The case of money laundering Real administrative procedure used in the detection of fraudulent transactions

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1. Introduction

The commitment to combat money laundering preventively began more than twenty years ago when, in 1989, a group of industrial countries, including Belgium, decided to create the Financial Action Task Force (FATF).

The FATF [1] is an international organisation based at the OECD in Paris, which aims to combat money laundering and, more recently, terrorist financing activities, as well as others related threats to the integrity of the financial system.

The FATF's main purpose is to set up international standards to prevent money laundering and terrorist financing activities [2]: in 1990, it has adopted a series of recommendations which have been revised several times (in 1996, 2001, 2003 and 2012.

These 40 recommendations are now more or less implemented in most of the world's industrial countries.

They mainly include:

- know your customer due diligence measures;
- measures to identify beneficial owners and beneficial ownership of legal structures;
- constant due diligence measures regarding the transactions of customers;
- suspicious transactions reporting obligations;
- AML/CFT supervision of the financial sector and the designated non-financial businesses and professions;

[1] www.fatf.gafi.org.

[2] Its mandate also covers the fight against proliferation of weapons of mass destruction. But this will not be covered in this contribution.

– vigilance with regard to the NPO sector;
– measures with regard to the freezing of terrorist assets, ...

FATF Recommendation 29 requires countries to create a central and independent body in charge of receiving, analysing and disclosing financial information relating to money laundering and terrorist financing.

This body can be administrative, judicial or be part of the law enforcement authorities.

Many countries in the world have now set up Financial Intelligence Units (FIUs) and imposed AML/CFT measures to prevent the use of their financial system for money laundering and terrorist financing purposes.

The Belgian Financial Intelligence Unit CTIF-CFI[3], which was set up in 1993[4], is the Belgian central body that has been designated to apply recommendation 29.

CTIF-CFI is supervised by the ministers of justice and finance but is operationally independent.

CTIF-CFI acts as a filter between on the one hand the financial sector and a list of Designated Non-Financial Businesses and Professions (DNFBPs) and on the other hand the law enforcement authorities.

CTIF-CFI manages a huge database composed of different types of financial data collected from suspicious transactions' reports[5] (STRs), currency transactions' reports[6] (CTRs), cross-border transactions' reports[7] (CBTRs) and cross-border cash transactions' reports[8] (CBCTRs).

CTIF-CFI shares this intelligence with law enforcement authorities, tax authorities and intelligence services in case of serious indications of money laundering or terrorist financing.

2. General context

Nowadays, criminals use increasingly complex and international schemes to carry out their criminal activities and to launder the proceeds of these activities. They have abandoned the traditional banking system in favour of new payments methods, offshore financial centres and opaque offshore structures.

All these facilities are used by criminals but also by taxpayers misusing transfer pricing, trade misinvoicing and tax disparities between different countries.

As a consequence, criminal and financial investigations are now more complex.

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[3] http: //www.ctif-cfi.be.

[4] *Loi du 11 janvier 1993 relative à la prévention de l'utilisation du système financier aux fins du blanchiement de capitaux et du financement du terrorisme (modifiée à plusieurs reprises)*.

[5] STRs: any kind of suspicious transaction reported to the FIU and based on a subjective analysis of the suspicious transactions with regard to the profile of the customer.

[6] CTRs: transactions in cash automatically reported to the FIU when exceeding a given threshold (in general: EUR/USD 10,000).

[7] CBTRs: international transactions (wire transfers) automatically reported to the FIU when exceeding a given threshold (in general: EUR/USD 10,000).

[8] CBCTRs: declaration made by travellers when they travel with more than EUR 10,000 in cash.

A. The globalisation and interconnection of our economies and financial systems

The globalisation and interconnection of our economies and financial systems associated with the development of information technology (*e.g.* via the internet and e-money) make criminal and financial investigations more difficult.

It is a fact that, nowadays, criminals and terrorist financiers can move their dirty money from one country to another in less than two hours while criminal investigations take two years or so.

If correctly and efficiently applied, the preventive AML/CFT legislation is the right answer to money laundering and criminal activities.

FIUs now have extensive experience in financial analysis. Locating assets belonging to criminals is one of the FIU's assignments.

The FIU's capacity to respond is also much greater than law enforcement and the judicial authorities. FIUs have the capacity to take action sooner than law enforcement authorities because they only need indications of money laundering, instead of real evidence that could be used in court. Administrative information can be exchanged with foreign counterparts in just a few days as opposed to it taking months for evidence used in court to be exchanged.

In some countries FIUs can also, for a limited number of days and without a court order, freeze a suspicious transaction or funds suspected of being the proceeds of crime (see infra).

B. The transparency of legal persons and arrangements

In today's world, opaque and complex corporate structures are easy to acquire because they are provided "ready-made" and at very low cost by some local legal professionals but also by professionals in tax havens where the opacity of the structures provided is even greater.

Such corporate structures can be created as part of a multi-layered chain of inter-jurisdictional structures whereby a corporation in one jurisdiction may control or be controlled by other companies in another jurisdiction, making it harder to identify the real beneficial owner of the structures.

Services helping to conceal the identity of the beneficial owners of corporate structures, such as being nominee managers for corporations and limited companies and trustees for trusts as well as mailing or postal addresses for shell companies, are provided by many Trust and Company Services Providers.

Improving the transparency of corporate structures is crucial both to the financial sector that has obligations with regards to the beneficial owners and FIUs and law enforcement authorities.

Since 2008 the international community has been taking steps to deal with offshore financial centres and countries with legal professionals providing opaque legal structures.

These efforts have resulted in better international cooperation. But improving transparency is a difficult and ongoing task.

Even though FIUs have acquired experience in exchanging information with FIUs in offshore financial centres and the quality of the replies has improved, it is difficult

and can be even impossible to combat money laundering if the beneficial owner of the corporate structure is hidden and therefore unknown.

It is also worth mentioning that opaque corporate structures are not only available in tax havens but that legal professionals from certain prominent FATF country members, which claim to be "fit and proper", also provide such opaque corporate structures.

These countries have areas or zones (Jersey, Guernsey, Gibraltar, Delaware...) that can be considered to be tax havens as they have preferential tax rates or legal professionals providing opaque structures, facilitating tax fraud and the money laundering of criminal proceeds.

C. The overemphasis of tax havens

Some tax haven experts estimate that, today, more than 50% of the financial flows of money pass through structures or bank accounts in offshore financial centres.

It is a fact that many financial institutions around the world, and especially financial institutions active in the city of London and on the New York stock exchange, have branches and subsidiaries in offshore financial centres.

The globalisation of our economies contributes to greater opacity in the international financial markets, especially when transactions related to criminal activities are mixed up with legitimate and genuine financial transactions and when offshore subsidiaries of well-known financial institutions are used to move assets from one part of the world to another.

Bank accounts and investments in offshore financial centres and via offshore structures are, nowadays, also easily accessible to ordinary people as well.

Research results recently published by The International Consortium of Investigative Journalists showed that, in Belgium, not only rich people invest in tax havens but that mainly ordinary people use the offshore financial system for the purpose of tax evasion.

We must also be aware that the facilities provided by these offshore structures are not only used for tax evasion but that they are also used by criminals to launder the proceeds of their criminal activities.

The financial web formed by all these branches and subsidiaries and their parent companies makes it ever more difficult to distinguish illicit transactions from all the transactions circulating inside the international financial system.

D. Poor international cooperation

Today criminal activities, especially money laundering activities, have no borders and borders are not a problem for criminals but an advantage. Criminals skilfully use borders to avoid disruption by law enforcement.

This means that appropriate international cooperation is important to combat criminal activities effectively and to trace financial flows, identify the origin or the destination of the funds and seize them if possible.

In the field of international cooperation we are nowadays increasingly faced with the "counterproductive" objection claiming that "I do not cooperate because the others do not cooperate". This objection is becoming increasingly common nowadays.

However. it is crucial to combat this taboo and to put an end to one of the main obstacles to effective international cooperation.

With regard to administrative cooperation, CTIF-CFI never refuses a request for assistance but provides full assistance to foreign counterparts: law enforcement information, financial information and information from commercial databases are always provided on request. There are no legislative impediments that could restrict exchange of information with other FIUs. However, full administrative cooperation is not the case in many countries and the "fiscal alibi" is currently still used by many "offshore countries" to refuse international cooperation.

As it will be mentioned later on, in some Member States, FIUs have efficient tools/powers in their hands. This is for instance the case of the CTIF-CFI to freeze a bank account or to order the postponement of a suspicious transaction during a period of maximum five working days, and including upon request made in due form by a foreign FIU [9].

This best practice is not yet implemented in many countries in the world. This has an impact on the FIU's capacity to follow the flow of funds and on law enforcement's capacity to identify and seize criminal assets.

With regard to judicial cooperation, experience shows that some obstacles still exist:

- the requirement to start a police investigation in order to exchange information, especially to obtain bank information;
- ill will;
- a lengthy process to carry out international letters rogatory;
- no response, a late response or an incomplete response;
- no response in case of a fiscal dimension;
- insufficient available human resources;
- use of bank secrecy as justification for a refusal to cooperate;
- issues with certain countries in carrying out judicial seizures;
- as already mentioned, "fiscal alibi" to justify the lack of transparency of legal structures located in their jurisdiction to avoid responding to international requests regarding money laundering investigations.

E. The race to obtain bigger profits

The race to obtain bigger profits, especially in times of financial crisis, is sometimes more important for financial institutions than complying with the FATF's AML/CFT standards, as recent cases involving Standard Chartered, HSBC, ... or ING have proved.

These financial institutions have recently been involved in AML/CFT cases and have been punished in the United States with huge fines or settlements (between USD 600 and 2,000 million).

It is no longer possible today to apply full AML/CFT measures to every single financial transaction and it is generally accepted that a risk-based approach is fundamental.

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[9] See Article 23, para. 2, of the abovementionned Law of 11 January 1993.

This is why the FATF asks financial institutions to analyse their ML/TF risks and apply risk-based policies to lower the identified risks.

This means that the AML/CFT measures applied will depend on the level of risk associated with a customer type or a product type.

Some customers, like PEPs [10], could entail higher risk than an ordinary citizen.

As the aforementioned AML/CFT cases prove, in practice, some financial institutions do not fully and properly apply the FATF risk-based approach recommendations.

Some financial institutions do not analyse their customer and product ML/TF associated risks but analyse their own risks of being involved in a money laundering or terrorist financing case and the financial consequences for them and for their reputation.

F. Serious tax crimes

Capital flight, including tax evasion, is facilitated by tax systems that are vulnerable to harmful tax practices.

Various cases have recently come to light involving companies such as Apple, British Tobacco, Arcelor Mittal or Amazon, to name but a few. These show that, nowadays, large industrial groups are quick to take advantage of tax disparities between jurisdictions.

Legal professionals do not consider these mechanisms as tax crime but as "tax optimisation".

However, the voluntary use of multiple opaque shell companies or shell companies in offshore financial centres as well as the use of foreign legal professionals as front men (representatives) and the use of manipulated transfer prices (to avoid paying corporate taxes anywhere in the world except in the country offering the lowest income tax rate) should perhaps be considered as tax crimes and not as "tax optimisation".

But it is difficult for a country alone to combat these corporate tax evasion mechanisms because they are a result of protectionist measures decided by some (offshore) countries.

Nowadays, some countries still misuse the "professional secrecy principle" to protect their banking sector and legal professionals provide opaque corporate structures, which also creates unfair competition.

Protectionism is also one of the "unacknowledged" reasons why these (offshore) countries are reluctant to cooperate with foreign law enforcement authorities and FIUs.

Experience shows that handling cases regarding tax fraud or with potential tax connections is generally more complex and some countries do not or are reluctant to grant authorisation to use or report the information to the judicial authorities in case there is a fiscal dimension (see *supra* the "fiscal alibi").

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[10] PEPs: Politically Exposed Persons (former prime minister or minister, ambassadors, ...).

3. How can the financial sector (and DNFBPs) and Financial Intelligence Units help criminal investigations?

A. Have up-to-date national cooperation

Adequate cooperation between all national competent authorities (regulators and supervisors, FIU, law enforcement, judicial authorities, tax authorities, customs...) in charge of combating money laundering and terrorist financing is a valuable instrument to trace, disrupt and confiscate funds of illicit origin.

It is imperative for countries to use financial intelligence upstream and downstream within their value chain. This means that the flow of financial intelligence between regulators, supervisors, FIUs, law enforcement and other competent authorities should be free-flowing to and from all entities in accordance with existing domestic laws, policies and procedures [11].

Cooperation between these authorities is important not only for ML/TF cases (operational cooperation) but also to identify and analyse new trends, risks and vulnerabilities relating to money laundering or terrorist financing.

The FATF standards now formally request Member States and other countries that they assess their risks of and vulnerabilities to money laundering and terrorist financing [12] and, based on the risks identified, have national up-to-date AML/CFT policies. This includes designating a national coordination authority (or another coordination mechanism) responsible for such AML/CFT policies [13].

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[11] FATF Operational Issues – Financial Investigations Guidance, June 2012, www.fatf.gafi.org.

[12] Countries should identify, assess, and understand the money laundering and terrorist financing risks for the country, and should take action, including designating an authority or mechanism to coordinate actions to assess risks, and apply resources, aimed at ensuring the risks are mitigated effectively. Based on that assessment, countries should apply a risk-based approach (RBA) to ensure that measures to prevent or mitigate money laundering and terrorist financing are commensurate with the risks identified. This approach should be an essential foundation to efficient allocation of resources across the anti-money laundering and countering the financing of terrorism (AML/CFT) regime and the implementation of risk-based measures throughout the FATF recommendations. Where countries identify higher risks, they should ensure that their AML/CFT regime adequately addresses such risks. Where countries identify lower risks, they may decide to allow simplified measures for some of the FATF recommendations under certain conditions. Countries should require financial institutions and designated non-financial businesses and professions (DNFBPs) to identify, assess and take effective action to mitigate their money laundering and terrorist financing risks. (FATF recommendation 1), www.fatf-gafi.org

[13] Countries should have national AML/CFT policies, based on the risks identified, which should be regularly reviewed and should designate an authority or have a coordination or other mechanism that is responsible for such policies. Countries should ensure that policy-makers, the financial intelligence unit (FIU), law enforcement authorities, supervisors and other relevant competent authorities, at the policymaking and operational levels, have effective mechanisms in place which enable them to cooperate, and, where appropriate, coordinate domestically with each other concerning the development and implementation of policies and activities to combat money laundering, terrorist financing and the financing of the proliferation of weapons of mass destruction. (FATF recommendation 2), www.fatf-gafi.org.

B. Collecting and analysing financial information related to criminal conduct

The FIUs, which act as a filter between the financial sector and the law enforcement authorities, manage huge databases composed of different types of financial data collected from suspicious transactions' reports [14] (STRs), currency transactions' reports [15] (CTRs), cross-border transactions' reports [16] (CBTRs) and cross-border cash transactions' reports [17] (CBCTRs).

Not sharing this intelligence with other competent authorities is unwise and counterproductive.

Sharing this intelligence with law enforcement authorities only on request of law enforcement authorities is also counterproductive.

It is essential that FIUs proactively analyse the STRs, CTRs, CBTRs and CBCTRs received to detect potential unknown money laundering and predicate offences activities.

This means that, when, during the FIUs analytical process, FIUs identify serious indications of money laundering or terrorist financing activities, FIUs must immediately share this intelligence with law enforcement, with tax authorities and with intelligence services.

Most FIUs now have the legal power to request (additional) information from:

- the reporting entity itself;
- other reporting entities;
- law enforcement, prosecutor offices, intelligence services;
- tax authorities, social security services.

However, an administrative FIU has no legal power to intercept and interrogate criminals, to execute house searches and to arrest and take criminals into custody.

C. Freezing assets belonging to criminals

As underlined previously, some FIUs have been equipped with important powers and tools. The Belgian law of 11 January 1993 on the prevention of the use of the financial system for money laundering or terrorist financing purposes allows CTIF-CFI, in case of indication of a suspicion of money laundering or terrorist financings, to freeze, for a period of a maximum of five working days, the execution of a financial transaction or any transaction on a specific bank account. If the CTIF-CFI deems that this measure must be extended, it immediately refers the matter to the competent Public Prosecutor or to the Federal Public Prosecutor.

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[14] STRs: any kind of suspicious transactions' reported to the FIU and based on a subjective analysis of the suspicious transactions with regard to the profile of the customer.

[15] CTRs: transactions in cash automatically reported to the FIU when exceeding a given threshold (in general: EUR/USD 10,000).

[16] CBTRs: international transactions (wire transfers) automatically reported to the FIU when exceeding a given threshold (in general: EUR/USD 10,000)

[17] CBCTRs: declaration made by travellers when they travel with more than EUR 10,000 in cash.

In case of serious indications of money laundering, the judicial authorities may freeze the funds for a longer period of time and will cooperate with the judicial authorities from the requesting country to repatriate the criminal funds.

4. Conclusions

A. Main weaknesses and obstacles

It is a fact that the fight against money laundering, predicate offences and terrorist financing lacks effectiveness.

According to estimates by the United Nations, only 1% of the proceeds of crime is seized and confiscated annually in the world.

Even though the legal systems and AML/CFT legislation of certain countries are rather effective, their effectiveness is badly affected by the lack of effectiveness or by the weaknesses of their neighbours. It is difficult for one country alone to be effective in fighting criminals and criminal activities if, in the meantime, (offshore) countries continue to provide criminals with facilities to launder the proceeds of their criminal activities.

Amongst these facilities we have:

i) Opaque corporate structures

Financial investigations are crucial in fighting money laundering and terrorist financing, yet the transparency of the financial structures used to launder money or finance terrorism is also very important, both for FIUs and law enforcement to identify the actual beneficial owners of corporate structures. Many countries in the world still allow legal professionals to set up legal structures with a high level of anonymity.

The fight against offshore financial centres is a long and difficult ongoing task for the international community.

Initiatives taken at national level are important but must be supplemented by initiatives taken by the international community.

For several years now Belgium has requested that every citizen mentions on his/her tax return if he/she holds a foreign bank account. More recently, Belgium requests that every citizen mentions on his/her tax return if he/she has links with a structure in an offshore financial centre.

These initiatives can improve transparency but must be coordinated at international level.

ii) Our legal systems are not yet sufficiently harmonised

The different legal systems are not yet fully harmonised (including within the 28 EU Member States), which sometimes makes financial investigations more difficult or impossible.

In Belgium, the AML/CFT legal framework[18] authorises the FIU to request financial information from all reporting entities, also upon request from a foreign counterpart. The FIU can obtain information such as the contact details of a bank

[18] Article 33 of the Law of 11 January 1993 on preventing the use of the financial system for money laundering or terrorist financing.

account holder, the references of bank accounts held by a suspect or details of transactions on a bank account. The FIU can analyse and share this information with a foreign counterpart upon request and without any prior consent or a court order.

In other countries, the FIU is not allowed by law or by other regulations to request this financial information upon request of a foreign counterpart. As a result, the ability of the requesting FIU to trace the flow of suspicious funds and the ability of law enforcement authorities to confiscate the proceeds of crime are affected or the confiscation becomes impossible.

Unlike the Belgian FIU (CTIF-CFI) (see *infra*) many foreign FIUs are still not allowed to freeze money upon the request of a counterpart FIU.

iii) Protection from the state still helps some countries to provide these opaque offshore structures and bank accounts without any risk, consequence or repercussions

The protection that offshore countries provide to their financial sector (principle of professional secrecy and the "fiscal alibi") and their legal professionals (opaque corporate structures) is no longer acceptable.

B. What can be done to disrupt criminal activities, tax evasion and money laundering?

First of all, it is crucial that solutions to the problem of tax evasion and to the problem of capital flight (illicit financial flows from tax evasion and from illicit and criminal activities) are found.

To achieve this objective, every country in the world, and especially tax havens, must effectively and efficiently apply all the FATF's international standards and abolish tax disparities.

If a solution is not found to both issues (tax rates disparities and capital flight), criminals, tax evaders and money launderers will continue to move their assets into the countries that are most appealing in terms of tax rates and opacity.

In addition, it is also crucial to have:

i) Well-informed (risk-based) and coordinated intelligence-led policies and actions

The cooperation between law enforcement, FIU and intelligence services… is important not only for a specific criminal activity investigation or for a ML/TF case but also to identify and analyse new trends, risks and vulnerabilities.

As mentioned previously (see *supra*), the FATF standards formally require States to assess their risks of and vulnerabilities to money laundering and terrorist financing and, based on the risks identified, have national up-to-date AML/CFT policies.

This national ML/TF risk assessment must receive input from a specific risk assessment made by the law enforcement authorities, by the supervisory authorities of the financial institutions and DNFBPs, by their professional associations, by the intelligence services and Customs and Excise administration.

The FATF recommendations include the designation of a national coordination authority (or another mechanism of coordination) responsible for the national risk assessment and the AML/CFT policies.

Hoever, currently, only a few countries already have such mechanisms in place. The concerned FATF recommendations should be better implemented

ii) More intelligence-sharing

Different law enforcement departments or law enforcement, tax authorities and intelligence services are still, for objectionable reasons (self protectionism), reluctant to exchange information and to act following consultation.

Looking beyond this taboo is crucial for a country to be effective. Experience has shown that coordinated actions are the actions that have generated the best results.

Intelligence obtained from other law enforcement departments, from local police, from the tax authorities, from customs or from foreign counterparts can be essential in targetting specific controls and targetting seizure and confiscation measures.

Cooperation between all the competent authorities is also crucial in terrorist financing cases because the nature of transactions related to terrorist financing make them more difficult to detect and to intercept.

Terrorist financiers use terrorist financing techniques that conceal terrorist financing transactions from law enforcement authorities:

– funds financing terrorism sometimes have a (apparent) legal origin;
– official and legitimate non-profit organisations are sometimes used as a vehicle for terrorist financing purposes so that legal and illegal financing transactions are mixed up;
– the funds are sometimes sent to countries where it it is difficult for law enforcement authorities to prove the illicit use of the funds;
– apparent legal wire transfers (payments made in favour of a school for the education of the children of a terrorist) could be a compensation for the contribution to a terrorist act or plot.

The use of intelligence from intelligence services or foreign counterparts is sometimes the best approach to disrupt terrorist financing activities.

iii) More and faster international cooperation

More and faster unlimited international cooperation is one of the main conditions needed to fight criminal activities, money laundering and terrorist financing effectively.

However many obstacles still affect or hamper international cooperation. These need to be identified and overcome.

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Nowadays, a criminal investigation is not the only approach to disrupt criminal activities effectively because criminals attach more value to the proceeds of their criminal activities (the benefits of their criminal activities) than to a jail sentence.

Intercepting the proceeds of crime is therefore important to disrupt criminal activities.

Depriving criminals of the proceeds of their criminal activities and using more effective and coordinated investigation techniques is also crucial in times of financial crisis and huge state deficits.

For all these reasons it is now appropriate to add or attach a financial investigation to each investigation into criminal activities generating potential pecuniary benefits.

If the law enforcement authorities have the ability and skill to carry out these financial investigations, all the intelligence collected by FIUs from STRs, CTRs... must also be used by law enforcement authorities to identify and disrupt criminal activities and to seize illicit assets.