

International Efforts against Money Laundering

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INTRODUCTION

The explosion of international financial activity over the last decade has been a central fact of international economic life. Balance of payments statistics indicate that cross-border transactions in bonds and equities for the G-7 states rose from less than 10 percent of gross domestic product in 1980 to over 140 percent in 1995.¹ International bond markets have reached staggering proportions: by the end of 1995, some US\$ 2.803 trillion of international debt securities were outstanding worldwide. Capital flows to developing countries and countries in transition grew from US\$ 57 billion in 1990 to over US\$ 211 billion in 1995.² Foreign lending in the form of international syndicated credit facilities has surged since the 1980s, to over US\$ 320 billion at the end of 1995. Foreign exchange transactions—which represent the world's largest market—reached an estimated average *daily* turnover of nearly US\$1.2 trillion in 1995 compared to US\$590 billion daily turnover in 1989.³

The growth of international capital markets has been a boon to economic efficiency and growth for many countries, but enlarges the opportunities for resources raised from illicit financial activities to cross borders undetected and make their way into the legitimate stream of capital, increasing the opportunity to use international markets for illicit activities. Money laundering—or the transferring of illegally obtained money or investments through an outside party to conceal the true nature of the source—has exploded as a

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¹ Figures exclude the U.K. Cited by White, W., *International Agreements in the Area of Banking and Finance: Accomplishments and Outstanding Issues*, paper presented at the conference Monetary and Financial Integration in an Expanding (N)AFTA: Organization and Consequences, organized by the Center for International Studies at the University of Toronto, Toronto, May 15–17, 1996, 3.

² International Monetary Fund, World Economic Outlook Database.

³ Bank for International Settlements, *Central Bank Survey of Foreign Exchange and Derivative Market Activity* (1996) 5.

result. The Financial Action Task Force (FATF), created by the major industrial countries in 1989, estimated that by 1990 about US\$ 122 billion was being laundered annually in Europe and the United States (or about US\$85 billion net after 'expenses')⁴. By some estimates, one billion dollars of criminal profits finds its way into the world's financial markets *every day*.⁵ Lifting capital controls has made laundering easier by reducing the scrutiny given to international transactions.⁶ Money laundering has become a global phenomenon: as North American and European regulators have stepped up enforcement efforts, sometimes with notable success, illicit funds have moved on to eastern Europe, the former Soviet Republics, the Middle East, and parts of Southeast Asia.⁷

Since the late 1980s national decision makers, regulators, standard setters, and law enforcers have stitched together standards to address the problem of money laundering in increasingly globalized financial markets. This effort has been hampered by disagreements among states as to whether money laundering itself should be illegal; the relative responsibilities of the banking sector versus law enforcement bodies; and, most importantly, the best way to address the problem without jeopardizing legitimate financial activities. Non-binding legal accords have been used extensively among states to coordinate their rules and procedures and to strengthen cooperation for purposes of prosecution. This essay will discuss why it is that compliance has been difficult to obtain in this issue area, and will examine in some depth the role of the Financial Action Task Force (FATF) and its 'Forty Recommendations' in securing a measure of coordination, at least among the most industrialized countries, with respect to rules to detect and discourage money laundering. The rub for compliance has been the strong political resistance in a number of important financial centers to highly demanding financial disclosure rules, as well as deeper resistance in a number of jurisdictions to close scrutiny of foreign capital that might aid in development. Despite their non-binding nature, however, the FATF standards do have significant influence: peer review and pressure have helped to bring some countries into line with the most significant of the recommendations. Globally, however, compliance

⁴ Harrington, H., 'Go East—or Bust' (1993) 143 *The Banker* 15–17. The Task Force included the G-7 plus Austria, Australia, Belgium, Luxembourg, the Netherlands, Spain, Sweden, and Switzerland.

⁵ Estimate given by Eduardo Vetere, head of the Crime Prevention and Criminal Justice Branch at the opening sitting of the European Regional Preparatory Meeting for the 9th UN Congress on Crime Prevention and the Treatment of Offenders (1995) February 28, 1994, Vienna.

⁶ See testimony in April 1989 of the Governor of the Bank of Italy, quoted in Gurwin, L., '1992 Means a Single Market for Crime, Too' (1990) 4 *Global Finance* 46–50 at 48. See also Tanzi, V., *Money Laundering and the International Financial System*, International Monetary Fund: Fiscal Affairs Department, Working Paper 96/55, May 1996.

⁷ Harrington, *supra* note 4 at 15; Colitt, R., 'Survey of Ecuador', *Financial Times*, July 27, 1995, 28.

remains minimal, as the financial rewards for a 'don't ask, don't tell' approach to financial transactions have to date largely exceeded the benefits of cooperation for many jurisdictions.

A. BACKGROUND TO INTERNATIONAL EFFORTS AGAINST MONEY LAUNDERING

International initiatives to control money laundering have come primarily from the United States, in alliance with the United Kingdom, France, and increasingly Australia. In 1986, the United States was the only country to have criminalized money laundering, and it remains by far the leader in prosecutions.⁸ Relatively few prosecutions have taken place in Europe, although regulations have tightened significantly as a result of an E.U. directive on money laundering. Australia has begun to take on a crucial leadership role with one of the most technologically sophisticated methods for detecting financial patterns associated with illicit activities. Australian authorities have used forfeiture funds to establish a secretariat for the FATF in Asia.⁹

I. The Nature of the Problem

Money laundering cannot be handled effectively on a unilateral or bilateral basis. Significantly different rules across jurisdictions invite 'forum shopping', the shifting of business to countries with weaker controls.¹⁰ When the United States passed the Bank Secrecy Act of 1970, tightening reporting requirements for cash transactions over US\$10,000, illicit money moved to Europe, where most banks were not required to collect information on large cash deposits.¹¹ As the rules have tightened in Western Europe, illegal-source money is increasingly directed towards jurisdictions where regulations are more lax (Eastern Europe and the former Soviet Republics, the Gulf and Mediterranean regions, and the emerging economies of Asia¹²) or to non-bank institutions, where stockbrokers are much less likely than bankers to know their customers.¹³ One Bank of England official has reportedly said

⁸ Between 1991 and 1993 the number of cases filed and tried under Title 18 U.S.C. 1956 or 1957 approximately quintupled. In 1993, 822 cases were filed and 106 tried. Justice Department figures, reported in Courtney, A., 'The Buck Never Stops' (1994) 144 *The Banker* 82-5.

⁹ Discussion with officials from the US Treasury and FINCEN, August 5 and 8, 1996.

¹⁰ Ron Noble, immediate past president of the FATF.

¹¹ Switzerland, Andorra, the Channel Islands, and Luxembourg, with their strict bank secrecy rules, and Austria where anonymous numbered accounts are permitted, probably absorbed a significant share of these funds. Gurwin, *supra* note 6.

¹² Burns, J., 'MPs Urge Money Laundering Crackdown', *Financial Times*, July 26, 1995, 8. Harrington, *supra* note 4 at 16-17; MacDonald, S.B., 'Asia-Pacific Money Laundering' (1993) 22 *International Currency Review* 30-4.

¹³ Courtney, *supra* note 8.

fighting money-laundering is like squeezing a balloon—you simply displace the activity to wherever there is the least resistance.¹⁴ To yield significant benefits, near-global cooperation is a virtual necessity.

Despite the need for cooperative efforts, individual jurisdictions have incentives to resist international agreements to control money laundering. First, banking secrecy is often considered essential in attracting legitimate business; extensive inquiry into the source of funds is likely to push funds offshore.¹⁵ Private banking, as it has been practiced in Switzerland, Liechtenstein, and Luxembourg, for example, has established a lucrative financial niche. The business of managing the funds of wealthy clients provides a third of the Swiss Bank Corporation's very stable profits.¹⁶ These funds also provide the basis for the country's relatively large capital and securities market. Swiss officials have long recognized that bank secrecy has contributed significantly to the high standard of living and thus 'at least indirectly concerns substantial economic interests of the state'.¹⁷ In Liechtenstein, even mild rules regarding 'due diligence', which require bankers to report suspicious activities to authorities, 'pose a direct threat to Liechtenstein's basic competitiveness', according to bankers in Vaduz.¹⁸

Banking secrecy combined with loose supervision may be an attractive policy for a large number of resource-poor who hope to augment national revenues. Some jurisdictions have instituted easy rules of incorporation, eschewed recording requirements for large cash transactions, and have a limited or non-existent capacity for asset seizure or confiscation.¹⁹ Especially

¹⁴ *Ibid.*, 88-9; Dumbacher, J., 'The Fight Against Money Laundering' (1995) 30 *Intereconomics* 177-86.

¹⁵ Troshinsky, L., 'Ex-NatWest Lawyer Fears "Know Your Customer" Fallout' (1996) 96-31 *International Banking Regulator* 1 and 6.

¹⁶ Some estimates suggest that private assets managed in Switzerland total SFr 20,000bn, or about a third of all money placed by wealthy individuals in banks outside their home countries. Roger, I., 'Survey of Swiss Banking', *Financial Times*, October 26, 1995, London, III.

¹⁷ This statement is a translation of official Swiss Federal Government policy, quoted in Aubert, M., *et al.*, *Das Schweizerische Bankgeheimnis* (1978) 59 (translation provided in a summary generously supplied by an official of the International Monetary Fund). Recent changes in Swiss bank secrecy law now give banks the *right*—but *not the obligation*—to report suspicious clients. The current Swiss Federal Attorney General is now pressing for Switzerland to adopt obligatory reporting, in line with the rest of the E.U. But her attempt to introduce such an obligation in a bill last year was defeated by ferocious lobbying by the financial community, which claimed that such a rule would have turned bankers into policemen, and would have resulted in the whole detection process becoming buried in a blizzard of insignificant cases. See articles by Williams, F., and Roger, I., 'Survey of the Swiss Banking System', *Financial Times*, October 26, 1995, IV and V. See also Clarke, Th., and Tighe, J.J., *Dirty Money: Swiss Banks, the Mafia, Money Laundering, and White Collar Crime* (1975).

¹⁸ Liechtenstein offers a level of banking secrecy that is even tighter than that of Switzerland; bankers there are not required to know the identity of the account's ultimate beneficiary as would be required in Switzerland. 'So Far but no Further' (July 1996) *EuroMoney* 151.

¹⁹ Not all offshore centers can be characterized by these priorities. Bermuda, for example, has shunned an influx of foreign banks because of fears of money laundering. Saul, D., 'Survey of Bermuda', *Financial Times*, November 7, 1995, V. Malta, which is attempting to establish itself

where banks and other financial institutions allow dollar deposits, these practices often unintendedly attract drug money.²⁰ 'The core of the dilemma is that not all the money that needs to be laundered necessarily stems from criminal activity. Dirty money is hot money, but the reverse is not [always] true.'²¹

Another motive to decline cooperative initiatives may be the costs involved, because extensive financial reporting systems are expensive.²² Tradition and idiosyncratic domestic political constraints in some countries also may be a factor. Austria's unwillingness to give up its anonymous savings accounts provoked a dispute with the E.U. about whether Austria has fulfilled its obligations under the 1991 directive on money laundering.²³ Unlike the interest financial institutions may have in developing a reputation for safety, 'it is not necessarily in the direct financial interest of financial institutions to adopt anti-laundering behavior'.²⁴ Anti-money laundering efforts provide no clear economic payoff, and may in fact exact immediate costs.

2. Major International Anti-money Laundering Efforts

International political pressure, largely from the United States, has been the driving force behind harmonization of national money laundering rules to date.²⁵ The earliest and clumsiest initiatives came when the U.S. Congress

as a financial center, has closely followed British regulatory practice and has enacted a range of laws, including the Prevention of Money Laundering Act. Graham, R., 'Survey of Malta', *Financial Times*, September 22, 1995, III. The British Virgin Islands have developed strict rules and a clean reputation as an offshore center. 'British Virgin Islands: International Financial Center', *Asia Money Supplement*, July/August 1996, 2.

²⁰ MacDonald, S., *supra* note 12 at 32.

²¹ Bosworth-Davies, R., 'Money Laundering—Cleaning Up', *Banking World* vol. 11, no. 3, March 1993, 28.

²² In the U.S., approximately 10 million Currency Transaction Reports for cash transactions exceeding US\$10,000 were filled out in 1993. Estimated costs for the financial institutions per report were between US\$15–17. Additional costs include training, recording, and storing the data. Dumbacher, *supra* note 14 at 181. Some industry sources place the cost of CTR preparation alone as high as US\$136 annually. Powis, R., 'Money Laundering: Problems and Solutions' (1992) 175 *The Banker Magazine* 52–6.

²³ Anonymous accounts were introduced in the 19th century to protect savers against arbitrary taxation by the authorities and now number some 26 million passbooks with a total value of about 1,400 billion shillings (about US\$140 billion). Discussions with an official of the International Monetary Fund, August 2, 1996.

²⁴ Quirk, P.J., *Macroeconomic Implications of Money Laundering*, IMF Working Paper 96/66, Monetary and Exchange Affairs Department (1996) 24.

²⁵ For general reference to such pressure, see Dumbacher, *supra* note 14 at 180–1; see also 'Falling Out with Uncle Sam' (1996) 338 *The Economist* No. 7957. Firms subject to more stringent regulations of course very much support strict enforcement of the rules for their competitors, including penalties such as banning disreputable institutions from payments systems such as CHIPS and SWIFT, or legislation calling for suspension of banking licenses in cases of gross negligence, see the comments of Fullerton, R.D., Chairman and CEO, Canadian Imperial Bank of Commerce, Toronto, Canada, *Clearing Out the Money Launderers*, portions of a speech made before the Bankers Association for Foreign Trade Conference, reprinted in (1990) 9 *The World of Banking* 5–7.

passed the 'Kerry Amendment',²⁶ that required the Treasury to negotiate with foreign countries with the objective of having foreign banks record all U.S. cash deposits over US\$ 10,000 and provide information to U.S. authorities in the event of a narcotics related investigation. Should a bank fail to agree, the amendment gave the President the power to deny that bank access to the U.S.'s clearinghouse system, in an effort to isolate it from world trade. For a number of reasons (including the universal nature of the problem, opposition from Treasury,²⁷ the fear of stimulating foreign alternatives to U.S. clearing facilities, and the fear of retaliation against U.S. banks) this unilateral approach had few tangible results.

Since 1988, political efforts have had a broad regional or multilateral focus, as shown in Table 6.1. The United States' role was central to the drafting of the 1988 Vienna Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances,²⁸ which calls 'intentionally' laundering drug profits a criminal activity.²⁹ Such a designation is meant to assist information-sharing, since mutual legal assistance agreements usually specify that an activity under investigation must be a crime in both the requesting and the receiving country.³⁰ The U.S. Federal Reserve also brought the issue of money laundering to the initially unenthusiastic G-10 banking supervisors. There was some suspicion that congressional pressure underlay the Federal Reserve's interest in the matter. Nevertheless, as the wrongdoing at BCCI began to unfold, both the Swiss and Italian regulators were won over to the idea that the Basel banking committee should issue some kind of statement that financial systems must not be allowed to be used to aid criminal activity.³¹ In December 1988 the G-10 bank supervisors came up with a 'statement of principles'. It recommended that banks cooperate with investigators and limit their dealings with customers if they believed the funds were either derived from illegal activity or to be used for illegal purposes, but the agreement noted explicitly that bank supervisors in the G-10 had very different roles and responsibilities in this area, that this was *not* a legal document and *not* in any way intended to supersede national legal approaches.

²⁶ S. 4702 of the 1988 Omnibus Drug Bill. See also Crocker, T., 'Bankers, Police Yourselves' (1990) 9 *International Financial Law Review* 10–11.

²⁷ Treasury's lack of enthusiasm for this approach is described in *Drug Money Laundering, Banks, and Foreign Policy: A Report to the Committee on Foreign Relations*, United States Senate, by the Subcommittee on Narcotics, Terrorism, and International Operations (USGPO), 101st Congress 2d session, February 1990, 28. This opposition was also confirmed in an interview with a Treasury official, August 7, 1996, Washington, D.C.

²⁸ The Vienna Convention (December 20, 1988). 20 ratifications were needed for it to enter into force, which it did in 1990; 100 ratifications had been deposited by the end of 1994.

²⁹ Art. 3, s. 1, (b)(i) and (ii).

³⁰ Crocker, *supra* note 26.

³¹ Telephone interview with a Federal Reserve Official who was involved in the drafting and negotiation of the 1988 agreement, Washington, D.C., August 8, 1996.

Table 6.1: Major international anti-money laundering initiatives

Sponsoring Organization:	Agreement:	Binding?	Major Provisions
Group of Ten Committee on Banking Regulation and Supervisory Practices. ¹	Basle Statement of Principles; Prevention of Criminal Use of the Banking System for the Purpose of Money Laundering (December 1988)	NO	—establishes a minimum set of operating standards and management principles by which all banks in the IMF member countries should operate. —includes standards on customer identification, and adherence to national laws and policies intended to prevent money laundering.
United Nations International Drug Control Program	UN Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances (Vienna Convention; December 1988)	YES	—treaty ratified by 115 nations, attempts to coordinate international efforts to control illicit drugs. —requires signatories to criminalize the laundering of drug money.
United Nations International Drug Control Program	Legal Assistance Money Laundering Model Law (November 1993)	NO	—outlines model prevention measures, including limitations on the amount of cash deposits, reporting of international transfers of funds and securities, creating standards of vigilance required of financial institutions. —outlines detection procedures, including requirements for reporting suspected launderers; recommends that banking secrecy not be legally invoked as a reason for not doing so.
United Nations Commission on Narcotic Drugs	Encouraging the Reporting of Suspicious or Unusual Transactions ... to Facilitate the Investigation and Prosecution of Money Laundering Activities. (March 1995)	NO	—urges states to encourage reporting of suspicious or unusual transactions, and to collect national data on these; and to share this information with the 'competent authorities' —recommends states with experience in financial investigations lend technical assistance, at their request, to

Sponsoring Organization:	Agreement:	Binding?	Major Provisions
OECD Financial Action Task Force (FATF). ²	Financial Action Task Force on Money Laundering Report: Forty Recommendations (February 1990)	NO	states whose financial systems make them especially vulnerable to money laundering. —establishes a framework of comprehensive programs to address money laundering and facilitate greater cooperation in international investigations, prosecutions, and confiscations. —calls for each country to define money laundering and make it a criminal offense; recommends that countries extend the definition to 'knowingly' having laundered, and to the proceeds from all illegal activities, not just drug proceeds. —recommends that financial institutions not keep anonymous accounts or accounts in fictitious names; financial institutions should establish the principal owners and beneficiaries of all accounts. —financial institutions should be permitted or required to report suspicious activity to the competent authorities.
Caribbean Financial Action Task Force (CFATC) ³	19 Aruba Recommendations (June 1990)	NO	—countries need to establish competent authorities and provide resources for combating financial crimes. —calls for countries to make money laundering a crime. —endorses many aspects of FATF's 40 Recommendations. —each country ought to decide for itself what counts as a 'predicate offense' in determining whether money has been laundered, and should decide for itself

Table 6.1: cont.

<i>Sponsoring Organization:</i>	<i>Agreement:</i>	<i>Binding?</i>	<i>Major Provisions</i>
			whether laundering was done 'knowingly' or whether objective facts establish that the offender ought to have known this was the case. —establishes a series of recommendations on confiscation measures, record keeping, and currency reporting.
Caribbean Financial Action Task Force (CFATC)	Kingston Declaration on Money Laundering (November 1992)	NO	—declaration that member governments should sign and ratify the 1988 Vienna Convention, and endorse and implement the 40 FATF recommendations and the 19 Aruba recommendations, and adopt as soon as possible the OAS Model Regulations concerning money laundering offenses. —creates a secretariat for the CFATF —creates a 'forfeiture fund' to dispose of illegally obtained property. —says that individual governments should choose between voluntary and mandatory reporting of suspicious activities.
Council of Europe ⁴	Convention on Laundering, Search, Seizure, and Confiscation of the Proceeds of Crime (Strasbourg Convention) (November 1990)	YES	—effort to coordinate policies with respect to investigation of suspected money laundering and confiscation of the property and proceeds associated with illegal activities. —creates an obligation to assist other parties with the 'widest possible measure of assistance in the identification and tracing' of property and proceeds, including providing and securing evidence to establish its existence, location, nature, etc.

<i>Sponsoring Organization:</i>	<i>Agreement:</i>	<i>Binding?</i>	<i>Major Provisions</i>
European Union	Directive on Prevention of the Use of Financial System for the Purpose of Money Laundering. (June 1991)	YES	—obliges credit and financial institutions to require proper identification for all their customers when beginning a business relationship, when a single transaction or linked transactions are conducted exceeding 15,000 ECU, or when money laundering is suspected. —allows member states to put stricter rules in place than those provided in the directive (these should be coordinated by and communicated to a 'contact committee' to be established by the European Commission).
Organization of American States (OAS) ⁵	Model Regulations Concerning Laundering Offenses Connected to Illicit Drug Trafficking and Related Offenses (May 1992)	NO	—in conformity with the 1988 Vienna Convention, criminalizing money laundering related to drug proceeds, preventing the use of financial systems for laundering, strengthening national seizure and forfeiture laws, and changing legal and regulatory systems to ensure that bank secrecy laws do not impede effective law enforcement and mutual legal assistance. —bar anonymous accounts. —reporting of large transactions involving domestic or foreign currency exceeding an amount specified by the competent authority; regardless of amounts involved, financial institutions shall report suspicious transactions to the competent authorities. —provide for international cooperation with competent foreign authorities.

Table 6.1: cont.

Sponsoring Organization:	Agreement:	Binding?	Major Provisions
Summit of the Americas ⁶	Buenos Aires Ministerial Communiqué; Ministerial Conference Concerning the Laundering of Proceeds and Instrumentalities of Crime (December 1995)		<p>—calls on all countries in the hemisphere to declare money laundering a crime but allows each to define the 'predicate offenses' that give rise to laundering in national legislation.</p> <p>—calls on each government to come into compliance with the 1988 Vienna Convention, and recommends the adoption of OAS/CICAD Model Regulations.</p> <p>—recommends the thorough review and strengthening of national capabilities and procedures with respect to reporting, seizure and forfeiture, and law enforcement.</p>
INTERPOL ⁷	Anti-Money Laundering Resolution (draft, October 1995)	NO	<p>Recommends that INTERPOL members:</p> <p>—provide for the criminal prosecution of persons who knowingly participate in the laundering proceeds derived from serious criminal activity.</p> <p>—allow for legal authority for seizure of assets derived from illicit activities.</p> <p>—allow for reporting of unusual or suspect currency or other transactions to competent authorities.</p> <p>—require financial institutions to maintain records of transactions for at least five years.</p> <p>—allow for expeditious extradition of individuals charged with money laundering offenses.</p>

¹ G-7 countries plus Austria, Switzerland, Sweden, and Luxembourg.

² The original FATF consisted of the G-7 members, eight other industrialized nations, and the European Commission.

³ Members: Anguilla, Antigua and Barbuda, Aruba, Bahamas, Barbados, Bermuda, British Virgin Islands, Cayman Islands, Colombia, Costa Rica, Dominica, Dominican Republic, Grenada, Guyana, Jamaica, Mexico, Monserrat, Netherlands Antilles, Panama, St. Kitts, St. Lucia, St. Vincent and the Grenadines, Suriname, Trinidad and Tobago, Turks and Caicos Islands, and Venezuela.

⁴ Membership currently includes 25 nations from Western Europe, Scandinavia, and several Central and Eastern European nations.

⁵ Members include 35 countries from North, Central, and South America, plus 31 states with 'observer status' from around the world. Anti-money laundering efforts are centered in the Intern-American Drug Abuse Control Commission (CICAD), which was created by the OAS General Assembly in 1986.

⁶ Involving heads of state of 34 nations in the Western Hemisphere.

⁷ 176 members. General purpose is to establish information network for seeking foreign investigative assistance and for alerting foreign authorities to criminal threats.

B. FATF'S FORTY RECOMMENDATIONS

I. Major Provisions

The center of multilateral political pressure to secure rules against money laundering is the headquarters of FATF in Paris. The FATF has given more sustained attention to the problem of capital from illicit activities than any other organization. It is comprised of experts from government ministries, law enforcement authorities, and bank supervisory and regulatory agencies from twenty-six industrialized countries. To induce compliance with its 'Forty Recommendations' promulgated in 1990,³² it regularly employs peer pressure and potentially a graduated set of sanctions to review and influence the policies of its members and those of non-members.

The Forty Recommendations are addressed to state authorities (financial regulators) and to financial institutions. Section B addresses ways in which national legal systems can be improved to combat money laundering. In addition to Recommendation 1 that states ratify the 1988 Vienna Convention, it urges countries to define money laundering to include at least the proceeds of criminal drug activities, where such laundering was knowingly undertaken or such knowledge could be inferred from objective factual circumstances (Recommendations 4-6). The FATF recommended that states adopt effective seizure and forfeiture laws, including in them authority to identify and trace property subject to confiscation, to freeze or seize assets to prevent their

³² The Financial Action Task Force has only recently involved private actors in its rule making process. Private actors were excluded from the formation of the original 40 recommendations, but in September 1995, the FATF met with leading banking and securities federations in order to involve them in its review and update its 40 guidelines.

disposal or transfer, and to undertake any appropriate investigative measures (Recommendation 8).

Section C makes specific recommendations to enhance the role of the financial system in cracking down on money laundering. These recommendations are supposed to apply not only to banks but also to non-bank financial institutions. A key provision recommends the prohibition of anonymous accounts (Recommendation 12) and thus effectively endorses the Basel group's 'know your customer' guidelines. Recommendation 12 suggests that financial institutions be required 'by law, by regulations, by agreements between supervisory authorities and financial institutions or by self-regulatory agreements among financial institutions' to identify and record the identity of their clients when establishing business relations or conducting transactions. Recommendation 13 further suggests that in case of doubt about a client's identity, financial institutions should take reasonable measures to obtain information about the true identity of the persons on whose behalf an account is being opened or a transaction conducted. If financial institutions suspect that funds stem from a criminal activity, they should be permitted or required to report promptly their suspicions to the competent domestic regulatory authorities (Recommendation 16). In the absence of such an obligation, such suspicions should at least lead the institution to sever relations with the customer and close the account (Recommendation 19).

Many of the specific recommendations of the FATF indicate that there is still noticeable disagreement among members over how stringent reporting efforts ought to be and how to handle the sensitive issue of branches and subsidiaries located abroad. While the U.S. has a strict reporting standard for all cash transactions over US\$10,000, the FATF only recommends that countries study the feasibility of creating such a system within their jurisdictions (Recommendation 24). Moreover, extraterritorial enforcement is precluded, despite the desirability of strengthening the ability of the financial system to detect money laundering globally, '[w]hen local applicable law and regulations prohibit this implementation, competent authorities in the country of the mother institution should be informed by the financial institutions that they cannot apply these Recommendations' (Recommendation 22).

Finally, Section D addresses the problem of strengthening international cooperation among regulatory and law enforcement authorities, including the exchange of information, cooperation in confiscation, mutual assistance and extradition, and improving asset forfeiture capabilities.

2. FATF Compliance Supervision

The FATF employs a system of mutual review in which each member's laws and efforts are scrutinized by an FATF team and then assessed by the full membership. Implementation of the Forty Recommendations by each mem-

ber is monitored through an annual self-assessment exercise, as well as a more detailed mutual evaluation process under which each member is subject to an on-site examination. In addition, the FATF carries out cross-country reviews of measures taken by its members to implement specific Recommendations.

Each member provides information for the self-assessment, which is then compiled and analyzed to evaluate the extent to which the Forty Recommendations have been implemented. Through this process, the FATF has determined that there has been a steady improvement in compliance over the past few years, with noticeable improvements, for example, in New Zealand, where major anti-money laundering legislation was adopted over the past year.³³ Turkey is the only country in the FATF that has failed to date to make money laundering a crime;³⁴ nineteen members have criminalized laundering of money beyond that gained from illicit drug trafficking. Still, as of 1996 only seventeen members had ratified the Vienna Convention, the basic international legal commitment to make money laundering a crime.

All members but one had put into place measures to facilitate mutual legal assistance in investigations. However, with respect to the freezing, seizure, and confiscation of assets pursuant to mutual legal assistance, sixteen members were deemed to be in full compliance, four were expected to be within the year, and another four were determined to be in partial compliance. While almost all members comply fully with customer identification and record-keeping recommendations of the FATF, the organization considered it a 'matter for serious concern' that Austria and Turkey still permit anonymous accounts.³⁵ All but three members require banks to look into unusually large, complex transactions; all but two require banks to develop specific programs to combat money laundering; and twenty-three members require banks to report suspicious transactions.³⁶

Monitoring is also done through mutual evaluation, in which members are examined by a select team of experts from among the FATF countries. These reports generally are not made public; they are for internal discussion only. For this reason, it is difficult to cull systematic information from the mutual evaluation process. Information was available on two of FATF's 'model members', France and Sweden. In France's case, mutual review indicated super-compliance: France regularly went beyond the text of the recommendations, by extending the definition of laundering, widening reporting requirements,³⁷ and creating a new specialized unit within the Ministry of

³³ Financial Action Task Force on Money Laundering, Annual Report, 1995-6, June 28, 1996 (hereafter FATF Annual Report).

³⁴ Interview with a Treasury Official, August 5, 1996, Washington, D.C.

³⁵ FATF Annual Report, *supra* note 33 at para. 44.

³⁶ *Ibid.*, para. 45.

³⁷ In France new rules will force all banks with a presence in France, including French branches of foreign banks, to collect detailed information on all transfers of clients' funds of above FF100,000 to other countries, similar to the U.S.\$10,000 rule in the U.S. The move is opposed in French banking circles, where concerns include confidentiality and the cost of

Justice to focus on combating money laundering. Sweden also was cited for general compliance with the Forty Recommendations, although laws relating to asset tracing and confiscation were seen as needing better enforcement.³⁸

Members can be sanctioned for making no effort to implement the Forty Recommendations. The mildest sanction is a letter from the president to the country indicating the shortcomings; the harshest sanction is expulsion. Turkey is now being sanctioned, the sole country singled out in the 1995-6 Annual Report as being seriously deficient in overall compliance. The sanctioning began with a letter from the FATF president to the relevant Turkish ministers about lack of progress in compliance. A high-level mission then met with several members of the Turkish government in April 1996, in order to encourage Turkey to expedite the enactment of its anti-money laundering bill. In the absence of any progress, the FATF Plenary likely will take more serious steps. Sanctioning is therefore a graduated system of embarrassment through peer pressure.

The FATF also encourages non-member countries to adopt its recommendations. The purpose of maintaining nonmember contacts is explicitly to encourage adoption of the Forty Recommendations and to monitor and 'reinforce' this process rather than merely to provide technical assistance.³⁹ The FATF also sanctions non-cooperative non-members. Recommendation 21 suggests that members publicize flagrantly uncooperative behavior and warn businesses and financial institutions to be careful in their business dealings in non-cooperative countries.⁴⁰ The Seychelles has recently been on the receiving end of a Recommendation 21 sanction. In February 1996, the FATF vigorously and publicly opposed provisions of the country's Economic Development Act (EDA) that guaranteed anonymity, immunity from criminal prosecution, and protection of all assets to anyone who invested more than US\$ 10 million in approved investment schemes in the Seychelles. The American FATF president, Ron Nobles, termed the EDA 'an incitement to criminals throughout the world to use the Seychelles as a clearing bank for their illegally acquired gains with full immunity'. France, the U.K., the U.S., and the British Commonwealth Secretariat all urged the Seychelles to repeal the EDA. The FATF used Recommendation 21 to warn financial institutions worldwide 'to scrutinize closely business relations' having to do with the

implementation. A. Jack, 'France Might Force Banks to Disclose Transfers', *Financial Times*, December 23, 1995, 18.

³⁸ FATF Annual Report, *supra* note 33 at para. 58.

³⁹ *Ibid.*, para. 64.

⁴⁰ Recommendation 21 reads: '[f]inancial institutions should give special attention to business relations and transactions with persons, including companies and financial institutions, from countries which do not or insufficiently apply these Recommendations. Whenever these transactions have no apparent economic or visible lawful purpose, their background and purpose should, as far as possible, be examined, the findings established in writing, and be available to help supervisors, auditors, and law enforcement agencies.' FATF, Forty Recommendations, <<http://www.oecd.org/fatf/recommendations.htm>>.

Seychelles, and called on all OECD members to 'bring all pressure to bear on the government of the Seychelles to repeal the EDA',⁴¹ so far with only limited effects.⁴²

3. Extra-FATF Sources of Pressure to Comply

The FATF is not the only international organization that is concerned with money laundering, although it is one of the most specialized and visible. A number of regional groupings also have tried to address flows of illegal money through their financial systems, with varying degrees of zeal. It is clear that the efforts of the FATF are strengthened by regional authorities which have taken money laundering seriously. Some of these have cooperated explicitly with the FATF; others have well-established mechanisms for achieving their anti-money laundering goals.

The European Community, for example, is a significant source of pressure to control money laundering, along lines very similar to those advocated by the FATF. Removal of capital controls, with the concomitant potential danger of importing criminal activity from Eastern Europe, has helped to forge a strong consensus that money laundering rules must be stringent and harmonized across the market. The E.U. Directive on the Prevention of the Use of the Financial System for the Purposes of Money Laundering (1991) applies to all credit and financial institutions, including insurance companies. The rules require the identification of customers, data recording and storage, an obligation to report suspicious transactions, and internal control mechanisms and staff training.⁴³ The rules have entailed costly adjustments, for example in Luxembourg,⁴⁴ and influenced a major 1995 overhaul of the Spanish penal code, encompassing money laundering and corruption.⁴⁵ But the most contentious case has been that of Austria, which, despite significant reforms,⁴⁶ is on a collision course with the Commission over anonymous bank accounts.

⁴¹ Quotations reported by AP, Worldstream, International News, dateline Paris, February 1, 1996; and in 'We Love the EDA' 705 *The Indian Ocean Newsletter*, February 10, 1996. Seychelles' defense of the law is reported by Litchen, M., 'Storm Rages over Proposed Seychelles Investor Legislation', *International Money Marketing*, February 16, 1996, 17.

⁴² An anti-money laundering law was passed in March 1996, but the dialog is continuing at this writing over the immunity provisions of the EDA, which is not yet in force. 'FATF Says "Wait and See"', 726 *Indian Ocean Newsletter*, July 6, 1996, 5.

⁴³ Dumbacher, *supra* note 14 at 183.

⁴⁴ Financial services account for an estimated 20% of Luxembourg's GDP, four times the proportion in most other European countries. It hosts 220 banks, almost twice as many as a decade ago. Treasury Minister Ivo Mersch lamented the loss of some of this business with the E.U. reforms: 'I've never seen private banking in the absence of confidentiality agreements. Why should we leave this business to non-European countries?' quoted by Eade, P., 'Facing Up to Harder Times', *Euromoney*, May 1996, 132-43 at 133.

⁴⁵ White, D., 'Spain Overhauls Penal Code', *Financial Times*, November 9, 1995, 3.

⁴⁶ In Austria, the 1994 Banking Act revisions had put in place a strong set of measures, including an obligation to report any 'suspicious' dealing or clients. Austria's anonymous numbered

The FATF has made efforts to work systematically with other international forums in regions around the world to secure better compliance. In Latin America, a major initiative was undertaken through the Summit of the Americas Ministerial Conference on Money Laundering, which took place in Buenos Aires in November and December 1995. Though much more limited in scope, the ministerial communiqué added weight to the FATF's external efforts by informally committing each of the thirty-four governments to enact laws to criminalize money laundering of drugs and other serious crimes,⁴⁷ to modify bank secrecy laws,⁴⁸ and to establish an ongoing assessment of the progress of each country in implementing these steps. Though limited to self-assessment, the OAS' Inter-American Drug Abuse Control Commission (CICAD) was given an important role in the monitoring process.⁴⁹

In the Caribbean, the FATF has continued to support its regional counterpart, the CFATF, rather than launch any independent initiatives. The regional group undertakes systematic self-assessment, though it has not moved to mutual assessment. Regional institutions have only begun to develop in Asia, and little has been done to tackle the problem systematically in eastern Europe and the former Soviet Union, beyond the organization of a money laundering seminar in cooperation with the countries of the Black Sea Economic Cooperation.⁵⁰

CONCLUSIONS

The convergence across national jurisdictions since 1986 has been significant but hard fought and hardly complete. Almost all industrialized countries would agree that money laundering should be considered a crime, although there is continuing disagreement on the 'precedent offensives' that produce illicit gains. Furthermore, few countries have embraced the American approach of comprehensive reporting of all cash transactions above US\$ 10,000 and extensive record keeping for all international wire transactions. Indeed, most banks have lobbied their governments hard to reject U.S.-style record keeping and reporting,⁵¹ although recent rules in France bring that

bank accounts remain (though foreigners are not allowed to use them). 'Survey of Austria', *Financial Times*, December 12, 1995, III.

⁴⁷ Summit of the Americas, Ministerial Conference Concerning the Laundering of Proceeds and Instrumentalities of Crime (Buenos Aires, Argentina, December 2, 1995), Ministerial Communiqué, para. A1.

⁴⁸ *Ibid.*, paras. C2, C9.

⁴⁹ *Ibid.*, para. F1.

⁵⁰ FATF Annual Report, *supra* note 34 at para. 81.

⁵¹ Opposition to extensive reporting schemes was common from non-U.S. international banks which criticize the vastness of the scheme and the meagerness of its payoffs: *e.g.*, international bankers have criticized the U.S. reporting system for cash transactions over U.S.\$10,000, which in 1989 resulted in about 7 million submissions to the IRS and generated virtually no evidence which led to money-laundering cases. Fullerton, *supra* note 25 at 5-7.

jurisdiction closer to the American approach. The traditional European approach of leaving it to the banks to know their customers and to report suspicious activities has found much more favor worldwide and is currently the basis of the FATF recommendations.

Tightening money laundering rules continues to meet with significant resistance in much of the financially-influential world. Outside of Japan, Singapore, and Hong Kong, money laundering is not a crime in much of Asia. Nor have these three powerful financial centers taken a leadership position on money laundering in their region. Although the United States and Australia tried to put the issue on APEC's agenda, no other APEC participant has shown any interest in contributing funds to the Asian FATF secretariat in Sydney.⁵² Cooperation in the Western Hemisphere provides an interesting contrast: here, sustained U.S. leadership during the Summit of the Americas kept the pressure on and laggards in the international spot-light. Many more central and south American countries have made money laundering a crime, and have even agreed to 'self-assessment' in their own regional grouping, the Caribbean Financial Action Task Force (CFATF).

Though non-binding, the FATF's Forty Recommendations have provided the substantive core for developing international rules with respect to anti-money laundering efforts. Among the most advanced industrialized countries, the degree of compliance has been fairly high, with a few notable exceptions. Only one country within the FATF, Turkey, has been the subject of group censure for falling far short of the standards set by the recommendations. A larger group that cannot be quantified precisely but probably amounts to some four or five members, seems likely to have failed to comply with a significant number of recommendations, while making progress in other areas. Outside of the FATF, the most progress seems to have taken place in the Western Hemisphere (Latin America and the Caribbean) where the FATF model is used to coordinate regional efforts.

The key to FATF's success seems to flow from the serious and sustained attention the organization gives to monitoring and assessment. FATF has succeeded in providing a larger and more credible pool of information regarding the fate of money laundering efforts across countries. It has also shown a spotlight on countries that do not live up to its standards. The formal consequences have been slight; violations as flagrant as those of Turkey are not punished, but have been reprimanded in formal letters from the organization's president. Bids for illicit money as indiscreet as those of the Seychelles have met with strong disapproval, though no material sanctions.

⁵² Interview with a Treasury official, Washington, D.C., August 5, 1996. In December 1995 the FATF held a conference in Tokyo to encourage Asian countries to implement similar guidelines (Japan, Hong Kong, and Singapore already belong to the Task Force) but the response was meager.

Still, it is clear that such negative publicity has been the basis for bringing national laws and rules in closer accord with those of the FATF membership.

It should be recognized that the FATF tests compliance by the extent to which national rules reflect FATF recommendations (implementation). A tougher standard yet would be the extent to which the crime of money-laundering is actually prosecuted and punished. Such a measure of compliance is still a long way off: even the most highly compliant European countries do not begin to approach U.S. rates of prosecution. Moreover, as in other cases where domestic practice parallels international norms, it remains difficult to infer significant behavioral changes based on the adoption into national law of the international standard.

The choice of a non-binding legal accord in the area of money laundering was a significant step toward harmonizing national rules to fight money laundering. The reason the FATF has given for using recommended principles for action rather than binding legal accords is straightforward: its members have diverse legal frameworks and financial systems, and so are in no position to take identical measures. Guidelines in the form of recommendations permit countries to implement them according to their particular circumstances, in contrast to mandatory detailed obligations in a binding document.⁵³ This nod to practicality is easy to understand and has likely contributed to a more influential agreement as a result. First, the use of non-binding legal accords may be the most appropriate way to deal with rapidly changing financial practices and market conditions. Like other financial issues, anti-money laundering efforts are subject to rapid changes in the appropriate 'state of the art'. It is much easier to amend non-binding recommendations, as the FATF did in 1996, than agreements that require formal ratification.

Secondly, it is less likely that mechanisms for mutual monitoring and surveillance would have been agreed to in a binding legal context. Such supervisory mechanisms have proved crucial to the FATF's effectiveness. It is hard to imagine any significant progress in this area without consistent, informed pressure for change. Thirdly, the cooperation of the financial sector and financial regulators is central to the effectiveness of this regime. It is difficult to imagine gaining the cooperation of private financiers with a binding international agreement that forces change in the way they conduct much legitimate business and alters, for many, their fundamental relationship with their clients. In most of the countries where money laundering has become a significant concern, the financial sector is an important political actor. Many have long been successful in convincing their government that what is good for the financial sector is good for the economy as a whole. Stringent legal requirements instead of non-binding recommendations would have made

⁵³ Background paper by the FATF Secretariat, *Combatting Money Laundering: The Role of the Financial Action Task Force*, para. 8. (no date; faxed to the author July 24, 1996).

international accord much less likely, especially given the close alliance in many cases between the regulatory authorities and the financial sector.

The Forty Recommendations hardly stand isolated from more formal commitments states have made to combat money laundering. The top priority of the FATF is to get a legally binding commitment from states on the broadest possible principle—that money laundering should be considered a crime, however each jurisdiction defines the 'precedent offenses' and whatever the particular technique for nabbing offenders. The first Recommendation of the FATF is that countries should sign and ratify the Vienna Convention committing them legally to this principle. Virtually every other non-binding agreement signed over the past decade has similarly called for states to make a legally binding commitment. This suggests that while the means may be flexible, a legal commitment to the most basic principle of the regime is viewed as a prerequisite to its success.