

# **MONEY LAUNDERING, CORRUPTION AND THE PROCEEDS OF CRIME - AN INTERNATIONAL REALITY CHECK**

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**H**AVING SPENT THE PAST 30 YEARS traveling the globe in the investigation, prosecution, training and studying of international economic crime and money laundering, I thought it might be topical to offer a global perspective on what has become an area of international concern.

An indication of the growth of this concern, from a personal standpoint, arises as a result of my chairmanship for the past 20 years of the International Symposium on Economic Crime held at Jesus College, Cambridge (England) in September annually. At our first meeting in 1982, there were some 35 delegates from six countries in attendance. Over the past 3 years, we have had between 800-900 delegates from over 90 countries.

Where the laundering of the proceedings of narcotics trafficking used to be the major impetus, now the funds of terrorists, tax evaders, and corrupt officials have also become prime targets of the international community.

The breadth and scope of the topic of money laundering is so wide as to make it impossible to do justice to the subject in the time allotted. One could spend many days discussing definitions of money laundering, the modus operandi of those engaged in it and the justifications for attempting to stop or at least deter it.

Accordingly, I shall attempt in these few minutes to give a broad-brush look at the subject.

The IMF has estimated that money laundering represents two to five percent of global GDP - that represents trillions of dollars. The largest source of that tainted money is clearly derived from drug trafficking. Somewhere between US\$600 billion and US\$1.5 trillion, the proceeds of drug trafficking, corruption and organized crime flows through the global financial system each year. These funds must not only be concealed from the prying eyes of the police, but must be legitimized so that the ultimate recipients may enjoy their benefits. The launderer therefore seeks what

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appear to be normal banking services in international private banking, such as established offshore trusts, back-to-back loans, and the establishment of offshore corporate entities as the recipients of these funds.

The impact on various jurisdictions, although substantial in each case, differs widely. The main crisis originally facing the U.S. was drug trafficking, but now includes terrorism and tax evasion. On the other hand the use and abuse of drugs is not the greatest concern of African Nations and India. It is the outflow of hard currency, which destroys their economic stability.

Capital flight normally results from anticipated political or economic uncertainty, or perceived excessive tax rates. As a result, complex but highly effective underground banking systems have emerged such as the Hawala in India, and the Fei Ch'ien in Chinese communities. These systems are virtually impenetrable by outsiders, and are the mechanisms by which incredible sums of money, both illicit and lawful, flow. An international survey conducted on behalf of India disclosed that Indian Hawala operations were spread from the Philippines and Hong Kong in the East, to Singapore and Sri Lanka, Oman and Dubai in the Middle East, and the UK, Europe and the U.S. The capital involved was estimated at US\$10 billion. Obviously these underground banking systems are also employed by those who must legitimize or conceal the proceeds of their illegal activities.

In the past, great emphasis and huge resources have been expended in the investigation and prosecution of those who launder "narco-dollars", and in the confiscation of their assets. Governments now however, have recognized the use to which offshore jurisdictions have been put in the laundering of other illicit or questionable funds, and the threats resulting to their financial institutions, and their own economic viability.

The collapse of BCCI is a case in point, demonstrating how institutions (financial and regulatory), politicians, professional advisors and depositors can be destroyed almost overnight.

The scope and magnitude of the problem is astronomical:

- In June 1998, U.S. Customs agents at Port Newark searched a 20 foot cargo container which was enroute to Venezuela. They discovered through the use of a mobile x-ray \$11.2 million hidden in truck transmissions.
- According to the International Finance Institute, over \$140 billion was taken out of Russia between 1991 - 1999, of which \$20 billion was removed in 1999 alone.
- In 2000, 15 banks in London were investigated for laundering over \$4 billion which were alleged to be funds loot-

ed from Nigeria by the late dictator Sani Abacha. A month earlier the Swiss authorities temporarily froze \$660 million in Abacha family funds.

- In the same year the U.K. Government indicated they had identified 400 cases where criminals have built up personal fortunes worth a total of £440 million from the drugs trade and organized crime.
- An in-depth computer analysis conducted by two professors of the Florida International College of Business indicated that the U.S. Government lost more than \$42 billion in tax revenues in 1999 due to the artificial overpricing and under-pricing of products entering and leaving the U.S. The study showed that a conservative estimate of the taxes lost in 1999 due to the abnormal pricing in international trade was \$42.71 billion - more than \$117 million per day.

If to the estimated US\$400 billion generated from the sale of drugs in the U.S. and Europe is added the many billions of dollars generated from flight capital, traditional criminal activity and tax evasion, it is patently obvious that money-laundering has been an international growth industry. There is, to my knowledge, no reason to believe that the situation will improve in the foreseeable future.

It is important to bear in mind that in order for money laundering to be successful, there must be facilitators. These include financial institutions, corrupt politicians, regulators and professional advisors.

Virtually every country is subject to being adversely affected by the problem, either as a victim or as a facilitator. Capital flight, tax evasion and exchange control violations all attack the economic stability of a country. Monies earmarked to build schools and hospitals from anticipated revenues may not be available. The unlawful expatriation of hard currency may affect the ability of a country to pay its foreign debt. At the same time the domicile of the facilitators will be affected by the potential of corruption of its officials and institutions, and the loss of international credibility. In October 1995, the Presidential Directive in the U.S. stated very firmly its commitment to ascertain those overseas jurisdictions which welcomed those with illegal wealth and threatened serious sanctions against them should they refuse or neglect to deter money laundering.

The Clinton administration, in an attempt to stop the flow through the U.S. financial institutions of billions of dollars from drug trafficking, sought Congressional approval to fight money laundering. One of the proposals from the Treasury Department sought to give it approval to cut off foreign governments from the U.S. financial system, without seeking

Congressional approval, in cases where those foreign governments shield banks from investigation. The U.S.A. Patriot Act, 2001, prohibits, *inter alia* U.S. financial institutions from maintaining correspondent accounts for foreign shell banks.

The concerns of the U.S. were aroused in the fall of 1999 when it was disclosed that some \$7 billion in suspect Russian funds were found to have been transferred by the Bank of New York.

In February of 2000, Finance Ministers from 34 Western Hemisphere countries agreed to set up a regional alliance to coordinate the fight against white collar crime and drug trafficking.

As a further step to stem this tidal wave, the international community has threatened stern measures against those who facilitate the laundering of these vast sums of illicit monies.

The Financial Action Task Force on Money Laundering, set up by the OECD, identified so-called "tax havens" that fail to cooperate in the international fight against economic crime and money laundering. The members are threatening counter measures to protect their jurisdictions from the inflow of illicit monies.

The Task Force identified four main obstacles to the fight against the laundering of dirty money, as follows:

- Failings in financial regulations, which amount to inadequate controls of the financial sector, obligations that are not binding for granting financial institution approval or client identification, and excessive financial secret regimes and a lack of a system for declaration of suspect transactions;
- Weaknesses in the provisions of commercial law, including the identification of owners-beneficiaries and procedures for company registration;
- Obstacles to international cooperation, both at administrative and judicial level;
- Inadequacy of resources for the prevention, detection and repression of laundering activities.

As if the problem was not already difficult enough, it now appears clear that illegal money launderers are targeting financial institutions which do business on the Internet. Unfortunately, the law enforcement agencies and the laws of most jurisdictions remain undeveloped and appear to be unable so far to cope with this added dimension. Considerable effort must be exerted internationally to require customer identification and the avoidance of anonymous accounts, tightening bank licensing rules and agreeing upon uniform international standards of compliance and regulation.

We in the international community have every reason to be concerned. With the billions of dollars of illicit monies flowing through the international monetary system, there is created the potential of significant economic and political power. This power emanating from the fraudsters, narcotics traffickers, terrorists and organized crime groups, has and will produce detrimental effects upon our countries, their citizens and political institutions.

It is clear that no jurisdiction is immune from the threat of corruption. It is equally patently obvious that those jurisdictions that maintain a *laissez-faire* attitude to the source of money coming into their institutions, or the bona fides of those who bring it, are at greatest risk.

Through Operation "Greenback", conducted in the 1970's by the U.S. Treasury, officials discovered that money launderers were buying banks or placing their people in management institutions so that they could facilitate the evasion of the U.S. *Bank Secrecy Act*. Once our financial institutions are penetrated by money launderers or organized crime groups, our very economic survival is threatened.

Once our political institutions are corrupted, they are subject to the improper influences of the criminal element to affect laws and regulations designed to inhibit criminal enterprise. They may even exert sufficient pressure to prevent such laws from being enacted. I am personally aware of three jurisdictions whose laws in respect of banking, money laundering and off-shore business generally, were drafted by well-known money launderers.

The result of such a situation is economic and political instability and the reluctance by foreign investors to do business in those jurisdictions. Until such time as genuine international commitment exists, until sufficient resources are made available for the purpose and until real international cooperation is realized, we fight a losing battle.

With regards to the private sector, it is appropriate to ask why it should be concerned. The answer includes a myriad of multi-faceted factors:

- (i) the integrity of the market place is adversely affected;
- (ii) the reputations of the business or industry and those who form part of it, whether or not directly or indirectly involved in corrupt practices, are blackened;
- (iii) the cost of doing business is increased;
- (iv) the cost of goods and services are increased;
- (v) fair trade and competition become illusory objectives; and
- (vi) the community as a whole will mould their ethical standards based upon what they perceive is the morality of their business and political leaders.

The scope of corruption in the private sector is monumental. In April 2000, the Trade Promotion Coordinating Committee in its report to the U.S. Government stated that from mid-1994 to April 1999, allegations of bribery were leveled at foreign firms in 294 competitions for international contracts. These contracts were valued at \$145 billion (U.S.) The report identified 133 firms from 43 countries, which were implicated in offering bribes for contracts in 96 buyer countries over the five year period.

In the mid-1970's an SEC investigation discovered that over 400 U.S. companies admitted making questionable or illegal payments in excess of \$300 million (U.S.) to foreign government officials, politicians and political parties. As a result, the U.S. Congress enacted the Foreign Corrupt Practices Act, as a means of deterring the bribery of foreign officials and hopefully to restore the public confidence in the integrity in the way American business is conducted.

Subsequently, Congress became concerned that American businessmen were at a disadvantage compared to foreign companies whose officials regularly paid bribes and who, in many jurisdictions were permitted to declare those payments as business expenses in order to reduce their tax liability. As a result, in 1988 Congress directed the Executive Branch to commence negotiations in the OECD between the U.S. and its major trading partners to enact legislation similar to the FCPA. By 1997, some 10 years later, thirty-three other countries and the U.S. signed the OECD Convention On Combating Bribery of Foreign Public Officials in International Business Transactions. The U.S. ratified the Convention in 1998.

In February 1999, 11 African countries, under the aegis of the Global Coalition for Africa, adopted 24 anti-corruption principles to encourage the implementation of common standards at the national level and joint action between countries in the region.

If one then accepts that the private sector does indeed have a huge role to play in the deterrence of corruption, the issue then remains as to what that role is and how can it be practically fulfilled.

As a result of globalization, an increased pressure has been imposed upon the international business community for accountability, transparency and good corporate governance. If the private section wishes to attract investments and capital in foreign markets, those building blocks of a viable, stable and productive market economy must be established. Thus, the role of the private sector is clear - to establish and maintain its long term viability.

One need only look at the new Russia to observe the effect upon a nation emerging from a socialist market economy to a free market economy. In a report published in 1995 by senior Russian Government officials

entitled "Economic Crime and the Security of Citizens, Society and the State," the authors summarized the report as follows:

- Corruption in government is rated as a greater threat to Russia's economic security than in the sharp decline of industrial output and the explosive growth of organized crime;
- In 1993 and 1994, federal officials and bureaucrats took bribes and other forms of illegal income to misappropriate licensing export quotas, registration of commercial enterprises, and easement of real estate, the value of such fraud liberally estimated at \$100 billion;
- Despite its third ranking as a threat to economic security, organized crime presently controls about 40 percent of the Russian gross domestic product;
- Overall, organized crime encompasses 41,000 economic entities, including 1,500 state enterprises, 4,000 shareholding societies, 500 joint ventures, and 550 banks;
- Approximately 700 legal financial and commercial institutions have been created by criminal entities for the purpose of money laundering.

One must bear in mind that when the Soviet Union collapsed and the KGB were downsized, 100,000 agents were left unemployed. These individuals, experienced in covert operations with vast international contacts, have become the new entrepreneurs and business agents of the new Russia. That nation, struggling to find its place in the international business community, seeking foreign investment and attempting to resolve its myriad of social problems, is fighting to prevent the complete and total corruption of its institutions by those parasites who would seek to destroy them.

Around the world, corruption of governments has become endemic, as can be seen from recent events in Colombia, India, France, South Korea, Japan, Spain, Italy, Mexico, Ecuador and Kenya.

In October of 1999, the U.S. congressional Investigators commenced hearings into Citibank's private bank division, one of the largest private banking operations in the U.S.A. During the course of the investigation, four of the banks' private clients were discovered to be:

*Raul Salinas, who is the brother of the former president of Mexico who was imprisoned for murder and under investigation in Mexico for "illicit enrichment";*

*Asif Ali Zardari, who is the husband of Pakistan's former Prime Minister and imprisoned in Pakistani prison for accepting illegal kickbacks was indicted in Switzerland for money laundering;*

*El Hadj Omar Bongo, who was President of the West African country of Gabon and the subject of a French criminal investigation of bribery charges;*

*Mohammed, Ibrahim and Abba Sani Abacha, who are the sons of Nigerian General Sani Abacha. The former Nigerian military leader is now in prison on charges of murder. He is also under investigation in Nigeria and Switzerland for money laundering.*

The Investigators discovered that Raul Salinas sent \$80 - \$100 million through his accounts between 1992 and 1995 when the funds were frozen by the Swiss court, concluding that those funds were the proceeds of drug trafficking.

They found that Gen. Abacha's sons transferred more than \$110 million through the banks accounts in London between 1988 and 1999.

President Bongo moved more than \$130 million in and out of accounts at the New York branch of Citibank between 1970 and 1999.

It is further reported that of Citibank's 40,000 private bank accounts, 350 were held by senior foreign government officials or their families, including former Venezuelan Prime Minister Jaime Lusinchi and two daughters of former President Suharto.

More recently, an investigation into the Bank of New York revealed that \$7.5 billion was moved through accounts there between 1996 and August 1999, allegedly monies funneled out of Russia on behalf of senior government officials.

On 14<sup>th</sup> February, 2003, the U.K. Government brought into force legislation to outlaw acts of bribery by U.K. nationals and companies abroad. It is said to go beyond that set out in the U.S. *Foreign Corrupt Practices Act*. It is argued that unless the international community at large imposes similar restrictions, U.S. and U.K. businesses wanting to compete abroad will be at a serious disadvantage vis à vis those nations which permit such activity.

The effect of corruption upon government officials is incalculable. As Lord Templeman stated, in delivering the judgment of the Privy council in *A.G. for Hong Kong v. Reid* [1994] 1 all E.R. 1 at p. 4:



*"Bribery is an evil practice which threatens the foundations of any civilized society. In particular, bribery of policemen and prosecutors brings the administration of justice into disrepute. Where bribes are accepted by a trustee, servant, agent or other fiduciary, loss and damage are caused to the beneficiaries, master or principal whose interests have been betrayed. The amount of loss or damage resulting from the acceptance of a bribe may or may not be quantifiable. In the present case the amount of harm caused to the administration of justice in Hong Kong by Mr. Reid in return for bribes cannot be quantified."*

The same can be said of all those in government service who allow themselves to become corrupted. No nation large or small can afford to allow its financial institutions to be used or abused for nefarious activities. Failing to heed this warning will result in the destruction of the economic stability and international reputation of all involved.

One must not underestimate the scope of the problem, the extent of which can be seen when one realizes that in 1991, the government of Montserrat on one day revoked the licences of nearly 200 so-called "banks" for their alleged involvement in fraud, money laundering and other illegal activities.

Aside from shell banks such as existed in Montserrat and which today exist in many offshore jurisdictions, there exists in a number of countries' financial institutions which are owned or controlled by organized crime figures, narcotics traffickers and money launderers. With sufficient funds, and on occasion not substantial amounts, control or ownership can simply be purchased either directly or through nominees. This is particularly true where lax banking regulations exist or where the regulators can be corrupted.

Non-banking institutions such as check cashing businesses, fund transmitting businesses and bureaux de changes have also been acquired. By bribing officers or employees of financial institutions, criminals have gained a corrupt influence over these entities.

The magnitude of such a corrupted institution can be seen from one very recent isolated case. On February 25, 1999 in London, Yusama El-Kurd was jailed for 14 years and fined £1 million for running a money laundering operation out of a small bureau de change in Notting Hill Gate. The amount involved, allegedly from drug trafficking was £70 million per month. According to Customs officers who had him under surveillance, he made 40 trips to his establishment with a bag containing £250,000 at a time and when arrested was at his premises emptying £200,000 in cash

out of bags onto a table.

The permissiveness of the regulators of financial institutions in a jurisdiction will encourage criminal elements to situate their criminal activity there, corrupting financial institutions, politicians and regulators. By employing their economic power, criminal cartels will take over or monopolize legitimate businesses and institutions. This can result in economic and political instability and resistance from foreign investors.

I am not convinced that we can expect to see much improvement in the near future. My pessimistic view is based upon the following considerations:

- a) Organized crime, be it the traditional Mafia, the Russian Mafya, the Yakuza, the triads or the Jamaican Posses, have all become more sophisticated and entrepreneurial. They realize that there is more profit and less risk in e-commerce, money laundering and economic crime than in crimes of violence. The computer has become mightier than the gun;
- b) As more and more developing nations, with inadequate infrastructures, attempt to stabilize their economies and seek venture capital, the opportunity for infiltration by corrupt groups will increase;
- c) The pressure from the OECD, the United States and the United Nations upon legitimate international financial countries to restrict or eliminate lawful tax avoidance measures, will strengthen the role of the corrupt jurisdictions, which will ignore such pressures. The fraudsters, money launderers, terrorists and narco-traffickers, will accordingly flock to those open "wild-west mentality" locales where they will be allowed to loot, rape and pillage to their hearts' desire;
- d) The ongoing worldwide ethnic and political upheavals show no sign of abeyance. The result will be that the arms traffickers, terrorists and political pirates will continue to infiltrate and corrupt the competing regimes, fomenting continued instability and uncertainty.

Since September 11<sup>th</sup>, 2001, the world has become sensitized to the threat of terrorism. Consequently, many countries have recognized that, as in the case of drug trafficking, cutting off the source of funds of terrorist organizations is critical. It appears that those organizations have been funded by a myriad of different means, including donations from charitable groups, kidnapping, extortion and the smuggling of precious gems and other commodities.

Traditional means of transferring funds have been employed using various financial institutions such as al Barakaat, a Somali banking and telecommunications group and al Taqwa, (which has been re-named the Nada Management Organisation) reputed to be a Hawala operation.

The U.S. Treasury in a report in May 2002, discussed the blocking of the assets of some 210 alleged terrorist-related entities and individuals in the U.S. in the amount of \$34 million together with \$82 million worldwide. At the end of March 2002, the U.N. estimated that 144 countries had been involved in the blocking of \$103.8 million in assets of which half represented funds connected with Osama bin Laden and Al-Qaeda.

Considerably more funding is, in my view, moved through the Informal Money or Value Transfer Systems (the IMUT system). This system consists of the underground or parallel banking systems well known in India, the Middle East and Asia and includes the Hawala, Hundi, and Fei-Chien operations. Those systems have traditionally been used for legitimate purposes to move funds from one jurisdiction or another, particularly by itinerant workers to send funds to their families in places where in some instances banks don't exist. It is a system built on mutual trust and based upon family, ethnic or linguistic ties.

They are an obvious route for the transfer of illicit funds and in particular to terrorist organizations, for they are almost impossible to penetrate. However, because of the significant amounts involved many IMUT's must necessarily resort to utilizing legitimate financial institutions. Those institutions suspecting such activity are required to file suspicious transaction reports, opening the door to investigation and detection. If for example, a small Chinese grocery store, or a neighbourhood Indian travel agency is depositing into its bank account significantly more funds than one would reasonably expect from such a business, that ought to trigger a suspicious transaction report and set the train in motion for discovery of the underlying source of the funds.

I have no doubt that this means of moving and laundering illicit funds will continue to be employed and the vigilance of those under an obligation to report must be intensified in order to make more effective the fight against money-laundering generally and the funding of terrorism particularly.

Having taken you through a quick world tour I would like to conclude with a short anecdote.

In November, 1989, (long before the Enron debacle,) I appeared as a witness before the United Kingdom's House of Commons Trade and Industry Committee on Company Investigations. During my testimony, I referred to the common law exception to the duty of confidentiality, which permits disclosure of crime or fraud. I stated that as early as 1856, in

*Gartside v. Outram* (1856) 26 L.J. Ch. 113, it was held that:

*"The true doctrine is that there is no confidence as to the disclosure of iniquity. You cannot make me the confidant of a crime or a fraud, and be entitled to close up my lips upon any secret which you have the audacity to disclose to me relating to any fraudulent intention on your part: such a confidence cannot exist."*

During the course of my testimony before the Committee, I referred to the dicta of Lord Justice Lopes, in the case of *In re Kingston Cotton Mill Company (No. 2)* [1896] 2 Ch. 279. In that case, His Lordship, in dealing with the duties of an auditor said, at p. 288, "He is a watch-dog, but not a bloodhound." After referring to that dicta, and noting that times have changed dramatically since 1896, I said that, "We need watch-dogs with teeth, not toothless watch-dogs." The Chairman had interposed to say, "What we need are a few Rottweilers."

I recommended to the Committee that legislation be enacted to codify the common law and compel auditors to disclose evidence of crime. The Committee in its report to Court accepted that recommendation. The recommendation of the Committee and my views were apparently not well received by the accountants, as evidenced by the July 1990 edition of "Accountancy," the magazine published by the Institute of Chartered Accountants in England and Wales.

Under the editorial entitled "The Watchdog, The Bloodhound And The Man From Bermuda," the editor commented, *inter alia*, as follows:

*"Whatever the Committee's precise intentions, three points need to be made. The first is that no evidence has been produced of auditors having knowledge of serious crime, but then remaining silent about it. So what is the problem?"*

*Second, the profession already has guidance that deals with this subject satisfactorily; namely, the guideline on the auditor's responsibility in relation to fraud, other irregularities and errors. So why is legislation necessary?"*

*Third, the basic principle of confidentiality between auditor and client exists because it is in the public interest. The audit could not be performed effectively without it. An ill-defined statutory obligation could easily shatter this principle, and it is difficult to see how such an obligation could be well-defined.*

*The auditor must remain a watchdog. A profession of Rottweilers would be a dangerous and anti-social innovation."*

The Government in its White Paper chose not to accept that recommendation, and said:

*“For all these reasons the Government do not at present believe that it is right to impose a statutory duty on auditors. The Government would prefer to see how practice develops in the light of the recent legislation, and believe that the body of guidance developed by the profession meets the concern implicit in the Committee’s recommendation.”*

Well, as the Virginia Slim cigarette ads used to say, “You’ve come a long way baby.” I am pleased to see that many jurisdictions have placed an obligation on accountants to disclose evidence of suspicious transactions. Unfortunately, it has taken a series of major financial disasters for governments to respond to what was obvious to me and others more than a decade ago.

The late Sonny Bono used to sing, “And the beat goes on.” So it shall and hopefully the international community will one day all be marching to the beat of the same drummer. We live in hope.