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## Recent Developments in Anti-Money Laundering and Related Litigation Traps for the Unwary in International Trust Matters

Bruce Zagaris

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# A Brave New World: Recent Developments in Anti-Money Laundering and Related Litigation Traps for the Unwary in International Trust Matters\*

Bruce Zagaris\*\*

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## I. INTRODUCTION

In 1998, governments and international organizations continued their active efforts to increase regulatory and criminal enforcement of various laws to stem the tide of transnational crime. These efforts were reflected in the criminalization of various business and financial transactions, the imposition of new due diligence measures on the private sector and the concomitant weakening of privacy and confidentiality laws, strengthened penalties for non-compliance with regulatory efforts, and new law enforcement techniques, such as undercover sting operations, wiretapping, expanded powers to search homes and businesses, and controlled deliveries. So obtrusive are many of the law enforcement techniques and the privatization of law enforcement, whereby governments transfer their responsibilities to the private sector, that many professionals engaged in international transfer of wealth counseling analogized the trends to those in Aldous Huxley's *A Brave New World* (or perhaps the Steve Miller Band's rendition).

This discussion outlines the trends in six areas and draws some practice pointers from the trends. Section II will discuss the activities of international organizations that are driving much of the strategy, framework, and minimum standards for the development of an international anti-money laundering regime. Increasingly, international organizations, both of a universal and a more regional level, are consciously trying to build alliances and networks with each other and the private sector.

In Section III, selective elements of the substantive law of anti-money laundering are considered in the context of recent developments, such as the continued erosion of secrecy and the imposition of increased due diligence requirements. Section IV discusses major case and miscellaneous developments, such as the failure of Russian offshore banks in Antigua.

Section V highlights the growth of international tax enforcement, the increased reporting requirements and unilateral extraterritorial application of the law, the increasing bilateral and multilateral cooperation, and the new traps for the wary due to tax enforcement developments.

In Section VI, international asset forfeiture trends are highlighted. These activities pose a much graver threat to the ability of clients to do business internationally than ten years ago. The goal of immobilizing the assets of transnational criminals has

become increasingly the watchword. While the rights of innocent third parties are protected in principle, it sometimes takes a lot of money and professional acumen for such persons to obtain due process.

Section VII focuses on criminal cooperation mechanisms. Section VIII discusses the use of international human rights provisions as a shield for defendants, fiduciaries, and intermediaries in the context of international anti-money laundering and financial crime cases.

As an introductory matter, the life cycle of money laundering is important to grasp. It has three cycles: (1) placement, whereby the criminal has enormous amounts of dirty money in the form usually of cash that he needs to place or initiate in a way that neither law enforcement nor the private sector will identify as the proceeds of crime; (2) layering, which involves the creation of many layers between the dirty money and the ultimately cleaned money through the use of offshore vehicles, such as trusts in secrecy jurisdictions, in tandem with multiple, entities, such as companies, and secrecy mechanisms, such as nominees, stamen, bearer shares, and sophisticated structuring; and (3) integration is achieved when the criminal has transformed the dirty money through enough layers of the laundering cycle that a legitimate banker, lawyer, or fiduciary, even one with cutting edge due diligence, would never suspect the criminal source of the money.<sup>1</sup> Integration means that, in 1999, the money of the many heirs of Joseph Kennedy, the famous former bootlegger during the prohibition days, now is not questioned. Indeed, the money even finances federal elections (e.g., of the U.S. President, Senate, and House). In Colombia, the money of the Cali cartel has been integrated for two or three decades into the leading pharmaceutical companies, soccer teams, and also the financing of political elections (e.g., the United States imposed sanctions due to the financing of Samper's election).

Much of the emphasis of the politics of international anti-money laundering is to try to deprive criminals—especially transnational criminals—and organized crime of the fruits of the crimes and the means of their committing more crimes. Another goal is to allocate the seized proceeds to governments and law enforcement. Hence, the economics and politics of anti-money laundering are to redistribute economics and power of crime. To help with the fight, governments and international organizations have solicited the collaboration of the private sector to prevent

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1. For background on cycles of money laundering, see Office of the Comptroller of the Currency, *Money Laundering: A Banker's Guide to Avoiding Problems* 3 (1993), available at <<http://www.occ.trans.gov/laundry/orig1.htm>>.

money laundering through know-your-customer and identifying and reporting to law enforcement suspicious transactions.

## II. DEVELOPMENTS OF INTERNATIONAL ORGANIZATIONS

Multilateral organizations have set the framework for anti-money laundering standards, mechanisms, and institutions.<sup>2</sup> The United Nations pioneered the 1988 Vienna Convention Against the Trafficking in Illegal Narcotic and Psychotropic Substances, which contains the requirements to criminalize money laundering and immobilize the assets of persons involved in illegal narcotics trafficking.<sup>3</sup>

In 1989, the G-7 Economic Summit Group established the Financial Action Task Force (FATF), which operates out of the Office of Economic Cooperation and Development (OECD) headquarters in Paris.<sup>4</sup> FATF has issued a set of forty recommendations (Forty Recommendations) that concern legal requirements, financial and banking controls, and external affairs.<sup>5</sup> FATF operates through a Caribbean FATF (CFATF)<sup>6</sup> and is in the process of establishing a similar group in Asia. It issues an annual report that provides an overview of progress and problems in international anti-money laundering.<sup>7</sup>

The G-10 Basle Group of Central Banks has actively provided guidelines for central bank supervisors and regulatory controls.<sup>8</sup> As mentioned below, on September 23, 1997, the Basle Group issued guidelines on supervision.<sup>9</sup>

Regionally, the Council of Europe's 1991 Convention on Laundering, Search, Seizure and Confiscation of Assets has become the major international convention that obligates

2. For background on the role of the international organizations, see Bruce Zagaris & Sheila M. Castilla, *Constructing an International Financial Enforcement Subregime: The Implementation of Anti-Money-Laundering Policy*, 29 BROOKLYN J. INT'L L. 872, 882-907 (1993).

3. *United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances*, U.N. Conference for the Adoption of a Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, 6th plen. mtg. at 182-84, U.N. Doc. E/CONF.82/15 (1988).

4. For information about FATF, see <http://www.oecd.org/fatf/about.htm> (last modified Aug. 5, 1999).

5. 40 FATF Recommendations, available in original form at <<http://www.oecd.org/fatf/about.htm>>.

6. See FINANCIAL ACTION TASK FORCE ON MONEY LAUNDERING, ANNUAL REPORT 1996-1997, at 24 [hereinafter FATF ANNUAL REPORT 1996-1997], available in original form at <<http://www.oecd.org/fatf/pdf/97ar-en.pdf>>.

7. See *FATF Reports* <<http://www.oecd.org/fatf/reports.htm>>.

8. See *infra* notes 152-57 and accompanying text.

9. See *id.*

signatory governments to cooperate against anti-money laundering from all serious crimes.<sup>10</sup>

The European Union, as a signatory to the 1988 Vienna Drug Convention and due to its own actions to combat financial crimes against the Communities, issued a 1991 Anti-Money Laundering Directive that it is poised to strengthen.<sup>11</sup> As mentioned below, it is now in the process of an initiative against cybercrimes.<sup>12</sup>

An important regional organization in the anti-money laundering has been the Inter-American Drug Abuse Control Commission (CICAD). At its meeting on November 4-7, 1997, CICAD anti-money laundering experts recommended an ongoing assessment of compliance with standards and the creation of national financial intelligence units (FIUs).<sup>13</sup> National governments and international organizations are striving to create mechanisms to monitor regularly compliance with international standards.

Because the recent FATF annual reports and topologies provide cutting-edge discussions of the status of money laundering trends, they are discussed next.

#### A. FATF 1997 Annual Report

In June 1997, the Financial Action Task Force on Money Laundering issued its annual report for 1996-97.<sup>14</sup> The report highlighted the annual survey of money laundering methods and countermeasures covering a global overview of trends and techniques.<sup>15</sup> These methods included the increased use by money launderers of non-bank financial institutions, especially bureaux de change, remittance businesses and non-financial professionals.<sup>16</sup> Special attention was devoted to the money laundering threats of new payment technologies.<sup>17</sup>

The work of the FATF in 1996-97 focused on three main areas: "(i) reviewing money laundering methods and countermeasures; (ii) monitoring the implementation of anti-money laundering measures by its members; and (iii) undertaking

10. See generally Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime, Nov. 8, 1990, Europ. T.S. No. 141.

11. See Council Directive 91/308, 1991 O.J. (L 166) 77-82.

12. See *infra* notes 158-68 and accompanying text.

13. See generally *Meeting of the Group of Experts to Control Money Laundering, October 28-30, 1997: Final Report*, OEA/Ser.L/XIV.4 (CICAD/LAVEX/doc. 12/97) (Oct. 30, 1997) [hereinafter *Final Report, 1997*].

14. FATF ANNUAL REPORT 1996-1997, *supra* note 6, at 1.

15. See *id.* at 4.

16. See *id.*

17. See *id.*



an external relations program[ ] to promote the widest possible international action against money laundering.”<sup>18</sup>

## 1. Reviewing Money Laundering Methods and Countermeasures

A significant achievement of FATF during 1996-97 was the annual survey of money laundering methods and countermeasures.<sup>19</sup> The survey provides a global overview of trends and techniques, especially the issue of money laundering through new payment technologies, such as smart cards and banking through the Internet.<sup>20</sup> FATF reviewed the issue of electronic fund transfers and examined ways to improve the appropriate level of feedback that should be provided to reporting financial institutions.<sup>21</sup>

### a. Trends in FATF Members

While drug trafficking remains the single largest source of illegal proceeds, non-drug related crime is increasingly important.<sup>22</sup> The most noticeable trend is the continuing increase in the use by money launderers of non-bank financial institutions and of non-financial businesses relative to banking institutions. The trend reflects the increased level of compliance by banks with anti-money laundering measures. The survey noted, “Outside the banking sector, the use of bureaux de change or money remittance businesses remains the most frequently cited threat.”<sup>23</sup>

FATF members have continued to expand their money laundering laws, covering non-drug related predicate offenses, improving confiscation laws, and expanding the application of their laws in the financial sector in order to apply preventive measures to non-bank financial institutions and non-financial businesses.<sup>24</sup>

FATF discussed money laundering threats that may be inherent in the new e-money technologies, of which there are three categories: stored value cards, Internet/network based systems, and hybrid systems.<sup>25</sup> Important features of the systems that will affect this threat are: (1) the value limits

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18. *Id.* at 6.  
 19. *See id.* at 7.  
 20. *See id.*  
 21. *See id.*  
 22. *See id.*  
 23. *Id.*  
 24. *See id.*  
 25. *See id.* at 8.

imposed on accounts and transactions; (2) the extent to which stored value cards become inoperable with Internet-based systems; (3) the possibility that stored value cards can transfer value between individuals; (4) the consistency of intermediaries in the new payment systems; and (5) the detail in which account and transaction records are kept.<sup>26</sup>

Future issues include the need to review regulatory regimes, the availability of adequate records, and "the difficulties in detecting and in tracking or identifying unusual patterns of financial transactions."<sup>27</sup> Since the application of new technologies to electronic payment systems is still in its infancy, law enforcement and regulators must continue to cooperate with the private sector.<sup>28</sup> Then authorities may understand the issues that must be considered and addressed as the market and technologies mature.

#### b. Policy Issues

*Electronic Fund Transfers.* As a result of difficulties in tracing illicit funds routed through the international funds transfer system, the Society for Worldwide Interbank Financial Telecommunications (SWIFT) board "issued a broadcast to its members and participating banks encouraging users to include full identifying information for originators and beneficiaries in SWIFT field tags 50 (Ordering Customer) and 59 (Beneficiary)."<sup>29</sup> Many countries have acted to encourage compliance within their financial communities with the SWIFT broadcast message.<sup>30</sup>

To strengthen the body of information on identifying the true originating parties in transfers, SWIFT has devised a new optional format (MT103) for implementation after November 1997.<sup>31</sup> The message format will have a new optional message field for inputting all data "relating to the identification of the sender and receiver (beneficiary) of the telegraphic transfer."<sup>32</sup> Additionally, "SWIFT has issued guidance to users of its current system to describe where such information may appear in the MT 100 format."<sup>33</sup> FATF has helped SWIFT devise the new mechanism and is encouraging the use of the new message format.<sup>34</sup>

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26. See *id.* at 8.

27. *Id.*

28. See *id.*

29. *Id.*

30. See *id.*

31. See *id.*

32. *Id.* at 8-9.

33. *Id.* at 9.

34. See *id.* at 8-9.

*Providing Feedback to Financial Institutions.* FATF recommends that at least the recipient of a suspicious transactions report should acknowledge receipt thereof.<sup>35</sup> If the report is then subject to a fuller investigation, the institution could be advised of either the agency that is going to investigate the report or the name of a contact officer. If a case is closed or completed, the sending institution should receive timely information on the decision or result. Further cooperative exchange of information and ideas is required for the partnership between units that receive suspicious transaction reports, general law enforcement, and the financial sector to work more effectively.<sup>36</sup>

*Estimate of Magnitude of Money Laundering.* Because of insufficient data, FATF has created an ad hoc group that "will consider the available statistical information and other information concerning the proceeds of crime and money laundering."<sup>37</sup> This ad hoc group will also "define the parameters of a study on the magnitude of money laundering and agree on a methodology and a timetable for the study."<sup>38</sup>

## 2. Monitoring the Implementation of Anti-Money Laundering Measures

As part of FATF's work, its members have pledged to monitor the implementation of its Forty Recommendations through a two-pronged approach consisting of (1) "an annual self-assessment exercise," and (2) "more detailed mutual evaluation process under which each member is subject to an onsite examination."<sup>39</sup>

As a result of Turkey's failure to implement FATF's recommendations, FATF issued a public statement, in accordance with Recommendation 21, that Turkey, a member country, was insufficiently in compliance with the Forty Recommendations.<sup>40</sup> Recommendation 21 states that "[f]inancial institutions should give special attention to business relations and transactions with persons, including companies and financial institutions, from countries that do not or insufficiently apply" the Forty Recommendations.<sup>41</sup> On November 19, 1996, Turkey enacted Law no. 4208 on the Prevention of Money Laundering.<sup>42</sup> As a

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35. See *id.* at 9.

36. See *id.*

37. *Id.*

38. *Id.*

39. *Id.* at 10.

40. See *id.* at 10-11.

41. *Id.* at 11 n.7.

42. See *id.* at 11.

result, FATF decided to lift the application of Recommendation 21.<sup>43</sup>

In 1995, after completing its first round of mutual evaluations of whether all members had adequately implemented the Forty Recommendations, a second round of mutual evaluations was conducted.<sup>44</sup> The second round focused on the effectiveness of members' anti-money laundering measures in practice. Mutual evaluations of Australia, the United Kingdom, Denmark, the United States, Austria, and Belgium occurred in 1996-97.<sup>45</sup>

*Asset Confiscation and Provisional Measures.* The FATF Secretariat conducted a study evaluating members' confiscation measures and found that an effective confiscation mechanism should encompass a range of serious offenses and should act

in appropriate cases to confiscate proceeds of crime where it is held in the name of third parties. Countries should also consider widening confiscation laws to permit confiscation without conviction in certain cases, or the more limited alternative of freezing, and where possible, confiscation action against absconders and fugitives from justice.<sup>46</sup>

For most members, the crucial issue was the burden of proof upon the government and whether it can be eased or reversed.<sup>47</sup> Countries have enacted or considered the following measures: "applying an easier standard of proof than the normal criminal standard; reversing the burden of proof and requiring the defendant to prove that his assets are legitimately acquired; and enabling courts to confiscate the proceeds of criminal activity other than the crimes of which the defendant is immediately convicted."<sup>48</sup> Further options are to provide the court with discretion to confiscate a convicted drug trafficker's assets or to require the court to order the confiscation of all assets that are disproportionate to the person's legitimate income.<sup>49</sup>

Mutual legal assistance problems include instances arising from questionable members that have ratified the relevant international conventions or do not have the necessary domestic legislation in effect.<sup>50</sup> Relatively limited mutual assistance experience exists among members in the confiscation field, and

43. See *id.*

44. See *id.*

45. See *id.* at 12-19 (setting forth the results of each nation's evaluation).

46. *Id.* at 20.

47. See *id.*

48. *Id.*

49. See *id.*

50. See *id.*

asset sharing and coordinating seizure and confiscation proceedings are still emerging.

*Customer Identification.* Because of the comparatively weaker regimes for customer identification in non-bank financial institutions and bureaux de change, these institutions have become more attractive routes for money launderers.<sup>51</sup> Refinements are required for overseas and nominee accounts. In addition, refinements are required for the structuring of large non-financial business intermediaries and situations in which no face-to-face contact between the customer and the financial institution exists. The issue of customer identification arises in the context of rapid development of electronic transactions and financial services through new technologies.<sup>52</sup>

### 3. External Relations

In external relations, FATF encourages countries to adopt and implement the FATF Recommendations and monitors and reinforces this process.<sup>53</sup> FATF also cooperates and coordinates with all the international and regional organizations concerned with counter-money laundering measures.<sup>54</sup> Finally, it pursues a flexible approach, "tailoring external relations activity to the circumstances of the region or countries involved."<sup>55</sup>

FATF will embark upon more initiatives to encourage the adoption and implementation of the Forty Recommendations. FATF is working to develop a long-term strategic plan in collaboration with other relevant international organizations.<sup>56</sup>

In 1996, FATF adopted both a policy and rules for "assessing the implementation of anti-money laundering measures in non-member governments."<sup>57</sup> The development of a mutual evaluation procedure should encourage countries and jurisdictions not only to develop anti-money laundering laws, but also to improve countermeasures already in existence. Hence, FATF has worked with other international organizations such as CFATF, the Council of Europe, and the Offshore Group of Banking Supervisors (OGBS) to develop countermeasures.<sup>58</sup>

51. See *id.* at 21.

52. See *id.*

53. See *id.* at 22.

54. See *id.*

55. *Id.*

56. To provide wider and easier access to the Recommendations, FATF has created a website at <http://www.oecd.org/fatf>.

57. FATF ANNUAL REPORT 1996-1997, *supra* note 6, at 23.

58. See *id.*

In 1996 and 1997, important counter-money laundering developments included the establishment of the Asia/Pacific Group on Money Laundering and the Southern and Eastern African Money Laundering Conference.<sup>59</sup> FATF has supported existing bodies rather than starting new initiatives. The new global project of the U.N. Drug Control Programme/U.N. Crime Prevention and Criminal Justice Division (UNDCP/UNCPCJD) on money laundering will help implement these measures through training and technical assistance.<sup>60</sup>

In the Caribbean, FATF supported the endorsement of the Memorandum of Understanding (MOU) at the 1996 Ministerial meeting of the CFATF.<sup>61</sup> CFATF finalized mutual evaluation reports of the Cayman Islands and Trinidad & Tobago, and planned six evaluation visits for 1997.<sup>62</sup> CFATF also started its typologies exercise, whereby it will "develop and share among its members the latest intelligence on money laundering and other financial crime techniques used in the Caribbean region and elsewhere."<sup>63</sup>

In April 1997, the Finance Ministers of the Asia Pacific Economic Cooperation (APEC) issued a ministerial statement welcoming the establishment of the Asia/Pacific Group on Money Laundering.<sup>64</sup> FATF stated that the endeavor required urgent funding from FATF members and those of the Asia/Pacific Group on Money Laundering.<sup>65</sup>

Finally, from October 1-3, 1996, representatives of thirteen African countries attended a conference on anti-money laundering and agreed on a proposal to establish a Southern and Eastern African Financial Action Task Force.<sup>66</sup>

### B. FATF 1998 Annual Report

In June 1998, the Financial Action Task Force on Money Laundering released its annual report for 1997-98.<sup>67</sup> The ninth round of FATF was chaired by Belgium and was marked by the elaboration of a five year plan for 1999-2004, highlighted by a decision to broaden the FATF network and the scope of its work,

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59. *See id.*

60. *See id.*

61. *See id.* at 24.

62. *See id.*

63. *Id.*

64. *See id.* at 25.

65. *See id.*

66. *See id.*

67. FINANCIAL ACTION TASK FORCE ON MONEY LAUNDERING (FATF), ANNUAL REPORT 1997-1998, available in original form at <<http://www.oecd.org/fatf/pdf/98ar-en.pdf>>.

and to strengthen the review of money laundering trends and countermeasures.<sup>68</sup>

### 1. Trends and Future Mission of FATF

The most noticeable trend is the continuing increase in the use by money launderers of non-bank financial institutions and of non-financial businesses relative to banking institutions. The trend reflects the increased level of compliance by banks with anti-money laundering measures. Outside the banking sector, the use of bureaux de change or money remittance businesses remain the most frequently cited.

In 1994, five years after the 1989 G-7 Summit established FATF, its members decided that the Task Force—which is not a permanent international organization—should continue its work for a further five years until 1999. Moreover, it was agreed in 1994 that no final decision on the future of FATF would be taken until 1997-98.<sup>69</sup>

By mid-1999, it is expected that every FATF member will have experienced two evaluations of their anti-money laundering systems.<sup>70</sup> While the first round of evaluations dealt with the issue of whether all members had adequately implemented the Forty Recommendations, the second round concerns the effectiveness of the anti-money laundering system in each member country.<sup>71</sup> FATF organized “missions and seminars in non-member countries to promote awareness of the money laundering problem” and encourage countermeasures.<sup>72</sup> Although FATF’s Forty Recommendations have gained some international recognition, a large number of countries still have not implemented anti-money laundering systems.<sup>73</sup>

FATF has succeeded in achieving an international consensus on the money laundering countermeasures, in persuading many countries to implement the measures, and in establishing a “network” of money laundering experts in each of the FATF members.<sup>74</sup> FATF has improved the flow of information both at the domestic level and internationally.<sup>75</sup>

The first major task in the future that the report outlined is “[t]o establish a world-wide anti-money laundering network and to

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68. See *id.* at 4.

69. See *id.* at 7.

70. See *id.*

71. See *id.*

72. *Id.*

73. See *id.*

74. *Id.*

75. See *id.*

spread the FATF's message to all continents and regions of the globe."<sup>76</sup> To accomplish the task, FATF will expand its membership to "strategically important countries which already have certain key anti-money laundering measures in place . . . [and] are politically determined to make a full commitment towards the implementation of the [F]orty Recommendations, and which could play a major role in their regions in the process of combating money laundering."<sup>77</sup> FATF will also develop regional bodies emulating FATF, and will cooperate closely with relevant international organizations such as the U.N. bodies and the International Financial Institutions.<sup>78</sup>

The second major task will be to improve the implementation of the Forty Recommendations in FATF members. The focus will be to "ensure that all members have implemented the revised [F]orty Recommendations in their entirety and in an effective manner."<sup>79</sup> Hence, the existing monitoring mechanisms will receive a renewed assessment focusing on the 1996 Recommendations. This assessment will involve

[a]n enhanced self-assessment process; and a third round of simplified mutual evaluations for all FATF members starting in 2001, focusing exclusively on compliance with the revised parts of the Recommendations, the areas of significant deficiencies identified in the second round, and generally the effectiveness of the countermeasures.<sup>80</sup>

The third main task will be to strengthen the review of money laundering trends and countermeasures.<sup>81</sup> Because money laundering is an evolving activity, FATF members must follow laundering trends and techniques and assess the effectiveness of the FATF recommendations. The geographical scope of the future typologies exercises must be extended. The close monitoring of trends will enable FATF to anticipate and react to the trends by elaborating countermeasures.<sup>82</sup>

## 2. Monitoring the Implementation of Anti-Money Laundering Measures

Much of FATF's work consists of monitoring the implementation by its members of the Forty Recommendations. FATF members are committed to the discipline of multilateral

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76. *Id.*  
 77. *Id.* at 8.  
 78. *See id.*  
 79. *Id.*  
 80. *Id.*  
 81. *See id.*  
 82. *See id.*



surveillance and peer review. Member countries have their implementation of the recommendations monitored through a two-pronged approach comprised of (1) "an annual self-assessment exercise," and (2) a "more mutual evaluation process under which each member is subject to an on-site examination."<sup>83</sup>

The 1997-98 self-assessment process consisted of each member providing information concerning the status of their implementation of the Forty Recommendations.<sup>84</sup> The information is then compiled and analyzed, providing the basis for assessing to what extent the Forty Recommendations have been implemented.

With respect to legal issues, all members have enacted laws criminalizing drug money laundering.<sup>85</sup> All but three FATF members have criminalized laundering of the proceeds of range of crimes in addition to drug trafficking.<sup>86</sup> The report notes that "[t]he overall level of compliance will improve considerably when Japan, Luxembourg, and Singapore have extended their drug money laundering offenses to serious crimes,"<sup>87</sup> which all three are in the process of doing.

"A number of members still must take measures in relation to confiscation and provisional measures, both domestically and pursuant to mutual legal assistance."<sup>88</sup> In regard to domestic confiscation, nineteen members are in full compliance, and six in partial compliance.<sup>89</sup> For mutual legal assistance, seventeen members are in full compliance, five in partial compliance, and three are out of compliance (Canada, Greece and the United States).<sup>90</sup> Urgent action by some FATF members is required to bring themselves into compliance with the relevant recommendations.<sup>91</sup>

Slight improvement occurred in the 1997-98 implementation of the FATF recommendations on financial issues.<sup>92</sup> Major improvements occurred in relation to two new recommendations that were introduced in 1996, namely Recommendation 13 dealing with the need to monitor laundering using new technologies, and Recommendation 25 on shell corporations.<sup>93</sup>

83. *Id.* at 9-10.

84. *See id.* at 10.

85. *See id.*

86. *See id.*

87. *Id.* at 10.

88. *Id.*

89. *See id.* at 10.

90. *See id.*

91. *See id.*

92. *See id.*

93. *See id.*

However, non-bank institutions still are not properly implementing the recommendations at the same level as the banking sector.

While nearly all FATF members “comply fully with customer identification and record-keeping requirements for banks . . . some persistent gaps in coverage with respect to certain categories of non-bank financial institutions” still exist.<sup>94</sup> Serious concerns exist regarding the anonymous passbooks for residents in Austria that FATF is pursuing through the FATF non-compliance procedures.<sup>95</sup>

The requirement for financial institutions to report suspicious transactions and related measures has received “very satisfactory” implementation in relation to banks and almost as good for non-bank financial institutions.<sup>96</sup> However, improvement is required with respect to non-bank financial institutions, especially in countries such as Canada, Iceland, and the United States.

The report also discusses the mutual evaluations of Canada, Switzerland, the Netherlands, Germany, Italy, Norway, Japan, and Greece.<sup>97</sup>

A section of the report concerning the application of the FATF policy for non-complying members covers, *inter alia*, the failure of Austria to abolish anonymous passbooks for Austria residents and a series of concerns on Canadian countermeasures.<sup>98</sup> The proposed Canadian countermeasures include mandatory suspicious transaction reporting, penalizing failures to file a report and filing a false report, as well as a “tipping-off” offense, the establishment of a new financial intelligence unit, protection from criminal and civil liability for any person or body that makes a report, and establishing a cross border reporting system for currency and monetary instruments.<sup>99</sup>

### 3. Reviewing Money Laundering Methods and Countermeasures

FATF performed a further survey of money laundering methods and countermeasures that provides a global overview of trends and techniques.<sup>100</sup> The issues of money laundering through new payments technologies—smart cards, banking through the Internet—and of the non-financial businesses and

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94. *Id.* at 11.

95. *See id.*

96. *Id.*

97. *See id.* at 12-23.

98. *See id.*

99. *See id.*

100. *See id.* at 25-28.

remittance companies were discussed.<sup>101</sup> The survey also considered the issues of how to “improve the appropriate level of feedback which should be provided to reporting financial institutions, and the continuation of work on estimating the magnitude of money laundering.”<sup>102</sup> Moreover, FATF convened a second meeting with representatives of the world’s financial sector trade institutions.

With respect to new technology—for example, e-cash—the report concluded that much work remains before all the related money laundering dangers can be clearly identified and before any possible specific countermeasures can be considered.<sup>103</sup> FATF has also directed its attention toward money laundering in sectors such as insurance or money changing.<sup>104</sup> In connection with the latter, consideration is given to the consequences of the conversion of European currencies into the Euro.<sup>105</sup>

With respect to providing feedback to financial institutions, the FATF guidelines are not mandatory because they recognize “that ongoing law enforcement investigations should not be put at risk, that secrecy laws in some countries may prevent their financial intelligence unit from disclosing significant feedback, and that general privacy laws can also limit feedback.”<sup>106</sup> Hence, the guidelines are designed to assist financial intelligence units, law enforcement and other government bodies involved in the receipt, analysis, and investigation of suspicious transaction reports, and in the provision of feedback to reporting institutions on those reports.<sup>107</sup> The guidelines suggest that at least regulatory authorities make available sanitized cases to reporting institutions, and “each case could include a description of the fact, a summary of the result, a description of the inquiries made by the FIU if appropriate, and a description of the lessons to be learn[ed] from the reporting and investigative procedures that were adopted in the case.”<sup>108</sup> Additionally, new money laundering methods, as well as trends in existing techniques, are described and identified and the guidelines provide that institutions are advised of such trends and techniques.<sup>109</sup>

The guidelines also consider means for providing general feedback, such as “annual reports, regular newsletters, videos,

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101. *See id.* at 25.

102. *Id.*

103. *See id.* at 26.

104. *See id.*

105. *See id.*

106. *Id.*

107. *See id.*

108. *Id.*

109. *See id.*

electronic information systems such as websites, electronic databases or message systems, meetings with institutions, conferences and workshops, and working or liaison groups."<sup>110</sup>

The report notes that specific feedback is more difficult to provide than general feedback due to legal and practical concerns, such as potential jeopardy to ongoing law enforcement investigations and resource limitations, and secrecy laws relating to the financial intelligence or general privacy laws.<sup>111</sup> Still, whenever possible, specific feedback should include acknowledgment by the FIU of receipt of the report and advice to the institution that a particular agency will investigate the report when this occurs and if the investigation would not be adversely affected.<sup>112</sup> "[I]f a case is closed or completed, whether because of a concluded prosecution, because the report was found to relate to a legitimate transaction or for other reasons," the institution should be notified of that decision or result.<sup>113</sup>

#### 4. FATF's External Relations and Other International Initiatives

As the third component of its mission, FATF undertakes external relations actions designed to raise awareness in non-member countries or regions on the need to prevent or combat money laundering, and offers the Forty Recommendations as a basis for doing so.<sup>114</sup>

In September 1997, FATF's external relations included a mission to Cyprus, resulting in Cyprus undergoing a joint Council of Europe/Offshore Group of Banking Supervisors (OGBS) mutual evaluation of Cyprus' money laundering system in the spring of 1998.<sup>115</sup> In October 1997, FATF helped organize a conference in St. Petersburg to complement a high-level mission to Moscow in 1996.<sup>116</sup> Various new and proposed countermeasures are in place and in the works in Russia.<sup>117</sup>

FATF-style regional bodies are active. CFATF has grown to twenty-four states and has instituted measures to ensure the effective implementation of, and compliance with, the Forty Recommendations.<sup>118</sup>

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110. *Id.* at 27.

111. *See id.*

112. *See id.*

113. *Id.*

114. *See id.* at 28.

115. *See id.* at 29.

116. *See id.*

117. *See id.*

118. *See id.* at 30.

The CFATF Secretariat monitors members' implementation of the Kingston Ministerial Declaration through the following activities: self-assessment of the implementation of the [R]ecommendations; an on-going programme of mutual evaluation of members; coordination of, and participation in, training and technical assistance programs; biannual plenary meetings for technical representatives; and annual Ministerial meetings.<sup>119</sup>

The report notes that "[s]upported by, and in collaboration with UNDCP, the CFATF Secretariat has developed a regional strategy for technical assistance and training to aid effective investigation and prosecution of money laundering and related asset forfeiture cases."<sup>120</sup> In 1997-98, three mutual evaluation reports were discussed and six on-site visits occurred. A timetable was set for the remaining mutual evaluations.<sup>121</sup>

In July 1997, the Working Party meeting of the Asia/Pacific Group on Money Laundering (APG) made progress. It currently consists of sixteen members<sup>122</sup> that "have started to exchange information and to examine the strengths and weaknesses of their systems through the mechanism of jurisdiction reports."<sup>123</sup> Measures have been proposed to improve technical assistance and training, strengthen mutual legal assistance and improve cooperation with the financial sector.<sup>124</sup>

FATF adopted a policy for assessing the implementation of anti-money laundering measures in non-member governments.<sup>125</sup> The procedure will encourage countries and territories not only to implement anti-money laundering measures, but also to improve the countermeasures already in place. In this regard,

the FATF assessed the CFATF, the Council of Europe and the OGBS's mutual evaluation procedures as being in conformity with its own principles. As the latter is comprised of representatives of banking supervisory authorities, the FATF has sought formal political endorsement of the procedures and the forty Recommendations from those governments of the members of the OGBS that are not represented in either the CFATF or the FATF.<sup>126</sup>

FATF cooperates with other international organizations. In this regard, the U.N. Office for Drug Control and Crime Prevention (UNODCCP) has started the Global Programme Against Money

119. *Id.* The Kingston Ministerial Declaration includes the Forty Recommendations.

120. *Id.*

121. *See id.*

122. *See id.* at 31.

123. *Id.* at 30.

124. *See id.*

125. *See id.* at 31.

126. *Id.*

Laundering (GPML), a research and technical cooperation program. In the context of the GPML, the UNODCCP organized several important international anti-money laundering events in 1997-1998, including awareness-raising seminars for West Africa in Ivory Coast, and for South Asian countries plus Myanmar and Thailand.<sup>127</sup> On June 8-10, 1998, the U.N. General Assembly on international narcotics trafficking adopted a political declaration in which U.N. members undertake to make special efforts against the laundering of money linked to drug trafficking. The declaration recommends that states that have not yet done so adopt by the year 2003 national anti-money laundering legislation and programs in accordance with relevant provisions of the 1988 Vienna Convention Against the Traffic in Illicit Narcotic and Psychotropic Substances, and a package of countermeasures that were adopted at the same session.<sup>128</sup>

The Commonwealth Heads of Government recently has held summits calling for concerted anti-money laundering actions. At its June 1998 London meeting, it considered four main items:

- (1) improving domestic coordination through national interdisciplinary coordinating structure;
- (2) the special problems of dealing with money laundering in countries with large parallel economies;
- (3) strengthening regional initiatives for more effective implementation of anti-money laundering measures; and
- (4) self-evaluation of progress made in implementing anti-money laundering measures in the financial sector.<sup>129</sup>

The Inter-American Development Bank has held meetings and is starting to become involved in anti-money laundering activities, such as training, supporting dialogue with the private sector, and funding programs).<sup>130</sup>

The Organization of American States (OAS)/Inter-American Drug Abuse Control Commission (CICAD) has a group of experts that meets twice a year. In May 1998, it "approved a training program for judges, prosecutors, FIU personnel and law enforcement. It also undertook to amend the model regulations to expand the predicate offence for money laundering and to provide for the establishment of national forfeiture funds."<sup>131</sup> It finished a directory of contact points to effect information exchange and mutual legal assistance that would be accessible through OAS's webpage.<sup>132</sup>

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127. See *id.* at 32.

128. See *id.* at 32.

129. *Id.* at 33.

130. See *id.*

131. *Id.*

132. See *id.*

## 5. Summary and Conclusion

The expansion of the FATF network and of the scope of its countermeasures will mean that launderers will use their power and know-how to try to take advantage of globalization and new technology, and to identify and exploit jurisdictions whose systems are vulnerable. For a five-year assessment, noticeably absent in the discussion is the use of international relations and particularly international-regime theory, including the rise and fall of linkages that make regimes rise and fall, and the targeting of key elements within such regimes. Additional limitations that exacerbate the absence of this element of its strategic planning are the temporal—its existence is limited to five years—and informal commitments—FATF is still not a formal entity. Given the threats arising from money laundering, one would think the world community would make commitments commensurate with the threats, but then progress in evolving international enforcement regimes can be slow.

During 1996-97, progress was made in combating money laundering, both within and outside the FATF membership. Implementation of the Forty Recommendations by FATF has again improved and the monitoring mechanisms have been further strengthened and refined. The international anti-money laundering activities undertaken by FATF and other international organizations have increased.<sup>133</sup>

### *C. The Egmont Group Agrees on Harmonization Measures and Cooperation Among Financial Intelligence Units*

On June 23-24, 1997, the Egmont Group, composed of specialists in financial investigation from thirty-six countries and seven international organizations, including Interpol and Europol, approved at its fifth meeting a declaration of principles to harmonize policies and intensify its efforts in combating money laundering.<sup>134</sup> The Spanish Executive Service of the Commission to Prevent Money Laundering and Financial Offenses (Servicio Ejecutivo Español de la Comisión de Prevención del Blanqueo de Capitales e Infracciones Monetarias, or Sepblac) organized the meeting at the Bank of Spain.

Among the principles agreed upon were the following: (1) the stimulation of exchanges among various FIUs; (2) the adoption of

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133. See *id.* at 34.

134. For background, see Carlos Novo, *Una Cumbre de Expertos Perfila en Madrid Estrategias Contra El Blanqueo de Dinero* [Experts Set Forth in Madrid Anti-Money Laundering Strategies], LA VANGUARDIA, July 18, 1997.

a program of communication among FIUs through the Internet; (3) the holding and development of regional workshops or seminars for their members and their units and sub-units; and (4) the study of a formal structure to maintain the continuation and consolidation of the Egmont group and the articulation of procedures for FIUs and their counterparts.<sup>135</sup>

The Egmont Group was established on June 9, 1995, at the palace of Egmont-Arenberg in Brussels as a result of an international movement directed at the promulgation in all countries of a norm pertaining to the prevention of money laundering and the establishment in each state of an organization to fulfill the obligations imposed on FIUs. The Egmont Group does not constitute an international organization or set forth hard law obligations under an international agreement, but rather provides an informal means for interested entities to meet and cooperate voluntarily.

The conclusions of the meeting indicate that Spanish norms on preventing money laundering and collaboration among credit entities, banks, and savings and loan associations, have gained momentum. Sepblac took action during 1989 on 1,530 cases on various fronts.<sup>136</sup> In the matter of international business transactions, Sepblac verified the fulfillment of requirements of enterprises owned by foreign shareholders. In so doing, it discovered the manipulation in the formation of stock exchange prices. Furthermore, Sepblac observed foreign loans that hide increases of capital in Spanish affiliate enterprises abroad.<sup>137</sup>

In the matter of money laundering, Sepblac transmitted and finalized 412 cases in 1998, 58 of which were referred to the anti-drug prosecutor, 54 to the special anti-corruption prosecutor, 10 to different judicial authorities, and 43 to police authorities.<sup>138</sup> The remaining cases were shelved without further investigation or prosecution. Sepblac also investigated, among other activities, suspicious dealings in sectors such as jewelry and precious metals, the importation of vehicles, contraband tobacco, hotel businesses, the industry of information technology and products, value added tax fraud, and casinos.<sup>139</sup>

The work of the Egmont Group and Sepblac indicate the emergence and coalescence of a financial enforcement regime, of which money laundering is an important component. The cooperation within the Egmont Group exemplifies the role of informal cooperation and its impact on the formation and growth

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135. *See id.*

136. *See id.*

137. *See id.*

138. *See id.*

139. *See id.*



of national enforcement activities. The achievement of a financial enforcement regime has occurred within the goals and activities of both formal organizations and obligations—such as the U.N. Drug Programme, the 1988 U.N. Vienna Convention Against the Traffic in Illicit Narcotic and Psychotropic Substances and the European Union, and the 1991 EU Anti-Money Laundering Directive—and informal organizations and undertakings—such as FATF and its Forty Recommendations, and the Caribbean FATF and its additional recommendations.

#### D. G-8 Group Agree on Cooperation Against Cybercrimes

On December 10, 1997, at a meeting in Washington, D.C., ministers from eight industrialized governments agreed to combat cybercrime with enhanced technology and a harmonized crime legislation.<sup>140</sup>

The arrangements to cooperate against cybercrime result from the ongoing discussions among the G-7 nations, that is, the G-7 Economic Summit countries—plus the European Union and Russia. In particular, the governments agreed to cooperate in investigations and enforcement actions involving cyber criminals.<sup>141</sup>

The G-8 countries agreed on a series of principles, such as denying a safe haven to abusers of information technology.<sup>142</sup> Just as important will be the establishment of a network and contacts to assist in investigating and arresting perpetrators of cybercrimes, including computer hackers, online peddlers of child pornography, drug traffickers, organized crime, and people who use computer networks to perpetrate illicit activities.<sup>143</sup>

The ministers agreed on the following steps:

- (1) ensuring that law enforcement is properly staffed and trained to fight cybercrime;
- (2) developing improved means to quickly trace attacks coming through computer networks; allocating the same time and resources to the prosecution of cybercriminals who have attacked other countries as would be allocated for domestic attacks, if extradition is not possible due to nationality;

140. See *"The Eight" Agree to Attack Cyber Crime Through Tough Laws, Technology*, DAILY REP. FOR EXECUTIVES, Dec. 11, 1997, at A-12.

141. See *id.*

142. See *id.*

143. In the future, "the ministers will revisit their cyber crime agenda after a group of experts makes recommendations on the matter." *Id.* A time-table has not yet been set for the report.

- (3) ensuring the preservation of electronic evidence and developing solutions for transborder searches and computer searches involving data whose location is not known to officials;
- (4) cooperating with the private sector to develop new solutions for preserving and collecting critical evidence;
- (5) accelerating the process by which traffic data from communications carriers can be obtained;
- (6) ensuring expeditious responses to mutual assistance requests, in appropriate cases, by voice, fax, or e-mail communications followed by written confirmation, if needed;
- (7) encouraging the development of international standards for reliable and secure telecommunications and data processing technologies;
- (8) using compatible forensic standards to retrieve and authenticate electronic data; and
- (9) including cybercrime issues when negotiating mutual assistance agreements or arrangements.<sup>144</sup>

A 1996 survey of the Computer Security Institute revealed that forty-two percent of Fortune 500 companies had experienced an unauthorized use of their computer systems during the last year.<sup>145</sup>

While U.S. Attorney General Janet Reno has said that the action plan does not require new legislation by the United States, wiretap laws must be adjusted to accommodate the digital era.<sup>146</sup>

All ministers promised to review their legal systems, "to ensure that [their laws] appropriately criminalize abuses of telecommunications and computer systems and promote the investigation of high crimes."<sup>147</sup>

During the week of the meeting, the vulnerability of the Internet to such crimes was emphasized when hackers broke into computers at Yahoo!, one of the most popular sites on the World Wide Web, and threatened to infect users' computers with a damaging computer virus unless an alleged hacker was released from jail.<sup>148</sup>

144. *See id.*

145. *See id.*

146. *See id.*

147. *Id.* (quoting U.S. Attorney General Janet Reno).

148. *See id.*

Many cybercrimes involve fraudulent pyramid schemes distributed by electronic mail.<sup>149</sup> Another fraud includes tricking Internet users into relinquishing passwords that can be used to access their accounts.<sup>150</sup> The G-8 agreement is an effort by national governments to enable international criminal cooperation developments to keep pace with technology and its use by transnational criminals.

E. *G-10 Basle Committee Issues Final Guide on Supervision*

On September 23, 1997, the Basle Committee on Banking Supervision, the central bank organ of the G-10 countries, agreed on a final version of supervision principles to strengthen the supervisory regime.<sup>151</sup> While the new guide contains no substantive changes, the text has gained support. For example, delegates attending the Denver Summit endorsed it.<sup>152</sup>

The Committee also obtained comments from many countries outside the group, including Chile, China, the Czech Republic, Hong Kong, Mexico, Russia, and Thailand. In addition, bankers and banking regulators from Argentina, Brazil, Hungary, India, Indonesia, South Korea, Malaysia, Poland, and Singapore contributed to the summit.<sup>153</sup>

Major financial countries have been asked to endorse the two principles by no later than October 1998. The principles "outline the basic elements of a banking supervisory system including licensing and structure, prudential regulations and requirements, methods of ongoing banking supervision, information requirements, the formal powers of supervisors and cross-border banking."<sup>154</sup> A compendium of laws accompanies the regulations that banks are requested to update on a regular basis.<sup>155</sup>

The Basle Core Principles aim to provide a basic reference with which supervisory and other public authorities worldwide may supervise all of the banks within their jurisdictions. Central banks that endorse the principles will review and update their own current supervisory arrangements in accordance with the principles.

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149. See Mark Suzman & Louise Kehoe, *G7 in Push to Combat Cybercrime*, FIN. TIMES (London), Dec. 11, 1997, at 5.

150. See *id.*

151. For background, see *Final Guide on Supervision Principles Issued in Geneva by Basle Commission*, DAILY REP. FOR EXECUTIVES, Sept. 23, 1997, at A-2.

152. See *id.*

153. See *id.*

154. *Id.*

155. See *id.*

The Committee urged national legislators to ensure that required changes in the law be enacted quickly. Since the measures outlined in the principles took one and a half years to coordinate, and since they are minimum requirements, the Committee observes that many countries may want to tighten their own rules further than the principles require.<sup>156</sup> The Committee pledged technical assistance and training for regulatory agencies from non-G-10 countries that want to take advantage of the principles.<sup>157</sup>

The continued review and strengthening of global and domestic financial supervisory mechanisms has become more urgent in a globalized world in which transnational crime and organized groups operate. Increasingly, international organizations and groups, such as the Basle Committee, the FATF, the World Bank Group, and Interpol, are exchanging information and cooperating among themselves to complement their regulatory and enforcement frameworks.

#### F. *European Union Takes Initiative Against Cybercrimes*

On April 24, 1997, members of the European Parliament (MEPs) proposed to enact legislation against certain cybercrimes, namely pornography, paedophilia, and racist material.<sup>158</sup> The measures will include establishing teams of cyberpolice to monitor the Internet, requiring industry self-regulation, and concluding international enforcement cooperation agreements. The European Union also scheduled for July 6-8, 1997 a ministerial conference on global information networks that was intended to lead to a declaration on regulatory principles.<sup>159</sup>

The MEPs will try to strike a balance between protecting the public from obscenity and respecting an individual's right to free speech and privacy. The United States, Germany and France have regulated the Internet, but with limited success.<sup>160</sup> The French and German authorities have focused on Internet service providers. For instance, Karlheinz Moewes, the chief officer of the Munich police, heads the first German force to combat Internet crime. His team of five Internet police investigated 110 cases of child pornography worldwide in 1996.<sup>161</sup> They patrol the Internet

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156. See *id.*

157. See *id.*

158. See Sandra Smith, *EU Takes Lead on Internet Porn*, EUROPEAN, May 1, 1997, at 2.

159. See *id.*

160. See *id.*

161. See *id.*

on a regular basis, searching for child pornography and trying to follow and penetrate groups of paedophiles.

In Belgium and the United Kingdom, similar law enforcement groups operate. For instance, in the United Kingdom the teams cooperate with the Internet Service Providers Association, which blocks access if illegal sites are discovered.<sup>162</sup> The difficulty is that the persons responsible for perpetrating the crimes may be outside the European Union and in remote parts of the world where law enforcement cooperation is not effective.

MEPs have called on the European Commission to propose a common framework for self-regulation and to agree on a code of good behavior.<sup>163</sup> According to EU Industrial Affairs Commissioner Martin Bangemann, the EU must introduce binding measures on service providers, with penalties.<sup>164</sup> MEPs believe that service providers must be liable for illicit material on their systems.<sup>165</sup>

In April 1997, German authorities charged the managing director of CompuServe in Bavaria with providing access to pornographic and racist material.<sup>166</sup> The situation is seen as a test case. Service providers contend that they should be treated like telecommunications companies, who are not prosecuted when criminals use their lines.<sup>167</sup>

French MEP Pierre Pradier wants to make users responsible because families can use software devices to screen criminal and harmful material.<sup>168</sup>

One problem is the classic issue of whether the law can keep up with the technology. Undoubtedly, the European Union and other major powers will need to update their laws constantly. Meanwhile, criminal organizations are likely to search for, identify, and utilize the states that intentionally or accidentally have the lowest law and regulatory regime.

*G. CICAD Experts Recommend On-Going Assessment  
of Compliance with Standards and Creation of  
National Financial Intelligence Units*

At its meeting on November 4-7, 1997 in Lima, Peru, CICAD, a branch of the OAS, made several decisions and recommendations of importance to international enforcement,

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162. *See id.*

163. *See id.*

164. *See id.*

165. *See id.*

166. *See id.*

167. *See id.*

168. *See id.*

including steps to undertake an ongoing assessment of money laundering in the hemisphere, the creation of national FIUs, and measures to strengthen the training of officials and the exchange of information and reciprocal judicial assistance.<sup>169</sup>

### 1. Creation of Financial Intelligence Units

The CIAD recommended to CICAD the amendment of the Model Regulations as follows:

In accordance with the law, each member state shall establish or designate a central agency responsible for receiving, requesting, analyzing and disseminating to the competent authorities, disclosures of information relating to financial transactions that are required to be reported pursuant to these Model Regulations or that concern suspected proceeds of crime.<sup>170</sup>

The recommendation explains that the objective is to receive and analyze information so that it can be utilized by the competent authorities.<sup>171</sup> The entities can be referred to variously as Financial Intelligence Units, Financial Investigation Units, Financial Information Units, or Financial Analysis Units.<sup>172</sup>

Depending on its location in the governmental structure of a country, FIUs may assume one of the following modes as identified by the Egmont Group: a police model; a judicial model; a mixed police and judicial model; or an administrative model.<sup>173</sup>

### 2. Ongoing Assessment of the Plan of Action of Buenos Aires

After discussing the results of responses to a questionnaire on the status of anti-money laundering regulations in twenty-one CICAD countries, the CICAD Group of Experts determined that the top two priority areas on which to focus their efforts for the immediate future would be (1) the training of officials, and (2) strengthening the exchange of information and reciprocal judicial assistance.<sup>174</sup>

Training should focus on officials who work in FIUs or in other entities—whose purpose is to receive and analyze information, investigate on the basis thereof, or both—transactions that appear to involve money laundering.<sup>175</sup> Training also is required for investigators on the applicable investigation methods and

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169. See generally *Final Report, 1997, supra* note 13.

170. *Id.* at 4-5.

171. See *id.* at 4-5.

172. See *id.* at 5.

173. See *id.*

174. See *id.* at 6-8.

175. See *id.* at 7.

techniques for money laundering offenses and on methods of presenting evidence regarding money laundering before the courts or other competent entities.

Moreover, training is required for prosecutors and judges to ensure full understanding of the offense, the importance of stringent conviction and prosecution, evidence in money laundering cases, international cooperation among judges for mutual legal assistance purposes (especially in exchanging the probative elements of the offense), the importance of seizure, confiscation pending trial, ultimate forfeiture of laundered assets and instrumentalities, and the difficulties in securing convictions.

Training also is required for officials of supervisory and regulatory agencies responsible for overseeing financial institutions. In this connection, training should be focused on the development and application of the appropriate control systems over financial institutions. It should also include training with respect to reporting systems for required cash and suspicious transaction reports, on the authority and law under which the agency operates, and on comparative approaches in other countries.

The Group of Experts will organize an informal working group for the purpose of identifying a training program based on the priority areas identified in the Group's discussion and the replies to the questionnaire.<sup>176</sup>

The Group discussed the difficulties in investigating and proving money laundering, especially due to its transnational nature that complicates, in particular, investigation and issues of proof.<sup>177</sup> These aspects require a high level of international cooperation, formal and informal, that must be efficient and effective. There must exist a reciprocal capability to seize and freeze assets as well as to provide for their confiscation when they are situated in a country other than where the investigation and trial are occurring.

The Group noted the importance of studies to facilitate the compilation, systematization, and diffusion of information on applicable national and international norms to identify the appropriate central authorities to give effect to the intended cooperation.<sup>178</sup>

For their next meeting, the Group of Experts agreed to consider the applicability of developing a manual on these matters that would set out the applicable laws and contact points

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176. *See id.* at 6.

177. *See id.*

178. *See id.* at 7.

in the various administrations in CICAD member states.<sup>179</sup> The Executive Secretariat will develop a model outline for such a manual for the next meeting of the Group. To assist in this work, CICAD members will provide an explanatory report on these measures and identify the competent authorities.

The Group of Experts agreed that a typologies exercise will become part of their ongoing agenda.<sup>180</sup> For the next meeting certain countries would prepare, on a voluntary basis, a report on their experience in detecting money laundering typologies.

### 3. Amendments to Model Regulations, Manual, and Mutual Evaluations

On May 12-14, 1998, the OAS-CICAD met and agreed to strengthen anti-money laundering enforcement efforts.<sup>181</sup> This section outlines the Commission's initiatives.

#### a. Training

The Group approved a training plan based on modules for the training of judges, prosecutors, FIU personnel, and law enforcement officials. Wherever possible, the training plan would be implemented on a sub-regional basis, following a needs assessment and diagnosis to determine the priorities of each country or region.

#### b. Amendments to the Model Regulations

To bring the model regulations approved in May 1992 in line with the broad international policy guidelines, especially those contained in the Summit of the Americas Plan of Action of Buenos Aires of 1995, the model regulations will incorporate the concept of "serious offenses," so that anti-money laundering laws and regulations are designed to counteract serious crimes rather than just drug violations.<sup>182</sup> As a result, the title of the regulations was modified to read Model Regulations Concerning Laundering Offenses Connected to Illicit Drug Trafficking, Related and Other Serious Offenses. As defined, "serious offenses" means "those defined by the legislation of each country, including, for example

179. See *id.* at 8.

180. See *id.* at 7.

181. See *Meeting of the Group of Experts to Control Money Laundering*, OEA/Ser.L/XIV.4 (CICAD/LAVEX/doc.23/98) (May 14, 1998).

182. See *Meeting of the Group of Experts to Control Money Laundering, October 26-30, 1998: Final Report*, 4, OEA/Ser.L/XIV.2.24 (CICAD/doc.990/98, rev.1) (Nov. 10, 1998) [hereinafter *Final Report, 1998*].



illegal activities that relate to organized crime, terrorism, illicit trafficking of arms, persons or body organs, corruption, fraud, extortion and kidnapping."<sup>183</sup>

Another change is that under new Article 7(d) CICAD members will "facilitate the sharing of the objects of the forfeiture or the proceeds from their sale, on a basis commensurate with participation, with the country or countries that assisted or participated in the investigation or legal proceedings that resulted in the objects being forfeited."<sup>184</sup> In addition, new Article 7(f) obligates members to "promote and facilitate the creation of a national forfeiture fund to administer the objects of forfeiture and to authorize their use or allocation to support programs for judicial management [and] training," as well as for counterdrug efforts and related programs.<sup>185</sup>

The group adopted a proposal by St. Lucia to amend Article 10, § 1(b) to broaden the definition of financial institutions to include businesses authorized to conduct "offshore" financial activities.<sup>186</sup> The group deferred until the next meeting action on proposals of St. Lucia to add collective investment funds, such as mutual funds and unit trusts, to Article 9(2).

#### c. Manual on Information Exchange for Anti-Laundering and Mutual Assistance

Consideration was given to the information page that could become a valuable tool for all countries in facilitating points of contact for information exchange and mutual legal assistance.<sup>187</sup> The pages would be accessible through CICAD's webpage and would be kept current.

The United States discussed the operation of the Egmont website system as an example of how secure information exchanges are occurring among the FIU Egmont members. Eventually, the CICAD system may be set up for secure information exchange.

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183. INTER-AMERICAN DRUG ABUSE CONTROL COMMISSION (CICAD), MODEL REGULATIONS CONCERNING LAUNDERING OFFENSES CONNECTED TO ILLICIT DRUG TRAFFICKING AND OTHER SERIOUS OFFENSES, art. 1, § 9 (as amended in 1998) [hereinafter CICAD, MODEL REGULATIONS].

184. *Id.* art. 7(d).

185. *Id.* art. 7(f).

186. *See id.* art. 10, §1(b).

187. *See Final Report, 1997, supra* note 13, at 7-8.

d. Cooperation with the CICAD Working Group on the Multilateral Evaluation Mechanism

The Group of Experts agreed that they would offer their assistance and technical capabilities to the CICAD Working Group on the Multilateral Evaluation Mechanism. The assistance would permit the experts can help with anti-money laundering evaluation, so that once the OAS members agree to undertake multilateral evaluations of the member's counterdrug policies.<sup>188</sup>

e. Permanent Council Working Group

The Group of Experts reviewed the draft resolution to the OAS General Assembly of the Permanent Council Working Group—that was established to consider the desirability of an Inter-American convention against money laundering.<sup>189</sup> The Experts will advise the working group of their own views on a convention from its technical perspective.

4. Analysis

The expansion of the anti-money laundering efforts in the Western Hemisphere to include serious crimes rather than just drug trafficking brings this group current with practice in the rest of the world. The consideration of a multilateral evaluation mechanism, the exchange of information, training, and even a convention are all efforts to strengthen compliance and indicate broader political agreement and acceptance of the purposes of anti-money laundering.

The ongoing assessment,<sup>190</sup> the establishment of FIUs, and the typologies exercise are small steps towards cooperation in hemispheric anti-money laundering enforcement. Meaningful and effective cooperation, harmonization of laws and standards, and effective establishment of an anti-money laundering regime must await the establishment of a proper network. A solid legal infrastructure with funding for professionals is needed for intensive and daily work on compliance with conventions and resolutions, harmonization of laws, collaboration on common

188. See *Final Report, 1998*, *supra* note 182, at 7.

189. See *id.*

190. Developing an ongoing evaluation or assessment of counterdrug policies and their implementation is part of a broader hemispheric initiative that was discussed at the Santiago Summit in April 1998. See, e.g., Bruce Zagaris, *U.S. Considers an Initiative on Enhanced Multilateral Drug Control Cooperation*, 13 INT'L ENFORCEMENT L. REP. 491 (1997).

approaches to mechanisms and technology, and common approaches to operational problems.

At present, the governments and international organizations in the Western Hemisphere are searching for ways to develop ad hoc solutions to individual criminal problems, such as anti-money laundering.

### III. SUBSTANTIVE LAW OF ANTI-MONEY LAUNDERING

Since the initiation of international anti-money laundering efforts in the mid-1980s, various substantive requirements have been established: the requirement to criminalize money laundering activities; the requirement that covered persons must know-their-customer; the requirement to identify and report to authorities suspicious transactions; the requirement to freeze, trace, seize, and ultimately forfeit the proceeds and instrumentalities of money laundering crimes; the requirement of covered persons to have a compliance officer and to train employees; the requirement for covered persons to have outside audits the compliance of their organization with anti-money laundering standards; and the prohibition of secrecy as a reason for a country and covered persons to refuse to follow any of the anti-money laundering obligations.<sup>191</sup>

In U.S. law, the main provisions of anti-money laundering are found in Titles 12, 18 and 31 of the U.S. Code.

The Bank Secrecy Act of 1970 (BSA)<sup>192</sup> was a precursor to anti-money laundering. It was intended to deter laundering and the use of secret foreign bank accounts. It established an investigative "paper trail" for large currency transactions by establishing regulatory reporting standards and requirements, such as the Currency Transaction Report requirement (CTR Form 4789). This requirement early distinguished the United States from other countries' approach to anti-money laundering. The BSA imposed civil and criminal penalties for noncompliance with its reporting requirements. It was designed to improved the detection and investigation of criminal, tax, and regulatory violations. A unique aspect of U.S. anti-money laundering laws that other countries are starting to emulate is the simultaneous use of anti-money laundering, tax, regulatory, and even criminal,—especially organized crime—goals.

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191. See generally CICAD, MODEL REGULATIONS, *supra*, note 183.

192. Bank Secrecy Act, Pub. L. No. 91-508, 84 Stat. 1114 (1970) (codified as amended in scattered sections of 12, 18, 131 U.S.C.).

The Money Laundering Control Act of 1986,<sup>193</sup> which was part of the Anti-Drug Abuse Act of 1986, created three new criminal offenses for money laundering activities by, through, or to a financial institution: (1) knowingly helping launder money; (2) knowingly engaging—including by being willfully blind—in a transaction of more than \$10,000 that involves property from criminal activity; and (3) structuring transactions to avoid the BSA reporting.

The Anti-Drug Abuse Act of 1988<sup>194</sup> strengthened anti-money laundering by: significantly increasing civil, criminal and forfeiture sanctions for laundering crimes and BSA violations, including forfeiture of "any property, real or personal, involved in a transaction or attempted transaction in violation of laws" relating to the filing of Currency Transaction Reports, money laundering, or structuring transactions; requiring stronger and more precise identification and recording of cash purchases of certain monetary instruments; allowing the Treasury Department to require financial institutions to file additional, geographically targeted reports; requiring the Treasury Department to negotiate bilateral international agreements covering the recording of large U.S. currency transactions and the sharing of such information; and increasing the criminal sanction for tax evasion when money from criminal activity is involved.

In 1992, the Housing and Community Development Act of 1992<sup>195</sup> made changes in anti-money laundering laws. It strengthened penalties for financial institutions violating anti-money laundering laws, and allows regulators to close or seize institutions by appointing a conservator or receiver or terminating the institution's charges. Regulators can suspend or remove institution-affiliated parties who have violated the BSA or been indicted for money laundering or criminal activity under the BSA. It forbids any individual convicted of money laundering from unauthorized participation in any federally insured institutions.

Under the Annunzio-Wylie Act, the Treasury must issue regulations requiring national banks and other depository institutions to identify which of their account holders—other than other depository institutions or regulated broker dealers—are non-bank financial institutions, such as money transmitters or check cashing services. Treasury, along with the Federal Reserve, must promulgate regulations requiring financial institutions and

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193. Money Laundering Control Act of 1986, Pub. L. No. 99-570, 100 Stat. 3207 (codified as amended in scattered sections of 12, 18, 131 U.S.C.).

194. Anti-Drug Abuse Act of 1988, Pub. L. No. 100-690, 102 Stat. 4181 (codified as amended in scattered sections U.S.C.).

195. Housing and Community Development Act of 1992, Pub. L. No. 102-550, 106 Stat. 3672 (codified as amended in scattered sections of U.S.C.).

other entities that cash checks, transmit money, or perform similar services to maintain records of domestic and international wire transfers that are useful in law enforcement investigations. Under the Act, the U.S. Government has established a BSA Advisory Group that includes representatives from the Departments of Treasury as well as Justice, and the Office of National Drug Control Policy and other interested persons and financial institutions. The group was created for the purpose of developing a harmonious private-public cooperation on anti-money laundering.

Under the Annunzio-Wylie Act,<sup>196</sup> Treasury can require financial institutions to adopt anti-money laundering programs that include: internal policies, procedures, and controls; designation of a compliance officer; and continuation of an ongoing employee training program; and an independent audit function to test the adequacy of the program.

Treasury can require any financial institution, or any financial institution employee, to report suspicious transactions relevant to possible violation of law or regulation under the protection from civil suit arising from such reports by virtue of a "safe harbor." The American Bankers' Association and the banking industry had long sought such a safe harbor.

Under the Act, a financial institution or employee may be prosecuted for "tipping off"—that is, if they disclose, to the subject of a referral or a grand jury subpoena, that a criminal referral has been filed or a grand jury investigation has been started concerning a possible crime of money laundering and BSA laws. Officers who improperly disclose information concerning a grand jury subpoena for bank records are subject to prosecution.

#### A. *The 1998 U.S. Money Laundering Act: Fostering Partnerships and Better Targeting*

Before adjourning in 1998, Congress considered and almost enacted the Money Laundering Deterrence Act of 1998.<sup>197</sup> On October 5, 1998, it passed in the House, but died in the Senate. Because it has the support of the Administration and many other people, the bill is worth considering. It would amend title 31 of the U.S. Code to improve methods for preventing financial crimes, and for other purposes. It amends Title 31 of the U.S. Code to improve methods for preventing financial crimes.<sup>198</sup>

196. Annunzio-Wylie Act Anti-Money Launder Act, Pub. L. No. 102-550, 106 Stat. 4044 (codified as amended in scattered sections of U.S.C.).

197. Money Laundering Deterrence Act of 1998, H.R. 4005, 105th Cong. (1998).

198. *See id.* § 2(b).

Section 2 notes that organized crime groups are continually devising new methods to launder money, "including the use of financial service providers that are not depository institutions, such as money transmitters and check cashing services, the purchase and resale of durable goods," and the exchange of black market foreign currency.<sup>199</sup> The involvement of international criminal enterprises engaged in money laundering is complex, diverse, and fragmented. Many foreign gangs and groups have financial management and organizational infrastructures that are highly sophisticated and difficult to track because of the globalization of the financial service industry.

Section 2 lists as the purposes of the Act to provide the law enforcement community with the necessary legal authority to combat money laundering, to broaden the law enforcement community's access to transactional information already being collected" in a non-financial trade or business, and "[t]o expedite the issuance by the Secretary of the Treasury of regulations designed to deter money laundering activities at certain types of financial institutions."<sup>200</sup>

Section 3 amends the suspicious activity reporting requirements in the Bank Secrecy Act to facilitate the flow of financial regulatory agencies.<sup>201</sup> Subsection (a) broadens the "safe harbor" provisions of 31 U.S.C. § 5318 to independent public accountants who file Suspicious Activity Reports (SAR).<sup>202</sup> It is hoped that accountants conducting audits and routine examinations of a financial institution's books and records will report wrongdoing. Subsection (b) limits the circumstances under which the filing of a SAR may be disclosed.<sup>203</sup> Subsection (c) "provides financial institutions with immunity from liability when making employment references that include suspicion of a prospective employee's possible involvement in a violation of law or regulation," unless the financial institution knows such suspicion "to be false or if the institution acts with malice or reckless disregard for the truth in making such a reference."<sup>204</sup> Subsection (d) makes SARs available to self-regulatory organizations as defined by the Securities and Exchange Act of 1934.<sup>205</sup>

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199. *Id.* § 2(a)(3).

200. *Id.* § 2(b)(1)-(3).

201. H.R. Rept. 105-611, pt. 1, at 20 (1998) (discussing the proposed Money Laundering Deterrence Act of 1998).

202. *See id.*

203. *See id.*

204. *Id.*

205. *See id.*

Section 4 expands the scope of the summons authority under 31 U.S.C. § 5318(b)(1) from merely "investigations for the purpose of civil enforcement" of the Bank Secrecy Act to "examinations to determine compliance with the Bank Secrecy Act, as well as investigations relating to reports filed pursuant to the Act."<sup>206</sup> The expanded summons authority will help in the case of non-depository institutions whose activities are not subject to regulatory oversight.

Section 5 "clarifies existing statutory language making it illegal to violate reporting requirements mandated by a geographic targeting order issued by the Secretary of the Treasury or the funds transfer record-keeping rules."<sup>207</sup>

Section 6 eliminates Treasury Secretary's obligation "to report to Congress on the status of states' adoption of uniform laws regulating money transmitters."<sup>208</sup> The Treasury Department's recently promulgated regulations for Money Services Businesses, which include money transmitters, has rendered this directive unnecessary.<sup>209</sup>

Section 7 "exempts Bank Secrecy Act reporting requirements, including those imposed by geographic targeting orders, from consideration under the Paperwork Reduction Act."<sup>210</sup>

Section 8 "transfers from the Internal Revenue Code to the Bank Secrecy Act the requirement that any person engaged in a trade or business (other than financial institutions required to report under the Bank Secrecy Act) file a report with the Federal government on cash transactions in excess of \$10,000."<sup>211</sup> Reports made pursuant to this requirement "provide law enforcement authorities with a paper trail that can help identify a lifestyle that is not commensurate with an individual's known sources of legitimate income."<sup>212</sup>

Under prior law, non-financial institutions had to report cash transactions exceeding \$10,000 to the Internal Revenue Service (IRS) on IRS Form 8300.<sup>213</sup> Because such reports must be filed pursuant to the Internal Revenue Code, Form 8300 information is considered tax return information.<sup>214</sup> As such, it

may not be disclosed to any persons or used in any manner not authorized by the Internal Revenue Code. Authorized disclosures of Form 8300 information are subject to the procedural and record-keeping requirements of Section 6103 of the Internal Revenue

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206. *Id.*  
 207. *Id.*  
 208. *Id.* at 21.  
 209. *See id.*  
 210. *Id.*  
 211. *Id.*  
 212. *Id.*  
 213. *See id.*  
 214. *See id.*

Code. For example, Section 6103(p)(4)(E) requires agencies seeking Form 8300 information to file a report with the Secretary of the Treasury that describes the procedures established and utilized by the agency for ensuring the confidentiality of the information.<sup>215</sup>

The IRS requires that agencies requesting Form 8300 information file a "Safeguard Procedures Report," which must be approved by the IRS before such information can be released.<sup>216</sup>

While the IRS uses Form 8300 to identify individuals who may be engaged in tax evasion, the information collected on the form can also be useful to other law enforcement agencies investigating other financial crimes, including money laundering. Form 8300 information can be instrumental in helping law enforcement authorities trace cash payments by drug traffickers and other criminals for luxury cars, jewelry, and other expensive merchandise. However, Form 8300s are not accessible to law enforcement authorities and, as a result of the above-mentioned restrictions under Section 6103, they cannot be retrieved electronically from a database maintained by the Treasury Department.<sup>217</sup> The change will make the reports much more accessible.

Section 9 requires that within 120 days of enactment the Treasury must promulgate know-your-customer regulations for financial institutions.<sup>218</sup> The regulations have been under discussion and study among Federal banking and financial regulatory agencies, including the Treasury Department, the Federal Reserve Board of Governors, the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation.<sup>219</sup> The regulations "are intended to assist financial institutions in verifying that their customers' funds are derived from legitimate sources."<sup>220</sup>

Section 10 extends the statute of limitations period from one to two years in forfeitable fungible property in bank accounts under 18 U.S.C. § 984.<sup>221</sup> It provides that all bank deposits are fungible and authorizes the forfeiture of money held to prove that the money in the account on one day is the "same money" as was in the account on a prior occasion.<sup>222</sup>

Section 11 requires the Treasury Secretary,

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215. *Id.*  
216. *See id.*  
217. *See id.* at 21-22.  
218. *See id.* at 22.  
219. *See id.*  
220. *Id.*  
221. *See id.* at 23.  
222. *Id.*



in consultation with "federal banking agencies" and within one year of enactment of [the law], to prepare a report on the nature and extent of private banking activities in the U.S.; regulatory efforts to monitor private banking activities and ensure that they are conducted in compliance with the Bank Secrecy Act; and policies and procedures of depository institutions that are designed to ensure that private banking activities are conducted in compliance with the Bank Secrecy Act.<sup>223</sup>

Section 12 requires the Treasury Secretary,

to prescribe regulations requiring financial institutions to maintain all accounts in such a way as to ensure that the name of an account holder and the number of the account are associated with all account activity of the account holder, and to ensure that all such information is available for purposes of account supervision and law enforcement.<sup>224</sup>

Section 13 "expresses the sense of the Congress that the Secretary of the Treasury should make available to all Federal, State and local law enforcement agencies and financial regulatory agencies the full contents of the electronic database of reports required to be filed under the Bank Secrecy Act."<sup>225</sup>

Section 14 "directs the Secretary of the Treasury, in consultation with appropriate Federal law enforcement authorities, to develop criteria . . . to identify areas outside the [United States] in which money laundering activities are concentrated, and to designate any areas so identified as foreign high intensity money laundering areas."<sup>226</sup>

Section 15 "authorizes the doubling of criminal penalties for Bank Secrecy Act violations committed with respect to a transaction involving a person in, a relationship maintained in, or transport of a monetary instrument involving a foreign country known to have been designated as a foreign high intensity money laundering area" pursuant to Section 14,<sup>227</sup> which refers to the portions of the Department of State's annual International Narcotics Strategy Control Report that identifies foreign countries that serve as safe havens for money laundering.<sup>228</sup>

### B. *Erosion of Secrecy*

For professionals involved in the international transfer of wealth techniques, financial privacy is an important principle. Fiduciaries have obligations under law—both common law and

223. *Id.*  
 224. *Id.* at 24.  
 225. *Id.*  
 226. *Id.*  
 227. *Id.* at 25.  
 228. *See id.* § 15.

statutory law in some countries—contract, and ethics to uphold confidentiality. Increasingly, in the era of globalization and since the start of the anti-money laundering regime in the mid-1980s, secrecy is sometimes overridden by obligations of banks, financial institutions, solicitors, and other covered persons to “know their customer” (or client) and identify and report suspicious transactions.

Two developments indicate the fragility and nature of exceptions to bank secrecy: the initiatives to rectify the Nazi gold losses and the intensive efforts by liquidators of a Cayman bank to recover computer bank records turned over by its former chairman and managing director to the U.S. Government.

### 1. Swiss Foreign Minister Reassures Swiss Bankers on Secrecy

One of the exceptions to bank and business secrecy has been the effort to ascertain the extent of wrongdoing and pay compensation to the victims of the Holocaust. The effort is sometimes referred to as the Nazi gold debacle. The various investigations, agreements, and lawsuits all have succeeded in overcoming bank secrecy in Switzerland and other countries, and demonstrate yet another exception to such secrecy. In this context, the Swiss Government has tried to assure its investors about its efforts to maintain legitimate secrecy.<sup>229</sup>

On September 5, 1997, Flavio Cotti, Switzerland’s foreign minister, assured Swiss bankers that the Swiss Government would not buckle to international demands to dilute Switzerland’s bank secrecy laws, one of the main factors for Switzerland’s dominance in the private banking business.<sup>230</sup> His remarks were made during the annual meeting of the Swiss Bankers Association (SBA) in Berne and were designed to reassure Swiss bankers that Swiss authorities are aware of the financial risks facing the banks in the aftermath of growing criticism of the banks’ wartime role in dealing with the accounts of Holocaust victims and looted Nazi gold.<sup>231</sup>

According to Cotti, the Swiss Government would ensure that the Swiss banking industry remains a “central pillar of the Swiss economy.”<sup>232</sup> The banking sector generates ten percent of gross domestic product, employs 108,000 people, and contributes eleven percent of tax revenues.<sup>233</sup>

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229. See William Hall, *Cotti Reassures Swiss Bankers*, FIN. TIMES (London), Sept. 6-7, 1997, at 2.

230. See *id.*

231. See *id.*

232. *Id.*

233. See *id.*

Cotti complimented Swiss bankers for helping improve Switzerland's international image and for the "extraordinary speed" with which they had prepared a "package of measures comparable to no other."<sup>234</sup> In addition, Cotti noted that the issue of "unfair tax competition" had assumed greater significance and that "Swiss banking secrecy and other laws supporting the Swiss financial centre had become frequent targets of criticism at OECD meeting."<sup>235</sup>

Cotti also discussed the role of the Swiss banking community in accepting assets of "dubious origin from heads of state."<sup>236</sup> In this connection, the Swiss Government had responded in an "active and efficient manner" in 1997 to block the Swiss bank accounts of ex-President Mobutu.<sup>237</sup> The lessons from this and other cases is that "[t]he efficiency of Switzerland's financial cent[er] attracts assets of criminal or dubious origin and it was in the deepest interests of the financial centre to keep such monies at a distance."<sup>238</sup>

Ultimately, the lifting of bank secrecy helped facilitate the agreement announced on August 12, 1998, whereby representatives of Swiss commercial banks and Holocaust survivors reached a settlement, in which the banks agreed to "pay \$1.25 billion in reparations to victims of the Nazi era, in exchange for the dismissal of three class action suits . . . and recommendations by the victims groups that the state and local authorities cancel plans to impose sanctions."<sup>239</sup>

Cotti's remarks and the lifting of bank secrecy to resolve the controversy over the claims of Holocaust victims indicate the transition that the Swiss government and private sector are undergoing with respect to bank secrecy, vetting to exclude illegitimate money, the new anti-money laundering regime concerning "know-your-customer", "identifying and reporting suspicious transactions", "criminalizing money laundering", and freezing and forfeiting illegal proceeds and the instrumentalities of the same. The transition becomes more complex when governments, international organizations, non-governmental organizations, and public opinion assess and impose moral judgments about the private sector and the government's role during World War II nearly forty years later.

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234. *Id.*

235. *Id.*

236. *Id.*

237. *Id.*

238. *Id.*

239. *Swiss Banks Reach Agreement over Holocaust Claims*, 14 INT'L ENFORCEMENT L. REP. 382-83 (1998).

## 2. U.S. Court Denies Cayman's Petition to Obtain Seized Bank Records

A case involving an effort by the Cayman Government to reclaim computer bank records obtained from a former managing director and target of a U.S. law enforcement proceeding provides a perspective of the practical limitations of bank secrecy in an increasingly shrinking world. On May 7, 1997, the U.S. District Court for the District of New Jersey issued an order denying a petition by liquidators of a Cayman bank seeking the return of its computer bank records that its former chairman and managing director had turned over to the U.S. Government.<sup>240</sup> The managing director was a target of a law enforcement proceeding when he "voluntarily" turned over the documents.<sup>241</sup> The liquidator then filed a petition for the return of property pursuant to Federal Rule of Criminal Procedure 41(e).<sup>242</sup>

On January 18, 1995, the Cayman Government appointed an interim controller to take control of the affairs of the offshore bank.<sup>243</sup> At the time, the offshore bank had approximately 1,000 clients, including corporations, trusts and individuals, some of which were U.S. residents.<sup>244</sup>

On January 24, 1994, the Cayman Government revoked the offshore bank's "category 'B' Bank & Trust company licenses" and closed the bank.<sup>245</sup> The Cayman Government also filed a petition for an order to wind-up the affairs of the offshore bank due to "serious irregularities" identified in the conduct of the offshore bank's business.<sup>246</sup> On February 10, 1995, the Grand Court of the Cayman Islands ordered the offshore bank "wound up" (liquidated).<sup>247</sup>

On June 21, 1996, a federal grand jury in Newark, New Jersey returned a multi-count indictment charging the individual defendant and others with conspiracy and money laundering.<sup>248</sup> FBI agents subsequently arrested the individual defendant.

In June 1996, the individual defendant gave the FBI a tape containing "copies of certain computer back-up tapes containing detailed financial and operating records of the [Offshore] Bank."<sup>249</sup> The individual defendant voluntarily gave the tape to

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240. See *Johnson v. United States*, 971 F. Supp. 862 (D.N.J. 1997).

241. See *id.* at 864.

242. See *id.* at 863.

243. See *id.*

244. See *id.*

245. *Id.* at 864.

246. *Id.*

247. See *id.*

248. See *id.*

249. *Id.*

the Federal Bureau of Investigation (FBI) "without the issuance of a warrant, subpoena or other compulsory process."<sup>250</sup> It remains in the possession of the U.S. Government.<sup>251</sup>

The FBI contacted the Royal Cayman Islands Police and sought assistance in its efforts to gain access to the information stored on the tape.<sup>252</sup> On August 6, 1996, Christopher Johnson, the liquidator, "filed a formal, written complaint of the 'theft' of the tape to the Cayman Police."<sup>253</sup> The petition focused on the inevitability of the eventual transfer of the tape to the IRS "for the purpose of investigating and, where appropriate, prosecuting any bank clients subject to U.S. taxation."<sup>254</sup>

The Advisory Committee's Report for Rule 41(e) of the Federal Rules Criminal Procedure provides "that an aggrieved person may seek return of property that has been unlawfully seized, and a person whose property has been lawfully seized may seek return of property when aggrieved by the [G]overnment's continued possession of it."<sup>255</sup> Moreover, Rule 41(e) allows a court to "order either the originals or copies of seized documents be returned to their owner and permit the Government access and/or use of the information."<sup>256</sup> Using four factors in entertaining a Rule 41(e) motion, the court denied the order.

The first factor is "whether the Government displayed a callous disregard for the constitutional rights of the petitioner."<sup>257</sup> The Cayman liquidator and government did not meet the test.<sup>258</sup> The *Johnson* court noted that the U.S. Government had no role in the procurement of the tape.<sup>259</sup> Instead, the individual defendant voluntarily provided the tape to the U.S. Government.<sup>260</sup> Since there was no U.S. Government involvement in the procurement of the tape, no constitutional rights were at issue in the instant case.<sup>261</sup> Thus, the *Johnson* court held that the rights afforded by the Fourth Amendment are "wholly inapplicable to a 'search or seizure, even an unreasonable one, effected by a private

250. *Id.*

251. *See id.* The tape in the possession of the U.S. Government contains "a duplicate of substantially all of the [offshore] Bank's records." *Id.* at 865.

252. *See id.*

253. *Id.*

254. *Id.*

255. *Id.* at 865-66 (quoting FED. R. CRIM. P. 41(e), Advisory Committee's Report).

256. *Id.* at 866.

257. *Id.*

258. *See id.*

259. *See id.*

260. *See id.*

261. *See id.*

individual not acting as an agent of the Government or with the participation or knowledge of any government official."<sup>262</sup>

Because the documents were voluntarily given to the U.S. Government, the latter's "use of the [t]ape in its investigation of the suspected tax evasion scheme and other suspected financial crimes connected to the [o]ffshore [b]ank and in future prosecutions will not violate the constitutional rights of the [o]ffshore [b]ank or any of its clients."<sup>263</sup>

The second factor the *Johnson* court considered was whether the petitioner had an individual interest in and need for the property he wanted returned.<sup>264</sup> The court found against the petitioner, stating that the petitioner already possessed the information contained on the tape and, hence, its return did not appear necessary for petitioner to carry on the offshore bank's business.<sup>265</sup> That the offshore bank was in liquidation and apparently would be defunct shortly invalidated the claim that petitioners did not need the tape to undertake their duties.<sup>266</sup>

The *Johnson* court found unpersuasive the speculative argument that the use of the tape may expose the offshore bank to "numerous complaints and claims" because U.S. nationals are in any event "required to reveal the existence of foreign bank accounts and report certain foreign transactions."<sup>267</sup> The reporting requirement meant that the U.S. nationals lacked a reasonable expectation of privacy in the offshore bank records.<sup>268</sup>

Upon consideration of the third factor, the *Johnson* court found that the offshore bank would not suffer "irreparable harm" if the tape was not returned, since the offshore bank's licenses have been revoked and the bank was in liquidation.<sup>269</sup>

The court also considered and rejected the fourth factor, whether the petitioners had an adequate remedy at law.<sup>270</sup> Even if the petitioner was able to establish that the bank would suffer irreparable harm, the court found that the exercise of equitable jurisdiction to forbid the Government the use of the tape was not justified.<sup>271</sup> Generally, even when the U.S. Government improperly has possession of evidence, and when the aggrieved

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262. *Id.* at 867 (quoting *United States v. Jacobsen*, 466 U.S. 109, 113-14 (1984)); see also *United States v. Kinney*, 953 F.2d 863, 865 (4th Cir. 1992).

263. *Id.* at 866-67

264. See *id.* at 866.

265. See *id.* at 867.

266. See *id.* at 868.

267. *Id.*

268. See *id.*

269. See *id.*

270. See *id.*

271. See *id.*

party's Rule 41(d) motion is successful, courts have permitted the Government to retain copies of the evidence.<sup>272</sup>

The *Johnson* court rejected the petitioners' argument that the doctrine of international comity requires the suppression of the tapes.<sup>273</sup> While comity is "the spirit of cooperation in which a domestic tribunal approaches the resolution of cases touching the laws and interests of other sovereign states," it must yield to domestic policy.<sup>274</sup> In particular, the *Johnson* court stated that no country will suffer the law of another to interfere with its own to the injury of its citizens.<sup>275</sup> Here, the court noted that the U.S. Government declared that the information on the tape constitute "significant evidence" of a "widespread tax evasion scheme" and has "initiated multiple investigations concerning suspected criminal activities by customers of the [Offshore] bank."<sup>276</sup>

The *Johnson* court rejected the arguments that disclosure of the information contained on the tape to U.S. Government agencies, such as the IRS, may expose the offshore bank to numerous complaints and claims.<sup>277</sup> The court noted that, notwithstanding the Cayman Government's claim that its Mutual Legal Assistance in Criminal Matters Treaty enabled the United States to obtain the information on the tapes from it on request, the U.S. Government is not able to obtain information on pure tax matters under the Cayman-U.S. MLAT.<sup>278</sup>

In rejecting the arguments of the petitioner under international comity, the *Johnson* court found the speculative arguments regarding harm that may result to the offshore bank and the banking industry of the Cayman Government insufficient to overcome the interest of the United States in its ongoing criminal investigation.<sup>279</sup>

The case represents a setback to Cayman secrecy and indicates the practical limitations of secrecy. Any person who relies on secrecy of one country now must factor into the equation

272. See *id.* at 869; *Ramsden v. United States*, 2 F.3d 322, 327 (9th Cir. 1993), *cert. denied*, 511 U.S. 1058 (1994).

273. See *Johnson v. United States*, 971 F. Supp. 862, 874 (D.N.J. 1997).

274. *Id.* at 870 (quoting *Société Nationale Industrielle Aérospatiale v. United States Dist. Ct.*, 482 U.S. 522, 543 n.7 (1987)).

275. See *id.* (quoting *Republic of Philippines v. Westinghouse Elec. Corp.*, 43 F.3d 65, 75 (3d Cir. 1994)).

276. *Id.* (alteration in original)

277. See *id.* at 870-74.

278. See *id.* at 870-72.

279. See *id.* at 872-73.

the limitations that may eventually eliminate the confidentiality on which it seeks to rely.<sup>280</sup>

### C. Due Diligence

Since the mid-1980s, a major component of international anti-money laundering efforts has been due diligence requirements. These requirements include: the duty to know-your-client, the duty to identify and report to authorities suspicious transactions, the requirement to appoint a compliance officer with access to the top executives of an organization, the duty to train employees on anti-money laundering, and the duty to ensure that anti-money laundering obligations are properly audited so that any violations will be detected and remedied. Increasingly, those bodies covered by due diligence include non-bank financial institutions, such as money transmitters. In addition, the requirements for bank and financial supervisors to monitor and audit continue to multiply.<sup>281</sup> On November 19, 1998, the release by the British Government of its report on financial services in the Channel Islands initiated a number of changes in due diligence to prevent and combat money laundering.<sup>282</sup>

#### 1. U.K. Edwards Report on Channel Islands Calls for Improved Due Diligence against Anti-Money Laundering

In its November 1998 report on problems in international financial services in the Channel Islands, the British Government called for reforms, many of which presage similar reforms it will demand from other offshore territories.<sup>283</sup> The so-called Edwards report—named for its author, a former top official at the British Treasury—reviews financial supervision in the Channel Islands

280. For background on the case, see *Cayman Liquidators Sue to Recover Bank Documents from U.S. Government*, 13 INT'L ENFORCEMENT L. REP. 14-15 (1997).

281. See, e.g., Proposal for a European Parliament and Council Directive amending Council Directive 91/308/EEC of 10 June 1991 on prevention of the use of the financial system for the purpose of money laundering, and the attached Explanatory Memorandum, especially Articles 3 and 6 expanding due diligence requirements for the private sector and Articles 1 and 2, requiring EU members to expand the person's covered by due diligence.

282. See George Graham and Robert Wright, UK Seeks Tighter Curbs from Offshore Tax Havens, FIN. TIMES, Nov. 20, 1998, at 1.

283. See REVIEW OF FINANCIAL REGULATION IN THE CROWN DEPENDENCIES, 1998, Cmnd. 4109 [hereinafter EDWARDS REPORT] <<http://visar.csustdn.edu/aaba/jersey.htm>>; George Graham & Robert Wright, *Move to Tighten Tax Haven Rules*, FIN. TIMES (London), Nov. 20, 1998, at 1.



(consisting of Guernsey, Jersey, and the Isle of Man) and calls on them to strengthen restrictions on offshore companies and start cooperating with foreign financial investigations.<sup>284</sup> Lord Williams, a British Home Office minister, subsequently agreed to chair a series of meetings with the three territories starting in January 1999, to follow up on the list of proposed reforms in the Edwards report.

The Edwards Report applauds the efforts of the islands, which are self-governing dependencies of the British crown, to strengthen standards in their £350 million financial industry. The report notes that one-third of investments come from U.K. residents.<sup>285</sup> However, the report contains detailed recommendations for major reforms focusing especially on the rules for establishing offshore companies and trusts used to shelter assets from tax or from outside scrutiny.<sup>286</sup> While all three islands have accepted the recommendations generally, they resist a number of specific recommendations—such as requiring companies to file audited accounts, and, in the case of the Isle of Man, vetting companies established on the island—in the hope that new measures to control company agents will solve the problem.<sup>287</sup>

The report calls on all of the islands to improve the regulation of companies and company directors.<sup>288</sup> The islands' low tax rates and relatively flexible regulatory controls have attracted large numbers of international companies. Approximately 100,000 companies are incorporated in the islands, especially in the Isle of Man.<sup>289</sup> Many more are administered from, but not incorporated in, the islands.<sup>290</sup> According to former Minister Edwards, company regulation requires tightening in all three islands.<sup>291</sup> The priority for the authorities in all three islands is to cooperate fully with other countries in the pursuit of financial crime and money laundering.<sup>292</sup>

In recent years, several high profile financial court cases have called attention to the Channel Islands' regulatory procedures. For example, in 1998 Bank Cantrade was forced to pay fines of \$3 million because one of its traders had misled investors by showing profits of \$15 million on foreign currency transactions

284. See EDWARDS REPORT, *supra* note 258.

285. See *id.* at 2.

286. See *id.* at 3-30, 135-39.

287. See *id.* at 9; see also *UK Report on Channel Islands Call for More International Tax and Anti-Money Laundering Cooperation and Presages Tougher Regime for Offshore Territories*, 15 INT'L ENFORCEMENT L. REP. 1 (1999).

288. See *id.*

289. See *id.*

290. See *id.*

291. See *id.* at 9-10.

292. See *id.* at 13-18.

when he had actually lost \$11 million.<sup>293</sup> In 1995, when the Barings merchant bank failed, "the bank's Guernsey subsidiary had lent deposits well in excess of its capital base and was technically insolvent. However, the unit was not declared insolvent while the authorities tried to find a buyer."<sup>294</sup>

According to the Edwards Report, these and other cases indicate the need for more on-site inspections of financial institutions as well as the need some kind for of reform, moratorium, or administration procedures as in the United Kingdom to assist them in dealing with insolvency.<sup>295</sup> The report also calls for a financial ombudsman to deal with customer complaints.<sup>296</sup>

The Edwards Report recommends that the Isle of Man strengthen its regulation of companies.<sup>297</sup> Thousands of companies are incorporated in the Isle of Man and thousands more are administered from Guernsey and Jersey, if not actually incorporated there.<sup>298</sup> Most of the companies are private and formed by non-residents or trusts to hold assets or interests outside the islands.<sup>299</sup> The Isle of Man has no system to vet new companies that want to register or for persons to obtain disclosure about the companies already registered.

For Guernsey, the Edwards report calls for dealing with the problem of nominee directors—the so called "Sark lark."<sup>300</sup> This phenomenon involves residents of Sark, a small island under Guernsey's jurisdictions, who sit as directors on many different company boards. While the population of Sark is only 575, the total directorships held amount to approximately 15,000.<sup>301</sup> Three residents hold between 1,600 and 3,000 directorships each.<sup>302</sup>

Guernsey has started to crack down on "false domiciles," whereby islanders were responding to phone calls for companies located elsewhere.<sup>303</sup> However, the island has resisted divesting residents of their directorships.<sup>304</sup>

293. See *Report Urges Channel Islands to Tighten Rules*, IRISH TIMES, Nov. 20, 1998, at 51.

294. *Id.*

295. EDWARDS REPORT, *supra* note 283, at 5-6.

296. See *id.* at 5, 20.

297. See *id.* at 7-10.

298. See *id.* at 9.

299. See *id.*

300. See *id.* at 82-83.

301. See *id.*

302. See *id.* at 82.

303. See *id.* at 83.

304. See Charles Piggott, *Stamping Out the Sark Lark: War Is Being Waged Against "Nominee Directors" in Tax Havens*, INDEPENDENT (London), June 27, 1999, at 6.

In general, the islands reacted positively to the Edwards report. However, bankers complained that the report's recommendations would erode client confidentiality.<sup>305</sup> The financial industry is likely to oppose and resist many of the detailed changes, including comprehensive customer compensation schemes in Jersey and Guernsey, and some changes in trust law.

The Edwards report recommends the establishment of a confidential hotline for whistle blowers, such as the person who reported improprieties in Cantrade, but was ignored by his superiors.<sup>306</sup> Jersey authorities are considering providing statutory protection for such informers.

The Jersey Bankers Associations has indicated that it favors the release of information to other authorities where the latter are investigating crimes.<sup>307</sup> However, they worry about "areas which potentially affect the fine dividing line between protecting [their] clients' confidentiality and the disclosure of information about customer affairs to authorities outside the jurisdiction of Jersey."<sup>308</sup>

The preparation and release of the Edwards report takes place in the context of the OECD Report on Harmful Tax Competition and the EU initiative towards tax harmonization and imposing minimum withholding tax, reporting requirements for the payment of interest to residents of other EU countries earned on bank deposits in the other host country, or both.<sup>309</sup> In fact, the United Kingdom's membership in the European Union has been a contributing element in its own initiatives to strengthen international financial supervision in its dependent and overseas territories.<sup>310</sup>

The Edwards report takes a balanced approach of acknowledging and applauding the comparatively favorable financial supervisory standards in the three islands, considering the dependence of each of the islands on international financial business.<sup>311</sup> The recommendations recognize the need to help the international financial services sector evolve rather than trying to destroy them. The pragmatic approach to improving financial supervisory standards is prudent, especially given the

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305. Brian Groom, *Regulators Jubilant as Critics are 'Routed'*, FIN. TIMES (London), Nov. 20, 1998, at 10.

306. See EDWARDS REPORT, *supra* note 283, at 8.

307. See Groom, *supra* note 305, at 10.

308. *Id.*

309. See Jim Kelly, *EU Puts Future of 'Unfair' Havens in Question*, FIN. TIMES (London), Nov. 20, 1998, at 10.

310. See EDWARDS REPORT, *supra* note 283, at 4, 115.

311. *Offshore Verdict*, FIN. TIMES (London), Nov. 20, 1998, at 25.

positive attitude of the three jurisdictions to cooperate in the implementation of the recommendations. Regulators and professionals in jurisdictions in which international financial services are an important part of the economy will recognize that many recommendations of the Edwards report will be adopted by international organizations active in the relevant subject matter areas.

## 2. The Proposed U.S. Know-Your-Customer Rule Will Formalize Internal Control Procedures

### a. The Proposed Regulations

The proposed know-your-customer regulation contained in the Board of Governors of the Federal Reserve System's memorandum dated September 28, 1998, requires banks to develop for the first time their know-your-customer program, and continues to generate discussion.<sup>312</sup> The proposed rule will also apply eventually to non-bank financial institutions and will have broad implications for private banking, offshore accounts, and the imposition of responsibility on covered persons to design, implement, and regularly update and adjust their know-your-customer internal control systems.<sup>313</sup>

The proposed regulation will require institutions supervised by the Federal Reserve Board to develop and implement a know-your-customer program.<sup>314</sup> According to the proposal, the establishment of a know-your-customer program is designed to

protect the reputation of the bank; facilitate the bank's compliance with all applicable statutes and regulations (including the Bank Secrecy Act and the Board's suspicious activity reporting regulations) and with safe and sound banking practices; and protect the bank from becoming a vehicle for or a victim of illegal activities perpetrated by its customers.<sup>315</sup>

Because the Board recognized that banks vary considerably in the way in which they conduct their business, the proposal permits each bank to develop its own know-your-customer program as a system designed to meet the goals of the

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312. For background, see Bruce Zagaris, *U.S. Federal Reserve Will Issue New "Know Your Customer" Regulations*, 14 INT'L ENFORCEMENT L. REP. 445 (1998); see also *Know Your Customer*, 63 Fed. Reg. 67,516 (1998) (to be codified at 12 C.F.R. pts. 208, 211, & 225) (proposed Dec. 7, 1998) (withdrawn 64 Fed. Reg. 15310, Mar. 31, 1999).

313. See *Know Your Customer*, 63 Fed. Reg. at 67,517.

314. See *id.*

315. *Id.* at 67,518.

proposal.<sup>316</sup> The proposed Federal Register notice will require banks to develop a know-your-customer program that at least will provide a system for handling the following tasks:

- (1) determining the true identities of the bank's customers;
- (2) determining the customer's sources of funds for transactions involving the bank, including the types of instruments used and the sources from which the funds were derived or generated;
- (3) determining the specific customer's normal and expected transactions involving the bank;
- (4) monitoring customer transactions to ascertain if such transactions are consistent with normal and expected transactions for that particular customer or for customers in the same or similar categories or classes, as established by the bank;
- (5) identifying customer transactions that do not appear to be consistent with "normal and expected transactions for that specific customer or for customers in the same or similar categories or classes, as established by the bank"; and
- (6) ascertaining if a transaction is unusual or suspicious, in accordance with the Board's suspicious activity reporting regulations, and reporting it accordingly.<sup>317</sup>

The proposal permits each bank to decide how best, consistent with its own business practices, it can identify its customers, understand the normal and expected transactions of its customers, and then monitor on an ongoing basis the transactions of its customers. Under the proposal, a bank must decide the know-your-customer program suited to its specific needs, delineate the program in writing, and demonstrate that it is complying with the program.<sup>318</sup> The proposal will require banks to understand to whom they are providing their services at the start of the relationship, to develop an understanding of the transactions the customers will be conducting, and then to monitor the transactions of those customers.<sup>319</sup>

Some banks, especially those offering private banking services, have raised concerns about identifying their clients, especially since a main tenet of such services is the confidentiality

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316. *See id.*

317. *See id.* at 67,523.

318. *See id.*

319. *See id.*

offered and demanded by these customers through the use of intermediary entities, such as private investment companies, trusts, private mutual funds, or investment advisory accounts, and since these entities are often based at offshore locations. The Federal Reserve is convinced that the beneficial owner's identity is usually well known to bank personnel or that banks can obtain waivers from their customers for any perceived restriction of the release of beneficial owner information. In this regard, the Federal Deposit Insurance Corporation (FDIC) seeks comments on whether any actual or perceived invasion of personal privacy interest is outweighed by the compliance benefit.<sup>320</sup>

While the proposal's requirement of identifying the true beneficial owner of each account of the bank is not intended to force a bank to disclose information in violation of foreign law, allowing any bank to avoid identification of beneficial ownership of any account would defeat the main purpose of the proposed rule—to ensure that each bank knows to whom it is offering its service. In this connection, the proposed rule responds to the criticism of a recent General Accounting Office (GAO) report that U.S. banks lacked sufficient documentation regarding the beneficial owners of offshore entities that maintained accounts in the United States.<sup>321</sup>

In response to concerns raised by several banks as to the severe hardship and cost of the new monitoring requirements, the Board of Governors has emphasized that the regulation will offer flexibility and require banks to develop and implement effective monitoring systems, commensurate with the risks presented by the types of accounts maintained at the bank and the types of transactions conducted through those accounts.<sup>322</sup> The effectiveness of the monitoring system of a bank's know-your-customer program will be based on that particular bank's ability to monitor transactions consistent with the volume and types of transactions conducted at the bank.<sup>323</sup> The FDIC is seeking comment on whether the benefits of implementing the know-your-customer requirements outweigh the costs involved and whether there should be a minimum account size threshold below which the requirements should be waived.

The design of a monitoring system should correspond to the risk associated with the types of accounts maintained and types of transactions conducted through those accounts. Hence, the design of such a system

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320. See *id.* at 67,529-30.

321. See UNITED STATES GENERAL ACCOUNTING OFFICE, MONEY LAUNDERING: REGULATORY OVERSIGHT OF OFFSHORE PRIVATE BANKING ACTIVITIES, 7-9 (June 1998).

322. See Know Your Customer, 63 Fed. Reg. at 67,517.

323. See *id.* at 67,521.

could involve the classification of accounts into various categories based on such factors as the type of account, the types of transactions conducted in the various types of accounts, the size of the account, the number and size of transactions conducted through the account, and the risk of illicit activity associated with the type of account and the transactions conducted through the account.<sup>324</sup>

For certain categories of accounts, it may be sufficient for an effective monitoring system to establish parameters for which the transactions within these accounts will normally occur. Instead of monitoring each transaction, an effective monitoring system may involve monitoring only for those transactions that exceed the established parameters for that particular category of accounts.<sup>325</sup>

The proposed know-your-customer rule asks for the public to provide input on specific questions.<sup>326</sup> The Federal Reserve wants comments to focus on the proposed definition of "customer" to ensure, at a minimum, that the definition is not overly broad and adequately covers "beneficial" ownership-related issues. Respondents are asked whether the proposal creates an uneven playing field for non-bank financial institutions, such as money transmitters and broker-dealers.<sup>327</sup>

The proposed rule arises out of the Congressional hearings that have produced the enactment of the Money Laundering Deterrence Act of 1998, which requires that the Secretary of the Treasury implement know-your-customer regulations within 120 days of passage of the legislation.<sup>328</sup> Congressman Leach's staff informed the Federal Reserve that the primary reasons for the provision in the draft legislation is to ensure that legal enforceable regulations exist to require that financial institutions adopt know-your-customer procedures and that similar regulations are developed for the non-bank financial sector, including broker-dealers and money transmitters. The Federal Reserve will continue to work with FinCEN and will start to coordinate with the staff of the SEC in helping program such rules for non-bank financial institutions.

The Federal Reserve is awaiting feedback from other regulatory agencies, especially the Office of the Comptroller of the Currency (OCC) and the Office of the Thrift Supervision (OTS), before submitting the proposal to the Federal Register. It is also awaiting input from the Board of Directors of the FDIC on

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324. *Id.* at 67,521.

325. *See id.*

326. *See id.* at 67,522.

327. *See id.*

328. *See Zagaris, supra* note 312, at 446.

whether know-your-customer standards should be issued as regulations or guidelines.

The Federal Reserve believes that the proposed know-your-customer rule will enable financial institutions to obtain information from their customers regarding the identity, the types of transactions to be conducted, and the source of funds, among other things.<sup>329</sup> Obtaining and reviewing such information will assist financial institutions in making a risk-based determination on various matters—including the extent of identifying necessary information and the amount of monitoring required—by permitting institutions to categorize their customers into different groups based on the types of services being requested and the magnitude and extent of the transactions being conducted.<sup>330</sup> Effective know-your-customer programs will require that banking organizations develop “customer profiles” to understand their customers’ intended relationships with the institution and, thereafter, to determine realistically when customers conduct suspicious or potentially illegal transactions.<sup>331</sup>

Legally, the Federal Reserve’s proposal will revise 12 C.F.R. pts. 208, 211, and 225 by requiring state member banks, certain bank holding companies and their non-bank subsidiaries, U.S. branches and agencies and other offices of foreign banks, and Edge and Agreement corporations to develop and implement a know-your-customer program within their institutions.<sup>332</sup>

The proposed rules define “customer” as “the person or entity who has an account involving the receipt or disbursal of funds at a bank and any other person or entity on behalf of whom such an account is maintained.”<sup>333</sup> The term encompasses direct and indirect beneficiaries of the account when the activity in the account involves the receipt or disbursal of funds.<sup>334</sup> “It also includes a person or entity who owns or is represented by the customer.”<sup>335</sup> Hence, a customer would include an account holder, a beneficial owner of an account, or a borrower. A customer could also include “the beneficiary of a trust, an investment fund, a pension fund or company whose assets are managed by an asset manager, a controlling shareholder of a closely held corporation or the grantor of a trust established in an offshore jurisdiction.”<sup>336</sup>

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329. See Know Your Customer, 63 Fed. Reg. at 67,516-17.

330. See *id.* at 67,517.

331. See *id.*

332. See *id.*

333. *Id.* at 67,518.

334. See *id.*

335. *Id.*

336. *Id.*



The proposed rule underscores the need to target private banking operations, since these customers utilize such account vehicles as personal investment companies (PICs), trusts, personal mutual investment funds, or are clients of financial advisors.<sup>337</sup> Such accounts help protect the legitimate confidentiality and financial privacy of the customers that use such accounts. However, the need to identify properly the beneficial owners of such accounts, through an effective know-your-customer program, is required to continue safe and sound operation of the bank. Hence, know-your-customer procedures for identifying the beneficial owners of private bank accounts should be no different than the procedures for identifying other customers of the bank. By developing special protections to limit access to information that would generally reveal the beneficial owners of these accounts, a private bank can address any needed confidentiality.<sup>338</sup>

Once the proposed rule is published in the Federal Register, the public will have sixty days from that date to comment on the rule.<sup>339</sup> The final rule may take effect at the start of the year 2000. Once the rule becomes final, the Federal Reserve will allow covered financial institutions a six-month grace period to fully implement know-your-customer programs, after which time bank examiners may bring disciplinary action against institutions that violate the rules.

During the annual American Bankers Association/American Bar Association conference on money laundering, Susan Tucillo, Vice-President and Senior Compliance Officer of Citibank, N.A., noted that the know-your-customer rules will generate a substantial amount of new employment because of the complexity of issues raised, thereby requiring "a fundamental retooling of the branch operation process."<sup>340</sup> The proposed rules cover virtually every product line and will particularly cause problems for attorney trust accounts, escrow accounts, other high-turnover attorney accounts, letters of credit, and other banking and lending transactions.<sup>341</sup>

The know-your-customer rule would require that banks ensure that all documentation on accounts domiciled in the

337. See *id.* at 67,520. The issuance by the Federal Reserve of Guidance on Private Banking presaged the proposed rule. For a summary of the guidance and its implications, see generally *Federal Reserve Guidance on Private Banking Requires New Due Diligence from Banks*, 13 INT'L ENFORCEMENT L. REP. 391 (1997).

338. See *Know Your Customer*, 63 Fed. Reg. at 67,520.

339. See *id.* at 67,516.

340. S. Ali Sartipzadeh, "Know Your Customer" Proposed Rules Provoke Criticism, *Complaints from Banks*, DAILY REP. FOR EXEC., Nov. 4, 1998, at A-13.

341. See *id.*

United States. be made available to Federal Reserve examiners within forty-eight hours of a request.<sup>342</sup> U.S. banks are concerned that these rules will limit their ability to do business in offshore jurisdictions where they compete with foreign banks from jurisdictions with less restrictive know-your-customer rules.<sup>343</sup>

An important issue raised is the definition of customer.<sup>344</sup> The preamble explains that "customer" includes "direct and indirect beneficiaries" of the account, as well as "a person or entity who owns or is represented by the customer." The proposed regulation specifically the beneficial owners of PICs, trusts and "personal mutual investment funds," clients of financial advisors, and "borrowers."<sup>345</sup> The Federal Reserve and FDIC maintain a customer also could include the beneficiary of an investment fund, a pension fund, a company whose assets are managed by an asset manager, or a controlling shareholder of a closely-held corporation.<sup>346</sup> The regulations and preambles are conspicuously silent on what a customer does not include, for example, shareholders of publicly-traded corporations or of widely-held non-publicly traded businesses. Further, the regulators state that in some cases persons with the know-your-customer obligation might need to obtain information about the controlling owners of a business or other legal entity.<sup>347</sup> Hence, the definition of customer may have significant impact on many fiduciaries. In this connection, the Federal Reserve and FDIC are seeking comments on whether the proposed definition of "customer" is adequate to include all persons who "benefit from the transactions conducted at the bank, such as persons who establish off-shore shell companies . . . or otherwise conduct business through intermediaries."<sup>348</sup> In addition, they seek comments on whether the proposed definition of customer is too wide and will unnecessarily include persons that pose minimal know-your-customer risk, that is, whether additional regulatory exceptions are appropriate.<sup>349</sup>

At present, the proposed regulations do not have exceptions for foreign banks, foreign broker-dealers, or foreign investment

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342. See Know Your Customer, 63 Fed. Reg. at 67,521-22.

343. See *KYC Rule Will Give Enforcement Agents New Information Sources*, 10 MONEY LAUNDERING ALERT 9 (1998).

344. For the proposed regulation's definition of "customer," see *supra* notes 323-25 and accompanying text.

345. *Id.* at 67,520.

346. See *id.* at 67,518.

347. See GIBSON, DUNN & CRUTCHER, LLP, *Official Notices of Proposed "Know Your Customer" Regulations for Banks* (Jan. 7, 1999), available at <<http://www.gibsondunninstitute.com/docs/FinInst/fimema01.htm>>.

348. Know Your Customer, 63 Fed. Reg. at 67,522.

349. See *id.*

advisors that are regulated in their home countries or in certain home countries that have sufficient anti-money laundering countries. Similarly, no exceptions exist for foreign open-ended collective investment funds such as mutual funds, which may have thousands of investors. However, the regulators would expect banks to identify the shareholders of a mutual fund established in an offshore jurisdiction that has a limited number of shareholders.<sup>350</sup> In the case of accounts opened by mail or Internet, banks and other covered persons must give special attention to verifying addresses and telephone numbers, and to use commercially available data sources to verify the customer's date of birth and social security number.<sup>351</sup>

The regulations require the bank to identify the beneficial owners of account holders that are offshore private investment companies, trusts, "private mutual funds," or investment advisors—in other words, high-risk customers—and to maintain data about the beneficial owner to the same extent as for U.S. persons.<sup>352</sup> In the event that banks maintain the documentation about the identity of foreign beneficial owners, such as customers of a foreign investment advisor or the principal of a personal investment company outside the United States in a foreign branch or holding company, regulators would require that the bank furnish the documentation to a bank examiner in the United States within forty-eight hours of the examiner's request.<sup>353</sup> No exceptions exist if bank secrecy or other law, such as the EU privacy directive, would preclude providing the documentation in the United States, especially with respect to existing customers.<sup>354</sup>

#### b. Opposition from Private Sector and Congress

On February 3, 1999, a dozen members of Congress introduced four pieces of legislation:

- (1) H.R. 220- Freedom and Privacy Restoration Act of 1999 to prohibit the federal government from creating a national ID and medical ID by repealing sections of the laws passed in 1996 and would prohibit the use of social security numbers as an identifier.

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350. *See id.* at 67,520.

351. *See id.* at 67,519.

352. *See id.* at 67,520.

353. *See id.* at 67,521-22.

354. *See id.*

- (2) H.R. 516- Know-Your-Customer Sunset Act of 1999 would bar agencies from following through on proposed Know-Your-Customer regulations.
- (3) H.R. 518- Bank Secrecy Sunset Act would repeal the law that gives federal bank regulators monitoring authority and devolves the power to the states unless Congress passes a better version of the law.
- (4) HR 517- FinCEN Public Accountability Act of 1999 would let bank customers check their own files and challenge information they believe to be false or inaccurate.

On March 4, 1999, Comptroller of the Currency John D. Hawke, Jr. testified that federal banking regulators' proposed know-your-customer rules should be withdrawn at the end of the public comment period.<sup>355</sup> Hawke said any marginal advantages for law enforcement would be strongly outweighed by its potential for inflicting lasting damage on the banking system.

Christie Sciacca, associate director of FDIC's division of supervisor, also testified that his agency believes the "proposal cannot become final in its current form, if at all."<sup>356</sup> Sciacca explained that most comments from the banking industry involved concerns about "the cost of compliance, customer privacy, and the competitive disadvantage if all financial institutions are not subject to the same requirements."<sup>357</sup>

At present, the status of the know-your-customer regulations are uncertain and controversial.

### 3. International Standards for Accounting in Anti-Money Laundering Campaigns

An important development is the establishment of international standards for accounting in anti-money laundering and financial crimes.<sup>358</sup> The goals of accounting, as defined by the American Accounting Association, are to make decisions on the use of limited resources, including crucial decision areas, determine goals and objectives, direct and control effectively an organization's human and material resources, maintain and

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355. See Eileen Canning, *Know-Your-Customer Proposed Rules Should Be Scrapped*, *OCC's Hawke Urges*, DAILY REP. FOR EXEC., Mar. 5, 1999, at A-35, col. 1.

356. *Id.*

357. *Id.*

358. See Charles Klingman, *Accounting for Money Laundering: International Perspectives* (Jan. 7, 1998) (e-mail note, on file with author).

report on the custodianship of resources, and facilitate social functions and controls.<sup>359</sup>

Auditing encompasses the following three major categories: (1) financial statement audit; (2) operational audit; and (3) compliance audit.<sup>360</sup> In particular, a compliance audit has as its principal goal determining whether the entity under audit is following procedures or rules established by a higher authority.

Both accounting and auditing include within themselves certain fundamental notions on conformity with, and obedience to, applicable legal authority. These basic concepts involve the intersection of accounting and money laundering.

In every jurisdiction, accountancy contains long-standing and deeply rooted requirements of impartiality, objectivity, and accuracy, using uniform standards and principles, and a code of mandatory professional ethics to support those obligations. These obligations entrust accountants with the responsibility for determining whether financial statements are free from material misstatements, and for auditing internal controls and procedures relevant to the production of those internal controls. The "core competence" of accountancy in the area of internal controls and the accountant's obligations for impartiality, objectivity, and accuracy have led many countries to rely on accountancy in detecting and preventing money laundering and financial crimes such as fraud.<sup>361</sup>

Training provides accountants with the requisite professional tools and expertise to enable them to compare different entities within a single industry and thereby detect certain anomalies. Accountancy emphasizes operational knowledge of industries audited and appropriate internal controls, applied to a particular industry. A growing requirement in accounting jurisdictions to combat financial crimes requires accountants to report discoveries of serious abnormalities to higher authorities in appropriate circumstances.

Worldwide accounting organizations have begun to give guidance to their accounting professionals concerning money laundering issues.<sup>362</sup> However, little or no international coordination has occurred, despite accountancy's overall global harmonization and increasing emphasis on international accounting standards.

The Basle Committee on Banking Supervision of the Bank for International Settlements has issued its Core Principles for

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359. *See id.*

360. *See id.*

361. *See id.*

362. *See id.*

Effective Banking Supervision. In particular, Principle 15 states that “[b]anking supervisors must determine that banks have adequate policies, practices and procedures in place, including strict ‘know-your-customer’ rules, that promote high ethical and professional standards in the financial sector and prevent the bank being used, intentionally or unintentionally, by criminal elements.”<sup>363</sup> In addition, Principle 14 provides that bank supervisors must ensure that banks employ “appropriate independent internal or external audit and compliance functions to test adherence to” policies, procedures, practices and legal requirements, which include know-your-customer and anti-money laundering rules.<sup>364</sup>

In the United States, the Bank Secrecy Act Advisory Group has established a sub-group, in coordination with appropriate accounting organizations and headed by an industry expert, to explore appropriate guidelines within the United States concerning money laundering.<sup>365</sup> The group will explore issues and develop guidelines or suggestions on how to effectively provide useful guidance to the U.S. accounting profession on money laundering.

Accounting bodies and researchers working on money laundering problems have concentrated on six important issues: (1) legal issues; (2) auditing issues; (3) internal controls; (4) reporting obligations; (5) effect on financial statement presentation; and (6) enforcement activity.

With respect to legal issues, all jurisdictions whose accounting bodies have worked on accounting guidance concerning money laundering have provided an explanation in layman’s terms of appropriate legal issues that an accounting professional is likely to encounter.

For auditing issues, many accounting jurisdictions have issued a checklist of significant indicators accounting professionals can apply to potential money laundering concerns.<sup>366</sup> Such guidance assists accountants in effectively performing their duties. Clear, specific guidance on standards within an audit of potential money laundering are critical to the accounting profession. While the technical specifics of accounting standards may differ throughout the world, the indicators of potential money laundering often do not. Use of harmonized checklists and indicators are important since money laundering is

363. BANK FOR INTERNATIONAL SETTLEMENTS: BASLE COMMITTEE ON BANKING SUPERVISION, *Core Principles for Effective Banking Supervision* 36 (Sept. 22, 1997) available at <<http://www.bis.org/press/index/htm>>.

364. *Id.*

365. See Klingman, *supra* note 353.

366. See *id.*

often transnational; prevention and investigation thus may require cooperation between accounting professionals in various jurisdictions.

Comprehensive internal risk control assessment is critical to application of auditing standards. The Swiss and U.S. professionals have provided effective models for internal risk assessment with respect to money laundering.<sup>367</sup>

Various jurisdictions have provided guidance as to the obligations of an accounting profession when potential money laundering is discovered. The guidance is divided between legal requirements and ethical obligations to report. While accounting professionals have ethical obligations of confidentiality toward clients, exceptions apply with respect to reporting crimes, such as money laundering.

With respect to the effect on financial statement presentation, several jurisdictions have discussed such effect after discovery of potential money laundering. The questions concern whether, and to what extent, an accounting professional must report to the audited entity the discovery of potential money laundering in the financial statements. Conflicts may exist between ethical and legal obligations of accounting professionals to disclose fully and impartially all relevant or material information in a financial statement on the one hand, and legal restrictions on the notification to unauthorized personnel of potential money laundering on the other.

Enforcement of accounting standards in money laundering is largely self-regulatory and authorizes a self-regulatory body to impose sanctions. One accounting jurisdiction has already imposed sanctions on a member based on money laundering and in the absence of any legal sanctions against that member. The accounting professional can play a critical role in preventing money laundering, especially in the development and application of internal controls and the assessment of risks. International cooperation is critical to effectively combating money laundering.<sup>368</sup>

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367. *See id.*

368. Until now, the countries known to have provided or to be in the process of providing guidance specifically intended for the accounting professional regarding money laundering are Australia, Canada, France, Germany, Hong Kong, Luxembourg, the Netherlands, New Zealand, Switzerland, the United Kingdom, and the United States.

## IV. CASE LAW AND OTHER DEVELOPMENTS

In many countries around the world, major litigation is raging over the implementation of national anti-money laundering laws, often continuing for five years or more. For instance, the anti-money laundering litigation in the early 1990s in Luxembourg over assets of the Cali cartel in Luxembourg generated simultaneous litigation in Panama and New York, and subsequently resulted in criminal proceedings against one of the U.S.-based attorneys for the Cali cartel over his conduct in handling the case. The broad nature of money laundering laws means that it can, and often is, added by U.S. prosecutors as a charge whenever a crime has been committed involving the transfer of money, property or both. Moreover, the technical distinctions in money laundering statutes sometimes can be important internationally.<sup>369</sup>

A. *Antigua Government Announces the Failure of a Russian-Owned Bank*

During the first week of August 1997, the Government of Antigua and Barbuda announced the failure of the European Union Bank (EUB)—a fraud warning—and appointed Coopers & Lybrand as the receiver of a Russian-owned bank.<sup>370</sup> The Antiguan Government further announced that it was pursuing Serbeveo Ushakov of Texas and Vitali Papsouev of Ontario, Canada, two Russian nationals who founded EUB and are believed to have fled.<sup>371</sup> According to a media report, Evan Hermiston, resident manager in Antigua of Coopers & Lybrand's Caribbean branch, said the Antiguan Government had asked his firm to start investigating the bank during mid-July.<sup>372</sup> Hermiston delivered a report during the first week of August.

The webpage established by EUB on the World Wide Web invited depositors to take advantage of "excellent interest rates, offered in a stable, tax-free environment, with utmost privacy,

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369. See the discussion of *United States v. Dynar* [1997] 2 S.C.R. 461, *infra* notes 383-97 and accompanying text.

370. See George Graham & Canute James, *Antigua Hunts Russians as 'Bank' Fails*, *FIN. TIMES*, (London), Aug. 9-10, 1997, at 3.

371. See *id.*

372. See *id.* According to one media report, "Antigua had become one of the Caribbean's most notorious havens for shady banks, but the government earlier this year launched a bid to clean up the sector." *Id.*



confidentiality and security."<sup>373</sup> In October 1996, both the Bank of England and the U.S. Comptroller of the Currency issued warnings on EUB's operations.<sup>374</sup>

Two Russians, Aleksandr P. Konanikhin and Mikhail B. Khodorovsky, founded EUB in June 1994.<sup>375</sup> They described themselves as "brokers of oil, metals, and construction supplies and officers of the Menatop Bank of Moscow."<sup>376</sup> U.S. and British officials allege the bank is linked to Russian organized crime. According to U.S. officials, Konanikhin was arrested in the United States on visa violation charges and is accused of embezzling more than \$8 million from a Moscow bank. Both Konanikhin and Khodorovsky have since severed their formal connections with the EUB. Two other Russians, Ushakov and Papsouev, who have disappeared, were listed as the bank's directors when it collapsed.<sup>377</sup>

As part of EUB's marketing on its now dormant Internet webpage,<sup>378</sup> the bank stressed the benefits of the lax regulatory climate. The webpage announced that "[s]ince there are no government withholding or reporting requirements on accounts, the burdensome and expensive accounting requirements are reduced for you."<sup>379</sup> EUB's Internet webpage allowed clients anywhere in the world to open accounts, transfer money, write checks by computer, and obtain credit cards twenty-four hours a day.

Although the Antigua Government is claiming confidentiality laws and has declined to provide information regarding the number of depositors at EUB or the amount of money it had reported in accounts, bank records show the bank violated the rules almost from the start.<sup>380</sup> Indeed, in October 1995, an official letter from the Ministry of Finance noted that the bank had failed to file an audited financial statement for 1994.

In May 1997, the Idaho Department of Finance "declared the bank to be operating illegally" and ordered it to "stop soliciting deposits from Idaho residents over the Internet."<sup>381</sup>

As a result of international pressure—that is, the warnings issued by the Bank of England, the OCC, and the U.S. State

373. *Id.*

374. *See id.*

375. *See* Larry Rohter, *New Bank Fraud Wrinkle in Antigua: Russians on the Internet*, N.Y. TIMES, Aug. 20, 1997, at A4.

376. *Id.*

377. *See id.*

378. *See* The European Union Bank at <http://www.eubank.ag> (website no longer active).

379. *Id.*

380. *See* Rohter, *supra* note 375, at A4.

381. *Id.*

Department—the Antiguan Government closed another five Russian banks established in Antigua and issued new anti-money laundering regulations.<sup>382</sup>

The combination of the U.K. and U.S. warnings and the latest problems experienced by EUB clearly hurts the reputation of Antigua and Barbuda as stable and secure environment.<sup>383</sup> Indeed, overreliance on secrecy and insufficient regulatory frameworks and supervision can undermine stability. Ironically, secrecy and lack of regulation also focus the attention of foreign regulators and international financial organizations on financial institutions in such jurisdictions. Nevertheless, since the British Government has closed many of the offshore banks and financial institutions in the Caribbean Dependent Territories, and since more traditional jurisdictions such as Panama and the Bahamas have tightened their own vetting and regulatory processes, unsavory characters and organized crime have targeted countries whose frameworks and vetting processes are comparatively liberal.

John E. St. Luce, the Antiguan Finance Minister, has claimed that his government has passed strong legislation on anti-money laundering and has a committee reviewing these developments.<sup>384</sup> Earlier statements from the Antiguan Government stating that it had remedied the problems of offshore banks, however, have proven to be mere rhetoric and little substance.<sup>385</sup>

On May 6, 1998, the U.S. Attorney filed an indictment in the U.S. District Court for the Northern District of Florida charging “the Caribbean American Bank of Antigua and eight individuals with a loan scam that allegedly bilked more than \$60 million from hundreds of people in ten countries and with related money laundering.”<sup>386</sup> The indictment seeks as one remedy the forfeiture of all the bank’s funds and assets.<sup>387</sup>

382. See Graham & Canute, *supra* note 370, at 3.

383. For background, see *Antigua to Clean Up Banking Image*, COM. CRIME INT’L 6 (Apr. 1997).

384. See Rohter, *supra* note 375, at A4.

385. For prior discussions on Antiguan statements, see *Antigua Will Close Five Russian Offshore Banks and Tighten Vetting*, 13 INT’L ENFORCEMENT L. REP. 129 (1997); *Antigua Appoints Adviser to Combat Illicit Drug Trafficking and Money Laundering*, 12 INT’L ENFORCEMENT L. REP. 340 (1996).

386. *U.S. Indicts and Seeks Forfeiture of Antiguan Bank for Loan Scam*, 14 INT’L ENFORCEMENT L. REP. 314 (1998).

387. See *id.*

B. *Canadian Supreme Court Orders Extradition  
for U.S. Money Laundering Sting*

On July 26, 1997, the Canadian Supreme Court reversed the Ontario provincial appeals court and held that a Canadian citizen should be extradited to the United States.<sup>388</sup> On a dual criminality issue, the Court concluded that the failed sting constituted the offenses of attempt and conspiracy in Canada.<sup>389</sup>

Arye Dynar, a Canadian citizen, was the subject of a U.S. money laundering investigation during the 1980s. In 1990, the FBI in Nevada began recording telephone conversations between Dynar in Canada and a cooperating informant in the United States known as "Anthony." According to the Court, "Mr. Dynar agreed with alacrity to launder money for Anthony."<sup>390</sup>

Moreover, these conversations indicated that the money to be laundered was drug money.<sup>391</sup> However, as it was a government sting, no real drug money existed. Dynar refused to travel to the United States. Instead, it was determined that Dynar's associate, another Canadian citizen named Maurice Cohen, would meet with Anthony's associate in Buffalo, New York, collect the money, and return it to Dynar in Toronto where it would be laundered. Cohen would return the laundered money less, of course, Dynar's commission. Cohen entered the United States and met with undercover U.S. law enforcement agents. No money was transferred, and the FBI aborted the operation by pretending to arrest one of the undercover officers.<sup>392</sup>

Subsequently, the United States sought the extradition of Dynar on a two-count indictment returned in Las Vegas, Nevada. The indictment charged Dynar and Cohen with violations of U.S. money laundering laws of under the sting provisions of the U.S. Code.<sup>393</sup> The first count of the indictment accused "both Dynar and Cohen of attempting to conduct a financial transaction involving property represented by a law enforcement officer to be the proceeds of drug dealing and the second count accused the two of conspiring to do so."<sup>394</sup>

388. See Kirk W. Monroe, *Canadian Supreme Court Reinstates Extradition for U.S. Money Laundering Sting*, 14 INT'L ENFORCEMENT L. REP. 3 (1998) (discussing *United States v. Dynar* [1997] 2 S.C.R. 461).

389. See *id.*

390. *Id.*

391. See *id.*

392. See *id.*

393. See 18 U.S.C.A. §1956(a)(3) (West Supp. 1999).

394. Monroe, *supra* note 388, at 3.

The United States requested the extradition of Dynar from Canada in 1992.<sup>395</sup> Following an extradition hearing, Dynar was ordered committed for extradition. Dynar appealed to the Ontario Court of Appeal.

The Ontario Court of Appeal reversed and set aside the extradition on the basis that there was a lack of dual criminality under Canadian law.<sup>396</sup> According to the provincial appeals court, Dynar did not commit a crime under Canadian law because at the time of the activity no sting provision existed.<sup>397</sup> As such, the money must in fact be derived from the commission of a crime.<sup>398</sup> The Crown appealed to the Supreme Court of Canada.

The Supreme Court framed the issue before it in this way:

The issue in this appeal is whether the respondent's conduct in the United States would constitute a crime if carried out in this country, thereby meeting the requirement of "double criminality" which is the precondition for the surrender of a Canadian fugitive for trial in a foreign jurisdiction. This issue requires the Court to consider the scope of the liability for attempted offenses and conspiracy under Canadian criminal law, specifically, whether impossibility constitutes a defense to a charge of attempt or conspiracy in Canada.<sup>399</sup>

A majority of the Court ruled that "Dynar's conduct would have amounted to a criminal attempt and a criminal conspiracy under Canadian law."<sup>400</sup> Even though Dynar's plan, if successful, would not have constituted a violation of the substantive criminal law in Canada at that time, the Court found that "the steps that Mr. Dynar took towards the realization of his plan to launder money would have amounted to a criminal attempt and a criminal conspiracy under Canadian law."<sup>401</sup> As a consequence, the Court ruled that the trial court was correct in holding Dynar extraditable on both the charge of attempt to launder money and conspiracy to launder. The extradition order was reinstated.<sup>402</sup>

395. See *United States v. Dynar* [1997] 2 S.C.R. 461, 470.

396. See *id.* at 479-80. For a discussion of the Ontario Court of Appeal decision, see Kirk W. Monroe, *Canadian Appeals Court Refuses to Extradite for U.S. Money Laundering Sting*, 12 INT'L ENFORCEMENT L. REP. 138 (1996).

397. See *Dynar*, [1997] 2 S.C.R. at 479-80. This law has since changed. Effective May 14, 1997, the Parliament of Canada effectively enacted a sting provision by amending the existing money laundering statute's knowledge element to include "believing." See R.S.C., ch. 46, §462.31(1) (1985).

398. See *Dynar*, [1997] 2 S.C.R. at 479.

399. *Id.* at 469.

400. *Id.* at 481.

401. *Id.* at 485.

402. See *id.* at 523.

### C. *United States and Mexico Duel over Money Laundering Case*

A case that illustrates the tension over international money laundering and corruption between the United States and Mexico is a case resulting from a sting operation conducted by U.S. authorities primarily against Mexican banks. On May 18, 1998, a federal grand jury in Los Angeles charged three Mexican banks and twenty-six Mexican bankers with laundering millions of dollars in drug profits.<sup>403</sup> According to an announcement by Treasury Secretary Robert Rubin and Attorney General Janet Reno, the charges represent the first time that Mexican banks and bank officials were directly linked to laundering U.S. drug proceeds for the Cali cartel of Colombia and the Juarez cartel of Mexico.<sup>404</sup> The indictment was the culmination of "Operation Casablanca," a three-year undercover sting operation led by the U.S. Customs Service that resulted in the arrests of twenty-two bankers from twelve of Mexico's nineteen largest banking institutions. The indictment indicated gaping loopholes in U.S. and Mexican laws that permit traffickers to move their proceeds relatively easily in spite of various anti-money laundering and reporting laws and regulations in both countries.<sup>405</sup> The loopholes have been widely reported by law enforcement authorities. This section outlines some of the highlights of the investigation, the indictment, responses by the Mexican Government, and its consequences for U.S.-Mexican law enforcement cooperation.

#### 1. Indictment

The three Mexican banks charged were Bancomer and Banca Serfin—Mexico's second- and third-largest banks, respectively—as well as Banca Confia, a smaller institution recently bought by Citibank.<sup>406</sup> On May 18, 1998, the Federal Reserve Board announced it was filing civil actions against five banks with branches in the United States.

Shortly after the indictment, Banca Serfin announced it would plead not guilty and asked William Isaac, former Chairman of the FDIC, to conduct an independent investigation of the accusations.

403. See Don Van Natta, Jr., *U.S. Indicts 26 Mexican Bankers in Laundering of Drug Funds*, N.Y. TIMES, May 19, 1998, at A6.

404. See *id.*

405. See Julia Preston, *Mexicans Belittle Drug-Money Sting*, N.Y. TIMES, May 20, 1998, at A6.

406. See Van Natta, *supra* note 403, at A6.

In a statement announcing the indictment, Secretary Rubin said that “[b]y infiltrating the highest levels of the international drug trafficking financial infrastructure, [U.S. Customs officials were] able to crack the elaborate financial schemes the drug traffickers developed to launder the tremendous volumes of cash acquired as proceeds from their deadly trade.”<sup>407</sup> Attorney General Reno said that “the arrests and seizures disrupted a major money laundering operation that had served as an engine of the international drug trafficking trade.”<sup>408</sup>

Since its start in November 1995, the undercover sting was kept secret from the Mexican Government. On May 18, 1998, Mexican officials first learned of the investigation when Reno notified Mexican Attorney General Jorge Madrazo Cuellar by phone.<sup>409</sup> Secretary Rubin also alerted his counterpart, Jose Angel Gurria Trevino, Secretary of Finance and Public Credit in Mexico.

U.S. authorities said that they discovered nearly 100 bank accounts in the United States had been used by drug traffickers to deposit laundered funds. On May 18, 1998, investigators seized those accounts that they estimated to hold approximately \$122 million.<sup>410</sup>

The investigation began after the U.S. Customs Office in Los Angeles discovered that drug cartel members had laundered proceeds from U.S. drug sales in branches of Mexican banks near the border. The investigation grew to include the financial infrastructure of the Ciudad Juarez cartel. During the investigation, Customs Service undercover agents established a front company, the Emerald Empire Corp., with offices in the Los Angeles suburb of Santa Fe Springs, and posed as middlemen between the cartel financial directors and the Mexican bankers (mostly mid-level executives), who agreed, for a fee of four or five percent, to launder funds. The bankers had established phony accounts and used bank drafts to evade money laundering regulations.

The indictment indicated gaping loopholes in U.S. and Mexican laws that permit traffickers to move their proceeds relatively easily in spite of various anti-money laundering and reporting laws and regulations in both countries.<sup>411</sup> The loopholes have been widely reported by law enforcement authorities.

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407. *Id.*

408. *Id.*

409. *See id.*

410. *See id.*

411. *See* Julia Preston, *Mexicans Belittle Drug-Money Sting*, N.Y. TIMES, May 20, 1998, at A6.

According to the indictment, between February 1997 and May 1998, Confia branch lawyer Miguel Barba Martin and employee Jorge Milton Diaz managed to direct \$11 million in drug money deposits into false accounts and transfer the funds into easily cashed bank drafts and other instruments.<sup>412</sup> At one time, Reyes Ortega warned Victor Manuel Alcala, alias Dr. Navarro, an alleged capo for the Juarez cocaine cartel, that the new Mexican banking rules would make it more difficult to launder money in Mexico.

Hence, in late 1996, \$650,000 from one deposit turned up belatedly in a phony business account established in the Cayman Islands as part of the scheme. "New accounts in false names were regularly opened and closed in various offshore locales to avoid detection."<sup>413</sup> For instance, Alcala is alleged to have established "a textile company as a front in Tepatitlan, which opened accounts at Banoro, where the branch manager also proved helpful."<sup>414</sup>

On May 18, 1998, the Federal Reserve issued "cease and desist" orders against five foreign banks, including two of those under indictment, for failing to address serious deficiencies in their anti-money laundering programs.<sup>415</sup> The banks are Banca Serfin, Bancomer, Banamex and Bitat of Mexico and Banco Santander of Spain, each of which operates offices in the United States.<sup>416</sup> The Federal Reserve order requires the banks to implement new anti-money laundering procedures.

## 2. Mexico Will Prosecute U.S. Agents Who Operated Sting

Attorney General Madrazo Cuellar accused the United States of deceiving Mexico by making officials there believe that the entire three-year undercover operation had been conducted inside the United States.<sup>417</sup>

President Ernesto Zedillo ordered his diplomats to deliver the protest after he determined that conducting a hidden operation on Mexican soil violated the terms of several agreements between the two countries as well as the spirit of the close bilateral relationship.

412. See James F. Smith, *Town Is Unlikely Star of Money-Laundering Probe*, L.A. TIMES, May 22, 1998, at A1.

413. *Id.*

414. *Id.*

415. David Rosenweig & Mary Beth Sheridan, *Mexican Banks Indicted in Drug Money Probe*, L.A. TIMES, May 19, 1998, at A1.

416. See *id.*

417. See Julia Preston, *Mexico Faults U.S. Secrecy in Bank Sting of Drug Profit*, N.Y. TIMES, May 22, 1998, at A3.

On May 21, 1998, the Mexican Permanent Commission, which represents Mexico's Congress when it is not in session, voted unanimously to demand an investigation into "Operation Casablanca" and criticized possible intervention by U.S. agents.<sup>418</sup> On June 3, 1998, the Mexican Government advised the United States that it would prosecute U.S. Customs agents and informers who executed an undercover money laundering operation in Mexican territory and would seek the agents' extradition in connection with the charges.<sup>419</sup>

At a meeting on June 1, 1998 in Caracas, Venezuela, Foreign Secretary Rosario Green of Mexico handed to U.S. Secretary of State Madeleine K. Albright a list of Mexican laws that the Customs agents violated according to preliminary results of Mexican investigations. In news interviews, Secretary Green reported that "Mexico is preparing to accuse the agents of entrapment, engaging in money-laundering, and usurping the authority of Mexican law enforcement."<sup>420</sup> Meanwhile, Secretary Albright acknowledged that ties with Mexico had been damaged at a meeting of the Organization of American States in Caracas.<sup>421</sup>

In the aftermath of the indictments against Mexican banks and bankers resulting from "Operation Casablanca," Secretary Green has stated that Mexico now has evidence that U.S. agents broke Mexican laws during their investigations.<sup>422</sup> The inducement of illegal acts, apparently conducted during the three-year money laundering sting when U.S. agents posing as drug traffickers persuaded Mexican bankers to launder alleged drug profits, violates Mexican law.<sup>423</sup> As a result of the U.S. handling of the investigation, the whole structure of U.S.-Mexican anti-drug cooperation will be reassessed in future meetings with U.S. officials.

Mexican officials are angry that indictments were issued only against Mexican banks and bankers, while U.S. banks named in the investigation went unindicted. The indictments "also reinforced perceptions of corruption in Mexican law-enforcement institutions and undermined efforts by the Zedillo government" to strengthen Mexican agencies responsible for monitoring and combating money laundering.<sup>424</sup>

418. See *Mexicans Lament the Timing of U.S. Operations on Money Laundering*, FIN. TIMES (London), May 22, 1998, at 4.

419. See Julia Preston, *Mexico to Prosecute U.S. Agents Who Run an Anti-Drug Sting*, N.Y. TIMES, June 4, 1998, at A5.

420. *Id.*

421. *See id.*

422. See Jose de Cordoba, *Bank Bust Stings U.S.-Mexico Relations*, WALL ST. J., May 28, 1998, at A18.

423. *See id.*

424. *Id.*



### 3. U.S. Response on its Lack of Notification to Mexico

In January 1996, U.S. officials informed Rafael Estrada Samano about the operation and asked for his help.<sup>425</sup> Separately, however, U.S. officials gave a less detailed presentation to a deputy finance minister, Ismael Gomez Gordillo. Although U.S. officials asked Estrada to conduct a joint investigation, he did not respond and the United States abandoned the idea. Attorney General Madrazo Cuellar has said that the United States was vague about the operation and asked Gordillo only for information on some Mexican bank accounts, which he provided.<sup>426</sup> Yet, U.S. customs officials grew suspicious about the lack of response they received from Mexican officials.<sup>427</sup>

Julie Shemitz, an Assistant U.S. Attorney in Los Angeles, stated that U.S. officials did not share any information about the operation with Mexico while it was under way out of fear for the safety of the undercover agents.<sup>428</sup> Shemitz said “[i]t’s not that we don’t trust Mexicans. We just didn’t tell anyone. This kind of operation is so dangerous, and you can’t play games with the lives of the officers.”<sup>429</sup>

### 4. Summary and Conclusion

As a result of the indictment, hopes of obtaining diplomatic protection for U.S. law enforcement agents have been discarded. Similarly, thoughts of following up on the investigation are fading.<sup>430</sup>

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425. See Tim Golden, *U.S. Drug Sting Riles Mexico, Imperiling Future Cooperation*, N.Y. TIMES, June 11, 1998, at A1.

426. See *id.*

427. See *id.*

428. See Preston, *supra* note 419, at A3.

429. *Id.* For instance, “One Customs agent working under cover was shot and wounded in a shootout between narcotics traffickers and police officers in New York City on August 6, 1997.” *Id.*

430. See Golden, *supra* note 425, at A1. A few suspects who could not be lured to the United States have been arrested in Mexico. One of the most important, Enrique Mendez Urena, an investment banker who was said to have worked for Carrillo Fuentes, a former alleged head of a major Mexican drug cartel, died of extensive head injuries following his arrest in Puerto Vallarta. See *id.* “The state police, who apparently arrested him, said he had been acting strangely and had hurt himself in jail.” *Id.*

## V. CRIMINAL AND QUASI-CRIMINAL TAX DEVELOPMENTS

Professionals involved in international wealth transfer techniques must be aware of developments in international tax enforcement. Moreover, practitioners working in international tax enforcement must be aware of several important trends.

Recently concluded and ratified tax treaties indicate the trend toward more active enforcement and cooperation within such treaties and increased merging of provisions from treaties of mutual assistance in criminal matters with traditional tax treaty provisions.<sup>431</sup> The United States has concluded several treaties with key countries used in international tax and estate planning, such as Switzerland, Austria, Luxembourg, and Ireland. These treaties contain active enforcement cooperation provisions.<sup>432</sup>

The trend toward increased unilateral assistance in tax enforcement affects clients and practitioners in sometimes unexpected ways. While U.S. tax authorities have been in the forefront, many other countries, sometimes under pressure from multilateral development banks in the context of structural readjustment programs, are conditioning loans on better tax administration and more active enforcement.<sup>433</sup> Multilateral development banks are also making effective tax administration part of their good governance programs. In recent years, the unilateral extraterritorial tax enforcement has manifested itself in draconian reporting requirements for foreign persons, foreign trusts, and persons who expatriate, such as surrendering their citizenship.<sup>434</sup>

A growth area in international tax enforcement concerns pre- and post-judgment attachment, seizure, and freezing of assets. Increasingly, tax officials recognize that in an interconnected world at the end of a controversial tax dispute the ability to move funds instantly may make for a hollow victory unless tax authorities have the means to seize the funds in dispute or obtain sufficient security in lieu of the funds.<sup>435</sup>

Increasingly, the tax and non-tax enforcement areas are interacting. In this regard, tax enforcement officials and law enforcement officials are cooperating in an effort to combat the

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431. See generally Bruce Zagaris, *Developments in Mutual Cooperation, Coordination and Assistance Between the U.S. and Other Countries in International Tax Enforcement*, 27 *TAX MGMT. INT'L J.* 506 (1998).

432. See *id.* at 506-07.

433. See *id.* at 515.

434. See *id.* at 504.

435. See *id.* at 510-12.

threats from transnational crime, especially transnational organized crime.<sup>436</sup>

An engine of increased international tax enforcement is multilateral tax cooperation. International organizations, such as the OECD, economic integration groups, and ad hoc groups are developing novel enforcement cooperation approaches and a more institutionalized approach.<sup>437</sup> In particular, the OECD Harmful Tax Competition report has significant implications for fiduciaries operating internationally.<sup>438</sup>

## VI. ASSET FORFEITURE

From the beginning, one goal in anti-money laundering and other anti-crime initiatives has been to immobilize criminals and their assets by identifying, freezing, tracing, seizing, confiscating, and forfeiting the instrumentalities and proceeds of the crimes.<sup>439</sup> Some countries, such as the United States, have active criminal, administrative, and civil asset forfeiture programs.<sup>440</sup> Some prosecutors prioritize asset forfeiture over criminal prosecution of defendants, especially in cases in which prosecution of defendants may not be possible.

Two Swiss cases discussed below indicate the increasing cooperation by the Swiss Government in assisting foreign governments prosecute corruption cases against former high level officials. The discussion below of the Mexican Government's seizure of accounts illustrates how many governments that traditionally have not had active anti-money laundering programs are now implementing new programs.

### A. Swiss Freeze \$13 Million of Bhutto Accounts

On October 15, 1997, the Swiss police announced that it identified SFr20 million (U.S. \$13.6 million) in frozen bank accounts belonging to the family of former Pakistani Prime Minister Benazir Bhutto, in connection with corruption inquiries.<sup>441</sup> During the weekend of October 10-11, 1997, Bhutto

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436. See *id.* at 512, 515.

437. See *id.* at 515.

438. For background on the OECD Report and its implications, see Bruce Zagaris, *OECD Report on Harmful Tax Competition: Strategic Implications for Caribbean Offshore Jurisdictions*, 17 TAX NOTES INT'L 1507-18 (1998).

439. See Zagaris, *supra* note 431, at 510.

440. See *id.* at 512.

441. See Jimmy Burns, *Swiss Find £8.4m in 'Bhutto Bank Accounts'*, FIN. TIMES, (London) Oct. 16, 1997, at 20.

denied for the first time that the Swiss accounts belonged either to her or to her relatives.<sup>442</sup> Bhutto had been fired as Prime Minister in November 1996 on charges of corruption and misrule. As a result of the freeze order that followed the provisional blocking of the assets—a preventive measure taken the month preceding the freeze—the assets will remain frozen until the end of the investigation.

The Swiss authorities responded to a formal request for judicial assistance from the Pakistani Government. Pakistani investigators claim that the Bhuttos have deposited between \$50-80 million in Swiss bank accounts. According to Falco Galli, Swiss federal police spokesman, the Swiss police “have not excluded the possibility of freezing more accounts.”<sup>443</sup>

According to Galli, the Swiss police froze seven accounts in seven different Geneva-based banks in three stages—on September 8, September 17, and October 8, 1997. The owners of the frozen accounts are Bhutto, her husband, Asif Ali Zardari, and her mother, Nusrat Bhutto. Senator Saifur Rehman, who heads a Pakistani government corruption commission investigating the affair, said that he would visit Switzerland to give evidence to Swiss authorities and request the freezing of more accounts.

The freeze orders and provisional blocking of funds, along with the Swiss actions in the Mobutu case<sup>444</sup> and the overriding of bank secrecy in dealing with the accounts related to the Holocaust, indicate a new environment of Swiss cooperation with respect to foreign asset forfeiture cases. Nevertheless, the Swiss will act only in response to an actual criminal investigation and a request for judicial assistance, mutual assistance, or both, in connection therewith.<sup>445</sup>

The Swiss action indicates the increased cooperation by governments when they are requested to provide assistance in corruption cases. Until the mid-1990s, governments and courts were reluctant to act in corruption cases, especially when they concerned former high level officials or political leaders.

442. *See id.*

443. *Id.*

444. *See Swiss Appellate Court Affirms Freeze of Mobutu Assets*, 13 INT'L ENFORCEMENT L. REP. 361 (1997) (stating that the Mobutu case enabled the Swiss Government to freeze, confiscate, and forfeit the assets of corrupt leaders from foreign countries); *Swiss Government Announces Freeze of \$3.4 Million in Bank Accounts for Mobutu*, 13 INT'L ENFORCEMENT L. REP. 270 (1997) (discussing the Swiss Government's search and subsequent freeze of Mobutu's assets).

445. *See Clemens Kohinke & Cornelia Beck, Judicial Assistance Requests: The Devaker and Marios Cases—Two Approaches Toward Switzerland*, 2 INT'L ENFORCEMENT L. REP. 370, 372 (1986) (discussing factors necessary for Swiss action in locating and freezing assets).

### B. *Swiss Supreme Court Forfeits Portion of Marcos Money*

On December 10, 1997, the Swiss Supreme Court, in a landmark decision after eleven years of litigation, ruled that \$100 million of assets belonging to the late dictator Ferdinand Marcos must be returned to the Philippines Government, provided certain conditions are met.<sup>446</sup> The decision applies to \$100 million of the \$500 million frozen in Swiss bank accounts since Marcos' abdication in 1986.

According to Peter Cosandey, the Zurich District Attorney, a decision on the disposition of the remaining funds would be forthcoming.<sup>447</sup>

The court ordered that the money be placed in an escrow account at the Philippine National Bank, which is partly owned by the Philippine Government. Provided certain conditions are met, the court has ordered that the funds held by Swiss Bank Corporation must be transferred to the Philippine courts, which will decide how to distribute them.<sup>448</sup> The same decision will apply as well to the funds held by Credit Suisse, which are subject to the jurisdiction of another Swiss canton.<sup>449</sup>

The order reverses prior rulings that the disputed assets could not be released until Imelda Marcos, who also claims the money, was convicted by a Philippine court.<sup>450</sup> While she has been convicted and sentenced to a total of forty-two years for corruption, Marcos has not served time in prison. Instead, she is an active member of Congress.

To ensure the transfer of the money, the Philippine Government must demonstrate and guarantee that the money "will be distributed by a court complying with the United Nations standards of legal process."<sup>451</sup> The order also requests information "about deliberations on the award of the money and measures being taken to compensate victims of human rights abuses under the Marcos regime."<sup>452</sup>

446. See *Swiss Court to Return Some Marcos Money*, N.Y. TIMES, Dec. 13, 1997, at A6.

447. See *id.*

448. See William Hall & Justin Marozzi, *Swiss Act to Unfreeze Marcos Cash*, FIN. TIMES (London), Dec. 13-14, 1997, at 4.

449. See *id.*

450. For a discussion of prior Swiss rulings on the case, see Clemens Kochinke, *Update on Swiss Duvalier and Marcos Cases*, 3 INT'L ENFORCEMENT L. REP. 251 (1987); Clemens Kochinille, *Marcos Judicial Assistance Cases Ready for Swiss Supreme Court*, 3 INT'L ENFORCEMENT L. REP. 79 (1987); Kochinke & Beck, *supra* note 445, at 370-74.

451. Hall & Morozzi, *supra* note 448, at 4.

452. *Id.*

The ruling represented a setback for approximately 9,500 victims of international human right violations during the Marcos regime who have already obtained a judgment but are trying to levy against many of the same assets that the Philippine Government is seeking. Approximately one week before the order, a U.S. federal appeals court dismissed a lawsuit by Philippine human rights victims who had also made claims upon the money in the Swiss banks.<sup>453</sup> The court ruled that the Swiss decision to block the Marcos accounts forestalled any action on the matter by U.S. courts.<sup>454</sup>

In 1994, a U.S. federal jury in Hawaii found the Marcos Administration guilty of murder, torture, and violations of the provisions of international human rights conventions.<sup>455</sup> It awarded the plaintiffs \$1.2 billion in damages. But the pendency of the court actions by the Philippine Government left Swiss courts and banks in a quandary. While they feared having to pay twice, they wanted to demonstrate that they would not protect a corrupt government that had stolen so much money over a long period of time.

Activity is underway in Manila to resolve the dispute between the Philippine Government and the Marcos family. The initiative is led by Magtanggol Guunigundo, chairman of the Philippines Presidential Commission on Good Government, which was established by former President Corazon Achino in 1986 to recover assets fraudulently amassed under Marcos and the Marcos family. Now, both the government and the Marcos family have said they want a final settlement.<sup>456</sup> However, differences regarding the amount of Marcos assets still outstanding complicate such a settlement.

The decision represents a victory for those wanting to pursue civil prosecution against corrupt politicians, even when the assets are moved to foreign jurisdictions in which strong secrecy laws predominate. The effort to forfeit the Swiss assets of Marcos was especially difficult because the environment to penetrate and forfeit assets of government corruption was much less developed in the late 1980s than today. The case is also a precursor to future efforts to pursue the assets of corrupt leaders.

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453. *Id.*

454. *See id.*

455. *See Federal Jury Awards \$1.2 Billion to Marcos' Victims*, 10 INT'L ENFORCEMENT L. REP. 68 (1994).

456. *See Hall & Marozzi, supra note 448, at 4.*

C. *Mexican Seizure of Gaxiola Bank Account Signals  
New Cooperation and Tension in Anti-Money  
Laundering Enforcement Cooperation*

Testimony by U.S. Deputy Treasury Secretary Lawrence H. Summers before the Senate Foreign Relations Committee on March 12, 1997, as well as other reports, indicate that the Mexican and U.S. Governments are actively cooperating in freezing and seizing assets, and on prosecuting money laundering, although tension exists over the effectiveness of the cooperation.<sup>457</sup>

On January 8, 1997, the United States requested that the Mexican Government freeze assets belonging to a drug-trafficking suspect, Rigoberto Gaxiola Medina.<sup>458</sup> The United States believes that substantial amounts of money may have flowed out of the account after the freeze request was made, perhaps because of corruption and a tip-off. Rather than seizing \$183 million, only \$16.7 million was frozen and seized.

According to a media report, two confidential chronologies of the case produced by U.S. officials show that agents of Mexico's National Institute for Combating Drugs did not act on the January 8, 1997 order until January 20.<sup>459</sup> Another problem was that the Mexican official in charge of executing the order was Colonel Jose Felix Name, the Institute's chief of investigations. Name has been under suspicion since he was arrested and charged with allowing Humberto Garcia Abrego, a man accused of being one of Mexico's most important money launderers, to escape from custody.<sup>460</sup>

When Mexican authorities reported to the U.S. Customs Service on the Gaxiola case, they reported that the accounts in question were depleted and only about \$16.7 million remained. Mexican officials argued that the \$183 million requested seizure did not take account of the frequent withdrawals Gaxiola had made over a thirty month period.<sup>461</sup>

According to media reports, on March 11, 1997, at a meeting of law enforcement officials of the two countries in Mexico City, Assistant U.S. Attorney General Mary Lee Warren protested the

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457. For background, see Tim Golden, *The Missing Drug Millions: Just a Misunderstanding?*, N.Y. TIMES, April 3, 1997, at A3 (discussing the money laundering case of drug trafficking suspect Rigoberto Gaxiola Medina).

458. *See id.*

459. *See id.*

460. *See id.*

461. *See id.*

apparent disappearance of the money.<sup>462</sup> However, a senior Mexican Justice official who was present said "in no way" did the United States complain about the matter.<sup>463</sup>

Mexican officials have stated that Gaxiola's accounts contained only \$393,000 on December 31, 1996.<sup>464</sup> On January 10, 1997, just before the Mexican Government moved to seize the accounts, the accounts contained \$1.47 million. After the money was frozen on January 23, 1997, the combined balance was up to \$16.7 million.<sup>465</sup> These new deposits seem to rebut allegations of a tip-off.

The case indicates that, despite the tension between the two governments, progress is occurring in establishing legal and law enforcement framework to freeze assets in Mexico. The next push will come in the effort to enforce Mexico's anti-money laundering laws.

#### VII. MUTUAL ASSISTANCE, BRIBERY, DRUGS, AND OTHER CRIMINAL COOPERATION MECHANISMS

Increasingly, practitioners must be aware of an ever-growing web of bilateral and multilateral treaties, executive agreements, and memoranda of understanding that enable governments and law enforcement officials to obtain information on various crimes. Sometimes tax crimes are covered. For instance, all the modern U.S. mutual assistance in criminal matters treaties cover tax. On October 21, 1998, the U.S. Senate voted to approve for ratification thirty-nine treaties providing for international criminal cooperation, including nineteen mutual assistance in criminal matters treaties, eighteen extradition treaties, and one prisoner transfer treaty.<sup>466</sup>

The evidence law enforcement officials need to prosecute tax crimes is often the same evidence that is required to show wrongdoing with respect to securities or commodities futures trading, drug trafficking, or transnational bribery. For instance, the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, which took effect

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462. *See id.*

463. *Id.*

464. *See id.*

465. *See id.*

466. *See U.S. Senate Approves 39 Criminal Cooperation Treaties*, 14 INT'L ENFORCEMENT L. REP. 459 (1998); *see generally* Bruce Zagaris & Danielle Barranca, *U.S. Senate Considers Ratification of 38 Criminal Cooperation Treaties*, 14 INT'L ENFORCEMENT L. REP. 404 (1998) (discussing the scope of the treaties in some detail).



on February 15, 1999, obligates signatory countries to provide evidence in connection with alleged bribes of foreign public officials and eventually will require all signatories to eliminate tax deductions for payments that are bribes.<sup>467</sup>

Similarly, in the investigation and prosecution of transnational organized crime, many law enforcement officials can obtain evidence on a variety of economic matters. Many governments, such as the United States, target alleged transnational organized crime members for tax crimes, as the United States did successfully with Al Capone.<sup>468</sup>

### VIII. INTERNATIONAL HUMAN RIGHTS AND RELATED PROTECTIONS

Proactive policing vis-à-vis transnational organized crime has produced transformations in international criminal cooperation law in the United States and throughout the world, especially in the development of a financial enforcement regime.<sup>469</sup> Anti-money laundering and immobilization of the assets and profits of criminals play an important role in these efforts. Globalization ensures that the number of transnational criminal investigations and prosecutions involving the United States will increase. Undoubtedly, an increasing number of cases will bring into play the potential applicability of the various rights guaranteed by the U.S. Bill of Rights or applicable provisions of international human rights conventions, such as the International Civil and Political Covenant.<sup>470</sup> "The tension between the need for the United States to cooperate more with national governments and international tribunals and the concern for the fulfillment of constitutional and international human rights standards is likely to continue to grow."<sup>471</sup>

Counsel representing investors, business entities, and fiduciaries can increasingly resort to international human rights provisions—in national judicial fora, international tribunals, or both—to adjudicate conflicts between new intrusive law

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467. See *OECD Anti-Corruption Convention Will Take Effect on February 15, 1999*, 15 INT'L ENFORCEMENT L. REP. 13 (1999) (discussing the specific requirements of the Convention).

468. For background on the international criminal cooperative mechanisms to combat organized crime from a U.S. perspective, see Bruce Zagaris, *U.S. International Cooperation against Transnational Organized Crime*, 44 WAYNE L. REV. 1401 (1998); *Special Issue: The United States International Crime Control Strategy*, 4 TRENDS IN ORGANIZED CRIME (1998) [hereinafter *U.S. International Cooperation*].

469. *U.S. International Cooperation*, *supra* note 468, at 1447.

470. See generally Michael Abbell & Mark Andrew Sherman, *The Bill of Rights in Transnational Criminal Litigation*, THE CHAMPION 22-29 (1992).

471. *U.S. International Cooperation*, *supra* note 468, at 1448.

enforcement techniques and substantive laws and international human rights and constitutional rights. These conflicts often result in intrusive search and seizure cases, enforcement of new due diligence requirements for businesses and individuals, asset forfeiture cases, restraint of individuals at borders, and so forth. The discussion of the restrictive provisions in U.S. mutual legal assistance treaties (MLATs) and the efforts to conduct intrusive search and seizure and evidence gathering without proper safeguards illustrate the types of defenses that persons implicated by these provisions can raise.

#### A. U.S. MLATs Restrict Their Use to Governments

Recent U.S. MLATs in criminal matters that grant the government compulsory process rights, as delimited by the respective treaties, expressly state that the treaties do not create the right for a private person to obtain evidence.<sup>472</sup> The purpose is to prevent the use of its MLATs for suppressing or excluding evidence or for impeding its investigations.<sup>473</sup> Hence, if an adversely affected person wants to prevent the execution of a request that he believes was made in violation of the treaty, his only recourse under the treaty is to the executive authority of the requested country, not to its courts. Similarly, if he wants to contest that the requested country violated the terms of the treaty in executing a request, he may do so only to the executive authorities of the respective countries.<sup>474</sup>

The treaty provisions do not prevent a person adversely affected by a request or its execution from asserting whatever rights he has under the laws of the appropriate country in its courts. For instance, a person whose home or place of business was searched and whose property was seized under a search warrant issued pursuant to a treaty request may assert whatever rights he has under the laws of the requested country to prevent that property from being turned over to the requesting country.<sup>475</sup>

Similarly, a person whose records have been subpoenaed pursuant to a treaty request may assert whatever rights he has under the laws of the requested country, to prevent the production of those records, their transmittal to the requesting country, or both. An affected person would also presumably be able to seek to enjoin the requested country from taking an action

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472. See Michael Abbell & Bruno A. Ristaj, 3 INTERNATIONAL JUDICIAL ASSISTANCE § 12-4-7(2) (Supp. 1997) (discussing the use of mutual assistance treaties to obtain evidence).

473. See *id.* § 12-4-7(1).

474. See *id.*

475. See *id.*

not authorized by the treaty or its laws.<sup>476</sup> In at least one case in which a defendant sought to use a U.S. MLAT to obtain evidence from a treaty partner pursuant to a treaty that was silent with respect to a defendant's right to seek evidence under it, "the trial court directed the Department of Justice to make a treaty request on behalf of the defendant."<sup>477</sup>

The U.S. Government has agreed to provisions in its MLATs that accommodate concerns of its treaty partners about safeguarding provisions on international human rights. For instance, in the MLAT between the United States and Australia signed on April 30, 1997, the term "essential interests" that may be invoked to deny assistance to a requesting state includes a discretionary limitation on providing assistance in death penalty cases.<sup>478</sup>

Potential remedies for rectifying apparent violations of binding provisions of international human rights include the following: to urge governments and international organizations to condition applicable MLATs, extradition treaties, and other international criminal cooperation agreements to comply with such provisions; to urge judicial tribunals through amicae briefs to condition criminal cooperation agreements on international human rights obligations; and, where appropriate, to help aggrieved persons initiate and prosecute actions in international human rights fora in order to reflect equitably their respective contributions.

#### B. *The Fourth Amendment Right Against Unlawful Search and Seizure*

"All searches and seizures in the U.S. must fulfill the requirements of the Fourth Amendment."<sup>479</sup> Hence, a search warrant issued pursuant to a treaty request must fulfill U.S. constitutional requirements regarding probable cause, specification of the place to be searched, and specification of the things to be seized.<sup>480</sup>

The majority of U.S. mutual legal assistance treaties in criminal matters specifically provide authority to U.S. courts to

476. *See id.*

477. *Id.* § 12-2-1(2) (discussing the request made by the Department of Justice to Switzerland in the case of Michele Sindona).

478. *See* Treaty with Australia on Mutual Assistance in Criminal Matters, April 30, 1997, U.S.-Austl., S. TREATY DOC. NO. 105-27, at VI (1997) (discussing Art. 3(1)(c)).

479. *U.S. International Cooperation*, *supra* note 468, at 1453.

480. *See* U.S. CONST. amend. XIV; *see also* United States v. Merchant Diamond Group, Inc., 565 F.2d 252 (2d Cir. 1997).

issue search warrants in execution of requests for assistance under such treaties.<sup>481</sup> While some of treaties do not expressly confer such authority on U.S. courts, they still require the United States to conduct searches and seizures at the request of its treaty partners if the request contains information justifying such action under U.S. laws.<sup>482</sup> "The absence in some cases of specific statutory authorization raises the issue as to whether those treaties sufficiently authorize the courts to issue such warrants."<sup>483</sup>

In a decision that has potentially important implications for international criminal cooperation, the U.S. District Court for the Central District of California held that a freeze of a target's bank account of a U.S. securities enforcement investigation is unconstitutional as violative of the Fifth Amendment right to due process and the Fourth Amendment right to be protected from unreasonable seizures.<sup>484</sup>

The case began as a derivative action of an Securities and Exchange Commission (SEC) enforcement action. The SEC sued one of the plaintiffs, Michael Colello, for his role in a pyramid scheme.<sup>485</sup> Colello asserted his Fifth Amendment right against self-incrimination during the investigative stage and has continued to maintain his silence.<sup>486</sup>

The day before the Commission filed the enforcement action against Colello and the other defendants, the SEC sought the freeze Colello's Swiss bank accounts.<sup>487</sup> The U.S. Department of Justice transmitted a request under the U.S.-Swiss Mutual Legal Assistance in Criminal Matters Treaty<sup>488</sup> and Swiss authorities complied.<sup>489</sup>

Simultaneously with the SEC enforcement action, the court issued a temporary restraining order in the enforcement action, freezing all the defendants' assets located in the United States, including Colello's.<sup>490</sup> The court, in a decision by U.S. District Judge Richard A. Paez, refused to grant the SEC's motion for a preliminary injunction against Colello, and the domestic asset freeze dissolved along with the temporary restraining order.<sup>491</sup>

481. Abbell & Ristaj, *supra* note 477, at § 12-4-8(3).

482. *See id.* § 12-6-1(1).

483. *U.S. International Cooperation*, *supra* note 468, at 1454.

484. *See Colello v. SEC*, 908 F. Supp. 738, 755 (C.D. Cal. 1995).

485. *See id.* at 740.

486. *See id.*

487. *See id.*

488. Treaty on Mutual Assistance in Criminal Matters, May 25, 1973, U.S.-Switz., 27 U.S.T. 2019.

489. *See id.*

490. *See Colello*, 908 F. Supp. at 740.

491. *See id.* at 742-43.

Colello and plaintiff Robert Romano—who was not a defendant in the enforcement action—filed a separate case on September 2, 1994 to challenge the constitutionality of the Swiss asset freeze, Colello and Romano named as defendants, among others, the SEC, its lawyers, and the Director of the Department of Justice Criminal Division's Office of International Affairs.<sup>492</sup>

The SEC had commenced its investigation in October 1993 against Cross Financial Services, Inc. (CFS) after discovering through a newspaper article that CFS promised very high rates of return to investors in a "government receivables" investment program.<sup>493</sup> On December 3, 1993, the SEC issued a formal order of investigation.<sup>494</sup>

In April 1994, the SEC subpoenaed records and testimony from Michael Colello in connection with the investigation of CFS.<sup>495</sup> During his testimony, when SEC lawyers questioned Colello about Carroll Siemens, letters of credit, European and American banks, and his bank accounts, he asserted his Fifth Amendment right against self-incrimination and refused to answer.<sup>496</sup>

On June 13, 1994, the Department of Justice sent a request under the U.S.-Swiss treaty for assistance from the Swiss Government, "seeking documents and testimony from banks in Switzerland to establish whether CFS made false statements about its investment scheme to induce people to invest and, thereafter, misappropriated investors' funds in violation of U.S. federal securities laws."<sup>497</sup> In addition, the SEC requested that any funds "traceable to the subject matter of the request be frozen so that the funds later may be returned to the U.S. to compensate the victims of the fraud."<sup>498</sup>

On June 15, 1995, the Swiss Federal Supreme Court rejected plaintiffs' contention that the asset freeze was improper.<sup>499</sup> It explained, "[I]n matters of judicial assistance, the Federal Supreme Court examines an administrative court complaint only to determine whether the preconditions for the provisions of judicial assistance have been fulfilled."<sup>500</sup> If the judicial assistance is requested by the United States, the request cannot be denied merely on the basis of deficiencies in the U.S.

492. *See id.* at 740.

493. *Id.* at 741.

494. *See id.*

495. *See id.*

496. *See id.*

497. *Id.* at 741-42.

498. *Id.* at 742.

499. *See id.* at 743.

500. *Id.* at 743-44.

proceedings, because the treaty does not contain any corresponding provision.<sup>501</sup>

Meanwhile, in ruling that the freeze was an unconstitutional seizure in violation of the Fourth Amendment to the Constitution, the *Colello* court rejected the government's contention that plaintiffs "assumed the risk" of depositing their money in a foreign country. The court stated that U.S. citizens are protected by the Bill of Rights from incursions by the U.S. Government on them or their property, regardless of its location.<sup>502</sup> Similarly, the court found no authority for the government's notion that it "can circumscribe or limit the entitlement of citizens to constitutional rights via a treaty."<sup>503</sup>

The court was troubled that freezing is permitted under the treaty based on "reasonable suspicion," whereas the Fourth Amendment requires showing "probable cause."<sup>504</sup>

The court appeared troubled by the failure to implement legislation and regulations, although legislation was initially contemplated.<sup>505</sup> The court also noted that, while the Department of Justice manual governs the conduct of the SEC and the Department of Justice, it does not require them to notify "the subject of a Treaty request or to provide a hearing before or after making the request."<sup>506</sup> Additionally, the court noted that the manual contains no standards and includes a disclaimer stating that the manual provides only internal Department of Justice guidance and "is not intended to, does not, and may not be relied on to create any rights, substantive or procedural, enforceable by law by any party in any matter civil or criminal."<sup>507</sup>

Finally, the manual states that no limitations are placed "on otherwise lawful prerogatives of the Department of Justice."<sup>508</sup>

The absence of U.S. statutory and regulatory provisions contrasts with Switzerland's approach.<sup>509</sup> Switzerland has enacted law and guidelines under the treaty. The Federal Law on the Treaty with the U.S. on Mutual Legal Assistance in Criminal Matters of October 3, 1975 provides for certain "precautionary measures" to guarantee due process through requiring notice to

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501. See *id.* at 744.

502. See *id.* at 754.

503. *Id.* at 754.

504. See *id.* at 754-55.

505. See *id.* at 751.

506. *Id.*

507. *Id.*

508. *Id.*

509. See Nathalie Kohler, *The Confiscation of Criminal Assets in the United States and Switzerland*, 13 HOUS. J. INT'L LAW, 1 (1990) (providing an analysis of the Swiss approach to the confiscation of assets).

the affected parties.<sup>510</sup> In addition, the Federal Office for Police Matters (FOPM) has also issued guidelines to inform interested authorities and citizens on what is meant and encompassed by international mutual assistance in criminal matters.<sup>511</sup>

The decision may presage trouble on other criminal mutual assistance agreements when the U.S. Government tries to enforce them in courts. Indeed, although the American Bar Association and other interested bar groups testified previously against excluding from such treaties due process protections for defendants and third parties, the U.S. Government vehemently opposed such arguments.<sup>512</sup> The decision seems to indicate that at least the court believes that a better balance is constitutionally required.<sup>513</sup>

A similar difficulty may arise in the tax information exchange and cooperation area. There, in order to secure support for ratification of the Council of Europe and OECD Treaty on Mutual Administrative Assistance in Tax Matters, the U.S. Department of Treasury

promised to issue regulations and stated that it would consider extending such regulations across the board to all tax information exchange agreements. Indeed, such due process seems compelled. However, many months after the Convention has taken effect, Treasury officials claim that their workload does not permit time for such a project. It appears that the role of courts can be important in developing incentives for officials to prioritize due process rights.

The absence of adequate rights within enforcement cooperation treaties, together with aggressive enforcement actions and the inevitable cases where rights of individuals have been abused, may jeopardize the potential for success in enforcement actions.<sup>514</sup>

## IX. CONCLUSION AND PROSPECTS

International anti-money laundering efforts will increase as transnational crime and especially transnational organized crime continue to spread. The efforts of the United Nations and the G-7

510. See *Colello*, 908 F. Supp. at 746.

511. See *id.*

512. See *Mutual Legal Assistance Treaty Concerning the Cayman Islands, Hearing, Senate Foreign Relations Committee*, Sen. Exec. Rept. 100-26, 100th Cong., 2d Sess., resolution of the American Bar Association, at 186-90; Statement of Bruce Zagaris, 166-68, 205-12; S. Rep. No. 100-26, at 166-68 (1988); Teresita Ferrera, *Second MLAT Hearings Spark Debate on Policy Issues*, 4 INT'L ENFORCEMENT L. REP. 197 (1988); Bruce Zagaris, *Sen. Helms' Inquiries over Individual Rights in MLATs Delay Mark-up*, 4 INT'L ENFORCEMENT L. REP. 160 (1988).

513. See *U.S. International Cooperation*, *supra* note 468, at 1457-58.

514. *Id.* at 1458.

Economic Summit Group to develop a convention and other mechanisms to tackle transnational crime illustrate the political consensus behind the new efforts.

Some of the prospects for international anti-money laundering efforts can be viewed in the March 1997 release of the International Narcotics Control Strategy Report (INCSR), which contains a large section on anti-money laundering.<sup>515</sup> It is worthwhile to summarize some of the discussions in order to identify trends, as well as develop and improve due diligence.

In October 1995, the United States initiated Presidential Decision Directive 42, which freezes assets and imposes economic sanctions against certain persons designated as narcotics traffickers affiliated with the Cali cartel.<sup>516</sup> U.S. agencies in 1996 assessed which money laundering and financial crime situations affected U.S. national security interests, including drug trafficking, contraband smuggling, arms sales, terrorist financing, sanctions violations, and sales of weapons of mass destruction. In some cases, teams of U.S. officials visited governments to secure agreements on actions needed.<sup>517</sup>

FATF achieved progress through starting the second round of mutual evaluations of each of its twenty-six members. FATF also warned its own members of shortcomings, especially Turkey and Greece.<sup>518</sup> FATF approved proposals to update its universally-accepted Forty Recommendations to reflect new typologies and methodologies.<sup>519</sup> Additionally, the Caribbean FATF started evaluations on its members. In Asia, an outreach program was initiated. Finally, a common forum for major international bankers and government policy makers was organized.<sup>520</sup>

In 1997, FATF's high-impact initiative external relations program that began in 1992 and 1993 succeeded in establishing agreements with the Council of Europe, the Offshore Group of Banking Supervisors, and the CFATF.<sup>521</sup> These agreements are intended to secure evaluation by outside experts to determine whether the majority of financial center countries were properly implementing the minimal global standards on anti-money laundering.<sup>522</sup>

515. See BUREAU OF INT'L NARCOTICS & LAW ENFORCEMENT AFFAIRS, INTERNATIONAL NARCOTICS CONTROL STRATEGY REPORT 539 (1998).

516. See *id.* at 548-49 (describing the objectives of Presidential Decision Directive 42).

517. See *id.* at 548.

518. See *id.*

519. See *id.*

520. See *id.*

521. See *id.* at 512.

522. See generally *id.* at 511-12 (reviewing the significant developments in the money laundering sphere in 1996).



During 1996, increased cooperation with foreign governments on major money laundering cases occurred. Asset sharing cooperation increased, as did the amount of U.S. mutual assistance treaties in criminal matters, all with important anti-money laundering and asset forfeiture-sharing provisions.<sup>523</sup>

Adverse developments identified by the INCSR include the further penetration of financial systems by organized crime groups.<sup>524</sup> Transnational crime groups increasingly have used "new drug transit routes across ever more remote countries, most of which have no or few anti-money laundering laws."<sup>525</sup> The result is the ability to move crime proceeds to the countries and systems whose financial standards are vulnerable and easily manipulated. Transnational crime groups can more easily identify and exploit "the differential between the levels of compliance with international anti-money standards," especially in Asia and Latin America.<sup>526</sup>

#### A. *New Laundering Modes*

One development is that as new drug trafficking routes are spawned in Africa and the lower regions of the old Soviet regime, the list of countries more vulnerable to money laundering widens.

Perhaps more dangerous is the absence of implementation of anti-money laws or even ratification of the 1988 Vienna-U.N. Drug Convention.<sup>527</sup> The INCSR lists Aruba, Colombia, Mexico, the Netherlands Antilles, Nigeria, Singapore, Turkey and Venezuela. Just as important, the anti-money laundering laws that governments enacted in the early 1990s are now no longer sufficient, especially given the increase in non-drug crimes, the use of new technologies, and more sophisticated ways to move money.<sup>528</sup>

The proliferation of financial crimes include the more common types of financial frauds and new variations, especially the use of prime bank guarantees, phony or fictitious letters of credit, counterfeit or stolen bonds, and other monetary instruments offered as surety for loans, and other scams. Some of the new methods include the use of secret telex codes for bank-to-bank transactions in order to move \$42 million in cash from

523. *See id.* at 512.

524. *See id.*

525. *Id.*

526. *Id.*

527. *See id.* (identifying INCSR lists Aruba, Colombia, Mexico, the Netherlands Antilles, Nigeria, Singapore, Turkey, and Venezuela as countries that have failed to meet these standards).

528. *See id.* at 513.

the Hong Kong and Shanghai Bank in Jakarta.<sup>529</sup> The use of fake certificates of deposit drawn on other branches of an international bank that can range from \$10 million to \$25 million recently occurred.<sup>530</sup> "Fraudsters' will also use counterfeit letters of agreement, drawn on bank letterheads, seemingly vouching for a client from another branch of that bank," or confirming the approval of a bogus deal.<sup>531</sup>

The INCSR reports on the ways in which money is laundered. Professional money launderers differ little in their money management than corporate money managers. Money brokers and transnational criminals collaborate to minimize their risk, partly through diversification of the means to transport, convert cash, or both, as well as to layer and integrate the laundered funds.<sup>532</sup>

### B. Challenges to Anti-Laundering Enforcement

Several aspects of contemporary banking make counter-money laundering initiatives difficult.

#### 1. Correspondent Banking

Banking is increasingly global, inter-connected, and operates twenty-four hours. Large multinational banks have global branch and subsidiary networks as well as correspondent relationships.

Correspondent banking enables launderers to initiate transactions through the weakest link in the bank. Once launderers start a bank relationship, they can quickly move money globally within the bank.<sup>533</sup>

#### 2. Offshore Banking

At the June 1996 International Conference of Banking Supervisors, banking supervisors from 140 countries agreed to adhere to twenty-nine recommendations "designed to strengthen the effectiveness of supervision by both home and host-country authorities of banks that operate outside their national boundaries."<sup>534</sup> The recommendations were incorporated into a

529. See *id.* at 514.

530. See *id.*

531. *Id.*

532. See *id.* at 515-17 (providing a full explanation on how money is laundered).

533. See *id.* at 518-19 (providing analysis of the banking world's transnational network).

534. *Id.* at 514.

report by the Basle Committee on Banking Supervision, issued in October 1996.<sup>535</sup>

Home supervisors must be able to assess "all significant aspects of their banks' operations, using whatever supervisory techniques are needed, including on-site inspections."<sup>536</sup> Means to overcome impediments to effective consolidated supervision are suggested. The Basle report sets forth "guidelines for determining the effectiveness of home country supervision, for monitoring supervisory standards in host countries, and for dealing with corporate structures which create potential supervisory gaps."<sup>537</sup> Additional guidelines are provided for host country supervision.

When the recommendations conflict with bank secrecy or similar legislation in certain countries, supervisors have agreed to use best efforts to amend the secrecy legislation. Countries with further recommendations were reviewed prior to the international meeting scheduled for October 1998.<sup>538</sup>

### 3. The Offshore Group of Banking Supervisors

The Offshore Group of Banking Supervisors (OGBS) has concluded "an agreement with FATF on a protocol for evaluating the effectiveness of the money laundering laws and policies of its members."<sup>539</sup> However, OGBS includes only about half of the known offshore banking centers among its members.<sup>540</sup>

A concern exists that different kinds of charters for financial facilities can be obtained for non-bank institutions—such as international business companies (IBCs)—that can conduct some of the same activities as banks and do not undergo the same regulatory oversight. This is a particular problem in the Caribbean.<sup>541</sup>

### 4. Private Banking

Much competition exists globally to attract high net-worth individuals and companies as private banking clients. The transactions of these clients are treated confidentially. Such customers are treated with more deference and receive various

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535. *See id.*

536. *Id.*

537. *Id.*

538. *See id.*

539. *Id.*

540. *See id.*

541. *See id.*

types of personal services.<sup>542</sup> A concern exists that, in the competition to attract and maintain these clients, financial institutions or their officials may suspend or not implement anti-money laundering and other due diligence procedures.<sup>543</sup>

## 5. Cybercurrency

The use of microchip-based electronic money for financial transactions, via smart cards and the Internet, has the potential to revolutionize the means for laundering money. Some new cyberpayments systems are engineered to be an electronic emulation of paper currency. Cybercurrency has the attributes of conventional currency: a store of value; a medium of exchange; a numeraire; potential anonymity; and convenience. Other features include transfer velocity—an almost instant electronic transfer from point to point—and substitution of electrons for paper currency and other physical means of payment. Cyberpayments also include other payment components, such as cyberchecks, cybercredit, cyberdebit, and so forth. This development requires close attention because the use of microchip and telecommunications technologies adds some significant new dimensions for law enforcement.

Cyberpayments also include other payment components, such as cyberchecks, which emulate paper checks, cybercredit, cyberdebit, etc.

Cyberpayments raise the issue of whether such payments can be made subject to monetary reporting and supervision measures. Law enforcement issues that will arise include fraud, counterfeiting, and computer hacking. High-speed, worldwide transfers add complexity to law enforcement's ability to trace criminal activity and recover illicit proceeds.<sup>544</sup>

## 6. Other Challenges

Other challenges to anti-money laundering enforcement include the counterfeiting of currencies and other monetary instruments, especially bonds, the rise in contraband smuggling, the acquisition of banks and other financial institutions by suspected criminal groups, and the resort by criminals to the use of smaller, pass-through banking, and electronic cash systems. As a result of the occurrence of financial crimes and money

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542. See *id.* at 520 (indicating that the fierce competition for lucrative private banking clients might lead to suspending bank rules on transactions).

543. See *id.*

544. See *id.* at 520-21.

laundering with varying degrees of regularity in more than 125 jurisdictions, a continuing concern exists that some governments still have not criminalized all forms of money laundering.

### C. *Continuing Concerns*

One major remaining problem is the inconsistent enforcement of anti-money laundering provisions.

Sixteen of the sixty-four eligible governments ranked as high, medium-high or medium priority money laundering concerns by the U.S. Government in 1997 have not ratified the 1988 U.N. Convention.<sup>545</sup> Hence, one-fourth of the world's important financial center countries had not ratified this universal accord six years after its entry into force.

Many governments "have not criminalized all forms of money laundering and financial crime, nor given sufficient authority to banking regulatory bodies."<sup>546</sup> Too many governments still limit money laundering countermeasures, "particularly the requirement that the offense of money laundering must be predicated on conviction for a drug trafficking offense."<sup>547</sup> An equally distressing number of governments "still refuse to share information about financial transactions with other governments to facilitate multinational money laundering investigations."<sup>548</sup>

In addition, a need exists for "enhanced bilateral and multinational communications to inform governments and financial systems in some systematic and ongoing way about the methods and typologies of drug and non-drug related money laundering and financial crimes."<sup>549</sup>

Concerns exist as well about "the concentration of economic power in drug cartels and other criminal organizations, and its potential translation into political power," especially in the Caribbean, Europe, the Middle East, and Asia, as well as the Americas.<sup>550</sup>

The growth of free trade agreements and regional integration increases the opportunities to launder money.

Finally, countries that cooperate on money laundering investigations and prosecutions need to share forfeited proceeds.

545. *See id.* at 525.

546. *Id.*

547. *Id.*

548. *Id.*

549. *Id.*

550. *Id.* at 526.

#### D. *Enforcement Agenda*

A broad enforcement agenda is suggested. Among the recommendations are the creation of international standards, agreements to exchange information, the establishment of linkages for cooperative investigations, and methods to supersede political resistance in various key countries to ensure such cooperation.

Among the national laws required are those that establish corporate criminal liability for bank and non-bank financial institutions, apply to all types of financial transactions not limited to cash at the teller's window, apply reporting and anti-money laundering laws to a long list of predicate offenses not limited to drug trafficking, criminalize investments in legitimate industry if the proceeds were derived from illegal acts, and facilitate the sharing of financial and corporate ownership information with law enforcement agencies and judicial authorities.

The INCSR Report proposed the following sixteen action items:

- (1) constant monitoring of money laundering patterns, trends, and apologies;
- (2) improving analysis of money management practices;
- (3) analyzing of non-drug-related money laundering and other financial crimes;
- (4) equating economic power with political clout;
- (5) eliminating systemic weaknesses;
- (6) assessing the trafficker as entrepreneur;
- (7) analyzing the impact of money laundering on national governments and economies;
- (8) regulating exchange houses and remittance systems;
- (9) concentrating efforts for maximum effectiveness;
- (10) pursuing a continuously evolving strategy;
- (11) intensifying the UNDCP program to ensure that all significant financial center countries implement fully the anti-money laundering and asset forfeiture provisions of the 1988 U.N. Convention;
- (12) continuing the FATF focus, along with the Offshore Group of Banking Supervisors and other relevant organizations, on offshore banking;
- (13) adopting of information standards by governments;

- (14) increasing diligence by governments and banking systems alike;
- (15) exerting greater efforts by governments and banking systems to identify and prevent a wide range of financial crimes; and
- (16) consolidating supervision of the international banking system.<sup>551</sup>

The report indicates that the anti-money laundering regime is in full-swing globally.<sup>552</sup> It will continue to deepen as an area where international law, policymakers, scholars, practitioners, and criminals and their advisers will occupy themselves for the indefinite future with its developments.

In the short- and medium-term future, key national governments and international organizations will increase their financial enforcement efforts. These endeavors will include privatization of the law enforcement efforts, which in turn will saddle the private sector with additional responsibilities and more potential sanctions for non-compliance. The private sector will need to monitor carefully these developments and participate in the legislative and executive decision-making and in the work of international organizations. If abuses occur and are imminent, private individuals may want to consider judicial or other challenges. In many cases, better networking is required within the private sector to participate effectively in the shaping and implementation of new policies and law, as well as the manner in which they are implemented.

#### *E. Private Sector Role*

Globalization means that in the next millennium practitioners and fiduciaries must constantly strengthen their due diligence against money laundering, fraud, and crime. The drawback is that it requires more attention, more work, and perhaps more selectivity vis-à-vis new clients. Globalization also means that the costs of international wealth transfer will rise, provided clients can pay the load. Counseling transnational clients in international wealth matters may be unduly risky for professionals who do not exercise care and apply modern due diligence. Professionals must stay abreast of a wide variety of national, foreign, and international law developments. These developments mean that the millennium indeed will be a brave new world.

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551. See *id.* at 528-31.

552. See *id.* at 511-44.