



To paraphrase *The Wire*, if you just go after the drugs, all you get is drugs; chase the money and you never know where it may lead. But with HSBC the latest bank to be embroiled in a drug money scandal, how effective are anti-money laundering strategies?

By Euan Grant

In April 2006, Mexican soldiers intercepted a plane carrying 5.7 tons of cocaine. But as reported in *The Observer* (3rd April 2011), they also found something far more significant than even nearly six tons of coke. They uncovered the paper trail behind the purchase of the plane itself by the Sinaloa drug cartel. That sparked a twenty two month investigation which revealed that nearly four hundred billion dollars in wire transfers, traveller's cheques and cash shipments – a sum nearly equivalent to a third of Mexico's GDP – went into Wachovia, one of America's biggest banks. The case never came to court; instead the bank settled with the federal authorities for a fine equivalent of less than 2% of its profit for 2009. And the only reason that all the details came to light was through the tenacity of the bank's London-based senior anti-money laundering officer who had to whistleblow in order to spark the investigation and was hounded out of the company for his troubles. The federal prosecutor remarked, "Wachovia's blatant disregard for our banking laws gave international cocaine cartels a virtual carte blanche to finance their operation".

Money laundering is the process by which the proceeds of criminal activity are cleaned (or laundered) by

a transaction or series of transactions which seek to disguise the criminal origins of the proceeds. It follows that nearly all criminal activities carried out for gain will involve money laundering. Cash is turned into other assets, and non-cash transactions are disguised through a series of financial transactions which make identification of the ultimate source or destination of the funds very difficult.

There are different types of money laundering. For example, cash smuggling involves the physical carrying of cash within countries and across borders. At its simplest this might involve the transfer of the proceeds of a drugs deal in a nightclub to a safe house, literally under the bed. It can equally apply to carrying the cash on international travel routes. That is certainly what many see money laundering as being. It is for these reasons that within the EU, cash sums of 10,000 euros equivalent and above must be declared to the border agencies, who keep records and use it for intelligence purposes. The Mexican authorities tackling their lethal drugs trafficking gangs place a lot of emphasis on how the cartels use cash businesses such as cafes and dry cleaners. Knowing this is one thing, however; trying to stop it in such a violent and corrupt environment is another.

Moving money internationally makes it harder to detect at destination but does run some risk of confiscation or detection at border controls (if there are any). Smugglers take countermeasures (more couriers, smaller sums) so cross-border identifications will often only be made if the person is already somebody who is being watched.

The key point is that cash remains cash and does not go through the banking system to any extent. Criminals have been making more use of *bureaux de change* and money transfer services such as Western Union to launder cash rather than relying solely on the banks. These more recent outlets are also the subject of law enforcement interest but the sheer number of transactions and lack of customer identification limits the chance of detection.

The HSBC case in Mexico and Florida is a classic example of where cash based money laundering schemes merge with bank transaction money laundering. In July, the US Senate on Homeland Security and Governmental Affairs published a scathing three hundred page report into the banking activities of HSBC, accusing it of exposing the US financial system to an array of financial risk including the washing of drug money from the Mexican drug cartels.

The very large sums which were

transferred from Mexico to the Miami branch of HSBC were originally deposited into the system in Mexico in cash from traditional cash businesses. The frequency, duration and scale of the transfers were later admitted to have been such that they were not considered consistent with legitimate activities. HSBC has admitted that the transactions should, like the transactions to Wachovia bank, have been positively identified earlier.

Launderers seek safety in numbers. Those involved in the HSBC case chose Miami which is a centre for transfers involving Latin America. They assumed correctly that the bank's on-site compliance staff would have been overwhelmed by the number of suspicious transactions from numerous accounts. The launderers felt there was safety in numbers, an argument which certainly applies to transactions to, from, and especially through the UK, particularly London. The bank's overseeing compliance staff were reportedly based in India and were probably using automated detection systems with limited human oversight. Both are needed. Staff numbers and staff training (or lack of it) contribute heavily to the detection failures.

Suspicious transactions are evidence of crime, but don't necessarily identify what kind of crime. The recent confiscation of assets from a drug dealer who was the son-in-law of Neil Aspinall, CEO of the Beatles Apple Corporation (London Evening Standard 15th October 2012) shows this. The bank transactions were originally investigated by the Metropolitan Police's National Terrorist Financial Investigation Unit but were found to be from drug dealing. The patterns of cash flows are typically very similar.

White collar money laundering is the same in principle as cash smuggling, but more complex. At the highest levels, these crimes see the involvement of 'deep state' national interests, which are very difficult indeed to confront. The recent reports of the involvement of Standard Chartered and RBS in dealings with Iran provide an example. The UK is especially used as a respectable transit destination for such movements as it is somewhat misleadingly considered to be clean by international law enforcement agencies and monitoring bodies. It also has a huge network of no questions asked facilitators, such as company formation agents, as a recent report in The Economist (22nd September 2012) has highlighted. The basic aim of the

creation of long corporate chains and bank accounts outside the jurisdictions of the companies – a classic giveaway is to disguise the true owner of the assets (the real or "beneficial owner"). The authors of the article asked 3700 agents in 182 countries to form 'shell' companies for them. Nearly half of the agents failed to ask for proper identification in direct contravention of the international standard for governing shell companies.

In most countries of the world money laundering is a criminal offence in itself, regardless of the nature of the criminal offence in relation to which the money laundering is carried out. Increasingly, criminals are being convicted of money laundering without proof of the original criminal being required.

WACHOVIA'S BLATANT DISREGARD FOR OUR BANKING LAWS GAVE INTERNATIONAL COCAINE CARTELS A VIRTUAL CARTE BLANCHE TO FINANCE THEIR OPERATION

However, in practice enforcement of the legislation is very difficult. Many countries with such legislation have produced very few convictions. The system in western developed countries is complex and cumbersome while in large parts of the middle income and developing world, the legal, financial and investigative infrastructures are virtually non-existent. So much needs to be done to improve the situation; the key tools of prosecution, civil confiscation and the freezing of assets need to be much more closely coordinated.

Progress is also inhibited because money laundering is 'asymmetric' as far as regulators and law enforcement agencies are concerned. Successful action in one country against an international criminal organisation might not be repeated in cooperating countries because the assisting agencies feel they are not getting sufficient credit for their role in the prosecutions: they are helping agencies in other countries without necessarily getting 'results' in their own.

Another reason why the success rate is low is because major money launderers have typically taken steps to place their assets beyond the reach of the UK's courts. Recent case successes involving Nigerian criminals have

involved positive developments with convictions and seizures of deposits and other assets and an extradition from Dubai, but the persons involved had much less political clout than the really big players such as Afghan politicians and Pakistani generals where political protection is bought for those who might be involved in drug trafficking and the financing of terrorism. Longer term, as Clare Short, former Secretary of State for International Development said, prosecution is not the only answer. There needs to be much greater civil enforcement and other regulatory cooperation between governments.

So you have a situation where major western banks have been ignoring the banking rules and governmental bureaucracy hampers intelligence gathering and sharing and that's just in countries which actually have any kind of anti-money laundering infrastructure in place. So how can the situation be improved?

The current embarrassments in the banking world do offer real opportunities. A posting to a bank's compliance department should be regarded as a positive career move and not the graveyard slot as it often is now. Banks must raise the level of training of cashier and other branch staff involved in applying the "know your customer" regulations appropriately. The banks should be enhancing their image by deploying some of their investment bankers (who know all about risk!) to support the retail banking compliance teams.

In the UK, there should be a greater emphasis on involving the tax authorities in producing improved guidance for identification of suspicious transactions, as these may well identify tax evasion too, given launderers' favoured use of cash businesses.

And then, what next? If the banking system is really tightened, how will the money launderers react? There may well be an increase in bartering of goods and services, but that has obvious practical limitations and requires unusual levels of trust, as do the hawala banking systems common in the Middle East, East Africa and South Asia and in their diaspora communities in Europe and North America. And these systems do involve cash transactions at either end, so old fashioned identification of unusually active retail outlets still comes into play.

■ **Euan Grant** is a customs, tax and border security consultant