat money laundering, which has not been addressed in the recommendations of the Financial Action Task Force and therefore requires to be brought within the ambit of effective anti-money laundering strategies for much of the developing world.

In an attempt to draw attention to the key issues in combating money laundering and possible action that could be taken on a co-ordinated basis, this paper was prepared by the Economic Affairs Division of the Secretariat and constituted the key document which was considered by a meeting of Commonwealth Senior Finance Officials in Colombo in 1995. The paper suggests measures to strengthen the financial sector, considers practical issues involved in combating money laundering in international financial centres and the problems of economic crime and tackling money laundering in the parallel economy. It concludes with a series of action steps which were subsequently presented to and adopted by Commonwealth Finance Ministers and Heads of Government as the basis for concrete action by Commonwealth countries. The Secretariat is also in the process of publishing the *Guidance Notes for the Financial Sector: Combating Money Laundering* for widespread dissemination among national financial institutions in Commonwealth countries.

Emeka Anyaoku, *Secretary-General*

1

Introduction

The problem of money laundering

Background

Money laundering is a global phenomenon that affects all countries in varying degrees. It is the process whereby the proceeds of criminal activity are disguised as legitimate money, so that they can be used by criminals for further activities.

Commonwealth Heads of Government, when they met in Limassol, Cyprus, in 1993:

> *"... identified money laundering as a serious threat to financial systems worldwide and agreed that the Commonwealth should support enhanced international co-operation in combating this financial crime. They commended the 40 Recommendations drawn up by the Financial Action Task Force (the international body founded for this purpose in 1989), urged steps to be taken for their early implementation and asked Commonwealth Law Ministers, Finance Ministers and the Secretary-General to see how best to carry this forward. They welcomed the formation of the Caribbean Financial Action Task Force. They also agreed to invite Law Ministers and Finance Ministers to examine how Commonwealth countries could best work collectively to combat the laundering of proceeds of all types of serious crime, through appropriate legislation and maintaining regulatory standards."*

Commonwealth Law Ministers at their 1993 meeting:

> *"expressed their desire that the issue of money laundering be addressed as a matter of urgency and their resolve, individually and collectively, to put in place comprehensive provisions criminalising money laundering in respect of the proceeds of all serious crimes, facilitating the disclosure by financial institutions of information giving rise to suspicion of money laundering activities, enabling confiscation of the proceeds of crime, making money laundering extraditable, and promoting international co-operation in the investigation and prosecution of money laundering and in confiscation proceedings."*

At the Commonwealth Finance Ministers Meeting in Valetta in September 1994, in the course of their discussions on Commonwealth functional co-operation, several Finance Ministers expressed views on money laundering. In particular:

The representative of the Minister of Finance of **Australia** noted that it had implemented the 40 Financial Action Task Force (FATF) Recommendations, and suggested that all other Commonwealth members should do likewise.

The representative of the Minister of Finance of **The Bahamas** was concerned that his country should not be used by money launderers; The Bahamas had endorsed work of FATF and had introduced appropriate legislation. The Bahamas also complied with the International Banks and Trusts Code of Conduct on money laundering, and had entered into bilateral agreements with the United States, Britain and Canada in this field.

The representative of the Minister of Finance of **Botswana** endorsed the proposal that the Commonwealth should take action on money

laundering. New Botswana legislation – the Banking Act and an Act on Economic Crime and Corruption – should help to prevent this from taking place in Botswana.

The Chancellor of the Exchequer, from **Britain**, pressed for action to be taken. He said that not only should the laundering of drug trafficking proceeds be tackled, but also the proceeds of other serious offences. It was particularly important for international financial centres to maintain standards; in particular banking confidentiality should not be used to protect criminals. A practical approach would involve financial institutions knowing their customers, and reporting suspicious transactions to the authorities. These institutions must have adequate internal controls and staff training procedures. Financial supervisors should ensure that this was done by those that they regulated. A programme of work within the Commonwealth should have four aims:

- assisting each government to implement the 40 Recommendations;
- establishing a mechanism for reporting progress;
- ensuring adequate communication between law and finance ministries; and
- keeping in contact with the FATF.

The representative of the Minister of Finance of **Cyprus** strongly supported international efforts to eradicate the problem of money laundering. Cyprus had taken concrete measures to combat it, including ratification of the Vienna and Strasbourg Conventions. The Central Bank had issued detailed instructions to all financial institutions based on the FATF Recommendations.

The Prime Minister of **Dominica** suggested that it would be helpful if the Commonwealth could draw up a blacklist of persons convicted of or involved in money laundering. It would also be helpful if legislation from countries already taking action could be made available to other Commonwealth governments.

The Minister of Finance and Economic Affairs of **The Gambia** welcomed a Commonwealth initiative on money laundering, and noted that it would need to take account of the need to balance effective steps to combat money laundering with the need to maintain banking confidentiality.

The Minister for Finance and Economic Planning of **Ghana** also endorsed the idea of a Commonwealth initiative on money laundering, and offered to co-operate fully in dealing with this on a multilateral basis, and without undermining faith in the banking system.

The Minister of Finance of **Namibia** called for concerted action by Commonwealth countries in imposing heavy penalties on persons convicted of carrying out illegal transactions.

The Minister of Finance of **Nigeria** noted that his country was working closely with the United States on a bilateral basis to combat laundering.

The Adviser on Finance and Economic Affairs to the Prime Minister of **Pakistan** supported the idea of work on money laundering, which should cover corruption and illicit payments, as well as tax evasion.

The Prime Minister of **St Vincent and the Grenadines** noted that money laundering was a universal problem requiring a collective response. He urged ratification of the Vienna Convention, and recommended a number of broad guidelines for Commonwealth action:

- a commonly acceptable definition of money laundering;
- asset sharing arrangements;
- a balance between bank secrecy and reporting suspicions;
- a framework for judges and magistrates to share information; and
- the provision of legal protection for money launderers as a fundamental human right.

The Minister of State in the Ministry of Finance of **Singapore** said that he supported the need for action on drug trafficking and money

laundering; it was Singapore's experience that a well regulated and strictly enforced regime encouraged rather than inhibited the growth of the financial services sector. Singapore had endorsed the FATF Recommendations and brought into force laws to combat money laundering.

The Minister of Finance and Economic Planning of **Uganda** said that one way of dealing with money laundering would be to assist producer countries to restructure their economies away from such problems.

The Acting Senior Minister of Finance of **Zimbabwe** said that his country was developing legislation requiring reporting of suspicious transactions, while maintaining secrecy. The legislation would also empower relevant authorities to confiscate the proceeds of criminal activity.

Following this discussion, Finance Ministers decided to include the following in their Communiqué:

> *"In response to the call by Commonwealth Heads of Government, [Finance] Ministers requested the Secretary-General to convene a meeting of relevant senior finance officials to identify appropriate strategies for, and review progress in, taking this matter forward in order to enable a report to be made to the 1995 Commonwealth Heads of Government Meeting."*

Why it is important to take action against Money Laundering

By its very nature, money laundering is a hidden activity, and it is impossible to measure its scale directly. However estimates may be made indirectly, on the basis of assessments of the level of criminal activity such as narcotics and arms trafficking, financial fraud and organised crime, combined with evidence from successful money laundering investigations. From these calculations it has been suggested that criminals may be laundering up to US$ 500 billion globally each year.

There are four principal arguments for tackling money laundering:

- failure to prevent money laundering permits criminals to benefit from their actions, thus making crime a more attractive proposition. It also allows criminal organisations to finance further criminal activity. Both of these factors will tend to increase the level of crime;
- the unchecked use of the financial system for this purpose has the potential to undermine individual financial institutions, and ultimately the entire financial system; it could also have adverse macro-economic effects and affect the exchange rate through large transfers of capital flows;
- at the same time, unchecked laundering may engender contempt for the law, thereby undermining public confidence in the legal system and in financial systems, in turn promoting economic crimes such as tax evasion;
- ultimately the accumulation of economic and financial power by criminal organisations can undermine national economies and democratic systems.

At the same time it is clear that effective mechanisms to combat money laundering can bring economic and developmental benefits to those countries that adopt them.

International Initiatives

Concerted international action to combat money laundering began in the 1980s, and three particular initiatives stand out.

The 1988 United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances (the Vienna Convention). Article 3 of this Convention provides a comprehensive legal definition of money laundering, which has been the basis of virtually all subsequent legislation. It is also the basis of the money laundering

offences in the draft Model Law for Commonwealth countries. As at 28 February 1995, 26 Commonwealth countries were states party to the Vienna Convention.

Basle Committee on Banking Regulations and Supervisory Practices: December 1988 Statement on Prevention of Criminal Use of the Banking System for the Purpose of Money Laundering (The Basle Statement of Principles). This document outlines some basic policies and procedures that banks' managements should ensure are in place in order to assist in the suppression of money laundering on both the national and international level. These procedures covered customer identification, compliance with laws and co-operation with law enforcement authorities.

The Financial Action Task Force on Money Laundering (FATF). The FATF was established initially by the 1989 Economic Summit. Its membership has now widened to cover 26 governments, of which five are Commonwealth members (Australia, Britain, Canada, New Zealand and Singapore) and a sixth, Hong Kong, is a British dependency. In early 1990 the FATF published 40 Recommendations aimed at governments and financial institutions, which together comprise a comprehensive regime against money laundering. The Recommendations fall into separate groupings, covering their General Framework (Recommendations 1-3), improvement of national legal systems to combat money laundering (Recommendations 4-8), enhancement of the role of the financial system (Recommendations 9-29) and strengthening of international co-operation (30-40). They have been accepted worldwide as one of the most comprehensive bases for tackling money laundering, and were commended by Commonwealth Heads of Government in 1993. A full list of the 40 FATF Recommendations,which were revised in June 1996, is in Annex C.

The Commonwealth Secretariat has worked closely with the FATF in recent years, organising and participating in a number of seminars and workshops addressing the legal, financial and law enforcement issues raised by money laundering.

Key elements of a Strategy against Money Laundering

Experience among FATF members and other countries that have sought to introduce comprehensive anti-money laundering regimes has suggested that there are five essential elements in any viable strategy. These are, with the relevant FATF Recommendations:

- the **criminalisation** of the strategy of money laundering. In some cases existing charges of handling or receiving stolen property may be a means of tackling laundering, but this does not usually apply to trafficking proceeds. It is also often difficult to prove the ***knowledge*** element required in these cases – that the accused ***knew*** that the money in question derived from crime. Most specific money laundering legislation now only requires that a person knows or ought reasonably to know that money represents the proceeds of crime. These issues are addressed in FATF Recommendations 1, 4, 5 and 6;
- a requirement on financial institutions to **know their customers** and to **keep records of transactions.** This is so that investigators will have an audit trail that will lead them to the money. The more comprehensive the audit trail, the less effective will be the launderer's attempts to conceal their assets. These issues are addressed in FATF Recommendations 2, 9-15, 21-22 and 25-29;
- powers to **trace, freeze and confiscate** criminal proceeds, keeping in mind the

need to maintain an appropriate level of confidentiality to protect legitimate customer interest and to ensure confidence in the financial system. In particular it is vital that investigators can have rapid access to account information and other such data where it is needed to progress their investigations. Banks and financial institutions, who do not usually wish to have criminal customers, will normally be happy to co-operate with investigators, providing that the latter have the necessary legal authority (which in turn protects the financial institutions from civil suit for breach of confidentiality). These issues are addressed in FATF Recommendations 1, 7 and 8;

- effective mechanisms for **international co-operation.** This will include the ability to assist in investigations by appropriate overseas authorities and the ability to provide evidence for judicial proceedings in other jurisdictions. This is a topic that is best addressed through multilateral conventions and bilateral treaty arrangements. These issues are addressed in FATF Recommendations 3 and 30-40; and finally
- a mechanism for **alerting the authorities** to potential cases of money laundering. This is addressed by FATF Recommendations 16-20, 23 and 24.

Of these five elements, two – the **criminalisation** of money laundering and the introduction of powers to **trace, freeze and confiscate** criminal proceeds – are primarily matters for Law Ministers. A further two – **customer identification** and **alerting the authorities** – are primarily for Finance Ministers. International co-operation is of concern to both as promoted through carefully crafted bilateral and multilateral treaties.

2

The Scope of Action to Combat Money Laundering

Criminal activities that should be made subject to money laundering offences

Introduction

Commonwealth Heads of Government agreed to tackle the laundering of the proceeds of **all types of serious crime.** There is however no universal definition of "serious crime".

Among those countries that have introduced wide-ranging money laundering legislation, a number of approaches have been adopted. These have included:

a list of specific offences – such lists invariably include drug trafficking, and may also cover blackmail, extortion, kidnapping and other activities associated with organised crime, arms trafficking, financial fraud, fiscal (tax) evasion, bank robbery and other highly profitable crimes. The list is usually capable of extension through secondary legislation;

a definition based on the severity of the sentence – this may be expressed in terms of the maximum or minimum length of sentence or size of fine available. In some cases additional highly profitable crimes may be included, even though the actual sentence available is below the chosen threshold;

a definition based on the category of court in which the prosecution may be conducted – where there are magistrates' courts covering lesser offences and higher courts covering more serious ones, laundering offences may be restricted to those which can or must be tried in the higher courts;

a definition that covers all criminal activity – this approach would allow laundering prosecutions relating to the proceeds of any criminal activity.

This is an issue that has been considered by Law Ministers, and in the light of their consideration, the draft model money laundering law adopts a definition based on the severity of the sentence. This does not preclude the possibility of using other approaches in accordance with individual country circumstances.

While the issue of predicate offences is primarily for Commonwealth Law Ministers, Finance Ministers have a distinct interest in the treatment of **economic crimes**, including tax evasion which was highlighted at the Finance Ministers Meeting in Malta as an important concern of some countries. This is an area that is considered in detail in Part 5 of this paper.

The role of the financial sector

Introduction

As is stated at the end of Part 1, of the five elements of an anti-money laundering strategy, two in particular are of direct relevance to the financial sector, and indeed require the active and willing participation of the financial sector if they are to work. These are **customer identification and record keeping,** and **alerting the authorities.**

Customer identification and record keeping

Practical aspects of customer identification and record keeping are discussed in Part 3 of this paper. However it is important to consider ***why*** these are such important issues.

Customer identification serves two purposes. The first is to provide an audit trail for investigators pursuing money laundering operations. If financial transactions can be linked to individual account holders it is possible for law enforcement authorities to put together an effective case when they wish to prosecute criminals and confiscate the proceeds of their crimes. Every failure of identification or record keeping makes it easier for criminals to retain their money.

Effective customer identification procedures serve a second purpose, in that they will ***make it difficult for*** criminals from using financial institutions. In situations where individuals are required to provide evidence of their identity, criminals have the choice of having their true identity recorded, leaving them open to greater risk of capture, conviction and confiscation, or of using false identification documentation, which may be spotted by staff in financial institutions, leading again to capture and conviction. The only alternative for determined launderers is to use non-financial institutions, which are clearly less well suited for their purposes. Again the costs are increased, and the risk of detection is higher.

Financial institutions tend to be very sensitive to any damage to their reputation. They will want the minimum of publicity about any money laundering investigations in which they are involved. Where they have effective customer identification and record keeping systems, the task of tracking transactions by the law enforcement agencies will be facilitated, and they will tend to co-operate in keeping the operation out of the public eye. However, where a financial institution helps to frustrate an investigation, there is less cause for the investigators to co-operate, and the involvement of the institution in a money laundering operation is more likely to become public, with the adverse consequences for that institution's reputation that inevitably follows such a revelation.

Experience in many countries has been that the introduction of identification and record keeping procedures has benefited financial institutions. The requirement to identify their customers has empowered the institutions to obtain information that assists them in their risk management, without deterring customers, who now know that they would be asked the same questions in any other institution. At the same time, legitimate customers who are aware of the legal responsibilities placed on financial institutions are more willing to provide information to the institutions.

Alerting the authorities

The mechanisms by which financial institutions may alert the authorities to suspicions of criminal activities are discussed in Part 3. It should be noted at this stage that money laundering legislation is not intended to turn financial institutions and their employees into detectives. Staff will not be expected to go looking for signs of criminal activity. However it is important that financial institutions and their staff do not ignore potential money laundering if they become aware of it. Financial institutions do owe a duty of confidentiality to their customers. This does not however extend to participation in, connivance with, or even turning a blind eye to, possible criminal activities carried on by their customers. Confidentiality issues are discussed in more detail in Part 4.

Issues for discussion

What steps can governments and Central Banks take to encourage all financial institutions to play their part in tackling money laundering? Is the reputational threat posed by potential, albeit unwitting, involvement in money laundering sufficient, or are further measures likely to be needed? How can the positive benefits of the introduction of an anti-money laundering regime be put across to financial institutions and their customers?

The FATF Recommendations relevant to the financial sector

The key FATF Recommendations relating to the financial sector are numbers 9 to 29. These are attached at Annex A. The FATF Recommendations were published in early 1990, and were drafted primarily with banks and similar deposit taking institutions in mind. Experience in FATF member countries since then has been that money laundering activity is also occurring within other parts of the financial sector, including the securities business. Annex B, based on work done by the FATF, describes how the FATF Recommendations can be applied to this area.

The scope of application of the legislation

Introduction

While the basic money laundering offences – conversion, transfer, concealment, etc. of funds knowing or suspecting that they derive from criminal activity – will apply universally, the legislation aimed at strengthening the financial sector against abuse by money launderers, which covers issues such as customer identification, record keeping and the reporting of suspicions can be limited in its application to financial institutions. It is, however, important that the definition of "financial institution" is sufficiently broad to cover all the types of commercial activity that might be considered particularly at risk from being used by launderers.

Definition of "Financial Institution"

Given that the intention is to apply the legislation to any institution that might be used to launder money, the best starting point is the legal definition of laundering, and the various operations that are covered by the definition. Any institution that conducts one or more of these operations for legitimate purposes might be unwittingly used by launderers to conduct the operation with the proceeds of crime.

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

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 in, association, conspiracy, attempting, aiding, abetting, facilitating and/or counselling – this might cover a wide range of advisory services, including investment advice and brokerage services.

The Vienna Convention definition clearly covers a wide range of financial activities, and the definition of "financial institution" needs to be equally wide. At the very least it must cover:

- **deposit taking** by institutions such as banks, building societies and credit unions;
- **money lending** including personal and mortgage lenders, factoring and financing of commercial transactions;
- **finance leasing;**
- **venture or risk capital;**
- **money transmission services;**
- **issuing and administrating means of payment** including credit cards, travellers' cheques and bankers drafts;
- **making guarantees and commitments;**
- **trading** in:

  money market instruments;

  foreign exchange;

  financial futures and options;

  exchange and interest rate instruments;

  transferable instruments;
- **underwriting and participating in share issues;**
- **money broking;**
- **investment advice and intermediation;**
- **insurance business.**

Several of the activities listed above may in some Commonwealth countries be conducted outside the formal financial sector, by unlicensed remitters, bureaux de change and in some cases casinos. It is important that these informal activities are captured as effectively as possible, to maximise the effectiveness of the system and to minimise displacement, which is discussed below.

Displacement

Experience in countries that have introduced legislation has indicated that where money laundering legislation is applied only to part of the financial sector, laundering activity shifts into those areas where the legislation does not apply. This process is known as displacement. Displacement also occurs out of the financial sector into other areas. These may include sectors such as retailing where money laundering is much harder to conceal, and in consequence takes longer, costs more, and is more likely to be detected.

More worryingly, money laundering activity may be displaced from the formal financial sector into the informal sector and the parallel economy. This is discussed in Part 5.

The legal definition of "financial institution"

Most money laundering legislation, including the draft model law, contains a definition of "financial institution" very much as described above. Most also contains provisions allowing the definition to be extended by secondary legislation. This gives flexibility to deal both with displacement and with developments in the financial sector, which might lead to the evolution of new forms of institution and new financial activities, which might offer new opportunities to the money launderer.

On the basis of the responses to the questionnaire circulated by the Secretariat in preparation for the Sri Lanka meeting, the financial sectors of Commonwealth countries demonstrate a great diversity. In almost all Commonwealth members banks are subject to a supervisory regime. In a small minority of countries there are some unlicensed deposit-taking institutions, although these are usually small in scale.

Other types of financial institution are less universally subject to a regulatory regime. These include money transmission services, foreign exchange dealers and institutions offering fiduciary services. In most countries these institutions are not considered to present any systemic risk to the financial sector, and they are not therefore

subject to prudential supervision in the same way as banks. Nonetheless these types of institutions have been shown on many occasions to be used, albeit unwittingly, in money laundering operations. It is essential therefore that they are made subject to the requirements of money laundering legislation, and that mechanisms are established to ensure their compliance. These mechanisms might involve a degree of supervision, but may well require a different kind of oversight.

More problematic, from the legislative angle, is the existence in many Commonwealth members of a large "parallel economy", where financial transactions including money transmission and foreign exchange may take place out of sight of any regulatory or legislative control. The particular problems posed by the existence of the parallel economy are considered more fully in Part 5.

Issues for discussion

What approaches can be taken for supervision of the parallel economy? What forms of financial institution are currently outside the supervisory regime? What approaches can be taken to widen the regulatory coverage without imposing too great a compliance burden on the institutions and/or too great an increase in government expenditure? How can effective coverage of the financial sector be reconciled with increased financial liberalisation?

3

Measures to Strengthen the Financial Sector

Customer identification

Introduction

FATF Recommendation 12 requires financial institutions to identify all customers when entering into business relationships or conducting significant transactions.

In those countries where there exists a national identity card system, that card can provide a clear basis for customer identification. However many Commonwealth countries do not have such a system, and in a number of countries the proportion of the population having some form of formal photographic documentation confirming their identity may be as low as 5 per cent. It is therefore necessary to devise an approach that will ensure that there is an adequate degree of customer identification, while not having the effect of denying access to the financial system to those who have no formal identification documents.

Possible approaches

As part of their financial and economic reforms some Commonwealth countries are seeking to increase the proportion of the population subject to some form of official identification, to combat electoral fraud and to improve the efficiency of tax collection. Where possible, other grounds for requiring identification – including tackling money laundering – should be taken into account in administering this identification process. Ideally this would extend to including a photograph, but failing that the signature of the person identified. If financial institutions were allowed access to a register of names and addresses, this would also assist in confirming that customers presenting such identification were who they claimed to be.

Where no system of identification extends over the bulk of the population it may be appropriate for identification procedures to be concentrated where there is the greatest risk of money laundering. At the most basic level this would be where the sums of money involved were large, or involved hard currency, or where there was movement of money in and out of the jurisdiction.

By and large, those individuals with large quantities of money are most likely to have formal identification documents – passports and driving licences in particular. The same is likely to be true of those customers who handle foreign currency or have transactions involving other countries. For those countries where wide-scale identification is not possible, it might be reasonable to require identification from customers conducting transactions over a certain size, or who hold accounts that may exceed a certain limit. Identification should also be required for all foreign currency accounts, and for all transactions over a certain amount involving the transmission of funds into or out of the country.

Clearly such an approach is less satisfactory than one involving comprehensive customer identification. It would therefore be necessary for financial supervisors and law enforcement agencies to monitor its effectiveness continuously, with a view to introducing tighter procedures if there was evidence of abuse by money launderers.

Corporate customers

One area that is particularly susceptible to abuse by money launderers is the use of corporate bank accounts, particularly those associated with international business companies and other offshore

corporate entities. Identification of corporate customers is more complex than identification of individuals, as it is desirable to identify both the beneficial ownership of the account, and those individuals who are able to use it.

With corporate customers, as with personal customers it is important that customer identification should amount to more than just verification of a company's legal standing and the identity of individual account signatories. It is good commercial sense for a bank or other financial institution to know as much as possible about the sort of business carried on by the customer. This will give the financial institution some idea of the likely cash flow through the customer's account, and the scale of operations that will be involved.

Issues for discussion

To what extent can customer identification for anti-money laundering purposes be integrated with action to improve the efficiency of the economy, through the use of identity cards, publicly accessible registers and other similar measures? What processes can be used for the identification of corporate customers?

It also provides an implicit standard against which to measure the performance of the customer, which will provide a potential early warning system in case the customer gets into financial difficulties or if the customer is or becomes involved in money laundering. Unduly large or illogical flows through an account might reflect business expansion or a change in direction – potentially an opportunity for additional business by the financial institution – or they could point to illicit transactions being put through the account. A financial institution that really knows its customers will be in a better position to judge, and to act accordingly. A financial institution that has at best just gone through the motions may well find itself involved in an unwelcome criminal investigation.

Internal systems and controls

Introduction

While legislation can specify the need for customer identification, record keeping and suspicions reporting, its implementation will be effective only if financial institutions develop internal systems and procedures to ensure that these tasks are carried out, and in particular to ensure that relevant staff know of their obligations under the legislation, and under any related guidance notes.

The money laundering reporting officer

The key to effective internal controls is a clear system of accountability. This is best achieved by the nomination of a single, senior officer within each institution who should take responsibility for ensuring that all aspects of money laundering legislation and regulation are complied with. This officer, often referred to as the money laundering reporting officer, has a number of key roles:

- he/she should act as the point of contact between the financial institution and the authorities responsible for countering money laundering. By focusing on a single point of contact, the relationship between the two is likely to develop more smoothly, and with a higher degree of confidentiality;
- internally he/she should be the initial recipient of all suspicions disclosures. This will allow the officer to act as a filter, using his/her wider knowledge of the operations of the financial institution to judge whether the suspicions of more junior staff are justified, and should be passed on to the authorities, or whether they relate to legitimate business;
- the officer should be responsible for monitoring customer identification and record keeping procedures within the

institution, and should report to both the financial institution, at the highest level, and, in parallel to the regulators on their correct implementation;

- the officer should be responsible for training staff in their obligations and in the institution's internal procedures, and should in turn be fully trained in his/her own duties by the supervisory authorities.

Clearly in small financial institutions these requirements will be less onerous than in major banks and investment firms. Nonetheless it is important that the responsibilities of the money laundering reporting officer are clearly recognised by the directors, management and staff of the institution, so that the officer is given all the necessary support and co-operation in carrying out these duties.

Issues for discussion

Are the responsibilities placed on the money laundering reporting officer manageable? What assistance might be necessary from the supervisory authorities to support this role?

Suspicious transactions

Introduction

The idea that financial institutions should spontaneously report transactions that they have conducted to the authorities is perhaps the most radical element of the whole anti- money laundering package. It runs contrary to the natural instincts of most financial institutions, which place a very strong emphasis on customer confidentiality.

However, with the development of sophisticated financial institutions able to move money rapidly around the world it is almost certainly impossible to combat money laundering without the assistance of financial institutions in making such reports. It is therefore important to recognise that the responsibilities placed on financial institutions are not unreasonable.

Why financial institutions should report suspicious transactions

There are two main reasons why financial institutions should co-operate in combating money laundering by disclosing details of suspicious transactions. The first is essentially a moral one. Given the growing importance of financial intermediaries across the whole economy, they are placed in a powerful and privileged position. It is because of this that financial institutions recognise a duty of confidentiality to their customers, which prevents them from abusing the power that their control over economic transactions grants them.

However their position also gives them a responsibility to the government not to abuse their power to commit criminal activities. Not only are financial institutions not above the law, but they have a duty to uphold the law more generally, 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 financial institutions to report suspicious transactions is simple self-interest. The basis of trust on which the financial system operates can easily be undermined by the involvement of financial institutions in criminal activity, even if the involvement was unwitting.

A financial institution that discovers that it is holding criminal proceeds may be subject to criminal penalties under the common law (as an aider or abettor), or civil suit for constructive trust, even in the absence of money laundering legislation. Given the ability to disclose its situation to the authorities, a financial institution will be able to put itself in a safe position.

Factors that might make a transaction suspicious

Financial institutions should be suspicious of any transaction that they believe might relate to criminal proceeds. Recognition of such transactions is made easier when financial institutions have a clear understanding of the legitimate business of their customers. This is why it is so important for financial institutions to know their customers.

It is not possible to draw up a checklist of factors that would determine whether any given transaction should be treated as suspicious. In each case the context of the transaction is as important as details of the transaction itself. In practice it is for financial institutions to decide on a case by case basis whether the transaction "makes sense". If it does not, then it may justify reporting.

In the absence of a checklist of features, it is still possible to identify some questions which an institution might ask itself in order to determine whether a transaction makes sense:

- is the ***size*** of the transaction consistent with the normal activities of the customer?
- is the transaction ***rational*** in the context of the customer's business or personal activities?
- has the ***pattern of transactions*** conducted by the customer changed?
- where the transaction is ***international*** in nature, does the customer have any obvious reason for conducting business with the other country involved?

In many countries that have introduced money laundering legislation the financial sector trade associations, the financial regulators and the law enforcement authorities have worked together to produce guidance for financial institutions covering the issue of identifying and reporting suspicious transactions. This is discussed further below.

The circumstances under which a financial institution should make disclosures

While money laundering legislation requires the co-operation of the financial sector in order to be effective, it is not the purpose of such legislation to turn financial institutions into detectives. Financial institutions cannot be expected to invest a large amount of time and resources in investigating their own customers' affairs to ensure that they are not laundering money. On the other hand it is important that financial institutions do not wilfully turn a blind eye to what their customers are doing.

Striking the right balance is something that will only come with experience – although guidance notes of the type discussed below may be helpful here. However, the more that a financial institution knows about the activities of its customers, the better able it is to identify scope for potential new business. Where the relationship between institution and client is healthy there will be no problem in the two discussing the nature of the customer's business. On the other hand, where the customer is acting suspiciously, it is important that the institution does not tip the customer off about its concerns.

"Tipping off"

"Tipping off" is when a financial institution alerts its customer to the fact that it suspects the customer of being involved in criminal activities, and has made or is about to make a report to the authorities. Advance warning would allow the customer to move itself and its funds elsewhere, thus preventing the authorities from recovering the money.

While "tipping off" is an offence under most money laundering legislation, this should not prevent financial institutions from deciding to cease doing business with a customer whom they suspect of engaging in money laundering. Under such circumstances, however, it is important that the institution does not reveal to the customer why it is taking this decision. Where possible the authorities should be alerted to the situa-

tion, even if the financial institution has not actually conducted the transaction that has given rise to the suspicions.

Issues for discussion

How can financial institutions in Commonwealth countries be encouraged to disclose suspicions? Can financial sector trade associations be encouraged to assist in this process?

Confidentiality

Introduction

It is sometimes argued that action to combat money laundering can itself pose a threat to confidence in the financial system, particularly in respect of damage to the confidential relationship between financial institutions and their clients which is essential for the conduct of legitimate financial business.

Experience among those countries and territories that have introduced money laundering legislation has indicated that effective anti-money laundering legislation is fully compatible with a high degree of commercial and financial confidentiality, provided that the legislation is drafted and implemented in a way that respects the nature of financial business.

The legal position

For those Common Law jurisdictions that have not introduced statutory provisions governing confidentiality, the legal position is effectively that set out in the *Tournier* decision (Tournier v. National Provincial and Union Bank of England [1924] 1 KB 461). This identifies a number of circumstances where the implied duty of confidentiality owed by a bank (or any other financial institution) to its client may be breached. The three most important 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, or else it makes it a defence against a possible charge of involvement in money laundering to make such a report. Under these two approaches the financial institution is protected from suit for breach of confidence by the first and second sets of circumstances respectively.

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. To be effective money laundering legislation must allow the passing on of ***suspicions*** as well as knowledge. This is discussed in more detail in Part 5.

[Despite the protection under the Common Law, however, most money laundering legislation gives explicit statutory protection to financial institutions that disclose suspicions of money laundering by their clients to the authorities in good faith.]

Institutional arrangements

While the legal situation protects financial institutions from civil action by clients or criminal liability for breach of statute, it does not by itself defend them against the reputational damage that might arise if a disclosure, made in good faith but not relating to actual criminal activity, were to become known to the customer to whom it related, and that customer made the fact public.

This problem is best tackled by establishing appropriate institutional arrangements for the handling of suspicion disclosures. These arrangements should ensure that:

- suspicions disclosures are only handled by a small number of people, all of whom are well trained and aware of the sensitive nature of this information;
- when suspicions are passed on to investigators, they are only passed to known contacts within investigating authorities, who are themselves aware of the sensitivity of the information that they receive;
- all information that is not either relevant to ongoing investigations or might provide leads for future investigations is destroyed at the earliest possible opportunity;
- financial institutions are kept informed of developments relating to disclosures that they have made as quickly and as fully as possible.

Regular and direct contact between financial institutions and the authorities responsible for handling suspicion disclosures should increase the confidence that financial institutions have in the handling of disclosures, and will also tend to help the investigators and central authorities to understand the concerns of financial institutions.

International co-operation

There may be particular concerns about the transfer of information deriving from suspicious disclosures to other jurisdictions. It is not always possible for the originating jurisdiction to specify precisely what should or should not be done with the information. Where the handling of the information is not covered by a pre-existing agreement, such as a tax or mutual legal assistance treaty, it may be useful to negotiate a memorandum of understanding (MoU), which can place restrictions on the use or further transmission of the information.

Issues for discussion

How can action against money laundering be publicly presented to maximise the recognition that confidentiality is not being undermined? Which existing institutions carry the greatest public trust, and thus are best placed to play leading roles in the anti-money laundering regime? How can their protection from political interference be enshrined in the constitution?

Central units for handling suspicious transaction reports

Introduction

Under FATF Recommendation 16, financial institutions which suspect that funds that they are asked to handle derive from criminal activity should report their suspicions to "the competent authorities". The FATF Recommendations do not define what "the competent authorities" should be, but it has been the experience of governments implementing the Recommendations that the most effective approach is to designate a single central unit to receive and process money laundering disclosures.

An effective money laundering regime will necessarily involve the law enforcement agencies, the financial sector regulators and, where the system is also used to address tax evasion, the revenue authorities. It would be possible to locate a specialised central unit in any one of these bodies, or to set it up as a free-standing agency. There are examples of most of the options among countries that have introduced money laundering legislation.

The choice of approach for each country will depend upon a range of factors. These include:

- **institutional capabilities and resources.** There is no point in establishing a central unit within an agency that lacks the resources, powers, motivation or

competence to carry out the required role. It is essential that the central unit be backed by clear political commitment to assist it in combating money laundering;

- **inter-agency relationships.** The central unit will need to work with all the other agencies with a role in combating money laundering. It should therefore be located where it is capable of commanding the respect of those agencies;
- **relationship with the financial sector.** The central unit will need to deal on a day- to-day basis with financial institutions, and achieve their co-operation rather than grudging enforced compliance;
- **international contacts.** Most laundering operations are international in nature. The central unit will need to use existing international channels of communication, or else have the powers to establish its own, in order to co-operate with money laundering investigations in other countries, and in order to obtain assistance from other countries in their own investigations.
- **public confidence.** It is essential not only that financial institutions have confidence in the capabilities of the central unit, but that there is general public trust in it. This unit will have access to confidential information about individuals, which could be used improperly to do political, financial or potentially physical harm to those individuals. Misuse of personal information would undermine public faith not only in the unit itself, but also in the financial institutions that made reports to it. Under these circumstances the system would do more harm than good.

This section sets out a range of possible structures for a central unit to receive suspicious transaction reports, giving examples where appropriate of countries where such structures are in place.

A designated unit within the police force

This is the most basic approach, and has been adopted in the **Isle of Man.** The local fraud squad are the contact point for all disclosures by local financial institutions. They will either investigate the disclosures themselves, where it relates to local activity, or pass the information to other investigators where it relates to activities in other jurisdictions.

This approach works best for jurisdictions where most financial sector activity is offshore-related. The low level of local activity means that the fraud squad are not swamped by investigations or analysis arising out of suspicions disclosures.

To be effective, such an approach relies upon the active involvement of the financial supervisory authorities in educating local financial institutions about their responsibilities under money laundering legislation, and monitoring its implementation. It is also essential that the local law enforcement agencies can give quick and effective assistance in money laundering cases involving offshore businesses operating from the jurisdiction (which will be the majority of the investigations arising from suspicion disclosures).

The adaptation of such an approach to cover tax evasion could in theory be achieved through an MoU between the police and the revenue authorities.

A specialised unit within the law enforcement system

This is the approach used in **Britain.** It is similar to the previous approach, but allows for jurisdictions where there is a higher level of reporting. The main function of the central unit is to allocate suspicion disclosures to the appropriate investigatory agency. With sufficient resources, the central unit would also be well placed to perform an analytical function, and might be able to generate information on trends in laundering techniques, and highlight sectors or individual institutions whose reporting patterns are anomalous.

As with the previous approach, this mechanism still requires the financial supervisors to

play an active part in monitoring compliance by financial institutions with appropriate legislation. Again the ability to co-operate in investigations from overseas, and the ability to exchange information is necessary here.

Such an approach could be extended to cover tax evasion as above, through an MoU between the central point and the revenue authorities, or else by making the central unit a joint revenue/law enforcement body.

This approach is best suited to jurisdictions where the existing supervisory regime is effective, and willing to co-operate with law enforcement agencies.

A specialised unit within the regulatory authority

An alternative to establishing the special unit within the law enforcement framework would be to establish it within the regulatory structure (e.g. within the Central Bank). This would have a number of potential advantages, for instance:

- financial institutions would already have a close working relationship with the regulatory authority, and they would possibly be more willing to make disclosures to them than to a law enforcement agency;
- where the regulatory authority suspected that a financial institution was not following the requirements of the legislation properly, it would be able to step in directly and either tackle the problem, or, if the financial institution appeared to be involved in laundering, it could take regulatory action up to and including licence revocation;
- the regulatory authority would be well placed to advise financial institutions on how they might improve their systems and controls to combat money laundering.

On the other hand there would be some disadvantages:

- the unit would not be in a position to ***investigate*** suspicions itself, and would therefore need to pass them on to the relevant law enforcement authorities. This could potentially introduce an element of delay;
- because it was not itself a criminal investigatory body, a unit within the regulatory system might find it difficult to exchange information and otherwise co-operate with central units in other countries;
- there might be no single regulator with responsibility for all institutions subject to the money laundering legislation. This might lead to uneven coverage of the financial sector (one possible way to tackle this where there are several regulators would be to establish a central unit shared by all the regulators, staffed by secondees).

This option might be appropriate where the Central Bank or other regulatory authority is well respected and both willing and able to take on this rôle. It would however require the regulatory authority to liaise effectively with the law enforcement agencies and, if the legislation is to be used to combat tax evasion as well, with the Revenue authorities.

A freestanding specialised unit

Establishing the central unit as a stand-alone body, separate from both the financial regulators and the law enforcement agencies would avoid some of the problems associated with the two previous alternatives, but it would lose some of the advantages. As an independent body it would not be seen to be working to any other agencies' agendas. However a unit with no role other than receiving, analysing and distributing disclosures might in practice be too weak to be effective, particularly as it would have clearly measurable costs, but the benefits of its activities would accrue elsewhere.

A freestanding specialised unit with regulatory powers

Under this approach a single freestanding body would be responsible for the handling of suspi-

cion disclosures and the monitoring of the implementation of money laundering legislation. For the former function it would act much as in the previous options, performing analysis on the disclosures received and distributing them to the relevant investigating agencies. For the latter function it would have the authority to inspect the systems and controls established by financial systems to enable them to make reports.

It would be necessary to consider the relationship between such a unit and existing financial regulators. Some aspects of supervision, such as solvency, would not be of direct concern to such a unit, and would be expected to remain with the Central Bank or with the insurance supervisor. There would however be a potential overlap in the areas of conduct of business regulation and investor protection. Where there is no effective body with such responsibilities it might be sensible to place these with the central money laundering unit, to minimise duplication of effort and the compliance burden on financial institutions.

A body along these lines is likely to be fairly large, and expensive to operate. That will increase the attractiveness of using it to address tax evasion. This might best be tackled by involving revenue officials in the analysis of disclosures.

Any effective **cash transaction reporting regime** would require a central unit with at least the powers set out here. The **Australian** Transaction Reports and Analysis Centre (AUSTRAC) is structured along these lines.

A specialised unit with regulatory and investigative powers

This option would create a very powerful body with potentially wide-ranging powers. In addition to the considerations discussed above, it would be necessary to address the interface with law enforcement and, where appropriate, revenue authority investigators. It might be possible to establish such a body with the ability to investigate tax evasion, passing other cases to the police, but this could give rise to conflicts of interest between apprehension of criminals and recovery of revenue.

This single agency approach is probably too monolithic to be workable.

Issues for discussion

Which of the existing agencies in each Commonwealth country currently command the trust and respect of the financial sector and the law enforcement agencies? Is any existing agency structured appropriately to take on responsibilities in this area, or would a new agency – perhaps drawing staff from a number of existing bodies – be a better option? What arrangements, such as interdepartmental arrangements, might be necessary to ensure a co-ordinated and co-operative approach to tackling money laundering?

Treatment of jurisdictions with inadequate money laundering regimes

Introduction

Given the international nature of both the global financial system and modern money laundering, there is a danger that domestic action to tackle the problem will be undermined by criminal proceeds that have been introduced into the financial system from other countries. Once the money is in the financial system it is harder to recognise its criminal origins, and thus to take action against it. A comprehensive approach to tackling money laundering must therefore include measures to deal with these flows.

The scale of the problem

Identifying those countries that pose the greatest money laundering risk is not easy. Even in countries where there is no relevant legislation, only a small fraction of financial flows will involve the proceeds of crime. Other factors, such as the scale and sophistication of the local financial

sector, geographical location, or level of criminality, may attract money launderers, so that some countries with legislation in place may suffer from more money laundering than others without. Furthermore, within any country, some financial institutions are likely to be more effective at deterring or detecting criminal proceeds than others. In particular, branches and subsidiaries of financial institutions whose headquarters are subject to an effective anti-money laundering regime may be obliged to follow much tougher procedures than might be required under local legislation.

Under these circumstances attempts to draw up lists of countries with inadequate money laundering countermeasures, or alternatively lists of countries that do have countermeasures in place, are likely to be ineffective, as well as politically contentious. Clearly it is important to pay careful attention to transactions arising from countries with a poor reputation for taking action against money laundering, but it is equally important to identify particular institutions, from whatever country, that may have inadequate systems and controls.

Identifying high risk transactions

This is best tackled through the exchange of information among financial supervisors, law enforcement agencies, and other bodies with a responsibility for tackling money laundering. While the exchange of mere suspicions may be inappropriate, information about convictions for money laundering, or regulatory action to tackle institutions failing to take adequate steps to guard against it, is likely to be of value to authorities in other countries, particularly where the financial institution involved has branches or subsidiaries in other countries, or conducts much of its business with residents of another country.

The exchange of such information is best handled through bilateral (or multilateral) agreements between the agencies involved, perhaps on the basis of MoUs. Such agreements would cover the basis upon which information might be exchanged, including any restrictions on further transmission of the information.

Issues for discussion

What arrangements already exist for the exchange of information between national authorities? Can these be developed to encompass information regarding institutions and/or countries that pose a significant money laundering threat? To what extent would such a system affect the relationship between financial institutions and the relevant authorities?

The role of the supervisory authorities

Introduction

It is clear from what has already been said, and from consideration of the draft model law, that legislation on its own is not sufficient to construct an effective regime for tackling money laundering. It is absolutely crucial that there is an appropriate institutional structure within which the law operates.

Whether or not a single body is given responsibility for ensuring compliance with all aspects of money laundering legislation, it is crucial that a number of functions are carried out. These include the inspection of financial institutions to monitor compliance, the compilation of statistics and other reports and reviews of the effectiveness of the legislation, issuing guidance notes to assist financial institutions in meeting their obligations under the legislation, providing training for the staff of financial institutions in appropriate systems to forestall, prevent and detect money laundering, and ensuring that financial institutions do not come under the control of criminals or criminal organisations.

Inspection of financial institutions

It is necessary to ensure that financial institutions have in place systems that address the requirements of Recommendations 12-18 and 20, that is to:

- identify their customers;

- keep records of all transactions;
- report any suspicious transactions to the relevant authorities and co-operate with subsequent instructions from those authorities;
- establish systems and controls to forestall and prevent money laundering, including the provision of appropriate training for staff.

Whatever agency is responsible for fulfilling this responsibility, it will need to be able to inspect financial institutions' records, and if necessary to interview their staff. Financial supervisors and Central Banks will often have such powers. Even where these authorities do not have primary responsibility for tackling money laundering within the financial sector, they will have an interest in the findings of such inspections – a financial institution that is not taking adequate steps to guard against money laundering may be cause for concern in other contexts. In order to maximise the effectiveness of such inspections, while minimising the burdens imposed by the inspection process on financial institutions, where responsibilities lie with more than one agency it may be appropriate for one authority to conduct inspections on behalf of others. This will require close co-operation between all the agencies concerned.

Compilation of statistics and reports

The effectiveness of money laundering legislation can best be maintained by ongoing assessment of its impact. Not only will governments wish to know what impact the legislation is having, but financial institutions will also benefit from feedback about the disclosures that they make, in aggregate as well as on a case by case basis. Reporting might usefully take a number of forms:

- statistical information detailing the number of disclosures made, the percentage which have been of value, and the classes of institution that made the disclosures;
- information on convictions obtained and assets confiscated, both domestically and as a result of international co-operation;
- regular appraisals of the costs of the anti-money laundering regime to government and to the financial sector;
- trends in laundering, both domestic and international.

Guidance notes

It has been the experience of financial institutions in many countries where money laundering legislation has been introduced that compliance with the legislation is made easier by the provision of officially approved guidance notes.

It is important that such guidance is:

accurate, reflecting the legal provisions in such a way that financial institutions can trust the guidance;

comprehensible, so that it is easy to use; and

kept up to date, so that it reflects any amendments to legislation or experience in using it.

For these reasons it is desirable for the drafting of guidance notes to involve not only the regulatory and law enforcement agencies responsible for supervising and operating the legislation, but also the financial institutions themselves.

The guidance notes should set out good practice in complying with the law in a more detailed way than is possible in the text of the legislation. They should also give examples of what might be considered suspicious transactions, and what elements might be appropriate for inclusion in staff training programmes. Examples of Commonwealth countries and territories that have produced guidance notes include Britain, the Isle of Man, Singapore and Australia.

Training

While guidance notes form an invaluable adjunct to money laundering legislation, they operate

best when combined with training for the staff of financial institutions. While it is appropriate for financial institutions to train their own staff, it is vital that those officers who are responsible for making suspicions disclosures, and who liaise with the supervisory authorities, receive sufficient training in their specific responsibilities. Such training is best provided by, or in close association with, those agencies responsible for the operation of the legislation.

This training should cover a range of topics:

- the requirements placed on financial institutions under the legislation, including the duties to identify customers, keep records and train staff in the appropriate systems, as well as reporting suspicions;
- recognising transactions which might relate to money laundering, and determining to what extent "mild" suspicions might be "filtered out" and not passed on to the authorities;
- understanding the sort of information that would be of value to the authorities, and the extent to which follow-up information might be valuable, and what level of feedback might be expected in response to disclosures;
- handling requests from law enforcement investigators for confidential information.

Issues for discussion

What institutional arrangements are needed to ensure that the authorities responsible for combatting money laundering are in a position to carry out all their responsibilities, or alternatively to ensure that they are carried out by other bodies?

In some Commonwealth countries the provision of training has been arranged in association with the financial sector trade associations, who have been able to devise appropriate manuals and materials for training staff at all levels within financial institutions. This approach has helped to develop mutual understanding between the authorities and the trade associations, which has allowed the effectiveness of the legislation to be monitored informally, and possible improvements to it to be identified at an early stage.

Preventing criminal control of financial institutions

The effectiveness of the measures outlined above depends critically upon the assumption that financial institutions themselves recognise the desirability of co-operating with the authorities to ensure that they do not find themselves inadvertently doing business with criminals. In almost all cases this assumption is justified, and financial institutions genuinely do want to "keep the crooks off the books". However this is not the case where financial institutions have been set up, or subsequently fall, under the control of criminals or criminal organisations.

A financial institution that knowingly launders criminal proceeds, and which conceals this behaviour from the authorities poses a severe threat to the financial system, and offers criminal organisations the best prospect of accessing the financial system without detection.

Unsurprisingly this situation has attracted criminal organisations in some countries to make active efforts to acquire control of financial institutions. There have also been banking crises in some jurisdictions that had set out to establish themselves as offshore centres through a combination of tax advantages and slack regulation. Even today, there is evidence that financial institutions in countries such as Russia are being established by criminal organisations.

It is essential that financial regulators and other authorities responsible for combatting money laundering take steps to ensure that criminal organisations cannot take control of, or set up, banks or other financial regulations. The key to this is to ensure that applicants for

licences to run financial institutions are adequately scrutinised to ensure that they are "fit and proper" to conduct the business that they propose.

International co-operation

Introduction

It has already been pointed out that money laundering is an international problem, and that effective measures to tackle it require international co-operation. This co-operation is necessary at a number of levels, and between a number of different agencies.

Co-operation between governments

Co-operation between governments is important to ensure that a legal and administrative framework exists for cross-border investigations into money laundering. At the most basic level it is important that the legal and constitutional definitions of money laundering adopted by different governments are compatible, so that a crime committed in one jurisdiction will be recognised as such by others. The widespread adoption of the 40 FATF Recommendations, together with the 1988 United Nations Convention (and, increasingly, the 1990 Council of Europe Convention), has greatly assisted in this process. For those Commonwealth countries that have yet to introduce their own money laundering legislation, the draft model law produced by the Secretariat will provide a legal framework that is fully compatible with the FATF Recommendations, and hence with the approach adopted in the majority of other countries.

At the intergovernmental level the processing of requests for international co-operation in money laundering cases is greatly eased by the negotiation of bilateral or multilateral treaties or agreements. In particular Mutual Legal Assistance Treaties, covering asset tracing, freezing and confiscation, the production of evidence and the questioning of witnesses, are extremely valuable tools in pursuing investigations across national boundaries.

Co-operation between government agencies

Within the framework of a common legal approach and a network of international agreements, most practical co-operation will take place on an agency to agency basis. This will tend to develop at both the formal and informal level. Formal arrangements for the exchange of information under international agreements will frequently, and rightly, be channelled through formal channels, involving nominated central authorities within Justice Ministries or the Attorney General's Department. These formal exchanges can be greatly strengthened, and frequently speeded up, by more informal, direct contact between investigatory and supervisory agencies.

Apart from contacts relating to specific cases, informal communication can develop national authorities' understanding of the nature of the information available to their counterparts in other jurisdictions, and the exchange of information about previous cases, and approaches that have been more or less successful, can help propagate good practice. Fora for exchanges of experience already exist for law enforcement bodies[1] and are developing among financial supervisors[2].

With individual cases, informal bilateral discussions may clarify the likely value of information that might be obtained through formal requests for information. It might also allow the authorities in different countries to identify common targets, and develop a mutually supportive approach to their investigations.

Just as co-operation between governments is assisted by formal treaties and agreements, specifying how requests for information should be made, and to whom they should be addressed, agency to agency co-operation can be assisted by the drawing up of MoUs, setting out clearly how information should be exchanged. MoUs are particularly valuable where there is a regular two-way flow of requests between the two parties to the agreement.

1 Interpol's FOPAC group, the Customs Co-operation Council

2 Through the International Organisation of Securities Commissions (IOSCO) and the Offshore Group of Banking Supervisors

Co-operation on best practice

The exchange of information between supervisory authorities need not only relate to suspected cases of money laundering. Those countries with longer experience of tackling money laundering will often be willing and able to offer advise and assistance to other countries that are establishing legislation, procedures and institutional structures for the first time.

Issues for discussion

Is the existing level of bilateral co-operation adequate? What are the shortcomings in existing arrangements? How can Commonwealth governments maximise the scope for international co-operation in combating money laundering? Is there a case for the establishment of a dedicated structure within the Commonwealth to assist in this process, or does Commonwealth participation in existing fora offer sufficient scope?

4

International Financial Centres

Economic development and the financial sector

Introduction

Many developing countries are looking to the development of a significant financial sector as a key to economic development. This approach has been stimulated by the increasing globalisation of financial and capital markets resulting from financial and economic liberalisation.

Threats to development

The expansion of global financial markets has not been without its problems. There has been increased volatility of capital flows as money has moved from market to market in search of short term returns. This is an issue that is already concerning Commonwealth governments.

A comparable threat comes from the increasing quantities of criminally derived and criminally controlled money flowing through the international system. These flows do not necessarily respond to normal economic stimuli, moving instead in response to changes in banking secrecy, or financial regulation. Such movements result in unpredictability and hence the instability of financial institutions through which they occur.

This instability should be of particular concern to those governments seeking to establish or develop their financial sectors. Criminal money may flow rapidly into new centres, providing an illusion of success and a short term boost to national savings. They may equally flow away rapidly as conditions change, attracted by another centre, or merely moving to complicate detection.

Combating instability

Those governments that resist the temptation to soak up short term flows from money laundering are likely to find themselves laying the foundations of a financial sector that can make a contribution to the economy over the longer term. By setting high standards of financial regulation, and by introducing effective money laundering countermeasures, they are likely to attract high quality financial institutions, which will not only provide a source of revenue directly, but which will contribute to wider economic development within the country.

While this point is relevant to all countries, it is particularly crucial to those seeking to develop as international financial centres.

The key feature of an international financial centre

Introduction

For the purposes of this paper, International Financial Centres (IFCs) may be defined as jurisdictions which are seeking to achieve a significant proportion of their economic development through attracting financial services activity. This activity is primarily conducted on behalf of non-residents, and may involve special tax concessions or bank licensing arrangements to cater for this "offshore" business. IFCs are often referred to as "Offshore Centres", or as "Tax Havens".

The attractions of IFCs

IFCs tend to attract business through offering a range of financial and professional services, combined with an attractive tax regime. Not all centres offer all services: some seek to specialise in particular niches. Key elements in IFCs include:

- **favourable taxation.** This may involve: very low (even zero) rates of corporate and

personal income tax for all or selected classes of companies and individuals; no withholding tax on bank interest or corporate dividends; and special arrangements with selected countries under dual-taxation treaties;

- **banking services.** Banking operations may be established on a "managed basis" where a bank with a physical presence in the jurisdiction manages a "booking operation", accepting deposits on behalf of a branch or subsidiary of another bank which has no physical presence. Deposits booked within the jurisdiction would be subject to local tax and legal requirements;
- **company formation and management.** Special classes of corporate entities (often known as "International Business Companies" (IBCs) or "exempt companies") may be created, often at very short notice, within the jurisdiction. Such companies would be able to hold assets and conduct financial transactions. Disclosure requirements are usually minimal for these companies, and they are often exempt from tax on any of their activities;
- **insurance.** The tax and regulatory structure may be attractive to insurance companies, particularly "captive insurers" – effectively separately incorporated self- insurance schemes;
- **trust business.** Asset protection trusts and other similar arrangements can be established to place assets out of the reach of lawsuits or similar demands. These may involve the use of IBCs as well as trusts;
- **confidentiality.** Commercial and financial confidentiality may be enshrined in statute, and subject to criminal penalties, rather than remaining a matter of Common Law.

While all these factors are designed to assist legitimate business activities, particularly when those activities are commercially or politically sensitive, they may also prove to be attractive to money launderers seeking to hide their illicitly gained assets. Those countries seeking to develop as IFCs must therefore be careful to deter criminal money, while still attracting legitimate international business.

The competitiveness of ifcs

Introduction

Because they look for business outside their own jurisdictions, IFCs are, to a greater or lesser degree, in competition with each other. This is particularly true of centres within the same time zone: all Caribbean and Caribbean Rim IFCs are effectively competing for business from the United States, Canada and Latin America. Pacific IFCs are competing for business from East Asia and Australasia. Some areas of IFC activity are not so dependent on time zones, and IBCs in particular may be used by customers worldwide.

This high level of competition tends to make individual IFCs reluctant to take any step that might cause them to lose business to a rival centre. Past experience has demonstrated that changes in tax regimes, or political instability can cause very rapid outflows of business. Indeed many offshore trusts are established in such a way that they can move to a new jurisdiction overnight, in the face of any threat to their situation.

Reputation

Because of the sensitivity of much IFC business to any threat, real or imagined, to their situation, IFCs must move carefully in introducing new legislative or regulatory positions. However the business is also likely to be sensitive to any scandal occurring within the jurisdiction, especially if it is related to the financial sector.

Several international financial centres that have attracted business through low regulatory standards and minimal vetting of bank licence applicants have subsequently suffered badly from the collapse of financial institutions, and the uncovering of fraud and money laundering within their jurisdiction. Such centres have sub-

sequently found it very difficult to re-establish themselves as viable financial centres.

However, where reasonable standards have been maintained, it has been possible for some IFCs to introduce progressively tighter regulatory requirements and money laundering legislation without losing much business. What little that has been lost has soon been replaced by new, higher quality business, attracted by the higher standards that have been introduced.

Collective action

The key to this success has often been a collective recognition by IFCs that higher regulatory and legislative standards are likely to have net overall benefits. This has led to collective action. The Caribbean Financial Action Task Force (CFATF) – to which 12 Commonwealth countries and 6 British Dependencies belong – is a good example of this. The CFATF was established at a Caribbean Drug Money Laundering Conference in Aruba in 1990, and has gradually developed as a regional initiative, with over two dozen members and a small secretariat. Members of CFATF have been prepared to move faster together than any individual members would probably have done separately.

Another example of collective action has been the work of the Offshore Group of Banking Supervisors, which was originally established to act as a central point of contact between a number of IFCs and the Basle Committee. This grouping has established a set of minimum standards for all its members (including implementation of the FATF Recommendations), and has recently evaluated its membership against those standards.

As an organisation containing most of the established IFCs, the Commonwealth is particularly well placed to take this exercise further. The commendation by Heads of Government of the FATF Recommendations, and the agreement by both Law and Finance Ministers to work collectively to combat the laundering of the proceeds of all types of serious crime provides a basis for co-ordinated progress among all Commonwealth countries.

Issues for discussion

What obstacles exist to collective action to introduce money laundering legislation? What role can Commonwealth Finance Ministers play in encouraging Commonwealth and non- Commonwealth IFCs to introduce effective regimes?

Regulatory standards

Introduction

The role of the regulatory authority is critical to the success of an IFC. The regulatory authority, in conjunction with the government, must maintain sufficiently strict authorisation criteria to keep away unsound financial institutions, while attracting a sufficient number of high-quality applications to maintain a viable sector. While the individual reputation of each IFC plays a major part in the second criterion, it is the determination and skill of the regulatory authority that ensures success with the first criterion.

Conflicts of interest

The biggest problem for regulatory authorities is the possibility of conflicts of interest arising between the promotion of the financial sector and its regulation. This can be exacerbated by political involvement in financial institutions or overambitious targets for growth of the sector.

Such conflicts of interest cannot always be avoided, but they can be addressed in a number of ways. These include:

- the separation of responsibility for regulation and promotion as far as this is possible;
- prohibition of any active involvement by serving members of the government in the running of financial institutions; and
- the full declaration of any interests in a decision by all those with any responsibility for it.

Relationships with overseas authorities

By their nature, regulators in IFCs are likely to have frequent contact with regulators in other jurisdictions, seeking legitimate information about the activities of financial institutions. At the same time they may well be subject to "fishing expeditions" conducted by foreign revenue authorities, seeking information on which to develop a case against a suspected tax evader. It is important that the means exist to offer suitable co-operation in both cases, while not breaching confidentiality by responding inappropriately.

One of the most effective ways of achieving this is through the negotiation of mutual legal assistance treaties (MLATs), or, less formally, MoUs, with those jurisdictions that most frequently make requests for assistance. These agreements can specify the circumstances under which a request for assistance will be considered, the nature of assistance that might be provided, and any restrictions that might be placed on the onward transmission of information.

Issues for discussion

What steps can be taken to ensure that regulatory standards are maintained in IFCs in the light of increasing international competition? How can these high standards be presented in a way that will attract sound business while deterring illicit funds?

Confidentiality legislation

Introduction

A feature of many IFCs (and of some other jurisdictions) is the adoption of a statutory basis for financial and commercial confidentiality. Such legislation is often introduced to reassure potential investors that their legitimate right to confidentiality will be respected. It is particularly attractive to those who consider that their domestic rights to confidentiality have been undermined for any reason, such as a hostile and confiscatory government, or corruption within the domestic financial system.

The possible grounds under the Common Law for overriding confidentiality are discussed in Part 3. Unless specific account is taken of these in framing such legislation, it may end up hampering an IFC from being able to take action against criminals, and particularly money launderers, operating within its territory. This situation can be tackled through the introduction of appropriate legislative **gateways.**

Gateways

The purpose of gateways in confidentiality legislation is to establish strictly limited circumstances under which confidentiality may be overridden. These circumstances normally reflect those established in common law by the *Tournier* decision (discussed in Part 3 of this paper). The legislation sets out:

- to whom confidential information may be passed;
- the circumstances under which this is permitted; and
- restrictions on the onward passage of the information.

Most confidentiality legislation permits information to be passed to the supervisory authorities to enable those authorities to carry out their proper functions. An effective anti-money laundering regime must also permit confidential information to be passed to the authorities responsible for combating money laundering where an institution knows or suspects that a transaction in which it is involved relates to the proceeds of crime. It must also permit the disclosure of confidential information to law enforcement agencies investigating money laundering cases, subject to appropriate judicial procedures, such as the obtaining of a court order.

Where the transaction involves other jurisdictions, it is important that it is permissible to

pass the appropriate information to the authorities in those other jurisdictions if this is desirable. It is however possible to restrict the use that may be made of that information. Information to be used for criminal or regulatory purposes may, for instance be passed subject to the proviso that it cannot be used for tax purposes.

Issues for discussion

Where there exists confidentiality legislation, to what extent do Commonwealth members envisage problems in introducing appropriate gateways? What steps can be taken to ensure that the correct balance is struck between the need to maintain confidentiality and the need to tackle money laundering effectively and thoroughly?

Practical issues

Introduction

The requirements of the FATF Recommendations discussed in Part III are relevant to IFCs as well as to other jurisdictions. However the international nature of much IFC business makes the practical application of some of the Recommendations more complicated.

Customer identification

Customer identification can be a problem for IFCs as the financial institutions located there will usually never have face-to-face contact with their customers. Indeed, where the financial institution is a "managed bank", or similar booking operation, such contact is non-existent.

In these circumstances reliance must be placed on financial institutions and intermediaries who have actual contact with the clients. Often these will be part of the same financial conglomerate as the local operation. Under these circumstances it is important to ensure that the overseas entities are subject to effective money laundering countermeasures. Where the client contact is through an unrelated intermediary, it is important that the intermediary is subject to adequate regulation, and has itself been subject to identification by the local financial institution. Some of the trade associations involved in international financial business have introduced codes of practice in this area. One example is the Association of International Life Offices (AILO), who recommend a very clear "know your intermediary" approach.

Record keeping

Record keeping also gives rise to concerns. It is important that sufficient information is held locally to allow the reconstruction of transactions. This may well need to include customer identification evidence, or at least sufficient evidence to link the transactions to the customer on whose behalf they were conducted. Where "booking operations" are permitted, it is vital that there is sufficient regulatory control to ensure that a person within the local jurisdiction – for instance the "managing" bank – is answerable for the transactions put through the booking operation if money laundering is involved.

Issues for discussion

Do the special features of IFCs present any particular practical problems for the implementation of the FATF Recommendations? What steps can the regulatory authorities in IFCs take to ensure that adequate anti-money laundering controls are in place in financial institutions without a physical presence within their jurisdiction?

Internal systems and controls

While "managed" banks have little in the way of internal systems, it is important that the business conducted through them is subject to the same

level of surveillance and control as any other transactions. This responsibility must fall upon the managing bank responsible for the managed bank's operations. This responsibility under money laundering legislation will tend to reflect the fiduciary duty owed by the managing bank. Depending upon the terms of the relationship between the two institutions the managing bank may in any case be responsible for the activities of the banks that it manages. The terms of this relationship will, of course, be a matter for the regulatory authorities.

5

Parallel Economy:
Tax Evasion, Economic Crime and Money Laundering

The problem of economic crime

Introduction

Many countries suffer from high levels of economic crime, which hinder their efforts to achieve sustainable economic growth. Particular problems include:

- **tax evasion.** Individuals and corporations systematically under-report or fail to declare their income for tax purposes, using anonymous bank accounts to hide the true situation, or relying on cash transactions;
- **evasion of exchange and capital controls.** Money is taken out of the country through over- and under-invoicing, or direct smuggling of currency or high value items, in breach of legal requirements;
- **corruption.** Government officials are bribed to award government contracts to particular firms or to divert aid flows.

These crimes have a number of common features. For instance they all rely on concealment of the movement of money, either across national boundaries or within a single country, and they are all ultimately tied into the financial system.

Financial and economic deregulation

A number of countries have deregulated their economies in order to improve both productive and resource allocative efficiency. The trend towards financial and economic deregulation has both a positive and a negative impact on the problems of economic crime. By removing the regulations and restrictions that are subject to abuse, certain forms of economic crime automatically fall away – it is impossible to have a crime of exchange control evasion if there are no exchange controls.

At the same time deregulation could bring 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.

It is important therefore to consider how the approaches to tackling money laundering discussed in Part 3 can be used to combat the laundering of the proceeds of economic crime.

Factors which complicate the combating of economic crime

There are a number of factors that have tended to make co-ordinated action against economic crime difficult. These include:

- different national definitions of offences. In some countries, for instance, tax evasion is not treated as a criminal matter;
- unclear border lines between criminal and non-criminal behaviour. What may in one case be treated as the legal payment of commissions to intermediaries may in another case count as bribery;
- the refusal by many countries actively to assist in the exchange of information and collection of taxes by another. Similarly countries with no exchange controls are often unwilling and unable to assist in monitoring the controls that are imposed by another country.

Some of the issues are dealt with in more detail below.

Tax evasion

Tax evasion and tax avoidance

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

Such an approach to tax law is bound to have an impact on the attitude that individuals and corporations have to tax law. It becomes an obstacle rather than an important element of the national infrastructure, and is thus treated with contempt rather than with respect.

This unfortunate situation, common to both developed and developing countries, is compounded by the complex nature of many tax regimes and the different methods by which tax law and other aspects of criminal law are enforced.

The legal treatment of tax evasion

In many countries tax evasion may frequently be pursued through civil, rather than criminal means. This is usually because the prime objective for the revenue authorities is to recover tax revenues, rather than to punish the tax evader. Such cases are usually treated outside the criminal courts, and settled through repayment of money, often coupled with an administrative fine.

In some countries tax evasion can ***only*** be dealt with through civil procedures. Under these circumstances international co-operation based on any form of dual criminality cannot be used to act against a suspected tax evader.

Many countries have taken the decision to exclude tax-related offences from their money laundering legislation. In other countries the offences are still subject to the money laundering legislation, but information that might relate to the laundering of the proceeds of fiscal offences are not passed to the revenue authorities. Other countries have, however, 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.

The attitude of financial institutions

Financial institutions are often key elements in the "tax planning industry". They are used by individuals and corporations in the process of tax planning and asset handling. This puts them in a difficult position when money laundering legislation is applied.

Financial institutions will frequently have insufficient information to determine whether a customer's activities – clearly aimed at minimising tax liabilities – represent avoidance or evasion. There will be a strong temptation for the institution not to "rock the boat", but instead to turn a blind eye and hope for the best.

Issues for discussion

Do sufficient channels of communication exist between law enforcement and revenue authorities to allow effective co-operation in following up money laundering cases? To what extent might financial institutions be encouraged to co-operate with the revenue authorities without their losing the trust of their legitimate clients?

As was discussed in Part 3, the co-operation of financial institutions is a major element of an effective anti-money laundering regime. It will be natural for financial institutions to seek to assist their clients rather than the tax authorities. Any heavy-handed action by the revenue authorities against financial institutions is likely to strength-

en this attitude, and thus to reduce the effectiveness of the regime as a whole. Thus the application of money laundering legislation to tax evasion must be carefully handled.

Bribery and corruption

Introduction

Bribery and corruption potentially throws up similar definitional problems. The borderline between legal and illegal payments may in some cases be as hard to police as that between tax avoidance and tax evasion. A more crucial problem however is that of international treatment of such payments. In particular there may be differences between the criminal treatment of the ***making*** of illicit payments and the ***receiving*** of corrupt payments.

International action against corrupt payments

There have been two recent international initiatives to respond to the problem of corrupt payments. The first has been taken by the OECD, which has drafted a recommendation designed to outlaw corrupt payments. The principal target of the recommendation has been commercial enterprises seeking contracts with developing country governments. The recommendation brings OECD countries more closely into line with the United States Foreign Corrupt Practices Act.

The second initiative is the establishment of a new non-governmental organisation, Transparency International (TI), which is working with governments, multilateral agencies and commercial companies to tackle the problems of bribery and corruption. One of the main areas of TI's early activity has been the creation of draft contract terms, which aim to ensure that contractors and subcontractors do not make corrupt payments while engaged in government contracts.

Money laundering legislation and corrupt payments

These two initiatives may, in time, provide a widely accepted basis for international co-operation to tackle corrupt payments directly. Meanwhile, however, money laundering legislation can assist in this.

Where financial institutions know their customers, and therefore can recognise abnormal financial flows within customer accounts, they should become suspicious of the large financial flows generated by corrupt payments. Government officials will tend to have a fairly regular flow of income, from the government, with a limited range of outside sources of funds. Payments from foreign corporations, or large deposits of cash arising from bribes, will therefore be noticeable. Provided that financial institutions are alert, they will be able to pass on indications of such illicit behaviour to the relevant authorities, as discussed in Part 3.

Issues for discussion

How can Commonwealth countries ensure that corrupt payments can be recognised clearly as such? How can governments ensure that corruption does not occur within the regulatory system itself? How can financial institutions guard against corruption?

Tackling money laundering in the informal financial sector

Introduction

In many Commonwealth countries it is recognised that there is a significant "parallel economy", in which money circulates. Because they are open to use by those seeking to avoid taxation or regulatory control, the existence of parallel economies is of direct relevance to efforts to combat money laundering.

Parallel economies, and within them, "informal financial institutions", often have origins in traditional social structures. However they are currently used to allow the circumvention of tax-

ation or certain aspects of government regulation (such as exchange controls). By their nature, parallel economies and those that operate within them avoid the scrutiny of government and law enforcement agencies, even when their activities are not strictly illegal, or are in practice condoned by government.

These circumstances tend to generate fertile ground for money launderers, who use the parallel economy to move money that is not merely seeking to avoid regulation, but in fact derives from serious criminal activity. Clearly this is distinctly unwelcome in itself, in that it offers another route for money laundering. It also has damaging effects on others who participate in the parallel economy by bringing them into contact with organised crime. Many people who facilitate the movement of money through informal financial institutions, while recognising that their activities are not strictly legal, do not see them as ***actually criminal.*** Their behaviour in other respects is likely therefore to be fully within the law. Once they have become corrupted by contact with organised and serious crime, however, this may change, making them less easy to monitor and control.

The impact of money laundering legislation

In those countries where a significant "parallel economy" exists, one effect of implementing anti-money laundering legislation in the formal financial sector may be to drive criminal business and other rent-seeking activities into the informal sector.

It is, in theory, possible to apply legislation directly to the informal financial sector, requiring customer identification and record keeping in the same way that it is required of formal financial institutions. In practice such an approach will not work. With no regulation and no supervision it would not be possible to identify which individuals or families were operating as informal financial institutions. With little or no written information within the network, as is often the case, it would be difficult to establish what transactions had occurred, and who was involved. There would certainly be no realistic prospect of suspicions being reported.

Alternative approaches to tackling the informal sector

Since the informal sector is not susceptible to a direct approach, it is necessary to consider indirect approaches. In practice these will tend to involve reducing the attractiveness of the informal sector to money launderers.

Wealth in the informal sector may be held in a number of ways, including real estate – where the difference between the "white" or declared price of property and the "black" or actual price represents an unrecorded asset. However for criminals using the parallel economy it is necessary for the wealth to be more easily transferable. This may involve holdings of gold, silver or precious stones, which are easily transportable. More often, however, it will be in the form of money in bank accounts which cannot be directly connected to the individuals to whom it belongs. Large scale activity in the parallel economy must therefore involve accounts at formal financial institutions.

The interface between the formal and informal sectors may provide an opportunity for tackling the problem. Financial institutions should, for instance, be encouraged to pay particular attention to the accounts that they suspect relate to informal sector operations – including foreign currency accounts and accounts held by trusts or offshore companies, whether or not the account holders are suspected of direct involvement in money laundering.

The use of informal financial systems to move money internationally is a particular problem for investigators tackling money laundering. International co-operation in tackling cases of laundering through the parallel economy may be of some value, particularly if it can increase understanding of the operation of the parallel economy in different countries.

Restrictions on the use of cash

At a broader level, the cash basis of the parallel economy can be tackled by measures aimed at

reducing the use of cash. Where it is practical, salaries could be paid directly into bank accounts. Modern electronic methods of money management, such as the greater use of credit and debit cards, could be encouraged. For many Commonwealth countries this would however be a major undertaking, and would need to be addressed as a long term project rather than as a quick fix.

An effective intermediate step might however be to outlaw the use of cash payments for transactions above a certain size. Large transactions would require the involvement of financial institutions. This would ensure that those involved in the transactions were subject to formal identification, the transactions would be recorded, and the process would be subject to the money laundering controls applying in the formal economy.

Such an approach could be introduced gradually, beginning with a relatively high threshold, and gradually reducing it as the financial system developed in response to the opportunity that this would present.

Issues for discussion

Can the interface between the formal and informal sector be more effectively controlled? Are existing initiatives to improve tax collection and to deregulate the economy likely to be useful in tackling money laundering in the informal sector? Can these initiatives be fine tuned to improve their effectiveness in this context.

Cash transaction reporting systems

Introduction

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 **cash transaction reporting (CTR) system.** This approach is outlined in FATF Recommendation 24.

How a CTR system works

Under a CTR regime financial institutions would report any transaction above a fixed threshold involving cash, or "near cash" (eg travellers cheques, bearer bonds and other easily negotiable monetary instruments) to the central unit. It would be possible to require the reporting of telegraphic transfers of money into and out of the country above the same limit (or alternatively of any size), and also the physical importation or exportation of cash or "near cash" above a fixed limit, to the same unit. This information would then be put on a database and thus made available to investigators.

Regimes of this sort are in place in Australia (where the threshold is AUS$10,000) and the United States (where the threshold is US$10,000). Experience suggests that such systems are expensive to operate. AUSTRAC, the central unit in the Australian system, received over 750,000 reports in 1993, and its operating budget for that year was about Aus$ 15 million.

The costs of AUSTRAC can be compared to the benefits, not merely in combatting the laundering of the proceeds of drug trafficking and other similar forms of crime, but also in recovering tax revenues that might otherwise have escaped the system. The Australian Tax Office (ATO) estimated that the CTR system led directly to the recovery of around AUS$30 million of revenue that would otherwise not have been paid in the first four years of AUSTRAC's operation. This is roughly equivalent to the operating costs of AUSTRAC over that period. There may have been additional benefits from the deterrent effect of the system on tax-payers who might otherwise have tried to evade paying tax. The ATO have said that they are looking to make more use of AUSTRAC data in future, which should lead to an even greater recovery of

tax for relatively little additional expenditure.

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 available to revenue authorities to use to pursue tax evasion,** this might be an attractive option for some Commonwealth governments. However, without an ongoing commitment to manage the large volumes of data generated, financed through recovered revenue, it is likely to be more of a burden than a benefit. In the early years of such a system the capital investment would be large, with returns initially low. The CTR approach therefore requires a clear long term commitment if it is to work.

The draft model law does not contain provisions establishing a CTR system. However the Australian Financial Transaction Reports Act 1988 offers an example of this approach which could be modified by other Commonwealth countries wishing to adopt such a system.

Issues for discussion

Is there sufficient commitment to support the large initial investment that an effective CTR system entails? Is the necessary infrastructural and technological base available to ensure that the system will be maintained? Is the scale of tax recovery likely to justify the operating costs?

Reducing the use of cash

Introduction

Legislation to combat money laundering tends to concentrate on the formal financial sector. However, not all economic activity involves the formal sector. The problems of the parallel economy have been discussed above. More generally, a high degree of cash intensiveness in an economy, even where this is not associated with tax or regulatory evasion, reduces the need to use financial institutions and hence increases the ease with which launderers can handle criminal proceeds. Measures to reduce the use of cash increase the difficulty – and therefore risk – to launderers of handling large quantities of cash. The more uncommon large cash transactions are, the more likely it is that they will be reported as suspicious, and thus the more likely that those relating to criminal activity will be identified.

The benefits of reducing cash intensiveness

Alternatives to cash have additional benefits, both for governments and for the private sector. Payment of wages directly into bank accounts, rather than in cash, is now a legal requirement in some Commonwealth countries, and contributes to preventing tax evasion, as well as reducing the costs and security risks of administering large quantities of cash.

The use of cheques, credit cards and debit cards reduces the costs to banks and other financial institutions of cash handling, and the development of stored value cards increases the convenience of using "electronic cash" while reducing the risks of theft and counterfeiting.

The effect of these measures is to encourage financial flows out of cash and into institutions, where they can be more effectively monitored and controlled. While this offers clear benefits to legitimate users of the financial system it greatly increases the risk to criminals, who are more likely to be required to explain the source of their money. However, the transitional issues have also to be recognised e.g. the higher cost of credit card transactions, credit card fraud, etc.

The costs of reducing cash intensiveness

It is important to recognise that such measures tend to require considerable investment by financial institutions and the Central Bank in order to work effectively. In the short to medium term the necessary investment may pose problems for small scale commercial enterprises. In many countries reliance on cash as a means of exchange is culturally embedded and there is a

distrust of cheques and other modern forms of payment. In some countries where there is a large rural population with limited access to banking there is no practical alternative to cash.

Clearly any move to reduce the use of cash must be considered as a long term initiative. Its value in combatting money laundering complements its advantages in terms of economic efficiency and potentially improved revenue collection.

Issues for discussion

What scope exists within Commonwealth countries to reduce dependence on cash? What steps are possible in the immediate and the longer term? How can financial institutions be encouraged to take action in this area? What measures can be taken to increase public confidence in alternatives to cash?

6

Key Issues, Action Steps and Conclusions

Action steps

Introduction

Many of the topics identified in this paper are technical matters, on which Senior Officials may wish to comment and reach a good measure of agreement in the course of their deliberations in Sri Lanka. Decisions in respect of other issues could be taken at the political level. For Senior Officials the main purpose of discussing these subjects will be to distil the key underlying issues, so that Finance Ministers can be presented with the clearest possible basis for reaching their conclusions.

The practical points include:

- the introduction of legislation where it is not already in place;
- the establishment of central unit for handling suspicion disclosures, with support for its role at the highest political level;
- a commitment by financial supervisors to cooperate closely with these central units;
- agreement that financial supervisors to produce guidance notes, in consultation with all interested parties;
- agreement to the establishing of a network of agreements between financial supervisors and others in Commonwealth countries to facilitate international co-operation;
- the introduction of a self-evaluation procedure;
- agreement on a role for the Secretariat, including research on new issues, co-ordination of the self evaluation process, liaison with FATF, acting as clearing house for technical assistance, and assistance with implementation of the model law.

The types of proposal that might be put to Finance Ministers are discussed below.

Legislation

Some Commonwealth members have already introduced comprehensive legislation to combat money laundering. Other members have legislation addressing some of the elements that have been discussed in this paper. Some have no money laundering legislation at all.

The Commonwealth Secretariat has produced a draft *Model Law for the Prohibition of Money Laundering*. This is intended for common law countries, and covers all the issues addressed by the 40 FATF Recommendations and discussed in this paper. Adoption of legislation based on the Model will allow all Commonwealth countries who do not yet have their own comprehensive legislation to meet the target endorsed by Heads of Government.

Senior Officials of Law Ministries are to discuss the Model at their meeting in Malta at the end of May. After taking account of any modifications proposed there, or by Senior Finance Officials in Sri Lanka, the law will be available for implementation, with the Secretariat able to offer assistance in adapting it to any particular local requirements within individual Commonwealth countries.*

* The Model Money Laundering Bill prepared by the Secretariat was presented to Law Ministers when they met in April 1996.

Senior officials might therefore be able to recommend to Finance Ministers that legislation, using the Model Law if desired, might be introduced by all Commonwealth countries at the earliest opportunity.

Central units for handling suspicion disclosures

It is clear from the discussion in this paper that a national central unit for handling suspicious disclosures is a crucial element in any anti-money laundering regime. The location of such a unit within the structure of government, supervision and law enforcement will, however, depend upon the situation prevailing in each individual Commonwealth member. Finance Ministers might be invited to give a commitment to the establishing of such a unit in each Commonwealth country where one is not already established.

For a central unit to be effective, it must be adequately resourced, and must be able to rely upon strong support at the highest political level. It is therefore important that Finance Ministers, Central Bank Governors and Heads of Government be requested to give the necessary public commitment to each central unit, if it is established, and to the role for which it is established.

The role of financial supervisors

Wherever the central unit is established it will need to work closely with the existing financial supervisory agencies, so that the respective tasks of the different organisations can be carried out efficiently without unnecessary additional administrative burdens being placed on financial institutions. Senior officials might recommend to Finance Ministers that their commitment to action against money laundering include a willingness to promote co-operation among all the agencies concerned, also at the highest level.

Guidance notes

In order to assist financial institutions to operate new money laundering legislation efficiently, it is important that they are given guidance by the supervisory authorities. Senior officials might recommend to Finance Ministers that the supervisory authorities, in conjunction with all other agencies with a role in the combatting of money laundering, and with the financial sector itself, might draw up guidance notes setting out best practice in all the areas covered by the legislation, and offering examples of money laundering cases and potentially suspicious transactions.

International co-operation

Senior officials of Commonwealth Law Ministries are already examining the scope for a network of agreements between Commonwealth business and financial regulatory agencies, to complement the agreements and treaties being established to assist co-operation in criminal matters. Clearly this work will be of assistance in developing international co-operation in cases of money laundering.

The situation may be complicated by the treatment of information relating to fiscal offences, which may fall outside existing tax treaties and mutual legal assistance treaties. Senior officials might therefore like to consider how they can take forward work in this area in consultation with their Law Ministry colleagues, and with the Secretariat. Finance Ministers might be invited to support this proposal.

Self-evaluation

One of the key elements of the strategy to tackle money laundering is a process of self- evaluation. Commonwealth countries who are members of the Financial Action Task Force or the Caribbean Financial Action Task Force are already familiar with this process. Self-evaluation serves two main purposes. Firstly it allows all Commonwealth countries to see how they are progressing in taking forward the mandate of Heads of Government to implement the FATF Recommendations. Secondly, and equally importantly, it allows those countries that are in need of technical assistance in carrying the project forward to analyse their needs clearly, so that an appropriate assistance programme can be devised.

Those countries that are members of FATF or CFATF might agree to the respective secretariats of those two task forces passing on the responses to their self-evaluation questionnaires to the Commonwealth Secretariat. Those countries who are not members of either task force might agree to complete a self-evaluation questionnaire modelled closely on the FATF version. The Commonwealth Secretariat could then produce an analysis of the responses to these questionnaires for the possible consideration of Finance Ministers.

If Senior Finance Officials endorse this approach, the proposal could be discussed at the Finance Ministers Meeting in Jamaica and if Ministers were to approve, the first questionnaires could be issued before the end of 1995.

The role of the Secretariat

In light of the above points, Senior Finance Officials might consider recommending that the Commonwealth Secretariat be given a number of responsibilities, subject to resource availability:

- assistance to Commonwealth countries in adapting and implementing the draft Model Law for the Prohibition of Money Laundering;
- liaison with both the FATF and CFATF Secretariats to ensure that Commonwealth countries remain up to date in their understanding of money laundering and strategies to combat it;
- co-ordination of the self-evaluation process; and
- acting as a clearing house for requests for and offers of technical assistance.

Key issues for possible further discussion by finance ministers

Introduction

In addition to the technical issues discussed above, there remain a number of more complex political issues which Finance Ministers might wish to discuss in more depth.

Compatibility with economic and financial reform

Finance Ministers will need to satisfy themselves that measures to tackle money laundering are compatible with the steps they are taking to reform their countries' economic and financial systems. The evidence suggests not only that action against money laundering is compatible with economic and financial reform, but that such action complements and reinforces those reforms if appropriately implemented.

Application of money laundering legislation to economic crime

Action against money laundering in developing countries can make a valuable contribution to combatting economic crime, and in particular tax evasion. This is an issue that has in general not been addressed by the Financial Action Task Force. International co-operation may well be complicated by an unwillingness on the part of many countries to provide information. Finance Ministers might be invited in particular to consider whether it is possible to agree upon a framework for the exchange of information relating to economic and fiscal crime between Commonwealth countries.

The parallel economy

A related issue which again has received relatively little consideration in the past is the implications for action against money laundering of the existence in many countries of a parallel economy. The fact that these parallel economies are largely cash-based implies that action to reduce the use of cash will, in the long term, address this problem. In the short to medium term, however, Ministers might wish to consider interim steps, such as prohibiting the use of cash for transactions above a certain size, or transactions within particular sectors of the economy (such as the property market).

Implementation of FATF Recommendations in international financial centres

Many Commonwealth countries are looking to the establishment of an international financial

sector as a key element in their economic growth and development. For these countries action to combat money laundering is an important part of the process of demonstrating an appropriate level of probity and soundness. However it is necessary that such action should be handled with care. Finance Ministers might wish to discuss this, and to consider how effective action against money laundering can be presented publicly without giving rise to unjustified fears over the erosion of client confidentiality, credibility of financial institutions and efforts of countries to develop financial centres.

Technical assistance

Officials might wish to discuss in Sri Lanka what technical assistance will be needed by countries moving to establish money laundering countermeasures, and what might be available from Commonwealth countries and elsewhere. Particular areas that will be important include:

- assistance with drafting and implementing legislation that is sufficiently wide-ranging and effective to meet the remit endorsed by Heads of Government;
- assistance with training staff within government departments and regulatory authorities to oversee the operation of systems and controls against money laundering;
- assistance with training within financial institutions so that they can play their part in combatting money laundering.

While officials could identify what assistance will be needed and might be available, it would be for Finance Ministers to consider how such assistance could be mobilised and deployed.

Timetable

Finally it would be for Finance Ministers to consider whether a timetable could be set for action on the various issues discussed above.

Conclusion

This paper has set out the background to the decision by Finance Ministers to convene a meeting of senior officials to discuss the economic and financial problems of money laundering and the way to tackle them. It has identified a number of issues for discussion, and has set out a possible way forward. Senior officials are invited to discuss all these points in the course of the Sri Lanka meeting. Following their discussions they are invited to report their conclusions to Finance Ministers at their meeting in Kingston, Jamaica, later in the year.

Annex A

FATF Recommendations relevant to the Financial Sector*

The scope of application of the Recommendations

9 The Recommendations 12 to 29 of this paper should apply not only to banks, but also to non-bank financial institutions.

10 The appropriate national authorities should take steps to ensure that these Recommendations are implemented on as broad a front as is practically possible.

11 A working group should further examine the possibility of establishing a common minimal list of non-bank financial institutions dealing with cash subject to these Recommendations.

Customer identification

12 Financial institutions should not keep anonymous accounts or accounts in obviously fictitious names: they should be required (by law, by regulations, by agreements among financial institutions or by self-regulatory agreements among financial institutions) to identify, on the basis of an official or otherwise reliable identifying document, and record the identity of clients, either occasional or usual, when establishing business relations or conducting transactions (in particular opening of accounts or passbooks, entering into fiduciary transactions, renting of safe deposit boxes, performing large cash transactions).

13 Financial institutions should take reasonable measures to obtain information about the true identity of the persons on whose behalf an account is opened or a transaction is conducted if there are any doubts as to whether these clients or their customers are not acting on their own behalf, in particular, in the case of domiciliary companies (i.e. institutions, corporations, foundations, trusts etc, that do not conduct any commercial or manufacturing business or any other form of commercial operation in the country where their registered office is located).

Record keeping

14 Financial institutions should 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 behaviour.

Financial institutions should keep records on customer identification (e.g. copies or records of official documentation of documents like passports, identity cards, driving licences or similar documents), account files and business correspondence for at least five years after the account is closed.

These documents should be available to domestic competent authorities, in the context of criminal prosecutions and investigations.

Handling of suspicious transactions

15 Financial institutions should pay special attention to all complex, unusual, large transactions, and all unusual patterns of transactions, which have no apparent economic or visible legal purpose. The background and purpose of such transactions should, as far as possible, be examined, the findings established in writing, and be available to help supervisors, auditors and law enforcement agencies.

16 If financial institutions suspect that funds stem from a criminal activity, they should be permitted or required to report promptly their suspicions to the competent authorities. Accordingly there should be legal provision to protect financial institutions and their employees from criminal or civil liability for breach of any legislative, regulatory or administrative provision, if they report in good faith, in disclosing suspected activity to the competent authorities, even if they have not known precisely what the underlying criminal activity was, and regardless of whether illegal activity actually occurred.

17 Financial institutions, their directors and employees, should not, or, where appropriate, should not be allowed to warn their customers when information relating to them is being reported to the competent authorities.

18 In the case of a mandatory reporting system, or in the case of a voluntary reporting system where appropriate, financial institutions reporting their

* the original FATF Recommendations were revised by the FAFT in June 1996 and are reproduced in in Annex C

suspicions should comply with instructions from the competent authorities.

19 In countries where no obligation of reporting these suspicions exists, when a financial institution develops suspicions about operations of a customer, and when the financial institution chooses to make no report to the competent authorities, it should deny assistance to this customer, sever relations with him and close his accounts.

Internal systems and controls for financial institutions

20 Financial institutions should develop programmes against money laundering. These programs should include, as a minimum:

(a) the development of internal policies, procedures and controls, including the designation of compliance officers at management level, and adequate screening procedures to ensure high standards when hiring employees;

(b) an ongoing employee training programme;

(c) an audit function to test the system.

Transactions involving countries that do not apply the FATF Recommendations

21 Financial institutions should give special attention to business relationships and transactions with persons,including companies and financial institutions, from countries which do not, or insufficiently apply these Recommendations. Whenever these transactions have no economic or visible lawful purpose, their background and purpose should, as far as possible, be examined, the findings established in writing, and be available to help supervisors, auditors and law enforcement agencies.

22 Financial institutions should ensure that the principles mentioned above are also applied to branches and majority owned subsidiaries located abroad, especially in countries which do not, or insufficiently apply these Recommendations, to the extent that local applicable laws and regulations permit. When local applicable laws and regulations prohibit their implementation, competent authorities in the country of the mother institution should be informed by the financial institutions that they cannot apply these Recommendations.

Other measures to combat money laundering

23 The feasibility of measures to detect or monitor cash at the border should be studied, subject to strict safeguards to ensure proper use of information and without impeding in any way the freedom of capital movements.

24 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 database, available to competent authorities for use in money laundering cases, subject to strict safeguards to ensure proper use of the information.

25 Countries should further encourage the development of modern and secure techniques of money management, including increased use of cheques, payment cards, direct deposit of salary cheques, and book entry recording of securities, as a means to encourage the replacement of cash transfers.

The role of the supervisory authorities

26 The competent authorities supervising banks or other financial institutions or intermediaries, or other competent authorities, should ensure that the supervised institutions have adequate programs to guard against money laundering. These authorities should cooperate and lend expertise spontaneously or on request with other domestic, judicial or law enforcement authorities in money laundering investigations and prosecutions.

27 Competent authorities should be designated to ensure an effective implementation of all these Recommendations, through administrative supervision and regulation, in all other professions dealing with cash as defined by each country.

28 The competent authorities should establish guidelines which will assist financial institutions in detecting suspicious patterns of behaviour by their customers. It is understood that such guidelines must develop over time, and will never be exhaustive. It is further understood that such guidelines will primarily serve as an educational tool for financial institutions' personnel.

29 The competent authorities regulating or supervising financial institutions should take the necessary legal or regulatory measures to guard against control of, or acquisition of a significant participation in financial institutions by criminals or their confederates.

Annex B

Tackling Money Laundering in the Securities Sector

1 Introduction

1.1 Action to combat money laundering has traditionally centred on banks and other deposit-taking institutions. This reflects the historic emphasis on the laundering of street cash derived from the sale of narcotics. However a comprehensive approach to money laundering must involve all aspects of the financial system, and must cover money that has already been placed into the financial system, and also money deriving from other forms of crime that has never been in the form of cash. Clearly such an approach needs to take account of the possibility of money being laundered through securities business as well as more traditional types of financial activity.

2 The Structure of the Securities Industry

2.1 For the purposes of this annex, the securities industry is defined as the following:

- the buying and selling of securities (both equity and debt);
- trading in financial derivatives (including both exchange traded and over the counter instruments);
- the operation and marketing of collective investment schemes;
- participation in share issues, including privatisations.

2.2 There is a wider range of institution/client relationships in securities business than in traditional banking. While there is no exact equivalent of a bank account into which and from which the customer may move money, a stockbroker may hold securities or money on his clients' behalf, usually in nominee accounts. However it is possible for a client to use a stockbroker merely to buy or sell securities, with no long term relationship being established.

2.3 The relationship between financial institutions and the beneficial owners of financial assets may also be more complicated in the securities field. In the case of collective investments, for instance, the beneficial owners are the unit holders whose direct contact is with the scheme operator, while the transactions involving the investment fund itself will be carried out by investment managers. There need be no direct contact between these investment managers and the beneficial owners of the funds that they manage.

2.4 There is also a very wide range of assets involved. Equities may be held in the form of registered shares, bearer shares, or in dematerialised form within an automated electronic settlement system. Derivatives range from standardised futures and options contracts, tradeable on exchanges, to complex swaps and other "manufactured" contracts, known as OTCs ("Over-the Counter" contracts).

2.5 Transactions in the securities business may take place on organised markets, involving large numbers of participants, including professional counterparties. These markets often operate at high speed and in circumstances where it is inappropriate for market participants to reveal their identity or that of their customers before the deal is complete, if at all, for fear of moving the market against them.

2.6 Finally, participants in the securities markets do not, in general, accept funds in the form of cash. Most transactions are settled through cheques drawn on or wire transfers from bank accounts. This renders the securities markets unlikely to be used as vehicles for the "placement" phase of money laundering, but vulnerable to the "layering" and "integration" phases.

2.7 With these features of the business in mind, it is possible to consider their relevance to the elements of a strategy to combat money laundering.

3 Customer identification and record keeping (FATF Recommendations 12 – 14)

3.1 In many countries, securities brokers are required to maintain information that can identify their "clients", and in most countries this will be done for commercial reasons in any case. However the extent to which this is effective as an element of an anti-money laundering strategy depends crucially upon what definition is adopted of the word "client".

3.2 Market participants will frequently be asked to deal on behalf of a client who is himself acting on instructions from a third party. Chains of instructions may be long, and may involve participants in more than one country. Individual instructions may be aggregated as they are passed down the chain, or groups of transactions may be broken up and given to different institutions. Clearly it is not practical for all those in the chain of instructions to know the identity of all those involved.

3.3 The most sensible option is probably to ensure that any participant in securities business is fully aware of the identity of his immediate clients, including both

those who instruct or are instructed to deal, and those involved in the settlement of accounts. With effective record keeping procedures, which should not cause particular difficulties in the securities area, it will then be possible, for any transaction, to reconstruct what happened, where the instructions came from, and where the assets, securities and money involved moved from and to.

3.4 Where transactions are conducted through a formal exchange, such as a Stock Exchange, the trading and settlement systems may mean that it is impossible, and probably inappropriate, for traders to know who is on the other side of their deals. For practical purposes each participant treats the exchange itself as their counterparty, for both trading and settlement (this latter function may be operated by a separate clearing house). In this situation it is very important that the exchange itself (and where appropriate, the clearing house) is aware of the identities of all its members.

3.5 The identification requirements outlined here are unlikely to place much, if any additional burden on financial institutions and financial exchanges and clearing houses. Most securities business involves the extension of credit to those involved, and the carrying of risk. Market participants will therefore be careful to know who it is with whom they are dealing, so that they can make a fair assessment of the degree of risk involved in the transactions.

3.6 Indeed the experience of some countries has been that legal identification requirements have had a wholly beneficial effect, empowering the institutions to establish their clients identities more firmly, without the fear of driving legitimate business away.

4 Recognising and handling suspicious transactions (FATF Recommendations 15-19)

4.1 One way of identifying a transaction as suspicious is to ask the question "does it make sense", in the context of the customer involved, and any other available information. The complexity of securities transactions, and the wide variety of instruments and strategies available mean that many transactions that at first glance look unusual may often be entirely sensible in the light of all the circumstances.

4.2 Derivatives transactions are particularly relevant here. Clients may take large and complex positions in derivatives markets, and then liquidate them after a few days. Such behaviour might well be unusual in equity or bond markets, but in derivatives markets it might reflect a range of entirely legitimate possibilities: a short term speculative position to benefit from market volatility, or indeed a short term hedge against such volatility; an arbitrage opportunity between markets that disappears fairly quickly; a hedge against a position taken in another market until that position can be laid off.

4.3 The close relationship between markets, especially between derivative markets and markets trading their underlying assets, means that an apparent run of loss-making investments in one market may actually be a hedge offset by a corresponding series of profitable investments elsewhere. The transactions and the hedges may well involve different brokers, as well as different markets. As a result, nobody is in a position to see the whole picture, except the beneficial investor himself.

4.4 Since the transactions themselves are unlikely to raise suspicions, it is all the more important that they should be considered in the context of the customer. If a normally unadventurous customer starts moving large sums of money, or starts taking risky positions, this may be indicative of something unusual – heavy losses on one market, paid for with criminal proceeds, and offset by profits on a related market paid out in clean funds, for instance. Changes in settlement instructions, especially those involving settlement to overseas banks apparently unrelated to normal business may also be danger signals. A securities institution that knows its customers well will often recognise such signs, and will be in a position not only to consider reporting them to the authorities, but also whether it wishes to continue to do business with such a customer.

5 Internal systems and controls (FATF Recommendation 20)

5.1 One factor within much of the securities industry that makes it particularly vulnerable to money laundering is the emphasis on trading as much as possible, as quickly as possible. Securities traders will often see any form of supervision as an inconvenience to be circumvented, so that they can go back to making money. Introducing internal systems and controls, and particularly staff training regimes, is therefore more difficult than in other areas, and at the same time arguably more important.

5.2 Ultimately, however, securities firms depend on their reputation almost as much as banks, and it is the threat to that reputation that is the biggest incentive for the introduction of effective internal systems.

6 Conclusion

6.1 The nature of the securities industry, the variety of activities involved and the range of relationships and structures all tend to complicate the task of introducing effective money laundering countermeasures. There are however no major impediments to the application of the strategy established in the policy paper to this sector. The ability of securities firms to move and transform large amounts of money very quickly makes them attractive to money launderers. No system of combating laundering can therefore be considered effective if it does not cover the securities sector.

Annex c

The FATF Forty Recommendations*

A General framework of the recommendations

1 Each country should take immediate steps to ratify and to implement fully, the 1988 United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances (the Vienna Convention).

2 Financial institution secrecy laws should be conceived so as not to inhibit implementation of these Recommendations.

3 An effective money laundering enforcement program should include increased multilateral co-operation and mutual legal assistance in money laundering investigations and prosecutions and extradition in money laundering cases where possible.

B Role of national legal systems in combating money laundering

Scope of the Criminal Offence of Money Laundering

4 Each country should take such measures as may be necessary, including legislative ones, to enable it to criminalise money laundering as set forth in the Vienna Convention. Each country should extend the offence of drug money laundering to one based on serious offences. Each country would determine which serious crimes would be designated as money laundering predicate offences.

NOTE TO 4:

Countries should consider introducing an offence money laundering based on all serious offences and/or on all offences that generate a significant amount of proceeds.

5 As provided in the Vienna Convention, the offence of money laundering should apply at least to knowing money laundering activity, including the concept that knowledge may be inferred from objective factual circumstances.

6 Where possible, corporations themselves – not only their employees – should be subject to criminal liability.

Provisional Measures and Confiscation

7 Countries should adopt measures similar to those set forth in the Vienna Convention, as may be necessary, including legislative ones, to enable their competent authorities to confiscate property laundered, proceeds from, instrumentalities used in or intended for use in the commission of any money laundering offence, or property of corresponding value without prejudicing the rights of bona fide third parties.

Such measures should include the authority to: (1) identify, trace and evaluate property which is subject to confiscation; (2) carry out provisional measures, such as freezing and seizing, to prevent any dealing, transfer or disposal of such property; and (3) take any appropriate investigative measures.

In addition to confiscation and criminal sanctions, countries also should consider monetary and civil penalties, and/or proceedings including civil proceedings, to void contracts entered into by parties, where parties knew or should have known that as a result of the contract, the State would be prejudiced in its ability to recover financial claims, e.g. through confiscation or collection of fines and penalties.

C Role of the financial system in combating money laundering

8 Recommendations 10 to 29 should apply not only to banks, but also to non-bank financial institutions. Even for those non-bank financial institutions which are not subject to a formal prudential supervisory regime in all countries, for example bureaux de change, governments should ensure that these institutions are subject to the same anti- money laundering laws or regulations as all other financial institutions and that these laws or regulations are implemented effectively.

NOTE TO 8:

The FATF Recommendations should be applied in particular to life insurance and other investment products offered by insurance companies, whereas Recommendation 29 applies to the whole of the insurance sector.

* The forty Recommendations were originally drawn up in 1990. In 1996 these were revised to take into account the experience gained over the last six years and to reflect the changes which have occurred in the money laundering problem. During the period 1990 to 1995, the FATF also elaborated various Interpretative Notes which are designed to clarify the application of specific Recommendations. Some of these Interpretative Notes have been updated in the Stocktaking Review to reflect changes in the Recommendations.

9 The appropriate national authorities should consider applying Recommendations 10 to 21 and 23 to the conduct of financial activities as a commercial undertaking by businesses or professions which are not financial institutions, where such conduct is allowed or not prohibited. Financial activities include, but are not limited to, those listed in the attached annex. It is left to each country to decide whether special situations should be defined where the application of anti-money laundering measures is not necessary, for example, when a financial activity is carried out on an occasional or limited basis.

NOTE TO 8 AND 9(BUREAUX DE CHANGE):

Introduction

1 *Bureaux de change are an important link in the money laundering chain since it is difficult to trace the origin of the money once it has been exchanged. Typologies exercises conducted by the FATF have indicated increasing use of bureaux de change in laundering operations. Hence it is important that there should be effective counter- measures in this area. This Interpretative Note clarifies the application of FATF Recommendations concerning the financial sector in relation to bureaux de change and, where appropriate, sets out options for their implementation.*

Definition of Bureaux de Change

2 *For the purpose of this Note, bureaux de change are defined as institutions which carry out retail foreign exchange operations (in cash, by cheque or credit card). Money changing operations which are conducted only as ancillary to the main activity of a business have already been covered in Recommendation 9. Such operations are therefore excluded from the scope of this Note.*

Necessary Counter-Measures Applicable to Bureaux de Change

3 *To counter the use of bureaux de change for money laundering purposes, the relevant authorities should take measures to know the existence of all natural and legal persons who, in a professional capacity, perform foreign exchange transactions.*

4 *As a* ***minimum*** *requirement, FATF members should have an effective system whereby the bureaux de change are known or declared to the relevant authorities (whether regulatory or law enforcement). One method by which this could be achieved would be a requirement on bureaux de change to submit to a designated authority, a simple declaration containing adequate information on the institution itself and its management. The authority could either issue a receipt or give a tacit authorisation: failure to voice an objection being considered as approval.*

5 *FATF members could also consider the introduction of a formal authorisation procedure. Those wishing to establish bureaux de change would have to submit an application to a designated authority empowered to grant authorisation on a case-by- case basis. The request for authorisation would need to contain such information as laid down by the authorities but should at least provide details of the applicant institution and its management. Authorisation would be granted, subject to the bureau de change meeting the specified conditions relating to its management and the shareholders, including the application of a "fit and proper" test.*

6 *Another option which could be considered would be a combination of declaration and authorisation procedures. Bureaux de change would have to notify their existence to a designated authority but would not need to be authorised before they could start business. It would be open to the authority to apply a "fit and proper" test to the management of bureaux de change after the bureau had commenced its activity, and to prohibit the bureau de change from continuing its business, if appropriate.*

7 *Where bureaux are required to submit a declaration of activity or an application for registration, the designated authority (which could be either a public body or a self-regulatory organisation) could be empowered to publish the list of registered bureaux de change. As a minimum, it should maintain a (computerised) file of bureaux de change. There should also be powers to take action against bureaux de change conducting business without having made a declaration of activity or having been registered.*

8 *As envisaged under FATF Recommendations 8 and 9, bureaux de change should be subject to the same anti-money laundering regulations as any other financial institution. The FATF Recommendations on financial matters should therefore be applied to bureaux de change. Of particular importance are those on identification requirements, suspicious transactions reporting, due diligence and record-keeping.*

9 *To ensure effective implementation of anti-money laundering requirements by bureaux de change, compliance monitoring mechanisms should be established and maintained. Where there is a registration authority for bureaux de change or a body which receives declarations of activity by bureaux de change, it should carry out this function. But the monitoring could also be done by other designated authorities (whether directly or through the agency of third parties such as private audit firms). Appropriate steps would need to be taken against bureaux de change which failed to comply with the anti-laundering requirements.*

10 *The bureaux de change sector tends to be an unstructured one without (unlike banks) national representative bodies which can act as a channel of communication with the authorities. Hence it is important that FATF members should establish effective means to ensure that bureaux de change are aware of their anti-money laundering responsibilities and to relay information, such as guidelines on suspicious transactions, to the profession. In this respect it would be useful to encourage the development of professional associations.*

Customer identification and record-keeping rules

10 Financial institutions should not keep anonymous accounts or accounts in obviously fictitious names: they should be required (by law, by regulations, by

agreements between supervisory authorities and financial institutions or by self-regulatory agreements among financial institutions) to identify, on the basis of an official or other reliable identifying document, and record the identity of their clients, either occasional or usual, when establishing business relations or conducting transactions (in particular opening of accounts or passbooks, entering into fiduciary transactions, renting of safe deposit boxes, performing large cash transactions).

In order to fulfill identification requirements concerning legal entities, financial institutions should, when necessary, take measures:

(i) to verify the legal existence and structure of the customer by obtaining either from a public register or from the customer or both, proof of incorporation, including information concerning the customer's name, legal form, address, directors and provisions regulating the power to bind the entity;

(ii) to verify that any person purporting to act on behalf of the customer is so authorised and identify that person.

11 Financial institutions should take reasonable measures to obtain information about the true identity of the persons on whose behalf an account is opened or a transaction conducted if there are any doubts as to whether these clients or customers are acting on their own behalf, for example, in the case of domiciliary companies (i.e. institutions, corporations, foundations, trusts, etc. that do not conduct any commercial or manufacturing business or any other form of commercial operation in the country where their registered office is located).

NOTES TO *11, 15-17*

Whenever it is necessary in order to know the true identity of the customer and to ensure that legal entities cannot be used by natural persons as a method of operating in reality anonymous accounts, financial institutions should, if the information is not otherwise available through public registers or other reliable sources, request information – and update that information – from the customer concerning principal owners and beneficiaries. If the customer does not have such information, the financial institution should request information from the customer on whoever has actual control.

If adequate information is not obtainable, financial institutions should give special attention to business relations and transactions with the customer.

If, based on information supplied from the customer or from other sources, the financial institution has reason to believe that the customer s account is being utilised in money

laundering transactions, the financial institution must comply with the relevant legislation, regulations, directives or agreements concerning reporting of suspicious transactions or termination of business with such customers.

Note to 11: *A bank or other financial institution should know the identity of its own customers, even if these are represented by lawyers, in order to detect and prevent suspicious transactions as well as to enable it to comply swiftly to information or seizure requests by the competent authorities. Accordingly Recommendation 11 also applies to the situation where an attorney is acting as an intermediary for financial services.*

12 Financial institutions should maintain, for at least five years, all necessary records on transactions, both domestic or 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 behaviour.

Financial institutions should keep records on customer identification (e.g. copies or records of official identification documents like passports, identity cards, driving licences or similar documents), account files and business correspondence for at least five years after the account is closed.

These documents should be available to domestic competent authorities in the context of relevant criminal prosecutions and investigations.

13 Countries should pay special attention to money laundering threats inherent in new or developing technologies that might favour anonymity, and take measures, if needed, to prevent their use in money laundering schemes.

Increased diligence of financial institutions

14 Financial institutions should pay special attention to all complex, unusual large transactions, and all unusual patterns of transactions, which have no apparent economic or visible lawful purpose. The background and purpose of such transactions should, as far as possible, be examined, the findings established in writing, and be available to help supervisors, auditors and law enforcement agencies.

NOTE TO *14:*

(a) In the interpretation of this requirement, special attention is required not only to transactions between financial institutions and their clients, but also to transactions and/or shipments especially of currency and equivalent instruments between financial institutions themselves or even to transactions within financial groups. As the wording of Recommendation 14 suggests that indeed all transactions are covered, Recommendation 14 must be read to incorporate these inter-bank transactions.

(b) The word transactions should be understood to refer to the insurance product itself, the premium payment and the benefits.

15 If financial institutions suspect that funds stem from a criminal activity, they should be required to report promptly their suspicions to the competent authorities.

16 Financial institutions, their directors, officers and employees, should be protected by legal provisions from criminal or civil liability for breach of any restriction on disclosure of information imposed by contract or by any legislative, regulatory or administrative provision, if they report their suspicions in good faith to the competent authorities, even if they did not know precisely what the underlying criminal activity was, and regardless of whether illegal activity actually occurred.

17 Financial institutions, their directors, officers and employees, should not, or, where appropriate, should not be allowed to, warn their customers when information relating to them is being reported to the competent authorities.

18 Financial institutions reporting their suspicions should comply with instructions from the competent authorities.

19 Financial institutions should develop programs against money laundering. These programs should include, as a minimum:

(i) the development of internal policies, procedures and controls, including the designation of compliance officers at management level, and adequate screening procedures to ensure high standards when hiring employees;

(ii) an ongoing employee training programme;

(iii) an audit function to test the system.

Measures to cope with the problem of countries with no or insufficient anti-money laundering measures

20 Financial institutions should ensure that the principles mentioned above are also applied to branches and majority owned subsidiaries located abroad, especially in countries which do not or insufficiently apply these Recommendations, to the extent that local applicable laws and regulations permit. When local applicable laws and regulations prohibit this implementation, competent authorities in the country of the mother institution should be informed by the financial institutions that they cannot apply these Recommendations.

21 Financial institutions should give special attention to business relations and transactions with persons, including companies and financial institutions, from countries which do not or insufficiently apply these Recommendations. Whenever these transactions have no apparent economic or visible lawful purpose, their background and purpose should, as far as possible, be examined, the findings established in writing, and be available to help supervisors, auditors and law enforcement agencies.

Other measures to avoid money laundering

22 Countries should consider implementing feasible measures to detect or monitor the physical cross-border transportation of cash and bearer negotiable instruments, subject to strict safeguards to ensure proper use of information and without impeding in any way the freedom of capital movements.

NOTE TO 22:

(a) To facilitate detection and monitoring of cash transactions, without impeding in any way the freedom of capital movements, members could consider the feasibility of subjecting all cross-border transfers, above a given threshold, to verification, administrative monitoring, declaration or record keeping requirements.

(b) If a country discovers an unusual international shipment of currency, monetary instruments, precious metals, or gems, etc., it should consider notifying, as appropriate, the Customs Service or other competent authorities of the countries from which the shipment originated and/or to which it is destined, and should co-operate with a view toward establishing the source, destination, and purpose of such shipment and toward the taking of appropriate action.

23 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 cases, subject to strict safeguards to ensure proper use of the information.

24 Countries should further encourage in general the development of modern and secure techniques of money management, including increased use of checks, payment cards, direct deposit of salary checks, and book entry recording of securities, as a means to encourage the replacement of cash transfers.

25 Countries should take notice of the potential for abuse of shell corporations by money launderers and should consider whether additional measures are required to prevent lawful use of such entities.

Implementation, and role of regulatory and other administrative authorities

26 The competent authorities supervising banks or other financial institutions or intermediaries, or other competent authorities, should ensure that the supervised institutions have adequate programs to guard against money laundering. These authorities should co-operate and lend expertise spontaneously or on request with other domestic judicial or law enforcement authorities in money laundering investigations and prosecutions.

NOTE TO 26:

In respect of this requirement, it should be noted that it would be useful to actively detect money laundering if the competent authorities make relevant statistical information available to the investigative authorities, especially if this information contains specific indicators of

money laundering activity. For instance, if the competent authorities statistics show an imbalance between the development of the financial services industry in a certain geographical area within a country and the development of the local economy, this imbalance might be indicative of money laundering activity in the region. Another example would be manifest changes in domestic currency flows without an apparent legitimate economic cause. However, prudent analysis of these statistical data is warranted, especially as there is not necessarily a direct relationship between financial flows and economic activity (e.g. the financial flows in an international financial centre with a high proportion of investment management services provided for foreign customers or a large inter-bank market not linked with local economic activity).

27 Competent authorities should be designated to ensure an effective implementation of all these Recommendations, through administrative supervision and regulation, in other professions dealing with cash as defined by each country.

28 The competent authorities should establish guidelines which will assist financial institutions in detecting suspicious patterns of behaviour by their customers. It is understood that such guidelines must develop over time, and will never be exhaustive. It is further understood that such guidelines will primarily serve as an educational tool for financial institutions personnel.

29 The competent authorities regulating or supervising financial institutions should take the necessary legal or regulatory measures to guard against control or acquisition of a significant participation in financial institutions by criminals or their confederates.

NOTE TO 29:

Recommendation 29 should not be read as to require the introduction of a system of regular review of licensing of controlling interests in financial institutions merely for anti-money laundering purposes, but as to stress the desirability of suitability review for controlling shareholders in financial institutions (banks and non-banks in particular) from a FATF point of view. Hence, where shareholder suitability (or fit and proper) tests exist, the attention of supervisors should be drawn to their relevance for anti-money laundering purposes.

D Strengthening of international co-operation

Administrative Co-operation

Exchange of general information

30 National administrations should consider recording, at least in the aggregate, international flows of cash in whatever currency, so that estimates can be made of cash flows and reflows from various sources abroad, when this is combined with central bank information. Such information should be made available to the International Monetary Fund and the Bank for International Settlements to facilitate international studies.

31 International competent authorities, perhaps Interpol and the World Customs Organisation, should be given responsibility for gathering and disseminating information to competent authorities about the latest developments in money laundering and money laundering techniques. Central banks and bank regulators could do the same on their network. National authorities in various spheres, in consultation with trade associations, could then disseminate this to financial institutions in individual countries.

Exchange of information relating to suspicious transactions

32 Each country should make efforts to improve a spontaneous or upon request international information exchange relating to suspicious transactions, persons and corporations involved in those transactions between competent authorities. Strict safeguards should be established to ensure that this exchange of information is consistent with national and international provisions on privacy and data protection.

Other forms of co-operation

Basis and means for co-operation in confiscation, mutual assistance and extradition

33 Countries should try to ensure, on a bilateral or multilateral basis, that different knowledge standards in national definitions – i.e. different standards concerning the intentional element of the infraction – do not affect the ability or willingness of countries to provide each other with mutual legal assistance.

NOTE TO 33:

Subject to principles of domestic law, countries should endeavour to ensure that differences in the national definitions of the money laundering offences,- e.g. different standards concerning the intentional element of the infraction, differences in the predicate offences, differences with regard to charging the perpetrator of the underlying offence with money laundering – do not affect the ability or willingness of countries to provide each other with mutual legal assistance.

34 International co-operation should be supported by a network of bilateral and multilateral agreements and arrangements based on generally shared legal concepts with the aim of providing practical measures to affect the widest possible range of mutual assistance.

35 Countries should be encouraged to ratify and implement relevant international conventions on money laundering such as the 1990 Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime.

Focus of improved mutual assistance on money laundering issues

36 Co-operative investigations among countries' appropriate competent authorities should be encouraged. One valid and effective investigative technique in this respect is controlled delivery

related to assets known or suspected to be the proceeds of crime. Countries are encouraged to support this technique, where possible.

NOTE TO 36:

The controlled delivery of funds known or suspected to be the proceeds of crime is a valid and effective law enforcement technique for obtaining information and evidence in particular on international money laundering operations. It can be of great value in pursuing particular criminal investigations and can also help in obtaining more general intelligence on money laundering activities. The use of these techniques should be strongly encouraged. The appropriate steps should therefore be taken so that no obstacles exist in legal systems preventing the use of controlled delivery techniques, subject to any legal requisites, including judicial authorisation for the conduct of such operations. The FATF welcomes and supports the undertakings by the World Customs Organisation and Interpol to encourage their members to take all appropriate steps to further the use of these techniques.

37 There should be procedures for mutual assistance in criminal matters regarding the use of compulsory measures including the production of records by financial institutions and other persons, the search of persons and premises, seizure and obtaining of evidence for use in money laundering investigations and prosecutions and in related actions in foreign jurisdictions.

38 There should be authority to take expeditious action in response to requests by foreign countries to identify, freeze, seize and confiscate proceeds or other property of corresponding value to such proceeds, based on money laundering or the crimes underlying the laundering activity. There should also be arrangements for co-ordinating seizure and confiscation proceedings which may include the sharing of confiscated assets.

NOTE TO 38:

(a) Each country shall consider, when possible, establishing an asset forfeiture fund in its respective country into which all or a portion of confiscated property will be deposited for law enforcement, health, education, or other appropriate purposes.

(b) Each country should consider, when possible, taking such measures as may be necessary to enable it to share among or between other countries confiscated property, in particular, when confiscation is directly or indirectly a result of co- ordinated law enforcement actions.

39 To avoid conflicts of jurisdiction, consideration should be given to devising and applying mechanisms for determining the best venue for prosecution of defendants in the interests of justice in cases that are subject to prosecution in more than one country. Similarly, there should be arrangements for co-ordinating seizure and confiscation proceedings which may include the sharing of confiscated assets.

40 Countries should have procedures in place to extradite, where possible, individuals charged with a money laundering offence or related offences. With respect to its national legal system, each country should recognise money laundering as an extraditable offence. Subject to their legal frameworks, countries may consider simplifying extradition by allowing direct transmission of extradition requests between appropriate ministries, extraditing persons based only on warrants of arrests or judgements, extraditing their nationals, and/or introducing a simplified extradition of consenting persons who waive formal extradition proceedings.

Miscellaneous Note: Deferred arrest and seizure

Countries should consider taking measures, including legislative ones, at the national level, to allow their competent authorities investigating money laundering cases to postpone or waive the arrest of suspected persons and/or the seizure of the money for the purpose of identifying persons involved in such activities for evidence gathering. Without such measures the use of procedures such as controlled deliveries and undercover operations are precluded.

List of Financial activities undertaken by business or professions which are not financial institutions

1 Acceptance of deposits and other repayable funds from the public.

2 Lending. Including *inter alia*:
consumer credit
mortgage credit
factoring, with or without recourse
finance of commercial transactions (including forfeiting).

3 Financial leasing.

4 Money transmission services.

5 Issuing and managing means of payment (e.g. credit and debit cards, cheques, traveller's cheques and banker's drafts ...)

6 Financial guarantees and commitments.

7 Trading foe account of customers (spot, forward, swaps, futures, options ...) in:
money market instruments (cheques, bills, CDs, etc.);
foreign exchange;
exchange; interest rate and index instruments;
transferable securities;
commodity futures trading.

8 Participation in securities issues and the provision of financial services related to such issues.

9 Individual and collective portfolio management.

10 Safe-keeping and administration of cash or liquid securities on behalf of clients.

11 Life insurance and other investment related insurance.

12 Money changing.

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