MONEY LAUNDERING: AN ASSESSMENT OF SOFT LAW AS A TECHNIQUE FOR REPRESSIVE AND PREVENTIVE ANTI-MONEY LAUNDERING CONTROL

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DECLARATION:

‘I confirm that this is my own work, and the use of all materials from other sources has been properly and fully acknowledged.’

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ABSTRACT

Large-scale money laundering (ML) schemes contain cross-border elements, which require cross-border international responses to the problem. A number of initiatives have been established for dealing with the problem at the international level. This includes a growing array of cooperative techniques designed to create a platform for harmonisation and approximation of domestic and international anti-money laundering law. These techniques, aimed at creating an environment for law enforcement and international cooperation, are intended to address the problem of ML, irrespective of the particular predicate criminal activity to which they may be applied.

However, given the nature of the problem of ML and the intended legal response, the traditional approach to international law making is limited and less effective as a method of creating the needed platform and atmosphere for effective law enforcement and international cooperation. The consequence of the combination of a non-traditional subject matter with the limitations of traditional international law instruments has meant that lawmakers, seeking international solutions to the problems of ML, have had to innovate. This innovation has found expression in particular with soft law.

A range of opinion exists on the theoretical and practical desirability of soft law. Some authors have long rejected formal distinctions between international law and policy; others acknowledged that the contemporary international law-making process is complex and deeply layered that there is a 'brave new world of international law' where "transnational actors, sources of law, allocation of decision function and modes of regulation have all mutated into

fascinating hybrid forms. International Law now comprises a complex blend of customary, positive, declarative and soft law".[1]

Adopting a mixed methods approach and drawing on the work of existing literature, the thesis seeks to distinguish itself from others by assessing the role of soft law as a technique to repress and prevent ML. The thesis addresses two fundamental issues in the context of existing international and domestic response to the problem of ML that remain largely uncovered by the other literature: the nature of the treaty obligations to criminalise ML and the role of soft law as a technique to repress and prevent ML. The thesis concludes that, international legal harmonisation and approximation of domestic anti-money laundering law through soft law remains useful to addressing the problem of ML.

[1] H. Koh, 'A World Transformed' (1995) 20 *Yale J. Int'L.* P.1x.

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CHAPTER ONE

The Significance of an International Anti-Money Laundering Control and the Challenges

1.1 Introduction

This thesis aims to provide an assessment of soft law as a technique for repressive and preventive anti-money laundering control (hereinafter AMLC).[2] The term repressive and preventive AMLC refers to the importance of an international response to money laundering (hereinafter ML), which centres on formal treaty obligations on state parties to criminalise and confiscate the proceeds of crime in their national law, followed by an informal non-treaty response to prevent it, through the regulation of financial and non-financial institutions.[3] The use of the word 'repressive' in the context of this thesis means to subdue or suppress criminal ML activities by the use of penal legislation. However, before elaborating on the precise research questions, it is necessary to introduce the significance of having an international response to ML, challenges with such an undertaking, and the concept of soft law.

The term ML describes graphically the process by which dirty money (money obtained through crime) is cleansed so that it is, or at least appears to be legitimate money with no taint of its criminal origin.[4] ML as a legal concept and legislation to combat ML is over 30 years old, currently, most states in the world now have legislation that criminalises ML and facilitates the recovery of the proceeds of crime. Criminal law has traditionally been the sovereign preserve of individual states and the global development of AML law and standards has been rapid and remarkable.

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2 E. Ebikake 'Money Laundering: An Assessment of Soft Law as Technique for Repressive and Preventive Anti-Money Laundering Control (2016) 19 (4) JMLC at 1.

3 *Ibid.*

4 R. Booth *et al Money Laundering Law and Regulation* (New York: OUP, 2011) p. 1.

Large-scale ML schemes, by its *modus operandi,* contain a cross-border element. Since ML is an international problem, international co-operation is a critical necessity in the fight against it. A number of initiatives have been established for dealing with the problem at the international level. International organisations, such as the United Nations[5] or the Basel Committee on Banking and Supervisory Practices[6], took some initial steps at the end of the 1980s to address the problem. Following the creation of the Financial Action Task Force (hereinafter FATF)[7] in 1989, regional groupings (e.g the Council of Europe[8], and Organisation of American States[9] , etc) established AML standards for their member states. The Caribbean[10], Asia[11], Europe[12] , and southern Africa[13] have created regional AML task force-like organisations.

The foregoing international AML initiatives (as would later be seen) are founded on two legal techniques: an initial formal treaty-based criminal/repressive technique, followed by

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5 1988 UN Convention against illicit traffic in narcotic drugs and psychotropic substances (hereinafter Vienna Convention 1988), 2000 UN Convention against Transnational Organised Crime (hereinafter Palermo Convention), 2003 UN Convention against Corruption (hereinafter UNCAC).

6 See the History of the Basel Committee and its Membership in ≤ https://www.bis.org/bcbs/history.htm ≥ last visited 18 April 2020.

7 What is FATF? Available at ≤ About - Financial Action Task Force (FATF) (fatf-gafi.org) last visited on the 01 February 2021. The FATF have other regional or international like bodies, which perform similar functions for their members. These are Asia Pacific Group on Money Laundering (APG), Caribbean Financial Action Task Force (CFATF), Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG), Financial Action Task Force for South America (GAFISUD).

8 Convention n 141 of 1991 from the Council of Europe (1990 Money Laundering Convention) available at ≤ https://www.coe.int/en/web/portal/home ≥ last visited on 18 April 2020; the Council of Europe Convention n 198 on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime and on the Financing of Terrorism (2005 Council of Europe Convention against Money Laundering) available at ≤www.coe.int≥ last visited on 18 April 2020; and EC Directive 91/308/EEC, OJ L166, 28.6.1991; Second EC Directive 2001/97/EC, OJ L344, 28.12.2001; Third EC Directive 2005/60/EEC, OJ L309, 25/11/2005; Fourth EC ML Directive 2015/849; Fifth EC ML Directive 2018/843 and Sixth Directive (EU) 2018/1673.

9 The Inter-American Drug Abuse Control Commission (CICADOAS) available at ≤www.cicad.oas.org/main/default_eng.asp≥ last visited on 18 April 2020.

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13 Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG) available at ≤www.esaamlg.org/≥. Similar bodies are now available for West Africa available at ≤https://www.giaba.org/≥ and Latin America available at ≤ http://www.gafilat.org/index.php/es/≥ last visited on 18 April 2020.

an informal preventive response. Repressive and preventive AMLC is now referred to as the *twin-track* approach[14] to AMLC.

Thus, with the advent of globalisation and the transformation in the structure of international law and politics, there is the demand for new governance structure to handle global challenges like ML. The legitimacy of traditional inter-state, consent-based international law is increasingly being challenged by the newly emerged international legal landscape: especially its general principles. They include the differentiation between international and domestic affairs, the principles of sovereignty and sovereign equality and the certainty of hard law. These general principles are called into question, as they are not applicable to the newly emerged actors, which consequently often act within a sphere of legal uncertainty.[15]

The thesis argues that the traditional approach to international law theory as a system of rules can no longer be sustained nor captured by the subtlety of the processes by which contemporary international law is created.[16] The traditional link between state consent and legal obligation has largely been replaced by non-consensual norm-making. Treaty mechanisms, for

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[14] For more on this concept see the works of T. Buranaruangote 'Money Laundering Controls: Evolution and Effective Solution to Organised Crime' The London Institute of International Banking, Finance and Development Law Ltd. ESSAYS IN INTERNATIONAL FINANCIAL & ECONOMIC LAW No.46 2003 at 37 and G. Stessens *Money Laundering: A New International Law Enforcement Model* (Cambridge: CUP 2008) p. 108.

[15] M. Wilke 'Emerging Informal Network Structures in Global Governance: Inside the Anti-Money Laundering Regime' NJIL 77(2008) at 509.

[16] One of the leading conjectures for a positivist basis for international legal obligation is consent. Under this theory, the rules of international law become positive law when the will of the state consents to being bound by them either expressly or by implication. The doctrine of consent generally teaches that the common consent states voluntarily entering the international community gives international law its validity. Dionisio Anzilotti explained that the duty to respect the obligations otherwise consented to was an absolute postulate of the international legal system. See Dionisio Anzilotti *Corso di Diritto Internazionale* (Lectures on International Law) in D. J. Bederman *The Spirit of International Law* (University of Georgia Press, 2002), p 15. The notion of consent is supposed to be applicable, irrespective of the particular source of an international legal obligation. However, consent positivists have sharply disagreed on this point. Alf Ross, for example, observed that the "positivist theory takes it for granted that all International Law is conventional [treaty] law. . . and that all validity of International Law is in the last instance derived from a union of the wills of sovereign state" – Alf Rose *A Textbook of International Law* (London: Longmans, 1947) p. 94. However, the majority of view, dating as back as Vattel and Bynkershoek, is that state consent to international law norms need not be made in reference to written treaties but may be also manifested in regard to customary obligations. According to the proponents of this approach, because consent can be either express or tacit, a broader range of obligations can be made binding on states –See Emmerich de Vattel, "Law of Nations 316(1758) [Joseph Chitty trans., Philadelphia, 1863]. Consent certainly has been regarded as the most intelligible of positivist theories of obligation in international law. Nevertheless, it suffers from many of the same analytic failings its competitor.

example, are including more 'soft' obligations, such as undertakings to endeavour to strive to cooperate,[17] and non-binding instruments in turn are incorporating supervisory mechanisms traditionally found in hard law texts.[18]

The legal nature of soft law, and equally its relationship with treaties, is far from clear. In particular, the expansion in recent years of certain types of treaties (for example, in the field of environmental protection) has given rise to international agreements that contain not only specific obligations, but also vague provisions of an ambiguous nature which do not impose 'hard' (absolute) obligations on states. As Boyle explains, some treaties may generate only principles but not rules, which do not have the strength of hard law. Such a treaty "may be potentially normative, but still 'soft' in character, because it articulates 'principles' rather than 'rules'".[19]

The study is thus, considering two interrelated issues: *(1) the nature of the international AML treaty obligations, (2) the role/function of 'soft law'* as a technique for preventive and repressive AMLC. This is because soft law signifies one of two things: informal obligations or principles and not rules. The point on 'soft law' is relevant to this enquiry, since Shelton has suggested that "recent inclusion of soft law commitments in hard law instruments suggests

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[17] Article 2 Vienna Convention 1988 similarly calls on parties' co-operation in the fight against drug related money laundering.

[18] Environmental soft law is quite often important for this reason, setting standards of best practice or due diligence to be achieved by the parties in implementing their obligations These 'ecostandards' are essential in giving hard content to the overly general and open-textured terms of framework environmental treaties. See P. Contini and P. H. Sand 'Methods to Expedite Environmental Protection: International Ecostandards' 66 (1972) *American Journal of International Law* 37.

[19] A. Boyle 'Some Reflections on Relationship of Treaties and Soft Law', in V. Gowland-Debbas (ed) *Multilateral Treaty-making: The Current Status of Challenges to and Reforms Needed in the International Legislative Process* (Martinus Nijhoff Publishers, 2000) p. 32. The 1992 Convention on Climate Change provides a good example of such principles explicitly included in a treaty. (for example Article 3 (Principles): 'in their actions to achieve the objective of the Convention and to implement its provisions, the parties shall be guided, *inter alia*, by the following: 1) The Parties should protect the climate system for the benefit of present and future generations of humankind, on the basis of equity and in accordance with their common but differentiated responsibilities; 2) The Parties should take precautionary measures to anticipate, prevent, or minimise the causes of climate change and mitigate its adverse effect; 3) The Parties have a right to, and should, promote sustainable development). See also A. Boyle and C. Chinkin *infra* note 67 p. 221.

that *both form and content are relevant to the sense of legal obligation*".[20] The focus of the enquiry is therefore on the role of soft law as a technique for repressive and preventive AMLC.

1.1 The rule versus principle debate in legal discuss

The thesis conceives rules as specific prescriptions, principles as unspecific or vague, and therefore soft law. The distinction is important, as the theory advanced in this thesis is that AML treaty obligations are legal principles and not rules. A central reason for this is that the obligations to criminalise ML, under relevant conventions[21] are expressed broadly and only refer to the process of laundering and not to a specific act of ML. It is argued that consistency in a complex domain like ML can be better realised by an appropriate mix of formal and informal obligations, than by treaties alone. A key choice here is between formal treaty obligations expressed as principles and non-binding informal obligation.

For some influential lawyers, law means quite simply decisions according to rules. One is United States Supreme Court Justice Antonin Scalia: "A government of laws means a government of rules. Today's decision on the basic issue of fragmentation of executive power is ungoverned by rule and hence ungoverned by law".[22] Philip Selznick conceives the crux of the rule of law in a more complex way to be the restraint of state power by "rational principles of civic order".[23] Principles are important on this view that "the proper aim of the legal order, and the special contribution of legal scholarship, is to minimise the arbitrary element in legal norms and decisions".[24]

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[20] D. Shelton Commitment and Compliance: The Role of Non-binding Norms in the International Legal System (New York: Oxford University Press, 2003) p 4.

[21] Articles 3 of the Vienna Convention 1988 and 6 of the Palermo Convention 2000.

[22] *Morrison* v. *Olson*, 108 S. Ct. 2597 (1988) cited in J Braithwaite 'Rules and Principles: A Theory of Legal Certainty', *Australia Journal of Legal Philosophy*, 27 (2002) pp. 47-82.

[23] P. Selznick, *Law, Society and Industrial Justice* 11 (Russell Sage Foundation, 1969) cited in Braithwaite *supra* note 22.

[24] *Ibid* at 3.

Since Aristotle, it has been understood that precision in this pursuit can be self-defeating: "our discussion will be adequate if it has as much clearness as the subject matter admits of, for precision is not to be sought for alike in all discussions".[25]

Ronald Dworkin sees rules as "applicable in an all-or-nothing fashion" when they are crafted to exhaustively include all their exceptions. According to him, "If the facts a rule stipulates are given, then either the rule is valid, in which case the answer it supplies must be accepted, or it is not, in which case it contributes nothing to the decision".[26] Dworkin, in contrast, sees legal principles, as not setting out legal consequences that follow automatically when the conditions provided are met. A principle states a reason that argues in one direction, but it does not prescribe a particular decision. Since principles have less specificity in this way, unlike rules, principles can conflict. Decision makers assigning weight to principles resolves such conflicts: "it is an integral part of the concept of a principle that it has this dimension, that it makes sense to ask how important or how weighty it is".[27] Joseph Raz[28] and Frederick Schauer[29] have attacked Dworkin's basis for the distinction. They argue that the logical difference between rules and principles has nothing to do with the possibility of conflict or the ways such conflicts are resolved.[30] For Raz, "rules prescribe relatively specific acts; principles prescribe highly unspecific actions".[31]

The specificity of rules is fairly common ground among leading positivists. For example, Campbell emphasises that rules "must not be general in the sense of being vague or unspecific".[32] Specificity, clarity and mutual consistency are seen as things that automatically go together. Hart points out that rules have a core meaning and a penumbra where their meaning

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25 Aristotle, *Nicomachean Ethics*, (W. Ross trans., 1940), Bk. 1, ch 3 at 10946.
26 R. M. Dworkin, The Model of Rules 35 (1967) U. CHI. L. REV. 25.
27 *Ibid*, at 27.
28 J. Raz, 'Legal Principles and the Limits of Law', (1972) 81 YALE L. J. 823.
29 F. Schauer, 'Prescriptions in Three Dimensions', (1997) 82 IOWA L. REV. 914.
30 Braithwaite *supra* note 22 at 5.
31 Raz *supra* note 28, at 838. Hart alluded to this point in p 29.
32 T. Campbell, *The Legal Theory of Ethical Positivism* (Dartmouth Pub. Co., 1996) cited in Braithwaite *supra* note 22.

is more uncertain. The more complex and changing the phenomenon being regulated, the wider that penumbra is likely to be.[33] According to the learned author, principles are relatively to rules, broad, general, or unspecific, in the sense that often what would be regarded as a number of distinct rules can be exhibited as the exemplifications or instantiations of a single principle.[34] According to Braithwaite, a principle of environmental regulation like 'continuous improvement' can imply an infinitely creative range of action possibilities; a rule preventing the dumping of chemical X relates only to that action.[35] This much is common ground between Raz, Schauer and Dworkin and is also a conception "which accounts for the non-legal use of these terms".[36]

For the purpose of this thesis, we focus on this common ground, which is that rules are specific and principles less specific or vague, and therefore soft law. The author would want to persist with this claim for the rest of the thesis, and this means restating the key claim in my introduction, which is that certain treaties may generate only principles but not rules, which do not have the strength of hard law. Such a treaty "may be potentially normative, but still 'soft' in character, because it articulates 'principles' rather than 'rules'".

The scholarly writing that some treaties may generate only principles but not rules, which do not have the strength of hard law, has piqued the above interest in the choice between rules and principles in the rule of law. Such a treaty, as earlier noted by Boyle, "may be potentially normative, but still 'soft' in character, because it articulates 'principles' rather than 'rules'".[37] I exemplify the reason for this by suggesting that soft law, in the form of principles, can function as vehicle for focusing consensus on the treaty obligations to criminalise ML and for mobilising a consistent general response for repressive and preventive AMLC. The reason

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33 Hart *The Concept of Law* in J. Braithwaite *supra* note 22 at 10.
34 H. L. A. Hart *The Concept of Law* (Oxford University Press, 2ed, 1994) p. 259.
35 Braithwaite *supra* note 22 at 6.
36 Raz *supra* note 28 at 834.
37 Boyle *supra* note 19.

for this is that it is not possible to capture every predicate offence[38] of ML in a single rule-based treaty obligation, as most states would prefer a situation where the law can be individuated to reflect their domestic AML legislation. Moreover, the policies and strategies against ML have as one of their prime objectives: the creation of an atmosphere of consensus regarding the AML measures to be implemented. This is in view of the fact that, the international AML law is not a universal homogeneous bloc, but is composed of several layers, some of which are universal and other regional.

1.2 The Research aim and objective for the thesis

The purpose of this thesis is to provide an assessment of soft law as a technique for repressive and preventive AMLC. To achieve the foregoing aim, the thesis has the following five research objectives:

1. To provide a conceptual framework to the study of ML by assessing the role of soft law as a technique for repressive and preventive AMLC.
2. To highlight the role of soft law as a tool for legal and regulatory harmonisation/convergence of international and domestic AML legislation, leading to greater cooperation in the global effort against ML.
3. To show that despite the effort to harmonise AML law – leading to greater convergence and international cooperation – the legal framework for international AMLC is still fragmented as shown in the variety of international and domestic legislation.
4. To illustrate the current limits of the legal response by proposing a uniform codification of AML legislation directed by a more representative body or commission of experts.

[38] The predicate offence for the Vienna Convention 1988 is Drug Trafficking, whilst for that of the Palermo Convention 2000, is Organised Crime. This is also different in the various domestic legislations of member states.

5. To contribute to the ongoing debate about the role of soft law as a new mode of governance in international relation by demonstrating the role of soft law in the regulation of global ML.

In light of the foregoing undertakings the initial approach to the research purpose is to examine the nature of the legal response to the problem of ML law by looking at the treaty and non-treaty AML obligations through a prism of two theoretical lenses (legal positivism and liberal/process theory) to explain the role of soft law in AMLC. The thesis, therefore, focuses heavily on understanding the nature of international AML law making process by looking at the role of soft law in global AMLC.

The phrase 'ML' brings to mind thoughts of an intriguing but reprehensible underworld.[39] It conjures up images of the Italian and Russian Mafia, the Colombian Cartels, terrorist groups, illegal gambling operations, and white-collar crime. The phrase, however, does not portray the sophistication, the breadth, and incongruities of the legal regime in the area. ML law is a complex legal field. It is a junction point for criminal law, regulatory law, banking law, international criminal law and administrative and criminal procedure. Each of these branches has its own concepts, problems, theories, and methods. In approaching the subject matter of AML law, one can be viewed as having two choices: either to treat the subject as a *sui generis* law or to approach it from within one of the areas of the law that it touches upon.[40]The first approach tends to generate technical studies that are useful for their

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39 H. Shams *Legal Globalisation: Money laundering law and Other Cases* (BIICL, 2004) p. 1.

40 *Ibid.*

purposes.[41]The second approach tends to produce technical or in-depth analysis of certain aspects of the law in terms of the field concerned.[42]

While these approaches to the study of the subject remains useful, current analyses of an AML law falls short of providing the conceptual framework that permits a better understanding of a *twin-track approach* that is based on repressing laundering offence and preventing it from entering into the legal economy. The *twin-track* approach to AMLC represents a repressive technique that is based on criminalisation and a preventive technique that is based on obligations of financial and non-financial institutions to undertake certain measures to disclose ML operations and to identify the 'beneficial ownership' of the object of crime. Both techniques are currently at the heart of recent international efforts to combat ML, as the initial attempt to criminalise ML through international treaties, has gathered momentum through an international collaborative effort to identify both the perpetrators and beneficiary/beneficiaries of the crime.

In the absence of such conceptual framework, the study of AML law will remain fragmented and limited to the individual subject areas that it touches. This thesis is thus an attempt to fill this gap in the study of AML law. It endeavours to provide a theoretical explanation that helps to identify the nature of the international AML treaty obligations and highlights the relevance of soft law as a technique for repressive and preventive AMLC. It is only through such theoretical analysis that the role of soft law as a tool for legal harmonisation and approximation of domestic AML law in the fight against ML can be better examined.

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41 See R. Booth *et al supra* note 4.

42 For the criminal justice perspective including substantive criminal law, criminal law enforcement, and international criminal cooperation see G. Stessens *supra* note 14. For a corporate and commercial law perspective see P. B. H. Birks (ed) *Laundering and Tracing* (Oxford OUP, 2003). For a discussion from an international law angle see B. Simmons International Efforts against Money Laundering in D. Shelton (ed) *supra* note 20, Shams *supra* note 39. For practitioners and regulators see R. Fox *et al A Practitioner's Guide to UK Money Laundering Law and Regulation: A Practical Guide* (London Thomson Reuters, 2010). See also J. D'Souza *Terrorist Financing, Money Laundering, and Tax Evasion* (Florida CRC Press, 2012), J. Blum *et al Financial Havens, Banking Secrecy and Money Laundering* available at ≤ https://www.amnet.co.il/attachments/UN-FINANCIAL%20HAVENS%20laundering.pdf> last visited on 18 April 2020 and Hatchard *et al Corruption and Misuse of Public Office* (2nd ed. OUP, 2011).

The thesis will focus on the role of soft law as a technique for repressive and preventive AMLC. Based on current analyses of the role of soft law as an alternative to hard law or as a complement to hard law, leading to greater cooperation, it attempts to outline the possible advantages and disadvantages that soft law could have in the context of AMLC. For example, the use of soft law promotes harmonisation of international AML standards through the FATF, while the role of the FATF remains unclear in international law. This is important for the purpose of responsibility, as the law on state responsibility clearly states when a State is responsible, in the event of a breach, and the consequence in international law.[43]

The thesis also seeks to identify factors specific to AMLC that might be important for the role of soft law. For example, it is suggested that the internationalisation and supranationalisation of ML have been driven by the belief that only through legal harmonisation and approximation of national law can the legal and regulatory loopholes be closed against the exploitation by transnational criminals. In the light of the foregoing, soft law is seen as a tool for legal and regulatory AMLC, given the territoriality of the criminal law and sovereignty of nation.

At the end, based on the assessment of soft law as a technique for AMLC, the thesis will propose a unification and progressive development of AML law under the aegis of the Hague Conference on Private International Law. It is hoped that by bringing the law under the aegis of Hague Conference on Private International Law, attempt would be made at progressive and systematic development of the law, which could then be used to address the current imbalance between what is classified as existing and emerging ML threats. This is important as current arrangements only highlight the danger of ML in such areas, as drug trafficking, corruption and certain transnational organised crime, with less emphasis on the peculiar needs of the individual state. Besides, the current work of the FATF is limited to the mandate given

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43 See M. N. Shaw *International Law* (Cambridge: Cambridge University Press, 2008) p. 694.

to it at any given time and prioritises only certain typologies. A global AMLC should not only prioritise ML typologies from Europe and America but should accommodate typologies from other regions of the world.

1.3 Methodology

In this thesis originality is demonstrated by a mixed methods approach combining doctrinal and interdisciplinary research methods to the study of ML. This is done by conducting macro-legal research on an assessment of soft law as a technique for preventive and repressive AMLC. Macro-legal analysis involves mixed methods research method because the author is examining the nature of the international legal response to the problem of ML and the role of soft law. Thus, the thesis focuses on understanding the nature of international AML law-making process. The approach toward this question is through a prism of two theoretical lenses (Legal positivism and liberal/legal process theory) to explain the role of soft law in the area. The approach suggested is that, whereas positivists take a narrow view of law as rules that regulate and constraint state behaviour, legal process scholars see law as facilitating and enabling international relations by providing modes of cooperation and legitimation, which is crucial to regulating ML.[44]

Legal process theory seeks to situate law in the political context; thus, law is not simply a system of rules to regulate state behaviour, but rather it is part of international policymaking processes. As Rosalyn Higgins, formerly of the London School of Economics and judge of the International Court of Justice puts it: "[t]his view rejects the notion of law merely as the impartial application of rules. International law is the entire decision-making process".[45] This view therefore recognises the role of soft law in the decision-making process, i.e., as a form of

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[44] D. Armstrong *et al International Law and International Relations* (New York: 2nd ed. CUP 2012) p. 97.

[45] R. Higgins, 'Policy, consideration and the international judicial process', *International and Comparative Law Quarterly* 17 (1968), 58 cited in D. Armstrong *et al supra* note 44 p. 93.

quasi-legal technical and policy agreements that prescribe behaviour for states, bureaucracies and private actors, but which are not, strictly speaking binding.[46]

The literatures considered in this thesis therefore provide two theoretical lenses through which to view the nature of the international AML treaty obligations and the role/function of 'soft law' as a technique for preventive and repressive AMLC. In generating each lens, we first conjure sources listed in Article 38(1) of the ICJ Statute, and from these identify the points of agreement that form the approach to the study of soft law, and in effect AMLC. We employ the foregoing approach to develop our concept of soft law by taking the formal and informal divide to explain our framework type of soft law and a further evaluation based on certain characteristics that vary along a continuum to amplify this concept.

In addition, since the research question of the thesis aims at assessing the role of soft law as a technique for repressive and preventive AMLC, the research will generally involve two different areas of law, namely, international law and ML. The primary focus is, however, on the assessment of soft law arguments raised in the field of international law scholarship to a particular area of law – the treaty AML obligations and informal AML arrangements.

A theoretical literature review concerning soft law from the perspective of international law is important not only for defining the scope of the subject matter, but also for setting out a conceptual framework for an assessment of soft law as a technique for AMLC in later chapters. The thesis takes the view that international law performs a broad range of functions. Whereas positivists take a narrow view of law as rules that regulate and constraint state behaviour, legal process scholars see law as facilitating and enabling international relations by providing modes of communication, legitimation, cooperation etc. This resonates with the rest of the thesis and restates the earlier claim that the international AML law is not just a universal homogeneous bloc, but is composed of several layers, some of which are universal and other regional.

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[46] D. Armstrong note 44 *supra* p. 99.

After examining available literature on soft law, the thesis develops a framework type of soft law largely based on binary categories between formal/treaty and informal/non-treaty-based AML obligations. The framework makes it clear what category of soft law (formal or informal) elements utilised in the area of AMLC will be examined in relation to its assessment as a technique for regulating ML.

The literature will cover all major international and regional AML instruments that are relevant. Besides existing AML instruments in force, the study will also examine the possibility of including other AML typologies that are currently not included in the existing formal and informal AML instruments. The limited time and resources available also lead to a methodology that confines the research work to drawing out relevant factors purely based on analysing the formal and informal AML obligation rather than empirical study of a particular typology or jurisdiction. As a result, the research is limited owing to the absence of quantifying the role of soft law in domestic AML perspective.

1.3.1 Doctrinal Research Methods

Doctrine has been defined as 'a synthesis of rules, principles, norms, interpretive guidelines and values' which 'explains, makes coherent or justifies a segment of the law as part of a larger system of law.[47]It follows that doctrinal research is research into the law and legal concepts.[48]Valid research is built on sound foundations, so before embarking on any theoretical critique of the law or empirical study about the law in operation, it is incumbent on the researcher to verify the authority and status of the legal doctrine being examined. The way to accomplish this is by using a doctrinal legal research method.[49]

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47 T. Mann, *Australian Law Dictionary,* South Melbourne, Victoria: (Oxford University Press, 2010) 197.

48 T. Hutchinson and N Duncan, 'Defining and Describing What We Do: Doctrinal Legal Research' *Deakin Law Review* 83(2012) at 85.

49 D. Watkins and M. Burton *Research Methods in Law* (2ed Routledge, 2017) p.9

Doctrinal method is normally a two-part process, because it involves first locating the sources of the law and then interpreting and analysing the text.[50]It is, therefore, the location analysis of the primary documents of the law in order to establish the nature and parameters of the law.[51] It is a distinctive part of legal research, and that distinctiveness permeates every other aspect of legal research which the identification, analysis and evaluation of legal doctrine is a basis, starting point, platform or underpinning.[52]

Critiques have questioned the importance of traditional doctrinal research in the face of growing interdisciplinary academic law scholarship. The reason for this perception – in legal scholarship – is based on the fact that traditional doctrinal method does not generate the excitement of the newer branches of legal scholarship.[53] However, despite this observation, doctrinal scholarship continues to dominate legal scholarship if one counts the number of articles, students note, treatises, casebooks, and textbooks, and even more so if one weights the number of publications by number of pages.[54]

Accordingly, Siems identifies four ways of being original in legal research:[55]first is by dealing with micro-legal questions; second is by pursuing research in macro-legal questions; third is by scientific legal research; and finally, is research in non-legal topics. In this thesis originality is demonstrated by conducting macro-legal research on an assessment of soft law as a technique for preventive and repressive AMLC. This thesis begins by identifying the concept of law under Article 38 of the International Court of Justice (hereinafter ICJ) and nature of the treaty and non-treaty response to the problem of ML in international law. The author then supplements this with micro-legal analysis by examining case law and domestic legislation to demonstrate the interaction of international soft law and domestic AML legislation.

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50 T. Hutchinson and N Duncan *supra* note 48 *at 110.*
51 *Ibid at 113.*
52 T. Mann, *supra* note 47 p.16
53 R. A. Posner The Present Situation in Legal Scholarship *The Yale Law Journal 90(5) (1981)* at 1117.
54 R. A. Posner Legal Scholarship Today *Harvard Law Review 115(5) (2002)* at 1317.
55 M. M. Siems Legal Originality *28(1) Oxford Journal of Legal Studies* at 147

1.3.2 Interdisciplinary Research Method

Interdisciplinary legal studies emerged as a response to the known traditional approach of studying the law until the 1960s[56].Posner observes that law has lost its original identity as an independent discipline.[57]He notes that until the 1960s, legal education and scholarship helped sustain autonomous legal thought, making law an autonomous discipline.[58] According to Posner, law is no longer a subject dominated by those training to be practising lawyers only. He noted therefore that law can no longer afford to function as an autonomous discipline because of the emergence of disciplines that clearly augment the discipline of law.[59] The Interdisciplinary approach, has been adapted by contemporary legal researchers as an important hybrid to the acquisition of legal knowledge.[60]

Accordingly, interdisciplinary legal studies refer to an approach to the development of legal scholarship based on information and methodology beyond the boundaries of law. This is an attempt by researchers to create opportunities for legal scholars to familiarise themselves with the methods and research culture from other discipline.[61] This requires an interaction which facilitates an examination of legal issues beyond the traditional approach and culture associated with law schools and legal studies.[62] Within the qualitative research framework, an interdisciplinary legal study becomes a choice where a study would require expansive sources of data beyond traditional legal sources to allow for contextual analysis of the dynamic involved.[63]

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56 S. Halliday, Judicial Review and Compliance with Administrative Law cited in L.A. Nkansah and V. Chimbwanda 'Interdisciplinary Approach to Legal Scholarship: A Blend from the Qualitative Paradigm' (2015) *Asian Journal of Legal Education* 3(1) at 55.

57 R. A. Posner, 'The Decline of Law as an Autonomous Discipline (1962-1987) HARV. L.REV.at 761

58 *Ibid* at 762.

59 *Ibid* at 767.

60 S. Halliday *supra* note 56 at 60.

61 D. W. Vick, 'Interdisciplinarity and the Discipline of Law (2004) 31(2) *Journal of Law and Society* at 164.

62 *Ibid* at 62.

63 *Ibid.*

In this thesis originality is further demonstrated by taking an interdisciplinary approach to the study of soft law because of the limits of traditional black letter research and the various ways in which soft law can be captured in international agreements.

1.4 Originality and Publication

Excerpt summarising this thesis has since been published in a peer review journal –Journal of Money Laundering Control (hereinafter JMLC) in 2016.[64] The published article has had over one thousand downloads and been cited nine times since its publication.

The author, therefore, takes a new, original approach to the study of ML by focusing on the nature, operation, and effectiveness of current international response to the problem of ML and AMLC; which adds to the body of research already undertaking in the area.

1.5 Outline of the Thesis

Together with chapter one and the conclusion, the thesis will be divided into seven chapters.

Chapter 2 mainly involves a theoretical analysis taking the perspective formal and informal divide to explain our framework type of soft law. This part includes not only a definition of 'soft law' and an analysis of the concept, but also it sets out a background for studying the role of soft law for the rest of the thesis.

Chapter 3 examines the history and development of the international AML regime, and its emergence from an initial treaty obligation to criminalise ML, the later internationalisation of ML and supranationalisation through the work of the FATF.

Chapter 4 examines the nature and role of existing repressive AML instruments: the Vienna Convention 1988, the Palermo Convention, the 1990 Money Laundering Convention, the UNCAC and the 2005 Council of Europe Convention against Money Laundering. It

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64 E. Ebikake *supra* note 2.

conceives the role of repressive AMLC in light of the obligations to criminalise the offence and confiscation of the proceeds of crime.

Chapter 5 also examines the nature and role of the preventive AML instruments: the FATF, the Basel Committee on Banking and Supervisory Practices, the various EC Directives and other initiatives in the area. It elaborates on the informal nature of the preventive AML arrangements and their role.

Chapter 6 highlights the role of Financial Intelligence Unit (FIU) as a tool for informal cooperation under existing arrangements. It demonstrates the new and emerging method of international evidence gathering through soft law, and the role of the FIU in the prevention and repression of ML.

Chapter 7 is concerned with the internationalisation of ML and the jurisdictional consequences. The chapter explore this development by looking at the relative importance of criminalisation as a treaty-based initiative and the subsequent development of the law as the legal basis for asserting jurisdiction.

The conclusion examines the role of soft law as a tool for legal harmonisation, and the relevance of this to the prevention and repression of ML. The conclusion also proposes a unification and progressive development of AML law under the aegis of the Hague Conference on Private International Law and suggests a new Hague type convention for ML.

CHAPTER TWO

Identifying Soft Law

2.1 Introduction

As formulated in the Statute of the Permanent Court of International Justice (hereinafter PCIJ),[65] the Court should decide an international dispute primarily through application of international conventions and international custom. This remains the same under Article 38 of the Statute of the International Court of Justice (hereinafter ICJ)[66]. Even though the Statute of the ICJ is directed at the Court, it represents a general text in which states have articulated the authoritative procedures by which they agree to be legally bound to an international norm. Treaties and custom must, therefore, be recognised by scholars and other non-state actors as the means states have chosen to create international legal obligations for themselves.

However, the question is whether it is possible to explain the product of contemporary international *law-making processes* within the terms of Article 38 (1) of the Statute of the ICJ. The greater number of multilateral instruments containing compulsory or optional dispute resolution clauses has ensured that judicial tribunals have had greater opportunity both to amplify the understanding of how international law derives from the sources listed in Article 38(1) of the ICJ Statute and to have developed substantive rules and principles.[67] For example, the political processes involved in the creation of international courts and the negotiation of dispute settlement clauses in treaties significantly affect the discretion left to adjudicate in determining the substantive law they are to apply. The widest discretion is accorded by Article

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65 Available at ≤Statute of the Court | International Court of Justice (icj-cij.org)≥ visited on 2 February 2021. General principles of law are a third, more rarely used, source of international law, with judicial decisions and teachings of highly qualified publicist providing evidence of a norm. For the present Court, see article 38, Statute of the International Court of Justice.

66 United Nations, *Statute of the International Court of Justice*, 18 April 1946, available at: ≤www.refworld.org/docid/3deb4b9c0.html≥visited on 12 December 2020.

67 A. Boyle and C. Chinkin *The Making of International Law* (New York OUP, 2007) p. 272.

38(2) of the Statute of the ICJ, which envisages that with agreement of the parties the Court may decide a case according to what is equitable and good– in effect a decision not necessarily based on legal rules.[68]

Although the above choice has never been exercised, states have sometimes agreed that a dispute will be adjudicated on the basis of rules that are not yet law. Thus in the *Tunisia–Libya Continental Shelf* case the *compromise* provided that the Court would apply international law including the recent trends admitted at the Third Conference on the Law of the Sea.[69] The 1982 United Nations Convention on the Law of the Sea (hereinafter UNCLOS) makes reference for this purpose to "generally accepted international rules and standards established through the competent international organisation or general diplomatic conference".[70]The applicable law here include related treaties and soft law instruments, which set standards with which the parties to the principal treaty are required to conform.

This is perhaps the most important lesson to be drawn from the ICJ's reference to sustainable development in the Case Concerning the *Gabcikovo-Nagymaros Dam.*[71] Even if sustainable development is not in the nature of a legal obligation, it does represent a policy goal or principle that can influence the outcome of litigation and the practice of states and international organisations, and it may lead to significant changes and developments in the existing law.[72] In the foregoing sense, international law appears to require states and international bodies to take account of the objective of sustainable development, and to establish appropriate processes for doing so. What these examples show is that subtle changes

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68 This point was referenced in Charlesworth, H. Law-making and sources. In J. Crawford & M. Koskenniemi (eds.), *The Cambridge Companion to International Law* (Cambridge Companions to Law, pp.187-202). Cambridge: Cambridge University Press, 2012) p. 189.

69 (1982) ICJ Reports 18.

70 Article 211 (2). See also Article 207, 208, and 210.

71 *Hungary* v. *Slovakia* (1997) ICJ Reports 7, para 140.

72 See for example the inclusion of provisions on sustainable use or sustainable development in the 1994 WTO Agreement, the 1995 UN Fish Stocks Agreement, and the 1997 UN Convention on International Watercourses.

in the existing law and in existing treaties may come about through the application of non-legal measures.

The legal positivist,[73] seeking rules deriving from state consent will tend to adhere to recognisable sources of authority, treaties and custom, and will give weight to those other sources identified in the Statute of the ICJ, Article 38(1). However, the adherent to the New Haven (Yale) policy science approach to international law focuses not on rules but explicitly on the *processes* by which legal decisions and policies are made.[74]Unlike the positivist view, under the New Haven approach the decision-making process that generates international law is not limited to states or the actions of states officials. Instead, it looks at "the aggregate actual decision process, comprised, as it is, of governments, inter-governmental organisations, non-governmental organisations. . . [a]ll the actors, who assess, retrospectively or prospectively, the lawfulness of international actions and whose consequent reactions shape the flow of events, now constitute, in sum, the international legal decision process."[75]

In 2004, in its Report on the United Nations (UN) Reform, [76]the High-Level Panel on Threats, Challenges and Change called for the development of international regimes and norms, and of new legal mechanisms where existing ones were deemed inadequate for responding to the threats to collective security that it had identified. In this thesis, the author commences the discussion by examining soft law as a form of international law-making process, in response to the particular threat of global ML. However, before examining the role

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73 Positivism is a label for a whole array of differing approaches to international legal theory. See *supra* note 16.

74 For a concise, account of the New Haven approach, see M. Reisman, 'The View from the New Haven School of International Law' (1992) *ASIL Proceedings* 118.

75 M. Reisman, 'Unilateral Action and the Transformation of the World Constitutive Process: The Special Problem of Humanitarian Intervention', 11(2000) EJIL at 121. For a profound and compelling literature on this view, see the work of R Higgins *Theme and Theories: Selected Essays, Speeches, and Writings in International Law* (New York, OUP 2009) pp. 19–43. For an earlier thought on the subject by this author, see R. Higgins *Problems and Process: International Law and How We Use It* (New York, OUP 2007).

76 *A More Secure World: Our Shared Responsibility*, Report of the High-Level Panel on Threats, Challenges and Change, UN Doc A/59/565, 2 December 2004 cited in A. Boyle and C. Chinkin *supra* note 67 p. 1.

of soft law in the context of international AMLC, it may be helpful to identify the subject of soft law in international law.

According to Dupuy the term 'soft law' was coined by McNair, and since the 1970's has become relatively widespread and controversial at the same time.[77] Opinions, however, abound on the legal nature of soft law in international law, and jurists have come up with different interpretations of soft law. Some restrict the term soft law to norms in legally binding form, usually created by treaties but with vague content or weak requirements,[78] while others concentrate on the non-legal form of the instrument, such as declaration,[79] resolutions,[80] codes of conduct[81] and recommendations.[82]

In addition, there is considerable disagreement in the existing literature on the definition of soft law. Positivist legal scholars tend to deny the very concept of 'soft law' since law by definition, for them, is 'binding'. According to Klabber "law cannot be more or less binding,

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77 R. J. Dupuy, *Declaratory Law and Programmatory Law: From Revolutionary Custom to 'Soft Law'*- in 'Declarations on Principles. A Quest for Universal Peace' cited in J. Sztucki Reflections on International Soft Law (1990) DE LEGE (UPPSALA) p. 549. Also cited in R. J. Akkerman, *et al* (eds) *Declarations on Principles, a Quest for World Peace (Liber Riling)* (1977) Sijthoff, Leyden pp. 247-257

78 On the meaning of soft law under this category see: L. Blutman 'In the trap of a legal metaphor: international soft law' (2010) *International and Comparative Law Quarterly* 1; Boyle and Chinkin *supra* note 67 p. 851; J. Sztucki 'Reflections on International Soft Law' (1990) *De lege* (Uppsala) at 551 and Boyle 'Some Reflections on the relationship of treaties and soft law' (1999) *International and Comparative Law Quarterly* at 906.

79 Declaration is generally issued by states to express their will, intent or opinion regarding certain international issues. This can be made through an international conference on the particular subject in question, or through an international organisation. Examples here include the 1948 Universal Declaration of Human Rights by the United Nations General Assembly (UNGA) ≤www.un.org/en/documents/udhr/history.shtml≥ visited on 14 December 2020; the 1990 Cairo Declaration on Human Rights in Islam available at ≤www.refworld.org/docid/3ae6b3822c.html≥ visited 14 December 2020; the 2000 United Nations Millennium Declaration available at ≤ http://en.wikisource.org/wiki/United_Nations_Millennium_Declaration≥ last visited 14 December 2020.

80 An example of a non-binding resolution is the United Nations General Assembly Resolution (UNGA). Article 10 and 14 of the United Nations Charter, 1945, refers to UNGA resolution as mere 'recommendations.' This should be contrasted with Article 25 of the United Nations Charter, 1945, which provides that United Nations member states are bound to carry out "decisions of the Security Council in accordance with the present charter".

81 A code of conduct may be referred to as a set of rules outlining the responsibilities of or proper practices for an individual party or Organisation. Examples here include the Code of Conduct for International Red Cross and Red Crescent Movement and NGOs in Disaster Relief, the ICC Cricket Code of Conduct etc.

82 A recommendation refers to a suggestion or proposal as to the best course of action. Example of non-binding recommendations in international law includes the UNGA resolutions or the International Recommendations for Water Statistics (IRWS). The IRWS is a statistical intermediate output framework developed by the United Nations Statistics Division (UNSD) and approved by the United Nations Statistical Commission (UNSC) that was designed for guiding countries in the development of their water information systems to design and evaluate policies for better water management.

so that the soft law concept is logically flawed".[83] Weil takes a normative approach, arguing that the increasing use of soft law represents a shift pursuant to which international law norms vary in their relative normativity, and he finds that this trend "might well destabilise the whole international normative systems and turn it into an instrument that can no longer serve its purpose".[84]

Positivist legal scholars find that soft law is inferior to hard law because it lacks formally binding obligations, which are interpreted and enforced by courts, and it thus fails to generate jurisprudence over time.[85] For this reason, these scholars view soft law as a second-best alternative to hard law, either as a way station on the way to hard law, or as a fall back when hard law approaches fail.[86] John Kirton and Michael Trebilcock, for example, in a volume regarding the use of hard and soft law in global trade, environment, and social governance, found "strong support for the familiar feeling that soft law is a second-best substitute for a first-best hard law, being created when and because the relevant hard law does not exist and the intergovernmental negotiations to produce it have failed".[87]

Rational institutionalist scholar's response was that "the term binding agreement [in international affairs] is a misleading hyperbole".[88] They nonetheless find that the language of 'binding commitments' matter because through it states signal the seriousness of their commitments, so noncompliance entails greater reputational costs.[89] Guzman opined that, "an agreement is soft law if it is not a formal treaty". [90]He finds that states rationally choose soft

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83 J. Klabbers, 'The Redundancy of Soft law' (1996) 65 *Nordic Law Journal of International Law* at 181.

84 P. Weil, 'Towards Relative Normativity in International Law? (1983) *American Journal of International Law* at 413, 423.

85 *supra*.

86 J. Klabbers, 'The Undesirability of Soft Law' (1998) 67 *Nordic Journal of International Law* at 382.

87 J. J. Kirton and M. J. Trebilock, *Introduction to HARD CHOICES, SOFT LAW: VOLUNTARY STANDARDS IN GLOBAL TRADE, ENVIRONMENT, AND SOCIAL GOVERNANCE* cited in cited in G. C. Shaffer and M. A. Pollack 'Hard vs Soft Law: Alternatives, Complements, and Antagonists in International Governance' (2009-2010) 94 Minn. L. Rev. at 724.

88 C. Lipson, 'Why Are Some International Agreements Informal?' (1991) 45 Int'l Org. 495, 508.

89 *Ibid*.

90 A. Guzman 'The Design of International Agreements' (2005) 16 EUR. J. INT'L. at 591 ft 56.

law because they wish to reduce the cost to their reputation of potentially violating the soft law in light of uncertainty.[91]

Abbott and Snidal, taking a rational institutionalist political economy approach, focus on varying states interests in different contexts. They contend that, states sometimes prefer hard law and other times prefer soft law to advance their joint policy aims.[92] In their work on 'pathways to cooperation', they nonetheless define three pathways, two of which explicitly involve the progressive hardening of soft law.[93] The three pathways are the use of a framework convention, which subsequently deepens in the precision of its coverage; the use of a plurilateral agreement, which subsequently broadens in its membership; and the use of a soft-law instrument, which subsequently leads to binding legal commitments.[94]

Allied to this is Abbott *et al*'s definition of legalisation in international relations.[95] The approach adopted was to illustrate the wide variety of international legal arrangements by developing a typology that characterises different instruments in terms of their precision, binding legal obligation and delegation along a continuum. Legalisation is thus, defined as varying across three dimensions – precision of rules, obligation, and delegation to a third-party decision maker – which taken together can give laws a 'harder' or 'softer' legal character.[96] In this respect, hard law "refers to legally binding obligations that are precise (or can be made precise through adjudication or the issuance of detailed regulations) and that delegate authority for interpreting and implementing the law".[97]

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91 *Ibid* at 582.

92 K. W. Abbott and D. Snidal, 'Hard and Soft Law in International Governance' (2000) 54 (3) INT'L ORG at 421-456.

93 K. W. Abbott and D. Snidal, 'Pathway to International Cooperation'. In The Impact of International Law on International Cooperation: Theoretical Perspectives (Cambridge University Press, 2004) p.50-84

94 *Ibid.*

95 K. W. Abbott *et al* 'The Concept of Legalisation' (2000) 54 (3) INT'L ORG at 401-419.

96 D. Trubek *et al* 'Soft Law, Hard Law and EU Integration, in LAW AND NEW GOVERNANCE IN THE EU AND THE US' cited in Shaffer and Pollack *supra* note 87 at 714.

97 K. W. Abbott and D. Snidal *supra* note 92 at 421.

In contrast, to this ideal type of hard law, soft law is defined as a residual capacity: "the realm of 'soft law' begins once legal arrangements are weakened along one or more of the dimensions of obligation, precision, and delegation".[98] Thus, if an agreement is not formally binding, it is soft law along one dimension. Similarly, if an agreement is formally binding but its content is vague so that the agreement leaves almost complete discretion to the parties as to its implementation, then the agreement is soft along a second dimension. Finally, if an agreement does not delegate any authority to a third party to monitor its implementation or to interpret and enforce it, then the agreement again can be soft (along a third dimension). This is because there is no third party providing a 'focal point' around which parties can reassess their positions, and thus the parties can discursively justify their acts more easily in legalistic terms with less consequence, whether in terms of reputational costs or other sanctions.

Constructivist scholars, in contrast, focus less on the binding nature of law at the enactment stage and more on the effectiveness of law at the implementation stage, addressing the gap between the law-in-the-books and the law-in-action. They note how even domestic law varies in terms of its impact on behaviour, so that binary distinctions between binding hard law and nonbinding soft law are illusory.[99] However, constructivist, like legal process theory, acknowledge the broad functions of international law and consistent with legal process theory, international law is conceived in terms of a process involving transnational networks of governmental and non-governmental actors.[100]This view permits the role of soft law in authoritative decision-making process.

There are, thus, scholars who evaluate hard and soft law in terms of a binary binding/non-binding distinction and those who evaluate it based on characteristics that vary along a continuum.[101] The difference between these scholars depends on whether they address

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98 *Ibid.* at 422.
99 *Supra* note 95 at 713.
100 D. Armstrong *et al supra* note 44 pp. 109-110.
101 Shaffer and Pollack *supra* note 87 at 715.

international law primarily from an *ex-post* enforcement perspective or an *ex-ante* negotiating one. From an *ex-post* enforcement perspective, legal positivists are right when they state that, to a judge, a given instrument is either legally binding or non-binding. However, from an *ex-ante* negotiation perspective, actors have choices that, in practice, can render agreements relatively more or less binding in the ways Abbott and Snidal note.[102]

In this thesis, the author takes an interdisciplinary approach to the study of soft law. First, he takes the positivist perspective (binding and non-binding) to highlight the difference between hard and soft law. However, he employs the term formal and informal to explain our framework type of soft law, building on Abbott and Snidal evaluation (based on certain characteristics that vary along a continuum) to amplify this concept. The reason for such an interdisciplinary approach to the study of soft law is that resort must be taken of the various ways in which soft law can be captured in international agreements. In examining the role of soft law, attention must be given to the interaction between different types of instruments as well as between hard law and soft law instruments. In agreement with scholars from legal process theory, he acknowledges the fact that international law fulfils a broad range of functions permitting states and other actors to communicate and cooperate thereby situating law in broader socio-political context beyond rule-based obligation.

Thus, hard law in this thesis refers to formally binding rules that create definitive rights or obligations on the parties. This definition only applies to international agreements[103] and not to customary international law or general principles of law. Norms in these latter categories are either international law or not, depending on whether the norm in question meets the relevant

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[102] K. W. Abbott *et al supra* note 95.

[103] States negotiate the Vienna Convention on the Law of Treaties, 1969, to govern the most formal of international agreements between parties.

mark of identification.[104] Soft law, in comparison to hard law, is defined as rules of conduct formulated in formal or informal instruments, which lack certain core elements of hard law. As rules of conduct formulated in informal instruments, they are characterised as non-binding, emanating from bodies lacking international law-making authority, directed at non-state and are of a voluntary nature with no corresponding theory of responsibility in international law. However, the reverse is the case with soft law formulated in formal instruments, as the distinguishing mark between soft law in this category and hard law is the fact that they contain vague and imprecise terms.[105]

An obligation is, therefore, soft law in the sense that either it adopts an informal/non-binding form, or it contains vague, imprecise, or ambiguous provisions embodying merely a language that is hortatory, aspirational or promotional in character. The foregoing definition of soft law underscore the type of instruments employed in the preventive and repressive AMLC. The chapter will thus, develop a framework type of soft law along the foregoing line, which will then be employed when assessing the type of instrument in the international AMLC, in later chapters. Apart from developing a framework type of soft law, the chapter will also examine the reason for the choice of soft law to hard law in international commitments. The aim here is to demonstrate the inappropriateness of hard law in certain situations. For example, soft law may be preferred to hard law, where the latter is inappropriate or an effective response to the issue is not yet identified in the area. Lastly, the chapter will address the benefit of soft law as a tool for legal harmonisation and challenge.

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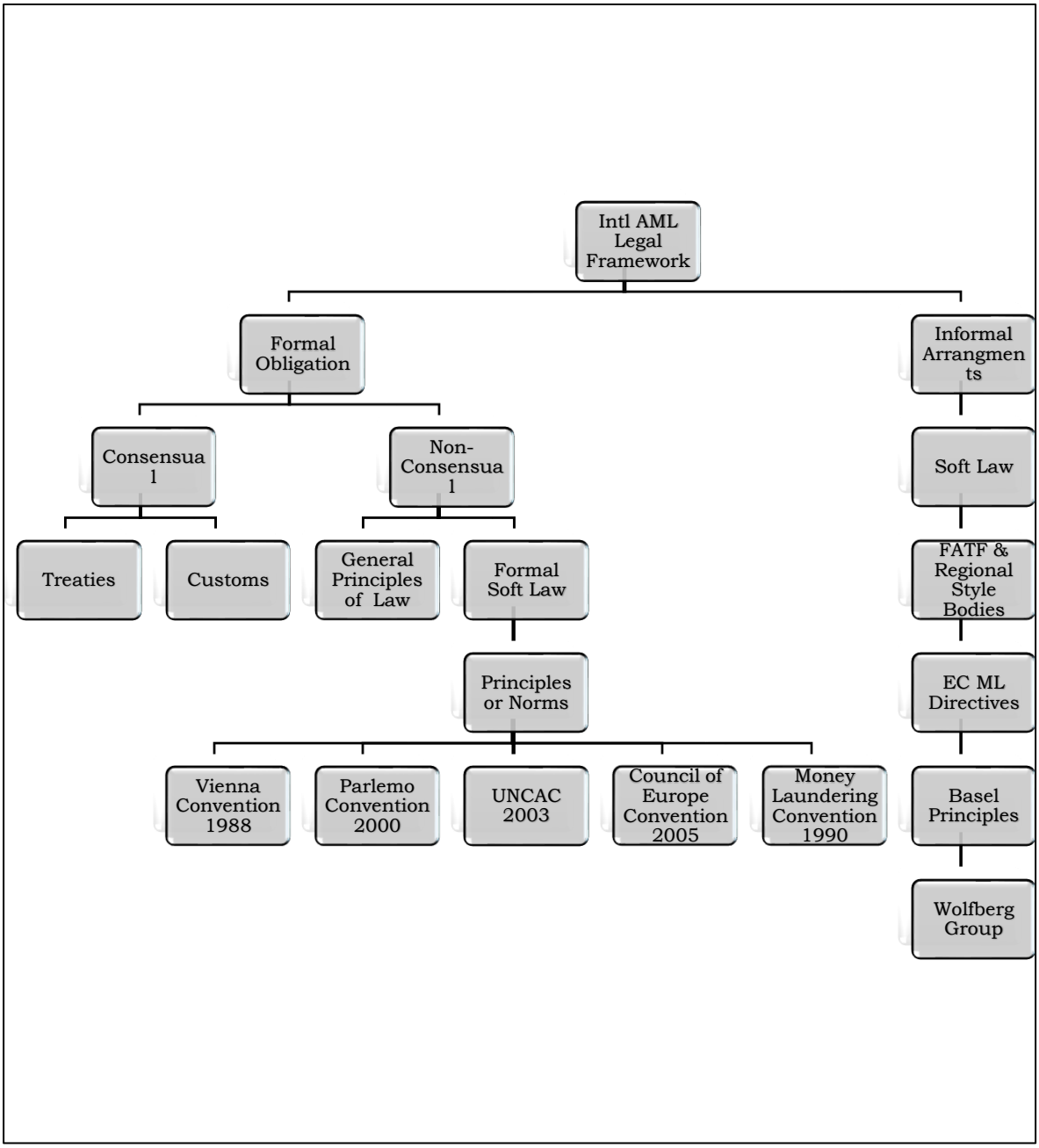
104 Following Article 38(1) (b) of the Statute of the ICJ, Customary International Law (CIL) apart from widespread consistent state practice ICJ Reports p. 3 must also be supported by *Opinio Juris necessitates*; the subjective intention or belief on the part of states to accept certain patterns of state practice as being obligatory as a matter of law. See generally *Fisheries Jurisdiction (Merit)* Case (1974) ICJ Reports, p. 3 and the *North Sea Continental Shelf Cases* (1969) ICJ Reports, p 3.

105 See pp 25-28 on the difference between rules and principles in legal discussion.

GRAPHIC REPRESENTATION OF FORMAL AND INFORMAL AMLC



2.2 Formal Soft Law

The concept of formal soft law refers to treaty provisions that do not tend to create definitive obligations, despite their legally binding form but are rather imprecise or flexible in character. This was the point noted by Baxter when he argued that some treaties are soft in the sense that they impose no real obligations on the parties.[106] Boyle is more poignant on this point when he stated that clear and reasonably specific rules are hard law, while 'norm' or 'principle', which are open textured or general in their content and wording, are seen as soft law.[107] Scholars holding such view persist that "the conclusion of an agreement in treaty form does not ensure that a hard obligation has been incurred".[108] Treaties with imprecise, subjective, or indeterminate language have been termed 'legal soft law' in that they fuse legal form with soft obligations.[109]

Some writers, however, reject this claim arguing that the treaty form is conclusive binding obligation.[110] Opinions like this would find support in Article 26 of the Vienna Convention on the Law of Treaties 1969 (hereinafter VCLT 1969), where the legal form of a treaty under the convention is conclusive of its binding nature upon the parties.[111] A compromise position is that a treaty with soft provisions creates an obligation of good faith performance,[112] although this is barely borne out by state practice.

The foregoing observation is represented in a growing number of treaty provisions. The framework Convention on Climate Change provides a good example. Adopted at the Rio Conference in 1992, this treaty does impose some commitments on the parties, but its core

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106 R. R. Baxter, 'International Law in 'Her Infinite Variety'' (1980) 29 Int'l & Comp. L. Q. 549.
107 A. Boyle *supra* note 19 p. 32.
108 C. Chinkin, *Normative Development in the International Legal System* in D. Shelton *supra* note 20 p. 25.
109 *Ibid* p 26.
110 C. Ingelse, 'Soft Law' in D. Shelton *supra* note 20 p. 26.
111 Article 2(1)(a) of the VCLT, 1969, defines a treaty as follows: "An international agreement concluded between States in written form and governed by international law, whether embodied in a single instrument or in two or more related instruments and whatever its particular designation".
112 *Supra*.

articles, dealing with policies and measures to tackle greenhouse gas emissions, are so cautiously and obscurely worded and so weak that it is uncertain whether any real obligations are created.[113] Moreover, whatever commitments have been undertaken by developing states are also conditional on performance of solidarity commitments by developed state parties to provide funding and transfer of technology.[114] More of a political bargain than a legal one, these are 'soft' undertakings of a very fragile kind. They are not normative and cannot be described as creating 'hard rules' in any meaningful sense.[115] This is a point recognised by the International Court of Justice (ICJ) in the *North Sea Continental Shelf* Case when it specified that one of the conditions to be met before a treaty could be regarded as law-making is that it should be so drafted as to be 'potentially normative' in *character*.[116]

There is, however, a second and more significant sense in which a treaty, like a non-binding resolution or declaration, may be potentially normative, but still 'soft' in character, because it articulate 'principles' rather than 'rule'. Here, it is the formulation of the provision which is decisive in determining whether it is hard or soft, not its form as a treaty or binding instrument. An example of a soft formulation, which nevertheless has binding form is, Article 87(2) of the 1982 UNCLOS, providing that high seas freedoms "shall be exercised by all states with due regard for the interests of other states in their exercise of the freedom of the high seas". What is meant by 'due regard' for the interests of other states will necessarily depend on the particular circumstances of each case and in that sense the provision is more of a 'principle' than a 'rule'.[117]

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113 Especially Article 4(1) and (2). The parties determined at the first meeting in 1995 that the commitments were inadequate, and they agreed to commence negotiation of the much more specific commitments now contained in the 1997 Kyoto Protocol.

114 Article 4(7).

115 Boyle *supra* note 19.

116 (1961) ICJ Report 3.

117 See *Fisheries Jurisdiction Cases* (1974) ICJ Reports 3 and 175; *Nuclear Tests Cases* (1974) ICJ Reports 253 and 457.

The Convention on Climate Change once again provides other good examples of such principles explicitly included in a major treaty. Indeed, given how week the rest of the treaty is, the principles found in Article 3 are arguably the most important 'law' in the whole agreement because they prescribe how the regime for regulating climate change is to be developed by the parties. The main elements of this provision provide thus:

"In their actions to achieve the objective of the Convention and to implement its provisions, the parties shall be guided, *inter alia,* by the following:

1. The Parties should protect the climate systems for the benefit of present and future generations of humankind, on the basis of equity and in accordance with their common but differentiated responsibilities . . .
2. The Parties should take precautionary measures to anticipate, prevent, or minimise the causes of climate change and mitigate its adverse effects . . .
3. The Parties have a right to, and should, promote sustainable development. . ."

These elements of Article 3 are not expressed in obligatory term: the use of 'should' qualifies their application. The obligations are open textured in the sense that there is considerable uncertainty concerning their specific content and they leave room for interpretation and elaboration. They are not like rules requiring states to conduct an environmental impact assessment, or to prevent harm to other states.[118]

In addition, certain treaties whereby states enter into alliance, agree to co-ordinate their military action, declare the neutrality of an area, or lay out their agreed policies for the future have sometimes been characterised as 'political treaties'.[119] They are referred to as soft law, as they are merely political agreements and concluded with no expectation of effective

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118 Boyle and Chinkin *supra* note 67 p. 222.
119 Baxter *supra* note 106 at 550.

enforcement. The most quoted in this category are the 1973 Agreement on the Prevention of Nuclear War between the United States and the Soviet Union and the Yalta Agreement.[120]

According to Dupuy, that an agreement is soft or hard law does not refer to the formally binding character of the instrument. Here the 'softness' of the instrument corresponds to the 'softness' of its contents.[121]

2.3 Informal Soft Law

Apart from the above classification of soft law, states may deliberately eschew the form of legally binding treaty form and reach agreement in diverse non-treaty form, such as memoranda of understanding, joint communiqués, minutes, or gentlemen's agreements.[122] A variety of motives influences the choice of form in this context. Participants may choose informal or non-binding agreement to avoid national legal requirements for the incorporation of treaties, or international provisions relating to treaties, such as registration pursuant to the United Nations Charter, Article 102. The choice also may reflect the need for ease of amendment and terminations,[123] or a desire simply to buy time.

Soft law under this category is represented in several agreements. For example, the Helsinki Final Act[124] was deliberately drafted as a legally non-binding document,[125] although

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120 Although the Yalta Agreement was published by the State Department in the Executive Agreements Series (No.498) and was also published in the U.S. Treaties in Force (1963), the State Department stated to the Japanese Government that "the United States regards the so-called Yalta Agreement as simply a statement of common purposes by the heads of the participating governments and . . . not as of any legal effect in transferring territories – cited in O. Schachter 'The Twilight Existence of Nonbinding International Agreements' (1977) 71 Am. J. Int'l L. 298.

121 P. M. Dupuy 'Soft Law and the International Law of the Environment' (1990-1991) 12 Mich. J. Int'l L. 429.

122 D. Shelton *supra* note 20 p. 28.

123 The ICJ affirmed that treaty law does not allow for unilateral termination: Case Concerning the *Gabcikovo-Nagymaros Project (Hungary/Slovakia),* 1997 ICJ Rep. (Judgement of September 25).

124 The full name is the Final Act of the Conference on Security and Cooperation in Europe. The text of the document signed in Helsinki on August 1, 1975, is reproduced in 14 ILM 1293 (1975) and in 73 DEPT. STATES BULL 323 (1975) cited in O. Schachter *supra* note 120 at 297.

125 S. Bastid, 'The Special Significance of the Final Act' in T. Beurgenthal (ed), *The Effectiveness of International Decision* (1977) 11 cited in C. Chinkin *supra* note 108.

reliance upon it through the Conference on Security and Cooperation in Europe (OSCE),[126] and especially by non-state actors, far exceeded that accorded to binding instruments. In this example, the Heads of State and other 'High Representatives' of thirty-five countries signed the texts, covering sixty printed pages, after declaring in the last paragraph "their determination to act in accordance with the provisions contained in the above texts".[127] Another paragraph, among the final clauses, requests the Government of Finland to transmit to the Secretary-General of the United Nations the text of the Final Act "which is not eligible for registration under Article 102 of the Charter of the United Nations".[128] This clause was further clarified by a letter sent by the Government of Finland to the Secretary-General of the United Nations stating that the Final Act is not eligible for registration under Article 102 "as would be the case were it a matter of a treaty or an international agreement, under the aforesaid Articles".[129] Statements by delegates during the Conference, notably by the United States and other Western delegations expressed their understanding that the Final Act did not involve a 'legal' commitment and was not intended to be binding upon the signatory powers.

An important observation, in relation to the Helsinki Act, is that the parties did not intend for the agreement to be formally binding, as would a treaty. Put more formally, a treaty or international agreement is said to require an intention by the parties to create legal rights and obligations or to establish relations governed by international law. If that intention does not exist, an agreement is considered to be without legal effect.[130]

Of similar importance in this category is the 1993 Middle East peace process, reactivated by a political agreement between Israel and the PLO. Although the Declaration of

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126 V. Dronov, 'From CSCE to OSCE: Historical Retrospective', in M. Evans (ed), *Aspects of Statehood and Institutionalism in Contemporary Europe* (1997) 105 cited C. Chinkin *supra* note 108 ft 34.

127 14 ILM 1325 (1975) cited in Schachter *supra* note 120.

128 *Ibid.*

129 *Ibid.*

130 *International Status of South-West Africa Opinion* [1950] ICJ Rep. 128 at 140.

Principles on Interim Self-Government Arrangements in many ways mirrored a Peace Treaty, the lack of Palestinian statehood ensured the Declaration's non-treaty status.[131]

During the 1990s, a multiplicity of non-binding instruments in the form of declarations, agendas, programs, and platforms for action emanated from global conferences.[132] The subject matter of these conferences – human rights, population, environment, development, human habitation, the empowerment of women – could suggest that issues of social justice are deemed by states perhaps too intrusive into domestic jurisdiction to be the subject of binding obligations. Despite high governmental participation in the conferences and preparatory meetings, the normative weight of the final conference documents were uncertain.[133] Usually, they have been adopted only after heated negotiations, and have been subject to reservations and interpretive statements, a development somewhat inconsistent with their non-binding character.[134] The texts are both declaratory and programmatic, targeting governments, international organisations, and non-governmental organisations (NGOs) for future actions. They cut across established legal categories in ways that may shape future international legal discourse.[135] NGO fora have been held parallel to each of these conferences, attended by representatives of international NGOs, ensuring maximum publicity for the official proceedings.

Perhaps the most controversial claimants to international soft law status are those that emanate neither directly nor indirectly from states but are nonetheless intended to modify

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131 K. Meighan 'The Israel-PLO Declaration of Principles: Prelude to a Peace?' (1994) 34 Va. J Int'l L 435 at 448-59 cited C. Chinkin *supra* note 108.

132 This includes the World Summit for Children, New York 1990; the World Conference on the Environment and Development, Rio de Janeiro, 1992; the World Conference on Human Rights, Vienna, 1993; the International Conference on Population and Development, Cairo, 1994; the World Summit for Social Development, Copenhagen, 1995; the Fourth World Conference on Women, Beijing, 1995; and the Habitat II, Istanbul, 1996.

133 D. Shelton *supra* note 20 p. 28.

134 *Ibid.*

135 For example, the Beijing Platform for Action emphasises the linkages between armed conflicts, other forms of violence, civil and political, and economic, social, and cultural rights, sustainable economic development, equality between women and men, political power-sharing, and accountability. Cited in C. Chinkin *supra* note 108.

transnational behaviour. Private norm-making initiatives such as the MacBride and Sullivan Principles,[136] statements of principles from individuals in non-governmental capacity, texts prepared by expert groups,[137] the establishment of 'people' tribunals,[138] and self-regulating codes of conduct for networks of professional peoples[139] and corporations come within this category. The use of the non-legal form is dictated by lack of formal law-making capacity and the impact of a non-binding text depends upon the political and economic interests of the relevant players.

Of similar importance in this category is the role of standards or voluntary best practice in global regulation in the field of International Relations. The starting point of this approach is the proposition that global governance is characterised by a shift to soft regulation, which involves global regulators of all kinds frequently creating world order by setting voluntary standards.[140] Hulsee and Kerwer in an article on global standards hinted on the role of standards in global AMLC in reference to the then 40 + 9 FATF Recommendations as standards in the sense of the organisation theory featured in International Relations.[141]The force of the argument in this example is the fact that the FATF has backed up its voluntary standards with enforcement mechanism, particularly in relation how the Recommendations are enforced globally against non-member – an area that will be further considered in chapter 5 of this thesis.

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136 C. McCrudden 'Human Rights Codes for Transnational Corporation: What can the Sullivan and MacBride Principles Tell Us (1999) 19 *Oxford Journal of Legal Studies.* The Sullivan and MacBride Principles focused primarily on labour standards, particularly equality of employment of opportunities, in, respectively, South Africa and Northern Ireland. They are examples of attempts at transnational regulation of the workplace activities of employers. The Global Sullivan Principles of Corporate Social Responsibility available at http://hrlibrary.umn.edu/links/sullivanprinciples.html#:~:text=The%20objectives%20of%20the%20Global,and%20boards%3B%20to%20train%20and last visited on 27 July 2020.

137 For example, the Helsinki Rules on the use of international rivers prepared by the International Law Association.

138 A. Cassese, *International Law in a Divided World* (1986) p. 169 cited in Shelton *supra* note 20 p.21.

139 For example, the ICC Cricket Code of Conduct available at ≤ https://www.icc-cricket.com/about/cricket/rules-and-regulations/code-of-conduct> last visited on 20 April 2020.

140 R. Hulsse and D. Kerwer 'Global Standards in Action: Insights from Anti-Money Laundering Regulation' (2007) 14(5) *Organisation* at 626.

141 Ibid at 628.

Overall, it is possible to conclude that the formal and non-formal categorisation of soft law is neither absolute nor exempt from objections. Nor does this categorisation intend to draw a sharp distinction between those soft law instruments that create legal rights and/or obligation and those which do not create any legal rights and/or obligation. The emphasis is rather on the often-present gradual continuum between lesser and higher degrees of normative specificity.[142] In sum, the criteria used to identify 'soft law' cannot solely be based on the formal character of a legal instrument in which the norm at issue is integrated, but on the nature and specificity of the obligation that the state parties undertake.

2.4 Reasons for the Choice of Soft Law

Soft law is often explained based on the shortcoming of the 'traditional sources' of international law to respond to the needs of a rapidly changing world, that requires fast, flexible, adaptable/effective, and participatory 'normative' solutions.[143] Formal international instruments, such as treaties, are often more detailed and time-consuming due to the complexities of formal international instruments. Moreover, after the final approval of a treaty, there is often additional procedure of incorporating the treaty into the national legal system, as national constitutions often require the ratification of the treaty by parliament. Besides, if the government cannot obtain the necessary majority, this would prevent the state concerned from becoming a party to the treaty completely. On the other hand, it is rare that the domestic legal systems require non-legal international agreements to be submitted for parliamentary approval. It is not surprising therefore, that governments, in certain circumstances, would prefer legally non-binding soft law instruments, over which they have a conclusive control without the risk

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142 I. Alkan–Olsson *The Changing Nature and Role of Soft Law in International Economic Law and Regulation* (2007) PhD in Law, Kent University, p. 43.

143 *Ibid.*, p. 45.

of domestic legislative interference. This then makes the case for the choice of soft law, in such situations, the more compelling.

The origin of soft law is context-specific and different actors are likely to promote binding or non-binding instruments in different circumstances according to their political, economic, and military leanings.[144] Inevitably, the focus among the participants will be on what is politically possible or desirable. Economically and militarily powerful states may favour binding/hard obligations that they can impose and enforce. However, when the duties imposed are not deemed in their interest, such states might still favour a legally binding treaty to which they can refuse to adhere, or they may become parties with appropriate reservations.

Alternatively, international, or domestic pressure might convince such states of the political desirability of participating in the drafting of a soft law instrument that allows them to present a co-operative attitude while requiring no formal steps of adherence. Weaker states might promote a soft law instrument on matters of concern to themselves, realistically accepting it as the best they can politically achieve and in the hope that it might gain greater force in time.

Accordingly, growing diversity in the geo-political and economic circumstances of those states that gained independence after 1945 means that common interests can no longer be assumed and that there is a more nuanced approach to the desirability of law-making through soft instrumentalities.[145] Disparate concerns may mean that a soft law instrument is the best that can be accomplished, acknowledging that changed behaviour is required without making concrete concession. In this section, we explore how soft law provide alternative and often more desirable means to manage many interactions by providing some of the benefits of hard

144 Shelton *supra* note 20 p. 34.
145 *Ibid*., p. 35.

law with less implication. We consider these benefits by looking at some of the reasons for the choice of soft law to hard law, in a globalised international system.

2.4.1. Contracting Cost

A major advantage of soft law is the lower contracting costs.[146] First, the costs and risks of national ratification procedures led the International Labour Organisation (ILO) to modify its legalisation strategy. Throughout its history, the ILO has acted primarily by adopting draft conventions. In recent decades, however, states have been ratifying ILO conventions at a low and declining rate. Believing that this phenomenon was damaging the prestige of the organisation, two successive directors-general called for the ILO to emphasise non-legally binding instruments, such as recommendations and codes of conduct, at the expense of binding treaties in order to reduce the costs of national ratification. Although labour representatives resisted this change, the ILO has begun to adopt some new rules in softer legal form.[147]

Second, contracting costs were used as a delaying tactic in the negotiations that led to the 1997 Organisation for Economic Cooperation and Development (OECD) convention restricting foreign bribery in international business transactions.[148] In those discussions, the United States hoped to reduce the commercial disadvantage created by its Foreign Corrupt Practices Act by supporting a legally binding treaty, requiring all OECD members to adopt equivalent regulatory limits. As negotiations proceeded, however, the very states that had resisted any action on the issue came out in favour of a binding treaty. These nations hoped to use the high contracting costs of hard legalisation to impede agreement. The United States responded by supporting a non-legally binding OECD recommendation. The two sides

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146 K. W. Abbott and D. Snidal *supra* note 92 at 434.

147 *Ibid.*

148 *Convention on Combating Bribery of Foreign Public Official in International Business Transaction* cited at ≤www.oecd.org/corruption/oecdantibriberyconvention.htm≥ last visited on 20 April 2020.

eventually compromised by setting a short deadline for treaty negotiations and agreeing a recommendation if the deadline was not met.

Second, contracting costs were used as a delaying tactic in the negotiations that led to the 1997 Organisation for Economic Cooperation and Development (OECD) convention restricting foreign bribery in international business transactions.[149] In those discussions, the United States hoped to reduce the commercial disadvantage created by its Foreign Corrupt Practices Act by supporting a legally binding treaty, requiring all OECD members to adopt equivalent regulatory limits. As negotiations proceeded, however, the very states that had resisted any action on the issue came out in favour of a binding treaty. These nations hoped to use the high contracting costs of hard legalisation to impede agreement. The United States responded by supporting a non-legally binding OECD recommendation. The two sides eventually compromised by setting a short deadline for treaty negotiations and agreeing a recommendation if the deadline was not met.

Additionally, the costs of hard law are magnified by the circumstances of international politics. States, (protective of the idea of sovereign autonomy) are reluctant to limit it through hard law commitments. Security concerns intensify the distributional issues that accompany any agreement, especially ones of greater magnitude or involving greater uncertainty. Negotiations are often multilateral. The scope of bargaining is often not clearly delimited since the issues themselves may only become clearer as the negotiations progress.

Soft law mitigates these costs. For example, states can dampen security and distributional concerns by opting for escape clauses, imprecise commitments, or political forms of delegation that allow them to maintain future control if adverse circumstances arise. These institutional devices protect state sovereignty and reduce the costs and risks of agreements

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149 *Convention on Combating Bribery of Foreign Public Official in International Business Transaction* cited at ≤www.oecd.org/corruption/oecdantibriberyconvention.htm≥ last visited on 20 April 2020.

while providing some of the advantages of formal law making.[150] Furthermore, soft law offers states an opportunity to learn about the consequences of their agreement. In many cases, such learning processes will lower the perceived costs of subsequent moves to harder forms of obligation.

The international nuclear regime illustrates these advantages. Although fundamentally non-proliferation obligations are set out in the Nuclear Non-Proliferation Treaty and other legally binding agreements, many sensitive issues – such as the protection of nuclear material – are regulated predominantly through recommendations from the International Atomic Energy Agency (IAEA). Recommendations deal with technical matters, such as inventory control and transportation, at a level of detail that would be intractable in treaty negotiations. They also address issues of domestic policies, such as the organisation of national regulatory agencies and the supervision of private actors that states might regard as too sensitive for treaty regulation. When a high level of consensus forms around an IAEA recommendation, member states may incorporate its provisions into a binding treaty– as occurred with rules on the management of spent fuel and radioactive was– but even these treaties must usually be supplemented by recommendations on technical issues.[151]

Overall, states face trade-offs in choosing either a soft or a hard law obligation. Hard law agreements reduce the costs of operating within a legal framework– by strengthening commitments, reducing transactions costs, and the like– but they are hard to reach. Soft agreements cannot yield all these benefits, but they lower the costs of reaching consensus in most cases. Soft law will thus, appear to be more attractive to states as contracting cost increase.

150 *Ibid.*
151 *Ibid*.

2.4.2. Sovereignty Costs

Accepting a binding legal obligation (in the form of hard law), especially when it entails delegating authority to a supranational body, is costly to states. The costs involved can range from simple differences in outcome on particular issues, to loss of authority over decision making in an issue-area, to possible fundamental encroachment of state sovereignty.[152] Key aspects of sovereignty have been codified in a variety of legal instruments, including the 1933 Montevideo Convention on the Rights and Duties of States, Article 2 of the UN Charter, and the UN General Assembly Declaration on Principles of International Law Concerning Friendly Relations Among States. Regional level arrangements like the Organisation of American States (OAS) provide much-needed support for state sovereignty. Chapter IV of the OAS Charter promotes the independence and sovereign equality of member states regardless of power differentials and protects internal sovereignty through principles of non-intervention.

Sovereignty costs emerge when states accept external authority over significant decisions. International agreements may implicitly or explicitly insert international actors (who are neither elected nor otherwise subject to domestic scrutiny) into national procedures. These arrangements may limit the ability of states to govern whole classes of issues – such as subsidies or industrial policy– or require states to change domestic laws or governance structures. Their significance is reflected in European concerns over the 'domestic deficits' and complaints of American activists regarding the 'faceless bureaucrats' in the WTO. Nevertheless, the impact of such arrangements is tempered by states' ability to withdraw from international agreements.

Sovereignty costs are at their highest when international arrangements impinge on the relations between a state and its citizens or territory. For example, an international human rights

[152] For example, by Article 36 of the Statute of the ICJ, 1945, the Court has jurisdiction in all cases referred to it by parties, and regarding all matters specially provided for in the United Nations Charter or in treaties or conventions in force. See also Article 40 of the ICJ Statute and Article 39 of the Rules of the Court.

regime circumscribes a state's ability to regulate its citizens. Similarly, the United States has correctly been concerned that an International Criminal Court (ICC) might claim jurisdiction over United States soldiers participating in international peacekeeping activities or other foreign endeavours. Agreements such as the Law of the Sea Convention both redefine national territory (for example, the delineating jurisdiction over a territorial sea, exclusive economic zone, and continental shelf) and limit the capacity of states to restrict its use (for example, by establishing a right of innocent passage). Here, too, individual states retain the capacity to withdraw, but doing so may actually diminish their sovereignty, risking loss of recognition as members in good standing of the international community.

Delegation of sovereignty provides the greatest source of unanticipated sovereignty costs. The best example is the European Court of Justice (ECJ), where the ECJ rulings transformed the preliminary ruling procedure of Article 177 of the Treaty of Rome[153] from a check on supranational power into a device through which private litigants can challenge national policies as inconsistent with European law.[154] In addition, the United States opposition to autonomous international institutions like the ICC reflects the special concern that delegation of sovereignty raises. Even in North American Free Trade Agreement (NAFTA), where its political influence is paramount, the United States resisted delegating authority to supranational dispute settlement bodies for interstate disputes; only the Chapter 19 procedure for reviewing anti-dumping and countervailing duty rulings creates significant delegated authority.[155]

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153 In many ways the most important aspect of the work of the European Court of Justice (ECJ or Court of Justice) is its jurisdiction to give 'preliminary ruling' under Article 177 of the Treaty of Rome. (1) Disputes involving Community law never come directly before the Court of Justice, but rather before the courts and tribunal of the member states. Treaty provisions enable the Court of Justice to rule on questions of Community law, which arise in such litigation. (2) The system of 'preliminary ruling' has proved a particular effective means of securing rights claimed under the Community law –Cited in Shifrin, Vladimir 'Article 177 references to the European Court. (Treaty of Rome) (Recent Rulings of the European Court of Justices)' (1999) Denver Journal of International Law & Policy at 1.

154 K. W. Abbott and D. Snidal *supra* note 92 at 438.

155 *Ibid.*

Congress also explicitly provided that the agreement would not be self-executing in domestic law, limiting delegation to national courts.

The notion of sovereignty costs is more complicated when competing domestic and transnational interests affect the development of international legalisation. Certain domestic groups may perceive negative sovereignty costs from international agreements that provide them with more favourable outcomes than national policy. Examples include free-trade coalitions that prefer their states' trade policies to be bound by WTO rulings rather than open to the vagaries of individual legislatures, and environmental groups that believe they can gain more from an international accord than domestic politics. For similar reasons, although a government that anticipates staying in power may be reluctant to limit its control over an issue, a government less certain of its longevity may seek to bind its successors through international legal commitments.

States can, however, limit sovereignty costs through arrangements that are non-binding or imprecise or do not delegate extensive power. Most often, states protect themselves by adopting less precise rules and weaker legal institutions. The international AML regime provides a good example. Beginning in the 1980s, the United States led an effort to control the international laundering of criminal profits. Many nations resisted efforts to criminalise ML or to require greater scrutiny of financial transactions, fearing interference with legitimate business dealings and with the division of domestic authority between prudential regulators and prosecutors. Part of the method to address this concern was the creation, in 1989, of the FATF by the member states of the OECD. The task force has issued policy recommendations, administers a system of peer review, and can even impose mild sanctions.[156]

[156] The FATF comes under the category of informal/non-binding soft law under the author's classification and would still be considered in the chapter five.

The FATF guidelines are not as tightly constraining as hard legal commitments and are more difficult to 'enforce'. Yet they provide a common basis for domestic implementation (with enough flexibility to accommodate national differences), guide behaviour, and create expectations that violations will bring political costs. The FATF guidelines legitimise participation in national decisions by international actors and by concerned domestic bodies. The FATF, since inception, has fostered a significant degree of convergence around the principles contained in the recommendations.

Accordingly, as this example demonstrates, soft law provides a means to lessen sovereignty costs by expanding the range of available institutional arrangements along a more extensive and finely differentiated trade-off curve. How states evaluate these trade-offs depends on their own characteristics and the circumstances of particular issue-areas.[157] For example non-treaty-based obligations, like the FATF Recommendations and EU ML Directive, can exert pressure on states to adopt internationally recognised AML standards through mutual evaluation techniques under the FATF and the principle of *direct effect* under European Union law whilst still maintaining their non-binding nature in international law.

2.4.3. Uncertainty

Many international issues are new and complex. The underlying problems may not be well understood, and so states cannot anticipate all possible consequences of a legal arrangement. One way to deal with such problems is to delegate authority to a central party (for example, a court or international organisation) to implement, interpret, and adapt the agreement as circumstances unfold. This approach is thought to avoid the costs of having no agreement, or of having to renegotiate continuously, but it typically entails high sovereignty costs on the part

157 K. W. Abbott and D. Snidal *supra* note 92 at 440.

of the state. Soft law provides a number of more attractive alternatives for dealing with uncertainty.

First, states can reduce the precision of their commitments; uncertainty makes precision less desirable as well as less attainable.[158] The argument is that, when circumstances are fundamentally uncertain – that is, when even the range and/or distribution of possible outcomes are unknown – a more precise agreement may not be desirable. In particular, actors are 'ambiguity averse'[159] they will prefer to leave agreements imprecise rather than face the possibility of being caught in unfavourable commitments. For example, unfamiliar environmental conditions like global warming provide good illustrations: because the nature, the severity, and even the very existence of these threats – as well as the costs of responding to them– are highly uncertain, the imprecise commitments found in environmental 'framework' agreements[160] may be the optimal response.

A second way to deal with uncertainty is through arrangements that are precise but not legally binding, such as Agenda 21[161] and other hortatory instruments adopted at the 1992 Rio Conference on Environment and Development. These allow states to see the impact of an instrument in practice and to gain their benefits, while retaining flexibility to avoid any unpleasant surprises that commitments in the instrument might hold.

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158 *Ibid* at 442.

159 Ambiguity aversion means that actors prefer known outcomes (including the status quo) to unknown ones – Cited in K. W. Abbott and D. Snidal *supra* note 92 at 442.

160 A framework agreement on Climate Change was signed by 154 nations in Rio de Janeiro during the United Nations conference on Environment and Development (UNCED), June 3 to 14, 1992. The Convention came into effect on March 21, 1994, when more than 50 nations ratified the agreement. The carefully chosen but often controlled language in the convention was the end result of more than two years of intense international negotiations and debate between the United States and European Community (EC) states on approaches and commitments towards stabilising greenhouse gases – cited in A. D. Hecht and D. Tirpak 'Framework agreement on Climate Change: A Scientific and Policy History' 4 (1995) 29 Climate Change at 371.

161 Agenda 21 is an action plan of the UN related to sustainable development and was an outcome of the United Nations Conference on Environment and Development (UNCED) held in Rio de Janeiro, Brazil, in 1992. It is a comprehensive blueprint of action to be taken globally, nationally, and locally by organisations of the UN, governments, and major groups in every area in which humans directly affect the environment – United Nation, *Agenda 21: Earth Summit: The United Nations Programme of Action from Rio* (ISBN –13: 978 –1482672770).

Third, moderate delegation – typically involving political and administrative bodies where states retain significant control – provides another way to manage uncertainty. UN specialised agencies[162] and other international organisations, play restricted administrative roles across a wide variety of issues, and a small number of (mainly financial) organisations have more significant autonomy.[163] These organisations have the capacity to provide information (and thus reduce uncertainty) and some capacity to modify and adapt international commitments or to initiate standards.

The relevance of soft law in this area is that the obligations offer flexibility and protection for states to work out problems over time through negotiations shaped by normative guidelines, rather than constrained by precise rules. Thus, agreements that are precise but non-binding, like the Helsinki Final Act, often include institutional devices such as conferences and review sessions where states can potentially deepen their commitments as they resolve uncertainties about the issue.

In this section, the author has thus argued that soft law provides a rational adaptation to uncertainty. It allows states to capture the 'easy' gains they can recognise with incomplete knowledge, without allowing differences or uncertainties about the situation to impede completion of the bargain. Soft law further provides a framework within which states can adapt their arrangements as circumstances change and can pursue harder forms of obligation through further negotiations. Soft law avoids the sovereignty costs associated with centralised

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[162] Specialised agencies are autonomous organisations working with the United Nations and each other through the coordinating machinery of the United Nations Economic and Social Council at the intergovernmental level, and through the Chief Executives Board for coordination (CEB) at the inter-secretariat level. Specialised agencies may or may not have been originally created by the United Nations, but they are incorporated into the United Nations System by the United Nations Economic and Social Council acting under Articles 57 and 63 of the United Nations Charter. At present, the UN has in total 17 specialised agencies that carry out various functions on behalf of the UN. Examples are the United Nations Educational, Scientific and Cultural Organisation (UNESCO) and United Nations Children's Fund (UNICEF).

[163] K. W. Abbott and D. Snidal *supra* note 92 at 443. For example, International Monetary Fund (IMF) https://www.imf.org/external/index.htm and the World Bank https://www.worldbank.org/

adjudication or other strong delegation and is less costly than repeated renegotiation in light of new information or discovery.

2.5 Harmonisation Through Soft Law?

As noted in the introduction, the international response to ML was driven by the understanding that only through harmonisation and approximation of domestic law (via soft law) can the legal and regulatory loopholes be closed against the exploitation by transnational criminals. Thus, in this section, the author examines the role of soft law as a tool for legal harmonisation in the fight against ML. The relevance of the above line of enquiry is based on the importance of the role of international cooperation in the repressive and preventive AMLC. The section will therefore examine the role of soft law as a tool for legal and regulatory harmonisation – for the purpose of international cooperation – in the fight against ML.

Harmonisation (in the context of the current research) may be defined as the process through which the international and domestic response to ML is harmonised for the purpose of effective cross-border law enforcement and cooperation. As noted by Henry Deep Gabriel,[164] "Harmonisation may conceptually be thought of as the process through which domestic laws may be modified to enhance predictability in cross-border commercial transaction." According to Sandeep Gopalan the purpose of harmonisation is not merely to arrive at a uniformity that can be marvelled at, but to produce a harmony of result by deriving the best possible solution in any given area of law, quarrying from the mines of diverse legal systems.[165]

The foregoing is important because harmonisation of law has some inherent difficulties that do not arise in soft law. For example, soft law instruments are not subject to the same

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[164] H. D. Gabriel 'The Advantages of Soft Law in International Commercial Law: The Role of UNIDROIT, UNCITAL and the HAGUE Conference (2009) 34(3) Brooklyn Journal of International Law at 655.

[165] Sandeep Gopalan 'Transnational Commercial Law: The Way Forward' (2003) AM.U.INT'L L. REV. at 809.

pressure to be harmonised with existing law, as is the case with hard law.[166] Soft law can, therefore, ease bargaining problems among states even as it opens up opportunity for achieving mutually preferred compromises. Negotiating a hard, highly elaborate agreement among heterogeneous states is a costly and protracted process. It is therefore more practical to negotiate a softer form of agreement that enables harmonisation of divergent domestic legislation. In addition, soft law allows states to adapt their commitments to their particular situations rather than trying to accommodate divergent national circumstances within a single text. This provides for flexibility[167] in implementation, helping states deal with the domestic political and economic consequences of an agreement and thus increasing the efficiency with which it is carried out. Accordingly, soft law should be attractive in proportion to the degree of divergence among the preferences and capacities of states, a condition that increases almost automatically as one move from bilateral through regional multilateral negotiations.[168]

An example of soft law approach to legal harmonisation is seen in the interaction between soft and hard law as complementary tools for international cooperation. Accordingly, soft law regime can be 'hardened' through their links to hard law by losing the flexibility and informality, while hard law regimes can be 'softened' through their links to soft law regimes by reducing legal certainty and predictability.[169] Hard and Soft law can, therefore, build upon each other.[170] Thus, in some conditions hard law and soft law are operating as mutually reinforcing complements, but in other conditions they interact in international law as alternatives.[171]

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166 H. D. Gabriel *supra* note 164 at 663.

167 Flexibility is thought to be especially important when uncertainty or one sticky problem threatens to upset a larger 'package deal'. Rather than hold up the overall agreement, states can incorporate hortatory or imprecise provisions to deal with the difficult issues, allowing them to proceed with the rest of the bargain. Cited in K. W. Abbott and D. Snidal *supra* note 92 at 445.

168 Ibid at 445.

169 G. Shaffer and M. A. Pollack, *supra* note 87 at 710.

170 Ibid at 707.

171 Ibid at 798.

In the global regulation of ML, it is clear that the interaction of international soft law and domestic hard law has profound implications for international cooperation and cross-border law enforcement. This thesis attempts to examine the repressive and preventive AMLC, under which hard and soft law acts as complements crafting legal arrangements as tools for regulatory and legal harmonisation. How then should international cooperation and cross-border law enforcement of AML proceed, given the divergence in domestic AML legislation? The foregoing query will form the basis of the underlying discuss for the rest of the thesis.

2.6 Conclusion

Opinions abound on the legal nature of soft law in international law, and jurists have come up with different interpretations. Some restrict the term to norms in legally binding form (usually created by treaties but with vague content or weak requirements), while others concentrate on the non-legal form of the instrument. Furthermore, there are those who evaluate soft law based on a characteristic that vary along a continuum. In this thesis, the author takes the perspective binding or non-binding divide to highlight the differences between hard and soft law, and the term formal and informal to explain our framework type of soft law. The author supports the claim for the framework type of soft law looking at different kinds of instruments and the concept of legalisation by Abbott and Snidal.

Thus, in order to assess the role of soft law as a technique for AMLC, the thesis will limit the concept of soft law to a framework type that incorporates and captures a simply binary formal and informal categorisation. This framework type of soft law will then be used in subsequent chapters to explain the role of soft law in the repressive and preventive AMLC.
Apart from identifying soft law, the chapter also examined the reasons for the choice of soft law. The chapter examined how soft law offer alternative and often more desirable means to manage many interactions by providing some of the benefits of hard law with less implication.

These benefits were considered by looking at some of the reasons for the choice of soft law to hard law as it relates to contracting cost, sovereignty cost and uncertainty. These together with the section on ‘Harmonisation Through Soft Law’ demonstrate the role or flexibility of soft law in divergent national circumstance.

Thus, despite the respective costs and benefits of hard and soft law as alternatives, legal and political science scholars have moved increasingly towards a view that hard and soft international law can interact and build upon each other as complementary tools for international problem solving. The relevance of this is captured by the way soft law obligation is incorporated into domestic legislation of states in the fight against ML for the purpose of international cooperation and cross-border law enforcement.

CHAPTR THREE

Money Laundering: Nature of the Problem and the Legal Response

3.1 Introduction

ML connotes a compound word that mainly replicates the underlying motive behind the actual act of laundering and the effect on the legalised economy.[172] The difficulty placed with capturing a single act as ML is perhaps part of the reason for an international response to repress and prevent the crime through soft law. Soft law in the context of AMLC refers to the substance of formal and informal obligations, which includes both treaties and informal arrangements. The international response to ML –repressive and preventive AMLC– should then be seen in this light.

This chapter will accordingly examine the definition of ML, nature of the problem and the legal response to ML. The current chapter will confine its analysis to sources of formal and informal AMLC and the origin of the law from initial domestic legislation to an international undertaking that includes a repressive and preventive response. The aim, therefore, is to highlight the nature of the problem and the origin and development of the legal response that followed thereafter.

Of importance in this respect are the obligations to repress ML through international conventions, under Article 3 of the Vienna Convention 1988 and Articles 6 1990 Money Laundering Convention.[173] These instruments (together with the definition given under Article

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[172] According to the *Oxford English Dictionary,* the use of the word *launder* emerged out of the Watergate inquiry in the United States in 1970-4. Either "to transfer funds of dubious or illegal origin, usually, to a foreign country and then later to recover them from what seem to be 'clean' (legitimate) source". The Watergate investigation had uncovered the attempts by Nixon Committee to Re-elect the President (CRP) to hide the origin and receipt of anonymous campaign contributions and to sever the financial 'paper trail' between the CRP and the intruders that broke into the Democrat's campaign headquarters at the Watergate office building. See J. Robinson *The Laundrymen: Inside the World's Third Largest Business* (London Pocket Books 1994) p. 6.

[173] Article 6 of the Palermo Convention 2000 for similar provision; See also Article 9 2005 Council of Europe Convention against Money Laundering and Articles 23, 24 and 27 of the 2003 United Nations Convention against Corruption.

6 of the Palermo Convention) gave a broad definition of ML (formal soft law) by highlighting three categories of criminal conduct that are only distinguished by the extent to which their nexus with the predicate offence can be established.[174] Together with the FATF and other informal bodies, (referred to as informal soft law) they form the body of international and regional instruments, ratified and enforced through domestic AMLC. However, an initial undertaking will be to define the term ML.

3.2 What is Money Laundering?

The origin of the phrase ML, while traceable to the practice of the New York Mafia in the 1920s when they opened Laundromats as facades for their criminal activities, owes much prominence to activities in the 1970s when ML suddenly became part of everyday speech and journalistic reporting.[175] The legal usage of the term itself is traceable to a 1982 United States (US) Supreme Court case concerning the civil forfeiture of two large sums of money.[176] In that case, the Supreme Court concluded that the financial transfer that took place constituted more likely than not a ML process. These words by the US Supreme Court is regarded to represent the first recorded use of the term 'ML' in a primary legal document and heralded the birth of the subsequent international legal regime.

ML is thus defined as a process of manipulating legally or illegally acquired wealth in a way that obscures its existence, origin or ownership for the purpose of avoiding law enforcement.[177] ML therefore describes a deliberate, complicated and sophisticated process by which the proceeds of crime are camouflaged, disguised or made to appear as if they were

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174 The expression 'predicate offence', borrowed from the Vienna Convention 1988 and many subsequent international instruments, describes the offence by which the profits were acquired.

175 J. Robinson *supra* note 172.

176 *US* v *USD* 2 255 625, 39, 551 F Supp 314 (1982). The case represents the first legal development where the term 'money laundering' was adopted in legal language. The court in deciding for the Government in this case concluded that, Molina to Sonol to Capital Bank was, more likely than not a more laundering process the Court used the term 'laundering' repeatedly in its decision.

177 Shams, 'Using Money Laundering Control to Fight Corruption' in N. Mugarura *The Global Anti-Money Laundering Regulatory Landscape in Less Developed Countries* (Surrey, Ashgate Pub. Ltd, 2012) p. 3.

earned by legitimate means.[178] The person who has received some form of ill-gotten gains will seek to ensure that they can use these funds without people realising that they are the result of inappropriate behaviour. To do this they will need to disguise the proceeds such that the original source of the proceeds is hidden and therefore the funds themselves appear to be legitimate.[179]

According to a World Bank Study, in most definitions that are officially used by international organisations, ML will not happen through the financial system but with money that is already within the financial system.[180] The International Monetary Fund (IMF) and the World Bank thus defined ML as the "process in which assets obtained or generated by criminal activity, are moved or concealed to obscure their link with crime".[181]

The FATF, an inter-governmental body whose purpose is the development and promotion of policies to combat ML at both national and international levels, defined ML as the "processing of criminal proceeds to disguise their illegal origin".[182] According to the FATF, "the goal of a large number of criminal acts is to generate a profit for the individual or group that carries out the act. ML is therefore the processing of these criminal proceeds to disguise their illegal origin. The process is of critical importance, as it enables the criminal to enjoy these profits without jeopardising their source".[183]

Legal definitions of ML that many jurisdictions have adopted are even wider. Most states subscribe to the definition adopted by the Vienna Convention 1988 and the Palermo Convention 2000. According to this definition, even the possession, and all use, of illegally obtained money, is labelled as ML, regardless of whether people are trying to hide the source.[184]

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178 *Ibid.*

179 D. Cox *An Introduction to Money Laundering Deterrence* (West Sussex, John Wiley & Sons Ltd, 2011) p. 3.

180 S. Yikona *et al Illegal Money and the Economy: Experiences from Malawi and Namibia* (The International Bank for Reconstruction and Development/The World Bank, 2011) p. xiii p. 2

181 *Ibid.*

182 Available at https://www.fatf-gafi.org/faq/moneylaundering/last visited on 02 of July 2020.

183 R. Booth, *et al supra* note 4 p. 3.

184 S. Yikona *et al supra* note 180 p. 2.

Having illegally obtained money in a bank safe or hidden it under a mattress is also ML, including using it for consumption or other spending purposes.[185]

Two central notions from these definitions are that: first, the money is derived from crime and second, that there is concealment of the criminal source. In the commission of acquisitive crime, criminals seek to make significant profit from their unlawful activities by concealing the origin of their crime. This may include such conduct as drug trafficking, bribery and corruption, organised crime, commercial fraud, tax evasion. The list is not exhaustive as there are many other crimes that may give rise to a gain for the criminal, which constitute what would later be known as a predicate offence for ML.

In his book *The Laundrymen,*[186] Jeffrey Robinson noted thus:

"ML is called what it is because that perfectly describes what takes place – illegal, or dirty money is put through a cycle of transactions, or washed, so that it comes out the other end as legal or clean, money. In other words, the source of illegally obtained funds is obscured through a succession of transfers and deals in order that those same funds can eventually be made to reappear as legitimate income".

The above observation of ML as the deliberate washing clean of dirty money accords quite closely with the nature of the ML offence that FATF recommends states to incorporate in their criminal law. The wording of that offence is derived from the Conventions Vienna, 1988,[187] and Palermo Convention.[188] ML is accordingly a process by which one conceals the existence, illegal source, or illegal application of income, and then disguises that income to make it appear legitimate. The goal of ML is therefore two-fold: to conceal the predicate offence from which the proceeds are derived and to avoid the detection in a legal economy.[189]

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185 *Ibid.*
186 Simon & Schuster UK Ltd (revised edition 1998) cited in R. Booth *et al supra* note 4 p. 3.
187 Article 3.
188 Article 6.
189 G. Stessens *supra* note 14 p. 83.

Cash was identified as a major form in which illegal funds are generated ('criminal cash').[190] However, it should be recognised that although the 'perpetrators', whose illegal activities generate large amounts of cash, will need to attempt to 'recycle' the proceeds,[191] Criminals will look to exploit any means possible in order to achieve their objective to concealing the criminal origin of such cash. This disguise might mean the exchange or transfer of property (both real estate and intellectual), the use of loans, alternative remittance systems (Hawala)[192] and any opportunities presented by new technology.[193] In addition, ML can also involve sophisticated activities such as blending illegal with legal businesses, creating legal facades, or externalising proceeds of crime of foreign tax havens in 'no questions asked' banking systems.[194]

3.3 Money Laundering and Terrorist Financing

This section would proffer insight into the link between ML and terrorist financing (TF).

The section underscores the dynamics of the putative Anti-Money Laundering/ Countering of Terrorists Financing (AML/CTF) framework. This framework is made up of diverse AML/CFT regimes that have evolved at various institutional levels. Some of these regimes, as would later

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190 M. Simpson *et al International Guide to Money Laundering Law and Practice* (West Sussex: Bloomsbury Professional Ltd, 3rd edn, 2010) p. 2.

191 The use of couriers is thought to be a popular method for terrorists to move funds.

192 *Hawala* is an ancient underground banking system. It is rooted in family businesses, which have often operated as hawaladars for generations. The system is based upon trust and ethnic or familial ties, which allow debts to be carried for extensive periods. Thus, cash does not necessarily need to cross borders. Moreover, in the Middle East and South Asia, the cash economy is much more prevalent than in Europe or the US, so that hawaladars can avoid official scrutiny or regulation. Cited in L. Holmes *infra* note 217 p. 82.

193 M. Simpson *et al supra* note 190 p. 2.

194 S. Yikona *supra* note 180 p. 2.

be seen, have evolved under similar UN treaties, regional-based initiatives and *ad hoc* based arrangements.[195]

The shock of the 9/11 attack on the World Trade Centres, New York, led quickly to the widening of FAFT's Recommendations to counter TF and the promulgation of the 2005 Council of Europe Convention against Money Laundering. The earlier Special Recommendations bring to TF a similar approach to that of the 40 Recommendations on ML. They cover criminalisation of the financing of terrorism and associated ML, the freezing and confiscation of terrorist assets, and the reporting of suspicious transactions related to terrorism. There were also provisions to enhance international co-operation and specific Recommendations on alternative remittance systems, wire transfers and the abuse of non-profit organisation: all of which have now been incorporated into the new FATF Recommendations for 2012.[196]

TF is very different from ML and the differences make it harder to detect. ML is essentially about the cleaning of dirty money, turning the proceeds of crime into apparently legitimate money and assets, which can be freely used and traded in the normal way. Terrorist offences, however, are not crimes committed for the purpose of financial gain, and the motivation of terrorists, ideological rather than material is very different from that of drug or fraud-related type of laundering crime. TF is about the misuse of clean– or dirty– money for

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195 These initiatives include the International Convention for the Suppression of the Financing of Terrorism (1999) available at ≤www.un.org/law/cod/finterr.htm≥ last visited on 6 July 2020, the 2012 FATF Recommendations on the 'International Standards on Combating Money Laundering and the Financing of Terrorism and Proliferation, and the 2005 Council of Europe Convention against Money Laundering. On the specific aspect on terrorism, of note are the International Organisation of Securities Commission (IOSCO), the African initiatives, such as the Organisation for African Unity Convention on the Prevention and Combating of Terrorism in Africa (Algiers Convention), 1999 and the New Partnership for Africa's Development (NEPAD) (1999), and many more in Asia and worldwide.

196 Titled 'International Standards on Combating Money Laundering and the Financing of Terrorism &Proliferation the FATF Recommendations' ≤www.fatfgafi.org/topics/fatfrecommendations/documents/internationalstand≥.

terrorist purposes. The aim of counter-terrorist financing measures is, as far as possible, to cut off 'the life-blood of terrorism'.[197]

Terrorism is not necessarily an expensive enterprise. Maintaining a terrorist organisation over time requires significant funds, but individual acts of terrorism may cost little. The cost of the terrorist attacks in London on 7 July 2005 has been estimated at only about GBP 7,223.[198] The monetary cost bore no relation to the cost in human suffering that the terrorists inflicted. The terrorist attacks on the United States on 11 September 2001 required more elaborate and lengthy preparations, but the report of The National Commission on Terrorist Attacks Upon the United States[199]concluded that: "Bin Laden and his aides did not need a very large sum to finance their planned attacks on America. The 9/11 plotters eventually spent somewhere between USD 400,000 and USD 500, 000 to plan and conduct their attacks".

Although terrorist organisations often rely partly on criminal activities to generate funds for their activities, much terrorist financing involves legitimate funds that can be transferred and used through the banking system and normal channels in amounts that do not give rise to suspicion and in ways that are otherwise normal. What keeps the global terrorist networks running are funds from a variety of sources. The FATF has identified the major sources of terrorist funds, which include drug trafficking, extortion and kidnapping, robbery, fraud, gambling, smuggling and trafficking in counterfeit goods, sponsorship from certain governments, contributions and donations, sale of publications (legal and illegal), and funds derived from legitimate businesses.[200]

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197 R. Booth *et al supra* note 4 p.13.

198 See Simon Dilloway, *7/7 Attack –London Bombing* ≤www.lophamconsultancy.co.uk≥ cited in R. Booth *supra* note 4 p. 13.

199 Available at ≤www.9-11commission.gov/≥ last visited 6 July 2020.

200 J. D'Souza *Terrorist Financing, Money Laundering, and Tax Evasion,* (CRC Press, 2012), p. 29.

Accordingly, measures to those designed to combat ML are now applied to counter terrorist property and terrorist ML.[201] TF covers a wide range of proscribed activities[202] relating to the funding of terrorism and the use and possession of terrorist property, as well as terrorist ML.[203] Terrorist offences are not offences by which, other than incidentally, property are obtained. The ML offence in section 18 of the UK Terrorism Act 2000 may appear to be very similar to the arrangement offence in section 328 of Proceeds of Crime Act 2002(POCA), but in reality, it is quite different because terrorist property[204] is mainly about resources likely to be used for terrorist purposes, not about proceeds of crime, in relation to ML.

The relevance of TF to the ML is based mainly on the similarity between the efforts to combat ML and those of the financing of terrorism. The similarity is clearly demonstrated in the uniform definition of ML (as would later be seen) under the 2005 Council of Europe Convention against Money Laundering and the other conventions on the repression of ML. In addition, the 2012 FATF Recommendations for the prevention of ML now includes the prevention of terrorist financing as part of the Forty Recommendations. The earlier nine recommendations are now merged into the Forty Recommendations, which makes the new sets of recommendations on AMLC the same as those for the control of the financing of terrorism.

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201 Similar measures but with many differences in the detailed provision. For example, the obligation to criminalise laundering aspect of terrorist financing in 2005 Council of Europe Convention against Money Laundering is the same with those under the Vienna Convention. In addition, the FATF Recommendations for 2012 covers both money laundering and the financing of terrorism.

202 The 2006 Terrorism Act creates new offences related to terrorism and amends existing ones.

203 See section 18 of the Terrorism Act 2000.

204 Terrorist property is defined in section 14 of the Terrorism Act 2000.

3.4 . Understanding the Process of Money Laundering

ML as a process generally highlights three stages: 'placement'[205], 'layering'[206], and 'integration'.[207]

3.4.1 Placement Stage

The *placement stage* is where cash derived directly from criminal activity is initially placed in a financial institution or used to purchase an asset. Placement is the removal of the illegal cash from the location of acquisition to avoid detection by the authorities, such as:

- transforming it into assets such as travellers cheque, postal orders and bankers drafts;
- spreading the money into multiple accounts, each involving small sums just below levels which might trigger a 'suspicious transaction report'[208];
- putting the cash into legitimate businesses such as pubs, clubs, casinos, jewellers, auction houses and bureaux de change, which can then filter the money into the system even if extra tax has to be paid on the money in question.

Placement thus describes the process of introducing large cash proceeds of crime into the banking and financial system. Over the years, this has become necessary because the use of cash for large purchases is increasingly difficult and regarded with suspicion in many states. It has also become harder to introduce large amounts of cash because banks, as would later be seen, have become more vigilant about ML and more wary of large cash deposits.

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205 The stage could be said to clearly represent the Conversion stage, as expressed in Article 3(b) (i) of the Vienna Convention and Article 6(a) (i) of the Palermo Convention.

206 The stage is also said to have been captured in all three instruments, and it includes Article 3(b) (ii) of the Vienna Convention and Article 6(a) (ii) of the Palermo Convention.

207 T. Buranaruangrote *supra* note 14 at 8. See also J. E. Turner *Money Laundering Prevention: Deterring, Detecting, and Resolving Financial Fraud* (New Jersey, John Wiley & Sons, Inc, 2011) pp. 6-10.

208 See Chapter 5 for the meaning of 'suspicious transaction report'.

One method involves the use of 'smurfs'.[209] The money launderer gives a sum of cash to an individual known as a 'smurf'. The 'smurf' deposits the cash in small amounts into a number of different bank accounts, probably held at several different banks. The deposit amounts are small enough that they do not attract attention or suspicion. Once the money is deposited, the placement stage is complete.[210]

A second method involves the use of 'front companies.' The launderer selects companies and business bank accounts belonging to apparently respectable, high net worth individuals. The money launderer gives a much larger sum of cash to these people. The cash is then paid into their accounts and, with the support of forged documentation, is explained as a legitimate receipt from the sale of property or the sale of an interest in a business for example. Once the cash is deposited and the purpose of the transaction successfully explained, the placement stage is complete.

Another method involves the purchase of different types of insurance and investment policies for cash, through independent financial advisers or brokers who have persuaded themselves that the cash is of legal provenance. At a selected moment, the policy is surrendered, and a redemption cheque or funds transfer is received from the issuer. Ultimately, amounts so 'placed' in apparently legitimate accounts held by other people may then be transferred to a single account which acts as a conduit for the money as it is moved on elsewhere, as part of the layering process described below.

3.4.2 Layering Stage

The *layering stage* is where there is the first attempt at concealing or disguising the source of ownership of the funds. Layering is thus a term given to hiding the origin of the money by

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209 T. Parkman *Mastering Anti-Money Laundering and Counter-Terrorist Financing* (Great Britain, Ashford Colour Press Ltd, 2012), p. 6.

210 A training film of this can be previewed available at <https://www.youtube.com/watch?v=_d_1LAj-woY> last visited 6 of July 2020.

passing it through different accounts, shell companies and trusts (particularly in jurisdictions that still permit a substantial degree of anonymity) so that any audit trail is lost or difficult to follow. This may take many forms, but the motives and purposes are always the same: to obscure the criminal origin of the money and, as far as possible, to distance the funds and the beneficial owner of those funds from their source, and to make it difficult for an investigator to trace the funds back to that source.

Layering may be done in part through repeated transfers of money between accounts with financial institutions in different jurisdictions, especially ones with a low level of AML compliance and poor law enforcement co-operation with other countries.[211] It may involve the use of a variety of transactions and the use of corporate structures as cover to hide details of beneficial ownership. Whatever techniques are used, layering is central to the process and purpose of ML. With each transfer or transaction, the intention is that the dirty money is washed cleaner, and the taint of crime becomes fainter.

The following are possible examples of the layering stage of ML:

- investment in financial products which have good liquidity, and which can be bought and sold easily (e.g., unlisted stocks and shares);
- purchase and sale of real estate– apartments, houses, flats, commercial premises;
- transfer of the money to a business, ostensibly as a ‘loan’ with documents such as loan agreements and receipts to support the illusion that the loan is real;
- transfer of the money overseas or to other accounts under the guise of money destined for a specific purpose (e.g., education overseas of a family member);
- using fictitious business transactions to move money around (e.g., giving money to suppliers against invoices raised for goods that were never issued; or raising invoices to customers in respect of sales that never took place);

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211 R. Booth *et al supra* note 4 p. 4.

- transferring money to companies overseas in payment for non-existent shipments of imported goods;
- use of shell companies and shell banks, i.e., entities that have no real function, no real place of business and no real business operations, but which exists in name only as a conduit for the receipt and distribution of money;
- use of the international financial markets to buy and sell securities and move money across international borders.[212]

3.4.3 Integration Stage

The *integration stage* is where the money is integrated into the legitimate economic and financial system and is assimilated with all other assets in the system. The stage thus completes the process of ML by moving the now apparently clean funds into reputable banks and financial institutions from which the criminal can draw funds or invest and use the criminal proceeds freely within the legitimate economy.[213]

The conventional way of describing the process of ML has explanatory value, but ML is not a rigid and defined process. A complex series of conversion and transactions to obscure the true source of criminal proceeds is only necessary and practicable where large sums are involved. The placement stage may be necessary for cash proceeds of drug trafficking or people trafficking but will not generally be necessary for fraudsters perpetrating financial scams, where the proceeds of crime may be received by transfer directly into the fraudster's bank account.[214]

Moreover, the particular methods by which ML is carried out are changing all the time. Increasing sophisticated AML measures may prevent some ML and detect instances of ML, but

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212 See T. Parkman *note* 209 pp. 7-8.
213 *Supra*.
214 *Ibid*.

it is likely that it often merely displaces ML activity, leading criminals and those who assist them in the cleaning of dirty money to find and exploit new ways of doing so. Creating an international response, through repressive formal soft obligations and preventive informal soft instruments, remains the only legitimate way of tackling the problem of ML.

Evaluating the Impact of Global Money Laundering

Estimating the amount of ML has been recognised as problematic (if not impossible) because of the covert nature of the crime. However, some estimates have been developed which give the rough magnitude of the problem.

According to a report by the Global Financial Integrity in 2017 the global drug trafficking market was worth USD 426 to 652 billion.[215] However, the extent of ML worldwide is vast: using 2018 data, an IMF study estimates that the amount of money laundered annually is between two and five percent of global GDP (USD 1.6 trillion– USD 4 trillion).[216] The IMF also estimates that between 2 and 28 percent of the GDP of OECD economies is underground. In the Middle East and Asia, the figures are in the range of 13–71 per cent, while in Africa, the underground economy can account for 20–76 percent.[217]

According to a survey by 'The State of the Future, 2010,'[218] international organised crime continues to grow in the absence of a coherent global strategy to counter it and then lists some of the statistics. The best estimate for the annual value of counterfeiting and intellectual property piracy is about USD 300 billion to USD 1 trillion. For the global drug trade, about USD 386 billion; for the trade in environmental goods, about USD 63 billion; for human

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215 https://secureservercdn.net/45.40.149.159/34n.8bd.myftpupload.com/wp-content/uploads/2017/03/Transnational_Crime-final.pdf

216 https://www.imf.org/external/pubs/ft/fandd/2018/12/pdf/imf-anti-money-laundering-and-economic-stability-straight.pdf.

217 IMF 2001: 25 cited in Soft Law Regimes in L. Holmes *Terrorism, Organised Crime and Corruption: Networks and Linkages* (Cheltenham: Edward Elgar, 2010) p. 60.

218 A survey by the Millennium Project of the World Federation of the United Nations Association cited in T. Parkman *supra* note 209 p. ix.

trafficking and prostitution – USD 141 billion; and for the weapons trade, about USD 12 billion. It goes on to report the FBI's estimate that online fraud cost US businesses and consumers alone USD 560 million in 2009, up from USD 265 million in 2008. It points out that the overall organised crime figures do not include extortion or its part of USD 1 trillion in bribes that the World Bank estimates is paid annually, nor its part of the estimated USD 1.5–6.5 trillion in laundered money that exists.

3.6 Reasons for Fighting against Money Laundering

Over the last twenty years, the international community has significantly stepped up its efforts to prevent, detect, and deter money flows related to criminal activities and TF. Since the early 2000s, this drive has extended to developing countries, with most of them introducing AML policies.[219] ML is the first serious crime whose existence can be directly related to global economic concerns, rather than those of individual jurisdictions. This makes the crime transnational and across national borders and jurisdictions. Combating the crime therefore requires an equal response both in magnitude and in scale.

As studies have demonstrated, crime is bad for economic development.[220] The United Nations Office on Drugs and Crime (UNODC) has, for example, conducted a study on the internationalisation of crime. The UNODC stresses the economic relevance of anti-crime efforts for developing countries: "Crime is fuelling corruption, infiltrating business and politics, and hindering development". It is also "undermining governance by empowering those who operate outside the law".[221] In its report, UNODC highlights the globalisation of crime

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219 S. Yikona *et al supra* note 180 p. xiii.

220 For a past overview of the literature on the direct and indirect economic costs of crime see for example, S. Brand and R. Price *The Economic and Social Costs of Crime* (Home Office Research Study, 2000); M. A. Cohen *The Costs of Crime and Justice* (New York: Routledge, 2005), P. Mayhew *Counting the Costs of Crime in Australia* (Australian Institute of Criminology Technical and Background Paper Series, No.4, Griffith, Australia, 2003); and Shapiro *Costs of Crime: A Review of the Research Studies* (House Research Department, Minnesota House of Representatives, St. Paul, Minnesota, 1999), World Bank Study, 2011 cited in S. Yikona *et al supra* note 180.

221 UNODC 2010, World Bank Study, cited in S. Yikona, *et al* note 180 p.12.

and the need for a transnational anti-crime approach. According to the FATF ML is not a victimless crime and trillions of dollars are laundered each year. The money laundering then fuels serious crime like drug trafficking, sexual exploitation, human trafficking and harm to society.[222]Below are therefore some of the reasons for fighting global ML.

3.6.1 Reputation of the Financial Sector

The major economic contention resounding through the literature is that ML has a detrimental effect on the operation of markets.[223] One of the basic premises behind AML framework is that the abuse of the financial system for ML purposes is harmful to the financial sector, its reputation, and the people's confidence in it. A reputation for integrity is one of the most valuable assets of a financial institution and of the financial sector as a whole. Consequently, ML is harmful to the welfare of entire economies since trust in financial institutions is generally seen as a basic requirement for long-term economic growth.[224]

Bartlett argues that this is especially relevant for developing countries, with the immature or developing financial systems and a reputation for being highly corrupt.[225] Strong developing-country financial institutions are critical to economic growth. Bartlett emphasises that trust in the financial sector is not only a domestic necessity but that it is also essential to attracting foreign capital and investments.

As noted above, ML has a detrimental effect on the operation of markets. Some argue that the protection of the financial sector against corruption is the major motive underpinning

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222 http://www.fatf-gafi.org/about/ for a video on the harmful of ML on society.

223 *PIU Report 20: Second Commission Report to the European Parliament and the Council on the Implementation of Money Laundering Directive* COM (1998) 401 final 18–19 cited in P. Alldridge *Money Laundering Law: Forfeiture, Confiscation, Civil Recovery, Criminal Laundering and Taxation of the Proceeds of Crime* (Oxford, Hart Pub, 2003) p. 31.

224 S. Yikona, *et al* note 180 p. xiv.

225 B. L. Bartlett 'The Negative Effect of Money Laundering on Economic Development' (2002) 77 *Platypus Magazine* cited in S. Yikona *et al supra* note 180 p. 12.

global AML measures.[226] An IMF economist, Tanzi, argues that the resources that go into illegal activity might otherwise be directed legally.[227] ML allocates dirty money around the world not so much on the basis of expected rates of return but on the basis of the ease of avoiding controls, and this is inefficient.[228] As a consequence, the world allocation of resources is distorted, first by the criminal activities themselves, and then by the way the dirty money is allocated.[229]

3.6.2 Capital Flight

The internationalisation of crime and the internationalisation of ML are two sides of the same coin. It is often stated that ill-gotten money tends to flow to jurisdictions that are economically more advanced, financially more sophisticated, fiscally attractive, or that have a more permissive environment toward ML. Walker and Unger, for example, assume that ill-gotten money seeks states with attractive banking regimes (that is, advanced banking systems, tax havens, and 'no questions asked banking') and states with stable economies and low political risks.[230]

This is especially relevant for developing countries where corruption in recent decades has led to massive capital flight to financial centres elsewhere.[231] The well-recognised problem of illicit capital flight from developing countries is typically facilitated by either domestic financial institutions or by foreign financial institutions in foreign offshore centres or major

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226 M. Pieth, 'The Prevention of Money Laundering: A Comparative Analysis' (1998) *European Journal of Crime, Criminal Law and Criminal Justice* at 161.

227 V. Tanzi *Money Laundering and the International Financial System,* IMF Working Paper 95/55 (Washington DC, International Monetary Fund, 1996) cited in P. Alldridge *supra* note 223 p. 31.

228 Cabinet Office Performance and Innovation Unit, *Recovering the Proceeds of Crime* (London, Cabinet Office, 2000) cited in P. Alldridge *supra* note 223.

229 V. Tanzi *supra* note 227 at iii.

230 J. Walker and B. Unger 'Measuring Global Money Laundering: The Walker Gravity Model' (2009) 5(2) *Review of Law and Economics* 821-53.

231 See for example R. W. Baker *Capitalism's Achilles Heel* (Hoboken, NJ: John Wiley and Sons), D. Ker and D. Cartwright-Smith 'Illicit Financial Flows from Developing Countries: 2002-2006 (2008) Global Financial Integrity, Washington DC, and V. Le Quan and M. Rishi 'Corruption and Capital Flight: An Empirical Assessment' (2006) 20(4) International *Economic Journal* 523-40.

financial centres such as London, New York, Singapore, and Tokyo. Baker argues that the outflow of 'dirty money' from developing countries to advanced economies is ten times larger than the inflows of foreign aid.[232]

3.6.3 Spill-Over Effect into Crime and Corruption

ML can also facilitate and even stimulate criminal activity. It is stated to provide criminals with apparently legitimate money, which they can use to subsidise, continue, diversify, and expand their criminal activities.[233] ML therefore can be a link between crime and even more crime, because ample ML opportunities will make crime and corruption easier and more profitable. In addition, ample ML opportunities within a jurisdiction can attract foreign criminals. Masciandaro has labelled this the 'spill-over effect'.

3.6.4 Preference for 'Sterile Assets'

Criminological studies and asset forfeiture policies have shown that proceeds of crime and corruption are often placed in so-called 'sterile assets',[234] that is, assets that generate limited productivity for the broader economy, such as antiques, art, auto-mobiles, luxury goods, and real estate. This is the case in high-income economies, but also in developing economies. The preference for sterile assets is especially problematic for developing economies since this might divert valuable foreign reserves to the importation of luxury goods instead of basic necessities. Financial leakages from the national budget might also result in price distortions in other areas, like the real estate market.[235]For example ML impact on real estate market can lead to distortion of prices and increases in real estate prices thereby preventing people with legitimate housing

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232 R. W. Baker, *Ibid.*

233 M. Levi, 'Money Laundering and its Regulation', (2002) *Annals of the American Academy of Political and Social Science* p 582 cited in S. Yikona *et al* note 180 p.13.

234 Bartlett *supra* note 223 cited S. Yikona *et al* note 180 p.13.

235 S. Yikona *Ibid.*

need from accessing the market. This happens when prices are driven up with an immediate impact on housing affordability.

3.6.5 Unfair Competition

Ill-gotten money might also undermine fair competition. Walker, for example, has argued that criminals might be able to outbid honest buyers, in business or real estate, because of the availability to criminals of large amounts of funds and their primal interest in finding a 'safe haven' or ML opportunity for their ill-gotten money instead of profit making.[236]Illicit enterprises might, for the same reasons, be kept growing by means of ill-gotten money although they are structurally loss making.[237] The unfair competition effect of ill-gotten money could also influence the outcome of privatisation or tendering processes.

3.6.6 Corruptive Penetration of the Upper-World

Business and even government decisions might be affected by ill-gotten money. Van Duyne and Soudjin call this "corruptive penetration in the upper-world decision chambers"[238]– criminals buying their way into the government, the financial sector, and other public and private businesses. Corruptive penetration in the upper-world economy and criminal upper-world subsidy can occur on a national scale, but also on regional levels in specific markets or sectors of the economy.

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236 J. Walker 'Estimates of the Extent of Money Laundering in and through Australia' (1995) Paper prepared for the Australian Transaction Reports and Analysis Centre cited in S. Yikona *et al* note 180 p.14.

237 P. C. Van Duyne and M. R. J. Soudijn 'Crime Money in the Financial System. What We Fear and What We Don't Know' In: Martine Herzog-Evans, ed., *Transnational Criminology Manual* (Nijmegen:Wolf Legal Pub, 2edn, 2010), pp 253-279 cited in S. Yikona *et al* note 180 p.14.

238 *Ibid*.

3.6.7 Corruptive Penetration of the Anti-Money Laundering System

Chaikin and Sharman have discussed the symbiotic relationship between corruption and ML. They argue that corruption and ML tend to co-occur, but, more importantly, the presence of one trend to create and reciprocally reinforce the incidence of the other.[239] Corruption produces income that has to be laundered. At the same time, bribery, trading in influence and embezzlement can compromise the working of the AML system itself. The effect was referred to as the "corruptive penetration of the AML system".[240]

3.6.8 Distortion of the Foreign Exchange Market

Ill-gotten money from ML might flow unrecorded over national border – either because of the transnational nature of many illicit markets (involving cross-border financial transactions), or with the aim of laundering or spending the proceeds of crime or corruption in another jurisdiction. These cross-border flows could give way to distortion in the foreign exchange market[241]and, more specifically, fuel the existence of a black market for foreign exchange (demand and supply).

3.6.9 Distortion of Economic Statistics and Erosion of the Tax Base

A basic concern related to the circulation of unlaundered ill-gotten money is that there is money in circulation that is officially not known.[242] This could result in distortions of the national accounts and lower tax incomes. The concern is, however, not unique for ill-gotten money. Criminal activity can be considered a subset of the informal economy, which is particularly large in low – and middle– income countries.[243] Both illegal and informal (that is, legal but

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239 See D. Chaikin and J. C. Sharman *Corruption and Money Laundering, A Symbiotic Relationship* (New York: Palgrave Macmillan, 2009) cited in S. Yikona *et al* note 180 p.14.

240 S. Yikona *et al note* 180 p.14.

241 *Ibid*.

242 *Ibid*.

243 *Ibid*, p.15.

unrecorded) activities will distort economic statistics, or at least make the official statistics less reliable.

3.7 Understanding the Legal Response: History and Development

The history or background of ML, together with the subsequent international response, underline a unique blending of both international and national responses to AML law and enforcement– a development that highlights a vertical application of substantive norm making[244]in international law. The international response highlights the limits of the formal boundaries of mutual exclusiveness, which was inherent in a post-Westphalian world.[245] The emerging trend is not so much on the form of the instruments but rather on the substance of existing norms in an area of law, and the emphasis is less on the theory of a system of rules, but rather on a '*process*' where perspectives and goals play a prominent part.[246]

The subsequent legislative response to ML is classed into three broad categories: vis-à-vis *regulatory development*; *criminalisation and internationalisation* and, lastly, the *supranationalisation stage.*[247] The author has decided to adopt the above approach, (on the legal response and subsequent development of the law) since the growth and development of global ML demands a progressive response that is equal in magnitude and scale to the problem. As noted in chapter one, soft law is often explained based on the shortcoming of the 'traditional

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244 Vertical application of substantive norm-making highlights a new international law boundary that regulates not just activities between state, but as seen in the of field of Human Rights, regulates even the conducts of the individual The obligation to criminalise is seen in this light.

245 The discipline of law is becoming more cosmopolitan, partly because of globalisation jurisprudence, as the theoretical part of law as a discipline, has begun to respond to this challenge. During most of the twentieth century, mainstream Anglo-American jurisprudence focused almost entirely on two forms of law: municipal law and public international law. From a global or a broad transnational perspective, this Westaphalian focus is inadequate. Mainstream Westphalian legal theory does not seem to be well equipped to answer some important questions about the juridical status of particular legal orders. For example, what is the juridical status of EC law and even contemporary Islamic law. W. Twining 'A Post-Westphalian Conception of Law' (2003) 37(1) *Law and Society Review* 199.

246 M. McDougal *et al* 'Theories About International Law: Prologue to a Configurative Jurisprudence', *Virginia Law Journal*, 1967, at 202. Higgins noted that "International law is the whole process of competent persons making authoritative decisions in response to claims which various parties are pressing upon them, in respect of various views and interests." – Higgins *supra* note 45 p. 20.

247 The stage represents the emergence of preventive AMLC by the FATF.

sources' of international law to respond to the needs of a rapidly changing world, that requires fast, flexible, adaptable, effective, and participatory 'normative' solutions.[248] It is therefore my opinion that in order to understand the legal response to ML, there is a need to highlight the progressive nature of the legal development (from domestic to international) coupled with the ability to adapt in a rapidly changing world.

3.7.1 Regulatory Stage[249]

The starting point on the legislative ladder is the enactment of the United States Bank Secrecy Act 1970 (BSA).[250] The BSA is a federal statute that imposes and authorises the Secretary of the Treasury to require banks and financial services institutions a series of duties to report and record certain transactions that are of use for criminal, tax, and regulatory enforcement. Since that date, the evolution of ML law has gone through various phases and stages. The myriad of national, international and regional instruments has constituted a mosaic.[251]

At the inception of developing ML law, the emphasis was on the *regulative and preventive* models, stipulating the banks' duties to keep records and report transactions that might assist law enforcement agencies in carrying out their functions. This and other developments would clearly show that AML law was initially intended to curb the problem at the domestic level. The subsequent formal and informal international response was intended to strengthen an international AML response.

Seven years after the BSA, a self–regulatory but similar instrument came into being in Switzerland. In 1977, Swiss bankers signed an agreement on the 'Observance of Care by the

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248 I. Alkan–Olsson *supra* note 142 p. 45.

249 The expression 'regulation' is found in both legal and non-legal contexts. The expression for our purpose may be described as what an American social scientist has described as the 'central meaning' of regulation: a "sustained and focused control exercised by a public agency over activities that are valued by a community". See P. Selznick, 'Focusing Organisational Research on Regulation' in R. Noll (ed) cited in A. I. Ogus *Regulation: Legal Form and Economic Theory* (Portland, Oregon, Hart Publishing, 2004), p.1.

250 The Bank Secrecy Act (1970), Pub L 91 – 508; 84 Stat 1114.

251 Shams, 'Using Money Laundering Control to Fight Corruption' cited in N. Mugarura *supra* note 177 p. 3. The mosaic is accurately a blend of binding and non-binding instruments under current international law.

Banks in Accepting Funds and on the Practice of Banking Secrecy'[252] (hereinafter CDB). This was in addition to the limited developments in the area of international cooperation, which took the form of Mutual Legal Assistance Treaties (MLAT) [253] by some key states that were faced with the problem of cross-border enforcement of law. The original purpose of the 1977 CDB was to ensure careful clarification of the identity of bank customers and to prevent the right to banking secrecy from being used to facilitate the making of transactions contrary to the CDB. This would be the case where the funds in particular are criminally derived. Accordingly, when a bank knows or should have known through the exercise of required due care that the funds were criminally derived; it was required to refrain from entering into transactions or to sever the relations with the customer.[254]

However, a subsequent revision in 1982 deleted the express prohibition concerning the criminally derived funds since it was contended that, ML was already an offence under the law. Furthermore, the banks were no longer required to investigate the origin of the funds but simply obliged to verify the identity of a contracting partner. This includes the obligation to identify the actual beneficial ownership.[255]

The interstate cooperation in penal matters, in the form of MLAT by the United States and Switzerland, was particularly significant in that it was the first such legal arrangement to be concluded between a state belonging to a civil law tradition and another belonging to the common law tradition. The emergence of the MLAT was indicative of the limits of the existing modalities of international cooperation,[256] together with the differences in tradition and legal

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252 Legislative development here was a private one 'Swiss banks, Swiss Union of Banks and the Swiss National Banks in Accepting Funds and on Practice of Banking Secrecy'; referred to as *Agreement on the Swiss Banks Code of Conduct with Regard to the Exercise of Due Diligence* since the adoption it has been revised in 1982, 1987, and 1992.

253 The US – Switzerland Mutual Legal Assistance Treaty was signed as far back as 1973; referred to as *Treaty on Mutual Assistance in Criminal Matters, 12 ILM 916 (1974)* (hereinafter, US – Switzerland MLAT).

254 Buranaruangrote *supra* note 14, at 23.

255 *Ibid*, at 24.

256 Modalities of international cooperation here includes Extradition; Mutual Legal Assistance; Transfer of Prisoners; Seizure; Forfeiture of Illicit Proceeds; Recognition of Foreign Penal Judgement and Transfer of Penal Proceedings Of these lists, 'Extradition' is argued to be the only pre-war modality.

history. The MLAT is a form of bilateral treaty agreement and derives validity under formal classification in international law. It represents the first international initiative in fostering cooperation in AMLC and could be said to have been useful in determining the subsequent language in the Vienna Convention 1988 on international cooperation.[257]

The approach in the Vienna Convention 1988 is complimentary to existing domestic initiatives and was intended to take enforcement and crime control beyond the domestic borders where the predicate offence was perpetrated. This is because of the cross-border nature of the ML offence. This initial response to ML was a preventive approach, which was based on a combined approach of regulatory and preventive measures. It is stated that, the history of the BSA depicts the law as one passed in response to certain difficulties in the area of criminal, fiscal, and regulatory enforcement of law and *cross–border crime*. These challenges, together with the limited powers of extraterritorial enforcement of law, make the element of cooperation at the treaty level inevitable – for purpose of crime prevention and enforcement of law.

3.7.2 Era of Criminalisation and Internationalisation

The 1980s saw a departure from the traditional preventive and regulatory approach to AMLC, to a period of repressive technique and subsequent internationalisation of the offence. This period witnessed an increased application of the use of penal legislation in AMLC, both at domestic and international levels. One of the most dramatic developments during this period was the emergence of the global AML regime, which combines both treaties and informal responses to ML.[258]

The ML law (as a result of these developments) ceased from being a mere regulatory and preventive tool, but became a penal legislative response based on the repressive AMLC.

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257 Article 2(1) Vienna Convention.

258 The period saw the emergence of Basel Principles as an aspect of the first informal international response to the problem of money laundering.

The emergence of penal legislations to ML was simultaneous both in the United States and in the United Kingdom.[259] The parallel development in both states was evidenced by the introduction of ML prohibition law, which was complemented by other existing measures on the prevention and regulation of the laundering process.

In the United State, the passage of the Money Laundering Control Act (MLCA)[260] makes it a criminal offence to engage in the laundering of criminal proceeds. This includes willingly handling assets that are fruits of criminal activity: or to use structuring methods in order to evade the reporting requirements of law enforcement.[261] In addition, the Act imposed harsher civil and criminal forfeiture laws on money launderers and financial institutions who assist them in their practice.[262] A similar approach was adopted in England, whereby the Drug Trafficking Offences Act 1986 (DTOA) made it a criminal offence to enter an arrangement where the proceeds of another's drug trafficking activities are laundered.[263] The UK DTOA created an offence of assisting any person launder drug proceeds and also contained a disclosure defence.[264] Overall, both of these responses represented the type of piecemeal response that was prevalent at the time and were limited to drug related type of ML.

Based on this development, the criminalisation of ML in the United Kingdom and the United States witnessed the emergence of a new control or repression component being added to the legal approach to the already existing regulatory/preventive measures already adopted. The ML legal regime that evolved out of this development placed equal emphasis on both aspects of the regulatory and preventive strategy, which was reflective of the principles and mechanisms already introduced by earlier methods.

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259 UK Drug Trafficking Offences Act (1986), and the United State Money Laundering Control Act (1986).

260 PubL No 99 – 570, 100 Stat 3207 (1986), codified at 18 USC SS1956 – 57 and 31 USC SS5324 – 6 (hereinafter, MLCA 1986).

261 18 USC SS 1956 and 1957.

262 31 USC SS5324.

263 Drug Trafficking Offence Act 1986, section 24; The Prevention of Terrorism (Terrorism Provision) Act 1986 was based on similar purpose and object.

264 See section 24 of the DTOA.

However, in 1988, the trend towards criminalisation and internationalisation took a major leap. At the end of that year, the Vienna Convention 1988 was adopted. The language in the treaty did not actually use the term 'laundering', but the Convention defined a very broad offence of handling the proceeds of drug trafficking in any conceivable manner and imposed on states parties a duty to criminalise this conduct.[265]

The Vienna Convention 1988 is important in three aspects, in relation to ML. First, it's with respect to the provision in Article 3(1) of the convention, which require the parties to criminalise drug ML. Secondly, the convention required the parties to put in place measures to immobilise proceeds of crime.[266] The Vienna Convention 1988 also recognised the international nature of drug trafficking and related ML. It expressly contains provisions on mutual legal assistance and extradition (concerning relevant offences), as well as confiscation cooperation.[267] Cooperation here is strengthened by Article 5(5) (b) which permits the sharing among cooperating states either on regular or case by case basis of proceeds or property, or funds derived from the sale of such proceeds or property in accordance with domestic law, administrative procedure, bilateral or multilateral agreements entered into for this purpose.

Given the ambit of the Vienna Convention 1988 the relevant provisions of the convention is said only to pertain to the confiscation and laundering of drug proceeds, and not of the proceeds of other crime. Nonetheless, there are also a number of substantive criminal law provisions, as well as mechanisms for international cooperation in criminal matters as expressed in the language of the treaty. It is thus argued that the most important contribution

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[265] See Article 3 of the Vienna Convention, 1988, together with the subsequent Articles 6 of both the Palermo Convention and 1990 Money Laundering Convention.

[266] The ambit of Article 5(9) adequately provides for this, and the import is that parties are expressly prohibited from refusing the above requirements on the ground of bank secrecy laws. The requirement is said to reflect one of the aims of the Vienna Convention, which is to deprive drug traffickers of illicit proceeds and thereby eliminate their main incentive for engaging in drug traffics.

[267] Cooperation via these methods – mutual legal assistance and extradition – is effective tools in preventing the use of banking secrecy laws as an excuse for non-cooperation on the part of the Parties.

of the Vienna Convention 1988 to ML law is the creation of an international obligation upon states to repress or criminalise a series of laundering offences.

Although the Convention does not use the term 'laundering', its definition of the offence remains the prototypical definition of ML,[268] globally. Whilst the Vienna Convention 1988 is limited in scope, since it is strictly related to drug offences, the Convention did provide great impetus for the internationalisation of repressive AMLC.

The Vienna Convention 1988 is not isolated in this field of the internationalisation of the laundering offence; there are other categories of instruments that were also useful in promoting the much-needed consensus on the insidious nature of this form of criminality. Some of these instruments, unlike the Vienna Convention 1988, were conceived within the relevant institutional framework of the organ creating them, albeit with a global appeal and inclusion of non-members as parties to such agreements. One such instrument is the 1990 Money Laundering Convention, the text of which was drafted by a limited committee within the European Committee for Crime Problem (ECCP).[269]

The 1990 Money Laundering Convention constitutes the first international binding legal instrument that focuses exclusively on ML. Like the Vienna Convention 1988, it deals only with the repressive fight against ML. It contains a number of substantive criminal law provisions, as well as mechanisms for international cooperation in criminal matters. The convention, however, differs from the Vienna Convention 1988 in that the scope is not limited to drug proceeds, but in principle encompasses the proceeds from any offence.[270] The drafters

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[268] According to the Official Commentary on the Convention, the use of the word money laundering was abandoned because of its novelty and on account of translation difficulties Commentary on the United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances 1988, E/CN7/590 (1998) p 351 (hereinafter, the Official Commentary).

[269] G. Stessens *supra* note 14 p. 23. Of importance also in this area is the Palermo Convention, which specifically creates a laundering offence in Article 6 of the Convention.

[270] Article 6 of the Money Laundering Convention defines the offence of money laundering and does not limit the crime to only drug offences, but rather defines the predicate crime to be inclusive of the laundering of 'illicit property'; (d) went on to include in the definition, other offences of conspiracy attempt aiding, abetting, facilitating, and counselling the commission of any offence established in accordance with the article.

however attempted to use as far as possible the same terminology as the Vienna Convention 1988.[271] One unique feature about the convention is that it is open to all states, including states who are not members, and therefore who are not members of the Council of Europe.[272]

While the last two categories of instrument on internationalisation were focused on the criminal/repressive measure on the development of ML law, there is a third and most important body in this category. The emphasis of this body was not on criminalisation, but rather on preventive measures harnessed through prudential regulation of financial institutions. Thus, at the time of the coming into force of the Vienna Convention 1988, a parallel legal development was taking place in Basel, Switzerland, and in December that year, the Basel Committee on Banking Supervision issued a *Statement of Principles on the Prevention of Criminal Use of the Banking System for the Purpose of Money Laundering* (The Basel Principles 1988).[273] However, the Statement has no legal force (informal soft law), since it is a general Statement of ethical principles and its implementation will depend on national practice and law.[274]

The importance of the Basel Principle 1988 lies in the fact that it enabled internationalisation of the law. The Basel Principle 1988 is the first international instrument to address the issue of ML internationally. Whilst the Vienna Convention 1988, focused on ML repression and left out the preventive aspect of ML law, this parallel development bridged the gap by attempting to develop some consensus on the preventive ML law within the narrower context of the Basel Committee on Banking Supervision (hereinafter Basel Committee).

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271 The import of the last point is based on the fact that, implicit in the Money Laundering Convention, is the same emphasis on the process of laundering and not with regards to any specific act. While the Money Laundering Convention was stated to be a binding legal document, its application field could be said to have been undermined by relevant institutional framework under which it was created.

272 This explains the non-application of the epithet 'European Convention' to it, but rather the reference to it as the Money Laundering Convention. The convention was originally open for signature on 8 November 1990 and by the end of 2010, the Money Laundering Convention has been ratified by 48 states.

273 Basel Committee, *The Basel Committee – Compendium of Documents,* col1, ch III (May 2001) available at ≤www.bisorg≥ last visited on 7 October 2014. The Basel Committee comprises of the authorities charged with banking supervision of 12 western states: Belgium, Canada, France, Germany, Italy, Japan, Luxembourg, the Netherlands, Sweden, Switzerland, the UK and the USA.

274 See the sixth paragraph to the Preamble.

The Basel Principles of 1988 is based on the assumption that banks are being used unwittingly for ML and that the cooperation of financial institutions with law enforcement agencies will be very useful as a way of preventing this use.[275] The principles, accordingly, encourage the banks to put in place effective procedures that:

- ensure the identification of any customer that enters a relationship with the bank;
- prevent the engagement of the bank in transactions that appear illegitimate and
- secure close cooperation with law enforcement.[276]

Prior to the Basel Principles 1988, supervisory authorities were ambivalent about their role in the fight against ML thus resulting in some states imposing direct responsibility in this regard on the financial supervisory authorities – while others did not even bother to impose any such responsibility or duty.[277] The latter represent cases where supervisory authorities lack the jurisdiction to play a role in the suppression of ML through the financial system.

The value of the Basel Principles of 1988 was that it established some convergence in approach amongst its members by attempting to create a prudential system in suppressing the use of the financial system for ML purposes. The 'Preamble' to these Principles acknowledges that, "the primary function of [banking supervision] is to maintain the overall financial stability and soundness of banks, rather than to ensure that individual transactions conducted by banks customers are legitimate".[278] It goes on to argue that a bank's association with criminals is bound to result in adverse publicity that might undermine public confidence in banks and hence their stability. This point was based on the fact that, association with criminals expose banks to the possibility of fraud by those undesirable customers as well as by their own employees, whose integrity may be undermined by this inopportune association.[279]

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275 H. Shams *supra* note 39 p. 38.
276 See Chapter 5 below for more on the status of the Basel Committee.
277 *Supra*.
278 *Ibid.*
279 See Blum *et al supra* note 42 and R.W. Baker *supra* note 231.

The logic of the Principles has resulted in tying the ML suppression goal with the broader purpose in bank supervision and gradually led to the regulatory aspect of ML law becoming a core element of the legal regime as a whole.

In conclusion, the Basel Principles 1988 in terms of internationalisation of ML law were to the *regulatory/preventive* side of the ML regime, what the Vienna Convention 1988 was to the *criminal/repressive* side of it. Moreover, the influence of the Basel Principles 1988 did not remain confined to its limited membership; the extension was thus typical of the operation of the Basel Committee and was explicitly envisioned in the preamble to the Principles.[280] The Basel Principles 1988 highlights the emergence, influence of soft informal law, and is categorised under the preventive AMLC.

3.7.3 Supranationalisation Stage

Supranationalisation in the present context connotes an influence or power that transcends national boundaries or governments, and is said to be measured by the degree to which the ordering of a certain aspect of social life is conducted by an agency in a manner that derogates from states' sovereignty and the principle of consent in international order.[281] Whenever the term is used, it denotes an institutionalised exercise of power or authority over the state not by another state but by an international organisation or organ. The powers typically exercised are said to be either juridical or prescriptive. This would be the case, where the supranational character has been attached to an international organisations or organs that are either adjudicating disputes between states or prescribing rules of conduct to be followed by states.[282]

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280 *Supra* note 274.

281 Moreover, according to the Oxford English Dictionary, 2nd ed, it means having power or influence that transcends national boundaries or government.

282 The UN Collective Security System, by virtue of chapter 7 of the Charter stands out as an important example of a supranational enforcement mechanism in international law. However, the role of the International Court of Justice (ICJ) remains an important one in the area of supranational adjudication on matters of international concern.

Thus, in the context of the ML regime the aspect of supranationalisation centre on the FATF,[283] as a body created by the G7 Summit in Paris in 1989. It was initially given the specific task of studying the ML phenomenon and ways to deal with it. However, since the terrorist attack on the United States of America (and the subsequent global war on terror), the FATF is now the global ML and TF watchdog. It is, therefore, an inter-governmental body that sets international standards aimed at the preventing the harmful effect of ML activities on society. It represents a policy body that works to generate the necessary political will to bring national legislative and regulatory reforms to combat ML.[284] As an international body commissioned with the specific task of resolving the problem of controlling and preventing ML in the context of the global economy, its operation is said to have transpired into a supranational agency with a distinct feature. Anti-money laundering policies were being formulated within a deliberate unrepresentative agency and accordingly imposed worldwide through aggressive enforcement mechanisms and quasi-judicial review processes.[285]

Established in 1989 by the G7 Summit held in Paris, as a response to concerns about negative implications of ML on the financial systems, as of July 2020, it has 37 member Jurisdictions, 2 International Organisations – European Commission and Gulf Cooperation Council, and 31 international and regional organisations which are Associate Members or Observers. Its mission was initially to examine techniques and trends in ML, to review measures taken at national and international levels, and to set out measures still necessary to be taken.[286]

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283 *Supra* note 7 on the FATF.

284 Buranaruangrote *supra* note 14 at 33.

285 H. Shams *supra* note 39 p. 209.

286 During 1991 and 1992, the FATF expanded its membership from the original 16 to 28 members. In 2000, the FATF expanded to 31 members. In 2003 to 33 members and 2007 it expanded to 34 members. As at the time of writing, the FATF currently has 39 members, 37 jurisdictions and 2 regional organisations (Gulf Cooperation Council and the European Commission). These 37 members are said to be now at the core of global efforts to combat ML and TF available at ≤www.fatf-gafi.org≥.

Following its creation by the Summit, the FATF assumed a life of its own, without any limitations of mandate or timeframe. After a meeting called by France, the FATF produced its first report ahead of the deadline in February 1990,[287]and the most important feature of the 1990 Reports was the Forty Recommendations for action. The Recommendations as amended and interpreted over the past decade constitute the present blueprint of anti-money laundering law and TF.[288] The most important element in the Forty Recommendations is that they help in shaping domestic legislation.[289]

The other aspect on supranationalisation is concerning the EC ML Directives. Like the FATF 40 Recommendations, it has also yielded a harmonising influence on the Prevention of the Use of the Financial System for the Purpose of Money Laundering. No less than fifteen FATF Recommendations have found their way to the EC ML Directives, which made them into binding law for EC member states.[290] The EC ML Directives is an integral part of the European Union law making. This is because the directive whilst not a part of traditional international law, functions with the same binding effect as a treaty under the European Union on member states.[291]

The EC ML Directive is thus, taken to have a supranational effect given the doctrine of the supremacy of the EC law, which emerged from the European Court of Justice Decision in *Costa* v. *ENEL*.[292] However, the principle of direct effect was established in relation to the

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287 FATF, Report 1990 (7 Feb 1990).

288 The FATF exercise is subject to period review, and the more recent review took place in 2008, which this relates to its current mandate (for 2012-2020). The FATF 40 Recommendations now includes the 9 Recommendation on Terrorist Financing. The title for the recommendations after the latest review is "International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation - the FATF Recommendations".

289 An example here is the New Zealand Anti-Money Laundering and Counter Terrorism Act 2009. The Act incorporates most of the recommendations of the FATF and transforms them into domestic hard law legislation.

290 G. Stessens *supra* note 14 p.18. The latest directive is the sixth Directive (EU) 2018/1673 of the European Parliament and of the Council (hereinafter EC ML Directive) Other earlier directives in this regard are the Fifth EC ML Directive 2018/843, Fourth EC ML Directive 2015/849, Third EC ML Directive 2005/60/EC Directive 2001/97/EC of 4 December 2001 – amending Council Directive 91/308/EEC on the prevention of the use of the financial system for the purpose of money laundering. See Chapter 4 on the legal effect of EC Directives.

291 Article 189 of the EEC Treaty (now Article 249 EC) provides for the binding nature of directives, and this is said to be only in relation to each Member State.

292 *Falminio Costa* v. *ENEL* (1964) ECR 585, 593.

Treaties of the European Union, by the European Court of Justice (ECJ), in *Van Gend en Loos* v. *Nederlandse Administratie der Belastingen*[293] (commonly referred to as *Van Gend en Loos*).[294] Nevertheless, the principle has subsequently been loosened in its application to treaty articles[295] and the ECJ has expanded the principle, holding that it is capable of applying to virtually all of the possible forms of EU legislation,[296] the most important of which are regulations and in certain circumstances directives.

The modalities for cooperation concerning the international AML law could thus be said to have been aimed at both repressing the laundering offence and on the *prevention* of the proceeds of crime from entering into the legal economy. The above AML legal approach is what is commonly referred to as the *twin- track controls*[297] of ML and this is perfectly captured by the various stages in the legal development of the ML law.

Whilst the repressive measure was aimed at criminalisation and confiscation of the proceeds of crime,[298] the preventive aspect was directed at creating obligations for financial

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293 [1963] ECR 1; [1970] MLR 1. Other cases in this area are, *Defrenne* v. *Sabena* (No2) (43/75) [1976] ECR 455, in which the rights of an air hostess for equal pay guaranteed under Article 141 (old 119 EEC) were upheld against the employing airline Sabena who were in breach of the obligation. This ability to enforce rights against individual legal entities is termed 'horizontal direct effects' as it applies between two individuals See also *Walrave* v. *Associate Union Cycliste International* (36/74) [1974] ECR 1405 and *Hurd* v. *Jones* (Inspector of Taxes) (44/84) [1986] ECR 29.

294 The ECJ first articulated the doctrine in the case of *Van Gend en Loos.* The ECJ in that case laid down the criteria (commonly referred to as the 'Van Gend Criteria') for establishing direct effect The provisions must: be sufficiently clear and precisely stated. Be unconditional or non-dependent and confer a specific right for the citizen to base his or her claim on. See generally N. Foster *Foster on EU Law* (New York: Oxford University Press, 2006) pp. 174 -176.

295 *Van Gend en Loos* was a claim based on treaty article. The doctrine is therefore, applicable when the particular provision relied on fulfils the above criteria.

296 In *Defrenne* v. *SABENA* [1974] ECR 631 the ECJ decided that there were two varieties of direct effect. The difference between a Vertical direct effect and a Horizontal direct effect, is based on the entity against whom the right is to be enforced. Vertical direct effect concerns the relationship between EU law and national law, while Horizontal direct effect concerns the relationship between individual (including Companies). Directives are usually incapable of being horizontally directly effective due to the fact that they are only enforceable against the state. However, certain provisions of the treaties and legislative acts such as regulations are capable of being directly enforced horizontally.

297 See Buranaruangrote *supra* note 14.

298 ML is thought to be a derivative and confiscation is a tool to deprive perpetrators of proceeds generated from crime.

institutions.[299] This may include other agencies in the state (both private and public) taking steps to reduce ML. AML preventive measures, although initially limited to banks, has extended to non-banking financial institutions, even non-financial businesses, and certain professions, such as casinos, dealers in precious metals and stones and lawyers.[300]

3.8 Understanding the Global AMLC Strategy

According to Gallant[301]a new crime control strategy surfaced in the 1980s, designed to control the phenomenon of the proceeds of crime. The framework of this strategy originates principally in international law with national actors shaping the global model to suit national legal imperatives. Several discrete and interconnected factors contribute to the trepidation engendered by the link between money and crime.[302] With the evil clearly identified, countermeasures began to take shape. As noted in the last chapter, much of the press for strategies of containment comes from the harmonisation of AMLC through international soft law.

In this, the need for global harmonization springs largely from the global character of crimes with significant financial undercurrents as well as the increased mobility of capital and commodities brought about by globalisation.[303] The trade-in illegal drugs ignore national boundaries, with drugs produced in one country and sold in another. Terrorist plots conceived in one jurisdiction may be realised in another. Globalisation encourages the free movement of capital and commodities. Increased integration of global marketplaces facilitates the cross-border movement of lawful and unlawful activity alike. Global regimes, harmonised through

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299 The FATF defines the term 'financial institution' very broadly. It means any person or entity who conducts as a business a wide range of activities on behalf of a customer List of activities listed in Glossary to the FATF Forty Recommendation (2012).

300 The definition of designated non-financial businesses and profession is defined in the Glossary of the FATF Forty Recommendation (2012).

301 M. Gallant *Money Laundering and the proceeds of crime* (Edward Elgar, 2005) p. 1

302 *Ibid* p.3.

303 *Ibid* p.7.

international law, allow countermeasures to replicate the global character of the conduct they seek to suppress.[304] This is the role of soft law in countering the problem of ML, and it is a global AMLC strategy. Therefore, the global initiatives indicate the solidification of international consensus (via soft law) on a new proceeds-oriented approach to crime control through repressive and preventive AMLC.

Reviewing the global international AML legislative measures by the UN[305], the EU[306], the international best practices and industry guidelines, Ryder[307] identified a global ML policy strategy that can be divided into eight parts:

1. Implementation of international legal AML instruments;
2. Recognition and implementation of international best practices and industry guidelines;
3. Adoption of a risk-based policy;
4. Creation of competent AML authorities;
5. Criminalisation of ML;
6. Mutual Legal Assistance;
7. Preventive measure; and
8. Confiscation of the proceeds of crime.

3.9 Conclusion

The cross-border element of ML has made it impossible for the crime to be the subject of a separate regional or domestic control. The origin and development of the law clearly highlight the need for a harmonised response to the problem of ML. The limits of initial domestic AML

304 *Ibid*.
305 See *supra* note 5
306 See *supra* note 8.
307 N. Ryder *Money Laundering – An Endless Cycle? A Comparative Analysis of the Anti-Money Laundering Policies in the USA, UK, Australia, and Canada* (Routledge, 2012) p.3

responses (by the American and Swiss response) underscore the need for a better international co-ordination, which led to the various formal and informal international AMLC.

The foregoing international response, in the area of AMLC, demonstrate that both formal and informal soft law instruments can be vehicles for focusing consensus and for mobilising a consistent general response on the part of states. Subsequent chapters in this thesis will therefore build on this development and demonstrate the benefits and strength of a coordinated response to the problem of ML through soft law.

CHAPTER FOUR

Repressive Anti-Money Laundering Control

4.1 Introduction

The global response to the fight against ML consists of a repressive technique founded in criminal law and preventive technique, founded in financial regulation.[308] These techniques are the repressive and preventive AMLC, which is based on the formal treaty obligations to criminalise the offence and informal/non-treaty arrangements to prevent it. Both techniques, as would later be seen, come under our framework type of soft law – formal and informal categorisation of soft law.

Accordingly, the international AMLC is referred to as the *twin-track* technique[309] to repress and prevent global ML, through soft law. The emphasis, therefore, is on a repressive control that is focused on criminalisation and confiscation, and a preventive control that is based on obligations of financial and non-financial institutions to undertake certain measures to disclose ML operations and identification of beneficial ownership. However, the techniques are not independent one from the other, as certain aspects of preventive control have been transformed into criminal legislation,[310] and criminalisation of ML has since become a tool for international co-operation and relevant MLA.

The techniques are thought to have evolved from an initial American repressive or penal legislative model, and a Swiss preventive or private sector initiative.[311] The American penal model, just like existing treaty-based repressive technique, is based on criminalisation and

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308 G. Stessens *supra* note 14 p. 108 and T. Buranaruangrote *supra* note 14 at 8.

309 For more on this concept see the works of T. Buranaruangote *supra* note 14 at 37 and G. Stessens *supra* note 14 p. 108.

310 For example, in New Zealand, the Anti-Money Laundering and Counter Financing of Terrorism Act, 2009, incorporated (as part of domestic legislation) recommendations from the FATF that has elements of the Basel Principles.

311 *Supra* pp. 91-99.

confiscation of the proceeds from crime.[312] However, the main reason behind the Swiss model was for Bank's self-regulation and prevention of ML in the financial system. The role of financial and non-financial institutions in prevention of ML has since gained prominence through some of the informal/non-binding arrangements in this area. The focus here is on the obligations of financial and non-financial institutions to undertake certain measures to disclose ML operations and to identify the 'beneficial ownership' of the proceeds of crime.[313]

Thus, the repressive and preventive AMLC underscore the importance of an international response to ML, which centres on an initial formal treaty obligation to repress the crime, and an informal non-treaty response to prevent it. The measures were, therefore, with an instance of the need to control organised crime and to prevent the negative impact of ML on the global financial system.[314] The significance of these techniques is underlined by the treaty and non-treaty response, as the failure of 'traditional sources' of international law to respond to the needs of a rapidly changing world has now prompted fast, flexible, and adaptable/effective participatory 'normative' solutions.[315] Our framework type of soft law underscores this narrative.

ML criminalisation under the repressive technique was effected through a broad definition of the offence of ML under both the UN[316] and EU[317] Conventions. This policy definition tended to be much broader than the cases that instigated the concern and initiated the process of laundering. This breadth was incorporated into the legal definitions of the offences

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312 Most criminal justice systems are traditionally thought to be familiar with the possibility of confiscating property as a result of its relation to an offence. Article 1(f) of the Vienna Convention, 1988 refers to confiscation as the 'permanent deprivation of property by order of a court or other competent authority' and Article 1(d) of the 1990 Money Laundering Convention speaks of a 'penalty or a measure, ordered by a court following proceedings in relation to a criminal offence or criminal offences resulting in the final deprivation of property'.

313 Under this category will be the work of the FATF, Basel Principles and the various EU EC ML Directives.

314 T. Buranaruangrote *supra* note 14 at 8.

315 I. Alkan-Olsson *supra* note 142.

316 Under this category is the Vienna Convention, 1988, the Palermo Convention.

317 1990 Money Laundering Convention and the 2005 Council of Europe Convention against Money Laundering

of ML, which tended to be open-ended and unqualified. The only restriction of the *actus reus* in a ML offence is the subject of the predicate crime. Apart from that, the acts forming the offence are general enough to encompass any possible handling of these proceeds. The purpose of the acts is, therefore, all encompassing. The broad definition of the offence of ML corresponds to our earlier classification of formal soft law, under which we considered treaty provisions that are imprecise, subjective, or indeterminate in language.[318]

According to Dupuy, that an agreement is soft or hard law does not refer to the formally binding character of the instrument. Here the 'softness' of the instrument corresponds to the 'softness' of its contents.[319] This concept of soft law refer to treaty provisions that do not tend to create definitive obligations, despite their legally binding form, but are rather imprecise or flexible in character. The framework type of formal soft law is captured in the broad definition of ML and has led to the harmonisation and approximation of domestic AML criminal legislation. This is important for both formal and informal cooperation and is relevant for mutual legal assistance (MLA) in the fight against ML.

Accordingly, the approach under this chapter will be to examine the nature of the broad definition of the obligation to criminalise ML and how this has been transposed into domestic legislation. The chapter will, therefore, examine the broad definition of the obligation to criminalise under relevant treaties and a comparative study of domestic response to this obligation to criminalise ML. The chapter does this by examining the subject of the broad definition to criminalise, the elements of the offence of ML and the impact of the lack of uniformity in the definition of the predicate crime on harmonisation and approximation of domestic AML for purpose of international cooperation.

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318 C. Chinkin in D. Shelton *supra* note 108 p. 25.

319 P.M. Dupuy *supra* note 121.

In carrying out the comparative study, the chapter will examine the subject of the broad definition and the predicate crime in the United Kingdom, Canada and South Africa.

Broad Definition of the Obligations to Repress Money Laundering

The repressive AMLC represents a strategy that includes criminalisation of ML and confiscation or forfeiture of criminal profit. The obligations to criminalise ML that flowed from the UN and Council of Europe Conventions has led to a plethora of domestic criminal legislation. These Conventions, together with the UN Model Law on ML, are essential for legal harmonisation and approximation of domestic AML law and international cooperation.

Harmonisation and approximation of domestic law should therefore be seen as a soft law solution to the problem of territoriality of the criminal law and extra-territorial reach of crime. This is done by generating soft law norms that are incorporated by the national legislature into domestic law. An agreement that is to work between states with divergent legal systems, traditions and practices, in the area of ML, is likely to result in an instrument which, having taken into account the views and requirements of all potential states parties, represents the best available compromise on all issues rather than reflecting the most effective regime.[320]

The broad definition of ML is based on this understanding, and this is part of the reasons for the choice of soft law. As noted in chapter one, soft agreements lower the costs of reaching consensus in most cases, they are therefore more attractive to states as contracting cost and the cost to state sovereignty (given the intrusive nature of hard law) increase. In the section below, we shall examine how the broad definition of ML through soft law is adopted uniformly in all conventions and applied in domestic criminal legislation. The approach then is to first examine the language of the obligations to criminalise ML in the various conventions and impact this may have had on the subsequent domestic criminal legislation.

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[320] J. Hatchard alluded 'Combating Transnational Crime: International Cooperation in Criminal Matters Mutual Legal Assistance (2006) *Commonwealth Legal Education Association* at 10.

4.2.1 UN Conventions

The Anti-Money Laundering Unit (AMLU) of the United Nations Office on Drugs and Crime (UNODC) is responsible for carrying out the Global Programme against Money Laundering (GPML), which was established in 1997 in response to the mandate given by the Vienna Convention 1988.[321] The Vienna Convention 1988 expresses in its preamble the recognition by states that:

"Illicit traffic generates large financial profits and wealth enabling transnational criminal organisations to penetrate, contaminate and corrupt the structures of government, legitimate commercial and financial business, and society at all its levels" and affirms that the international community is henceforth "determined to deprive persons engaged in illicit traffic of proceeds of their criminal activities and hereby eliminate their main incentive for so doing".

Article 3(1) of the Vienna Convention 1988 therefore calls on states to criminalise the following types of ML activities:

b) (i) The *conversion* or transfer of property, knowing that such property is derived from any offence or offences established in accordance with subparagraph (a) of this paragraph, or from an act of participation in such offence or offences, for the purpose of concealing or disguising the illicit origin of the property or of assisting any person who is involved in the commission of such an offence or offences to evade the legal consequences of his actions.

(ii) The *concealment* or disguise of the true nature, source, location, disposition, movement, rights with respect to, or ownership of property, knowing that such property is derived from an offence or offences established in accordance with subparagraph (a) of this paragraph or from an act of participation in such an offence or offences.

(c) Subject to its constitutional principles and the basic concepts of its legal system:

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321 Article 3 Vienna Convention 1988.

(i) The *acquisition, possession or use of property*, knowing, at the time of the receipt, that such property was derived from an offence or offences established in accordance with subparagraph (a) of this paragraph or from an act of participation in such an offence or offences.

From the above definition, the Vienna Convention 1988 defines the obligation to criminalise ML broadly (formal soft law) and the definition of the various offences is thought not to be clearly delineated. The definition includes *conversion* or transfer of drug-derived property for the purpose of concealing the origin or evading the legal consequences of a person's drug-related activities. It also includes the mere *concealment* or disguise through any process of any fact regarding the drug-derived property such as its nature, location, dispositions movement and rights with respect to it.[322]

Although the ML offence established by the Vienna Convention 1988 has a narrow application, since it applies only to property derived from drug-related offences,[323] it is nonetheless very broad, in that it covers any manipulation of such property whether to conceal its origin, location, disposition, movement, ownership, or any other rights with respect to the property.[324] The broad definition of ML is similar to our model categorisation of soft law, where treaties with imprecise, subjective, or indeterminate language are termed 'legal soft law' in that they fuse legal form with soft obligations.[325] 'Property' is defined very broadly to include any possible kind of asset,[326] and the asset in the context generally refers to assets that are considered proceeds of the specified offences derived directly or indirectly from the offence.

It is important to note that the Vienna Convention 1988 does not address the preventive aspects of ML law. It, however, was aware of the importance of financial information for the effective enforcement of drug control systems. This recognition is reflected in the text of the

322 See also Article 6 of the 1990 Money Laundering Convention and Article 6 of the Palermo Convention.
323 Article 1(p) Vienna Convention 1988.
324 Article 3(1) (b) Vienna Convention 1988.
325 C. Chinkin in D. Shelton *supra* note 108, p. 26.
326 Article 1(q) Vienna Convention 1988.

Convention where states are explicitly precluded from denying assistance to other states merely on the basis of bank secrecy.[327] The preventive aspects of ML law were discussed in detail in a UN informal, non-binding soft law instrument that preceded and led on to the Vienna Convention 1988 namely, the '1987 United Nations International Conference on Drug Abuse and Illicit Trafficking: Comprehensive Outline of Future Activities in Drug Abuse Control'.[328] The preventive aspects of ML were also referred to with detail in the official 'Commentary on the United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances 1988.'[329] The foregoing informal non-binding references should not be neglected in terms of their impact on building an international consensus in this area of the law.

In September 2003 and December 2005, the UN Convention against Transnational Organised Crime (Palermo Convention)[330] and the UN Convention against Corruption (UNCAC)[331] respectively came into force. Both instruments widen the scope of the ML offence by stating that it should not only apply to the proceeds of illicit drug trafficking but should also cover the proceeds of all serious crimes – which covers organised crime and corruption related aspects of ML. Both Conventions urge states to create a comprehensive domestic supervisory and regulatory regime for banks and non-bank financial institutions, including natural and legal persons, as well as any entities particularly susceptible to being involved in a ML scheme. The

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327 Articles. 5(3) and 7(5) of the Vienna Convention 1988.

328 Hereinafter the Comprehensive Outline 1987.

329 Hereinafter the Official Commentary at pp 3.55-3.62.

330 The Palermo Convention, in Article 6, widens the definition of ML to include the proceeds of all serious crime, and gives legal force to a number of issues addressed in the 1988 UN General Assembly Special Session's (UNGASS) Political Declaration. Article 6 provides thus:
Each State Party shall adopt, in accordance with the fundamental principles of its domestic law, such legislative and other measures as may be necessary to establish as criminal offences, when committed intentionally:
(i) the conversion or transfer of property, knowing that such property is the proceeds of crime, for the purpose of concealing or disguising the illicit origin of the property or of helping any person who is involved in the commission of the predicate offence to evade the legal consequences of his or her action;
(ii) the concealment or disguise of the true nature, source, location, disposition, movement or ownership of or rights with respect to property, knowing that such property is the proceeds of crime;
Subject to the basic concepts of its legal system:
(i) the acquisition, possession or use of property, knowing, at the time of receipt, that such property is the proceeds of crime.

331 Article 23 of UNCAC creates as an offence the concealment and laundering of the proceeds of acts of corruption and includes further extensive measures to combat ML.

Conventions also call for the establishment of FIU, an informal, non-binding arrangement for exchange of information on AMLC.

Thus, in keeping with the requirements of the UN Conventions and other internationally accepted standards, such as the Recommendations of the FATF, the broad objective of the GPML is to strengthen the ability of member states to implement those standards through ML criminalisation and confiscation of the proceeds of crime. More specifically, GPML's objectives are:

- to assist in the achievement of the objective set up by the UN General Assembly Special Session (UNGASS) for all states to have in place legislation on ML;
- to equip states with the necessary knowledge, means and expertise to implement national legislation and UN Plan of Action against ML;
- to increase the capacity of states successfully to undertake financial investigations and prosecutions;
- to equip states with the necessary legal, institutional and operational framework to comply with international standards on countering the financing of terrorism including the relevant UN Security Council Resolutions;[332]
- to assist states in detecting, seizing and confiscating illicit proceeds.

The Programme also encourages ML policy development, raises public awareness about ML and acts as a coordinator of AML initiatives between the United Nations and other organisations.[333]

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[332] This is with particular reference to the International Convention for the Suppression of the Financing of Terrorism, which entered into force on 10 April 2002 and is not directly applicable to the subject under consideration.

[333] See W. H. Muller *et al Anti-Money Laundering: International Law and Practice* (John Wiley & Sons Ltd, 2007) p. 51.

4.2.2 Council of Europe Conventions

The European Union, through a series of reforms outlined in the Amsterdam Treaty has undertaken to construct an area of Justice, Freedom and Security. These three democratic ideals have been at the top of the Union's agenda for the last couple of years. However, this rapid expansion has not only resulted from an expansion of the competencies of the Union per se, but more so due to contingent events that have demonstrated the need for common policies in a number of key areas close to the daily life of every citizen. An area without internal frontiers must be an area of justice in order to serve its citizens, one where criminals can find no safe havens, and where citizens and business are not discouraged by cross-border obstacles in the exercising of their rights.[334]

This objective was reaffirmed in the Tampere Declaration following the European Council of October 1999. An entire paragraph was dedicated to actions necessary to counter ML. In particular, the European Council affirmed that: "Money Laundering is at the very heart of organised crime. It should be rooted out wherever it occurs. The European Council is determined to ensure that concrete steps are taken to trace, freeze, seize and confiscate the proceeds of crime".[335] No matter how effective preventive measures may be, crucial to the success and credibility of the AML scheme is that further action is taken along the line. This requires that suspicions of ML are effectively dealt with by the judiciary and lead to the swift implementation of appropriate sanctions.

An obvious starting point for action in this field was *Convention n 141* of 1990 from the Council of Europe (1990 Money Laundering Convention).[336] This laid down a comprehensive system of rules aimed at covering all procedural aspects connected to ML – from the initial investigations to the adoption and execution of the confiscation sentence. It

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334 *Ibid*., p. 63.
335 *Ibid*.
336 Available in ≤www.coe.int≥ last visited on 14 December 2020.

provided for special mechanisms promoting the widest possible cooperation required to deny criminal organisations access to ML instruments and to the proceeds of crime.

More than a deepening of existing MLA instruments, the 1990 Money Laundering Convention laid out detailed rules on the form international cooperation should take in the specific context of the fight against ML. International cooperation is critical in many laundering cases, where the proceeds of crime are often laundered in another country. The fact that all EU member states have signed and ratified the 1990 Money Laundering Convention, illustrates the value placed upon the instrument.

The Council of Europe, in May 2005, has since adopted a revamped instrument– Council of Europe Convention *n* 198 on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime and on the Financing of Terrorism (2005 Council of Europe Convention against Money Laundering).[337] The difference between this last instrument and the former is that the offence of ML is now extended to terrorist financing.

The definition of the three types of activities in the Vienna Convention 1988 was copied almost verbatim into Article 6 of the 1990 Money Laundering Convention. The predicate offence,[338] as noted above in Article 3(1) (a) of the Vienna Convention 1988, was limited to the proceeds from drug trafficking offences. However, the predicate offence under the 1990 Money Laundering Convention, in principle, applies to the proceeds from any predicate offence, even though contracting states are allowed to make a declaration (as many have done[339]) to the effect that ML will only be criminalised with respect to certain categories of predicate offences.[340] This applies to the most serious offences or solely intentional offences. The current trend is to

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337 Available at ≤www.coe.int≥ visited on 17 July 2020. This convention, whilst similar to the one before it, extends the offence of ML to include terrorist financing under Article 9 of the convention.

338 The expression 'predicate offence' borrowed from the Vienna Convention, 1988 and many subsequent international instruments, describes the offence by which the profits were acquired.

339 Declarations here were said to include those made by Austrian, Cyprus, Denmark, Italy, The Netherlands, Norway, Sweden and Switzerland.

340 Art 6(2) (a) of the Palermo Convention, provides that 'Each State Party shall seek to apply para 1 of this article to the widest range of predicate offences. The focus here is on organised crime.

cover all serious crimes, particularly those criminal activities that generate large amounts of profit.[341]

4.3 The Criminal Offence of Money Laundering

As noted above, the offence of ML was drafted broadly, which relates to three types of criminal conduct- *conversion, concealing and acquisition* of criminal property or criminal proceed.
The conducts are aimed at extending the application field of the obligations to criminalise ML by drafting the offence broadly to cover every possible manipulation of criminal proceeds,[342] or property,[343] whether to acquire, convert or conceals, the origin, location, disposition, movement, ownership, or any other rights with respect to the criminal property or proceed.

The definition of the offence under the Vienna Convention 1988 is limited to drug-related offences, but subject to that, Article 6 (1) (a) of the Palermo Convention corresponds to Article 3(1) (b) of the Vienna Convention 1988.[344] Similarly, Article 6(1) (b) of the Palermo Convention corresponds to Article 3(1) (c) (i) and (iv) of the Vienna Convention 1988.[345] On the subject of the intention to commit the crime Article 6 (1) (f) of the Palermo Convention also corresponds to Article 3(3) of the Vienna Convention 1988.[346]
In addition, the FATF in its 1990 Report adopted as a working definition a description of ML virtually identical to that in the Vienna Convention 1988, and its current 'Forty Recommendations' urge states to criminalise ML on the basis of the Vienna Convention 1988

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341 See Article 1(e) of the 1990 Money Laundering Convention, Article 1(7) third EC Money Laundering Directive, Recommendation 3 of the FATF, and the Resolution S-20/4 D on Countering Money Laundering at the Twentieth Special Session of the UN General Assembly devoted to 'countering the world drug problem together' in New York, June 10, 1998.
342 *Infra* pp. 119-134 on the *actus reus of ML*
343 *Infra* pp. 145-147 on the concept of 'property'
344 See also Article 23 (1) (a) (i) of UNCAC and Article 9 (1)(a) of 2005 Council of Europe Convention against Money Laundering
345 Article 23(1) (b) (i) of UNCAC and Article 9 (1) (c) of the 2005 Council of Europe Convention against Money Laundering.
346 Article 28 of UNCAC and Article 9(2)(c) of the 2005 Council of Europe Convention against Money Laundering

and the Palermo Convention.[347] Even closer to the text of the Article 3 of the Vienna Convention 1988 was Article 6(1) of the 1990 Money Laundering Convention. A new feature of the 1990 Money Laundering Convention was its application where the predicate offence was committed outside the jurisdiction of the state in which the ML offence was being tried,[348] a principle adopted in Article 6(2) (c) of the Palermo Convention. In addition, Article 9(1) of the 2005 Council of Europe Convention against Money Laundering is virtually identical to Article 3 of the Vienna Convention 1988 and Article 6(1) of the Palermo Convention.

Similar language has been used in European Community instruments. The First EC ML Directive on the prevention of the use of the financial system for ML[349] took further the approaches of both the Vienna Convention 1988 and 1990 Money Laundering Convention; both were referred to in its Preamble. It also reflected the view of the European Commission that the Community had a duty to protect its financial system.[350] While the First EC ML Directive requires that member states ensure that, the laundering of the proceeds of any serious crime is treated as a criminal offence,[351] its main purpose is to ensure that credit and financial institutions adopt a system, which allows effective supervision of their customer.[352]

The effect of a 1998 Joint Action[353] by the European Commission was that no member states would exercise a right of reservation against the definition of serious offences contained in the 1990 Money Laundering Convention, offences with a maximum prison sentence of more than one year or a minimum sentence of more than six months. Similar provisions in the Second EC ML Directive later replaced the Joint Action. The Second EC ML Directive itself was

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347 Recommendation 3.

348 Article 6(2) (a) of the 1990 Money Laundering Convention.

349 91/308/EEC, OJ L166, 28.6.1991 implemented in the United Kingdom by Part III of the Criminal Justice Act 1993, amending Part VI of the Criminal Justice Act 1988, and by the provisions of Part III of the Drug Trafficking Act 1994.

350 See the proposal contained in COM (90) 106 final cited in D. McClean *Transnational Organised Crime: A Commentary on the UN Convention and its Protocol* (New York OUP, 2007) p 70.

351 Article 2 of the First EC ML Directive.

352 An aspect that would later be the subject for discussion when the preventive AMLC is considered.

353 Joint Action on money laundering of 3 December 1998, OJ L333, 9.12.1998 cited in D. McClean *supra* note 350.

substantially amended in 2001,[354] principally by widening the scope to include predicate offences other than drug trafficking, and by extending the obligations under the First EC ML Directive to certain professions and activities outside the narrower financial sector.

The Third EC ML Directive replaced it in 2005.[355] This brought the definition of serious crime into line with the 2001 Second EC ML Directive, extended the scope to include the financing of terrorism and Internet transactions, and set out more detailed procedures for customer identification on the prevention of ML. The Third EC ML Directive was replaced by the Fourth EC ML Directive[356] which was mainly driven by the revision to the FATF Recommendations, adopted in February 2012 to address emerging AML and terrorist financing issues. The fourth ML Directive adopted a risk-based approach to tackling ML and terrorist financing, and moved away from the old rule-based system, whilst still maintaining the broad definition of the obligation to criminalise ML. The Fourth EC ML Directive was replaced by the Fifth EC ML Directive [357] which introduced new requirements for cryptocurrencies, ultimate beneficial owner register, and prepaid card transaction limits. The latest Sixth EC ML Directive [358] updates both the fourth and Fifth EC ML Directive s by broadening the scope of criminal liability to legal professionals and updates the list of predicate offences whilst imposing tougher penalties.

In the Sixth EC ML Directive, the definition of ML was taken verbatim from Article 3(1)(b), 3(c)(i), and 3(c)(iv) of the Vienna Convention 1988, but with more general reference

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354 Directive 2001/97/EC of the European Parliament and of the European Council of 4 December 2001 amending Council Directive 91/308/EEC on prevention of the use of the financial system for the purpose of money laundering, OJ L344, 28.12.2001.

355 European Parliament and Council Directive 2005/60/EC of October 2005 on the prevention of the use of the financial system for the purpose of money-laundering and terrorist financing OJ L309, 25/11/2005, p 15.

356 Directive (EU) 2015/849 of the European Parliament and of the Council of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, amending Regulation (EU) No 648/2012 of the European Parliament and of the Council, and repealing Directive 2005/60/EC of the European Parliament and of the Council and Commission Directive 2006/70/EC.

357 Directive (EU) 2018/843 of May 2018 amending Directive (EU) 2015/849 on the prevention of the use of the financial system for the purpose of money laundering, or terrorist financing and amending Directive 2009/138/EC and 2013/36/EU.

358 Directive (EU) 2018/1673 of 23 October 2018 on combating money laundering by criminal law.

to 'criminal activity' substituted for that to drug offences. The definition of ML offences therefore forms part of an international consensus to extend the scope of the offence of ML, through soft law, by defining the offence broadly to accommodate every manipulation of the offence. A most influential formulation is that in Article 3 of the Vienna Convention 1988, a text itself strongly influenced by the then legislation in the United States.[359]

The remainder of this section will examine components of the offence of ML, the subject of criminal property and the scope of the predicate offence, as a way of understanding how domestic legislations have responded to the broad definition of the offence of ML and criminalisation as a tool for the repression of ML.

4.3.1 Examining the *Actus Reus* of Money Laundering

It is a fundamental principle of criminal law that a person may not be convicted of a crime unless the prosecution have proved the existences of both physical element (*actus reus)*[360] and the mental element (*mens rea)*.[361] Later in this section, we will address the subjective or mental element of the criminal offence of ML. This section will try to examine the implementation of the physical *actus reus* elements of ML offence in domestic legislation through a broad definition of the offence. The section uses case law and legislation from mainly the United Kingdom and other jurisdictions to throw more light on the underlying subject of the offence of ML.

The legal definitions of the process of ML are to be found in the provisions defining the *actus reus* of ML offences. As indicated above, the most universally accepted definition of ML as an offence is that of Article 3 of the Vienna Convention 1988.[362] This Article does not

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359 18 USC 1956 ff since repealed and replaced.

360 D. Ormerod *Smith and Hogan's Criminal Law* (New York, OUP 2011) p.46 and N. Cross *Criminal Law and Criminal Justice* (London, SAGE Publications 2010) p. 16.

361 *Ibid*.

362 See also Article 6 of the 1990 Money Laundering Convention and Article 6 of the Palermo Convention for similar provision.

delimit the process of ML. The Article refers to '*conversion* or transfer of property' and to '*concealment* or disguise'. The latter designation is clearly based on the purpose of the process and does not provide any hint as to what type of process is envisioned. The former description, without being restrictive, provides more suggestions regarding the process that the state parties had in mind. There is also the third category of *acquisition.* These will all be considered under this section.

4.3.2 Conversion or Transfer of Criminal Property

This offence is defined in terms which follow very closely the language of Article 3(1)(b) of the Vienna Convention 1988 and Article 6 paragraph (1)(a) of the Palermo Convention. The Conversion suggests an alteration in the form of the property or proceeds and 'transfer' suggests physical movement of the property or legal change of title. According to the Black's Law Dictionary, ninth edition, "conversion entails the act of changing from one form to another or the wrongful possession or disposition of another's property as if it were one's own".[363] On the other hand, transfer of criminal property is thought to be the act of the transferor rather than the transferee, the recipient, who will be engaged in the acquisition of the property. The issue was central to the Supreme Court of Canada's decision in *R* v. *Daoust.*[364] The court held that *transfert* in the French text of section 462.31 of the Criminal Code did not apply to the receiver of the property.

The United Kingdom's ML offences are set out in section 327-329 of the POCA 2002.[365] By section 327(1) (c) of POCA 2002, a person commits an offence if he conceals, disguises, *converts*, *transfers* or removes criminal property from England and Wales, or from

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363 Black's Law Dictionary (9th ed., LawPros, Inc, Dallas, Texas, USA 2009) p. 381.

364 (2004) 235 DLR (4th) 216.

365 Part 7 of POCA creates a series of criminal offences relating to ML. These offences are defined in loose generalised language. For example, it is an offence to enter into or "become concerned in" an "arrangement" which the person charged knows or suspects "facilitates" the acquisition, retention, use or control of "criminal property", unless that person has made a disclosure under section 338 or intended to make such disclosure but had a reasonable excuse for not doing so.

Scotland or Northern Ireland. Section 327 offence has its root in section 14 of the Criminal Justice (International Cooperation) Act (CJA) 1990, and section 14 of the 1990 Act was partially re-enacted in section 49 of the Drug Trafficking Act (DTA) 1994 (mirrored in section 93C of CJA 1988).[366]

The offence is framed in a way that ensures that the UK meets its international obligations under the relevant conventions. Indeed, the UK has exceeded its obligations as it includes an *arrangement offence* under section 328 of POCA 2002 whereas Article 3 of the Vienna Convention 1988 only provides that parties to the convention are to establish, as offences: "[T]he concealment or disguise of the true nature, source, location, disposition, movement, rights with respect to, or ownership of property, knowing that such property is derived from an offence or offences. . ."

The word conversion may have technical meanings in a number of legal systems. For example, the common law knows the tort of conversion, described in *Kuwait Airways Corporation* v. *Iraq Airways Co (Nos 4 and 5)*[367] as the principal means whereby English law protected the ownership of goods, but it is clear that in the Vienna Convention 1988 context the word bears a more natural meaning.

This is the approach adopted in the Ontario Court of Appeal in a related context. In *R* v *Tejani*[368] the defendant was charged with ML offence under section 19(2) of the Narcotic Control Act[369] which required proof of 'the intent to conceal or convert'. Rejecting arguments to the contrary, the court held that the words 'conceal' and 'convert' were not synonymous.

366 Inserted in that Act by CJA 1993, s 31.

367 [2002] UKHL 19, [2002]2 AC 883. In that case, Lord Nicholls, while disclaiming any attempt to frame a comprehensive definition, said that the basic features of the tort were threefold. First, the defendant's conduct was inconsistent with the rights of the owner (or other person entitled to possession). Second, the conduct was deliberate, not accidental. Third, the conduct was so extensive an encroachment on the rights of the owner as to exclude him from use and possession of the goods. The contrast was with lesser acts of interference. If these caused damaged, they might give rise to claims for trespass or in negligence, but they did not constitute conversion.

368 (1999) 138 CCC (3d) 366.

369 RSC 1985, c N-1

Although conceal did mean to hide, convert had a broader meaning of to change or transform. A mere currency exchange was a 'conversion' for this purpose. In another Canadian case, *R* v. *Daoust,*[370] the Supreme Court of Canada held that the word 'convert'[371] had to be given its ordinary, literal meaning.

An example of conversion is a case where in the placement stage of ML (as noted in chapter two) different types of insurance and investment policies are purchased for cash, through independent financial advisers or brokers who have persuaded themselves that the cash is of legal provenance. At a selected moment, the policy is surrendered, and a redemption cheque or funds transfer is received from the issuer.[372] On the other hand, it might involve a business that is cash intensive, which then allows the criminal cash to be mingled with that of the business and banked as if it were the legitimate proceeds of the business.

In the case of *R* v. *Fazal* [373] D had allowed another person to lodge stolen monies into his bank account. An issue arose as to whether in law he had 'converted' criminal property in these circumstances. Victim purchased goods on the Internet, which were never delivered although payment was made. D allowed another person to use his bank account. He submitted there was no case to answer as D had not converted the money, there being no act of conversion by him, only by others, even if he had acquired the relevant suspicion and knowledge. He contended that he might have been guilty of an offence under section 328 of POCA[374] but none was charged. The Court of Appeal in dismissing the appeal held that D had 'converted' the stolen monies by allowing another to use his account. A person might lodge receive, retain, or withdraw money from his account each of which would amount to converting the money concerned, by asking or allowing another agent, innocent or not, to do so. That did not prevent

370 (2004) 235 DLR (4th) 216.
371 In the context of section 462.31 of the Criminal Code, dealing with laundering the proceeds of crime.
372 T. Parkman *supra* note 209 p. 7.
373 [2009] EWCA 1697.
374 See *infra* p. 132.

the owner of the account who used or operated it, albeit with the help of an agent, innocent or not, from converting the money. The reference to 'converting' in POCA was not necessarily the civil tort of conversion but could not be far removed from its nature.[375]

In *DPP* v. *Naylor*[376] a man, who was a second-hand car dealer, was convicted of ML. He had accepted cars bought with the proceeds of crime to sell through his business. In addition, travel agents are also thought to be good targets for this type of ML offence. A money launderer in this case may book an expensive holiday but cancel it before departing so that a refund by cheque is returned with a minor cancellation fee deducted there from.

Companies can also play a central role in ML schemes of this kind. It has been commonly appreciated for many years that the shield of incorporation is used to assist in the perpetration of fraud and other financial crimes. According to the FATF:

"The common methods identified by Irish law enforcement through which criminals have laundered money in Ireland have been through:

- the purchase of high value goods for cash;
- the use of credit institutions to receive and transfer funds in and out of Ireland
- the use of complex company structures to filter funds".[377]

Corporate structures may be used to disguise the source or nature of illegal funds by channelling such funds through them in order to infiltrate the legal economy. In *R* v. *H,*[378] the case concerned fraud involving 12 false identity companies, which issued invoices primarily for the sale or purchase of mobile phone. The unaccounted VAT element was approximately

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375 Conversion in civil law is a broad tort essentially concerned with wrongfully taking, receiving, or retaining another's property and although there is no *mens rea* requirement it involves dealing with another's property so far as to interfere with the owner's title to it.

376 (2006) The Irish Times, 8 November cited in S. Horan *Corporate Crime* (Bloomsbury Publishing Plc, Dublin 2011) p. 1511.

377 See FAFT's *Third Mutual Evaluation/Detailed Assessment Report Anti-Money Laundering and Combating the Financing of Terrorism – Ireland* (2006) 17 February, para 23 cited in S. Horan. *supra* note 376 p. 1510.

378 [2006] EWCA Crim 2385.

GBP 41, 600,000 and the fraud involved the use of cloned Hong Kong companies, forged invoices, and forged company documents.

Rather than pay a bookkeeper, solicitor, bank manager or a business to launder the proceeds of crime, in this type of offence, the money launderer may set up a business himself/herself. There is anecdotal evidence to suggest that criminals looking to convert their criminal proceeds into the legal economy have targeted struggling companies, which are badly in debt and in need of capital, deliberately. In some cases, the companies' officers have been persuaded to inject funds into the companies so that clean cheques emerge.[379]

With the emergence of artificial intelligence and digital technology, there is a trend towards the use of cryptocurrencies in this category of ML offence. Thus, in *AA v Persons Unknown*[380] an insurance company brought *ex parte* applications in respect of money which had been demanded from its customer as a ransom and paid in Bitcoin. The customer's computer systems had been hacked and encrypted. It received ransom demands from persons unknown (the first defendant). The insurer agreed to pay US $950,000 in Bitcoin and the system was decrypted. The money was transferred into Bitcoin account controlled by other links of persons unknown and the exchange defendant, which appeared to be based outside the jurisdiction. The links in the chains of exchange is the conversion of criminal proceeds.

The text of this first category of ML offence, under Article 3(b) (i) of the Vienna Convention 1988,[381] establishes that the conversion or transfer of property must be done with the aim of concealing the criminal origin of the proceeds of crime. The requirement that the conversion must be done with the aim of concealing the criminal origin of the proceeds or

379 S. Horan *supra* note 376 p. 1511.

380 [2020]4 W.L.R 35.

381 See also Article 6 of the 1990 Money Laundering Convention, Article 6(a) (i) of the Palermo Convention, Article 23(a) (i) of UNCAC and Article 9(1) (a) of the 2005 Council of Europe Convention against Money Laundering.

property, will immediately lead us to the second category of the offence of *concealing* the criminal origin of the proceed or property.

4.3.3 Concealing or Disguise of Criminal Property

This is defined under Article 3(1) (b) (ii) of the Vienna Convention 1988 and Article 6 paragraph 1(a) (ii) of the Palermo Convention. 'Concealment or disguise' includes preventing the discovery of the illicit origins of property or the proceeds of crime. Similar to the offence of conversion, the language in respect of the offence of concealing or disguising criminal property is drawn from various international conventions.[382]

The offence of concealing or disguising criminal property is drafted in broad terms and this is the trend in most domestic AML legislation. The language of Article 3 of the Vienna Convention 1988 provides thus: "the concealment or disguise of the true nature, source, location, disposition, movement, rights with respect to, or ownership of property, knowing that such property is derived from an offence or offences. . ." The language of the Article 3 is tailored towards criminal property in relation to drug related aspect of ML. However, this has been extended to criminal proceeds and to other predicate offence in several jurisdictions.

Section 327(1) (b) of the POCA 2002 provides for this offence. Section 327(1) (b) of POCA provides that it is an offence to conceal or disguise criminal property.[383] The terms 'concealing', and 'disguising' are not defined in POCA, but section 327(3) provides that they include concealing or disguising the nature, source, location, disposition, movement, ownership or any rights with respect to criminal proceeds. It is not clear whether 'concealing' must always involve a positive act or whether an omission or a failure to disclose the existence

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382 Article 6 of the 1990 Money Laundering Convention, Article 6(a) (ii) of the Palermo Convention, Article 23(1) (a)(ii) of UNCAC and Article 9(1)(b) of the 2005 Council of Europe Convention against Money Laundering.

383 Part 7 of POCA creates a series of criminal offences relating to ML. These offences are defined in loose generalised language. For example, it is an offence to enter into or "become concerned in" an "arrangement" which the person charged knows or suspects "facilitates" the acquisition, retention, use or control of "criminal property", unless that person has made a disclosure under section 338 or intended to make such disclosure but had a reasonable excuse for not doing so.

of criminal property might also constitute concealing. Suppose D1 knew that D2 stored painting in the loft of a house that they occupied jointly. D1 subsequently suspected (correctly) that the paintings were stolen but failed to alert the authorities of that fact. It is submitted that mere inaction is insufficient, but things done by D1 with respect to paintings after he or she became suspicious of their origin, may be enough to bring D1 within section 327 (for example locking the loft or covering the paintings with a dustsheet).[384]

The United States legislation uses very similar language to that in POCA. Title 18 of the US code makes it an offence, knowing that the property involved in a financial transaction represents the proceeds of some form of unlawful activity, to conduct or attempt to conduct such a financial transaction which in fact involves the proceeds of specified unlawful activity, knowing that the transaction is designed in whole or in part to conceal or disguise the nature, location, source, ownership or control of the proceeds.[385] In the *United States* v. *Majors,*[386] the court said that the offence was a provision structured to reach those types of ML activities designed to conceal or disguise the attributes of proceeds produced by unlawful activity. The activity that the offence seeks to prevent is the injection of illegal proceeds into the stream of commerce while obfuscating their source.

In order to prove the commission of the concealing or disguising offence in the UK, the prosecution essentially have to prove three elements. It is important to note that the evidence which is offered to prove one of the three elements may also be evidence that is offered to prove the other two elements. First, it must be proven that the property was the proceeds of crime. In *R* v. *Montila,*[387] the House of Lords held it was an essential part of the *actus reus* of ML offences that the prosecution prove that the property was, as a matter of fact, criminal proceeds. Section 340(3) provides that property is criminal property if it constitutes a person's

384 W. Blair and R. Brent *Banks and Financial Crime* (New York, OUP 2008) p. 176.
385 Section 1956(a) (1)(B)(i).
386 196 F.3d 1206 (11th Cir., 1999).
387 [2005] 1Cr. App. R. 425. Montila

benefit from conduct or it represents such a benefit (in whole or in part and whether directly or indirectly). This will usually be proved by circumstantial evidence. Second, it must be proven that the defendant knew or suspected that the property was such. Section 340(3) provides that for property to be criminal property, the alleged offender must know or suspect that it constitutes or represents such a benefit. Third, it must be proven that the defendant acted in such a way as to conceal or disguise the nature, source, location, disposition, movement or ownership or any rights with respect to the property.[388]

As noted above, the words 'conceal', or 'disguise' are not defined in POCA. When ordinary English words are used undefined in legislation, the courts assume that, in the absence of good reason to the contrary, they should be given their ordinary, natural meaning.[389] The Oxford Dictionary of English defines 'conceal' as "to not allow to be seen; hide",[390] while 'disguise' is defined as "to make something unrecognisable by altering its appearance".[391] Although there may be a difference between the ordinary meaning of the words 'conceal' and 'disguise', there appears not be a difference in the use of these words in a ML context. For example, in *United States* v. *Beddow,*[392] the court referred to the defendant using another person as "a 'front man' to disguise his ownership" of gemstones purchased with illegal drug proceeds when it could just have easily used the word 'conceal'. US indictments also tend to use 'conceal' or 'disguise' as a phrase rather than as separate terms with distinct meanings.

Thus, concealing and disguising in section 327 (3) of POCA includes concealing or disguising criminal property and its true nature, source, location, disposition, movement or ownership or any rights with respect to it. It is plain from that subsection and from the context

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388 E. Bell 'Concealing and disguising criminal property' (2009) 12(3) JMLC at 269.

389 The US supreme court discussed the plain meaning rule of interpretation in *Caminetti* v. *United States,* 243 U.S.470 (1917), reasoning "it is elementary that the meaning of a stature must, in the first instance, be sought in the language in which the act is framed, and it that is plain...the sole function of the courts is to enforce it according to its items".

390 *Oxford Dictionary of English* (New York, OUP 2005) p. 357.

391 *Ibid.*, p. 499.

392 957 F.2D 1330 (6th Cir., 1992).

as a whole that the terms are intended to be broad in their effect. Between them, they cover dealing with criminal property in a multitude of ways.[393] In *United States* v. *Sax,*[394] the court stated that those things, which could be concealed, were listed in the disjunctive, and held that the ML statute was not aimed solely at commercial transactions intended to disguise the relationship of the item purchased with the person providing the proceeds. It was rather aimed broadly at transactions designed in whole or part to conceal or disguise in any manner the nature, source, ownership or control of the proceed of unlawful activity.

Similarly, in *United States* v. *Barber and Barber,*[395] the defendants opened five joint accounts in various banks and deposited large amounts of cash into them, usually in small banknotes. Typically, a few days later they withdrew the cash in larger banknotes. Expert evidence was given explaining how the defendants' activities constituted concealment for purpose of ML. The expert testified, that by depositing cash into a bank account and then withdrawing it, the proceeds of drug sale could be concealed at several levels. First, because the deposit slip did not show the banknotes' denominations, it could not be determined later that a large number of small banknotes had been deposited. Second, because banknotes used for buying drugs often retain traces of drugs, the deposit eliminated the possibility of linking the money to drug trade. Third, depositing drug money into an account that contained legitimate income lent credence or credibility to drug proceeds. Fourth, withdrawals of large banknotes facilitated physical concealment because one large banknote was easier to conceal than several small ones.

In laundering criminal proceeds, a defendant may have a number of objectives. For example, he/she may often simultaneously be seeking to conceal the nature, location and ownership of criminal proceeds. Thus, the drafting of indictments by prosecutors, and the

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393 R. Booth *et al supra* note 4 p. 57.
394 39 F.3d 1380 (7th Cir., 1994).
395 80 F.3d 964 (4th Cir., 1996).

findings of guilt by courts, may therefore often be in relation to multiple objectives without falling foul of the principle of duplicity. In *United States* v. *Rahsepharian and Another*, a case of telemarketing fraud, the evidence showed that the defendant had income from fraud sent to a mailbox where his father would collect it and deposit it into different bank accounts, none of which were connected with the company through which the defendants committed their fraud. The Court of Appeals held that jury could reasonably infer from this evidence that these transactions were designed to "conceal the nature, location, source, ownership or control of the proceeds" and did not feel the need to distinguish between these objectives.[396]

As earlier observed, the offence of concealing or disguising criminal property is drafted in broad terms, which is intended to cover dealing with criminal proceeds, or property, in a multitude of ways. Given the transnational nature of ML, it is not surprising that the influence of soft law has been especially notable in the area of the criminalisation of ML.

4.3.4 Acquisition, Possession or Use of Criminal Property

In Article 3(1) (c) (i) of the Vienna Convention 1988,[397] apart from the concealing and conversion offences, each state is required to establish as a criminal offence of acquisition, possession or use of criminal property. This is similar to the offence in Section 329 of POCA, 2002. The section makes it an offence for a person to acquire, use, or possess, criminal property. No offence is however committed if the accused makes an 'authorised disclosure' under section 338 or intended to make such a disclosure but had a reasonable excuse for not doing so. It is also not an offence under the section if the accused gave adequate consideration at the time he acquired, used, or took possession of the property or performed a function he has relating to the enforcement of POCA or other relevant enactment. The defendant will similarly be excused

396 231 F.3d 1267 (10th Cir., 2000).
397 See also Article 6 (1) (b) (i) of the Palermo Convention.

from the crime in that section, if the conduct related to 'relevant criminal conduct' that occurs in a jurisdiction overseas and which is lawful there.

The section 329 offence has its origins in section 14(3) of the Criminal Justice (International Cooperation) Act (CJA) 1990, later enacted as section 23A of the Drug Trafficking Offence Act 1986, re-enacted as section 51 of DTA of 1994, and mirrored in section 93B of CJA 1988.[398] However, section 14(3) of the CJA was limited to the acquisition of property. Section 51 of DTA and section 93B of CJA extended the activities to 'use' and 'possession'. The prosecution must prove that the property handled is 'criminal property',[399] namely that it constitutes a person's benefit from criminal conduct, or it represents such a benefit (in whole or part and whether directly or indirectly).[400]

The word acquisition means gaining of possession or control over something.[401] In order to possess property, it is necessary that there be knowledge that there is something.[402] While possession only applies to tangible property, to acquire encompasses intangible property.[403] Put differently, acquisition means to obtain, to attain, by whatever means. It implies the act by which a person becomes the owner of something, and the thing acquired. The word acquisition covers everything that can be attained or obtained by a purchase, a donation or any other way; even what is obtained with money, in settlement, by skill or hard work, or in any similar way, although not what is obtained by inheritance.[404]

An acquisition can be obtained from another by sale, gift, purchase, and donation or in any other way. The acquisition of the proceeds or property of crime is typical ML offence, and it involves conducts envisaged in the layering stage of ML such as purchase and sale of real

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398 W. Blair and R. Brent *supra* note 384 p. 185.
399 Section 340(3) of POCA 2002.
400 *Supra*.
401 Black's Law Dictionary (2009) p. 26.
402 *Warner* v. *Metropolitan Police Commissioner* [1969]2 AC 526 (1968)52 CAR 373.
403 Such as that which is contemplated under POCA 2002, section 340(6).
404 See R. Pinto and O. Chevalier 'Money Laundering as an Autonomous Offence' (OAS-CICAD, Inter-American Drug Abuse Control Commission, Washington D.C 2000) p. 21.

estate – apartment, houses, flats, and commercial premises. It might also involve investment in financial products, which have good liquidity, which can be bought and sold easily – for example unlisted stocks and shares.

The word *possession* means "the fact of having or holding property in one's power; the exercise of dominion over property".[405] Possession has also been described as the *de facto* and *de jure* right to a material object, constituted by the intentional element or *animus* (the belief and purpose of owning the object) and the physical element or *corpus* (the control or effective enjoyment of a material object).[406] Meanwhile to '*use'* is "the application or employment of something;[407] to employ, to utilise".[408]

An example of a section 329 offence is the case of *R* v. *Gabriel.*[409] In that case, the police had searched the defendant's house and found GBP 10,000, hidden under the mattress of a waterbed, and on another occasion, GBP 6,070 inside an air pistol case. Within the house the officer observed a 42-inch plasma television screen, an ornate mahogany fireplace, a conservatory with a swimming pool and sauna, a large fridge, spa jets in the bathroom, a computer, good quality stereo equipment throughout the house, and PlayStation games and DVDs. There was also a closed-circuit television set up outside the house, which could be viewed, from a monitor in the living room. Evidence was read from Department for Work and Pension and Inland Revenue (now HM Revenue & Customs) officials to the effect that the household received social security benefits of about GBP 500 a week. The prosecution alleged that, in the circumstances, it could be inferred that the monies were proceeds of crime, and that the defendant, as the householders, knew it. She was charged with possessing criminal property.

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405 Black's Law Dictionary (2009) p. 1281.
406 *Supra*.
407 Black's Law Dictionary (2009) p. 1681.
408 R. Pinto and O. Chevalier *supra* note 404 p. 22.
409 [2006] EWCA Crim 229.

Similarly, *Griffith* v. *Pattison,*[410] the defendant Pattison was an estate agent who bought, at substantial undervalue, a house, from a known drug dealer who was awaiting the determination of confiscation proceedings against him. Pattison was charged with, amongst other charges, acquiring criminal property, namely the house.

4.3.5 The Section 328 POCA Offence: Concerned in an Arrangement

As earlier observed, the United Kingdom legislation goes further than the Conventions, and indeed further than EU ML Directives, by defining ML to include property known or suspected to constitute or represent a benefit from criminal activity.[411]It is an offence under section 328 of POCA, 2002, to enter into or become concerned in an arrangement which he knows or suspects facilitates (by whatever means) the acquisition, retention, use, or control of criminal property by or on behalf of *another person*. The section 328 offence has its origins in section 24 of the Drug Trafficking Offences Act 1986, and later section 50 of DTA 1994. Corresponding provisions relating to other forms of criminal conduct appears in section 93A of the CJA 1988,[412] and section 38 of the Criminal Law (Consolidation) (Scotland) Act 1995.

The '*another person'* need not be the person who originally obtained property as a result of, or in connection with, conduct carried on by him.[413] It is submitted that the '*another person'* referred to in section 328 of POCA 2002 can be someone named in the same indictment as the accused, although it cannot be someone named in the same count.[414] The submission is based on a decision of the Court of Appeal in *Connelly,*[415] albeit in the context of section 5(3) of the Misuse of Drugs Act 1971 (possession with intent to supply 'to another'). The key words in section 328 of POCA, 2002, are 'become concerned in', 'arrangement', and 'facilitates'.

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410 [2006] EWCA Crim 2155.
411 See *Bowman* v. *Fels* [2005] EWCA Civ 226, WLR 3083, paras [49]-[50].
412 Inserted by CJA 1993, section 29.
413 W. Blair and R. Brent *supra* note 384 p. 180.
414 *Ibid*.
415 [1992] Crim LR 296.

In *Bowman* v. *Fels*[416] the Court of Appeal took a robust and welcome approach to some of the more exaggerated views of what might amount to a breach under the section. In that case, the court held that, section 328 of the POCA, 2002, was not intended to cover or affect the ordinary conduct of litigation by legal professionals. That included any steps taken by such professionals in litigation from the issue of proceedings and securing of injunctive relief or a freezing order up to its final disposal by judgement. Thus, the central question in the case was whether section 328 applies to the ordinary conduct of legal proceedings 'or any aspect of such conduct – including, in particular, any step taken to pursue proceedings and the obtaining of a judgement'. According to the Court, Parliament could not have intended that proceedings or steps taken by lawyers in order to determine or secure legal rights and remedies for their clients should involve them in section 328 offence even if they suspected that the outcome of such proceedings might have such an effect.[417]

The section 328 offence is a source of considerable concern to those who handle or advise third parties in connection with money and other types of property. The court in that case left open whether section 328 means that a person who has done some previous act "such as giving advice, or playing a role in negotiations, can fall to be treated retroactively as having committed an offence by that act, if and when an arrangement is subsequently made".[418]

In *Kensington International* v. *Vitol*[419] the question arose of whether, by giving a bribe,[420]a person necessarily enters into an arrangement, which he knows facilitates the acquisition of criminal property by the recipient, contrary to section 328 of POCA 2002, on the grounds that the bribe, once received, constitutes the latter's benefit from criminal conduct. The Court of Appeal held that the answer is in the negative if the only arrangement into which

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416 [2005] EWCA 226, CA.
417 *Ibid.*, paras [85]-[90].
418 W. Blair and R. Brent *supra* note 384 p. 183.
419 [2007] EWCA Civ 1128.
420 Contrary to the Public Bodies Corrupt Practices Act 1889, section 1(2) or the Prevention of Corruption Act 1906, section 1, or contrary to common law (ie 'bribery').

he enters is one, by which the property in question first acquires its criminal character. A person who gives a bribe may know that it will constitute criminal property in the hands of the recipient, but that does not make him guilty of entering into an arrangement, which facilitates the acquisition of what is already a criminal property.

4.3.6 The Authorised Disclosure Defence: Section 338 of POCA 2002

It is a defence to a charge under sections 327 to 329 of POCA 2002 that a person makes an authorised disclosure under section 338 and (if the disclosure is made before he does the prohibited act) he has the 'appropriate consent', or he intended to make such a disclosure but had a reasonable excuse for not doing so. It is also a defence if he acted for the purpose of carrying out a function relating to the enforcement of any statutory provisions relating to criminal conduct or benefit from criminal conduct.[421] The expression 'authorised disclosure' is defined by section 338 of POCA 2002 to mean a disclosure authorised by a constable, an officer of HM Revenue & Customs, or a 'nominated officer'.[422] Section 337 protects disclosure – that is to say, a disclosure is not to be taken to breach any restriction on the disclosure of information 'however imposed'.[423]

However, where a disclosure has been made, it is the offence of '*tipping off'* to give information (typically to the suspected offender) which might prejudice an investigation, which might result from the initial disclosure.[424] This can cause problems to Banks and other institutions. In *C* v. *S,*[425] a bank had made a series of ML reports to the Economic Crime Unit of the National Crime Intelligence Service (NCIS). Later in civil proceedings, an order was

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421 See POCA 2002, sections 327, 328; 329(2) (a), (b), (d); and section 329.

422 Section 338(5).

423 Following amendments made by Serious Organised Crime and Police Act (SOPCA) 2005, to section 338 (SOPCA 2005 section 106(5) (6)), the disclosure must meet one of three conditions set out in section 338(2), 338(2A), or 338(3) of POCA 2002.

424 Section 333 of POCA 2002. There are exceptions, for example in respect of communications between a professional legal adviser and a client.

425 [1999]2 All ER 343 (CA).

made that the bank disclose certain papers, and the bank feared that compliance might amount to 'tipping-off'. The NCIS refused to give an assurance that it would not prosecute for that offence, and instead sought an order for the disclosure to it of the same papers. The bank faced the choice between possible prosecution and possible action for contempt of court. After an extraordinary appeal, extraordinary in that the appellant was excluded from most of the hearing, the Court of Appeal described the NCIS position as 'neither sensible nor appropriate'. It indicated that where such conflicting pressures existed, the party required to disclose should seek a ruling from NCIS as to what material they would 'clear' for disclosure, and in the case of failure to agree, the court should be asked for directions.

4.3.7 Implementing the *Actus Reus*: Other Examples

Implementing the *actus reus* of the offence of ML does take different forms in different states, and only a few selected examples, with differing degree of complexity, can be considered under this section. The aim is to show how the broad definition of ML, as stated in the conventions, is transposed into domestic AML legislation. The approach in all examples is to extend the application field of the obligations to criminalise ML by drafting the offence broadly to cover every possible manipulation of criminal process.

4.3.7.1 18 USC § 1956 of the United State of America

The United State (herein after the US) has adopted an aggressive stance towards ML and is the instigator of the 'war on drugs', which was the catalyst for the introduction of the Vienna Convention in 1988.[426] The US AML policy pre-dates those of the United Kingdom (UK) and it can be traced back to the 1990s when the Department of Treasury became concerned about the link 'between illegal activities and offshore bank accounts'.[427]Also, the legislative measure

[426] N. Ryder *supra* note 307 p.4
[427] cited in N Ryder note 307 p. 4.

of the US towards ML pre-date the international measures introduced by both the UN and the EU. The US is at the forefront of the global fight against ML, which is not surprising given the amount of laundered money that is transferred through its banking system.[428]

The US was the first country to criminalise ML by virtue of the Money Laundering Control Act (hereinafter MLCA 1986).[429] ML was criminalised because of the nature of non-compliance with the reporting provisions of the Banks Secrecy Act 1970 (hereinafter BSA 1970), the use of structured payments to avoid the financial reporting thresholds and the acceleration of the drug trade and the large amount of ML with it.[430]

The MCLA 1986 divided ML into four distinctive criminal offences:

1. Transaction ML;
2. Transportation ML;
3. Sting operations; and
4. Spending of laundered property.

The MCLA 1986, therefore, criminalised ML under 18 USC § 1956, the crime of monetary transactions under 18 USC § 1957 and it also criminalised structured or prepared financial transactions that seek to avoid the reporting requirements of the BSA 1970.[431] The criminalisation of ML under 18 USC § 1956 is divided into three parts and relates to domestic ML[432]international ML[433]and the use of sting operations by federal agencies to expose illegal activities.[434]In order to achieve conviction, the prosecution has to prove that the illegal funds were derived from a specified unlawful activity and the accused must have participated in such an activity.[435] 18 USC § 1956(c) (7) (1994) list examples of specified unlawful activities which

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428 N. Ryder *supra* p. 4.
429 D. Hopton, *Money Laundering: A Concise Guide for All Business,* Farnham: Gower, 2009, p.33.
430 S. Sultzer 'Money Laundering: the scope of the problem and attempts to combat it', *Tennessee Law Review* 63 (1995) at 158.
431 N. Ryder *supra* n 307 p.56.
432 18 USC § 1956(a)(1) (2006).
433 18 USC § 1956(a)(2) (2006).
434 18 USC § 1956(a)(3) (2006).
435 18 USC § 1956(a)(1)(A) (I).

includes, but not limited to, dealing with controlled substance, violent crime such as murder and fraud related offences. In order for a person to be convicted of international ML, the defendant must have knowledge that the proceeds derive from an illegal activity under 18 USC § 1956(a)(3).

In addition to criminalising ML, the Anti-Money Laundering Act 1992 (hereinafter AMLA 1992) was introduced as a direct result of the collapse of the Bank of Credit Commerce International.[436] The AMLA 1992 reinforced the penalties for breaching the BSA 1970, introduced the requirement for suspicious-activity reports, extended the scope of the AML obligations to wire transfers and created the Bank Secrecy Act Advisory Group.[437] More importantly, the AMLA 1992 provides authorities with the ability to revoke the charter of any US banks if guilty of ML – referred to as the death penalty provision.[438]

As a result of the terrorist attacks in 2001, President George Bush signed the International Money Laundering Abatement and Financial Anti-Terrorism Act 2001.[439] The purpose was to prevent, detect and prosecute international ML and terrorist financing. According to Ryder, the legislative powers outlined in the US response to ML (which include terrorist financing aspect of ML) represent a robust and formidable approach towards ML.[440]

4.3.7.2 Section 461.31(1) of the Canadian Criminal Code

With its sophisticated financial system, long borders, multicultural population, and of one of the world's highest rates of electronic banking and commerce, Canada may be considered an attractive place for ML. In Canada the FATF has identified drug trafficking as a significant source of illicit funds along with prostitution, illegal arms sales, migrant smuggling, and white-

436 N. Ryder *supra* n 307 p.57
437 *Ibid.*
438 *Ibid.*
439 Pub.L. No. 107-56, 115 Stat 272, Title III cited in N. Ryder n 307 ft 126.
440 N. Ryder *supra* n 307 p.58.

collar crime such as securities offences and payment systems, real estate and telemarketing fraud.[441]

In 1998, Canada amended its Criminal Code to make it a criminal offence to engage in ML. The Criminal Code also provides for the seizure and forfeiture of the proceeds and property derived from various criminal and drug offences.

Section 461.31(1) of the Criminal Code provides:

"Everyone commits an offence who uses, transfers the possession of, sends or delivers to any person or place, transports, transmits, alters, disposes of or otherwise deals with, in any manner and by any means, any property or any proceeds of any property with intent to conceal or convert that property or those proceeds, knowing or believing that all or a part of that property or of those proceeds was obtained or derived directly or indirectly as a result of:

a. the Commission in Canada of a designated offence; or
b. an act or omission anywhere that, if it had occurred in Canada, would have constituted a designated offence".[442]

A designated offence is defined as an indictable offence under the Criminal Code or any other Act of Parliament (other than an indictable offence prescribed by regulation) or a conspiracy or an attempt to commit, or being an accessory after the fact, or any counselling in relation to an offence referred to above.[443] This would include a range of federal offences that are usually motivated by profit. Similar provisions relating to drugs are found in the Controlled Drugs and Substances Act. ML offences in Canada therefore include offences relating to drug trafficking, bribery, fraud, forgery, murder, robbery, counterfeiting, and stock manipulation.

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441 FATF, *Third Mutual Evaluation on Anti-Money Laundering and Combating the Financing of Terrorism: Canada*, 29 February 2008 cited in M Simpson *et al supra* note 190, p. 445.
442 McClean *supra* note 350, p. 90.
443 M. Simpson *et al* note 190 p. 448.

4.3.7.3 Section 4 of the South Africa Prevention of Organised Crime Act 1998[444]

The concept of international organised crime and its negative effects are fairly recent phenomena in South Africa from the international community during the apartheid era which resulted in minimum exposure to and relative immunity from international organised crime.[445]The increasing effects of international organised crime in South Africa have coincided largely with South Africa's re-entry into the international community. This considered, it is not surprising that prior to 1998 the only legislation which addressed the issue of ML was the Drugs and Drug Trafficking Act 140 of 1992.[446]

The increasing need for effective legislation relating to ML following South Africa's re-entry into the international community, compounded by increasing pressure on South Africa to bring its legislation into line with international standards, resulted in the promulgation, in 1998, of the Prevention of Organised Crime Act 121 of 1998 (hereinafter POCA 1998).

Thus, in South Africa the *actus reus* of ML is established by section 4 of POCA, 1998. The offence is defined in these terms:

"Any person who knows or ought reasonably to have known that property is or forms part of the proceeds of unlawful activities and–

a. enter into any agreement or engages in any arrangement or transaction with anyone in connection with that property, whether such agreement, arrangement or transaction is legally enforceable or not; or

444 Act No. 121 of 1998.

445 M. Cowling, 'Fighting Organised Crime': Comment on the Prevention of Organised Crime Bill 1998' (1998) SACJ 350 cited in M Simpson *et al supra* p. 961.

446 This Act made it an offence to convert the proceeds of drug trafficking and provided for the reporting of suspicious transactions relating to drugs and drug trafficking. However, the manipulation of proceeds of crime in general was not recognised as an offence in South Africa at the time.

b. performs any other act in connection with such property, whether it is performed independently or in concert with any other person, which has or is likely to have the effect–

   i. of concealing or disguising the nature, source, location, disposition or movement of the said property or its ownership or any interest which anyone may have in respect thereof; or

   ii. of enabling or assisting any person who has committed or commits an offence, whether in the Republic or elsewhere–

   - to avoid prosecution; or
   - to remove or diminish any property acquired directly, or indirectly, as a result of the commission of an offence, shall be guilty of an offence".

4.3.8 Summary

The obligations to criminalise ML that flowed from the international AML conventions has led to a plethora of domestic criminal legislation. The criticism, which has often been levelled at these domestic AML legislations, is that their broad character has led to a drastic increase of criminal liability. Although it is true that the definition of *actus reus* is, under many domestic ML legislation, very wide, both in regard of type of activities that fall under the offence and in regard of the range of predicate offences (as shall later be seen) covered by these legislations. However, it will be argued that in most cases this broad or wide application field of the ML offences can be kept in balance by the requirement to prove *mens rea.*[447] In the next section, the author shall examine the requirement to prove the *mens rea* in light of the broad obligations to criminalise ML.

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447 G. Stessens *supra* note 14, p. 113.

4.4 Examining the *Mens Rea* in Light of the Broad Definition of the *Actus Reus*

The wide application field of AML legislation arising from the broad definition of the *actus reus* can only be kept in balance by the requirement for the prosecution to establish the *mens rea*. This moral element is two-fold: the required knowledge of the criminal origin of the proceeds and the required (specific) intent.[448] The first element, the guilty knowledge element, has undoubtedly caused most discussion. At the heart of almost every ML trial is a dispute about the knowledge of the defendant. As it is often difficult for the prosecution to establish that the defendant actually knew that proceeds were criminally derived (and even less that he knew from which offences they were derived), in most cases the prosecution will try to infer knowledge from factual circumstances.[449] This way of proving the knowledge requirement is sanctioned on an international level by Article 3(3) of the Vienna Convention 1998 and Article 6(2) (c) of the 1990 Money Laundering Convention and has been endorsed by other instruments likes the OAS-CICAD Model Regulation.[450]

Circumstantial evidence derives its main force from the fact that it usually consists of a number of terms pointing in the same direction. This point was made in *R* v. *Exall:* [451]

"[I]t has been said that circumstantial evidence is to be considered a chain, and each piece of evidence as a link in the chain, but that is not so, for then, if any one link breaks, the chain would fall. It is more like the case of a rope comprised of several cords. One strand of the cord might be insufficient to sustain the weight, but three stranded together may be of quite sufficient strength. Thus, it may be in circumstantial evidence – there may be a combination of circumstances, no one of which would raise a reasonable conviction or more than a mere

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448 *Ibid*., p. 123.

449 *Ibid.*

450 Article 5of the OAS-CICAD Model Regulation states that: 'Knowledge, intent or purpose required as an element of any (money laundering) offence set forth in this Article as well as the relationship of any proceeds or instrumentalities, to a serious criminal activity may be inferred from objective, factual circumstances. See also Article 6(2) (f) of the Palermo Convention, Article 28 of UNCAC and Article 1(5) of the third EU ML Directive.

451 (1866) 4 F & F 922.

suspicion; but the three taken together may create a conclusion of guilt with as much certainty as human affairs can require or admit of".

Thus, a useful analogy may be drawn between ML and handling stolen goods. That goods were stolen may be proved by circumstantial evidence, although there may be no direct evidence from the victim or the thief of the fact of their being stolen. Indeed, circumstances in which the defendant handled the goods may, of themselves, be sufficient to prove not only that the goods were stolen but also that, at the time when the defendant handled them, he knew or believed that they were stolen.[452]

As the illustration above indicates, the use of circumstantial evidence to prove the elements of ML offences is now a regular practice in a wide range of legal jurisdictions. Indeed, the circumstances from which the jury are asked to draw inferences that the property is the proceeds of crime are frequently the same evidence from which they asked to draw inferences that the defendant also had the requisite *mens rea*. In *United States* v. *Avery, Daniels and Daniels*[453] the US Court of Appeal held that Sherry and Michele Daniels were extensively involved in a ML operation. The court said that the evidence, much of it circumstantial, heavily incriminated them and went on to state: "Circumstantial evidence on its own can sustain a jury's verdict. . . Although they offered an innocent explanation for the incriminating facts proved by the government, the jury was free to disbelieve them". In *United States* v. *Quintero*[454] the conviction of a grandmother for laundering the drug-trafficking proceeds of her grandson was upheld. The US Court of Appeals held that the prosecution had presented sufficient circumstantial evidence for a jury to find that the grandson was a drug dealer, that the grandmother knew that he was a drug dealer and that she knew that car purchases and trade-ins, which she participated in, involved the proceeds of drug dealing. The evidence that the

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452 Archbold *Criminal Law and Pleadings* (London Sweet & Maxwell, 2000) para 21-294 cited in R. E. Bell 'Proving the criminal origin of property in money laundering prosecution' (2000) 4(1) JMLC at 13.

453 128 F.3d 966 (6th Cir. 1997).

454 Unreported (6th Cir. 1997).

prosecution adduced included evidence of the grandson's lifestyle, his vacations, his lack of gainful employment, his failure to submit income tax returns and his purchase of eight expensive cars which were registered in his grandmother's name.[455]

In *United States* v. *Garcia-Emmanuel,*[456] the court stated that there were a variety of types of evidence that had been considered when determining whether a transaction was designed to conceal or disguise the nature, location, source, ownership, or control of criminal proceeds. The list included unusual secrecy surrounding the transaction; structuring the transaction in a way to avoid attention; highly irregular features of the transaction; using third parties to conceal the real owner; a series of unusual financial moves culminating in the transaction; and expert evidence on the practices of criminals.[457] The preceding list might equally well, it is submitted, have been in relation to evidence that may be used when determining whether the property in question was the proceeds of crime.

4.4.1 The Required (Specific) Intent for Money Laundering

The mental standard of liability for the laundering offence differs from state to states. The Vienna Convention 1988 requires knowledge that the property is derived from drug-related crimes, although it may be inferred from objective circumstance.[458] The Palermo Convention similarly requires knowledge of property being the proceeds of crime.[459] The 1990 Money Laundering Convention, in addition to knowledge, permits members to criminalise ML on a negligence standard.[460]

Some variation of the mental standard is also thought to exist in domestic law of some states. For example, the POCA 2002 in the UK requires knowledge or suspicion of property

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455 R. E. Bell *supra* note 452, at 13.
456 14 F.3d 1469 (10th Cir. 1994).
457 *Supra*.
458 Article 3.
459 Article 6(1).
460 Article 6.

being criminal property. However, suspicion in this regard is subjective-based[461] and therefore cannot be equated with negligence, which is objective-based under the 1990 Money Laundering Convention. In the US, the mental standard required is knowledge of property being the proceeds of crime.[462]

By setting the threshold for *mens rea* as low as suspicion, or 'reasonable grounds for suspecting', the UK has exceeded its treaty obligations. The *mens rea* requirement is found in the definition of criminal property in section 340(3) of POCA, 2002. It requires the alleged offender to know or suspect that that property constitutes or represents the benefit of criminal conduct.

Suspicion is thought to be a much easier test and presents a greater risk. The meaning of the word 'suspicion' has been considered in a number of cases both under the predecessor of POCA 2002 (CJA 1988) and under POCA 2002 itself. The case of *R* v. *Da Silva*[463] concerned a prosecution under section 93A (1) (a) of the CJA 1988 which is the predecessor of POCA 2002, section 328. The Court of Appeal was required to consider the meaning of 'suspicion' and found that:

"It seems to us that the essential element in the word 'suspect' and its affiliates, in this context, is that the Defendant must think that there is a possibility, which is more than merely fanciful, that the relevant facts exist. A vague feeling of unease will not suffice. But the statute does not require the suspicion to be 'clear' or 'firmly grounded and targeted on specific facts' or based on 'reasonable ground".

The definition of suspicion used in *R* v. *Da Silva* was adopted in *K Ltd* v. *National Westminster Bank plc,*[464] which addressed the position of a bank that had refused to implement

461 Section 340(3).
462 18 USC §§ 1956 and 1957.
463 [2005] EWCA Crim 1654.
464 [2006] EWCA Civ 1039.

a customer order to transfer funds on the basis of a suspicion of ML. The issue arose as to what constituted a proper suspicion in law. The Court found that the existence of a suspicion is a subjective fact and that there is no legal requirement that there should be reasonable grounds for a suspicion. The issue was also considered in the case of *Shah* v. *HSBC Private Bank (UK Ltd.*[465] In that case the court rejected a contention that a suspicion should be a 'rational' suspicion and said that the decision in *K Ltd* clearly established that a suspicion under POCA 2002 is a subjective one.

In addition, in *R* v. *Montila*[466] the House of Lords noted the absence of 'reasonable suspicion' as a basis for criminal liability in the three main international instruments.[467] The third EU ML Directive defines culpable 'ML', as conduct that is committed intentionally, either knowing that property is derived from criminal activity or from an act of participation in such activity and, that 'knowing, intent or purpose required as an element of the activities mentioned may be inferred from objective factual circumstances.[468]The sixth EU ML Directive extends this to ML committed recklessly or by serious negligence.

4.5 Examining the Term 'Property' in the Context of the Obligations to Criminalise

In drafting the Vienna Convention 1988 the definition of the word 'property' was originally the definition of the term 'proceeds'.[469] However, it became clear that two definitions were needed, one (that of 'property') serving to emphasise that assets of every possible kind were included and the second ('proceeds') addressing the derivation of the property.[470] Surprisingly, when the definition first appeared in a draft of the Palermo Convention, that experience was overlooked,

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465 [2009] EWCA 79 (QB).
466 [2004] UKHL 50, [2004] 1WLR 624, [2004] 1 WLR 3141.
467 The three main instruments in this case are the Vienna Convention 1988, the 1990 Money Laundering Convention and third EU ML Directive.
468 Blair and Brent *supra* note 384, p.172.
469 EN/CN.7/1987/2, section 11 cited in D McClean note 350 p 43.
470 D. McClean note 350 p. 43.

and the language was part of a definition of 'proceeds of crime.[471] At the First Session of the *Ad Hoc* Committee, definitions of 'property' and 'proceeds of crime' based on those in the Vienna Convention, 1988, were inserted.[472]

The language used is apt for the various classifications of property to be found in national legal systems. In some systems the legal documents of title to property are not merely evidence but have value in themselves, and this is catered for in the definition. According to Article 2 (e) of the Palermo Convention "Proceeds of crime shall mean any property derived from or obtained, directly or indirectly, through the commission of an offence".[473]

In addition, the 2009 Model Provisions on ML, defines the word 'property' to mean:

"assets of every kind, whether tangible or intangible, corporeal or incorporeal, moveable or immovable, however acquired, and legal documents or instruments in any form, including electronic or digital, evidencing title to, or interest in, such assets, including but not limited to currency, bank credits, deposits and other financial resources, travellers cheques, bank cheques, money orders, shares, securities, bonds, drafts and letters of credits, whether situated in [insert name of State] or elsewhere, and includes a legal or equitable interest, whether full or partial, in any such property".[474]

The foregoing definition together with the definition of property in the conventions is broad and wide enough to include every conceivable aspect of the term 'property'.

For the purpose of POCA 2002, the definition of 'criminal property' is widely drawn.[475]

Property is 'criminal property' if "(a) it constitutes a person's benefit from criminal conduct or it represents such a benefit (in whole or in part and whether directly or indirectly) and (b) the alleged offender knows or suspects that it constitutes or represents such a benefit".

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471 E/CN.15/1988/11. P. 85 cited in D. McClean.

472 *Supra* p. 44.

473 See also Article 1(q) of the Vienna Convention 1988.

474 The 2009 Model Provisions on Money Laundering' (Report, April 2009) at 14 available at ≤www.imolin.org/> last visited on 27th July 2020.

475 Section 340(3) POCA 2002.

By section 340 (9) of POCA 2002, 'criminal property' extends to property anywhere in the world – and includes (a) money, (b) all forms of property, real or personal, heritable or moveable, (c) things in action and other intangible or incorporeal property.

Rules that apply in relation to property are set out in section 340(10) of POCA 2002. The most important rules are (1) that property is obtained by a person if he obtains an interest in it, and (2) that reference to an interest in relation to property other than land, include references to a right (including a right to possession). It is crucial to note that the definition of 'criminal property' has two principal elements. First, the property either is, or represents, any persons' benefit from 'criminal conduct'. Secondly, property is only criminal property if the person dealing with it 'knows or suspects' that it constitutes such a benefit.[476]

The concept of 'criminal property' is central to the way in which the ML offences of the POCA 2002 have been expressed. The term criminal property carries within itself the mental element of the offences, so that the sections creating the offences are expressed in very simple terms.[477] In arriving at a definition of criminal property, certain other terms have also to be defined. The most important terms are 'property',[478] 'criminal conduct',[479] 'benefits'[480] and 'criminal property'.[481]

4.6 Examining the concept and scope of the 'Predicate Offence'

Article 2(h) of the Palermo Convention defines the predicate offence as any offence as a result of which proceeds have been generated that may become the subject of an offence as defined in article 6 of the convention. A predicate offence is therefore the underlying criminal offence

476 Section 340(3) (b) of POCA 2002.
477 B. Gumpert *et al Proceeds of Crime Act 2002* (Bristol, Jordan Pub. Ltd, 2003) p 55.
478 Section 340(9) of POCA 2002.
479 Section 340(2) of POCA 2002.
480 Section 340(5), (6) and (7) of POCA 2002.
481 Section 340(3) of POCA 2002.

that gave rise to the criminal proceeds, which are the subject of a ML charge.[482] The concept is an important one in US law because, in order to prosecute successfully for ML, there must be proof that the property involved in the transaction was the proceeds of 'specified unlawful activities' (SUA) as defined by 18 USC 1956 (c)(7). This subsection contains a list of crimes that constitute SUA, most of which are crimes commonly associated with organised crime.[483]

The concept of predicate offence can also be observed in the ML legislation of other jurisdictions. For example, Canada introduced legislation which was limited to where the proceeds were derived from an 'enterprise crime offence' or a designated drug offence'[484] and New Zealand introduced legislation which applied to offences with a five-year minimum period imprisonment.[485] The concept of the predicate crime has also had an impact on international conventions dealing with ML. The Vienna Convention 1988[486] adopted to stem the threat of ML had a limited scope in the sense that it criminalised ML proceeds from drug offences only. Subsequent international conventions[487] and the FATF have however provided for optional extension of criminalisation to further categories of predicate offences in the glossary to the FATF 40 recommendations.[488]

Article 1(e) of the 1990 Money Laundering Convention defines the predicate offence as broadly to include "any criminal offence as a result of which proceeds were generated that

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482 R. E. Bell 'Abolishing the Concept of 'Predicate Offence (2002) 6(2) JMLC at 137.

483 Since the ML statutes were enacted in 1986, the US Congress has regularly added new offences to the list of SUAs.

484 Canada Criminal Code, RSC 1985, c. C-46, s. 462.31.

485 Section 243 of the Crimes Act and Section 12B of the Misuse of Drugs Act both create offences of ML. These offences involve dealing in property that is the proceeds of serious crime or a specified drug offence for the purpose of concealing that property (punishable by seven years' imprisonment) or having possession of such property with intent to engage in a ML transaction (punishable by five years' imprisonment).

486 Article 3.

487 Article 32 of UNCAC; while Article 6(4) of the 1990 Money Laundering Convention provides that parties to the Convention are permitted to limit the effect of ML offences as hey specify in a declaration. This was presumably a compromise so as to enable states to introduce some form of ML legislation, even though it may not be as extensive as other jurisdictions might wish.

488 Available at ≤ http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF%20Recommendations%202012.pdf> last visited on 27th July 2020.

may become the subject of laundering." As far as the European Union AML framework is concerned, the issue of ML predicate offences has been partly addressed in the specific context of the third pillar measures on fraud[489]and confiscation.[490]According to recommendation 26(b) of the action plan on organised crime, criminalisation of laundering of the proceeds of crime should be created as broad as possible to ensure a range of powers of investigations into it.[491] In its report on the first Commission Implementation Report, the European Parliament adopted a motion, whose resolution point 5 calls on all member states, in so far as they have already not done so, to extend their legislation on combating ML, not only to money derived from drug trafficking but also money acquired from professional and organised crime.[492]

Amongst others, the Sixth EU ML Directive includes a unified list of predicate offences as it aims to have a uniform definition for criminal activities which constitute predicate offences for ML. There are 22 predicate offences, in this directive, which now includes cybercrime as well as environmental crime.[493]

4.6.1 The UK Approach

UK legislation historically drew a distinction between laundering the proceeds of drug trafficking and laundering the proceeds of other. ML offences were first introduced in England

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489 The second protocol of the convention on the protection of the European Communities financial interests (OJL 221 19 July 1997, p.11) criminalises the laundering of proceeds of fraud, at least in serious cases, and active and passive corruption (article 1(e) and 2) cited in N. Mugarura 'The institutional framework against money laundering and its underlying predicate crimes' (2011) 19(2) *Journal of Financial Regulation & Compliance* at 179.

490 The joint action on money laundering, the identification, tracing, freezing and confiscation of the instrumentalities and the proceeds of crime (OJ L 333, 9December 1998, p.1) calls at member states to ensure that no reservations are made to article 6 of 1990 Money Laundering Convention in so far as serious offences are concerned.

491 V. Mitsilegas *Money Laundering Countermeasures in the European Union: A New Paradigm of Security Governance Versus Fundamental Legal Principles* (The Hague, Kluwer Law 2003) chapter 4 cited in N. Mugarura *supra* note 489.

492 W. C. Gilmore 'European Parliament Committee on legal affairs and citizens' rights: report on the First Commission's Report Submitted to the European Parliament and to the Council on the Implementation of the Directive on the Prevention of the Use of the Financial System for the Purpose of Money Laundering (91/308/EEC) (CM (95) 0054-C4-0137/95) cited in Mugarura note 489.

493 Available at: <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex:32018L1673> last visited on 27 July 2020.

and Wales under the DTA 1986, but it was not until 1993 that ML offences in crimes respect of the proceeds of non-drug trafficking criminal conduct were created by the CJA 1993 and inserted in the CJA 1988.

The POCA 2002 removed the distinction between these two different types of ML offences. The ML offences in the Act refer to 'criminal property', which is defined as property which constitutes a person's benefit from criminal conduct or represents such a benefit (in whole or in part and whether directly or indirectly) and which the alleged offender knows, or suspects constitutes or represents such a benefit. Criminal conduct is widely defined as conduct that constitutes an offence in any part of the UK or would constitute an offence in any part of the UK if it occurred there.

Arguably, referring to predicate offences in the context of the UK, ML legislation was always misleading in that the prosecution did not have to prove a predicate offence in the American sense, but merely which side of the drug trafficking/non-drug trafficking divide the criminal monies derived from. Use of the term since the passing of the POCA 2002 is, however, completely otiose.[494]There is no need to prove either a specific offence or a type of offence. if the jury can be satisfied beyond a reasonable doubt that the property in question was derived from criminal conduct and that the defendant knew or suspected this then, even if they do not know what particular type of offence was committed, they may still convict the defendant.[495]

It may be that in some cases the prosecution will be able to call evidence to prove exactly how the proceeds were derived. However, if not, then, as long as the jury is satisfied beyond reasonable doubt that the funds were derived from some sort of 'underlying criminality', a matter which may be proved entirely by circumstantial evidence, they will be entitled to convict.

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494 R. E. Bell *supra* note 452, at 139.

495 *Ibid*.

Given the cross-border nature of the offence of ML AML investigators and prosecutors will still have to turn their minds to the concept of 'predicate offence' when seeking mutual legal assistance and international cooperation from a jurisdiction where the term remains relevant. For example, when sending Letters of Request to the US, prosecutors will have to satisfy the US authorities that ML, as the US understands that offence has been committed. This will mean proving evidence that the proceeds were derived from a predicate offence as defined by US legislation. Whereas in the UK, laundering charges may be preferred, regardless of the particular type of crime that gave rise to the ill-gotten gains.

4.6.2 The Problem of Tax Offences

The most politically sensitive question in this area is whether tax offences are predicate offences for the purpose of ML charges. Although the UK position is that revenue offences are predicate as far as ML offences are concerned,[496] the same is not necessarily true of other jurisdictions. While some jurisdictions have no difficulty in accepting their own domestic tax offences as predicate offences, the position is often more difficult when it comes to foreign tax offences. Since a traditional approach has been that foreign taxation offences are not predicate offences for the purpose of ML charges.[497] Whether this position is likely to change needs to be examined in the global context of developments in relation to harmful tax practices.

In recent years, international initiatives[498] have placed pressure on offshore tax havens to be more transparent and to grant more cooperation in investigations by foreign tax authorities. A crucial issue for the future will therefore be whether such trends will eventually

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496 See for example, M. J. Bridge and P. Green 'Tax Evasion and Money Laundering – An Open and Shut Case', (2000) 4(1) JMLC at 12-25.

497 In *Government of India, Ministry of Finance (Revenue Division) v Taylor and Others* [1955] AC 491, [1955] 1 All ER 292 it was held that it was a well-recognised rule of English of law, applying equally in relation to the revenue laws of a member state of the British Commonwealth as to those of foreign country, that the courts of this country did not enforce the revenue laws of another country.

498 See the report by the 'Tax Justice Network' available at: ≤www.taxjustice.net/cms/upload/pdf/Identifying_Tax_Havens_Jul_07.pdf≥ last visited 27 July 2020).

result in an international initiative for all jurisdictions to remove the taxation 'loophole' from their ML legislation. This is a major source of concern as existing repressive and preventive AMLC have failed to address the specific cases of the tax element in cross border ML.

4.6.3 Summary

In summary, while the ML activities that should be criminalised are the same under the relevant conventions, the predicate offence is not the same. The Vienna Convention 1988, for example, only applies to proceeds from drug trafficking offences[499]whereas the Palermo Convention applies to the proceeds of all serious crime.[500] The EU ML Directive and the FATF are clearly part of soft law effort to expand the predicate offence beyond drug trafficking to other types of offences.

This trend is also notable, for example, in the 2002 amendments to the Inter-American Drug Abuse Control Commission (hereinafter CICAD) Model Regulations Concerning Laundering Offences and in the 1998 United Nations Political Declaration and Action Plan against Money Laundering.[501] This trend has led to the criminalisation of ML evolving as a technique that can be used against any type of acquisitive crime. This is especially the case of legislation where the operation of the confiscation of proceeds operates *in personam* and hence does not allow the removal of proceeds, which have been channelled, to third parties.

According to Stessens, once the criminalisation of ML is seen as an alternative, rather than a complement, to the *in-rem* confiscation of criminally derived proceeds[502] it is only

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499 As defined under Article 3(a) of the Vienna Convention 1988.

500 UNCAC has similar anti-money laundering provisions to the Palermo Convention, with detailed provisions and asset recovery –see in particular Article 52 dealing with the prevention and detection of transfers of proceeds of crime. The predicate offence under the Money Laundering Convention in principle applies to the proceeds from any predicate offence, even though it allows contracting parties to make a declaration.

501 Adopted at the Twentieth Special Session of the United Nations General Assembly devoted to 'countering the world drug problem together, New York, 10 June 1998. See specifically Resolution S-20/4D (Countering Money Laundering).

502 G. Stessens *supra* note 14, p. 117.

logical to have a wide application field of predicate offences. A conviction on a charge of ML may often then be the only way, save value confiscation,[503] to ensure deprivation of proceeds that can no longer be traced in the estate of the person who has committed the predicate offence.[504]

The latitude available to individual states arising from the flexibility of these international instruments (a peculiarity with soft law) has resulted in a patchwork of predicate offences, centred around drug trafficking,[505] corruption,[506] organised crime[507] and other criminalised types of ML activities.[508] The increase in international instruments has led to an increase in the number of offences, which are recognised by every state as predicate offence in relation to the offence of ML. With the increasing number of international instruments, States that confine the application field of their domestic AML legislation to a single category of predicate offence is becoming rare.

4.7 Criminalisation and Confiscation: A Repressive Technique

There is a further aspect to repressive AML technique. This has to do with the confiscation of the proceeds of crime, and this type of confiscation is of recent origin in relation to confiscation of subject and instrumentality of crime.

Confiscation as part of repressive AMLC generally operates *in-personam* and may not apply when the proceeds of crime have already been channelled to third parties.[509]

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503 *Infra* pp. 154-158.

504 *Supra*.

505 Article 3 of the Vienna Convention.

506 This is especially the case with Article 23 of UNCAC.

507 Article 6 of the Palermo Convention

508 Article 6 of the Money Laundering Convention has a wide application field of predicate crime, while the 2005 Council of Europe Convention against Money Laundering extends the predicate crime to terrorist financing.

509 Art1 (f) of the Vienna Convention refers to confiscation as the 'permanent deprivation of property by order of a court or other competent authority and Art 1(d) of the Money Laundering Convention speaks of a 'penalty or a measure, ordered by a court following proceedings in relation to a criminal offence or criminal offences resulting in the final deprivation of property'. See PBH Birks *Laundering and Tracing* (Oxford University Press, New York, 2003) on the limits with common law tracing and equitable rules on tracing.

Nevertheless, in most cases, confiscation as a legal tool for the repression of ML is also pursued both *in-rem* and *in-personam*. The point is that the use of confiscation without a general purpose, in relation to an *in-rem* application, may not have achieved the aim of the law since repressive AMLC, apart from punishing culprit in relation to the laundering offence, is also aimed at stopping criminals benefitting from their crime.

Referring to Confiscation *in rem,* the American Supreme Court, in *United States* v. *Various Items of Personal Property*[510] stated that, "it is the property, which is proceeded against and, by resort to legal fiction, held guilty and condemned as though it were conscious instead of inanimate and insentient". In view of this, criminalisation of ML was seen as an alternative (rather than a complement), to the *in-rem* confiscation of criminally derived proceeds. This, however, has resulted in the wide application field of predicate offences, as a conviction on a charge of ML may often be the only way to ensure deprivation of the proceeds that can no longer be traced in the estate of the person who has committed the predicate offence.

4.7.1 Confiscation and Models

Confiscation is said to be justified by a principle, deeply ingrained into the law that people should not profit from unlawful activity in general and from crime in particular.[511] This principle follows from the requirement that if law is to impact upon people's behaviour, it should deliver coherent messages. It is not coherent, on the one hand, to try to prevent a particular form of behaviour, but on the other, to permit someone who does it to benefit. The principle is stated in the judgement of Lawton LJ in *R* v. *Waterfield:*[512]

"The first thing the law should do is to ensure that those who break it . . . should not make any money out of their wrongdoing . . . This court is firmly of the opinion that if those

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510 82 US 577, 581 cited G. Stessens *supra* note 14, p. 39.

511 Goff and Jones, *The Law of Restitution* (5th ed. London, Sweet & Maxwell 1999) ch 37 'Benefits accruing to a Criminal from his crime' cited in P. Alldridge *supra* note 223, p. 45.

512 *R* v. *Waterfield* (17 February 1975, unreported) cited in P. Alldridge ft 78.

who take part in this kind of trade know that on conviction, they are likely to be stripped of every penny of profit they make and a good deal more, then the desire to enter it will be diminished".

Two models of confiscation can be distinguished: object confiscation and value confiscation. The distinction in the first place concerns the mode in which property rights are affected: either through the imposition of an obligation to pay a certain amount of money or through transfer of property. It will be argued, however, that this distinction also concerns the *in rem* or *in personam* character of confiscation. Both the Vienna Convention 1988[513] and the 1990 Money Laundering Convention[514] provide for both models.[515]

Object confiscation is a powerful criminal sanction: it results in the transfer of property title to the State.[516] Object confiscation, often known as forfeiture, function in many criminal justice systems in relation to the instrumentalities of crime. The application field of this type of confiscation, when extended to the proceeds from crime, creates a number of sometimes-insurmountable problems. A definite drawback of object confiscation, especially in relation to proceeds from crime, is its uncertain character; property which at the time of the judicial decision has been consumed or which cannot be traced any more, escapes confiscation. That this may cause inherently unjust consequences needs little explanation.

As an American judge once put it succinctly: "A racketeer who dissipates the profit...on wine, women and song has profited from organised crime to the same extent as if he had put the money in his bank account".[517] The goal of an effective deprivation of the fruits of crime may thus suffer from the fact that (some of) the property constituting the fruit of crime cannot be traced any more.

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513 See Article 5 of the Vienna Convention.
514 See Article 2 of the Money Laundering Convention.
515 See also Article13-14 of the Palermo Convention and Article 25 of UNCAC.
516 G. Stessens *supra* note 14, p. 32.
517 *United States* v. *Ginsgerg, 773* F.2d, 789, 802 (7th Cir.1985) cited in G. Stessens p. 31.

A possible more harmful disadvantage of object confiscation relates to the right of *bona fide* third parties, whose rights may suffer because of the 'blind' application of object confiscation.[518] In relation to proceeds from crime, this type of confiscation normally functions independently of any property rights that may be established in relation to the proceeds. As far as the person who committed the crime is concerned, this is only logical; he can indeed not have any *bona fide* rights with regards to property he obtained through an offence. This conclusion cannot be broadened, however, to third parties who have established rights with respect to the property representing the proceeds from crime, after the offence has been committed.

The second model of confiscation is value confiscation, and this type of confiscation does not consist in the deprivation of property (known as proceeds from crime) but of a judicial order to pay a certain amount of money, corresponding to the value of the proceeds from crime.[519] This entails that value confiscation can in principle only be in relation to the proceeds from crime.

Once a value confiscation has been ordered, the state can in principle use the remedies available to a private creditor to ensure payment (attachment of property etc). This will generally be the case in respect of object confiscation as well. The clearest advantage of value confiscation lies in the fact that, unlike object confiscation, it operates *in personam*, meaning that confiscation can in principle be pronounced only with regard to the proceeds enjoyed by the offender and can be enforced only on property owned by the offender.

Part 2 of POCA 2002 lays down the statutory framework for confiscation orders post-conviction, and restraint and receivership orders.[520] One of the requirements which has to be fulfilled before the court can make an order is that there should be "reasonable cause to believe

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518 *Supra* p. 33.
519 Ibid., p. 35.
520 Hatchard *et al Corruption and Misuse of Public Office* (2nd ed, OUP, 2011) p. 245.

that the alleged offender has benefitted from his criminal conduct".[521] It is now clearly established that this requirement must be fulfilled on the basis of full and complete evidence being put before the court, as was held in Early in 2011 by the Court of Appeal in the case of *Windsor* v. *CPS.*[522]

In addition to introducing new and stricter ML offences, POCA 2002 enhanced the courts' post-conviction confiscation powers, and transferred to the Crown Court powers formerly exercised by the High Court.[523] The confiscation provisions came into force on 24 March 2003.[524]They apply only in respect of offences committed on or after that date. Offences committed before that date are governed by the DTA 1994 and the Criminal Justice Act 1988. Confiscation procedures depend on the conviction of an offender because it is a criminal procedure.

Part 2 of POCA 2002 contains statutory powers to confiscate the assets of convicted criminals. The term 'confiscate order' is in many ways a misnomer, but a useful shorthand term: the actual order is to pay a sum of money equal to the benefit from the criminal conduct.[525]Confiscated assets are forfeit to the Crown. A victim of crime cannot intervene in confiscation hearing to seek, for example, the return of stolen funds. In practice, however, prosecutors will have in mind the possibility of asking the court to make a compensation order in appropriate cases. The amount of compensation payable will depend on the court's view of the defendant's means: the compensation can be paid out of the sums confiscated.[526] However,

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521 POCA, section 40(2)(b).
522 [2011] EWCA Crim 143.
523 Hatchard *et al supra* note 520, p. 249.
524 POCA 2002 (Commencement No 5, Transitional Provision, Savings and Amendment) Order 2003, SI 2003/333.
525 The question of whether a confiscation order is appropriate in cases involving major corruption has been called into question by Thomas LJ in his Sentencing Remarks in *R* v. *Innospec* [2010] Lloyd's Rep F.C. 462 cited in Hatchard *et al supra* ft. 84.
526 POCA 2002, section 13(5) and (6).

a court has discretion not to make a confiscation order, or to reduce its amount, if the victim of the criminal conduct has started or intends to start proceedings against the defendant.[527]

Confiscation is a harsh regime and intended to be so. Together with the criminalisation of ML, confiscation is a powerful repressive AMLC. Hardship is thought not to be a consideration, as general fair trial guarantees under Article 6(1) of the Human Right Act 1998 apply.[528] The presumption of innocence does not apply, as confiscation only arises after conviction.[529] The primary purpose of a confiscation order is to deprive the defendant of his ill-gotten gains, not to enrich the Crown; where possible, a compensation order will also be made.[530]

4.8 Conclusion

Since the Vienna Convention 1988, criminalisation of ML has developed beyond the scope of drug-related proceeds. It became obvious that such limitation is neither justified nor practical, in view of the trend in ML typologies. Drug trafficking is not the only serious offence that generates large criminal fortune; therefore, confining ML offences to the proceeds of drug-related crime creates a host of practical problems and renders the law ineffective. Defining the predicate offences of ML is now a policy issue to which subsequent international instruments and states give different solutions. It was now common to extend the offence of ML beyond the scope of drug-related offences.

Given that it was left open to States to decide exactly which crimes would qualify as predicate offences to ML, a veritable patchwork of national lists of predicate offences has resulted. Harmonisation through a broad definition of ML (by using soft law), has created the

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527 POCA 2002, 6(6).

528 See *Lloyd* v. *Bow Street Magistrate Court* [2004] 1CrAppR 11, DC and *ReS (Restraint Order: Release of Assets)* [2005] 1 WRL 1338 (CA). (An appeal against a refusal to vary a restraint order to permit funding for legal representation – appeal dismissed, having regard to funding available under the Access to Justice Act 1992 Sch 2.) cited in Hatchard *et al supra* note 520, p. 249.

529 Hatchard *et al* p. 249.

530 *Ibid.*

needed atmosphere for compromise in criminal AML repressive technique. Criminalisation is therefore a tool for repressive AMLC.

As noted in chapter one, soft law can ease bargaining problems among states by opening up opportunity for achieving mutually preferred compromises. Negotiating a hard, highly elaborate agreement among heterogeneous states is a costly and protracted process. It is therefore more practical to negotiate a softer form of agreement that establishes general goals but with less precision. Soft law, accordingly, allows states to adapt their commitments to their particular situations rather than trying to accommodate divergent national circumstances within a single text. This provides for flexibility in implementation, helping states deal with the domestic political and economic consequences of an agreement and thus increasing the efficiency with which it is carried out.[531] This is the effect of a broad definition of ML (as a repressive criminal technique) in a heterogeneous international system.

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531 *Supra* pp. 67-68.

CHAPTER FIVE

Preventive Anti-Money Laundering Control

5.1 Introduction

Chapter four of this thesis considered the role of soft law as a technique for repressive AMLC through criminalisation of the offence of ML and confiscation of the proceeds of crime. Criminalisation, as noted earlier, was effected through a broad definition of the offence of ML under both the UN[532] and EU[533] Conventions. The broad definition of the offence of ML relates to our earlier definition of formal soft law, under which we considered treaty provisions that are imprecise, subjective or indeterminate in language.[534]

In order to examine the role of soft law as a technique for preventive AMLC this chapter will consider the role of certain non-treaty or informal instruments and their relevance to the prevention of ML. These international instruments and initiatives, of non-binding origin, include the work of the FATF and other FATF-style regional bodies and organisations,[535] the EC ML Directives[536]and the Basel Statement of Principle of 12 December 1988, issued by the Basle Committee on Banking Regulations and Supervisory Practices.[537] The Basel Principle 1988 is directed specifically at prevention of laundering crimes and is targeted at the financial system, especially banks.

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532 Under this category is the Vienna Convention 1988, the Palermo Convention.

533 1990 Money Laundering Convention and the 2005 Council of Europe Convention against Money Laundering.

534 C. Chinkin *in* D. Shelton *supra* note 108, p. 25.

535 Caribbean Financial Action Task Force (hereinafter CFATF); Financial Action Task Force on Money Laundering in South America (GAFISUD); Middle East and North Africa Financial Action Task Force (hereinafter MENAFATF); Asia Pacific Group on Money Laundering (hereinafter APG).

536 The most recent EC Directive is the, Directive 2005/60 EC of the European Parliament and of the Council of 26 October 2005), on the prevention of the use of financial system for the purpose of Money Laundering and terrorist financing (hereinafter the EC ML Directive).

537 Available at https://www.bis.org/publ/bcbsc137.htm visited on 13 July 2020. See infra pp. 136-139 for more on the Basel Principle.

Thus, legal measures on the preventive aspect are understood as referring to obligations of financial and non-financial institutions to undertake certain actions to disclose ML operations. These obligations, while initially limited to banks have been extended to non-bank financial institutions,[538] and even non-financial businesses and certain professions.[539] The principal justification for this extension is that criminals turn more and more to those non-financial businesses and professions to launder proceeds from crime. This is the reason for the implementation of the preventive measures on banks and financial institutions. Reference in this regard should be made to the FATF suggestion that the preventive measures be applied to non-financial businesses and professions.[540]

However, there is a further aspect to the preventive AMLC. This is in relation to the identification of the beneficial ownership of the proceeds of crime, which work in tandem with the obligations placed on financial institutions to undertake certain actions to disclose laundering operation. The identification of beneficial ownership is important to preventive AMLC as it bears direct relation to the obligations placed on financial and non-financial institutions on the prevention of ML through reporting obligations and customer due diligence (hereinafter CDD). Unlike the earlier approach that dwelled on Customer Identification or KYC, the current trend is towards enhanced CDD in high-risk cases. Together with the current risk-based approach, the identification of beneficial ownership brings existing efforts in preventive AMLC to a natural person or the controlling entity behind a ML scheme.

Thus, the approach here, as with the last chapter, will be to examine the role of soft law (informal soft law) in the regulation of global ML. The aim is to identify the instruments, participants and processes employed in response to threat of ML by looking at the obligations

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538 The FATF defines the term 'financial institution' very broadly. It means any person or entity who conducts as a business a wide range of activities on behalf of a customer. See the list of activities in the Glossary to the FATF Forty Recommendation (2012).

539 See the definition of non-financial businesses and professions in Glossary to the FATF Forty Recommendation (2012).

540 See FATF Recommendations 12 and 16.

placed on financial and non-financial institutions in the prevention of ML. The emphasis here is not on repression through criminal law, but prevention through industry regulation. The chapter does this by examining the role of informal non-binding initiatives under existing international arrangements. Together with the obligations placed on financial and non-financial institutions on the prevention of ML, the prevention of ML operation through soft law has become a focal point for global AML policies and initiatives.

The chapter will therefore do two things: first, it will highlight the body of informal AML arrangements (or initiatives); second, it will examine the measures adopted under these instruments (as applied in domestic legislation) and the relevance to the prevention of global ML. The chapter is divided into two sections: informal instruments and initiatives on the prevention of ML and preventive AML measures.

5.2 Soft Law in the Preventive Anti-Money Laundering Control

The role of soft law in preventive AMLC is centred on the uniform application of preventive AML measures that transforms into domestic AML legislation. Unlike the repressive control that is based on criminalisation and confiscation of the proceeds of crime, the preventive AMLC is aimed at preventing the negative impact of ML on the financial system. These informal initiatives, of non-binding origin, legitimise participation in national decisions by international actors and concerned domestic bodies by fostering a significant degree of convergence around the principles contained in them. They are many and fluid and bear direct impact on the overall global challenge that the problem of ML poses.

According to Slaughter, soft law can "offer a focal point for convergence".[541] National adherence to international standards, such as the FATF Recommendations, can therefore foster a process of 'leading example'. Non-treaty-based obligations, like the FATF Recommendations

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541 A. M. Slaughter, *A New World Order* (Princeton: Princeton University Press, 2004), p. 180.

and EU ML Directive, can exert pressure on states to adopt internationally recognised AML standards through mutual evaluation techniques under the FATF and the principle of *direct effect* under European Union law. However, the initial priority under this section is to highlight the category of soft law instruments in the area of preventive AMLC.

5.3 The Basel Committee on Banking Regulations and Supervisory Practices

While it is generally accepted that efforts to combat ML and the broader financial aspects of serious forms of transnational criminality must place particular reliance on criminal justice mechanisms, the nature and extent of the problem are such as to require the imposition of internationally co-ordinated measures. This is aimed at preventing the use of the financial system and other vulnerable parts of the private sector for criminal purpose. The prevailing philosophy in this regard was well captured by Sherman in 1993 in these words:

"The fight against money laundering cannot be the sole responsibility of government and law enforcement agencies . . . if these activities are to be suppressed and hopefully, in the long term, substantially eliminating it will require the collective will and commitment of the public and private sector working together".[542]

The first major initiative to give substantive expression to this approach was the December 1988 Basel Statement of Principles. Its basic purpose is to encourage the banking sector, through 'a general statement of ethical principles', to adopt a common position in order to ensure that banks are not used to hide, or launder funds acquired through criminal activities and, in particular, through drug trafficking.[543] The Basel Committee is an informal committee of banking supervisory authorities that was established by the central bank governors of the

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[542] T. Sherman 'International Efforts to Combat Money Laundering: The Role of the Financial Action Task Force' in MacQueen (ed) *Money Laundering* (Edinburgh: Edinburgh University Press, 1993) p. 16.

[543] M. Simpson *et al supra* note 190, p. 209.

Group of Ten States in 1974.[544] It provides a forum for regular cooperation on banking supervisory matters. Its objective is to enhance understanding of key supervisory issues and improve the quality of banking supervision worldwide.

In the 1988 Statement of Principles, the Basel Committee acknowledged that ML could undermine public confidence in banks and their stability. The central principles, which it enunciates, have been summarised as follows:[545]

- *Know Your Customer:* Banks should make reasonable efforts to determine the customer's true identity and have effective procedures for verifying the *bona fides* of new customers (whether on the asset or liability side of the balance sheet).
- *Compliance with laws:* Bank management should ensure that business is concluded in conformity with high ethical standards, that laws and regulations are adhered to and that a service is not provided where there is good reason to suppose that transactions are associated with laundering activities.
- *Co-operation with law enforcement agencies:* Within any constraints imposed by rules relating to customer confidentiality, banks should cooperate fully with national law enforcement agencies including, where there are reasonable grounds for suspecting ML, taking appropriate measures, which are consistent with the law.
- *Policies, procedures and training:* All banks should formally adopt policies consistent with the principles set out in the Statement of Principles and should ensure that all members of their staff concerned, wherever located, are informed of the bank's policy. Attention should be given to staff's training in matters covered by the Statement. To promote adherence to these principles, banks should implement specific procedures for

544 See the History of the Basel Committee and its Membership in available at ≤History of the Basel Committee (bis.org) last visited on 14 December 2020.

545 J. Drage 'Countering Money Laundering: The Response of the Financial Sector' in MacQueen (ed) *Money Laundering* (Edinburgh: Edinburgh University Press, 1993) p. 65.

customer identification and for retaining internal records of transactions. Arrangements for internal audit may need to be extended in order to establish an effective means of testing for general compliance with the Statement of Principles.

In an effort to maximise the impact of these principles, the Basel Committee took the step of commending the Statement of Principles to supervisory authorities in other jurisdictions. It considered that banking supervisors had a general role to encourage ethical standards of professional conduct among banks. The Statement of Principles therefore encouraged the management of banks to put in place effective procedures to ensure that all persons conducting business with the institution concerned were properly identified. Transactions that did not appear legitimate were discouraged and that effective cooperation with law enforcement agencies was achieved.[546] Not restricting itself to the proceeds of drug trafficking as the Vienna Convention 1988 had done, the Basel Committee, as the 1990 Money Laundering Convention was to do two years later, stated that the Statement of Principles was to apply to criminal activity more generally.

Seven year later, in reviewing the findings of an internal survey of cross-border banking in 1999, the Basel Committee identified deficiencies in the bank know-your-customer (KYC) policies of a large number of states.[547] It consequently asked the Working Group on Cross-border Banking to examine the procedures then in place and to draw up recommended standards applicable to banks in all states. These were issued as a consultative document in January 2001. This resulted in the publication in October of that year of the Basel Committee's *Customer due diligence for banks report.*[548] The Basel Committee made clear its expectation that the report would become the benchmark for supervisors to establish national practices and

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546 R. Fox and B. Kingsley *A Practitioner's Guide to UK Money Laundering Law and Regulation* (Thomson Reuter, 2010) p. 152.

547 *Ibid*., p. 153.

548 Basel Committee for Banking Supervision, Publication No.85, Customer due diligence for banks, October 2001, available from ≤www.bis.org≥ cited in Fox and Kingsley *supra* note 546.

for banks to design their own KYC programmes although it noted that some jurisdictions already met or exceeded the standards set out in the report.

In publishing the report, the Basel Committee stressed that it continued strongly to support the adoption and implementation of the FATF Recommendations and that its KYC principles were intended to be consistent with them. It also said that it would consider the adoption of any higher standards introduced by the FATF as a result of its current review of the Recommendations.[549]

The Basel Committee's view was that KYC safeguards should exceed simple account opening and record-keeping and require banks to formulate customer acceptance policies and tiered customer identification programmes that involve more extensive due diligence for higher risk accounts and pro-active monitoring for suspicious activities. KYC should be a core feature of bank's risk management and control procedures and be complemented by regular compliance reviews and internal audit. The Basel Committee advised that the intensity of KYC programmes beyond such essential elements should be tailored to the degree of risk.[550]

In February 2003, the Basel Committee published an attachment to *Customer due diligence for banks*, entitled *General Guide to Account Opening and Customer Identification,* which was developed by the Working Group on Cross-Border-Banking. This provided additional guidance for banks with regards to the nature of information that should be obtained in relation to a new customer opening an account and the appropriate sources for verifying such information.[551]

Since 2003, the Basel Committee has published various other statements and documents. In particular, in May 2009, after consultations taking place over several years, it published a new paper on the importance of transparency in the processing of cross-border

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549 R. Fox and B. Kingsley *supra* note 546. This was in reference to prior FATF 40 Recommendations and the latest version for 2012.

550 *Ibid.*

551 M. Simpson *et al supra* note 190, p. 218.

payment transfers.[552] The paper addresses a significant problem that arises in the processing of cross-border payments involving several financial institutions (in particular SWIFT payments), in which many of the institutions will act as no more than intermediaries in the payment process between the originator of a transaction, and the ultimate beneficiary. The crucial element of the problem identified by the Basel Committee is the fact that existing messaging practice do not always ensure transparency for cover intermediary banks on the transfer they facilitate. Intermediary banks in the process may not be able to see sufficient information as to the identity of the originator of the transaction and the beneficiary, with the result that those intermediaries cannot adequately assess the risk associated with correspondent and clearing operations. For example, the cover intermediary bank may be unable to screen those entities or individuals against appropriate sanctions and other applicable lists. Clearly, this could present a serious problem where, for example, the jurisdiction in which a transaction originates has less stringent AML standards than those in the jurisdiction of an intermediary bank.

The Basel Committee paper therefore calls on supervisors worldwide to establish regulations ensuring that the full information, currently seen by the originating bank and the beneficiary's bank, is also provided to intermediary banks. The SWIFT community has been active in developing a technical solution in the form of a new transaction message format, which allows originator and beneficiary information to be transmitted with cover payments in a standardised manner.[553]

The Basel Principles 1988 has no legal force, since they are informal and non-binding under general international law. However, different methods have been adopted to provide the force in this regard. First, formal agreements among banks committing them to comply with the Statement of Principles were adopted in Austria, Italy and Switzerland.[554]Second, bank

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552 Basel Committee *Due diligence and transparency regarding cover payment messages related to cross-border wire transfers* available at ≤www.bis.org/publ/bcbs154.htm≥ last visisted on 14 December 2020.

553 *Supra*.

554 T. Buranaruangrote *supra* note 14, at 32.

regulators indicate that failure to comply with the Statement could lead to administrative sanctions, which was the case in France and the United Kingdom at the inception of the Principles. Finally, customer identification or KYC, is now included as part of wider customer due diligence (CDD) under the FATF Forty Recommendations; this is further considered 2011below.

In terms of the role of soft law to AMLC, the Basel principles of 1988 were to the preventive AMLC what the Vienna Convention 1988 was to the repressive AMLC.

5.4 The Wolfsberg Principles

As the public sector reacted to the threat to the financial system posed by ML with a multiplicity of initiatives and bodies, the private sector was also taken steps to address its own needs in the area. In October 2000, 11 major international banks[555] known as the Wolfsberg Group signed and unveiled a set of non-binding informal best practice guidelines called the Global Anti-Money Laundering Guidelines for Private Banking (known as the Wolfsberg Principles) governing the establishment and maintenance of relationships between private banks and clients.[556]The Principles contain guidelines on client acceptance and list a number of situations where additional due diligence should be carried out.

The guidelines were formulated with the practical needs of the above segment of banking sector in mind. In terms of innovation, most attention has been attracted by the guidelines on client acceptance and the enumeration, in that context, of situations requiring additional diligence or attention. These ranged from the problems posed by those connected with high-risk states to public officials and associated PEPs.[557] This refers to individuals who

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555 Now 13 – ABN AMRO Bank, Barclays Bank, Banco Santander Central Hispano, SA, The Chase Manhattan Private Bank, Citibank, NA, Credit Suisse Group, Deutsche Bank AG, HSBC, JP Morgan, Societe Generale and UBS AG.

556 R. Fox and B. Kingsley *supra* note 546, p.154.

557 M. Simpson *et al supra* note 190 p. 219.

have to have had positions of public trust and who should be subjected to heightened scrutiny. Additional guidance was published by the Group indicating that the term should be understood to include persons whose current or former positions[558] could attract publicity beyond the borders of the state concerned and whose financial circumstances may be the subject of additional public interest.[559]

The Wolfsberg Group has been active since 2000 in publishing further guidelines for the private banking industry. In June 2006 the Wolfsberg Group published two papers: *Guidelines on a Risk-Based Approach for Managing Money Laundering Risks* and *AML Guidance for Mutual Funds and Other Pooled Investment Vehicles*.[560] The Wolfsberg Group also works with other industry bodies to develop guidelines, and approve standards developed elsewhere in the financial industry to combat ML.

In 2008, the Group decided to refresh it 2003 FAQs on PEPs, followed by a reissued *Statement on Monitoring, Screening and Searching* in 2009. 2009 also saw the publication on the first *Trade Finance Principles and Guidance on Credit/Charge Card Issuing and Merchant Acquiring Activities.*[561] The Trade Finance Principles were expanded upon in 2011 and the Wolfsberg Group also replaced its 2007 *Wolfsberg Statement against Corruption* with a revised, expanded and renamed version of the paper: *Wolfsberg Anti-Corruption Guidance.*[562] This Guidance takes into account a number of recent developments and gives tailored advice to international financial institutions in support of their efforts to develop appropriate anti-corruption programmes, to combat and mitigate bribery risks associated with clients or transactions and also to prevent internal bribery.

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558 The rule of thumb being that they would continue to be PEPs for one year after leaving office.
559 R. Fox and B. Kingsley *supra* note 546 p.155.
560 *Ibid*.
561 D. Cox *Handbook of Anti-Money Laundering* (John Wiley & Sons, Incorp. 2014) p. 112
562 *Ibid.*

More recently, focus has expanded to the emergence of new payment methods and the Group published *Guidance on Prepaid and Stored Value Cards,* which considers the ML risks and mitigants of physical prepaid and stored value card issuing and merchants acquiring activities and supplements the Wolfsberg Group *Guidance on Credit/Charge Issuing and Merchant Acquiring Activities 2009.*[563] In 2014 the Group issued *Guidance on Mobile and Internet Payment Services (MIPS)* and reissued the *Principles for Correspondence Banking* first issued in November 2002.[564] Recently the Wolfsberg Group, in conjunction with other industry bodies such as the Bankers Association for Finance and Trade, and the Clearing House Association, has been active in assisting with developing and approving the new SWIFT message format for cover payments noted above.

Below is a summary of the Wolfsberg Standards consisting of the various sets of AML Principles, as well as related statements, issued by the Group since inception:

- Wolfsberg Principles for Correspondence Banking (2014)
- Wolfsberg Statement – Guidance on Mobile and Internet Payment Services (MIPS) (2014)
- Wolfsberg Private Banking Principles (May 2012)
- Wolfsberg Guidance on Prepaid and Stored Value Cards (14th October 2011)
- Wolsberg Anti-Corruption Guidance (20111)
- Statement on the publication of the Wolsberg Anti-Corruption Guidance (August 2011)
- The Wolfsberg Trade Finance Principles (2011)
- Wolfsberg Monitoring Screening Search Paper (9th November 2009)
- Wolsberg AML Guidance on Credit/Charge Card Issuing and Merchant Acquiring Activities (May 2009)

[563] *Ibid.*
[564] *Ibid.*

- The Wolfsberg Group, Clearing House Statement on Payment Message Standards (April 2007)
- Wolfsberg Group, Notification for Correspondence Bank Customers (April 2007)
- The Wolfsberg Statement against Corruption (February 2007)
- Wolfsberg Statement – Anti-Money Laundering Guidance for Mutual Funds and Other Pooled Investment Vehicles (March 2006)
- Wolfsberg Statement on Monitoring Screening and Searching (September 2003)
- Wolfsberg Statement on The Suppression of the Financing of Terrorism (January 2002)

As a voluntary code of conduct that focuses on private banking, the Wolfsberg Principles are specific to this busines segment. At the same, however, they are also broadly drawn and in certain areas vague. Whilst they are not a panacea for combating ML, the Wolfsberg Principles do have the potential to bridge the ML gap in the private banking sector. The real strength of the Wolfsberg Principles, however, lies in the fact that the participant banks commit to apply the rules to all their operations at home and abroad.[565]

Welcome though such developments are, they can only play a secondary role in effort to combat ML. As the October 2001 Basel Committee Report noted:

> "Voluntary codes of conduct issued by industry organisations or associations can be of considerable value in underpinning regulatory guidance, by giving practical advice to banks on operational matters. However, such codes cannot be regarded as a substitute for formal regulatory guidelines".[566] This attest to the informal non-binding nature of the codes.

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565 M. Pieth and G Aiolfi 'The Private Sector Becomes Active: The Wolfsberg Process' (2003) 10(4) *Journal of Financial Crime* at 361.

566 Basel Committee 2001 cited in M Simpson *et al supra* note 190, p. 219.

5.5 The EC Money Laundering Directives

European Union Law is a body of treaties, law and court judgements that operates alongside the legal systems of the European Union member States. It has direct effect within the EU member states and, where a conflict occurs, takes precedence over national law.[567] The primary source of EU law is the EU's treaties.[568] These are power-giving treaties, which set broad policy goals and establish institutions [569] that amongst other things can enact legislation in order to achieve those goals. The legislative acts of the EU come in two forms: regulations and directives. Regulations become law in all member states the moment they come into force, without the requirement for any implementing measure,[570] and automatically override conflicting domestic provisions. Directives require member states to achieve a certain result while giving the state the discretion as to how to achieve the result.

Treaties under EU law thus, have similar effect under general international law, as would any other treaty in international law. However, regulations and directives lack the attributes of a treaty since they are created for the specific purpose of meeting the obligations under an existing EU treaty. They are therefore outside the definition of an international agreement under Article 2 of the VCLT, 1969. In addition, given their mode of creation (which

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567 The principle of direct effect was established in relation to the Treaties of the European Union by the European Court of Justice (ECJ) in *Van en Loos* v. *Nederlandse Administratie der Belastinger* 1963] ECR 1; [1970] MLR 1 (commonly referred to as *Van Gend en Loos*). The ECJ in that case laid down the criteria (commonly referred to as the "Van Gend Criteria") for establishing direct effect. The provisions must be sufficiently clear and precisely stated. Be unconditional or non-dependent and confer a specific right for the citizen to base his or her claim on. See generally N. Foster *Foster on EU Law* (New York: Oxford University Press, 2006) pp. 174 -176.

568 The Treaty of Lisbon or Lisbon Treaty (initially known as the Reform Treaty) is an international agreement that amends the treaties, which comprise the constitutional basis of the European Union (EU). The Lisbon Treaty was signed by the EU member states on 13 December 2007 and entered into force on 1 December 2009 It amends the Treaty on European Union (TEU; also known as the Maastricht Treaty) and the Treaty establishing the European Community (TEU; also known as the Treaty of Rome).

569 The Maastricht Treaty led to the creation of the euro and created what was commonly referred to as the pillar structure of the European Union. This conception of the Union divided it into the European Community (EC) pillar, the Common Foreign and Security Policy (CFSP) pillar, and the Justice and Home Affairs (JHA) pillar. The first pillar was where the EU's supra-national institutions – the Commission, the European Parliament and the European Court of Justice – had the most power and influence The other two pillars were essentially more intergovernmental in nature with decisions being made by committees composed of national politicians and official.

570 *Variola* v *Amministrazione delle finanze* (3473) [1973] ECR 981.

is outside the traditional definition of a treaty in international law), they may be classed as informal soft law as noted under our model categorisation of soft law in chapter one.

However, the EC ML Directives is an integral part of the European Union law making. This is because the directive whilst not a part of traditional international law, functions with the same binding effect as a treaty under the European Union on member states.[571] The implication is that the EC ML Directives, though informal, are binding on the member states of the European Union under the principle of direct effect. The EC ML Directive is thus, taken to have a supranational effect given the doctrine of the supremacy of the EC law, which emerged from the European Court of Justice Decision in *Costa* v. *ENEL*.[572] Although the principle of direct effect was established by the ECJ in relation to the Treaties of the European Union, in *Van Gend en Loos,*[573] the principle has subsequently been loosed in its application to treaty articles.[574] The ECJ has expended the principle, holding that it is capable of applying to virtually all of the possible forms of EU legislation,[575] the most important of which are regulations and, in certain circumstances, directives.

Accordingly, it is to the European Commission's credit that it became aware early on of the need to effectively respond to the threat of ML. A Community regulation was first laid down in 1991 through the First EC ML Directive on the prevention of the use of the financial system for the purpose of ML.[576] The First EC ML Directive 's definition of ML specifies

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571 Article 189 of the EEC Treaty (now Article 249 EC) provides for the binding nature of directives and this is said to be only in relation to each Member State.

572 *Falminio Costa* v. *ENEL* (1964) ECR 585, 593.

573 *Supra* note 567.

574 *Van Gend en Loos* was a claim based on treaty article. The doctrine is therefore, applicable when the particular provision relied on fulfils the above criteria.

575 In *Defrenne* v. *SABENA* [1974] ECR 631 the ECJ decided that there were two varieties of direct effect. The difference between a Vertical direct effect and an Horizontal direct effect, is based on the entity against whom the right is to be enforced. Vertical direct effect concerns the relationship between EU law and national law, while Horizontal direct effect concerns the relationship between individual (including Companies). Directives are usually incapable of being horizontally directly effective due to the fact that they are only enforceable against the state. However, certain provisions of the treaties and legislative acts such as regulations are capable of being directly enforced horizontally.

576 Official Journal L166 of 28061991 p. 77.

categories of financial intermediaries and their obligations and requirements. It defines these obligations and requirements and indicates the public authorities responsible for the control functions. This general framework was devised as consistent with the 40 Recommendations of the FATF (at the time) on ML, which was then seen as the global standard-setter created shortly before.[577]

Key to this directive was distinguishing between 'competent authorities' and 'authorities responsible for combating ML'. This recognised that the authorities responsible for combating ML were mainly those who received and carried out analyses of suspicious transaction. When reporting entities or supervisory authorities become aware of such transactions, they are required to forward these on for subsequent analysis to the national authority responsible for combating ML. This distinction is fundamental to the AML framework developed according to the FATF Recommendations, which is thought to focus more on the role of 'competent authorities. The directive thus provides for a clustering of public sector expertise to analyse what could be very complex schemes.

The dual nature of this system also recognises the early warning role of the private sector in the prevention of ML. Leads provided from this source are purely indicative and are subject to a series of filters established by the authority responsible for combating ML. After the filtering, selected material can then be used by 'competent authorities', i.e., traditional law enforcement authorities who are better able to focus their investigative and judicial powers on relevant facts.

This directive was also said to be a landmark text in the sense that most of the key preventive measures that subsequently proved useful were first introduced here.[578] These consist of the earlier preventive measures, which include the need for customer identification,

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577 W. H. Muller *et al supra* note 333, p. 60.

578 *Ibid.*

record keeping, and reporting requirements associated with suspicious transactions. For a suspicious transaction to lead to investigation, reporting entities were required to maintain sufficient customer details and the relevant documentation admissible as evidence to an investigation into ML. Consistent with such an integrated approach, all reporting entities were required to implement appropriate internal control and communication procedures. In addition, they had to train their employees to be aware of possible laundering patterns.

However, the need for further progress was required to enhance the effectiveness of the EU and national AML frameworks, hence the introduction of the Second EC ML Directive .[579] The aim of the Second EC ML Directive was to refine existing provisions and to plug perceived gaps arising out of the successful implementation of the first directive.[580] As noted in chapter three, this directive also played a repressive role by extending the scope of predicate offences to all forms of large-scale criminal activity with links to organised crime, and thus liable to generate significant 'launderable' revenues.[581]

Other elements introduced in the second directive include extending the scope of reporting entities.[582] The European Parliament and some typological work[583] drew the Commission's attention to launderers passing numerous low-value wire transfers through *bureaux de change* and money remittance outlets in reaction to heightened culture of surveillance in the banking sector. Naturally, as larger institutions tightened their control, organised crime turned to financial intermediates operating under less stringent scrutiny. A result of this was to broaden the scope of financial institutions covered in the directive to include both mutual funds and independent legal professionals. Nevertheless, information

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579 Official Journal L344 of 28122001, p. 76.
580 *Supra* p. 61.
581 See *supra* pp. 147-149.
582 *Supra*.
583 See, generally, the current list of Money Laundering typology available at ≤wwwfatf-gafiorg/pages/≥ visited on 15 December 2020.

received by legal professionals in their role of defending or representing a client was exempted from the reporting obligation.

Thus, the majority of discussion on AML legislation proposed by the European Commission was stated to have taken place in a consensual atmosphere. This consensual spirit was present when the Commission tabled a proposal for a Third EC ML Directive,[584] and is noteworthy given the potential irritation of it following so soon after the Second EC ML Directive. In particular, some member states had not even completed transposition of the Second EC ML Directive, when the draft of the Third EC ML Directive was being released. The other explanation that could be given for the swift adoption of the directive is the very changed circumstances emerging in the wake of the 11 September and the Madrid bombings. It was also said to have been facilitated by the need to build on existing measures.[585] Put simply, the Third EC ML Directive release extended the scope to the financing of terrorism.

The Third EC ML Directive expanded the range of institutions within scope to include life insurance intermediaries and trust and company service providers and widened the definition of high value dealers to capture those who accept cash payment of EUR 15,000 or more. This is wider than the scope of the equivalent definition in the Second EC ML Directive , which included only dealers in goods such as precious stones.[586] It has however, been recognised that the nature of the relationship between professionals (especially lawyers) and their clients requires special treatment, particularly in the context of the operation of the obligation to report suspicious transactions to, and otherwise cooperate with, the authorities.[587] The exemptions for members of the professions, acting in circumstances where those persons are in the course of ascertaining the legal position for the client or performing their task of

584 Directive 2005/60/EC.
585 M. Simpson *et al supra* note 190, p. 62.
586 See Article 2 for the Third EC ML Directive for a full list of institutions affected.
587 The relevant exemptions are contained in Recital 20 to the Third EC ML Directive in which the rationale behind the safeguard is stated.

defending or representing that client in, or concerning judicial proceedings, are duly provided for under article 23. [588]

Accordingly, chapter II of the Third EC ML Directive requires CDD to be carried out by persons within the scope of the directive when:

a. establishing a business relationship.
b. carrying out occasional transactions amounting to EUR 15,000 or more (whether by way of a single operation or a series of operations that appear to be linked).
c. there is a suspicion of ML or terrorist financing (regardless of any derogation, exemption or threshold).[589] or
d. there are doubts about the veracity or adequacy of previously obtained customer identification data.[590]

The required CDD measures, which follow closely the measures set out in the Recommendation 5 of the 2003 FATF's Recommendations,[591] are set out in article 8 of the Third EC ML Directive, and comprise of:

a. identifying the customer and verifying the customer's identity on the basis of documents, data or information obtained from a reliable and independent source.
b. identifying, where applicable, the beneficial owner[592]and taking risk-based and adequate measures to verify his identity so that the institution or person is satisfied that it knows who the beneficial owner is, including, with regard to

588 Which provides an exemption from the requirement to make suspicious activity reports to the national FIU (FIU is further considered below) and article 9, which provides an exemption from the prohibition on carrying out transactions for clients in respect of whom adequate customer due diligence information has not been obtained?
589 See *infra* p. 192 for more on the CDD**.**
590 M. Simpson *et al supra* note 190, p. 214.
591 Now Recommendation 10 of the 2012 revised FATF Recommendations.
592 Defined broadly, as the person who ultimately owns the customer or on whose behalf a transaction or activity is carried out.

legal persons, trusts and similar arrangements, taking adequate steps to understand the ownership and control structure of the customer.

c. obtaining information on the purpose and intended nature of the business relationship; and

d. conducting ongoing monitoring of the business relationship including scrutiny of transactions undertaken throughout the course of the relationship to ensure that transaction being conducted are consistent with the institution's or person's knowledge of the customer, the business and risk profile, including, where necessary, the source of the funds, and ensuring that the documents, data or information held are kept up to date.

Under the Third EC ML Directive, the identification of beneficial ownership is crucial. Financial intermediates can no longer stop at knowing the identity of managers of a legal arrangement, such as a company or a trust. They are now required to go beyond the intermediary in order to determine who exactly the beneficiaries of deposited funds are. A crucial aspect of the Third EC ML Directive compared with its predecessors is the embodiment of a 'risk-based approach' to CDD. The institutions that apply CDD measures are therefore permitted to determine the extent of such measures on a risk-sensitive basis depending on the type of customer, business relationship, product or transaction.[593] The directive adopted a 'risk-based approach' in consideration of the daunting overhead such extensive cross-checking entails. As such, financial intermediaries have to set up adequate internal procedures to pinpoint areas of high, medium and low risk and adjust their level of scrutiny accordingly.

The Third EC ML Directive also includes provisions relating to the mandatory reporting by relevant institutions of suspicious transactions. Specifically, member states must require

593 Article 8(2) Third EC ML Directive.

such institutions to promptly inform the national FIU,[594] on their own initiative, where they know or suspect, or have reasonable grounds to suspect that ML is being or has been committed or attempted, and by promptly furnishing the FIU, at its request, with the procedures established by the applicable legislation.[595] There is also the requirement that such institutions must not carry out transactions, which they know, or suspect relate to ML, until they have informed the national FIU.[596] The Third EC ML Directive also includes provisions that prohibited 'tipping off'[597] a customer or any other third party that a suspicious activity report has been made, or that a ML investigation is being carried out.[598]

The Fourth EC ML Directive[599] came into force on 26 June 2017 and a key feature of this Directive was its much-increased emphasis on the use of risk-based approaches at every level The Third EC ML Directive gave legal recognition to the concept of a risk-based approach. The Fourth EC ML Directive went further, with requirements for:[600]

- EU states to commission national assessment of ML and terrorist financing risks.
- Individual institutions to develop risk-based policies, procedures and controls.
- Individuals working in these institutions to conduct risk-based Customer Due Diligence (hereinafter CDD) for all their business.

Counting the number of times, the use of the word 'risk' appears in consecutive Directives (except for the Sixth EC ML Directive) gives some indication of the increasing importance that has been attached to risk-based approaches. The Third EC ML Directive mentions 'risk' just 35 times whereas the Fourth EC ML Directive mentions it 149 times.[601]

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[594] Known as Financial Intelligence Unit – see chapter five below.

[595] Article 22. This is in line with the FATF Recommendation 20.

[596] Article 24 provides for an exemption where to refrain from carrying out a transaction is impossible or is likely to frustrate an investigation into the suspected ML.

[597] See *supra* p. 134 where the offence of 'tipping off 'is also used as a tool for repressive AMLC.

[598] Article 28 of the Third EC ML Directive, which is line with FATF Recommendation 21.

[599] *Supra* note 356.

[600] T. Parkman *Mastering Anti-Money Laundering And Counter-Terrorist Financing* (FT Publishing, 2019) p. 31.

[601] *Ibid*. The Fifth EC ML Directive mentions 'risk' 47 times, however in the Sixth EC ML Directive risk is only mentioned 2 times.

The Fourth EC ML Directive introduced other significant changes like lowering maximum threshold (Euro, 7,500) and tighter record keeping requirements for cash transaction; tightening up of the enhanced due diligence measures for Politically Exposed Person etc.

This Directive also included an amendment to the rules for Simplified Due Diligence (SDD) that had been introduced under the Third EC ML Directive. Under the Third EC ML Directive, firms were able automatically to apply SDD to certain types of legal person, for example firms subject to regulation under the EU AML Directives or equivalent legislation; companies whose securities are listed on a regulated market; and public authorities. However, under the Fourth EC ML Directive firms could no longer automatically default to SDD in any circumstance and may only use SDD following an evidence-based risk assessment of the individual or entity in question.[602]

On 19 June 2018 the EU published a Fifth EC ML Directive.[603] The Fifth EC ML Directive constitutes part of the EU's Action Plan against terrorism which was announced in February following terrorist attacks in Paris and Brussels and in response to the publication of the Panama Papers in April 2016. Hot on the heels of the Fourth EC ML Directive which had come into force just one year previously, the Fifth EC ML Directive is not as extensive as its precedent, although it does contain some important new provisions. Thus, under this Directive the scope of the regulatory regime has been extended to include virtual currency exchange platforms and customer wallet providers.

Other provisions under the Fifth EC ML Directive includes the strengthening of beneficial ownership of EU based companies available to the members of the general public; requiring firms to consult the beneficial ownership register as part of their due diligence activity; requiring EU member states to create a list of the national public offices and functions

602 *Ibid*, p. 32.
603 *Supra* note 357.

that qualify as having a Politically Exposed Person (hereinafter PEP) status; robust enhanced due diligence measures for financial flows emanating from high-risk countries; prohibiting anonymous bank accounts and safe deposit boxes; making real estate ownership information centrally available to public authorities; lowering the thresholds at which the purchasers of prepaid cards and users of e-money must be identified and strengthening the powers of Financial Intelligence Units (hereinafter FIUs).

A Sixth EC ML Directive [604] came into force at the EU level on 2 December 2018, and the EU member states are required to have implemented it by 3 December 2020. The Directive focuses on harmonising the EU approach to the offence of ML across the region. It calls for the introduction of a new corporate offence for failure to prevent ML, which could see the EU adopt a stricter approach to corporate criminal liability for ML. The United Kingdom has, however, opted out of the Sixth EC ML Directive perhaps in anticipation of the end of the Brexit transition period on 31 December 2020.

In summary, whilst the EC ML Directives have been concerned primarily with the regulation of financial services activities and the prevention of ML within the single market of the EU, they have had a direct and indirect impact well beyond the common external frontier.[605] This has been and is being achieved in a number of different ways. First, for example, the Directives themselves have been drafted in such a way as to ensure that all relevant institutions which operate within the EU are subject to their provisions, and not solely those institutions which have their head office within its borders. The Third EC ML Directive makes it clear that its application extends to branches in the EU of credit and financial institutions that have their head office outside the EU.[606] The impact is in effect, supranational.

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604 *Supra* note 358.
605 M. Simpson *et al supra* note 190, p. 216.
606 Article 3(1) and 3(2) of the Third EC ML Directive.

Secondly, and of greater importance, is the fact that the EC ML Directives (from the First Directive onward) have all applied to those European Free Trade Association (EFTA) states which ratified the Agreement for a European Economic Area (EEA). Consequently, Austria, Finland and Sweden were not faced with the need to address this issue *de novo* upon entry to the EU in January 1995.[607] Similarly, the fact that Norway, Liechtenstein and Iceland are not EU members[608] does not affect the need for them to comply with this measure as trading partners of the bloc.

The eastward expansion of the influence of the Directives has also been a feature of the strategy of the EC in this sphere. This has been most obvious in the negotiation of 'Europe Agreements'– association arrangements of the most advanced form –with the newest member states of the EU, including both those who joined in 2004,[609]as well as the current candidate states.[610] Each new candidate will be expected by the EC to adopt stringent standards on ML. The EU has been active in providing assistance to its current candidate states to combat ML, in order to help ensure that they meet the required standards prior to any future entry into the EU: in 2007, for instance, the EU provided EUR 1.5 million to help Macedonia strengthen its financial system to prevent ML.[611]

As the EC has previously stated in relation to an earlier set of candidate states:

"The ML directive is an integral part of the *acquis communautaire* and all candidate states will be required to implement it. Efforts to assist in this process form part of the pre-accession strategy."[612] This emphasis has been strengthened and deepened by the 1998 Pre–Accession Pact on Organised Crime between the applicant states and the member states of the EU. Principle 13 thereof expressed agreement that there should be not only full implementation of

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607 *Supra*.
608 Although in the wake of the global financial crisis, Iceland has now applied for full EU membership.
609 Malta, Cyprus, Slovenia, Estonia, Latvia, Lithuania, Poland, the Czech Republic, Slovakia and Hungary.
610 Croatia, Macedonia and Turkey.
611 M. Simpson *supra* note 190, p. 217.
612 *Ibid*.

the Directive, but also of the FATF Recommendations and the 1990 Money Laundering Convention. In this manner, as Cullen has pointed out, the First EC ML Directive provided "the basis for a comprehensive code of AML legislation throughout the continent of Europe";[613] and in the words of Koskenniemi, soft law provisions then become negotiating chips in an unending process of balancing members' interest.[614]

5.6 The FATF and the Forty Recommendations

When the heads of state and governments of the G7 states and the President of the European Commission convened in Paris in July 1989 for the fifteenth G7 summit, they met amid mounting international concern over the devastating proportions that the international drug problem had reached. There was widespread concern over the size of the threat posed by ML to financial institutions and the banking system. It was decided that firm action was needed at both national and international level to combat the problem. As a result, the G7 attendees convened a FATF to assess the results of cooperation already underway to prevent ML, to examine the current ML techniques and trends and to set out future implementation measures, including the adaptation as necessary of the statutory and regulatory systems of members to enhance multilateral assistance.

The FATF was thus conceived as an informal non-binding inter-governmental policy-making body that would work to generate the necessary political will to bring about national legislative and regulatory reforms to combat ML. It was intended to be flexible, with no closely drawn constitution, nor even an unlimited lifespan. The initial mandate of the FATF was to "assess the results of co-operation already undertaken in order to prevent the utilization of the banking system and financial institutions for the purpose of money laundering, and to consider

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613 P. J. Cullen 'The European Community Directive' in MacQueen (ed) *Money Laundering* (Edinburgh: Edinburgh University Press, 1993) p. 49.

614 M. Koskenniemi 'The Fate of Public International Law: Between Technique and Politics' (2007) 70 *Modern Law Review* 1 at 13.

the additional preventative efforts in this field, including the adaptation of the legal and regulatory systems so as to enhance multilateral judicial assistance."[615]

The FATF conducts reviews of its mission periodically. The current review extends the work of the FATF from 2012 until 2020. The presidency of the FATF is a one-year position held by a high-level government official appointed from among the FATF members. A small-specialised Secretariat unit services the FATF and assists the President. Housed at the headquarters of the OECD in Paris, it nevertheless remains an independent body and is not a part of the OECD.

Plenary meetings are used to discuss the policy direction and initiatives of the FATF. Discussions typically cover issues such as the analysis of ML trends and countermeasures, monitoring the implementation of AML measures within the FATF and the establishment of a worldwide AML network. There are three plenary meetings each year, held in February, June and September/October. A consensual decision-making process is employed, with decisions made by the FATF on the basis of papers prepared by the Secretariat or based on written or oral reports from delegations, with the FAFT's primary publication being its annual report published at the end of June each year. This sets out the FATF's work and activities during the year.

The FATF's annual report, apart from setting out the work and activities of the FATF during the year, also set the tone for the next phase of activity and the FATF's current priority. While the priority of the FATF, in a way, depends largely on the person that takes over the presidency, there are on-going projects that are of high priority. For example, in 2011, the President of the FATF noted in an interview with the International Bar Association (IBA)[616] that one of the on-going projects that are of a very high priority is the G20's call on the FATF to identify states that might be representing a large risk on ML and financing of terrorism to

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615 T. Doyle 'Cleaning Up Anti-Money Laundering Strategies: Current FATF Tactics Needlessly Violate International Law' (2005) 24 *Houston Journal of International Law* 293.

616 Available at <http://vimeo.com/16732425> visited on 15 December 2020.

the Financial System. Thus, with the financial crisis of 2008, the G20 requested the FATF to review in general all the jurisdictions around the world[617] that might still be posing a risk of ML and financing of terrorism to the Financial System. The 2010-2011 FATF annual report[618] and the current 2012 Forty Recommendations demonstrate a clear response on the part of the FATF to this call.[619]

In addition, ML techniques are examined each year at a 'typologies' meeting. This provides a forum for law enforcement and regulatory experts from FATF member states, together with certain international organisations and bodies, as well as representatives from other states, to discuss the prevailing ML methods, the emerging threats, and any effective countermeasures that have been developed. The FATF then releases annual typologies report in February each year. This contains FATF's findings on trends, techniques, and countermeasures. Various geographic *ad hoc* groups are also convened to discuss issues that are relevant to particular regions of the world, with further *ad hoc* groups covering special topics that require more analysis that is detailed. Such groups have specific mandates and report to each plenary meeting regarding their work.

The FAFT also holds a Financial Services Forum (FSF) every two years with national and international representatives of the financial services sector and other relevant professional or business interests to discuss topics of common concern. It works in close cooperation with various other international bodies, including the International Monetary Funds (hereinafter IMF), the World Bank and the United Nations.

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617 Although, there are no longer any jurisdictions on the list of NCCTs the call highlights the on-going nature of the work of the FATF and her priorities as they unfold.

618 Available at ≤www.fatf-gafi.org/media/fatf/documents/report.pdf≥ visited on 15 December 2020.

619 In 2009, the G-20 leaders similarly issued a statement calling on the FATF to 'help detect and deter the proceeds of corruption by prioritising work to strengthen standards on customer due diligence, beneficial ownership and transparency'.

5.6.1 The Current FATF Mandate

As terrorist financing (TF) has risen up the international agenda, the FATF ‘s role has naturally extended to encompass TF as well as its remit was recently extended to include the proliferation of weapons of mass destruction (WMDs). It currently works in close cooperation with various other international bodies, including the IMF, the World Bank and the United Nations. The FATF effectively has a manifold role at the heart of the overall international AML and counter terrorist financing (CFT) regime, described below.

First, FATF monitors the progress of states in introducing AML and CFT measures, using self-assessments and more detailed mutual evaluations techniques. Non-cooperative governments have found themselves under heavy moral, political and economic pressure to be up to standard through the reviews. For example, Austria eventually agreed to prohibit anonymous savings accounts as a result of pressure from the FATF, and the states of Eastern Europe and the former Soviet Union (including Russia) have embarked upon urgent national legislative programmes in a very short space of time as a result of their inclusion on the Non-Cooperative Countries and Territories (NCCT)[620] List.[621]

Second role is to review trends, techniques, and innovations in ML (which has led to annual and specialised ML typologies reports), and to keep member states abreast of the findings. The third role is to build a global AML and CFT network by extending the reach of FATF principles. This has resulted in new member states joining the group and has led to the formation of regional FATF-style groups.[622]

The last role is to define and promulgate international standards on the combating of ML, TF and WMD Proliferation. At the heart of FATF’s activities are the recommendations on measures for combating of ML, TF and WMD Proliferation, which were completely revised

620 Below pp. 200-208.
621 T. Parkman *supra* note 209, p. 26.
622 *Infra* p. 200.

and refreshed in February 2012 (now known as 'The FATF Recommendations'[623]). The extension beyond ML and TF into the field of proliferation of WMD has been a reaction to one of the major issues of our time. A number of states, notably Iran, appear to be taking steps to build a WMD capability and accordingly we may expect sequential action and guidance from FATF on the issue of WMD proliferation financing.[624] The FATF Recommendations are summarised below.

5.6.2 The Forty Recommendations[625]

At the heart of the work of the FATF in the prevention of global ML is the 40 Recommendations, which covers five main areas, namely: AML/CFT policies and coordination; criminalisation of ML and confiscation of the proceeds of crime; TF and financing of proliferation; financial sector and non-financial sector measures; and international cooperation.

5.6.2.1 AML/CFT Policies and Coordination

Recommendations 1 and 2 cover this area. Recommendation 1 requires national states to adopt a risk-based approach[626] to combating ML and TF to ensure that resources are as efficiently applied as possible. It also requires financial institutions and Designated Non-Financial Business and Professions (DNFBPs) to identify, assess and take effective action to mitigate their ML and TF risks. Recommendation 2 requires national coordination between policymakers, the FIU,[627] law enforcement authorities, supervisors and others, to ensure that

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623 This includes the Nine Special Recommendations on the Terrorist Financing, which are merged into 'The FATF Recommendations'.

624 FAFT have already in fact responded with a 'Typologies Report on Proliferation Financing', published in June 2008 and focusing specifically on the trends and methods used in financing the development of WMD programme cited in Parkman *supra* note 207.

625 Available at ≤www.fatf-gafi.org≥ visited on 15 December 2020.

626 See pp 179-181 above for more on risk-based approach.

627 See *infra* p. 227.

the implementation of policies and activities to combat ML, TF and WMD proliferation is effectively coordinated domestically.

In February 2018: Recommendation 2 was revised to require the compatibility of AML/CFT requirements and data protection and privacy rules, and to promote domestic inter-agency information sharing among competent authorities.

5.6.2.2 Criminalisation of Money Laundering and Confiscation of the Proceeds of Crime

Recommendation 3 and 4 cover this area. In general, states are required to strengthen their legal framework, particularly their criminal law and criminal procedure law, with respect to the laundering of the proceeds of crime and measures relating to freezing, seizing, and confiscation of the proceeds of crime. Recommendation 3 therefore requires states to criminalise ML as a specific offence and to apply the crime to the widest range of predicate offences.[628] Most notably, 2012 recommendations require that states include tax evasion as a predicate offence, which was never the case previously.

Recommendation 3 requires states to criminalise ML as an offence and to do so in a manner that is consistent with the Vienna Convention 1988 and the Palermo Convention. Here, whilst the FATF has become recognised as the standard setter for international standards and best practices in AML/CFT, it has consistently reinforced the provisions of the UN instruments. The FATF in Recommendation 3 defines serious offences as those punishable by a minimum penalty of six months' imprisonment.[629] This is broader than the Palermo Convention, which defines a serious offence as any conduct constituting an offence punishable by a term of imprisonment of at least four years.[630]

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628 See pp. 147-149 on the meaning of predicate offenc**e.** Additionally, the range of predicate offences should include the range of offences provided in the Glossary to the FATF 40 Recommendations –about twenty listed there.

629 Alternative, for states whose sentencing policies set penalties using a maximum threshold, as offences punishable by a maximum penalty of one years' imprisonment.

630 Palermo Convention, Articles 2 and 6(2).

Recommendation 4 requires states to empower their competent authorities (such as police and prosecutors) to identify, trace, freeze, seize and confiscate criminal assets. It also permits states to confiscate such assets ahead of any criminal conviction, which is likely to be sought. This is an important aspect of the FATF Recommendations (and likewise for the Vienna Convention 1988 and the Palermo Convention). This is because it requires states to ensure that

> their administrative and law enforcement agencies have adequate powers for identifying and appropriating proceeds and instrumentalities of crime, particularly in order to stem the flight of illicit funds and to provide for their eventual confiscation.[631] It essentially represents a shift towards targeting the financial incentives of organised crime and criminal activities, a significant development that was originally signalled in the Vienna Convention 1988.

5.6.2.3 Terrorist Financing and Financing of Proliferation

Recommendation 5 requires states to criminalise both the financing of terrorist acts and the financing of individual terrorists and terrorist organisations, as well as designated terrorist financing offences as predicate offences for ML purpose. The recommendation represents one of the new additions to the 2012 FATF Recommendations as it incorporates earlier provisions from the nine special recommendations to the body of new FATF 40 Recommendations.

The first three Special Recommendations under the earlier nine recommendations on terrorist financing, are concerned with the implementation of the 2002 International Convention for the Suppression of the Financing of Terrorism (hereinafter STF Convention), UN Security Council (UNSC) Resolution 1267 (and related resolution), and UNSC Resolution 1373. Special Recommendation 1 requires states to ratify and implement the STF Convention

631 W. Blair and R. Brent *supra* note 384, p. 92.

and implement Resolution 1373. Special Recommendation II then requires states to criminalise the financing of terrorism, terrorist acts, and terrorist organisations.

In October 2015, the interpretive note to Recommendation 5 was revised so as to clarify that countries must criminalise financing the travel of individuals who travel to a State other their State of residence or nationality for the purpose of the preparation, planning, or preparation of, or participating in, terrorist acts or the providing or receiving of terrorist training. In October 2016, a further revision of the interpretative note to Recommendation 5 replaced 'funds' with 'funds or other assets'; and revised the glossary definition of 'funds or other assets' by adding references to oil and other natural resources, and to other assets which may potentially be used to obtain fund.

Recommendation 6 of the 40 FATF Recommendations, accordingly, requires states to implement targeted financial sanctions regimes to prevent and suppress terrorism and terrorist financing pursuant to the various UNSC Resolutions, for the purpose of freezing terrorist funds and denying their availability to designated persons and entities. This was in relation to Special Recommendation III, which requires states to freeze funds and other assets pursuant to UNSC Resolution 1267 and 1373, and to have measures in place for confiscating such funds and other assets.

Recommendation 7 also requires that states implement targeted financial sanctions regime aimed at preventing, suppressing and disrupting WMD proliferation pursuant, again, to UN Security Council Resolutions.[632] In June 2017 the interpretative note to Recommendation 7 and glossary definitions of 'Designated person or entity', 'Designated' and 'Without delay' were revised to bring the text in line with the requirements of recent United Nations Security

[632] For example, UNSC Resolution 1874 adopted unanimously by the UNSC on 12 June 2009. The resolution passed under the Chapter VII, Article 41, of the UN Charter, imposes further economic and commercial sanctions on the Democratic Republic of Korea (the DPRK or North Korea) and encourages UN member states to search North Korea Cargo, in the aftermath of an underground nuclear test conducted on 25 May 2009.

Council Resolutions and to clarify the implementation of targeted financial sanctions relating to proliferation financing.

Final under this category is Recommendation 8, which requires states to pass laws that prevent the exploitation of Non-Profit Organisations (NPOs) for terrorist financing purpose. An example here will be donations from charities sympathetic to the terrorists' cause (or possibly even set up by the terrorist group itself), or from charities whose administration systems have been infiltrated and hijacked by terrorists who then divert legally obtained charitable donations to their own terrorist cause. The aim therefore is to combat terrorist ML typologies.

5.6.2.4 Preventive Measures: Financial and Non-Financial Sector Measures

The FAFT has consistently emphasised the need to strengthen oversight of the financial sector and has provided specified recommendations on the regulatory and supervisory framework of the financial sector and on requirements relating to CDD, record-keeping, and suspicious transactions reporting. Needless to say, that these measures are core to the preventive AMLC, and will still be examined later in this chapter.

Recommendation 9 requires that bank (and other financial institutions) secrecy laws should be subordinate to the implementation of the FATF recommendations (so that, for example, institutions reporting in good faith cannot be the subject of successful legal actions for damages by customers and clients claiming damages for breach of confidentiality). Moreover, financial institutions that are in the banking, insurance, or security businesses are subject to additional prudential requirements, such as pursuant to the 'Basel Committee on Banking Supervision's Core Principles for Effective Banking Supervision' (2006) and the 'International Association of Insurance Supervisors' Insurance Core Principles and Methodologies' (2003), where applicable.

Recommendation 10 relates to CDD, which provides that Financial institutions must undertake CDD when:

- establishing business relations;
- carrying out occasional transactions above USD/EUR 15, 000 or certain wire transfers;
- there is a suspicion of ML or TF or;
- there are doubts about the truth or adequacy of previously obtained identification information.

Under Recommendations 10, institutions must:

- identify and verify the customer's identity using reliable, independent source documents, date or information;
- identify the beneficial owner of the account (either the natural person or persons who own or control it, or for whose benefit it exists, and behind whom there are no further interest(s), and understand the ownership and control structure of corporations and other entities to this effect;
- understand the purpose and intended nature of the business relationship; and
- conduct ongoing due diligence and transaction scrutiny throughout the course of the relationship to ensure consistency between account activity and stated purpose.

The CDD measures should be determined according to a risk-based approach (this is further considered below in this section) and although customer identification and verification is not required to precede the opening of business relations, this is subject to the risks being effectively managed. An inability to conduct CDD for any reason should effectively prohibit a financial institution from providing the requested services and generate a need to consider the making of a suspicious transaction report.

Recommendation 10 is the subject of an extensive interpretative note containing expanded requirements on CDD for legal persons and arrangements. In particular, it contains a systematic process for the establishment of the identity of beneficial owners. Under this process, institutions should first identify the natural person or persons exercising control of the corporation or trust through ownership; failing that, they should attempt to establish those exercising control by means other than ownership (presumably, for example, through secret agreements, commercial arrangements etc.); failing that, they should establish a relevant natural person who holds a senior management position.[633]

Recommendation 11 requires financial institutions to maintain transaction and CDD records for a minimum period of five years from the date of the transaction (in relation to transaction records) or following the termination of the business relationship (in relation to CDD records). These records must also be made available to competent authorities within the jurisdiction.

Recommendations 22 and 23 contain a range of requirements in relation to DNFBPs. A substantial change from the 2003 FATF Recommendations is the requirements on CDD, record-keeping, and suspicious transaction reporting to a category of DNFBPs. DNFBPs are essentially casinos, real estate agents, dealers in precious metals and stones, and professionals such as lawyers and accountants, where they carry out certain transactions on behalf of their clients, such as the buying and selling of real estate and establishment and management of companies and other forms of arrangements.

Recommendations 22 and 23 require that states impose CDD, record-keeping, and suspicious transaction reporting requirements on these DNFBPs that are similar to those applicable to financial institutions. These are challenging requirements for a number of reasons.

633 T. Parkman *supra* note 209, p. 29.

First, the different categories of DNFBPs are different from each other and therefore their differences ought to be taken into account when AML/CFT requirements are imposed. For instance, casinos are specifically targeted given the extent of their cash operations and perception of the involvement of organised crime in the industry.

Lawyers and accountants are targeted where they are involved in setting up companies or other legal arrangements that can be used for layering or where they make use of client accounts to carry out transactions for their clients, both in offshore and onshore jurisdictions.[634] In the case of lawyers, there is the additional question of the extent to which the public interest in ensuring that AML/CFT requirements are satisfied outweighs legal professional privilege. This then justifies the requirement that lawyers are to report to an FIU [635] where they suspect or have reason to suspect that they are dealing with funds that are the proceeds of crime or are related to terrorism financing.

In addition, unlike financial institutions, DNFBPs are not subject to prudential regulations and therefore, typically, are not regulated and/or supervised in the way that financial institutions are. To introduce these measures requires the development of a suitable level of regulation and supervision of these categories of DNFBPs and ensuring that the measures adopted are proportionate and based on a suitable risk-based assessment.

Thus, the CDD and record-keeping requirements set out in the 2003 recommendations still apply to DNFBPs in designated situations, as do the recommendations relating to internal control/foreign branches and subsidiaries, higher-risk states, the reporting of suspicious transaction and tipping-off. Specifically, the interpretative notes to Recommendation 23 make it clear that lawyers (accountants providing legal advice) are not required to file suspicious transaction reports in circumstances where the information forming the basis of their suspicion

634 W. Blair and R. Brent *supra* note 384, p. 94.
635 See chapter six *infra*.

was acquired in a situation which was subject to professional secrecy or legal professional privilege. Furthermore, lawyers are not deemed to have tipped-off a client if they seek to dissuade them from engaging in certain types of activities that might constitute ML.

Recommendations 24 and 25 require states to ensure that information on beneficial ownership and control in relation to legal persons (for example, corporations) and legal arrangements (for example, trusts) is available and can be accessed by competent authorities, and that they should also consider measures to make information on beneficial ownership and control available to financial institutions and DNFBPs. These greatly expanded requirements in relation to beneficial ownership are the subject of an extensive interpretative note, which makes it clear that at the heart of the matter companies are going to have to be able to draw a distinction between legal ownership on the one hand, and beneficial ownership on the other. They are also to appoint one or more natural persons resident in the state to provide information on beneficial ownership to the authorities.

Recommendations 26, 27 and 28 require states to maintain adequate regulatory and supervisory frameworks for financial institutions and DNFBPs and set out the minimum standards applicable.

5.6.2.5 Additional Measures for Specific Customers and Activities

Along with enhancing requirements for financial institutions and DNFBPs, the FATF Recommendations are also concerned with strengthening regulators and law enforcement agencies. The aim is that regulators have suitable powers for monitoring and ensuring compliance with AML/CFT requirements and that law enforcement agencies have suitable powers to investigate and prosecute ML and TF. Specifically, Recommendations 29, 30 and 31 require states to enable regulators and law enforcement agencies to obtain records held by financial institutions. Thus, states are required to ensure that their FIUs, regulators, and law

enforcement agencies are adequately staffed and resourced. These bodies are also required to maintain comprehensive records and statistics on their work so that this information can be used for measuring the effectiveness of the AML regimes.

Recommendation 12 deals with PEPs[636] and their family members or close associates and requires institutions to take additional steps to the CDD measures outlined in Recommendation 10. To put in place systems to determine whether the proposed relationship involves a PEP, to obtain senior management approval for such relationships, to take 'reasonable measures' to establish the source of wealth and the source of funds and to conduct 'enhanced ongoing monitoring' of the relationship.

Recommendation 13 contains a series of requirements in relation to cross-border correspondent banking, under which, in addition to the CDD measures described in Recommendation 10, financial institutions must obtain information on and understand their respondents' business, reputation, quality of supervision and quality of AML control. This also extends to obtaining senior management approval for the establishment of new correspondent relationships and understanding the respective responsibilities of the respondent and co-respondent.

Recommendation 14 requires states to establish licensing and registration systems for customers who provide money value transfer services (MVTS) with appropriate penalties for unlicensed operators.

Recommendation 15 requires states and financial institutions to risk assess new products and delivery mechanisms and technologies for ML and to take steps to mitigate those risks. In October 2018 there was an insertion of new definitions for 'virtual asset' and 'virtual

636 See section 35(12) of the Money Laundering Regulation 2017 for the definition of a Politically Exposed Person.

asset service provider' in order to clarify how AML/CFT requirements apply in the context of virtual assets including cryptocurrencies.

Recommendation 16 relates to wire transfers and is the subject of extensive guidance in the interpretative notes. The headlines requirement is that states must require financial institutions to include both originator and beneficiary information in wire transfers, and that that information should remain with the transfer throughout the payment chain. There are also requirements for financial institutions to be able to detect wire transfers, which lack the necessary information, and to freeze the processing of wire transfers apparently involving designated persons and entities.

Recommendation 17 allows states to permit financial institutions to rely on third parties to perform CDD steps (other than ongoing due diligence) in certain circumstances. However, the relying institution must retain ultimate responsibility for the adequacy or otherwise of the CDD measures.

Recommendation 18 requires that states should compel their financial institutions to implement AML programmes, which, in the case of institutions with overseas branches and subsidiaries, should be a consistent standard throughout, based on the home state's requirements. On November 2017 there was a revision of the interpretative note to Recommendation 18 clarifying the requirements for information sharing in relation to unusual or suspicious transactions within financial groups, including a requirement to provide such information toto branches and subsidiaries as necessary for AML/CFT risk management.

Recommendation 19 requires that financial institutions should apply enhanced CDD measures to relationships involving states, which have been designated by FATF as higher risk.

Recommendation 20 requires that financial institutions be under an obligation to report suspicious ML promptly to the state's FIU, while Recommendation 21 requires that national laws should protect financial institutions and their staff who have reported suspicions of ML in

good faith, from civil or criminal liability for breach of confidentiality. Recommendation 21 also mandates that states prohibit by law the practice of 'tipping-off'; which has since been criminalised under section 333 of POCA 2002.

Recommendation 32 deals with cash couriers, and the requirement that couriers should put in place mechanisms to control the cross-border transportation of cash and negotiable instruments through declaration and/or disclosure systems. Recommendations 33 and 34 impose further obligations on couriers to maintain statistics pertaining to the effectiveness and efficiency of their AML systems and to provide feedback to financial institutions and DNFBPs, which will assist them in complying with their obligations, in particular their reporting of suspicious transactions. Thus, Recommendation 35 requires couriers to maintain a range of effective, proportionate, and dissuasive sanction against persons and entities which fail to comply with their AML obligations.

5.6.2.6 International Cooperation

A key aspect of the FATF Recommendations is their focus on international cooperation. This takes the form of government-to-government cooperation, notably in the areas of mutual legal assistance and extradition, and agency-to-agency cooperation, in particular between national regulators and law enforcement agencies.[637] Recommendations 36 to 40 therefore cover a range of requirements in relation to international cooperation, including becoming parties to relevant international conventions,[638] mutual legal assistance, cross-border asset freezing and confiscation, extradition and generally providing the widest range of international cooperation in relation to ML, associated predicate offences and terrorist financing.

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637 The subject of international cooperation will be considered in the next chapter.

638 The list here includes the 1988 Vienna Convention, the Palermo Convention, UNCAC, the 1999 Terrorist Financing Convention, the 2001 Council of Europe Convention against Cyber-Crime, the 2002 Inter-American Convention against Terrorism and the 2005 Council of Europe Convention against Money Laundering.

5.7 Key Differences between the 2012 Recommendations and their Predecessors

Apart from bringing the former nine special recommendations relating to terrorist financing within the body of the main AML recommendations, thereby creating a more unified and inclusive set of standards, the new 2012 FATF Recommendations are different in the following key areas:[639]

- Tax crimes are now predicate offences: Those who followed the subject over the years will be aware that the absence of tax evasion and other serious tax crimes within the definition of 'predicate offences' which could give rise to ML– and therefore trigger the application of the necessary laws and standards– was an issue of hot debate. That debate has now been resolved and tax evasion (and other serious tax crimes) now sits alongside fraud, kidnapping and narcotics trafficking as offences, which can give rise to ML.
- Politically Exposed Persons (PEPs): Whilst many financial institutions had included domestic PEPs within their PEP risk management processes for a number of years, the old standards did not actually require this, applying, as they did, only to foreign PEPs. This has now been remedied and the requirements for enhanced due diligence and other standards in relation to PEPs effectively now apply to both foreign and domestic PEPs alike.
- Wire Transfer: The previous standards (which in themselves significantly increased the information requirements relating to wire transfers) required only that originators information should remain with the wire transfer throughout its journey through the financial system. The new standard requires that both originator and beneficiary, and related information, should travel with the transfer.

639 T. Parkman *supra* note 209, p. 32.

- Beneficial Ownership: Responding, no doubt, to the growing realisation of the extent to which front companies, front trusts and other types of corporate and legal structures and arrangements can be used for laundering large amounts of criminal money,[640] the new standards have significantly expanded the requirements in relation to the establishment of beneficial ownership.

  Specifically, Recommendation 10 dealing with CDD now includes a step-by-step process to be followed when identifying beneficial ownership, as described earlier on. In addition, there are now major new requirements for states to create systems (including a company registry, if they do not already have one) in which information on beneficial ownership is both recorded and available.

  Required measures include the nomination of a specific person or persons who will be responsible for available information regarding beneficial ownership and for providing further assistance to the authorities. Similar requirements apply to trusts and other legal arrangements. There are also requirements for states to tackle 'obstacles to transparency' such as the misuse of bearer shares and nominee shareholding arrangements.

5.8 Non-Cooperative Countries and Territories and On-Going Evaluation and Assessment

As part of the effort to combat ML, in 2000, the FATF began an initiative to identify Non-Cooperative Countries and Territories (NCCTs). The aim of the process was to ensure that all financial centres adopt and implement AML measures according to internationally recognised standards.

640 As well as disguising funds destined for terrorism and proliferation.

Following its plenary meeting in February 2002, FATF published an initial report on NCCTs.[641] It set out 25 criteria to identify detrimental rules and practices that impede international cooperation in the fight against ML. The report also described a process designed to identify jurisdictions that have rules and practices, which impede the fight against ML, and to encourage these jurisdictions to implement international standards in the relevant area. Thirdly, the report contained a set of possible countermeasures that FATF members could use to protect their economy against the proceeds of crime. Three countermeasures were initially suggested:

a) imposing customer identification obligations for financial institutions in FATF member states in respect of transactions with persons whose account is at a financial institution in an NCCT.
b) imposing specific requirements for FATF members states that are faced with such transactions to pay special attention to or to report such financial transactions; and
c) conditioning, restricting, targeting, or even prohibiting financial transactions with NCCTs.

The FATF's aim was to apply countermeasures in a gradual, proportionate and flexible manner, in the hope that the prospect of enhanced surveillance and reporting of financial transactions with the NCCT would persuade it to introduce the required AML measures. Other suggested countermeasures included taking into account that a bank is in an NCCT when considering requests for the establishment of subsidiaries or branches of that bank in FATF member states and warning non-financial sector businesses that transaction with entities within the NCCT might run the risk of ML. In addition, the FATF automatically applies the then

641 FATF Report on Non-Cooperative Countries and Territories, 14 February 2000, available at Documents - Financial Action Task Force (FATF) (fatf-gafi.org) visited on 16 December 2020.

Recommendation 21[642] to all states on the NCCT list. It also remains open to member states to impose countermeasures of their own choosing that go beyond those suggested by the FATF.

At the plenary meeting in February 2000, the FATF also set up four regional review groups (covering the Americas, Asia-Pacific, Europe and Africa and the Middle East respectively) that would analyse the AML regimes of a number of jurisdictions against the 25 criteria in its initial report. These review groups have been maintained and continue to conduct analyses of jurisdictions for compliance and to assess the progress of those classified as NCCTs. In June 2000, the FATF was able to produce its first lists of NCCTs,[643] being jurisdictions that it considered had critical deficiencies in their AML systems or that had demonstrated an unwillingness to cooperate in AML efforts. Fifteen jurisdictions were initially named and shamed, being the Bahamas, Cayman Islands, Cook Islands, Dominica, Israel, Lebanon, Liechtenstein, Marshall Islands, Nauru, Niue, Panama, Philippines, Russia, St Kitts and Nevis, and St Vincent and the Grenadines.

The states on the list of the NCCTs for the most part made significant progress in remedying the areas in which they were deficient. In June 2001, the FATF updated the list of NCCTs with the publication of its second NCCT review.[644] Four states were removed from the list,[645] but six were added[646] with an additional two being added[647] at the FATF's plenary meeting in September 2001. In June 2002, four more states were removed from the list,[648] upon

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642 Recommendation 21 has been removed from the revised 2012 FATF Recommendations, and in its place is introduced Recommendation 19 and requirement of enhanced due diligence in higher risk cases.

643 Review to Identify Non-Cooperative Countries or Territories: Increasing the Worldwide Effectiveness of Anti-Money Laundering Measures, 22 June 2000, available at Documents - Financial Action Task Force (FATF) (fatf-gafi.org).

644 Review to Identify Non-Cooperative Countries or Territories: Increasing the Worldwide Effectiveness of Anti-Money Laundering Measures, 22 June 2001, available at Documents - Financial Action Task Force (FATF) (fatf-gafi.org).

645 Bahamas, Cayman Islands, Liechtenstein and Panama.

646 Egypt, Guatemala, Indonesia, Hungary, Myanmar and Nigeria.

647 Grenada and Ukraine.

648 Hungary, Israel, Lebanon and St Kitts and Nevis.

publication of a third NCCT review,[649] and another four were removed in October 2002.[650] In February 2003, the FATF removed Grenada from the list, and in June 2003, St Vincent and the Grenadines was removed from the list, upon publication of a fourth NCCT review.[651] Since the fifth NCCT review was published, Guatemala, the Cook Islands, Indonesia, the Philippines Nauru, Nigeria, and Myanmar have been de-listed. As of 13 October 2006, there were no NCCTs.[652]

The 2007 to 2008 Annual Report declared the NCCT process to have been a success. All the 23 jurisdictions named[653] in 2000 and 2001 made significant progress to avoid being listed by the FATF as non-cooperative and efforts were made to improve AML systems. To decide whether a jurisdiction should be removed from the NCCT list, the FATF must first be satisfied that it has addressed the identified deficiencies by enacting relevant legislation and regulations. These must not only have been enacted but also have come into effect. The FATF will also take into account whether the jurisdiction is actually enforcing the necessary changes effectively. Once the FATF has decided to remove a jurisdiction from the NCCT list, it continues to monitor developments in that state closely and in doing so works with the relevant FATF-style regional body.[654] The jurisdiction concerned must submit regular implementation reports and the FATF or relevant FATF-style regional body will carry out follow-up visits to assess progress. Progress is reviewed against the implementation plan drawn up by the de-listed jurisdiction and implementation issues encountered by FATF members in the past.

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649 Review to Identify Non-Cooperative Countries or Territories: Increasing the Worldwide Effectiveness of Anti-Money Laundering Measures, 21 June 2002, available at Documents - Financial Action Task Force (FATF) (fatf-gafi.org).

650 Dominica, Marshall Islands, Niue and Russia.

651 Annual Review of Non-Cooperative Countries or Territories, 20 June 2003, available at Documents - Financial Action Task Force (FATF) (fatf-gafi.org).

652 Available at Documents - Financial Action Task Force (FATF) (fatf-gafi.org).

653 See p. 14 of the reported cited in Microsoft Word - FATF_PLEN_2008_23_REV1_FINAL_WEB.doc (fatf-gafi.org) visited on 16 December 2020.

654 See *infra* p.208.

Although there are no longer any jurisdictions on the lists of NCCTs, the FATF remains alive to the risks posed by certain jurisdictions to the international effort to prevent ML. Where concerns arise, the FATF will release a statement to the effect. Two statements were released during 2008 and 2009 expressing concern at the lack of adequate AML systems in certain jurisdictions.[655] In February 2012, the FATF confirmed nine jurisdictions[656] with strategic AML deficiencies, already identified in the FAFT Public Statement in October 2011.The jurisdictions had still not made sufficient progress in addressing the deficiencies identified in their action plan. For all these jurisdictions, the FATF has called upon its members to consider risk arising from the deficiencies associated with each of the jurisdictions.

5.8.1 Arguments for and against the legitimacy of Non-Cooperative Countries and Territories Tactics

Despite its success in securing compliance the NCCT list was suspended in November 2002. The FATF continued to monitor those countries already on the list and updated the list whenever a backlisted country had made sufficient progress, but it did not review or blacklist any new country. A common argument is that the suspension of the NCCT list was due to a lack of legitimacy by the FATF to engage in the practice in the first place.

Taking an international law perspective, Doyle noted that the development (surrounding the NCCT tactics) suggests a policy redolent of extraterritorial bullying.[657] According to the author the FATF NCCT tactics violates Article 2 of the UN Charter[658] on the sovereign equality

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655 Uzbekistan, Iran, Pakistan, Turkmenistan, Sao Tome and Principe, and northern Cyprus available at ≤www.fatf-gafi.org/dataoecd/19/28/42242615.pdf> and ≤www.fatf-gafi.org/dataoecd/16/26/40181037.pdf> visited on 20 December 2020.

656 Bolivia, Ethiopia, Kenta, Myanmar, Nigeria, Sao Tome and Principe, Sri Lanka, Syria and Turkey– available at www.fatf-gafi.org/topics/high-riskandnon-cooperativejurisdictions/more> visited on 20 December 2020.

657 T. Doyle 'Cleaning Up Anti-Money Laundering Strategies: Current FATF Tactics Needlessly Violates International Law' (2002) *Houston Journal of International Law* at 281.

658 According to Article 2 of the UN Charter, each member state is deemed equal in sovereignty.

of the Member States and Article 41 of the UN Charter [659]on the use of non-military measures to give effect to the UN decisions. He further argues that the NCCT tactics also violates the Vienna Convention 1988 because the Convention repeatedly stresses that signatories "shall carry out their obligations under this Convention in a manner consistent with the principles of sovereign equality and territoriality integrity of States and that of non-intervention in the domestic affairs of other States.[660] By blacklisting Member States of the Vienna Convention, 1998, through its NCCT tactics, the FATF is alleged to have violated the principle of non-interference and an affront to the sovereign equality of the blacklisted states, whose independence decisions must be respected and upheld.

According to Hulsse a strong argument for the suspension of the NCCT list is because it was considered illegitimate by the International Financial Institutions (IFIs).[661] In the late 1990s, the FATF was said to have tried to cooperate more closely with the IFIs. However, the IFIs strongly opposed the NCCT practice, which – according to the IMF official – "is against the nature of the Funds".[662]The IMF's self-understanding was fittingly expressed by an official: "Everything we do is uniform, it is voluntary, and it is co-operative" (quoted in BBC News 2002).[663]Thus there was a clash of philosophies between confrontation and coercion on the one side, and consensus and voluntariness on the other. Since IFIs made the end of the blacklist a precondition for their engagement the FATF was suggested to have given in.[664]

However, taking an experimentalist interpretation to the compliance tactics of the FATF, Nance observed that despite current arguments suggesting that material coercion plays a key role in the FATF consolidation and diffusion of global AML regime, the FATF operates in line

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659 By Article 41 of the UN Charter, "The Security Council may decide what measures not involving the use of force are to be employed to give effect to its decisions, and it may call upon Members of the United Nations to apply such measures.

660 T. Doyle *supra* note 657 at 303.

661 R. Hulsse 'Even clubs can't do without legitimacy: why the anti-money laundering blacklist was suspended (2008) 2 *Regulation & Governance* at 463.

662 *Ibid.*

663 *Ibid.*

664 *Ibid.*

with the principles of "experimentalist governance."[665]According to the author, Experimentalism emphasises broad, participatory standard setting, contextualised implementation, intensive but diagnostic monitoring, and routinized updating in light of experience.[666]Thus, a distinction of experimentalism from command-and-control regulation is summarised as emphasising: flexible and revisable standards over fixed and universal rules; broadly participatory networks over state centric quasi-hierarchy; and dynamic problem-solving over rule enforcement.[667]

From an experimentalist interpretation, the FATF looks much more like a transnational, multi-level network than the quasi-hierarchical structure of many international organisations. According to Nance the history of blacklisting through NCCT reveals two points that bolster the case for experimentalist interpretation.[668]First, blacklisting clearly has changed over time and has done so in response to new knowledge about the problem. States initially rejected blacklists, but as described in the Annual Report (1996), developed them in response to the perception that continued non-compliance by Turkey and Austria was "clearly damaging" their efforts.[669]Members develop the NCCT process in reaction to the move by Seychelles to profit from ML.

They later developed the International Cooperation Review Group (hereinafter ICRG) process in 2007 as a synthesis model, merging the member and the NCCT processes in light of protests from FATF members, targets of the NCCT process, and most importantly, the World Bank and IMF, who refused to cooperate with FATF while the NCCT process was still in place.[670] Members have since altered the ICRG process in June 2009. The G20 gave additional

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665 M.T. Nance 'Re-thinking FATF: an experimentalist interpretation of the Financial Action Task Force' (2018) 69 *Crime Law Soc Change* at 131.
666 *Ibid.*
667 *Ibid* at 135.
668 *Ibid* at 142.
669 *Ibid.*
670 *Ibid.*

momentum to those efforts when it called for regularly updated lists of non-compliance jurisdictions. Nance noted that there is a clear pattern within the blacklisting process, a process that many see as vital to FATF's operation, whereby members alter it in light of perceptions about the challenges of implementation.[671]

Thus, blacklists in FATF more generally have been applied only when the state or jurisdiction in question has stopped engaging the reform process. This is in line with experimentalist expectations of the use of a "penalty default." An ideal typical penalty default entails a third-party imposing "rules sufficiently unpalatable to all parties that each is motivated to contribute to an information-sharing regime that allows fair and effective regulation of their interdependence."[672] This is noted to be true since participants routinely revise the standards of an experimentalist process, providing those that participate with more voice than in a more hierarchical regulatory system.

The ICRG current blacklisting process in place today operates similarly. It effectively establishes two categories of non-compliance and only those on the worst performing list face call for enforcement. The first list –so called grey list – has a rotating cast of inhabitants based on whether members determine different states to be cooperative or uncooperative, not whether they are compliant or non-compliant.[673]Thus since the ICRG process inception, only North Korea (the Democratic People's Republic of Korea) and Iran have been blacklisted. This suggests the dynamic of a penalty default as it is stated to cut against the argument that enforcement is credible, which should diminish its efficacy because once a state engages the process and makes credible plans to improve its AML system, members quickly remove the state from the grey list.[674]Experimentalism is, therefore, thought to provide a more

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671 *Ibid.*

672 *Ibid.*

673 As of June 2017, seven countries were on the list: Bosnia and Herzegovina, Ethiopia, Iraq, Syrian, Uganda, Vanuatu, and Yemen.

674 *Supra* at 143.

comprehensive understanding of the FATF blacklists, the core body of evidence for a coercive understanding of FATF, than do other approaches.

5.9 FATF-Style Regional Bodies and Organisations

As noted earlier, several regional or internal bodies (either exclusively or as part of their work) perform similar functions to the FATF and the FATF makes an active effort to support their development. Such groups now exist in the Caribbean, Europe (for non-FATF members of the Council of Europe), Asia/Pacific, Eastern and Southern Africa and South America with further groups being established in Western and Central Africa.

Many of the groups have observer status with the FATF and have similar form and functions of the FATF with some FATF members belonging to more than one body. Bodies include the Asia/Pacific Group on Money Laundering (APG), the Caribbean Financial Action Task Force (CFATF), the Council of Europe Select Committee OF Experts on the Evaluation of Anti-Money Laundering Measures (Moneyval), the Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG) and the Financial Action Task Force on Money Laundering in Southern America (GAFISUD).

The FATF also works with international organisations to implement effective worldwide AML measures, some of which also have FATF observer status, including the Egmont Group of FIUs.[675] Over the last 20 years, a number of states have established specialised government agencies, known as FIUs, as part of their response to ML activity. These increasingly serve as a focal point for AML programmes and allow rapid and effective cooperation between states. Since 1995, a number have worked together as an informal

675 See chapter 6 for more on the role of FIUs in area of international cooperation and general AMLC.

organisation called the Egmont Group[676] with the UK represented in the Group by the Serious Organised Crime Agency (SOCA).

5.10 Domestic Law Significance and Response

A unique aspect of the FATF Recommendations is the emphasis on their implementation through mutual evaluations undertaken by the FATF and assessments undertaken by the IMF and the World Bank. Essentially, whilst the FATF Recommendations are not binding even between FATF members and do not carry the force of law, the focus of their implementation, particularly through mutual evaluations and assessments, has meant that they have had supranational influence over (or at least provided impetus for) the development of preventive national AML laws and practice around the world. The non-binding nature of the FATF Recommendations underscores the role and importance of soft law in this area. As noted in chapter two, the essential characteristics of the soft law (informal soft law) are that it is not legally binding and cannot be enforced by legal means.[677] This therefore buttresses the significance and impact that the role of informal soft law (such as the FATF Recommendations) has had in the area of preventive AMLC.

Moreover, the FATF Recommendations have been deployed in parallel with the UN conventions and UNSC resolutions and they have taken into account developments at the international law level and reinforced these international law instruments. The publication of interpretative notes alongside the recommendations, have been instructive as regards the implementation of the international law instruments. Additionally, whilst the substance and drafting of the FAFT Recommendations ultimately reflect a consensus among the FATF members (and the scope and language of individual Recommendations are often heavily

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676 A list of members of the Egmont Group is available at ≤www.egmontgroup.org/≥ visited on 16 December 2020.

677 I. Seidi-Hohenveldern, 'International Economic Law' in *Collective Course of the Hague Academic of International Law* (1979) vol. II, 167.

negotiated in view of members' positions), they nevertheless contain a relatively high level of specificity as to what is expected in this area. In this respect, although FATF Recommendations are not legally binding in domestic courts, they can be relevant in constructing domestic law and practice, which gives effect to them.[678]

An area where the FATF Recommendations have made substantial inroads into the development of domestic law and practice is in the establishment of FIUs. As set above, Recommendation 29 requires states to establish an FIU for receiving, analysing, and disseminating suspicious transaction reports and other information regarding potential ML and to ensure that the FIU has access on timely basis to financial, administrative, and law enforcement information, especially for the purpose of analysing suspicious transaction reports. Recommendation 20 requires financial institutions to report to the FIU any suspicion that funds are the proceeds of crime.[679]

In addition, since the first reference to the filling of suspicious transaction report in the original version of the FATF Recommendations and the requirement relating to the establishment of the FIUs in the current version of the FATF Recommendations, FIUs[680] have sprouted in more than a hundred states around the world. However, whilst these FIUs may be cast in different modes and are part of different government agencies (or are even stand-alone national agencies), they are essentially national focal points for processing suspicious transaction reports with the view to identifying instances where further action is required in order to pursue ML or other criminal activities. The methodology used in the FATF mutual evaluations and in the IMF/World Bank assessments[681] and the mutual recognition of FIUs in

678 W. Blair and R. Brent *supra* note 384, p. 99.
679 *Ibid.*, p. 100.
680 Such as the Financial Crimes Enforcement Network in the US and the Serious Organised Crime Agency (SOCA) in the UK – this has assimilated the former National Criminal Intelligence Service.
681 This concerns detailed criteria relating to the establishment and operation FIUs.

the Egmont Group[682] of FIUs have helped to spur the development of FIUs in other states' AML regimes, including the development of domestic laws and practices for such FIUs.[683]

5.10.1 United Kingdom's Response

The Money Laundering Regulations 2017 (hereinafter MLR 2017), which came into force on 26 June 2017, give effect in the United Kingdom to the Fourth EC ML Directive. It implements FATF's 40 Recommendations and seeks to achieve a harmonised approach to AMLC across Europe.[684] The principal effect of the MLR 2017, which replaced the previous 2007 regulations, is to impose CDD, record-keeping, and certain other requirements on firms in the regulated sector.

The MLR 2017 impose five main duties or obligations on firms and importantly legally enshrines the concept of a 'risk-based approach' to the prevention of ML. Regulation 18 specifically required firms to prepare a written risk assessment which must take the EU and UK risk assessments into consideration.[685] The other main requirements are:

- Customer Due Diligence – firms are required to carry out customer due diligence measures on a risk-sensitive basis. These measures must involve the identification and verification of customers and beneficial owners. Firms must also obtain information regarding the purpose and intended nature of the business relationship.
- Internal Policies, Control and Procedures – Firms must develop and maintain adequate and appropriate policies, controls, and procedures to mitigate ML risks.

682 The role of the Egmont Group in the overall development of FIUs is further considered in chapter five.
683 *Supra* note 679.
684 A Srivastava *International Guide to Money Laundering Law and Practice* (Bloomsbury, 5th ed, 2019) p.
685 *Ibid.*

- Record Keeping –Firms must make and retain records of their customer due diligence measures and transactions carried out by the firm, as evidence that they have complied with their legal and regulatory obligations.
- Suspicious Transactions and Reporting Procedures –Firms must ensure that suspicious transactions are identified and reported to the firm's Money Laundering Reporting Officer (hereinafter MLRO), who may report the incident to the National Crime Agency (hereinafter NCA).

Thus, whilst the offences under POCA 2002 apply to all persons, the MLR 2017 are limited in scope to persons engaged in certain types of activities. The MRL 2017, therefore, apply to 'relevant persons', who are persons acting in the course of business carried on by them in the United Kingdom. These includes credit institutions, financial institutions, auditors, independent legal professionals, trust or company service providers, estate agents, high value dealers (being traders in good and cash in respect of any transaction of £10,000 or more) and casinos.

The FAFT carried out an onsite visit to the United Kingdom in March 2018 and published it Mutual Evaluation Report on the United Kingdom in December 2018. This found that the United Kingdom had significantly strengthened it AML/CFT framework since its last evaluation. It however identified certain areas for improvement, including the resourcing of the United Kingdom's FIU, the supervision of the regulated sector and the reporting and investigation of suspicious transaction.[686]

5.10.2 Canada's Response

With its sophisticated financial system, long border, multicultural population, and one of the world's highest rates of electronic banking and commerce, Canada may be considered an

686 *Supra* note 684 p. 65.

attractive place for ML. The FATF through its mutual evaluation of countries has identified that the main domestic sources of crime are fraud, corruption, bribery, counterfeiting and piracy, illicit drug trafficking, tobacco smuggling and trafficking, and tax evasion.[687]

Canada's AML response are mainly the Criminal Code and the Proceeds of Crime (Money Laundering) and Terrorist Financing Act (hereinafter PCMLTFA). The PCMLTFA has been amended several times in recent years, including in 2010, 2013, 2014, 2015 and 2017. The objective of the PCMLTFA is to combat the laundering of proceeds of crime and financing of terrorist activities.

The Act implements client identification, record keeping and reporting requirements for financial institutions and other financial intermediaries and professionals that are susceptible to being used for ML. It is, therefore, an implementation of FATF's 40 Recommendations and seeks to achieve a harmonised preventive AMLC like the MLR 2017 in the United Kingdom. Thus, financial institutions and intermediaries subject to the PCMLTFA must appoint a compliance officer, identify risk, establish policies and procedures to control risk and ensure compliance with their AML obligations.

The most recent evaluation of Canada by the FATF was in their Mutual Evaluation Report dated September 2016. The report confirms that Canadian authorities have a good understanding of most of Canada's ML and terrorist financing risks.[688]

5.10.3 South Africa's Response

In order to bring South African legislation in line with international standards, arising in part from the realisation that the criminalisation of the substantive ML under POCA 1998 was not enough to address the problem, the government promulgation the Financial Intelligence Centre

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687 FATF, Anti-Money Laundering and Counter-Terrorist Financing Measures: Canada Mutual Evaluation Report, September 2016. See TITLE (fatf-gafi.org) visited on 17 December 2020.

688 *Ibid*.

Act 38 of 2001 (hereinafter FICA). Whilst the POCA 1998 deals with the criminalisation of ML offence, the FICA provides the administrative framework for the regulation of AMLC.

The FICA was substantially amended by the Financial Intelligence Centre Amendment Act (hereinafter Amendment Act) in 2017 to ensure that South Africa is further aligned with AML/CTF standards of the FATF. The amendment makes provision for a risk-based approach to prevention and regulation of ML in financial and other sectors. The bulk of the amendment relates to CDD and included in the scope of the CDD is identification of beneficial owner to prevent natural persons misusing legal entities for ML, requirements relating to foreign prominent public official and domestic influential persons, and the prohibition on anonymous clients.[689]

5.11 Conclusion

One of the benefits of soft law, as noted in chapter one, is that it reduces sovereignty costs. States can limit sovereignty costs by expanding the range of available institutional arrangements along a more extensive and general line. The relevance of soft law in preventive AMLC is that most of the measures are informal non-binding arrangements, under general international law, and they offer the needed flexibility for states to work out problems over time through negotiations shaped by capacity to modify and adapt the commitments into domestic laws.

Unlike traditional treaty-based obligations that must be transposed by signatory states for them to generate a binding legal effect, the preventive AML measures, like those developed by the Basel Committee Principles on Banking and the Supervision of Banks, the Wolfsberg Principles and the FATF Recommendations, are legally non-binding and have been implemented using different means. For example, in the case of the Basel Principles 1988, this

689 Sections 21B, 21G and 20A of FICA.

includes formal agreements among banks and regulators committing them to comply with the provisions or even administrative sanctions, in some cases.

As noted above, a unique aspect of the FATF Recommendations is the emphasis on their implementation through mutual evaluations undertaken by the FATF and assessments undertaken by the IMF and the World Bank. Essentially, whilst the FATF Recommendations are not binding, the focus of their implementation, particularly through mutual evaluations and assessments, has meant that they have had supranational influence over the development of preventive national AML laws and practice around the world. Moreover, the FATF's Recommendations are now co-opted into World Bank and IMF conditionalities for borrowing from these agencies, which further creates a basis for their crystallisation into domestic law.

The EC ML Directives have similarly had direct and indirect impact well beyond the common external frontier. This was possible due to their impact on all relevant institutions operating within the EU and inclusion as a basis for negotiation even in European Agreements.

CHAPTER SIX

International Cooperation and Role of FIUs

6.1 Introduction

The international effort to control ML (soft law) has provided an impetus for harmonisation in the area of repressive and preventive AMLC. This was perceived as instrumental for enhancing the effectiveness of AML law and international cooperation.[690] International cooperation is crucial for AMLC as the cross-border nature of the crime of ML allows the launderer substantial benefits and time to move the laundered money, which allows the offender to place the assets beyond the jurisdiction of the state where the predicate offence was committed. International cooperation is thus the mainstay of international efforts against ML and is referred to in many of the repressive AML conventions, which contain provisions designed to mandate or encourage it.[691] The FATF, aware of the cross-border nature of ML dedicated Recommendations 36 to 40 to the question of strengthening international cooperation.

From a strictly international law point of view, international cooperation is necessitated by the concept of sovereignty, which limits powers of a state to take investigatory, provisional and enforcement measures to its own territory.[692] Thus, under international law, enforcement jurisdiction is strictly territorial in nature. A state seeking assistance from abroad may obtain it by formal means (mutual legal assistance) or informal means (mutual assistance). Mutual legal assistance (MLA) is that part of international cooperation that permits the use of compulsory measures in the requested state to obtain or produce evidence that is required in the requesting

690 Soft law has been identified as one of the vehicles for harmonisation of law and according to Fazio: "soft law has been increasingly used by state to regulate international relations and it currently constitutes one of the most significant sources of the harmonisation of laws" –S. Fazio *The Harmonisation of International Commercial Law* (The Netherlands, Kluwer Law International 2007) p. 17.

691 See for example, article 9 of the Vienna Convention, 1988.

692 G. Stessens *supra* note 14, p. 251.

state.[693] In contrast, the term 'mutual assistance' refers to the provision of informal assistance between states. This is often done through police-to-police cooperation or between agency to agency.

It follows that, conceptually, international cooperation in criminal matters is mostly intended to deal with the lack of enforcement jurisdiction on the side of the requesting state. In the context of the international AMLC, the lack of enforcement jurisdiction may take two forms. First, information required to prove the ML offence/or the predicate offence will often be located in the territory of another state than the state which intends to prosecute the ML offence. Second, criminally derived proceeds may be located in the territory of another state than the one, which intends to prosecute the ML offence or the predicate offence.[694]

International treaty-based cooperation between judicial authorities was traditionally portrayed as the sole mode of gathering evidence abroad. It will be shown in this chapter that in the context of the international fight against ML, new modes of international evidence gathering have become increasingly important. On the one hand, administrative or non-formal cooperation is expanding and have partly taken over the function of formal mutual legal assistance (judicial assistance). In this respect, the exchange of information between FIUs has obtained a very important role and conditions under which this type of mutual administrative assistance takes place, merit to be scrutinised. This new development in the field of international evidence gathering makes it necessary to investigate the exact position, and limits, of treaty-based cooperation in ML.

Thus, international cooperation in criminal matters in the context of ML is geared towards two goals: the gathering of information, which can be introduced as evidence in the requesting state and the tracing of criminally derived proceeds with a view to their seizure and

693 Hatchard *et al Corruption and Misuse of Public Office* (2nd ed, OUP, 2011), p. 434.
694 *Supra* p. 252.

confiscation. Confiscation, together with the criminalisation of ML, as a tool for repressive AMLC was examined in chapter four. The aim of this chapter is to highlight the information-gathering role of FIUs (informal assistance) as a national focal point for processing suspicious transaction reports with the view to identifying instances where further action is required in order to provide relevant information for AMLC.

The purpose of this chapter is to examine information gathering of FIUs through informal non-binding assistance in the AMLC. This is done by looking at the limits of current international practice in mutual legal assistance and the basis or benefits for informal assistance through FIUs. The chapter does this by illustrating the limits of compulsory measures through formal legal assistance, in the requested state to produce evidence that is required in the requesting state, and the benefit of using informal measures through FIUs in the global AMLC. The chapter will therefore do two things. First, it examines existing forms of international cooperation, and the limits. Second, it considers the information-gathering role of the FIUs through informal assistance.

6.2 The Bases for International Cooperation

The AML regime, comprising the formal and informal AML obligations to repress and prevent the crime, and the national laws that implement these obligations is, in part, a regime for the investigation of ML and international cooperation in this regard; with the ultimate goal of more effective AMLC and pursuit of funds to be used for, or proceeds of, crime. The introduction to the current 2012 version of the FATF recommendations makes it clear that one of the purposes is to "establish powers and responsibilities for the competent authorities (for example, investigative, law enforcement and supervisory authorities)."

ML and related offences often involve a transnational element and, in such cases, investigators and prosecutors may need to obtain information or evidence from outside their

jurisdiction. From law enforcement perspective information or evidence gathering has many attractions, as it allows law enforcement to repress or prevent the activities of those who provide laundering services or activities. It can also lead back to the criminals who organise and commit the predicate offence. In addition, findings from such investigations can be used as a surrogate charge for the predicate offence when the predicate offence cannot be proved or as one of multiple charges.[695] It also allows states to establish jurisdiction over ML within their territories in situations where they do not have jurisdiction over predicate offences that take place outside their territories. For all these reasons, it is particularly useful to have international cooperation between states in the fight against ML.

In criminal matters, there is no universal instrument or treaty, which governs the gathering of evidence abroad. However, the framework for formal requests is the conventions, schemes, and treaties that states have signed and ratified. For example, in an anti-corruption related aspect of ML investigation, the UNCAC[696] and the OECD Convention[697] each make specific provision for mutual legal assistance and the encouragement of international cooperation.

At a regional level, the EU has built on pioneering early steps in regional legal cooperation[698]with the 2000 EU Convention on Mutual Legal Assistance in Criminal Matters[699] and the 2008 European Evidence Warrant (a warrant for objects, documents, and data enforceable in other EU member states without further formality)[700]as examples. The EU has also proposed a European Investigation Order (EIO) (which provides for enforcement of

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695 N. Abrams, 'The New Ancillary Offences' *Criminal Law Forum* (1989) at 1and 2 cited in N. Boister, *An Introduction to Transnational Criminal Law* (Great Claredon Street, OUP 2012). p.100.

696 Article 41 of UNCAC.

697 Article 9.

698 Early steps included the Benelux Treaty on Extradition and Mutual Assistance in Criminal Matters of 27 June 1962 and the Schengen Agreement of 14 June 1985.

699 12 July 2000, OJC 197/3. It was followed by a Protocol on 21 November 2001, OJ C326.

700 Council Framework Decision 2008/978/JHA of 18 December 2008 on the European evidence warrant for the purpose of obtaining objects, documents, and data for use in proceedings in criminal matters, [2008] OJL 350.

investigative measures specified by the issuing EU member),[701]which would replace the existing legal framework applicable to the gathering and transfer of evidence between states. Various other regional treaties have been adopted, including the 1992 Inter-America Convention on Mutual Assistance in Criminal Matters[702]and the 2004 ASEAN Treaty on Mutual Assistance in Criminal Matters.[703]

At a bilateral level the United State has taken the lead in the development of bilateral Mutual Legal Assistance Treaties (MLATs), usually with states hesitant to give such cooperation. The MLAT between the United States and Switzerland signed on 25 May 1973[704] broke new grounds in legal assistance relation between common law and civil law states. It was followed by a proliferation of MLATs with strategic transnational crime suppression partners. The Mutual Legal Assistance Cooperation Treaty between the United States and Mexico, signed on 9 December 1987,[705] is just one of many relationships and they permit states to choose their treaty partners, thus avoiding obligations to provide information to unfriendly or untrustworthy states. The UN Model Treaty on Mutual Assistance in Criminal Matters 1990[706] is an attempt to standardise provisions in bilateral treaties. In the absence of such treaties, the US has been forced to conclude case-specific mutual legal assistance agreements (MLAAs).[707] Individual states are, therefore, free to develop MLATs on a bilateral basis. This is done to enable the provision of assistance between states of a different legal tradition. Here two states formally agree to MLAT, which enables them to extradite criminals or those

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701 [2010] OJ C 165/22.

702 23 May 1992, OASTS no 75, in force 14 April 1996 cited in N. Boister ft 635 p. 198.

703 29 November 2004, available at ASEAN Secretariat available at ≤www.aseansec.org/17363.pdf≥ cited in Boister ft 635 p. 198.

704 Treaty Between the United States of America and the Swiss Confederation on Mutual Assistance in Criminal Matters, 25 May 1973, 27 UST 209, TIAS 8302, in force 23 January 1977.

705 27 ILM (1998) 445.

706 Annexed to GA Res 45/117 (1990), 14 December 1990, as amended by GA Res 53/112 (1999), 9 December 1998.

707 See the OECD, *Mid Term Study of Phase 2 Reports: Application of the Convention on Combating Bribery of Foreign Officials in International Business Transactions and the 1997 Recommendations on Combating Bribery in International Business Transactions* (Paris: OECD, 2006), para. 401.

suspected of crime and/or to help in the investigation or prosecution of crime or the confiscation of the proceeds of crime. The bilateral treaty permits them to set out precisely the circumstances in which assistance will be granted.

In addition, there are varying kinds of multilateral treaties relating to mutual legal assistance (or extradition). Although multilateral extradition and mutual assistance treaties have the same general benefits as bilateral treaties, the obligations they contain are generally the subject of more exceptions than would be the case in bilateral treaty. The reason for this is that the treaty needs to reflect the negotiating position of a large (or relatively large) number of parties, each of whom must have included in the document the position it is prepared to adopt in respect of the state to whom it is prepared to grant the least benefit.[708] Perhaps the most influential instrument in the development of mutual legal assistance was the Vienna Convention 1988. This enables State Parties to seek and provide a broad range of assistance in evidence gathering in cases involving drug trafficking aspect of ML.[709]

More recent multilateral treaties places parties under a general duty to provide legal assistance in regard to the convention's crime, much as in bilateral and regional MLATs. For example, by article 46(1) of the UNCAC the parties promise to "afford one another the widest measures of mutual legal assistance".[710] However, the mere existence of such general obligations does not imply a guarantee that all requests for assistance will be met. They are to be realised in accordance with the domestic law of the requested party, and if the conditions, procedures etc are not adhered to, they may be refused.[711]

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708 J. Hatchard *supra* note 320, at 10.

709 *Ibid*., at 11.

710 See also, for example, article 7(1) of the 1988 Vienna Convention; article 18(1) of the Palermo Convention.

711 *Certain Questions of Mutual Assistance in Criminal Matters (Djibouti v France)*, Judgment, ICJ Reports 2008, 177, para. 123.

6.3 Conditions for and Exception to Legal Assistance

Requests for legal assistance are usually subject to limited conditions and exceptions borrowed from the law of extradition. The repressive AML obligations have tried to limit these conditions and exceptions, as legal assistance is not as serious an inroad into human rights as extradition. Some exceptions common in extradition treaties, such as the nationality exception, are simply inappropriate to legal assistance. Repressive AML treaties have specifically removed some reasons for refusal, such as bank secrecy.[712] The precise conditions and exceptions involved concerning any particular cross-border crime will depend on the contents of the convention or MLAT on which the requesting party is relying. Invoking these conditions and exceptions is a matter for the requested party, acting in good faith. For example, in *Djibouti* v. *France*[713] the French decision not to grant assistance was made by an investigating magistrate on grounds of national security, which could not be challenged by Djibouti.

6.3.1 Condition of Double Criminality

Legal assistance, like extradition, usually requires double criminality (the requirement that the conduct be criminal in both requesting and requested states). However, this may not always be the case, as some states do not require double criminality, unless the other party insists on its inclusion in an MLAT.[714] The definition of 'offence' in section 2 Canada's Mutual Legal Assistance in Criminal Matters Acts 1985, for example, refers to the relevant treaty, which will either require double criminality or not. Article 11(3) of the Canada–US MLAT provides that "assistance shall be provided without regard to whether the conduct under investigation or prosecution in the Requesting State constitutes an offence or may be prosecuted by the Requested State". In effect, a Canadian judge can order the issue of an arrest warrant under

712 See for example, Article 7(5) of the 1988 Vienna Convention and Article 46(8) of the UNCAC.
713 *Supra* para. 146.
714 N. Boister *supra* note 695, p. 203.

section 12 or order evidence gathering under section 18 without considering double criminality. The reverse is the case in Thailand, where section 9(2) of the Act on Mutual Assistance in Criminal Matters[715]provides that, unless the specific MLAT provides otherwise, "the act which is the cause of the request must be an offence punishable under Thai laws".

Under regional MLATs, such as the 1959 European Convention, dual criminality is not generally required[716] except in regard to more serious inroads into personal liberty such as search and seizure of property.[717] However, article 18(9) of the Palermo Convention permits a party to decline assistance on the basis of dual criminality if it chooses to. The UNCAC is in similar terms but does provide in article 46(9) (b) that parties shall provide assistance of a non-coercive nature even in the absence of dual criminality. FATF Recommendation 37 provides that "[states] should render mutual legal assistance, notwithstanding the absence of dual criminality, if the assistance does not involve coercive actions."

Lastly, if double criminality is a requirement, the question becomes whether the formal legal elements or only the underlying conduct need to be the same in both parties. The trend is thought to be towards the latter. Article 25(5) of the European Cybercrime Convention, for example, provides that if parties require dual criminality, the sole condition shall be if the conduct underlying the offence is criminal in its laws.

6.3.2 Condition of Specialty

Application of the doctrine of specialty (strictly a limitation on, rather than a condition of, legal assistance) to requests for the provisions of documents means that documents can only legally be used for the request for which they are handed over. For example, article 42(1) of the 2005 Council of Europe Convention against Money Laundering permits the requested party to make

715 Act on Mutual Assistance in Criminal Matters, B.E. 2535 (1992).

716 Article 1(1) of the 1959 European Convention on Mutual Assistance available at ≤http://conventions.coe.int/Treaty/en/Treaties/html/030.htm≥ last visited on 9 October 2014.

717 Article 5 and 6.

the "execution of a request dependent on the condition that the information or evidence obtained will not, without its prior consent, be used or transmitted by the authorities of the requesting Party for investigations or proceedings other than those specified in the request." Specialty conditions of this kind can also be found in article 12(3) of the 2002 International Convention for the Suppression of the Financing of Terrorism (hereinafter STF Convention) and in article 18(19) of the Palermo Convention.

By obliging financial institutions to cooperate in the fight against ML, an enormous pool of financial intelligence is tapped. Mostly this intelligence ends up in databases controlled by FIUs.[718] One of the moot points of the law surrounding the fight against ML is whether this information should also be made available for other purposes than fighting ML. Even if one restricts the use of information to the fight against ML, the question may arise as to the scope of the ML offence (and in particular its predicate offences), especially in those states where the definition of ML in the preventive legislation differs from the criminal legislation.[719]

Apart from ML prosecution, the information supplied by financial institutions can also prove to be very useful in other prosecutions, notably those regarding the predicate offence. Perhaps even more important, however, is the question as to whether information supplied by financial institutions in the context of the prevention of ML can also be used for non-judicial, notably tax, purposes. If tax administrations are allowed to have access to the information databases held by FIUs, tax administrations can circumvent the legal impediments to accessing bank files and the legislation on the prevention may turn out to be a very powerful device for combating criminal tax evasion.

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718 The role of the FIUs in informal cooperation is considered below.

719 The point here is that the repressive and preventive definition of ML must coincide to enable states benefit from international cooperation and MLATs.

However, a specialty condition defines and at the same time limits the purposes for which information can be used, often the same as those for which the information was gathered.[720]

6.3.3 Exceptions to Legal Assistance

There are few exceptions to Legal Assistance when it relates to: political offence, fiscal offence, military law, sovereignty and security, human right, and other prohibition. As in extradition, there has been steady pressure to remove the application of the political offence exception to legal assistance in regional MLATs. The UN Model Treaty on Mutual Assistance retains the discretion of the requested party to refuse on political grounds.[721] Whilst older regional MLATs still permit parties to refuse a request where the party considers that it concerns a fiscal offence or an offence connected with a fiscal offence,[722]recent conventions like the repressive AML obligations provide that a request may not be refused on fiscal grounds.[723]

Some MLATs retain the exception that mutual assistance cannot be requested for military offences that are not crimes under general criminal law.[724] Following the position in most MLATs,[725] the repressive AML obligations commonly contain a provision entitling the requested party to refuse if it considers "the execution of the request is likely to prejudice its sovereignty, security, *order public* or other essential interests".[726] Moreover, some states possess much broader investigative powers than others do. As a result, article 46(21) (c) of the

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720 G. Stessens *supra* note 14, p. 194.

721 Article 4 (10) (b).

722 Article 2(a) of the 1959 European Convention on Mutual Assistance; removed by article 1 of the additional protocol to the European Convention on Mutual Assistance in Criminal Matters Strasbourg 17.111.1978.

723 See for example, article 18(22) of the Palermo Convention; article 46(22) of the UNCAC.

724 See for example, article 49(1) of the Treaty Between the United States of America and the Russian Federation on Mutual Legal Assistance in Criminal Matters, 17 June 1999, US Treaty Doc No 107-13 (2002), in force 31 January 2002.

725 See, for example, article 2(b) of the 1959 European Convention on Mutual Assistance. See also article 4(1) (a) of the UN Model Treaty and para 7 (2a) of the Commonwealth Scheme.

726 See, for example, article 18(21) (b) of the Palermo Convention; article 46(21) of the UNCAC.

UNCAC entitles the requested party to refuse: "(c) If the authorities of the requested State Party would be prohibited by its domestic law from carrying out the action requested with regard to any similar offence, had it been subject to investigation, prosecution or judicial proceedings under their own jurisdiction. . ."

In addition, states are reluctant to refuse requests for MLA on the grounds that such assistance may result in an unfair trial in the requesting state because of the need for comity on certain crimes and a reluctance to involve the courts in executive competency in foreign policy.[727] Interestingly, while non-discrimination clauses are found in some MLATs[728] they have been omitted as a ground for refusing legal assistance in most of the repressive AML obligations. Yet human rights obligations can be a valid ground for refusing legal assistance not necessarily contemplated in an MLAT.[729]

Finally, legal assistance is costly and complex, and states generally tends to restrict its application to serious offences, although in Europe and in relations between the United States and Canada, where the systems are more integrated, more trivial offences are subject to cooperation. While some regional treaties make legal assistance available for any offence,[730] the obligations to provide legal assistance in the foregoing multilateral treaties are limited to the particular crime in the treaties. The obligation may also be limited to serious offences within a convention rather than all offences, so as to avoid requests for assistance in regard to trivial offences.[731]

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727 *Thatcher* v. *Minister of Justice and Constitutional Development and others,* Decision of High Court (2005) 1All SA 373 (C).

728 Paragraph 7(2b) of the Commonwealth Scheme; article 4(1)(c) of the UN Model Treaty.

729 N. Boister *supra* note 695, p. 206.

730 Article 1(1) of the 1959 European Convention on Mutual Assistance in Criminal Matters.

731 See draft article 30 of the Revised Chairperson's Text for a Protocol on the illicit Trade in Tobacco Products FCTC/COP/INB-IT/3/3 cited in N. Boister *supra* note 695, p. 200 ft. 20.

6.4 Informal Cooperation and the Role of Financial Intelligent Units

Whereas international cooperation in criminal matters was traditionally the province of judicial authorities, new forms of mutual assistance have come to light, in particular mutual police assistance and mutual administrative assistance. Thus, a wide range of information or evidence can be readily obtained directly from another state without any need for a formal mutual legal assistance request. If the enquiry is a routine one and does not require the requested state to seek to use coercive powers, then it may be possible for the request to be made and complied with without a formal letter of request.[732]

Over the past years, specialised governmental agencies have been created as states developed systems to deal with the problem of ML and other financial crimes. These entities are commonly referred to as '*financial intelligence units'* or 'FIUs'. The FIUs play an important role in the fight against ML, and in order to fulfil their role, they mutually exchange information. The international cooperation between FIUs takes place almost completely outside the framework of traditional judicial cooperation in criminal matters and they offer law enforcement agencies around the world an important avenue for information exchange.

ML investigations conceivably touch a number of law enforcement agencies within a particular jurisdiction. This means that a completely effective, multi-disciplined approach for combating ML is often beyond the reach of any single law enforcement or prosecutorial authority, which accounts for the hybrid nature of the FIUs as seen in the types of FIUs below. Combating ML therefore requires the expertise of specialised law enforcement agencies. The setting up of specialised FIUs designed to receive and process financial information from financial institutions (and possibly other institutions) should be seen against the background of the larger phenomenon of an increasing proliferation of specialised law enforcement

732 J. Hatchard *supra* note 320 at 7.

agencies.[733] Some of the international instruments on repressive and preventive AMLC have alluded to the role of the FIUs,[734] but none has hinted on the nature of this body.

Since money may transfer hands in a matter of seconds or be relocated to the other side of the world at the speed of an electronic wire transfer, law enforcement and prosecutorial agencies that investigate financial crimes must be able to count on a virtually immediate exchange of information. This information exchange must also be at an early point after possible detection of a crime – the so–called 'pre-investigative' or intelligence stage. At the same time, the information on innocent individuals and businesses must at all-time be protected.[735]

Under the auspices of the Egmont Group[736] (a loosely organised group of national FIUs), a general definition of a financial intelligence unit was drawn up which was later also formally inserted into the CICAD Model Regulation[737] (formally Article 8 now Article 13). The following definition is intended to function as the lowest common denominator:

"A central, national agency responsible for receiving (and, as permitted, requesting), analysing and disseminating to the competent authorities, disclosures of financial information: (i) concerning suspected proceeds from crime, or (ii) required by national legislation or regulation, in order to counter Money laundering. . ."[738]

The above definition contains three basic functions that are attributable to almost any type of FIU. First is that any FIU has a 'repository function'; meaning that the unit is called upon to be a centralised point of information on ML. Not only does it receive disclosed

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733 G. Stessens *supra* note 14, p 183.

734 Article 7(1) (b) of the Palermo Convention, article 14(1)(b) of the UNCAC and Recommendation 2 and 29 of the FATF.

735 W. H. Muller *et al supra* note 333, p 85.

736 The Egmont Group is a group of national FIUs that meet regularly to discuss the problems of international co-operation. The group derives its name from the Brussels Egmont Palace, where its first meeting took place at the initiative of the Belgian and American FIUs. The Egmont Group has made substantial and very commendable efforts in the field of international co-operation between FIUs resulting amongst other things in a Model Memorandum of Understanding, which has now been adopted by national FIUs.

737 Inter-American Drug Abuse Control Commission.

738 Available at ≤www.egmontgroup.org/≥last visited 19 December 2020.

information on financial transactions, but it also yields at least a certain degree of control over what happens to that information. The second function is the 'analysis function'. In processing the information, it receives, the unit is said to normally provide added value to the information. Thus, value to information would of course be dependent on the source of the information, which would further tell on a possible onward judicial investigation. The last function is the 'clearing house' function; and this allows the unit to serve as a conduit for facilitating the exchange of information on unusual or suspicious financial transactions. The exchange relates to information in various forms (individual or general) and can take place with various partners: with domestic regulatory agencies, with domestic judicial authorities, or with foreign FIUs.[739]

An FIU is therefore a central office that obtains financial reports information, processes it in some way and then discloses it to an appropriate government authority in support of a national AML effort. FIUs have attracted increasing attention with their ever more important role in AML programs. They are able to provide a rapid exchange of information (between financial institutions and law enforcement/prosecutorial authorities, as well as between jurisdictions), while protecting the interests of the innocent individuals contained in their data.

Accordingly, states have chosen to set up a central reporting unit to receive all the reports made by financial institutions.[740] The choice of setting up a central FIU, rather than having the reports made to (local) law enforcement agencies, is grounded in various reasons.

First is the need to have specialised expertise pooled in one institution, which may not be present within all law enforcement agencies. Secondly, centralising all reports and their processing in one specialised unit allows the authorities to move quickly, which is apt for the purpose of reducing the period during which suspicious transaction can be kept. Thirdly, FIUs

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739 G. Stessens *supra* note 14, p.184.

740 In the United Kingdom, this is formally known as the '*National Criminal Intelligence Service'* (NCIS), now incorporated within the newly formed '*Serious Organised Crime Agency'* (SOCA). The '*Nigeria Financial Intelligence Unit'* (NFIU) is the Nigeria version of the FIU. However, the law enforcement aspect is run by the Economic and Financial Crime Commission (hereinafter EFCC).

have two economic functions. On the one hand, they allow a much more efficient collection and analysis of information (by matching the information with intelligence). On the other hand, the processing and analytical tasks of the FIUs are said to alleviate the work of the investigating police and judicial authorities who can then concentrate their attention on files which have already been scrutinised or even documented by an FIU official. Fourth, the establishment of an intermediary between financial institutions and law enforcement authorities is in many cases intended to foster a climate of trust between financial institutions and authorities, since those institutions do not have to report their suspicions directly to the police or judicial authorities. They can instead report to FIUs that will first analyse the institutions' reports, which may decrease significantly the risk that 'innocent' customers may face in the case of police or judicial investigation.

One unique feature about the FIU is that its scope in the investigation and use of information passed on to it is also governed by a 'specialty principle', which defines and limits the purposes for which information can be used. The purpose here is often the same as those for which the information was gathered. For example, a tax authority in another jurisdiction cannot use information gathered for a serious crime in any one jurisdiction, since that would be contrary to the purpose for which the information was obtained in the first place.

An interesting aspect of the FIU, as noted above, is that most of the agreements are entered via a Memorandum of Understanding (MOU) and this is general between the respective government agencies in the various states. However, an area of concern is the weight to be attached to the Memorandum of Understanding between the parties, given the fact that the exchange of information is done between government agencies. It may thus be concluded that, given the origin and nature of the agreement (MOU), parties may not have intended any form of binding legal obligation under international law, and this is the case where the 'specialty principle' applies.

Unless the domestic law of either the state providing the information or of the state receiving the information contains a requirement to the effect that exchange of information with foreign FIUs can take place only on the basis of a formal agreement, mutual assistance of this type can also take place in the absence of an agreement. Even in the absence of such a statutory requirement, many FIUs prefer to cooperate only on the basis of MOU.

When there is an MOU, the question may arise as to whether the restrictions it imposes on exchange of information between the FIUs concerned are in any way judicially enforceable. In practice, this problem will pose itself only if information that was exchanged is being introduced as evidence into criminal proceedings. The problem is rather novel and no case law on the topic is known. The apparent lack of case law is probably in great part due to the fact that these MOUs are usually not made public. Unlike treaties, MOUs are not concluded between states but between national government authorities, notably between FIUs. The FIU is therefore part of the informal law-making process to control the crime of ML.

6.4.1 FIU and Types

Two major influences are thought to shape the creation of the FIUs. First, is the need to implement AML measures alongside already existing law enforcement systems, and second is the need to provide a single office for centralising the receipt and assessment of financial information and sending the resulting disclosures to competent authorities.[741] FIUs can therefore be classified by their nature: administrative, Judicial, Law Enforcement and hybrid models.

741 *Supra* p. 184.

6.4.1.1 The Judicial FIU Model[742]

The Judicial Model is established within the judicial branch of government wherein 'disclosure' of suspicious financial activity is received by the investigative agencies of a state from its financial sector such that the judiciary powers can be brought into play, e.g., seizing funds, freezing accounts, conducting interrogations, detaining people, conducting searches, etc. This type of FIU is established within the judicial branch of the state and most frequently under the prosecutor's jurisdiction. Instances of such an arrangement are found in states with a continental law tradition, where the public prosecutors are part of the judicial system and have authority over the investigatory bodies, allowing the former to direct and supervise criminal investigation.

Under this arrangement, disclosures of suspicious financial activity are usually received by the prosecutor's office, which may open an investigation if suspicion is confirmed by the first inquiries carried out under its investigation. The Judiciary's power (for example, seizing funds, freezing accounts, conducting interrogations, detaining suspects, and conducting searches) can then be brought into play without delay. Judicial and Prosecutorial FIUs can work well in states where banking secrecy laws are so strong that a direct link with the judicial or prosecutorial authorities is needed to ensure the cooperation of financial institutions. It may be noted that the choice of the prosecutor's office as the location of an FIU does not exclude the possibility of establishing a police service with special responsibility for financial investigation. In addition, in many states, the independence of the judiciary inspires confidence in financial circles.[743]

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742 Example here includes the Cyprus Unit for Combating Money Laundering (MOKAS) and Luxembourg's, Cellule de Renseignement Financier (FIU-LUX).

743 P. Gleason and G. Gottselig *Financial Intelligence Units: An Overview,* IMF and World Bank Working Paper (Washington DC, International Monetary Fund, 2004), p.16 available at <www.imf.org> last visited on 20/12/2020.

The principal advantage of this type of arrangement is that disclosed information is passed from the financial sector directly to an agency located in the judiciary for analysis and processing.

6.4.1.2 The Law Enforcement Model[744]

The Law Enforcement Model of FIU implements AML measures alongside already existing law enforcement systems. This is done by supporting the efforts of multiple law enforcement or judicial authorities with concurrent or sometimes competing jurisdictional authority to investigate ML. Operationally, under this arrangement, the FIU will be close to other law-enforcement units, such as a financial crimes unit, and will benefit from their expertise and sources of information. In return, information received by the FIU can be assessed more easily by law-enforcement agencies and can be used in any investigation, thus increasing its usefulness.

In addition, a law-enforcement-type FIU will normally have the law-enforcement powers of the law-enforcement agency itself (with specific legislative authority being required), including the power to freeze transactions and seize assets (with the same degree of judicial supervision as applies to other law-enforcement powers of the state). This is likely to facilitate the timely exercise of law-enforcement powers when this is needed.

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744 Example here includes Gursney Financial Intelligence Service (FIS), Jersey, Jersey States of Jersey Police-Joint Financial Crimes Unit and the United Kingdom's Serious Organised Crime Agency (SOCA). Originally, National Criminal Intelligence Service (NCIS) was the UK's FIU but SOCA was established by the Serious Organised Crime and Police Act 2005 (SOCPA) as a result of a merger of NCIS with related agencies (the National Crime Squad) and department of the Home Office (those with responsibilities for organised immigration crime) and HM Customs and Exercise (those dealing with drug trafficking).

6.4.1.3 The Administrative Model[745]

The Administrative Model is a centralised, independent, administrative authority, which receives and processes information from the financial sector and transmits disclosures to judicial or law enforcement authorities for prosecution. It functions as a 'buffer' between the financial and the law enforcement communities. Administrative-type FIUs are usually part of the structure, or under the supervision of, an administration or an agency other than the law-enforcement or judicial authorities. They sometimes constitute a separate agency, placed under the substantive supervision of a ministry or administration ('autonomous' FIUs) or not placed under supervision ('independent' FIUs). The main rationale for such an arrangement is to establish a 'buffer' between the financial sector (and, more generally, entities and professionals subject to reporting obligations) and the law-enforcement authorities in charge of financial crime investigations and prosecutions.[746]

Often, financial institutions facing a problematic transaction or relationship do not have hard evidence of the fact that such a transaction involves criminal activity or that the customer involved is part of a criminal operation or organisation. They will therefore be reluctant to disclose it directly to a law-enforcement agency, out of a concern that their suspicion may become an accusation that could be based on a wrong interpretation of facts. The role of the FIU is then to substantiate the suspicion and send the case to the authorities in charge of criminal investigations and prosecutions only if the suspicion is substantiated.[747]

The actual administrative location of such FIUs varies: the most frequent arrangements are to establish the FIU in the ministry of finance, the central bank, or regulatory agency. A few have been established as separate structures, independent of any ministry, for example, the

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745 Example includes the Australian Transaction Report and Analysis Centre (AUSTRAC), the Financial Transactions and Reports Analysis Centre of Canada (FINTRAC) and the United States Financial Crimes Enforcement Network (FinCEN).

746 *Supra* note 743, p. 10.

747 *Ibid*.

Belgian Financial Intelligence Processing Unit (CTIF/CFI). In most cases, the decision to establish the FIU outside the law-enforcement system also leads to the decision that the FIU's powers will be limited to the receipt, analysis, and dissemination of suspicious transaction and other reports, and that they will be given investigative or prosecutorial powers. Administrative-type FIUs may or may not be responsible for issuing Anti-Money Laundering Regulations or for supervising compliance with relevant laws and regulations on the part of reporting institutions.[748]

6.4.1.4 Hybrid Type FIU

This last category of FIU encompasses FIUs that contain different combinations of the arrangements described previously. This hybrid type of arrangements is an attempt to obtain the advantages of all the elements put together. Some FIUs combine the features of administrative-type and law-enforcement type FIUs, while others combine the powers of the customs office with those of the police – for some states, this is the result of joining two agencies that had been involved in combating ML into one.[749]

It may be noted that in some FIUs listed as administrative-type, staff from various regulatory and law-enforcement agencies work in the FIU while continuing to exercise the powers of their agency of origin. Examples of 'hybrid', FIUs are the Denmark State Prosecutors for Serious Economic Crime/Money Laundering Secretariat and The National Authority for Investigation and Prosecution of Economic and Environmental Crime –The Money Laundering Unit.

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748 *Ibid.*
749 *Ibid.*

6.5 Administrative Character of the International Exchange of Information between FIUs

According to Stessens, administrative assistance can generally be defined as international assistance that takes place between administrative government authorities, that is, outside the judicial framework, with a view to the application of or compliance with specific administrative rules.[750] It differs from judicial assistance both in terms of authorities concerned and of objectives.

As far as the exchange of information between FIUs is concerned, however, two remarks need to be made on the administrative nature of this type of assistance. First, not all FIUs are administrative authorities. The discussion of the types of FIUs revealed that in some state police or even judicial authorities have been charged with collecting and analysing information transmitted by financial institutions. As far as judicial FIUs are concerned, these are excluded from the international exchange of information that takes place between FIUs, as they cannot guarantee the limited and confidential use of information unless there is a specific statutory provision, which allows them to retain confidential information received from foreign FIUs.[751]Police authorities – such as a constable under the UK SOCA[752]– do, however, take part in the international information exchange. However, this does not necessarily preclude this type of information exchange from being classified as administrative assistance, since police assistance can also be considered as a type of administrative assistance, that is, assistance between non-judicial government authorities.

A second remark pertains to the objectives of administrative assistance between national FIUs. As was already pointed out, this assistance serves a clearly repressive goal, given

750 G. Stessens *supra* note 14, p. 262.
751 *Ibid*.
752 SOCA Officers can be designated the powers of a constable, customs officer or immigration officer and/ or any combination of these three sets of power.

the important role that FIUs play in the domestic enforcement of AML laws: they mostly act as an intermediary between the financial institutions and judicial authorities. Even though most of the FIUs have no proper law enforcement tasks,[753] their mission is nevertheless clearly geared towards criminal law enforcement.

Thus, the exchange of information between FIUs can be best classified as mutual administrative assistance. In many cases, the authorities are not police services and even if police services are involved, the exchange of information takes place outside the mainstream of international police cooperation. Stessens has argued that, it would be impracticable and unwise to bring this type of *sui generis* cooperation under the heading of police or judicial cooperation.[754]

Many states have therefore opted to create an administrative FIU as an interface between financial institutions and criminal justice system (i.e., the police and judicial authorities). This choice is especially motivated by the need to create a climate of trust and imposition of a specialty principle, and the need to have a centralised reporting unit. In addition, administrative FIUs are very suitable for dealing with reports made by financial institutions, as they are flexible.

In the view of the undeniable law enforcement background of the exchange of information between FIUs, the question is whether this type of cooperation could not take place through the channel of police assistance, or even via judicial assistance. As far as judicial assistance is concerned, such a movement would be in keeping with the more general trend of blurring borders between the various types of FIUs so that judicial cooperation can nowadays

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753 Whilst all administrative FIUs enjoy a considerable degree of independence, some are attached to a supervisory authority and hence are not completely independent. The American Financial Crimes Enforcement Network (FinCEN), for example, is a part of the US Department of Treasury and regards itself as a law enforcement service.

754 G. Stessens *supra* note 14, p. 263.

also include cooperation with administrative authorities. Nevertheless, several arguments can be invoked against exercising such an option.

The stringent specialty principle to which some of the administrative FIUs are subjected makes it impossible for them to forward information to foreign judicial FIUs, as these would not be able to safeguard this specialty principle. Apart from this specific obstacle, the procedural context of judicial assistance differs from that of administrative assistance. Whereas the former is concerned with exchanging evidence in the context of a criminal investigation that is often already centred on identified suspects, administrative FIUs assistance consists mainly of exchanging of information on suspicious transactions. Although this type of information may obviously also contain information on individuals, these individuals will not (yet) have the status of suspects. In fact, a substantial part of the so-called suspicion transactions that are scrutinised by FIUs will eventually turn out not to be related to ML operations.

The administrative concept of a suspicious transaction, as operated by (administrative and police) FIUs is therefore wider than the judicial concept of a suspicious transaction. This, in turn, also has implications for international cooperation and some states even go as far as to require a *prima facie* case for the purpose of accommodating a request for judicial assistance.[755]It is obvious that such a requirement cannot possibly be met at the preliminary stage during which FIUs exchange information on suspicious transaction. Moreover, it will often not be possible to assess other requirements that are generally posed in the context of judicial cooperation, not would the above exceptions listed in the case of formal legal assistance be applicable in such preliminary stages of an investigation.

[755] For example, requests for cooperation that are intended merely to confirm ungrounded suspicions are not allowed.

Thus, it may in practice be impossible to ascertain whether condition of double criminality is met as it will not be clear from what type of predicate offence (if from an offence at all) the funds are derived.

6.6 Conclusion

Traditionally, international cooperation in a criminal matter is treaty-based and between judicial authorities, as the sole mode of gathering evidence abroad. However, the emergence of profit-oriented crimes (as separate from the suspect-oriented perspective to crime) has resulted in further law-making in the context of the international effort to repress and prevent ML. As the international cooperation develops further, we see that emergence of binding and non-binding co-operative techniques in this field is not disconnected from a surge or increase in new waves of crimes that are profit oriented.

As a matter of legal certainty, the effectiveness of preventive/repressive AMLC would in part depend on an effective international co-operation in criminal matters, whether binding or non-binding. This is because the attainment of the goals of a domestic criminal justice system would in part be contingent upon international co-operation. In the end, the result is an emergence of new co-operative techniques, separate from the traditional principles of international co-operation in criminal matters, which was suspect and generally treaty based.

CHAPTER SEVEN

Jurisdictional Role of the Money Laundering Law

7.1 Introduction

The international nature of ML requires an international response. International harmonisation efforts in respect of the obligations to repress and prevent ML were set out in chapters three and four. In addition to this harmonisation of substantive repressive and preventive AML measures, an effective fight against ML also requires that jurisdictional problems that are likely to arise in an international ML context be solved. Often it will be unclear which state has jurisdiction to investigate ML offences and to prosecute and try alleged money launderers to seize and order the confiscation of alleged proceeds from crime.

There are substantial jurisdictional problems, as a result of the international character of ML, part of which has to do with exercising jurisdictional competence with respect to the confiscation of the proceeds of crime, extradition, and even dealing with so-called tax haven, where secrecy and anonymity is commonplace. The problem of confiscation arises where a state has jurisdiction over a ML offence but not the predicate crime[756] that generated the crime in the first place. As a rule, the criminal law is generally territorial, therefore the question of whether a state has jurisdiction to provide for the confiscation of criminal proceeds, and to criminalise ML, corresponds to the question as to whether the courts of that state can issue confiscation orders and try alleged ML offence.

As Fisher noted, the process of extradition in the case of ML is somewhat anachronistic,[757] and in terms of jurisdiction, this presents various legal obstacles for states. The general rule in international law is that, because of sovereignty, states do not have a legal

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[756] See pp. 147–1449 for the concept of the predicate crime.

[757] K. R. Fisher ‘In Rem Alternative to Extradition for Money Laundering’ (2002-2003) 25 Loy. L.A Int’l & Comp. L. Rev at 409.

obligation to extradite criminals to another state.[758] The duty to surrender arises from extradition treaties or agreements.[759] A state can only extradite an individual to another state if it has an extradition treaty with that state, and in the absence of such an agreement, a state has no obligation to extradite an alleged money launderer. For example, one of Nigeria's wealthiest politicians, James Onanefe Ibori, was convicted and jailed for thirteen years by a London court for ML. This was following a successful extradition request made by the UK to Dubai, where he was living as a fugitive from Nigeria.[760] The process leading to his arrest, trial and conviction was made possible as a result of an existing extradition treaty between the UK and United Arab Emirate.[761]

There is also the problem of financial secrecy jurisdictions and offshore financial centres (OFCs), which emphasis the strength of the provisions in their banking laws guaranteeing anonymity of customers in order to reap the benefits through licensing fees. The laws in these jurisdictions establish a right to anonymity for foreign nationals or residents who keep their property within that state, a right directed at investigations conducted by other states. An unreported judgment of the High Court of Cook Islands' Civil Division[762] confirmed, that the purpose of the Cook Island's financial secrecy law was to make it as difficult as possible

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758 As O'Connell indicates, until the nineteenth century "surrender of fugitive was the exception rather than the rule, and a matter of grace rather than of obligation" – D. P. O'Connell, *International Law* cited in M. Radomyski 'What Problems has Money Laundering Posed for the Law Relating to Jurisdiction?' (2010) Cov. L.J at 3.

759 For example, the European Convention on Extradition 1957 (member states of the EU); Pact of the League of Arab States (Egypt, Iraq, Trans Jordan, Lebanon, Saudi Arabia, Syria, Yemen); the Benelux Extradition Convention (Belgium and Luxembourg, and Belgium and the Netherlands); The Commonwealth Scheme (the Commonwealth); Convention between the UK, Australia, New Zealand, South Africa, India, and Portugal, supplementary to the extradition treaty of October 17, 1892; Montevideo Convention on extradition (Argentina, Chile, Colombia, Dominican Republic, Ecuador, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, United States); The Nordic States Scheme (Denmark, Finland, Iceland, Norway, Sweden); the O.C.A.M Convention (twelve of the fourteen former French territories in Equatorial and West Africa). Such treaties may be bilateral or multilateral.

760 The Economic and Financial Crime Commission of Nigeria (hereinafter EFCC) estimates the funds taken by Mr Ibori at USD 290 million: leaked Wikileaks cables put the sum at between USD 3 and 4 billion –J. Hatchard *et al supra* note 693 p. 285.

761 Extradition Treaty between the United Kingdom of Great Britain and Northern Ireland and the United Arab Emirate on Extradition *Treaties Series No.6* (2008) available at ≤www.official-documents.gov.uk/document/cm73/7382/7382.pdf≥last visited on 9 October 2014.

762 Case No 208/94, 6 November 1995, Judgment on Appeal 20 December 1995 cited in N. Boister *supra* note 695, p. 187.

for creditors to exercise their rights. Financial institutions benefit from such arrangement because they sell secrecy to individuals who want to deposit, hold, transfer, and withdraw money without any official awareness of this movement either in that jurisdiction or in any other.[763] They use various products, including numbered bank accounts (originally accounts where the name of the beneficial owner was unknown to the bank but more recently where it is a closely guarded secret), and shell banks (banks that have no physical presence in the jurisdiction in which they operate).[764] Thus, the unusual nature of these arrangements, and skills required to use them to engage in ML, forces cross-border criminals to rely on financial professionals, which presents a problem to law enforcement agency.

Accordingly, ML criminalisation in national law will be of limited practical effect unless the state enacting the crime establishes an adequate criminal jurisdiction for the crime. Although this chapter underlines the central role that the principle of territorial jurisdiction plays in response to the crime of ML, "a rigid territorial allocation of jurisdictional competence creates an impunity umbrella for those who act from abroad to achieve their illegal domestic objectives".[765] The chapter is therefore concerned with the internationalisation of ML and the jurisdictional role of the obligations to criminalise. The chapter explore this development by looking at the relative importance of criminalisation as a treaty-based initiative and the subsequent development of the law as the legal basis for asserting extraterritorial jurisdiction. It argues that criminalisation has numerous implications, part of which is the need for states to assert extra-territorial jurisdiction in view of the territoriality of the criminal law and the cross-border nature of ML.

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763 R. Murphy, 'Out of Sight' (2011) 33(8) *London Review of Books* at 21 cited in Boister.

764 In this category are companies and trusts where no information is kept on the public registers and owners or beneficiaries are not identifiable.

765 R. A. Falk, 'International Jurisdiction: Horizontal and Vertical Conceptions of Legal Order' (1959) 32 *Temple Law Quarterly* at 295 and 303 in N. Boister *supra* note 695, p. 135.

This chapter will, therefore, examine the jurisdictional role of the ML law in light of the obligations to repress and prevent ML. This is done by looking at the extra-territorial application of the law in light of current international arrangements. The chapter will accordingly do two things. First, it examines the bases for asserting jurisdiction in international law; second, it will examine the jurisdictional role of the ML law and the subject of extra-territorial application of ML. In order to provide a clear answer to these questions, it is necessary to distinguish between various forms of jurisdiction in international law.

7.2 Jurisdiction and Competence in International Law

Jurisdiction is a form of legal power or competence. It is a competence to control and alter the legal relationships of those subject to that competence through the creation and application of legal norms.[766] States that have consented to the exercise of the so-called compulsory jurisdiction of the ICJ can have some of their legal relationships adjudicated upon by the Court since it has a competence to determine the rights and obligations of states that have consented to its jurisdiction.[767] At the heart of this concept therefore is the question of competence, because jurisdiction is identified as a type of competence in international law.

The starting point for understanding how jurisdictional competences are allocated between states over individuals is the decision of the Permanent Court of International Justice (hereinafter PCIJ) in 1927 concerning the collision of the French mail steamer, the *Lotus*, and the Turkish collier, the *Boz-Kourt.*[768] The *Lotus* Case*,* is said to have introduced a theory of jurisdiction based upon what Brierly described as a "highly contentious metaphysical proposition of the extreme positivist school, that law emanates from the free will of sovereign

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766 W. Hohfeld 'Some Fundamental Legal Conceptions as applied in Judicial Reasoning' in (1913-1914) 23 *Yale Law Journal* 16 at 49.

767 See Articles 36(1) and (2) of the Statute of the ICJ.

768 The *S S Lotus* case (1927) PCIJ Reports Series A No. 10.

independent States",[769] (which has also been referred to as a permissive system of allocation of jurisdictional powers.[770]). The following section from the Courts decision explains this point:

"International law governs relations between independent States. The rules of law binding upon States therefore emanate from their own free will as expressed in conventions or usages generally accepted as expressing principles of law and established in order to regulate the relations between these co-existing independent communities or with a view to the achievement of common ends. Restrictions upon the independence of States cannot therefore be presumed. Now, the first and foremost restriction imposed by international law upon a State is that– failing the existence of a permissive rule to the contrary– it may not exercise its power in any form in the territory of another State. In this sense jurisdiction is certainly territorial; it cannot be exercised by a State outside its territory except by virtue of a permissive rule derived from international custom or from a convention."

However, despite the above rule on jurisdictional competence in light of the *Lotus* case, the law relating to asserting jurisdiction appears to follow a different prohibitive approach, whereby states are prohibited from asserting jurisdiction unless they are permitted to do. The *Cutting* Case in 1887[771] clearly illustrates this point.

In this case, Augustus K Cutting, a US national, was arrested and imprisoned by a Mexican court for committing libel against a Mexican citizen. The libellous acts were committed in Texas, United States. T F Bayard, the Secretary of State for the United States Government, challenged the right of Mexico to assert jurisdiction and demanded the release of Cutting. Bayard claimed that ". . . the judicial tribunals of Mexico were not competent under

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769 J. L. Brierly *'The 'Lotus"* Case (1928) 44 *LQR* 154 at 155.

770 P. Capps *et al Asserting Jurisdiction: International and European Legal Perspectives* (Oregon US, Hart Publishing, 2003) p. xx.

771 Foreign Relations of the United States (1887-1888) 751-869 and (1888-1889) 1133-1134. See also J. B. Moore, *Digest of International Law* (Stevens, London, 1906-11) 225-42 (Cited in P Capps *et al* p. 8).

the rules of international law to try a citizen of the United States for an offense committed and consummated in his own country, merely because that person offended happened to be a Mexican".[772]

Mexico attempted to justify the right to assert jurisdiction on two grounds: first, that the assertion of jurisdiction by Mexico was in accordance with rules of international law and the 'positive legislation of various states'[773] and, secondly that it was for Mexican courts to decide the scope of Mexican legislation. Bayard rejected both of these grounds arguing initially that there was little evidence, which supported the Mexican claim that their assertion of jurisdiction was consistent with international law and states practice. Whilst states can prosecute their own citizens for acts committed extraterritorially, to extend its jurisdiction to acts committed by foreigners outside the territory would impair (a) the independence of states and (b) amicable relations between states. Secondly, he argued that if a Government could set up its own municipal law as the final test of its international rights and obligations, then the rules of international law would be but the shadow of a name and would afford no protection either to States or to individuals.

Whilst it is fairly clear what is meant by jurisdiction as a legal concept in international law, state practice highlights somewhat of an opposing approach in the area. Combining these positions, it was concluded that there was no principle of international law that justifies such a pretension, and that "any assertion of jurisdiction must rest (as an exception to the rules), either upon the general concurrence of nations or upon express conventions"."[774]

Perhaps a useful instrument in this regard is the work of *The Harvard Research Draft Convention.*[775] The *Harvard Research,* remains useful in highlighting the circumstances where

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772 *Ibid*., p. 752. This is stated to be an expression of the passive personality principle of jurisdiction.
773 *Ibid*., p. 753.
774 *Ibid*., p. 754.
775 Harvard Research on Jurisdiction of Crime: Draft Convention on Jurisdiction with Respect to Crime 29 Am J Int L Supp (1935) 435, at 484 [hereinafter, Harvard Research or the Harvard Draft Convention].

states may be justified in asserting jurisdiction; an approach that still require states to justify a link which is recognised by international law between itself and the subject over which it seeks to assert jurisdiction. Five heads of jurisdiction have been identified according to the *Draft Convention*.

The first*, territorial*, is accepted as of primary importance and of fundamental character. Territorial jurisdiction is the ground on which the vast majority of offences are prosecuted. All crimes alleged to have been committed within the geographical territory of a state can be heard before the municipal courts of the state in question. In the case *Compania Naviera Vascongado* v. *Cristina SS,*[776] Lord Macmillan stated that:

"It is an essential attribute of the sovereignty of this realm, as of all sovereign independent states, that it should possess jurisdiction over all persons and things within its territorial limits and in all causes civil and criminal arising within these limits".

The principle is applicable notwithstanding the fact that the defendants are foreign nationals. Thus, territorial jurisdiction extends not only to crimes committed wholly within the territory of the state, but also to cases in which only part of the offence occurred in the state. Where a crime is a continuing one insofar as the perpetrator of the criminal act extends to two or more states, all states involved may claim jurisdiction.[777]

The second, *nationality*, is thought to be universally accepted, though there are said to be striking differences in the extent to which it is used in different national systems. Thus, the nexus established between a state and its citizens by the concept of nationality is the basis for the exercise of jurisdiction, even when the nationals in question are outside the territory of the

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776 [1938] AC 485.

777 This is because the territoriality principle may be divided into two parts: State in which the acts taken to initiate or perpetuate the offence may claim jurisdiction on the *subjective territoriality principle'.* This is thought to be the normal meaning of the term 'territorial jurisdiction' States in which injury takes place may claim jurisdiction in accordance with the '*objective territorial principle'*. The objective territorial principle has been applied in a number of cases at the international, national and supranational levels. L. Templeman *Public International Law* (Old Bailey Press, 1997) pp. 89 -90.

state itself.[778] In such circumstances, jurisdiction is said to be founded on the nationality principle.

The nationality jurisdiction is a constitutional rule in many civil law states. They consider their nationals responsible to the state wherever they are because they benefit from its protection, owe it a duty of allegiance, and their actions may injure its reputation. Its importance is thought to be increased by the fact that civil law states generally refuse to extradite their nationals.[779] Civil law states usually make a condition of establishing nationality that the offence the national is accused of is also an offence in the domestic law of the territory where it occurs (dual criminality). Article 5 of the Netherlands Criminal Code provides for jurisdiction over Dutch nationals, for example, but only if the offence is also "punishable under the law of the State in which it has been committed".

States from all legal traditions have begun to increase their use of nationality jurisdiction in order to ensure that egregious transnational crimes, such as sex tourism, committed wholly outside their territories do not go unpunished. For example, Article 10 of Japan's Law for Punishing Acts Relating to Child Prostitution and Child Pornography and for Protecting Children[780] provides for extraterritorial jurisdiction over Japanese nationals who commit child sex offences. In *United States* v. *Clark,*[781] the United States Court of Appeals for the Ninth Circuit held that the nationality principle justified jurisdiction for offences under the Prosecutorial Remedies and Other Tools to End the Exploitation of Children Today Act 2003[782] for the offence of a United States national apprehended having sex with minors in Cambodia.

However, nationality is useful against a range of extraterritorial transnational crimes. Section 7A of the New Zealand Crimes Act 1961, for example, applies nationality to

778 *Ibid*., L. Templeman p. 90.
779 N. Boister *supra* note 695, p. 143.
780 Law No. 52 of 1999.
781 435 F 3d 1100 (9th Cir 2006); ILDC 897 (US 2007), 25 January 2006.
782 18 USC § 2423 (c).

extraterritorial terrorism; dealing in people under 18 for sexual exploitation, removal of body parts, or engagement in forced labour; participation in organised criminal groups; smuggling migrants; human trafficking; ML and corruption of officials.[783] The option to establish nationality jurisdiction is now common in the repressive AML conventions,[784] a few (mainly European) treaties make is obligatory.[785] Some states limit its use to serious offences only.[786]

The principal weakness of nationality as a basis for criminal jurisdiction is that there are no agreed rules for the award of nationality; international law only requires a genuine link between state and individual,[787] and states are free to adopt whatever conditions they choose. Usually, they award it to natural persons on the basis of birth, parentage, or naturalisation or some other criterion. Common law states tend to confer nationality on juristic persons such as companies on the basis of where they were incorporated, civil law states on where they are managed.[788] The presumption that nationals are familiar with their state's law serves as the rationale for the legality of nationality jurisdiction, but global mobility and multiple nationalities undermines this rationale.

A modern development of nationality jurisdiction that overcomes some of these problems is the permissive establishment of jurisdiction over habitual residents. This is especially useful in the case of the repressive AML conventions, since Article 15(2) of the Palermo Convention provides that parties may establish jurisdiction when: "(a) The offence is committed by a . . . stateless person who has his or her habitual residence in its territory". Somewhat more broadly, Article 4(2) (b) of the Vienna Convention 1988 also permits states to

783 N. Boister *supra* note 695, p. 144.
784 Article 15(2) (b) of the Palermo Convention and Article 42(2) (b) of the UNCAC.
785 See, for example, Article 13(1) (d) of the European Convention relating to Offences against Cultural Property, 23 June 1985, CETS 119; not in force cited in N. Boister *supra* note 695, p.144.
786 See, for example, Article 7 of the Criminal Law of the People Republic of China, which provides for a two-year penalty threshold for its use.
787 The *Nottebohm*, Second Phase, Judgment (1955) ICJ Report 4.
788 N. Boister *supra* note 695, p.144.

establish jurisdiction over habitual residents, but does not require they be stateless, which means that parties may establish jurisdiction on the basis over the nationals of other parties.

Thirdly, *protective,* is claimed by most states (and regarded with misgivings by a few) and is generally ranked as the basis of an auxiliary competence. This extensive principle of jurisdiction would permit jurisdiction to be exercised over foreign nationals whose conduct threatens the security of a state. This allows states to punish acts threatening to undermine national security such as plotting to overthrow the government, spying, forging currency and conspiracy to violate immigration regulation.[789]

Protective jurisdiction is broader in scope than objective territoriality in that it allows the establishment of jurisdiction over conduct that poses a potential threat,[790] broader than nationality in that it applies to nationals and foreigners, and broader than passive personality in that it covers a more diffuse range of threats. It has usually been limited, however, to crimes that occur outside of any state's territorial jurisdiction – on the high seas or in international airspace.

The offence must affect directly or indirectly on the state's interests. States are in the best position to assess their own interests and they have usually established protective jurisdiction to suppress threats to their security (although some states have expanded the scope of the principle beyond security to include economic interests). Not surprisingly, there has been a growing tendency to characterise a number of transnational crimes as threats to security, particularly when other principles of jurisdiction are not available. The United States took the lead in this regard in 1980, enacting the Marijuana on the High Seas Act,[791] which in section 955(a) prohibits "any person on board a vessel of the United States, or on board a vessel subject

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789 In the case *Attorney-General for Israel* v. *Eichmann* [1962] 36 ILR 5**,** the Israeli court applied the doctrine of protective jurisdiction in order to exercise jurisdiction over a Nazi war criminal. The linking Israel had the right to pursue since the connection between the state of Israel and the Jewish people needed no explanation.

790 *US* v. *Pizzarusso,* 338 F 2d 8 (2nd Cir 1968).

791 21 USC § 955 (a)–955 (d).

to the jurisdiction of the United States on the high seas" from possessing a controlled substance with intent to distribute it.

In *US* v. *Gonzales*[792] the United States Court of Appeals held that the United States had protective jurisdiction for a violation of the Act over a Honduran Vessel found 125 miles east of Florida, carrying 114 bales of marijuana, which United States officials had boarded with Honduran permission. According to the Court, the protective principle allowed the establishment of jurisdiction "over a person whose conduct outside the nation's territory threatens the nation's security or could potentially interfere with the operation of its governmental functions".[793]

The United States has not been alone in using protective jurisdiction. The German Bundesgerichtshof established jurisdiction over a Dutch cannabis dealer operating in Netherlands on the basis of the protective principle on the condition that a direct domestic link to Germany could be established.[794] The Court held that the dealer had violated German interests by having sold over many years a considerable amount of hashish to German nationals who had taken the drug to Germany to consumer or resell it.

The protective principle appears in many forms in more recent multilateral conventions. For example, Article 4(1) (b) (ii) of the Vienna Convention 1988 provides for a special form of protective jurisdiction over vessels on which drug trafficking offences have occurred and the party has been "authorised to take appropriate action pursuant of Article 17". An even more unusual form of protective jurisdiction is provided for by the 1985 European Convention on Offences Relating to Cultural Property, which obliges parties under Article 13(1) to establish their jurisdiction when "any offence relating to cultural property is committed outside its territory when it was directed against cultural property originally found within its territory".

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792 776 F 2d 931 (11th Cir 1985).
793 *Ibid*., 938.
794 Judgement of the Federal Supreme Court, 34 BGHSt 334 [1988], 339.

Here the party establishes it jurisdiction to property originally found within its cultural property. Article 5(1) (c) of the Hostage Taking Convention, somewhat more orthodoxy, obliges parties to establish jurisdiction over hostage-taking when the offence is "committed . . . (c) in order to compel that state to do or abstain from doing any act." The protective jurisdiction is triggered by the fact the state, and its interests, are actually the target of the hostage-taker's pressure.

The fourth, *Universal*, widely thought by no means universally accepted, as the basis of an auxiliary competence except for the offence of piracy[795] (and War crimes[796] and War-related crimes[797]), with respect to which it is the generally recognised principle of jurisdiction. The basis for jurisdiction in accordance with the universality principle is that the state exercising jurisdiction has custody of a person accused of perpetrating an offence recognised by international law as an international crime.

In some repressive AML conventions, however, the provision to establish jurisdiction is still only permissive. Thus, while Article 4(2) (a) of the Vienna Convention 1988 obliges parties to establish jurisdiction when the alleged offender is present and the party does not extradite the alleged offender because that party has territorial or nationality jurisdiction, Article 4(2) (b) provides that a party *may* establish jurisdiction when the party's failure to extradite is on some other ground. In the former case, the party has a strong jurisdictional connection and thus must establish jurisdiction; in the latter, it may not have such a strong jurisdictional connection, so the provision is permissive. The state in question may have

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795 This was recognised as an international crime under customary international law and was codified in Article 14 to 17 of the *Geneva Convention on the High Seas* 1958 and Article 101 to 107 of the *Convention on the Law of the Sea* 1982. A state, which has apprehended an alleged pirate may try that person for that offence regardless of nationality and even if the activities of the pirate, have had no adverse effect on the shipping of the state in question.

796 Example of this is the judgement of the Nuremberg Tribunal.

797 For example the four Geneva 'Red Cross' Conventions of 1949 containing provisions for the universal jurisdiction over the grave breaches available at ≤www.icrc.org/eng/war-and-law/treaties-customary-law/geneva-conventions/overview-geneva-conventions.htm≥last visited 20 December 2020.

entirely valid grounds for refusing extradition or taking jurisdiction. These may include insufficiency of evidence, the previous conviction or acquittal of the alleged offender.

Lastly, is the *passive personality*, (asserted in some form by a considerable number of States and contested by others) which is admittedly auxiliary in character and is probably not essential for any State if the ends served are adequately provided for on other principles.[798] The principal grants jurisdiction to a state to punish alleged offences committed abroad against nationals of that state. An illustration of an exercise of jurisdiction on this basis was the request by the United States to Italy for the extradition of Palestinian nationals responsible for the murder of an American national aboard the Italian cruise ship, the Achille Lauro in 1985.[799]

The passive personality principle was included as an optional provision in the UNCAC and Palermo Convention, where its use is not as easily justified.[800] It is not immediately apparent why organised criminals would commit a crime against someone because of their nationality; Boister is of the opinion that perhaps an attack on a foreign judicial or law enforcement official may be what the authors of the Palermo Convention had in mind.[801]

7.3 Criminalisation and Extraterritorial Application of the Law

The crime of ML presupposes the occurrence of a 'predicate offence', whose proceeds are being laundered. This is only logical since ML is a separate offence from the predicate offence, and consequently independently gives rise to separate *jurisdictional* claim. The Vienna Convention 1988, whilst imposing a duty on the parties to criminalise the laundering of the proceeds of drug-related offences is, however, silent on the question of the location of the predicate offence. According to the commentary, "it would accord with recent practice if

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798 Dickinson's Commentary to *The Harvard Research Draft Convention on Jurisdiction with Respect to Crime* (1935) 29 *AJIL* at p 445 (Cited above in Patrick Capps *et al* 810).

799 Templeman *supra* note 777, p. 91.

800 Article 42(2) (a) of the UNCAC and Article 15(2) (a) of the Palermo Convention.

801 N. Boister *supra* note 695, p.145.

implementing legislation were to reflect the possibility that the predicate offence was located in a State other than the enacting one"[802] – the state enacting the ML offence.

Unlike the Vienna Convention 1988, the 1990 Money Laundering Convention established the extraterritorial application of the ML offence. After imposing the obligation on each Party to establish ML as a criminal offence, the 1990 Money Laundering Convention goes on to stipulate that: "it shall not matter whether the predicate offence was subject to the criminal jurisdiction of the Party".[803] Of similar effect is Article 6 of the Palermo Convention, which reinforced the approach in the 1990 Money Laundering Convention and extended the focus beyond targeting laundering of proceeds from drug-related activities to that of all serious offences. Under this convention, states were required to apply the offence of ML to broad range of predicate offences, including all serious offences as well as the offences of participating in an organised criminal group.[804] The ML offence can, therefore, fulfil its jurisdictional function only if it is not required that the state concerned should also have jurisdiction over the predicate offence. This is especially important in cases of states that – because of their limited geographical contour – are mostly confronted with proceeds from a foreign offence that, as such, have no connecting point with the state.

Thus, a ML offence that takes place purely on the territory of one state poses no problem of jurisdiction. However, since most ML operations at one point or another would generally entail a cross-border element, the question is likely to arise as to what degree a ML operation may have involved a violation of the legal order of a given state before the courts of that state can apply their criminal law. This relates, in general, to the question of applying the domestic AML legislation to the particular ML offence in question.

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802 UN, COMMENTARY ON THE UNITED NATIONS CONVENTION AGAINST ILLICIT TRAFFIC IN NARCOTIC DRUGS AND PSYCHOTROPIC SUBSTANCE 1988, (hereinafter referred to as COMMENTARY) p. 63. UN E/CN7/590 UN Sales No E98XI5, ISBN 92-1-148106-6 (1998).

803 Article 6(2) (a) of the Money Laundering Convention.

804 Article 5(1) of the Palermo Convention.

Two prevalent theories are relevant in this respect and are argued to be unique and appropriate in their specific mode of application – *ubiquity theory* and the *effects doctrine*. While the former is a prevalent international law theory and applies in a continental law system, the latter is stated to have been developed in the context of American competition law and is widely accepted in the United States and has since been the subject of fierce criticism in Europe.

7.3.1 Ubiquity Theory

Under this theory, an offence is deemed to have taken place on the territory of a state as soon as a constituent or essential element of this offence has taken place on that territory.[805] The pressure of a mobile social and economic reality is evident in the now classic definition of the territoriality principle in criminal law. According to Article 3 of the *Harvard Draft Convention* on Jurisdiction with Respect to Crime, "A State has jurisdiction with respect to any crime committed within its territory".[806] A crime is committed in whole within a state's territory when all its constituent parts (the conduct and the criminal result) have taken place within that territory.

Some crimes, however, start within the territory of a state but are committed outside that territory. Alternatively, a crime could start outside the territory of a state but produce its criminal result within the territory of the state. The latter two cases fall within the jurisdiction of the state based on the territoriality principle as crime committed in part within its territory. Traditionally, English courts are said to have claimed jurisdiction on the basis of the so-called 'last act' rule, according to which English courts had jurisdiction if the last relevant act took place in the UK.[807] However, this has often resulted in an unsatisfactory situation in which the

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805 G. Stessens *supra* note 14, p. 218; see also the *Lotus Case* –This is generally referred to as the 'territoriality principle'.

806 Harvard Draft Convention – cited in H. Shams *supra* note 39, p. 121.

807 *Supra* p. 219.

English courts had to decline to accept jurisdiction. In order to solve this problem, the Criminal Justice Act (CJA) 1993 introduced a new rule under which English courts can try an offence as soon as a relevant act that is any act or omission or other event[808] has taken place on the territory of the United Kingdom. Even the American concept of the *subjective territoriality principle*, which gives a state jurisdiction over offences that were initiated on its territory, but which were completed or consummated on the territory of another state,[809] can sometimes be categorised under the heading of the ubiquity doctrine, in that the preparatory acts concerned constitute constituent elements of the crime.

Given the broad scope of most ML criminalisation,[810] many acts can give rise to criminal liability. Whenever one transaction takes place on the territory of a state, even if the broader ML scheme is located abroad, that state will be able to assume jurisdiction. The combination of the very broad character of criminalisation ML and the *ubiquity doctrine* is therefore likely to result in a multiplication of jurisdictional claims over the same ML scheme. Apart from this jurisdictional effect of the ML offence, some applications of the ubiquity theory may also result in far-reaching jurisdictional claims. For example, it may suffice for a single accomplice to commit a ML act on the territory of a state in order for that state to be able to claim jurisdiction over all other acts of ML committed abroad– not only by that person but also by all other persons involved in the same offence. Similarly, courts have accepted extraterritorial jurisdiction over other offences by the mere connection of the offence, with the offence with which it had jurisdiction – either invoking unity of procedure because of the close connection among the offences.

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808 Section 2(1) CJA 1993 "any act or omission or other event (including any result of one or more acts or omission) proof of which is required of the offence".

809 *Supra* (Harvard Research in International Law, 'Jurisdiction with Respect to Crime', 484-7).

810 Article 3(1) of the Vienna Convention1988 calls on states to incriminate three types of money laundering activities. The section goes on to give a very broad definition of what amounts to the offence of 'Money Laundering' both international and locally.

The French Supreme Court, on this note, have accepted jurisdiction over the offence of handling stolen goods on the grounds that the offence was connected with a swindling offence that had taken place in France.[811] The only problem being that while the case is said to have been justified by the facts, it might generally have a far-reaching effect. This is because it could allow a state on whose territory the predicate offence took place to claim jurisdiction over any subsequent ML transaction carried out abroad by invoking such a connection.

Although application of the ubiquity doctrine appears to have its origin in unilateral state practice and not in an express treaty obligation, the doctrine is nevertheless relevant for the purpose of establishing jurisdiction in the case of ML.

7.3.2 Effects Doctrine

Expanding on ubiquity doctrine, certain states establish jurisdiction when no element of the offence occurs within the territory, but where a significant harmful consequence of the offence is felt within the state's territory (or on one of its vessels).[812] Originating in the establishment of US jurisdiction over transnational anti-trust violations (agreements between non-US companies operating outside the US to fix prices, etc) on the basis of adverse territorial effects in the US,[813] it has been adopted by US criminal law. For example, in the *United States* v. *Neil*[814] the US Court of Appeals established jurisdiction on the basis of the 'effects doctrine' over the sexual violation of a 12-years-old US minor on board a non-American vessel in the territorial waters of another state. The basis for asserting jurisdiction is simply because the cruise began and ended in the US and the victim had sought counselling in the US.

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811 G. Stessens *supra* note 14, p. 220. (French Court of Cassation, judgement of 9 December 1933, *Gazette du palais (*1934 79).

812 Article 6(1) (a) of the Convention for the Suppression of Unlawful Acts Against the Safety of Maritime Navigation and the Protocol for the Suppression of Unlawful Acts Against the Safety of Fixed Platforms on the Continental Shelf (hereinafter SUA Convention).

813 C. Ryngaert, *Jurisdiction in International Law* (Oxford: OUP, 2008) p. 42.

814 312 F 3d 419 (9th Cir 2002); ILDC 1247 (US 2002), 10 September 2002.

While many states are comfortable with establishment of jurisdiction where a harmful consequence of the crime is actual felt in the territory of the state establishing jurisdiction, the less substantial this consequence the more likely other states are to object to it. This limits its scope as a legitimate interpretation of the obligations to establish territorial jurisdiction in the case of the obligations to repress ML. In particular, difficulties have arisen with the establishment of jurisdiction over inchoate conduct such as attempts and conspiracies that occur abroad and which are intended to be completed in the state establishing jurisdiction, but where no actual effects is felt. In the *United States* v. *Ricardo*[815] the US District Court determined it had jurisdiction over defendants charged with conspiracy to import marijuana, even though the conspiracy took place outside the US and was thwarted before any marijuana was imported. The court ruled that US drug conspiracy laws had exterritorial reach, *inter alia*, as long as the defendant intended to violate those laws and to have the effects occur within the US.[816]

Reliance on an expanded version of objective territoriality to establish jurisdiction over transnational criminal conspiracies that do not actually have a harmful impact in the establishing states territory has been subject to criticism because the jurisdictional hook – effect – is only potential.[817] Article 4(1) (b)(iii) of the Vienna Convention 1988 provides that each party may establish its jurisdiction over article 3(1)(c)(iv) offences – inchoate drug related laundering offences and complicity in those offences – if the offence "is committed outside its territory with a view to the commission, within its territory . . ." of the drug supply and ML offences in Article 3(1). Article 4(1)(b)(iii) is therefore permissive because of the difficulties

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815 619 F 2d 1124 (5th Cir 1980).

816 *Ibid.*, 1128-9.

817 C. L. Blakesly and O. Lagodny, 'Finding Harmony amidst Disagreement over Extradition, Jurisdiction, the Role of Human Rights, and Issues of Extraterritoriality under International Criminal Law' (1991) *Vanderbilt Journal of Transnational Law* at 1 and 53.

some parties will have with establishing jurisdiction when the conspiracy takes place abroad and is wholly frustrated before any negative effects occurs within the territory.

However, states practice shows an increasing using of jurisdictional competence in such case.[818] For example, in *Liangsiriprasert* v. *US* [819]a Thai national arrested in Hong Kong pending extradition to the US appealed to the Privy Council on the basis that the US did not have jurisdiction. He had allegedly entered a conspiracy in Thailand with an undercover US agent to import drugs into the US (Thailand did not extradite drug offenders to the US) he was arrested at the request of the US. He argued *inter alia* that Hong Kong law followed English law and did not apply to conspiracies entered into abroad where there was no impact in that territory, and he had not performed any act that had an impact in the US. Lord Griffiths reasoned that inchoate actions are criminal in England, so there were no reason why extraterritorial actions should be required to be inchoate. According to the law Lord, "unfortunately in this country crime has ceased to be largely local in origin. Crime is now established on an international scale and the common law must face this new reality".

The potential affront to the sovereignty of states where the conduct actually occurs may provide some break on the application of this potential 'effects doctrine', but not if the affronted state is a party to repressive AML conventions, where the permission to establish this jurisdiction is now common.[820]

7.4 Regulatory Extraterritoriality

The repressive and preventive AML control, apart from fulfilling an initial jurisdictional role through the criminalisation, also performs a rather regulatory function. This was achieved using two methods. One is by direct imposition of the regulatory requirements on institutions that are

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818 J. D. A. Blackmore, 'The Jurisdictional Problem of the Extraterritorial Conspiracy' (2006) 17 *Criminal Law Forum* at 71.

819 [1990] All ER 866.

820 Article 15(2) (c) of the Palermo Convention and Article 42(2)(c) of the UNCAC.

not subject to the regulatory jurisdiction of the State concerned; and the other is by exerting pressure on another State to implement AML regulatory requirements even though it does not perceive them to be in its best economic interest. The current FATF Forty Recommendations envisaged both methods.

Recommendation 18 provides that, "Financial institutions should be required to ensure that their foreign branches and majority own subsidiaries apply AML measures consistent with the home country requirements implementing the FATF Recommendation . . ." By imposing the above requirement on the financial institutions in states that apply the FATF Recommendations, the FATF is actually extending the scope of the Recommendations extra-territorially. It also provides in Recommendation 19 that financial institutions should be required to apply enhanced due diligence measures to business relationships and transactions with natural and legal persons, and financial institutions from states for which this is called for by the FATF. In view of the interdependence of financial markets, strict application of this Recommendations results in placing pressures on states to implement the Recommendations in order to maintain their access to the global financial market.

The United States serves as an illustrative example of the extraterritorial reach of AML regulations. The US Bank Secrecy Act applies equally to US banks and to foreign banks operating within the jurisdiction. US regulators, unless denied access by the host nation, will examine branches of US banks that are operating abroad.[821] US banks may be denied the authority to open a branch in a state that is uncooperative and does not have a satisfactory AML mechanism. The criminalisation of ML extends the regulatory framework further to cover financial institutions that are neither branches of US banks nor operating within the US. The US criminal jurisdiction extends to offences that are committed in whole or in part within its

[821] M. Morgan 'Money Laundering: The United States Law and its Global Influence' in J. Norton 'Studies in International Financial and Economic Law' (*London Centre for Commercial Law Studies*, 1996), at 41.

borders. Given the very fluid nature of the *actus reus* in ML, this territorial link to the US jurisdiction can be stretched very far. For example, if illicit money was wired through a US bank as part of a cross-border process of laundering, this transit will be sufficient to give the US criminal jurisdiction over the whole process of laundering. Any foreign bank involved in this process will be subjected to the criminal jurisdiction of the US.

The case of *Banque Leu* is an illustrative example of the extraterritorial reach of the US criminal law–and how it leads to the extension of its regulatory system extraterritorially.[822] *Banque Leu* was a Luxembourg bank that had no offices in the US. In 1993 it was said to have entered a guilty plea to ML in the US and agreed to forfeit USD 2.3 million to the US and USD 1 million to Luxembourg. The bank was charged with ML under US law because it accepted deposits of USD 2.3 million in the form of cashier checks drawn on banks operating in the US, which formed part of ML operation initiated in the US. The bank sent the checks to the US to clear them and on basis of this action fell under the country's criminal jurisdiction. This clearly demonstrates how the loose definition of the *actus reus* in ML can result in extending the territorial reach or jurisdiction of the state.

In addition to entering into a forfeiture agreement with the US Government the Luxembourg bank, in this case, submitted to a three-year US audit specifically for ML. It also agreed to produce an AML monograph that should be updated annually for two years. Such regulatory requirements were imposed as a form of sanction for criminal conduct on a bank that was not regulated by the United States; hence extending the US regulatory jurisdiction extraterritorially. While the extension of regulatory jurisdiction in the above case was temporary and specific, the extraterritoriality of the criminal law of ML had a more durable effect on the scope of AML regulations. Thus, foreign institutions and states wishing to avoid

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822 For a discussion of the case see K Munroe 'Surviving the Solution: The Extraterritorial Reach of the United States Anti-Money Laundering Laws', 14 Dick J Int'L (1996) 505-24 at 520. (Cited in H. Shams *supra* note 45, p. 127).

prosecution for criminal ML and its devastating effects must show a good institutional record of fighting against ML.

An example of regulatory extraterritoriality is the example of Standard Chartered Bank and the New York regulators. In 2012, Standard Chartered Bank PLC agreed to pay USD 340 million to a New York regulator to settles allegations that the bank broke US ML laws in handling transactions for Iranian customers. The sum is said to be the largest fine ever collected by a single US-regulator in a ML case. The bank was accused of scheming transactions totalling USD 250 billion for Iranian clients. The settlement led the New York regulator to call off a hearing on the allegation.[823]

7.5 Conclusion

As noted above there are substantial jurisdictional problems as a result of the international character of ML, part of which has to do with exercising jurisdictional competence with respect to the enforcement of cross-border laundering offence and regulation. Enacting domestic AML offence will, therefore, be of no consequence unless the authorities can establish adequate criminal and regulatory cross-border AML jurisdiction. Whilst the current international AMLC was driven by the understanding that only through criminal and regulatory harmonisation of domestic law can the legal and regulatory loopholes be closed against cross-border crime, this will have limited effect without the necessary jurisdictional competence.

One of the common attributes of the internationalisation of the offence of ML is that it extends the reach of the criminal law beyond the territorial boundaries of the state. The repressive and preventive AML arrangements provide vehicles for the reasonable extension of parties' jurisdiction through criminal and regulatory law. Thus, by adopting existing AML

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[823] A version of this article appeared August 15, 2012 on page A1 in the US edition of the Wall Street Journal, with headline: Bank Settles Iran Money Case available at <http://online.wsj.com/article/SB10000872396390444318104577589380427559426.html> visited 20 December 2020.

conventions, the parties make reciprocal grants of special competence on the jurisdictional principles listed in the conventions and in doing so waive their rights to object to the establishment of extraterritorial jurisdiction on the basis of these principles.

CONCLUSION

The complexities of contemporary international relations and the changing international landscape has generated arguments in favour of expansion of law-making processes. Indeed, as noted in chapter one, the High-Level Panel on Threats, Challenges and Change called for the development of international regimes and norms, and of new legal mechanisms where existing ones were deemed inadequate for responding to the threats to collective security that it had identified.[824] The inadequacy of international law in changing conditions is a perennial concern, as are claims for a dynamic international legal system commensurate to the demand upon it.[825]

The requirements of contemporary international law-making have involved diverse participations. In some instances, demand for international regulation has come from civil society that perceive its interests as in conflict with those of states, especially in contexts such as human rights, disarmament, and the environment. Non- state actors purport to speak on behalf of diverse interests.[826] In areas like ML, and indeed cross-border crime, national legal systems face obstacles in exercising effective jurisdiction over entities that operate across state borders while international law, based upon the regulation of state behaviour, is ill-equipped to respond to corporate behaviour, or that of other non-states actors.[827]

The role, for example, of customary international law in this area is problematic as such law is derived from existing state practice and reliance cannot be placed on it as a means of regulating the problem of ML. The other traditional method of creating binding international law historically has been by means of treaties. Although, as the introductory part of this thesis noted, there is scope for international treaties in this area and they have indeed been much used,

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824 *Supra* note 76, p. 16.
825 *Supra* note 67, p. 19.
826 *Ibid*., p. 20.
827 International does regulate individual behaviour in certain instances, as seen in the area of human right law, and indeed humanitarian law.

and because of the need for compromise to obtain agreement between states, such treaties tend to be vague in form and uneven in implementation.[828]

This is the case with the international response to ML, as the treaty obligations to criminalise ML, for example, define the offence broadly and allows for local variations in relation to the predicate crime. There is thus considerable variation in the way in which signatory states to these conventions have approached the definition of predicate offences when criminalising the offence of ML. This approach to criminalising the offence of ML has since been adopted by a range of states in their domestic legislation, such as Canada's Criminal Code and New Zealand' Crimes Acts; this is not to mention the approach under POCA 2002. A variation in this approach concerns the scope of the predicate offence, where some states have adopted a broader approach by defining predicate offences to include either all criminal offences or criminal offences punishable by a term of at least twelve months and/ or an unlimited fine, such as in Sweden's Penal Code and the UK's POCA, 2002. Others have defined predicate offences by setting out a list of relevant offences or by combining a list of specific offences with a more general definition of predicate offences punishable by a certain level of punishment. Examples here are in Greece's Law 2331/1995 'on the Prevention and Combating of the Legislation on Income from Criminal Activities' and in China's Penal Code.

In addition, a notable difference with the approach to the definition of the ML offence in the Palermo Convention and 1990 Money Laundering Convention is that ML is no longer limited to laundering drug proceeds and is now applicable to a broader range of predicate offences. This approach was also endorsed in the FATF 40 Recommendation 3, which requires states to criminalise ML on the basis of the Vienna Convention 1988 and the Palermo Convention. With respect to the financial sector, the Palermo Convention required states to institute a comprehensive domestic regulatory and supervisory regime for banks and non-bank

828 See chapter three for the role of soft law in the broad definition of ML.

financial institutions and, where appropriate, other bodies particularly susceptible to ML.[829] This is an obligation also emphasised by the various preventive AML instruments (FATF, Basel Principles 1988, Wolfberg Principles, and the EC ML Directives) and it is intended to deter ML by emphasising CDD, suspicious transaction reporting, and record-keeping obligations and related requirements.

Given the cross-border nature of the crime of ML, and the problem of the territoriality of the criminal law, the traditional approach to international law-making is limited and less effective as a method of creating an international response to the problem of ML. The consequence of the combination of a non-traditional subject matter with the limitations of traditional international law instruments has meant that lawmakers, seeking international solution to the problems of ML have had to innovate. This innovation has found three forms of expression in particular.

First, soft law plays an increasingly important role in this area –which refers to both formal and informal obligations. Traditionally, soft law obligation has left States a considerable degree of discretion as regards implementation. However, in the case of soft law concerned with ML the reverse has been the case. For example, informal soft law, in the area of preventive AMLC, (in relation to CDD requirements) is in fact often quite detailed and prescriptive. The advantage of soft law in this area for state is that, because it is non-binding and does not require a wide international consensus for its adoption, it has enabled a group of (largely) Western states in particular to promote what they regard as ‘best practice’ in the area as a ‘guide’ for other states to follow. The leading promulgator of such law is the FATF, set up under the auspices of the OECD. However, this is not the only promulgator of this category of soft law. Other (largely Western-led) international groups and institutions, such as the Wolfberg Group of global banks and the Basel Committee also publish international standards.

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829 Article 7(1) (a).

Secondly, states have chosen legalisation of the problem of ML through the adoption of treaty obligations (formal soft law) to legislate for new crimes and treaty obligations to provide for international cooperation in the control of ML. Commentators question why this choice was made, given the enormous cost to develop and maintain them, the length of time they take to bring into operation, and weakness and flexibility of their provisions.[830] The answer is complex. Hard law is credible but only if its obligations are clear and precise, and substantive power is delegated to a third party to supervise the system.[831] The architects of the repressive AML conventions, individuals with experience of different crimes – faced what they considered similar problems and they used familiar solutions: hard treaty obligations using a mixture of inflexible form of a treaty and flexible treaty provision. The main barrier to be overcome was harmonisation of national criminal law, and once this could be settled through a broad and all-inclusive definition, AML obligations via the various conventions was implemented.

Thirdly, states have become increasingly innovative in making such 'soft law' binding both on their fellow states and, in the guise of meeting their international commitments, on their citizens. An example is the role that the EU has played in this area. Thus, one of the principal purposes underlying the third EU ML Directive is to implement the then revised FATF Recommendations. At the national level, the UK itself also gives effect to international soft law, independently of its membership of the EU. For example, the JMLSG Guidance has been approved by HM Treasury as a result of which a court may have regard to it for the purpose of deciding whether an offence has been committed under sections 330 and 331 of the POCA, 2002. The guidance in turn refers, as evidence of 'best practice', to the recommendations issued by the FATF, the Basel Committee and the Wolberg Group of global banks.

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830 C. Jojarth, *Crime, War, and Global Trafficking: Designing International Cooperation* (Cambridge: CUP, 2009), xiii, 27.

831 K. W. Abbott and D. Snidal *supra* note 92, at 421.

It is therefore right to conclude that harmonisation and approximation of existing AML arrangements through soft law is a cornerstone of existing international efforts to control ML, which inevitably results in the process of domestic law convergence and international cooperation. Domestic laws look more alike and are able to work together without as much friction as they would have been if there was no unified response through soft law. Describing the Palermo Convention and its protocol to a United States Committee an official explained that:

"[T]his growing array of cooperative initiatives was designed to create a platform for law enforcement, customs, and judicial cooperation that would function irrespective of the particular predicate criminal activity to which such initiatives would be applied. Although some of them had arisen in response to a particular problem, such as international drug trafficking, tax evasion, or computer crime, in general the initiatives were designed for general application regardless of the problem they would address".[832]

Towards a Uniform Codification of Money Laundering Law

As noted in the body of this thesis large-scale ML schemes contain cross-border elements, which require cross-border international response to the problem. A number of initiatives have been established to address the problem at the international level. This includes a growing array of cooperative techniques designed to create a platform for harmonisation and approximation of domestic and international AML law. These techniques, aimed at creating an environment of consensus in international cooperation and law enforcement are intended to address the problem of ML, irrespective of the particular predicate criminal activity to which they may be applied.

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832 J. M. Winner, 'Cops Across Borders: The Evolution of Transatlantic Enforcement and Judicial Cooperation', paper presented at the Council on Foreign Relations, Roundtable on Old Rules New Threats, 1 September 2004, cited in P. Andreas and E. Nadelmann, *Policing the Globe: Criminalisation and Crime Control in International Relations* (Oxford: OUP, 2006), 174.

However, given the nature of the problem of ML and the intended legal response, the traditional approach to international law-making is limited and less effective as a means of creating the needed platform and atmosphere for effective law enforcement and international cooperation. The consequence of the combination of a non-traditional subject matter with the limitations of traditional international law instruments has meant that lawmakers, seeking international solution to the problems of ML, have had to innovate. This innovation has found expression in particular with soft law.

A range of opinion exists on the theoretical and practical desirability of soft law. Some authors have long rejected formal distinctions between international law and policy; others acknowledged that the contemporary international law-making process is complex and deeply layered that there is a 'brave new world of international law' where "transnational actors, sources of law, allocation of decision function and modes of regulation have all mutated into fascinating hybrid forms. International Law now comprises a complex blend of customary, positive, declarative and soft law".[833]

Adopting a mixed method approach and drawing on the work of existing literature, the thesis seeks to distinguish itself from others by assessing the role of soft law as a technique to repress and prevent ML. The thesis addresses two fundamental issues in the context of existing international and domestic response to the problem of ML that remain largely uncovered by the other literature: the nature of the treaty obligations to criminalise ML and the role of soft law as a technique to repress and prevent ML. The thesis concludes that, international legal harmonisation and approximation of domestic anti-money laundering law through soft law remains useful to addressing the problem of ML.

[833] H. Koh *supra* note 1.

Notwithstanding the forgoing, current international effort to combat ML is still fragmented –as evident in the enormous variety of law-making processes. Part of the problem is the divergent nature of domestic criminal legislation, which is reflected in the choice of predicate crime and a lack of procedural rule to identify and enforce the law at state level. To address the limit of current efforts, the thesis will propose a uniform codification of AML law directed by a more representative body or commission of experts offering means of restating, clarifying and revising the law authoritatively and systematically.

Proposed Hague Conference Type Work

The Hague Conference on Private International Law[834] is an inter-governmental organisation in its own right. It is not an agency of the UN or even the EU. Under Article 1 of the Hague Conference,[835] its purpose is to work towards the progressive unification of the rules of private international law on questions bordering on the jurisdiction, applicable law, recognition of foreign judgement and international cooperation. The Hague Conference currently has 78 member states plus the EU. It has 145 states connected to the Hague Conference's work and 68 non-members benefitting from its work. Therefore, the normative work of the Hague Conference provides legal certainty and predictability of the law.

In 2015 it developed the first soft law instrument in international commercial law titled 'Principles on Choice of Law in International Commercial Contract'.[836] This is the most comprehensive regime establishing the rules for effective choice of law in the commercial contract, which has since been endorsed by the United Nations Commission on International Trade Law (hereinafter UNCITRAL) in July 2015. Given the Hague Conference independence

834 Established as an intergovernmental organisation in 1893 for purpose of progressive unification of the rules of private international law and still the principal forum for this purpose. It remains very active in concluding treaties, many of which are widely ratified.

835 See d7d051ae-6dd1-4881-a3b5-f7dbcaad02ea.pdf (hcch.net) last visited on 16/11/2021.

836 See HCCH | Choice of Law in International Commercial Contracts Section last visited on 16/11/2021.

and expertise in normative work bordering on jurisdiction, applicable law, recognition of foreign judgement and international cooperation, the author is proposing the development of AML normative work by the Hague's Conference in the aforementioned areas.

Part of the proposed normative AML work by the Hague Conference should establish a comprehensive regime on jurisdiction in cases of cross-border law enforcement and applicable law because of the problem of the location of the predicate in establishing jurisdiction and applicable law in ML cases. This is important because, as noted in chapter 6 of this thesis, ML is a separate offence from the predicate offence, which consequently gives rise to a separate claim of jurisdiction.

In addition, normative work on international AML cooperation by the Hague Conference will also provide certainty on rules around the current work of FIUs on legal assistance in the absence of MLATs. This is important because, as noted in chapter 5 of the thesis, international cooperation is crucial for AMLC as the cross-border nature of the crime of ML allows the offender to place the assets beyond the jurisdiction of the state where the predicate offence was committed. Thus, the Hague Conference expertise in this area will provide certainty and predictability to the current work of FIUs in the absence of MLATs.

Lastly, Hague Conference expertise in the enforcement of a foreign judgment is also relevant to a future global AML strategy that will aid the confiscation of proceeds of crime and cross-border asset recovery. The law on asset recovery is generally territorial, and the expertise of the Hague Conference would provide invaluable contribution to creating international consensus in the area.

Since the Hague Conference does not deal with domestic substantive law, questions bordering on domestic AML law and typologies are beyond the scope of its operation. However, an endorsement by the UN and FATF will provide the needed legitimacy any work in the aforementioned areas.

Research Limitation

This research was conducted from a qualitative research tradition with an emphasis on understanding the global AML phenomenon and the resulting legal/regulatory landscape via soft law. The research is, therefore, limited in scope because it is mainly focused on the nature of the global AML law and not on any empirical case study of the impact of current AMLC.

The author would like to conduct further empirical research on the effectiveness of current AMLC and the risk associated with international trade-based financial services ML. Financing international commercial transaction by financial institutions is known as trade finance. Sellers of good usually aim to ensure that they receive payment for the goods they provided once the goods leave the warehouse. Similarly, it is the buyer's aim to ensure that the seller has provided the goods to the exact specifications stipulated in the contract, and to make sure that the seller has shipped the goods before payment is made. Thus, one possible option to facilitate trade finance is by means of Letters of Credit (L/C), which are issued by the bank of a buyer to the bank of the seller, guaranteeing payment for the goods or services once certain conditions have been met.[837]

The International Chamber of Commerce estimates that global trade finance transactions totalled $9.1 trillion in 2015 ($9 trillion in 2020)[838] and has noted that in the becoming party to an L/C, a bank reduces risk and increases liquidity for the counterparties by taking on a proportion of the risk itself.[839] It has, however, been observed that the current emphasis of AMLC focus on the flow of money within the financial system could lead to the

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837 M. Menz, 'Beyond placement, layering and integration –the perception of trade-based money laundering risk in UK financial services'22 (2019)4 *Journal of Money Laundering Control* at 615.

838 See 2020 ICC Global Survey on Trade Finance: Securing future growth - ICC - International Chamber of Commerce (iccwbo.org) [accessed 09 April 2021].

839 Ibid.

flow of funds within international trade to be overlooked.[840] This is because the current approach to trade-based ML in financial services is overly focused on existing placement, layering and integration stages of ML. Conducting empirical research in the operation of L/C in the financing of international trade and associated risks could form the basis of understanding the effectiveness of this method.

[840] M.R.J. Soudijn, 'A critical approach to trade-based money laundering'17(2014)2 *Journal of Money Laundering Control* pp.230-242.

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