

financial sectors ‘makes every jurisdiction a potential money laundering center’ (United States Department of State, Bureau for International Narcotics and Law Enforcement Affairs, 2012). It is for that reason that the Third EU Money Laundering Directive (European Parliament Directive 2005/60/EC) (2005) stated that ‘money laundering and terrorist financing are international problems and the effort to combat them should be global’.

Our summary therefore aims to provide a broad overview of the money laundering typologies which have become increasingly prevalent in recent years. The commentary is designed to give an insight to the world of money laundering, and highlight some of the mechanics and practices which are used by serious and organised crime groups today.

### WHAT IS MONEY LAUNDERING?

**1.11** The expression ‘money laundering’ is well known. It is originally believed to have emanated from the United States authorities, describing the mafia’s use and ownership of ‘washing salons’ (laundromats) through which they intermixed their criminal proceeds (which they had derived from bootlegging, gambling and prostitution) with legitimate business revenues in order to avoid potential seizure by those authorities and to evade tax liabilities.<sup>4</sup>

**1.12** Due to its complex nature there are many definitions to describe money laundering. For example, the US Customs Service defines it as:

‘The process whereby proceeds reasonably believed to have been derived from criminal activity, are transported, transferred, transformed, converted or intermingled with legitimate funds, for the purpose of concealing or disguising the true nature, source, disposition, movement or ownership of these proceeds. The goal of the money laundering process is to make funds derived from, or associated with illicit activity appear legitimate’. (Richards, 1999)

**1.13** Article 1 of the draft European Community directive of March 1990 describes money laundering as:

‘The conversion or transfer of property, knowing that such property is derived from a serious crime, for the purpose of concealing or disguising the illicit

<sup>3</sup> We have adopted the definition of ‘serious’ crime as that found within section 93(4) Police Act 1997, that is a crime that ‘involves the use of violence, results in substantial financial gain or is conducted by a large number of persons in pursuit of a common purpose’, or crime for which a person aged 21 or over, on first conviction ‘could reasonably be expected to be sentenced to imprisonment for a term of three years or more’.

<sup>4</sup> Derived from DA Chaikin, ‘Money Laundering: An Investigatory Perspective’ (1991) 2 Criminal Law Forum 467, 468, quoting a comment by the US delegation of the Working Committee on the Development of Financial Investigative Techniques, ICPO-Interpol, Paris (1985); see also F Schneider and U Windischbauer (2010) ‘Money Laundering: Some Facts’, Economics of Security Working Paper 25, Berlin: Economics of Security.

origin of the property or of assisting any person who is involved in committing such an offence or offences to evade the legal consequences of his action and the concealment or disguise of the true nature, source, location, disposition, movement, rights with respect to, or ownership of property, knowing that such property is derived from a serious crime.’

**1.14** These definitions provide a basic conceptual insight into the nature of money laundering in that it involves the various procedures attempting to clean money derived from illegal activity.

It is evident that most definitions of money laundering (even the most complex ones) contain one simple principle at their core, ie that money laundering is the process through which criminal funds are put, in a bid to disguise their illicit origins.

**1.15** As early as 1980 the Council of Europe considered the ‘transfer of funds of criminal origin’,<sup>5</sup> and it wasn’t until 1988 that a ‘supranational’ legal definition of money laundering was fashioned by the United Nations Convention on ‘Drugs’,<sup>6</sup> and, in its various forms, this is now enshrined in the legislation of most countries. A succession of national and international legal instruments, together with the ratification of some significant directives,<sup>7</sup> initiatives and Convention agreements,<sup>8</sup> have gradually established the technical money laundering frameworks we see today.

**1.16** In addition to the money laundering assessments conducted by the International Monetary Fund (‘IMF’) and The World Bank, it could be argued that the present international anti-money laundering structures were principally fashioned by the 40 recommendations of the Financial Action Task Force (‘FATF’).<sup>9</sup> The FATF number 1 Recommendation is that ‘Countries should criminalise money laundering’, and this was formulated on the basis of the United Nations Convention previously mentioned.

<sup>5</sup> Council of Europe, Committee of Ministers, Recommendation No R (80) 10: On measures against the transfer and the safekeeping of funds of criminal origin.

<sup>6</sup> See United Nations Convention (1988) Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances. See also the Basel Statement of Principle adopted by the Basel Committee on Banking Supervision (1988).

<sup>7</sup> For example, Council Directive 91/308/EEC (1991) on the prevention of the use of the financial system for the purpose of money laundering (later amended by Directive 2001/97/EC); or the later Directive 2005/60/EC of the European Parliament and of the Council of the European Union (2005) on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing.

<sup>8</sup> See, for example, the Strasbourg Convention, aka The Council of Europe’s Convention on Laundering, Search, Seizure and Confiscation of the Proceeds of Crime (1990); or the more recent Palermo Convention against Transnational Organised Crime (2000).

<sup>9</sup> The Forty Recommendations were first promulgated in a FATF report during the 1990s, and have since been revised and modified to cater for modern money laundering scenarios. These recommendations have also been supplemented by the so-called Special Recommendations on Terrorist Financing.

## CONCLUSION

1.172 This chapter has aimed to provide a brief introduction to the key concepts of money laundering through an exploration of some contemporary money laundering typologies which have been used by serious and organised crime groups in recent years. This chapter is not designed to provide a detailed taxonomy or overview of all money laundering typologies, but is intended to act as an informative guide to those seeking an introduction to the tools and techniques used by criminal groups to launder the proceeds of their criminal activities.

1.173 We give our final word to Min Zhu, Deputy Managing Director of the IMF:

‘Money laundering and the financing of terrorism are financial crimes with economic effects. They can threaten the stability of a country’s financial sector or its external stability more generally. Effective anti-money laundering and combating the financing of terrorism regimes are essential to protect the integrity of markets and of the global financial framework as they help mitigate the factors that facilitate financial abuse. Action to prevent and combat money laundering and the financing of terrorism thus responds not only to a moral imperative, but also to an economic need.’ (IMF, 2012)

1.174 This chapter is not a comprehensive dictionary of every variation in money laundering scheme and therefore deviation from the literature may be observed in different cases. Money laundering is a complex practice and the specific details of individual schemes can vary from case to case. Professional advice should always be sought from qualified persons, expert witnesses and/or forensic accountants on a case-by-case basis. The chapter is based upon information contained in published reports, academic papers and other literature, as such it does not necessarily reflect the personal views of the authors or the views of HM Government, the SOCA or any other enforcement/regulatory agencies.

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the cases of *R v Rollins* and *R v McInerney*.<sup>145</sup> These cases concerned allegations of insider dealing contrary to the Criminal Justice Act 1993 ('CJA') and the conduct of a 'boiler room' business in contravention of s 23 of FSMA. In both cases, the defendants were charged with breaches of ss 327 and 328 of POCA in addition to the offences under the CJA and FSMA. Pursuant to s 402 of FSMA, the FSA was the statutory prosecutor for the purposes of Part V of the CJA and FSMA but had no express statutory power to prosecute contraventions of POCA. The defendants challenged the charges under POCA on the basis that the FSA had no power to bring such charges. However, the Court of Appeal found in each case that the FSA had the power to bring such charges on the basis that it enjoyed a right to bring private prosecutions in relation to offences not specified under FSMA.

**2.219** The FSA brought a number of civil enforcement cases against firms and individuals relating to breaches of the FSA's Rules and requirements relating to AML systems and controls requirements.

**2.220** In 2003 Abbey National plc was fined £2 million for breaches of the FSA's Money Laundering Sourcebook. The FSA's investigation concluded that there were weaknesses in Abbey National's AML controls across its retail banking division. These weaknesses included a reliance on a system of self-certification of AML compliance by branches, a lack of monitoring by a central function and a failure to provide key management information to the MLRO. The FSA further concluded that these failings contributed to a high rate of non-compliance with know your customer requirements. The FSA also pointed to a failure to ensure that internal SARs were promptly considered and reported to NCIS, which at that time acted as the UK FIU.

**2.221** Enforcement action relating to money laundering was also taken against Sindicatum Holdings Limited and its MLRO, Michael Wheelhouse who were fined respectively £49,000 and £17,500. This was the first occasion on which the FSA had imposed a fine on an MLRO.<sup>146</sup>

**2.222** Mr Wheelhouse was approved to perform the money laundering reporting function and as such was the firm's MLRO. The FSA found that Mr Wheelhouse had failed to take reasonable steps to ensure that Sindicatum's business for which he was responsible as MLRO complied with the relevant standards and requirements of the regulatory system as required by Statement of Principle 7 of APER. Mr Wheelhouse was said by the FSA to have breached Statement of Principle 7 by failing to take reasonable steps to implement adequate procedures for verifying the identity of the firm's clients, by failing to ensure that the firm adequately verified the identity of a significant number of its clients and by failing to ensure that the firm kept adequate records to

<sup>145</sup> [2009] EWCA Crim 1941.

<sup>146</sup> Although in 2005 the FSA fined an individual, Mr Ram Melwani for breaches of Statements of Principle for Approved Persons and for being knowingly concerned in his firm's breach of the Money Laundering Sourcebook. Mr Melwani was at that time the firm's managing director.

demonstrate that it had verified the identity of a significant number of its clients.

**2.223** In relation to a number of clients, although some customer due diligence had been obtained, the FSA said that the MLRO had failed to ensure that the documentation was adequate to verify their identity. Client acceptance checklists had not been completed in all cases. Certain checklists had not been completed for a significant period of time or had not been completed at all and the MLRO had failed to comply with his obligations in incorrectly applying an exemption from AML requirements for a bank. The FSA noted that the MLRO had in this case acted both as the MLRO and account executive meaning that it was less likely that the failure would be identified.

**2.224** The FSA and now the FCA continue to bring enforcement action against individuals and firms for money laundering related failings. Fines have been imposed on Coutts & Co (£8.75 million), Habib Bank (£525,000), Turkish Bank UK (£294,000) and EFG Private Bank (£4.2 million). Each of the above cases was brought for a breach of Principle 3 of the FSA's Principles for Businesses (Management and Control), with the exception of Turkish Bank that was fined by the FSA under reg 42 of the Money Laundering Regulations 2007 which conferred on the FSA the power to impose a civil penalty. In addition to this, the FSA fined Syed Hussain £17,500 for failings in his role as Habib Bank's CF11 (Money Laundering Reporting). The recent enforcement cases have highlighted a number of issues, particularly with regard to higher risk customers. These include the following:

*Proper identification and management of money laundering risk.*

**2.225** Certain of the criticisms made by the FSA concern the failure of firms to properly identify money laundering risks. The Turkish Bank case, for example, concerned correspondent banking services provided to respondents in Turkey and Northern Cyprus. The bank was criticised for failing to have sufficient regard to the higher risk posed by relationships with institutions in non-EEA jurisdictions. The lack of equivalence of Turkey, for example, had been identified in a FATF national evaluation report. A further aspect concerning the management of risk arose in the EFG Private Bank case. In this case, concerns relating to certain clients were identified in the course of performing due diligence. The FSA found that the bank had proceeded with the client relationship without properly documenting the reasons for continuing the relationship in spite of the adverse information obtained by the firm.

*Performing proper customer due diligence.*

**2.226** In some cases the FSA has found that firms have not performed basic due diligence checks properly. In particular, firms continue not to understand ownership structures properly. A failure to obtain details of beneficial ownership will mean that the firm will also not be in a position to identify PEPs related to

knowing, at the time of receipt' that it was derived from drug trafficking as well as conspiracy, aiding and abetting and facilitating the commission of drug trafficking offences, including money laundering.<sup>15</sup> The important issue of the appropriate burden of proof in relation to all such offences is addressed in art 3(3), which provides that knowledge, intent or purpose 'may be inferred from objective factual circumstances'. Finally, and in an effort to maximise the possibility of cooperation among participating countries, steps have been taken to reduce the possibility of drug-related money laundering and other prohibited trafficking activities being regarded as either political or fiscal in nature.<sup>16</sup>

6.13 Having thus required a broad degree of harmonisation of approach to domestic criminal justice systems, the 1988 UN Convention proceeds to impose a number of obligations designed to ensure that the necessary international cooperation between parties is made available. To this end, art 7 makes provision for orthodox forms of mutual legal assistance in the investigation and prosecution of relevant offences while art 5 details the measures to be taken both domestically and internationally to enable the competent authorities to identify, trace, freeze and confiscate the proceeds derived from drug trafficking and drug-related money laundering. In both contexts specific obligations are imposed to ensure that bank secrecy does not act as a barrier to national action or international cooperation.<sup>17</sup>

6.14 The importance and centrality of the 1988 UN Convention to the current efforts to generate the widest possible mobilisation of effort to counter money laundering cannot be over-emphasised. It was the first, and for many years the only, treaty of global reach to require the criminalisation of this activity. It imposed then unprecedented obligations on its participants which include many of the most important drug producing, transit and consumer states. It is not surprising, therefore, that the very first of the 40 Recommendations originally formulated by the influential FATF in 1990 was that 'each country should, without further delay, take steps to fully implement the Vienna Convention, and proceed to ratify it'.

*The 1990 Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds of Crime*

6.15 Important though the 1988 UN Convention has proved to be, it was not the intention or the expectation that efforts to combat money laundering and promote international cooperation to counter the financial aspects of drug trafficking and other forms of transnational criminal activity would rest exclusively on that instrument. One important early development was the conclusion in 1990 of the Council of Europe Convention on Laundering, Search, Seizure and Confiscation

<sup>14</sup> UN Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, art 3(1)(c).

<sup>15</sup> UN Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, art 3(1)(c).

<sup>16</sup> UN Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, art 3(1)(c).

<sup>17</sup> UN Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, art 3(1)(c) and 5(3).

of the Proceeds of Crime (the 1990 Convention), which entered into force in September 1993. Some 46 European countries, including the UK, were parties to it, as was Australia which, along with the US and Canada, had participated in its negotiation.<sup>18</sup>

6.16 As discussed in further detail below, the Council of Europe decided, in 2005, to widen the scope of the Convention to take into account the fact that not only could terrorism be financed through money laundering from criminal activity, but also through legitimate activities.<sup>19</sup>

6.17 Whilst taking considerable care to ensure that its provisions were fully compatible with the 1988 UN Convention, the Committee of Experts which drafted the 1990 Convention agreed to extend its obligations beyond the area of drug trafficking.

6.18 It has been recognised, however, that in extending the reach of its provisions on an 'all crimes' basis, they were breaking new ground at the international level in a radical manner and that, accordingly, it would be appropriate to provide a facility for the making of reservations. In so far as money laundering, (which was governed by art 6 of the 1990 Convention), is concerned, the basic approach adopted was summarised by the UK House of Lords Select Committee on the European Communities as follows:<sup>20</sup>

'Article 6 of the [1990] Convention requires State Parties to establish an offence of intentional money laundering. The property involved in any conversion or transfer could be proceeds not only of drug trafficking or terrorism but of any criminal offence (described as the 'predicate offence') and the State Party prosecuting need not have criminal jurisdiction over the predicate offence. Although this constitutes a very wide definition of money laundering, it is open to States on signature or ratification to limit the definition for themselves to more limited categories of predicate offence.'

6.19 Whilst the expansion of the definition of money laundering beyond its 1988 association with drug trafficking had no precedent in a binding international agreement, it was a development which was not unexpected. For example, it had support in the legislative practice of a (then) small minority of countries, including Switzerland. The Swiss Penal Code 1990, art 305(bis), which came into effect on 1 August 1990 (the month before the 1990 Convention was adopted), rendered money laundering in respect of all forms of crime a criminal offence. It was, in addition, a policy development which had attracted the cautiously worded support of FATF which, in the fifth of its (then current) 40 Recommendations contained in its February 1990 Report, had expressed the view that 'each country should

<sup>18</sup> Various factors account for this broad geographic coverage including pressure from the EU. See eg EU Action Plan to Combat Organized Crime, OJ No C251, 15.8.97 (1997) Recommendation 13.

<sup>19</sup> Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds of Crime and on the Financing of Terrorism (2005).

<sup>20</sup> HL Select Committee on the European Communities 'Money Laundering' December 1990, session 1990-91, 1st Report (with evidence).

and prosecutions.<sup>31</sup> Reporting entities must record executed transactions in a way as to enable the entity to respond to information requests by the CTIF-CFI. All designated professions, financial as well as non-financial, must comply with the record-keeping obligations of the AML Act.

### Recruitment and training

**11.69** Reporting entities are required to train their employees and agents in order to familiarise them with provisions of the AML Act. The employees and representatives must participate in special training covering the detection and processing of transactions that could be linked to money laundering or terrorist financing. To ensure that their employees and representatives show appropriate reliability depending on the risk associated with the tasks and duties to be carried out, the reporting entities must establish appropriate procedures upon recruitment and appointment of their employees or representatives. Non-compliance with these provisions may be sanctioned.<sup>32</sup>

**11.70** The federal police and its specialised units, including the Central Office for the Fight Against Economic and Financial Crime, have to ensure that money laundering and terrorist financing offences are investigated properly. Various types of training are provided both for the relevant police units and for judges. At the judicial level, the federal prosecutor's office and the College of Attorneys General play a critical role in combating economic, financial and tax crimes.

### Adequate organisation

#### (i) Internal organisation

**11.71** Reporting entities must appoint a person responsible for anti-money laundering, who is responsible for the relevant entity's implementation of the AML Act. They are primarily responsible for the establishment of internal control procedures, communication of information, and centralisation of information in order to prevent, identify and to eliminate transactions that are linked to money laundering or terrorist financing.<sup>34</sup> The person responsible for money laundering must be chosen from the management of the relevant entity and must be of an appropriate level of seniority.<sup>35</sup> Once a year, he must provide a report concerning

<sup>31</sup> P Berger, «Witwassen van misdaadgeld», *NV in de Praktijk*, December 2005, 136z; G. Stessens, 'Commentaar bij art. 4 Wet 11 januari 1993', in *Financieel recht. Commentaar met overzicht van rechtspraak en rechtsleer*, 212.

<sup>32</sup> P Berger, «Witwassen van misdaadgeld», *NV in de Praktijk*, December 2005, 136z6; Mémorie van Toelichting bij het ontwerp tot voorkoming van het gebruik van het financiële stelsel voor het witwassen van geld, *Parl. St. Senaat BZ. 1991-1992*, nr. 468-1, 12.

<sup>33</sup> FATF, 'Belgium - Report on observance of standards and codes. FATF recommendations for anti-money laundering and combating the financing of terrorism', [www.fatf-fagi.org](http://www.fatf-fagi.org), 21 November 2005, nr. 13.

<sup>34</sup> Article 18 AML Act; P. BERGER, «Witwassen van misdaadgeld», *NV in de Praktijk*, 13 november 2008, p. 136z6.

<sup>35</sup> P Berger, «Witwassen van misdaadgeld», *NV in de Praktijk*, December 2005, 136z6.

his activities to the management of the legal entity. If the person responsible for money laundering neglects to report to the CTIF-CFI, according to the AML Act, each employee and each representative has the obligation to report the information in person to the CTIF-CFI (article 29 of the AML Act).

**11.72** Notaries, bailiffs, company auditors, external accountants, tax advisors and lawyers must also appoint a person responsible for money laundering if this is justified in light of the size and structure within which they carry out their activities (article 18 of the AML Act).

#### (ii) External organisation

**11.73** The supervisory authorities are empowered to supervise compliance by financial institutions and individuals specified by the AML Act with their obligations to prevent money laundering. If they identify, in the course of their inspections, facts that may be related to money laundering, they must immediately inform the CTIF-CFI. Furthermore, the supervisory authorities must inform the CTIF-CFI if they forward information relating to the laundering of money derived from an offence over which they have investigatory powers, to the Public Prosecutor or the Federal Public Prosecutor. On the other hand, the CTIF-CFI may also inform the supervisory authorities when it finds a breach of the AML Act in order to enable them to take any necessary measures. The supervisory authorities may impose administrative sanctions if necessary. They always have to inform the CTIF-CFI of all final sanctions imposed.

**11.74** Furthermore, the CTIF-CFI or the supervisory or disciplinary authorities of the reporting entities provide and make publicly available information notes to facilitate the compliance of the reporting entities with their legal obligations.<sup>36</sup> The CBFA previously issued circulars with recommendations for auditing and internal control procedures.<sup>37</sup>

## SUPERVISION AND SANCTIONS

### Supervision

**11.75** The NBB or FSMA is the responsible authority for overseeing compliance with the AML obligations by the financial institutions subject to its supervision. Entities and professionals that are not subject to the NBB's or FSMA's prudential control are supervised by the CTIF-CFI in respect of their compliance with the obligations laid down in the AML Act. The CTIF-CFI must report any non-compliance with these obligations to the Federal Department of Economic Affairs.<sup>38</sup> Furthermore, the disciplinary authorities of each non-

<sup>36</sup> CTIF-CFI, « Information notes », [www.ctif-cfi.be](http://www.ctif-cfi.be).

<sup>37</sup> FATF, 'Belgium - Report on observance of standards and codes. FATF recommendations for anti-money laundering and combating the financing of terrorism', [www.fatf-fagi.org](http://www.fatf-fagi.org), 21 November 2005, nr. 21.

<sup>38</sup> FATF, 'Belgium - Report on observance of standards and codes. FATF recommendations for anti-money laundering and combating the financing of terrorism', [www.fatf-fagi.org](http://www.fatf-fagi.org), 21 November 2005, nr. 25.

### Risk assessment

**15.107** The Canadian AML/ATF regime places an emphasis on risk-based compliance that requires Reporting Entities to prepare a customised risk assessment program for money laundering and terrorist financing risks and mitigation measures to address the risks identified. This risk assessment is based into account the nature of the business, its geographic scope, clients, products and delivery channels. It requires the recording of current client identification and, in some cases, beneficial ownership information. High risk areas require special attention and ongoing monitoring to mitigate risk.

**15.108** Since 23 June 2008, financial entities such as banks have been required to take certain measures before entering into a correspondent banking relationship with prescribed high-risk foreign entities. These measures include obtaining specified information, ensuring the entity is not a shell bank, obtaining the approval of senior management, and setting out in writing the obligations of the parties with respect to correspondent banking services.

### Compliance reviews

**15.109** Reporting Entities are required to conduct a review of their compliance policies and procedures to test their effectiveness every two years. The review must address risk assessment, mitigation and monitoring, as well as AML/ATF policies, procedures and training. Senior management must be informed of the results of these compliance reviews within 30 days of completion.

**15.110** Additionally, FINTRAC and industry regulators such as OSFI may periodically provide feedback to ensure the adequacy and completeness of an entity's compliance policy and the information reported to FINTRAC. The Reporting Entity and its staff must cooperate with the regulators in this regard and, in particular, must be able to demonstrate that they have developed and implemented policies and procedures consistent with the PCMLTFA and any guidelines issued by FINTRAC or the regulator. The compliance officer must keep a record of any compliance reviews made by FINTRAC and the entity's regulator in a compliance records file.

**15.111** A person authorised by FINTRAC has the power to enter a Reporting Entity's premises at any reasonable time, without a search warrant, to determine whether there is compliance with applicable obligations to report and record transactions. In the course of a compliance search, the subject entity must give the person authorised by FINTRAC: (i) full use and access to the data on any computer or data processing system in the premises; (ii) the right to examine and reproduce any data in print or electronic form; and (iii) the right to use any copying equipment to make any required copies. In addition, it must give or furnish the authorised persons with all reasonable assistance to enable them to carry out their responsibilities, and any information with respect to the administration of the reporting and recording obligations that they may reasonably require.

## ENFORCEMENT AND PENALTIES

**15.112** The PCMLTFA includes criminal penalties consisting of fines of up to C\$2 million and imprisonment for up to five years, depending on the type of offence. Liability may extend to directors, officers and agents of any entities guilty of an offence, although due diligence is a statutory defence. However, employees who report their suspicions to their superior or to the compliance officer are immune from penalty. A person who makes a suspicious transaction report in good faith is protected from criminal and civil liability.

**15.113** Penalties under the Cross-border Currency and Monetary Instruments Reporting Regulations include seizure and forfeiture, as discussed above, as well as fines ranging from C\$250 to C\$5,000.

### Administrative monetary penalties

**15.114** An administrative monetary penalty ('AMP') system has been in place since 30 December 2008. Modelled after similar federal AMP schemes in other areas such as customs, it provides civil penalties or fines for a much wider range of offences in proportion to the offence, with violations classified into one of three categories: minor, serious and very serious. There is a specific maximum penalty for each category, and the maximum fine for 'very serious' contraventions under this scheme is C\$100,000 for individuals and C\$500,000 for entities including corporations.

**15.115** The substance of the AMP system is found in the Proceeds of Crime (Money Laundering) and Terrorist Financing Monetary Penalties Regulations.<sup>49</sup>

**15.116** The AMP provisions allow FINTRAC to impose penalties itself without having to refer cases to the police for investigation and prosecution, although that recourse will remain an option for serious offences of a criminal nature. However, an individual or entity cannot be subject to both an AMP and a criminal sanction for the same offence.

AMPs can be reviewed by FINTRAC on application, and there are certain rights of appeal to the Federal Court.

**15.117** FINTRAC has indicated that penalties are used as a last recourse after other measures to ensure compliance have been exhausted. FINTRAC has the right to publicly identify persons subject to AMPs and regularly issues public notices of penalties imposed.

<sup>49</sup> SOR/2007-292.

**20.2** Gibraltar's Parliament is elected every four years. It has legislative responsibility for all matters except for those for which the Governor remains responsible. Gibraltar's executive consists in the main of the Council of Ministers<sup>1</sup> on whose advice the Governor must act, save in those matters in which only the United Kingdom Government is constitutionally competent. The Council of Ministers is made up from the majority party in Parliament. The Governor (acting on behalf of the United Kingdom Government) is the executive for matters relating to external affairs, defence, the police, and internal security and all powers of making appointments conferred on him by the Constitution. The Governor is said to have 'special responsibility' in these fields, although he must act in consultation with the Chief Minister in relation to external affairs and must fully inform the Chief Minister concerning the general conduct of the areas of special responsibility. He also retains full legislative powers in these areas. The Government of Gibraltar is made up, therefore, of the Governor and the Council of Ministers depending on which powers are exercised (although the Governor acts entirely on the advice of the Council of Ministers in relation to those matters over which it has responsibility).

**20.3** Gibraltar is within the European Union (EU)<sup>3</sup> as a European Territory for whose external affairs a member state (Great Britain) is responsible. It is excluded from the Common Agricultural Policy and the Customs Union. Hence there is no value added tax applied in Gibraltar. Gibraltar is bound by the Regulations and is required to and does implement EU Directives, except for directives relating to freedom of movement of goods and value added tax, in which it has a full derogation.

**20.4** Common law and the rules of equity in force in England apply in Gibraltar,<sup>4</sup> so far as they are applicable to its circumstances and subject to such modifications thereto as such circumstances may require, and except in so far as they are modified by any Order in Council of the United Kingdom Privy Council, Act of the United Kingdom Parliament or any Act of Gibraltar's Parliament. English Judicial decisions based on Common Law are binding in Gibraltar. Those based on statute law are considered by the courts as highly persuasive where statute law is comparable. For example, English case law involving the interpretation of such terms as 'suspicion', including *R v Montila*,<sup>5</sup> *R v da Silva* and *R v El Kurd*<sup>7</sup> will invariably be followed.

**20.5** Gibraltar has various courts. Its main court of first instance is the Supreme Court, consisting of three judges who sit singly and hear criminal cases on indictment, with a jury, and civil cases, where trial is by judge alone (save

<sup>1</sup> Constitution, s 45.

<sup>2</sup> Constitution, s 47.

<sup>3</sup> Treaty of Rome, Art 355(3) (on accession, Art 227(4)).

<sup>4</sup> English Law (Application) Act.

<sup>5</sup> [2005] 1 All ER 113.

<sup>6</sup> [2007] 1 WLR 303.

<sup>7</sup> [2007] 1 WLR 3190.

for one exception in the case of libel). Gibraltar has its own peripatetic Court of Appeal (the President of which is also the President of the Courts), consisting of four judges drawn from the Senior English Judiciary of which three sit at hearings of appeals. A final appeal lies to the Privy Council in London, with the permission of the Court of Appeal or the Privy Council. The magistrates' court deals with criminal matters and also has jurisdiction in sundry less complex civil matters requiring speedy and affordable justice, such as certain aspects of family law.

**20.6** Gibraltar is a member of the Offshore Group of Banking Supervisors and was the subject of an independent review of its anti-money laundering regime by it in September 2002 for the Financial Action Task Force (FATF). The FATF report commented as follows;

'Gibraltar has in place a robust arsenal of legislation, regulations and administrative practices to counter money laundering. The authorities clearly demonstrate the political will to ensure that their financial institutions and associated professionals maximise their defences against money laundering, and cooperate effectively in international investigations into criminal funds. Gibraltar is close to complete adherence with the FATF 40 Recommendations. Once the appropriate changes are made to the few remaining deficient areas, these standards will be fully met.'

There has been progress on remedying those areas where Gibraltar's regime was considered deficient.

**20.7** The International Monetary Fund (IMF) also produced an assessment of the regulation and supervision of financial services, initially in October 2000, followed by a further review in 2007.<sup>8</sup> The 2007 review included a review of Gibraltar's anti-money laundering regime. In its 2001 executive summary, the IMF commented that the development of the financial sector in Gibraltar has been facilitated by its location, favourable tax regime, a stable government, its status within the EU, no exchange controls, a legal framework based on the English system, and the availability of a well-qualified labour force, particularly well-endowed with accounting and legal skills.

**20.8** The 2007 IMF update commented on Gibraltar's successful transition from an economy 60% reliant on the maintenance of its British military base to one dominated by three pillars; tourism, ports and shipping, and financial services. Mention was also made of the rapid growth of the online gaming industry within Gibraltar.

**20.9** In 2001, the IMF found that:

'Current anti money laundering measures as they related to the Basel Core Principles, the IOSCO Principles and the LAIS Principles appear to be effective, although as in other jurisdictions there is always scope for improving know your customer requirements. The Financial Services Commission (FSC) complies with

<sup>8</sup> Available on the FSC website [www.fsc.gi](http://www.fsc.gi).

*The Criminal Justice (Proceeds of Crime) Bailiwick of Guernsey Law 1999*

22.47 CJ(PC)BGL 1999 contains three offences in connection with the proceeds of criminal conduct:

- (1) *Concealing or transferring the proceeds of criminal conduct.*<sup>8</sup> A person is guilty of this offence if they:
  - (i) conceal or disguise any property which is, or in whole or in part directly or indirectly represents, their own or another's proceeds of criminal conduct; or
  - (ii) convert or transfer that property or remove it from the Bailiwick for the purpose of avoiding the prosecution of themselves or another for criminal conduct or the making or enforcement in their case, or the case of another, of a confiscation order.
- (2) *Assisting another person to retain the proceeds of criminal conduct.*<sup>9</sup> A person is guilty of this offence if they enter into or are otherwise concerned in an arrangement whereby:
  - (i) the retention or control by or on behalf of another ('A') of A's proceeds of criminal conduct is facilitated (whether by concealment, removal from the Bailiwick, transfer to nominees or otherwise); or
  - (ii) A's proceeds of criminal conduct:
    - are used to secure that funds are placed at A's disposal; or
    - are used for A's benefit to acquire property by way of investment knowing or suspecting that A is or has been engaged in criminal conduct or has benefited from criminal conduct. It is a defence for a person to prove that they did not know or suspect that the arrangement was of this kind.
- (3) *Acquisition, possession or use of the proceeds of criminal conduct.*<sup>10</sup> A person is guilty of an offence if, knowing that any property is, or in whole or in part directly or indirectly represents, another's proceeds of criminal conduct, they acquire or use that property or have possession of it. It is a defence that they did so for adequate consideration.

22.48 A person whose conduct would otherwise constitute an offence under CJ(PC)BGL 1999, s 39 or 40 will not commit an offence if they disclose their suspicion that the property in question is the proceeds of criminal conduct to a police officer. This is provided that the disclosure is made before they do the act concerned and the act is done with the consent of the police officer; or that the disclosure is made after they do the act, but is made on their own initiative and as soon as it is reasonable for them to make it. A person who is in employment

<sup>8</sup> CJ(PC)BGL 1999, s 38.

<sup>9</sup> CJ(PC)BGL 1999, s 39.

<sup>10</sup> CJ(PC)BGL 1999, s 40.

at the relevant time may instead make the disclosure to the appropriate person under their employer's internal reporting procedures. The employer is required to have in place such procedures under the Regulations and the Handbook (or their equivalent for Guernsey lawyers, accountants and estate agents).

22.49 It is a defence to a charge under CJ(PC)BGL 1999, s 39 or 40 for a person to prove that they intended to make a material disclosure to a police officer or under their employer's internal reporting procedures but that there is a reasonable excuse for their failure to do so.

22.50 Criminal conduct' means any conduct, other than drug trafficking (which is covered by DT(BG)L 2000), which constitutes a criminal offence under the laws of the Bailiwick and is triable on indictment or which would constitute such an offence if it were to take place in the Bailiwick. It is therefore irrelevant whether the conduct is criminal in the jurisdiction in which it was committed.

22.51 Certain categories of criminal conduct call for brief comment.

22.52 *Fiscal offences.* It is a common law offence to cheat the Revenue. The States of Guernsey, which is the legislature for the island, levies income, property and other taxes and import duties for Guernsey and Alderney. In the case of the proceeds of the evasion of tax due in another jurisdiction, it is submitted that the correct approach would be to ask whether tax evasion is also an offence in the Bailiwick rather than to ask whether it is an offence in the Bailiwick to evade taxes due in that jurisdiction.<sup>11</sup> But the point is not free from doubt. In any case, tax evasion in other jurisdictions will tend to involve conduct, such as false accounting, which is indictable in the Bailiwick.

22.53 *Exchange control offences.* There are no general exchange control regulations in the Bailiwick. However, the Control of Borrowing (Bailiwick of Guernsey) Ordinance 1959, as amended, in effect imposes exchange controls with respect to borrowing by companies.<sup>12</sup> Moreover, as with tax evasion, exchange control offences in other jurisdictions will tend to involve conduct, such as false accounting, which is indictable in the Bailiwick.

22.54 *Bribery.* Bribery and other corrupt practices are offences under the Prevention of Corruption (Bailiwick of Guernsey) Law 2003. It is irrelevant whether the corrupt practice takes place outside the jurisdiction. It is also noted that the provisions of the UK Bribery Act 2010 often extend to Guernsey in practice because many companies here are subsidiaries of those in the UK or because Guernsey residents are also British citizens.

22.55 If a person is charged with an offence in connection with the proceeds of criminal conduct, then applying English case law the prosecution must prove

<sup>11</sup> In England and Wales the Court of Appeal took this approach in analogous circumstances in *Quatrocchi* [2004] EWCA Civ 40; *The Times* 28 January 2004.

<sup>12</sup> Although even these are under consideration for repeal.



**22.170 Guernsey**

Measures) (Channel Islands) Order 2001 may be disclosed by the authorities as follows.

**22.171** They may be disclosed to the Crown on behalf of the UK government, the States of Jersey, or the government of the Isle of Man or any British Overseas Territory listed in the Schedule to the Terrorism (United Nations Measures) (Channel Islands) Order 2001. They may also be disclosed to the UN or the government of any other country for the purpose of monitoring or securing compliance with the Order. They may further be disclosed in connection with proceedings for an offence under the Order in Jersey or under equivalent legislation in the UK, the Isle of Man or any British Overseas Territory listed in the Schedule to the Order.

**22.172** Although the foregoing disclosure provisions remain in force, it is likely that, in general, disclosure of information by police officers will be made pursuant to The D(BG)L 2007. This provides that information obtained by a police officer under that Law or any other enactment, or in connection with the carrying on of any of the officer's functions, may be disclosed to any other person if the disclosure is for any one of a number of specified purposes. These include the prevention, detection, investigation or prosecution of criminal offences, whether in the Bailiwick or elsewhere. The disclosure must not contravene legislation governing either data protection<sup>104</sup> or the regulation of investigatory powers.

**ENFORCEMENT**

**22.173** There are three levels of enforcement agency: the Commission, the FIS, and the Law Officers of the Crown. Ultimately, however, enforcement is a matter for the courts.

**The Guernsey Financial Services Commission**

**22.174** The Commission is a statutory body which regulates finance business in Guernsey. It was established in 1988 by the Financial Services Commission (Bailiwick of Guernsey) Law 1987, with both general and statutory functions. The general functions include taking 'such steps as the Commission considers necessary or expedient for the development and effective supervision of finance business in the Bailiwick', and the statutory functions include the administration of financial legislation in the Bailiwick. The Commission's stated objective is to provide effective supervision and modern regulation of the finance sector to the highest international standards in a diverse and innovative environment.

<sup>104</sup> The Data Protection (Bailiwick of Guernsey) Law 2001.

<sup>105</sup> Part I of The Regulation of Investigatory Powers (Bailiwick of Guernsey) Law 2003.

**22.175** The Commission has stated that, whilst for any financial services business the primary consequences of any significant failure to measure up to the requirements of the Handbook may be legal ones, the Commission is entitled to take such failure into consideration in the exercise of its regulatory and supervisory functions and, particularly, in the exercise of its judgment as to whether the directors and managers are fit and proper persons. Financial services businesses which do not measure up to the standards set by the Handbook are at risk of, ultimately, having their licences to carry on business within the Bailiwick revoked. It is an offence to carry on regulated activities without a licence. In addition the Commission has powers to levy 'administrative penalties' for regulatory breaches which are serious but not criminal. These are financial penalties and can be unlimited.

**The Financial Intelligence Service**

**22.176** The FIS, which is a joint police and customs body, is the central point within the Bailiwick for the gathering, collating, evaluation and dissemination of financial crime intelligence, including disclosure reports. The FIS also has specific responsibility within the Bailiwick for the investigation of any person suspected of money laundering. It has developed a strong working relationship with law enforcement agencies in the UK, the other Crown Dependencies and overseas, particularly in Europe and the US. Technically it is divided into two sections: The Financial Intelligence Service and The Financial Investigation Unit. It is known simply as the FIS.

**The Law Officers of the Crown**

**22.177** There are two Law Officers, who are both appointed by the Crown. They are the HM Procureur, whose position is equivalent to Attorney-General, and HM Comptroller, whose position is equivalent to Solicitor-General. They are legal advisors to the Crown and the Bailiwick's legislatures. Their primary allegiance is to the Crown and so, in the event of a conflict of interest, they will act for the Crown and not for the legislatures.

**22.178** The Chambers of the Law Officers are concerned with all aspects of the administration of justice. All prosecutions in the Bailiwick are brought in the name of the Law Officers and are subject to their supervision. It is to the Law Officers that requests will be made from other jurisdictions for assistance by way of external restraint and confiscation orders and the provision of material to assist criminal investigations and prosecutions overseas. The Law Officers are supported by a specialised staff of lawyers. They are independent of the Bailiwick's courts and legislatures and are answerable only to the Crown.

China, Hong Kong is considered to be the principal channel for 'dirty money' transferred in and out of mainland China, which maintains strict controls on the movement of capital.

23.3 In an effort to combat money laundering, Hong Kong became a signatory to the 1988 UN Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances and a member of the Financial Action Task Force (FATF), and the Asia/Pacific Group on Money Laundering (APGML). As a member of FATF and APGML, Hong Kong is required to and has implemented legislative measures to combat money laundering, and, after the 11 September 2001 terrorist attacks on the United States of America, measures to combat terrorism and terrorist financing activities.

23.4 The three main pieces of legislation in Hong Kong that are concerned with money laundering are the Drug Trafficking (Recovery of Proceeds) Ordinance (Chapter 405 of the Laws of Hong Kong) (DTRPO), the Organized and Serious Crimes Ordinance (Chapter 455 of the Laws of Hong Kong) (OSCO), and the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Ordinance (Chapter 615 of the Laws of Hong Kong) (AMLO), whilst the United Nations (Anti-Terrorism Measures) Ordinance (Chapter 401 of the Laws of Hong Kong) (UNATMO) deals with combating terrorism and terrorist financing. From a technical perspective, there is no offence under the UNATMO that is not caught under the OSCO.

23.5 The AMLO empowers certain authorities to supervise compliance with the requirements under AMLO, as well as to publish guidelines regarding the application of its customer due diligence and record-keeping provisions. These authorities are the Hong Kong Monetary Authority (HKMA), the Securities and Futures Commission (SFC), the Office of the Commissioner of Insurance (OCI) and the Hong Kong Customs & Excise Department (CED). An analysis of these very proscriptive guidelines is beyond the scope of this chapter.

23.6 Both the Hong Kong Police Force and the CED have been empowered to investigate money laundering and terrorism and terrorist financing activities in Hong Kong and a Joint Financial Intelligence Unit (JFIU), run jointly by the two departments, was set up in 1989 to receive reports concerning suspicious financial activity. Since the enactment of the UNATMO, the JFIU also receives suspicious transaction reports related to terrorist property.

23.7 The role of the JFIU is not to investigate suspicious transactions, but simply to receive, analyse and store reports of suspicious transactions and refer them to the appropriate investigative unit. A suspicious transaction report will usually be referred to either the Narcotics Bureau, the Organized Crime & Triad Bureau of the Hong Kong Police Force or the Customs Drug Investigation Bureau of the CED.

23.8 The JFIU also advises on money laundering issues generally, both domestically and internationally, and offers practical guidance and assistance to the financial sector on the subject of money laundering.

## PRIMARY LEGISLATION

### Anti-money laundering legislation

23.9 The two principal pieces of anti-money laundering legislation in Hong Kong are the DTRPO and OSCO. The two Ordinances contain similar provisions against money laundering and for the tracing, confiscation and recovery of illegal proceeds, except that the DTRPO relates to drug trafficking whereas the OSCO relates to organised and serious crime. Moreover, the provisions of the UNATMO are modelled on the DTRPO and OSCO.

### Money laundering

#### The money laundering offence

23.10 Under the DTRPO and OSCO, it is an offence to deal with any property knowing or having reasonable grounds to believe that such property in whole or in part, directly or indirectly represents the proceeds of drug trafficking or of an indictable offence.<sup>3</sup>

23.11 In Hong Kong, crimes are defined by statute as being triable either summarily or on indictment. Generally, indictable offences are more serious offences, and include tax evasion, murder, kidnapping, drug trafficking, assault, theft, robbery, obtaining property by deception, false accounting, firearms offences, manslaughter, bribery, illegal gambling and smuggling.

23.12 It is irrelevant where the drug trafficking or indictable offence took place. Drug trafficking is defined to include drug trafficking anywhere in the world.<sup>4</sup> An indictable offence includes conduct which would constitute an indictable offence if it had occurred in Hong Kong,<sup>5</sup> regardless of whether the conduct is illegal in the jurisdiction where it is committed. Accordingly, money laundering can be of proceeds of drug trafficking or of an indictable offence committed either in Hong Kong or elsewhere. The purpose is to deter people from using Hong Kong to launder proceeds of crime. Moreover, from a technical perspective, dealing in Hong Kong with the proceeds from conduct which is legal (or at least not illegal) in another jurisdiction but which is illegal in Hong Kong is caught under the OSCO (eg, the proceeds of non-Hong Kong legal gambling). Similarly, dealing

<sup>3</sup> DTRPO, s 25 and OSCO, s 25.

<sup>4</sup> DTRPO, s 2(1).

<sup>5</sup> OSCO, s 25(4).

**24.65** Under the PML Act, all Reporting Entities are required to maintain a record of all transactions including information relating to transactions on the clause (b) in such manner as to enable it to reconstruct individual transactions. However, the period of time for which these records are required to be maintained have been reduced in the 2012 Amendments from ten years from the date of the transaction to five years from the date of the transaction between the client and the Reporting Entity.<sup>76</sup>

The reduction in the period of time for record keeping from ten to five years is in line with Recommendation 10 of the FATF which requires financial institutions to maintain all necessary records on transactions for at least five years. Under Recommendation 10, financial institutions should keep records of the identification data obtained through the customer due diligence process for at least five years after the business relationship is ended.

The Reporting Entities are required to furnish to the Director appointed under the PML Act, within the prescribed time, information relating to such transactions, whether attempted or executed, the nature and value of which may be prescribed. Every Reporting Entity must also verify the identity of its clients in such manner and subject to such conditions as may be prescribed, identify the beneficial owner, if any, of such of its clients as may be prescribed and maintain records of documents evidencing identity of its clients and beneficial owners as well as account files and business correspondence relating to its clients.<sup>77</sup> The foregoing are all new obligations introduced in the 2012 Amendments except for the verification and maintenance of records regarding the identity of clients which existed earlier as well. The 2012 Amendments also reduced the period of time for which the foregoing records have to be maintained from ten years after the business relationship between a client and the Reporting Entity has ended to five years after the business relationship between a client and the Reporting Entity has ended or the account has been closed whichever is later.<sup>78</sup>

The 2012 Amendments also introduced a new s 12A which provides that the Director appointed by the Central Government under the PML Act may call from any Reporting Entity any of the records referred to above and any additional information as he considers necessary for the purposes of this Act. Further, every information sought by the Director shall be kept confidential.

If the Director<sup>79</sup> finds that a Reporting Entity has failed to comply with these record keeping obligations, then he may levy a fine on such institution which shall be not less than Rs 10,000 but may extend to Rs 100,000 for each failure.<sup>80</sup>

<sup>75</sup> PML Act, s 12(1)(a).

<sup>76</sup> 2012 Amendments, s 9(3) amending s 12(2)(a) of the PML Act.

<sup>77</sup> PML Act, s 12 (1)(a)-(e) as amended by the 2012 Amendments.

<sup>78</sup> PML (Amendment) Act, s. 9 (4) amending s 12(2)(b) of the PML Act.

<sup>79</sup> The term 'Director' means a person appointed by the Central Government under s 49 of the PML Act who has the rank of either a Director, Additional director or Joint Director.

<sup>80</sup> PML Act, s. 13.

Importantly, the PML Act gives Reporting Entities, its directors and employees, immunity against liability in any civil proceedings brought against them for furnishing information as required under s 12 of the PML Act.<sup>81</sup> This provision is in keeping with FATF as Recommendation 14 of the FATF provides that financial institutions, their directors, officers and employees should be protected from criminal and civil liability for breach of any restriction on disclosure of information imposed by contract or law if they report their suspicions in good faith to the FIU even if they did not know precisely what the underlying criminal activity was, and regardless of whether illegal activity actually occurred.

**24.66** The PML Act empowers the Central Government, in consultation with the RBI, to prescribe the procedure and the manner of maintaining and furnishing information under s 12 of the PML Act for the purpose of implementing the Act.

The RBI, *vide* a series of circulars commencing on 15 February 2006, issued its rules requiring maintenance of records of transactions by commercial banks, cooperative banks, and regional rural banks.<sup>82</sup> On 1 July 2012, the RBI issued a Master Circular to all Scheduled Commercial Banks, Financial Institutions<sup>83</sup> and Cooperative Banks with regard to Know Your Customer, Anti-Money Laundering and Combating of Financing of Terrorism.<sup>84</sup> Banks, financial institutions and intermediaries must also verify and maintain records of the identity of all clients in the manner prescribed as per the KYC norms discussed below.<sup>85</sup> Notably, SEBI has also issued guidelines and circulars on anti-money laundering since 2006 which impose record keeping, reporting and KYC obligations on intermediaries.

**24.67** The guidelines issued by SEBI enhance the foregoing record keeping requirements by providing that registered intermediaries should maintain such records as are sufficient to permit the reconstruction of individual transactions (including the amounts and types of currencies involved, if any) so as to provide, if necessary, evidence for the prosecution of criminal behaviour.<sup>86</sup> Registered intermediaries are required to maintain a satisfactory audit trail, including the following information:

- (a) the beneficial owner of the account;
- (b) the volume of funds flowing through the account; and
- (c) for selected transactions:

<sup>81</sup> PML Act, s 14 as amended by s 12 of the 2012 Amendments.

<sup>82</sup> RBI/2005-06/301 DBOD.NO. AML.BC.63/14.01.001/2005-06 15 February 2006; RBI/2005-06/313/RPCD.CO.RF. AML. BC.65/07/02/12/2005-06 3 March 2006; RBI/2005-06/321/RPCD.CO.RRB.AML.BC.68/03.05.33(E)/2005-06 9 March 2006; RBI/2009-10/152 DBOD.AML.BC.No.43/14.01.001/2009-10.

<sup>83</sup> RBI/2012 - 13/45DBOD. AML. BC. No. 11 /14.01.001/2012-13 dated 2 July 2012

<sup>84</sup> RBI/2012-13/55 UBD.BPD. (PCB).MC.No.16/12.05.001/2012-13 dated 2 July 2012.

<sup>85</sup> PML Act, s 12(1)(c).

<sup>86</sup> SEBI Anti Money Laundering Standards/Combating Financing of Terrorism/Obligations of Securities Market Intermediaries under Prevention of Money Laundering Act 2002 and Rules thereunder, ISD/AML/CIR-1/2008 19 December 2008.

### Legal challenge of enforcement mechanisms

**24.118** The provisions of the PML Act providing for an adjudicatory authority, appellate tribunal and special courts were challenged in a public interest litigation before the Supreme Court of India as being in violation of the Constitution of India in that they did not provide for an independent judiciary to decide cases under the PML Act but instead Members and Chairperson to be selected by a Selection Committee headed by the Revenue Secretary. In the case, the sections challenged were s 6 dealing with Adjudicatory Authorities, s 25 which deals with composition of the Appellate Tribunal, s 28 which deals with qualifications for appointment of Chairperson and Members of the Appellate Tribunal, s 32 which deals with resignation and removal and s 40 which deals with members. The petitioner highlighted the following alleged defects in the PML Act:

**24.119** In its 2008 judgment, *Pareena Swarup v Union of India*,<sup>193</sup> the Supreme Court agreed with the petitioner and felt that the executive branch had crossed a line in taking over bit by bit judicial functions and powers exercised by the courts. While creating new judicial fora, it is the duty of the Government to see that they are not in breach of basic constitutional scheme of separation of powers and independence of judicial functions. The Supreme Court found that the constitutional guarantees of a free and independent judiciary and the scheme of separation of powers can be easily and seriously undermined if the legislatures divest the regular courts of their jurisdiction in all matters and vest the same to newly created tribunals which are not entitled to protection similar to the constitutional protection afforded to the regular courts. According to the Supreme Court, independence and impartiality must also be secured not only for the regular courts but also for tribunals and their members although they do not belong to the 'judicial service.' In the words of the Supreme Court of India:

'The safeguards which ensure independence and impartiality are not for promoting person prestige of the functionary but for preserving and protecting the rights of the citizens and other persons who are subject to the jurisdiction of the Tribunal and for ensuring that such Tribunal will be able to command the confidence of the public. Freedom from control and potential domination by the executive are necessary pre-conditions for the independence and impartiality of the judges. To make it clear a judiciary free from control by the executive and the Legislature are essential preconditions if there has to be a right to have claims decided by the Judges who are free from potential domination by other branches of the Government.'

**24.120** The constitutional validity of various provisions of the PML Act was subsequently challenged again in *B Rama Raju, S/o B Ramalinga Raju v Union of India (UOI), Ministry of Finance, Department of Revenue, and Ors*,<sup>194</sup> which arose from the following facts.

<sup>193</sup> [2008] 88 SCL 1 (SC).

<sup>194</sup> MANU/AP/0125/2011, [2011]164, CompCas149(AP).

On 7 January 2009, Sri B Ramalinga Raju, the then Chairman of Satyam Computers addressed a letter to the Board of Directors admitting to inflated cash and bank balances, non-existent accrued interest, understated liability in respect of funds arranged by himself, overstated debtors position, inflated revenues and operating margins and consequent artificial cash and bank balances. The letter admitted that falsified projections of the financial position of the SCSL in the balance sheet was the consequence of inflated profits over several years devaluated over the years by the company having to carry additional resources and assets to justify artificial higher levels of operation, thereby increasing the costs significantly. The letter further stated that the aborted MAYTAS acquisition deal by the SCSL was an attempt to fill the fictitious assets with real ones and that this stratagem would have solved the SCSL problem but MAYTAS payments would have been delayed. The shares of the companies crashed following these disclosures and investors suffered huge loss.

Investigation was done by the Enforcement Directorate and the report was filed by Enforcement Directorate and provisional order was passed by the Enforcement Directorate attaching all moveable and immovable properties. B Rama Raju s/o B Ramalinga Raju, B Teja Raju also s/o B Ramalinga Raju, filed a writ petition under Article 226 of the Constitution of India challenging various sections of the PML Act as unconstitutional on the following basis.

#### (i) Section 2(u) of the PML Act

**24.121** Section 2(u) of the PML Act defines 'proceeds of crime' expansively to include property or the value thereof, derived or obtained, directly or indirectly, as a result of criminal activity relating to a scheduled offence even if in the hands of a person who has no knowledge or nexus with such criminal activity allegedly committed by others. The expansive definition thus inflicts grossly unreasonable consequences on innocent persons and is, therefore, unconstitutional offending Articles 14, 20, 21 and Article 300-A of the Constitution.

The High Court of Andhra Pradesh observed that s 2(u) of the PML Act defines proceeds of crime as property derived and involved in criminal activity relating to scheduled offence. According to the petitioner, under the s 2(u) the property of innocent persons who are not involved in criminal activity are also put in jeopardy, preventing the enjoyment of the innocent person over his property. The High Court of Andhra Pradesh referred to the observation made by the Supreme Court in *Attorney General for India and Ors v Amratlal Prajivandas and Ors*.<sup>195</sup> In this case, the Supreme Court observed that application of Smugglers and Foreign Exchange Manipulators (Forfeiture of Property) Act 1976 ('SAFEMA') to the relatives is valid as the purpose of application of SAFEMA to relatives is to reach the properties of the detenu or convict. The property of relatives of accused are included not to jeopardize the relatives of accused but to reach the property of the accused.

<sup>195</sup> MANU/SC/0774/1994, (1994) 5 SCC 54.

of Accession annexed to the 1972 Treaty of Accession by which the UK became a member of the EU. Apart from the application of Value Added Tax ('VAT'), the Island is outside the EU in the field of financial services and products and is not bound by EU directives in this area. Nor is it subject to EU regulations or harmonisation of tax, corporate and other laws, except in respect of the common customs tariff and certain agricultural levies.

25.3 The Isle of Man is an established international finance centre with a secure base built upon political stability, low taxation and a firmly established fiscal and regulatory environment. This emergence as a serious player in the world of finance has arisen not least because of the Isle of Man Government's willingness to attract business by implementing facilitative legislation where appropriate and refining the existing legal position in other cases. The result is a sophisticated but flexible regulatory environment within which to do business. As testimony to its status, the International Monetary Fund ('IMF') in its 2009 report following its latest review of supervision and regulation of the Isle of Man's financial sector stated that 'the quality of implementation of AML/CFT measures by financial institutions was found to be mainly of a high standard' and that 'the Isle of Man authorities take their responsibilities in the area of international co-operation seriously', citing supervisory co-operation, mutual legal assistance and tax exchange agreements.

25.4 The Isle of Man actively participates in and cooperates with a number of international organisations, including the Financial Action Task Force ('FATF'), the Organisation for Economic Co-operation and Development ('OECD'), the Financial Stability Forum (an IMF body), the Basle Committee on Banking Supervision, the International Organisation of Securities Commissions ('IOSCO'), the International Association of Insurance Supervisors ('IAIS'), the Offshore Group of Banking Supervisors ('OGBS') and the Egmont Group. In particular, the Isle of Man participates in those specific international legislative initiatives aimed at combating the prevalence of drug trafficking, terrorism and associated money laundering activities. The Island's primary legislation in respect of money laundering is broadly in line with EU legislation and regulations and the international initiatives being undertaken by those countries who are members of FATF.

25.5 The Isle of Man's willingness to legislate against money laundering has long been internationally recognised in positive terms. Recognition of the comprehensive steps taken by the Isle of Man to combat money laundering was given by FATF in its review of the worldwide effectiveness of anti-money laundering measures published in June 2001. FATF welcomed the significant progress made by the Island in respect of money laundering legislation and implementation and regarded the Island as a cooperative jurisdiction. The FATF Annual Report 2000–2001 stated that:

'the Isle of Man has a robust arsenal of legislation, regulations and administrative practices to counter money laundering. Perhaps more importantly, the authorities clearly demonstrate the political will to ensure that their offshore financial

institutions and the associated professionals maximise their defences against money laundering, and co-operate effectively in international investigations into criminal funds'.

The report added that 'the standards set in the Isle of Man are close to complete adherence with the FATF's 40 recommendations'. The Island's desire to cooperate with international law enforcement agencies was affirmed more recently by the IMF in its 2009 evaluation of the Island's AML/CFT measures.

25.6 Since 2001, the Isle of Man has continued to review and re-new its anti-money laundering legislation. Updated anti-money laundering regulations were introduced in September 2010 and a large scale revision of the Island's primary legislation dealing with the proceeds of crime came into force from 1 August 2009.

25.7 This chapter seeks to provide an introduction to the Isle of Man's current anti-money laundering measures. It addresses the substantive anti-money laundering laws that have been enacted by the Isle of Man and comments on the relevant rules and guidance currently in issue. It concludes with a short identification of the provisions in the Isle of Man that enforce these measures and assist overseas territories.

## LEGISLATION AND REGULATION OVERVIEW – MONEY LAUNDERING IN THE ISLE OF MAN

25.8 The Isle of Man's primary anti-money laundering offences largely mirror their equivalent in the UK. This is perhaps not surprising. The two jurisdictions not only maintain a close relationship, both politically and geographically, but each have a shared, if independent, common law system of jurisprudence. Whilst the Isle of Man's independent legal status should always be emphasised, it is a feature of Manx law which was affirmed by the Privy Council in *Frankland v R*<sup>1</sup> that decisions of the English courts, especially those from England's appellate courts, whilst not binding are of high persuasive value in the Isle of Man. Notwithstanding, the Isle of Man Court of Appeal has stated in *Gilbertson SL and other v Dominator Ltd*,<sup>2</sup> that the Isle of Man's legal system is becoming increasingly independent of English statutes and procedures, and frequently chooses to be informed by or to adopt the common law and practices found in jurisdictions other than England. Although this demonstrates a preparedness on the part of the Manx courts to seek guidance from other jurisdictions, in the context of its primary anti-money laundering laws, the Isle of Man will undoubtedly still be highly influenced by decisions of the English courts given that the Island's

<sup>1</sup> Manx Law Reports (MLR) 1987–80 65.

<sup>2</sup> Unreported, 1 May 2009.

## LEGISLATION

## Overview

26.4 There has been specific anti-money laundering domestic legislation in Italy for over 30 years, but in recent years the law has become more sophisticated.

26.5 In 2007, Italy implemented Directives 2005/60/EC and 2006/70/EC and conformed its regulations to international best practice, in particular to the FATF 40 + 9 Recommendations.

26.6 Legislative Decree No 109 of 22 June 2007 provides for certain measures to prevent and repress terrorist financing and the activities of those countries which may jeopardise peace and the international security. Inter alia, this decree:

- introduces the possibility of giving direct application in Italy to the freezing measures resolved by the UN;
- clearly expresses the duty to report transactions suspected to finance terrorism; and
- fixes the procedures to freeze funds and other assets.

26.7 Legislative Decree No 231 of 21 November 2007, as amended, introduces significant amendments to the former regulation concerning the tasks and cooperation between the different authorities and the duties for those entities subject to AML regulation. Inter alia, this decree:

- abolishes the 'Ufficio Italiano dei Cambi' and transfers its duties to the Bank of Italy. The 'Unità di Informazione Finanziaria' has been established within the Bank of Italy to act as the financial intelligence unit ('FIU'), as required by Directive 2005/60/EC;
- introduces the duty to identify the 'beneficial owner' of the transaction or the relationship;
- requires the application of customer due diligence measures on a risk-based approach;
- provides for different reporting obligations in light of the specific activities carried out by the entity subject to AML regulation;
- sets down the authority responsible for suggesting the criteria for detecting suspicious transactions;
- abolishes the penalty fee for failure to create an electronic database containing data and information regarding clients and transactions (so called 'archivio unico informatico');
- introduces an administrative penalty for failure to create appropriate internal procedures and to provide appropriate personnel training;

- introduces the joint and several liability of the entity where the perpetrator of the breach is not identifiable or not prosecutable; and
- adds money laundering to the list of offences for which companies may be subject to administrative liabilities.

## The specific offences: money laundering and terrorist financing

26.8 Money laundering and terrorist financing are defined by art 2 of Legislative Decree No 231 of 21 November 2007. Pursuant to the Decree, money laundering means, if committed intentionally:

- the conversion or transfer of goods, made being aware that such goods come from a crime or from a participation in a crime, with the purpose of hiding or masking the illegal provenance of such goods or with the purpose of helping anyone who is involved in such activities to avoid the legal consequences of his/her behaviour;
- the hiding and masking of the real nature, provenance, location, disposal, movement, property of the goods or of the rights on such goods, made being aware that such goods come from a crime or from a participation in a crime;
- the purchase, holding or use of goods being aware, at the time of receiving them, that such goods come from a crime or from participation in a crime;
- participation in one of the actions described under (a), (b) or (c) above, being associated in the commission of such acts, attempting to commit them, helping, inciting or advising other persons to commit such acts or helping to implement them.

Money laundering is considered as such even if the activities which produced the goods to be laundered have been committed outside Italian territory.

26.9 Pursuant to art 2 of Legislative Decree No 231 of 21 November 2007, which makes reference to art 1 of Legislative Decree No 109 of 22 June 2007, terrorist financing means any activity intended, by whatever means, to collect, supply, intermediate, deposit, safeguard, or deliver funds or other assets, in any way achieved, and intended to be used, in full or in part, to commit one or more crimes having a terrorist nature, or in any case addressed to help the commitment of one or more crimes having a terrorist nature, independently from the actual use of the funds and the assets to commit such crimes.

## Penalties

26.10 Non-compliance with the duty to identify a client is punished by a fine ranging from €2,600 to €13,000.

26.11 A client who does not provide information on the purpose and nature of the continuing relationship with the intermediary or about the professional service

that the fraud, either because of its magnitude or character, may lead to one or more public hearings being held, in which either the company, its board members or its senior officers may be involved. The possibility of a public hearing being held must also be considered when considering whether or not the associated negative publicity may lead to financial damage to the relevant company, as this may have a bearing on whether fraud is considered to be 'substantial'.

#### The magnitude of the fraud

**31.71** The following observations can be made with respect to the magnitude of the fraud. In the event that a person has been convicted in criminal proceedings the court may order the person to pay the State an amount equal to the profits which he made as a result of the criminal offence for which he has been convicted (or as a result of other criminal offences which in the court's view the person is also likely to have committed).<sup>78</sup> For example, where a company has generated turnover and profits from corrupt activities, the company may be ordered to pay back amounts equal to these profits (ie the revenues minus the costs incurred in connection with those revenues, to be determined by the court).

**31.72** As a consequence, it is possible that the mere fact that a company has committed an offence will mean that there has been fraud of 'substantial size' within the meaning of Art 36 of the Bta. It follows that an accountant who discovers or suspects that fraud has been committed by a client should advise both the criminal offences involved as well as their possible legal consequences.

#### Duty to report: 'reasonable suspicion'

**31.73** The consequences of the broad and imprecise definition of 'substantial fraud' are that an accountant must take action as soon as 'data or information' (*gegevens of inlichtingen*) justify 'reasonable suspicion' that there has been 'substantial fraud with respect to the financial accounts of the company'.<sup>79</sup> It is not necessary for the accountant to have hard evidence that fraud may have been committed. 'Information' is sufficient. Nor is it necessary for the accountant to be convinced that fraud has actually been committed. He is obliged to take action as soon as he has 'reasonable suspicion' of fraud. The wording – 'reasonable suspicion' – is similar to the wording used in Art 27 of the Dutch Code of Criminal Procedures. Art 27 provides that a 'suspect' is anyone with respect to whom there is, on the basis of facts and circumstances, a reasonable suspicion of being guilty of a criminal offence. The Code distinguishes various categories of suspicion. The lightest form of suspicion is 'reasonable suspicion'.<sup>80</sup> The standard of probability required for 'reasonable suspicion', is not very high. Suspicion merely has to be 'reasonable', on the basis of facts, or even on the basis of 'information', to compel an accountant to report his suspicions to his client.

<sup>78</sup> Art 36e, subs 2 of the PC.

<sup>79</sup> Art 26 subs 2 of the Wta.

<sup>80</sup> Spronken, Art. 27 Sv. aant. 3.

**31.74** The Wta and the Bta do not leave much discretion for the accountant to determine whether or not he must report suspicions of fraud to his client. Where an accountant has reasonable suspicions of substantial fraud, it is not up to him to investigate further. The duty of the accountant is to inform his client of his suspicions. It is for the client to investigate the suspicions. The fact that the definition of 'substantial fraud' is broad and vague may mean that suspicions of 'substantial fraud' arise even sooner than would be the case if the definition was more precise. The obligations of the Wta and the Bta do not influence the obligation to report suspicious transactions. As discussed above, an accountant who reports his suspicions of fraud to his client, does not have to report those suspicions to the police if his client takes adequate measures to counter the fraud, in accordance with Art 37 of the Bta. However, in such circumstances the accountant must submit a suspicious transaction report to the FIU as, when a client has committed fraud, he is likely to have engaged in asset-laundering Activities as designated by Art 420bis of the PC.<sup>81</sup> Any company which is informed by its accountant that he has reasonable suspicion that there has been substantial fraud, should assume that the accountant has already made a suspicious transaction report to the FIU. If an accountant reports a suspicious transaction to the FIU, the FIU assumes that the accountant will prepare an appropriate file. The client is obliged to start his investigations when his accountant reports his suspicions. The client will have to prepare a written plan describing the consequences of the fraud and the measures taken to rectify them.<sup>82</sup> The accountant must prepare a file to record his judgement on the client's plan and how he supervised its implementation.<sup>83</sup> The file will contain information about the fraud and the client's investigations.

**31.75** If the FIU informs the public prosecutor that an accountant has reported suspicious transactions which might justify reasonable suspicions of substantial fraud, it is possible that the public prosecutor will at some stage demand that the accountant hands over his files. The public prosecutor has the authority to make such a demand under the Dutch Code of Criminal Procedures.<sup>84</sup>

#### Forensic accountants

**31.76** As a result of the combined duties imposed by: (a) the Wta; (b) the Wwft; and (c) the Dutch Code of Criminal Procedures, the accountant may in practice operate in a similar way to a forensic accountant. Ultimately, he may do so in favour of the public prosecutor in the sense that the accountant may be compelled to hand over any files relating to the fraud.

<sup>81</sup> During parliamentary discussions of the Bill preceding the Wta, the possibility that an accountant will have reporting duties both on the basis of the Wta and Bta as well as on the basis of the Act regarding suspicious transactions, has been mentioned explicitly. Kamerstukken I, 2005–2006, 29658, No c (MvA, p 23).

<sup>82</sup> Art 37 subsection 1, a, 1N Bta.

<sup>83</sup> Art 37 subsection 2 Bta.

<sup>84</sup> Code of Criminal Procedures, Art 126nd.