

## THE ROLE OF MISINVOICING IN THE MONEY LAUNDERING CYCLE

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### ABSTRACT

Traditionally, the emphasis of trade-based money laundering policy development has been directed towards financial transactions where the origin of capital is illegal, neglecting private sector companies utilising trade to launder money. Thus, can commercial businesses which engage in trade misinvoicing through cross-border trade be prosecuted for money laundering? With limited understanding of the money laundering cycle in international trade, it will be difficult for prosecutors to bring money laundering charges against commercial businesses operating in this sector.

This paper looks at two cross-cutting themes: trade misinvoicing and trade-based money laundering. It argues that any motivation of trade misinvoicing that generates the proceeds of crime and eventually leads to the concealment or disguise of the true nature, source, location, disposition, movement or ownership rights with respect to property in contravention of the Palermo Convention are variants of money laundering. It finally determines that trade misinvoicing can be used for two purposes: firstly, to generate the proceeds of crime and, secondly, to launder money.

### 1 INTRODUCTION

According to an International Monetary Fund (IMF) study in 1998, about 2%–5% (US\$800 billion – US\$2 trillion) of global GDP is estimated to be laundered

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annually.<sup>1</sup> In 2009, the United Nations Office on Drugs and Crime (UNODC) also conducted a study which estimated that criminal proceeds amounted to 3.6% of global GDP, with 2.7% (or US\$1.6 trillion) being laundered. This finding falls within the widely quoted estimate by the IMF.<sup>2</sup>

As a global challenge, money laundering involves a complex series of transactions across several jurisdictions, making it extremely difficult to investigate and prosecute.<sup>3</sup> The Financial Action Task Force (FATF) identifies three main methods by which criminal organisations and terrorist financiers move money for the purpose of disguising its origins and integrating it into the formal economy.<sup>4</sup> They involve the use of the financial system; the physical movement of cash; and the movement of value through trade, otherwise known as trade-based money laundering (TBML).<sup>5</sup> Criminals use TBML to avoid the stricter anti-money laundering controls of financial institutions,<sup>6</sup> and it is here that the intersection scenario between TBML and trade misinvoicing (TMI) presents itself. By co-mingling the proceeds of crime with the proceeds of legitimate business, criminals can move large quantities of illicit money between countries, thereby disguising the ultimate source of the illicit money.<sup>7</sup> Global Financial Integrity (GFI) finds that more than 87% of illicit financial flows (IFFs) are accompanied by TMI<sup>8</sup> to move capital in or out of a country in order to evade taxes and customs duties, to avoid quotas, for smuggling, to launder money, or as a means of capital flight.<sup>9</sup> This paper will focus on the motivation to launder money through TMI, as understanding the linkages of TMI to TBML likely is the next frontier in international anti-money laundering enforcement.<sup>10</sup>

1 UNODC “Money-Laundering and Globalisation”, available at <https://www.unodc.org/unodc/en/money-laundering/globalization.html> (visited 15 May 2020).

2 FATF “What is Money Laundering?”, available at <https://www.fatf-gafi.org/faq/moneylaundering/> (visited 15 May 2020).

3 UNECA (2018) “A Study on the Global Governance Architecture for Combatting Illicit Financial Flows” at 15.

4 FATF (2006) “Trade-Based Money Laundering” paragraph 1.

5 FATF (2006) paragraph 1.

6 FAFT (2008) “Best Practices Paper on Trade Based Money Laundering” at 1.

7 GFI “Money Laundering”, available at <https://gointegrity.org/issue/money-laundering/> (visited 15 May 2020).

8 GFI (2017) “Illicit Financial Flows to and from Developing Countries: 2005-2014” *Global Financial Integrity* at vii.

9 De Boyrie M, Nelson J & Pak S (2007) “Capital Movement through Trade Misinvoicing: The Case of Africa” 14(4) *Journal of Financial Crime* 474-489 at 475.

10 Nicolaou-Manias K & Wu Y (2016) “Illicit Financial Flows: Estimating Trade Mispricing and Trade-Based Money Laundering for Five African Countries” *Global Economic Governance Discussion Series* at 56.

TBML and TMI have been the subject of extensive attention from high-level institutions and authors. However, despite the robust literature in both areas, very little work has been done on the interrelation between TBML and TMI. While TMI is motivated by a variety of reasons (including money laundering), it is difficult to analyse it without reference to TBML, because TMI utilises the TBML techniques of over-invoicing and under-invoicing to perpetuate illegal activity. There is a clear nexus between the two issues. Preventing the commercial misuse of trade through misinvoicing cannot be addressed without also confronting the criminal use of TMI for money laundering.

This paper contributes to the debate on the relationship between TMI and TBML by examining the use of misinvoicing in the money laundering cycle and by seeking to ascertain when the proceeds of crime is generated through misinvoicing during an illicit international trade transaction.

## 2 CONCEPTUAL CLARIFICATION

The literature on IFFs is riddled with so many terms that they sometimes create misconceptions. The most prominent terms regarding cross border trade include transfer pricing, TBML, TMI and tax evasion/avoidance. TBML and TMI have garnered global momentum of late, reflecting an increasing concern about the abuse of trade for illicit purposes. For whatever reason misinvoicing occurs, the economic development of the given country can be hindered severely. Of particular concern is that such misconduct not only reduces revenues, but also finances terrorism, facilitates the illicit drug trade and corruption, and fosters other illegal practices.<sup>11</sup>

### 2.1 Trade Misinvoicing

The Report of the High-Level Panel on Illicit Financial Flows defines TMI as:

the act of misrepresenting the price or quantity of imports or exports in order to hide or accumulate money in other jurisdictions, with the motive to evade taxes, avoid customs duties, and transfer a kickback or launder money.<sup>12</sup>

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11 Kravchenko A (2018). "Where and How to Dodge Taxes and Shift Money Abroad Using Trade Misinvoicing: A Beginner's Guide" *TIID Working Paper* No 01/18, ESCAP, at 7.

12 AU/ECA (2015) "Report of the High Level Panel on Illicit Financial Flows from Africa" *AU/ECA Conference of Ministers of Finance, Planning and Economic Development* at 10.

According to Baker *et al*, this is done by manipulating the customs invoices or other incoming customs documents, such as receipts, bills of lading, bills of sale, titles, and export certificates.<sup>13</sup>

TMI is associated closely with the study of IFFs, the fight against which has been included explicitly as part of the 2030 Development Agenda (target 16.4).<sup>14</sup> In its 2015 Report, GFI observes that IFFs originate from two sources: deliberate TMI; and leakages in the balance of payments (Hot Money Narrow).<sup>15</sup> These methods vary from country to country. For instance, TMI has been identified by GFI as the major channel for the transfer of illicit capital from China, India and South Africa, whereas the balance of payments (BOP) approach is the primary conduit for the unrecorded transfer of capital from oil exporters such as Kuwait, Nigeria, Qatar, Russia, Saudi Arabia, the United Arab Emirates and Venezuela.<sup>16</sup> In a trade transaction, every cross-border shipment of goods is recorded independently by the customs authority of both the exporting country and the importing country, hence any discrepancies between corresponding data entries may provide a direct indication of misreporting.<sup>17</sup> These discrepancies between the records of exporting countries and importing countries long have been noted by trade researchers and policymakers.<sup>18</sup> Ideally, when two countries engage in trade, the data reported by one country ought to be the same as that reported by the other country.<sup>19</sup> GFI now recognises that TMI is a form of TBML made possible by trading partners falsifying their own trade documents to manipulate the price, quantity or quality of goods or services, to allow criminals, corrupt government officials and commercial tax evaders to shift vast amounts of money across borders quickly, easily and nearly always undetected.<sup>20</sup>

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- 13 Baker R *et al* (2014) "Hiding in Plain Sight: Trade Misinvoicing and the Impact of Revenue Loss in Ghana, Kenya, Mozambique, Tanzania, and Uganda: 2002-2011" *Global Financial Integrity* at 4. See also Ekananda K (2018) "Misinvoicing Analysis in ASEAN-China Free Trade Agreement (ACFTA)" XXI(1) *European Research Studies Journal* 187-205 at 190; Razah W (no date) "Role of Customs in Identifying and Combating Trade Based Money Laundering in Guyana: Invoice Frauds or Mis-invoicing" *ACAMS* at 2.
- 14 Kravchenko (2018) at 1.
- 15 Kar D & Spanjers J (2015) "Illicit Financial Flows from Developing Countries: 2004-2013" *Global Financial Integrity* at vii.
- 16 Nicolaou-Manias & Wu (2016) at 20.
- 17 Nitsch V (2017) "Trade Misinvoicing in Developing Countries" *CGD Policy Paper* 103 paragraph 3.
- 18 Kravchenko (2018) at 1.
- 19 Qureshi A & Mahmood Z (2016) "The Magnitude of Trade Misinvoicing and Resulting Revenue Loss in Pakistan" 21 *Lahore Journal of Economics* 1-3 at 1.
- 20 GFI (2019a) "Illicit Financial Flows to and from 148 Developing Countries: 2006-2015" *Global Financial Integrity* at xi.

### 2.1.1 Motivations for Trade Misinvoicing

Importers and exporters engage in misinvoicing for several reasons other than money laundering. Boyce & Ndikumana submit that TMI is motivated by the desire to evade import restrictions or customs duties, and by the desire to evade controls on transferring foreign exchange out of the country.<sup>21</sup> Buehn & Eichler find robust evidence that TMI typically is grounded in financial incentives, with perpetrators seeking to benefit from a premium on the black market for foreign exchange or evading tariffs and taxes.<sup>22</sup> De Boyrie, Nelson & Pak also identify several reasons for TMI, which include evading customs duties and restrictions, avoiding payment of taxes and fees, bypassing quotas, smuggling, and laundering of illegally obtained money.<sup>23</sup> According to GFI, criminals also utilise TMI to launder the proceeds of crime or corruption.<sup>24</sup> Indeed, TMI is a very complex problem with a range of motivations.

**Figure 1: Typology of Commercially Driven IFFs through Trade Misinvoicing**

Flow	Manipulation	Illicit Motivation	IFF Type
Exports	Overpricing	<ul style="list-style-type: none"> <li>Exploit subsidy regime</li> <li>(Re)patriate undeclared capital</li> </ul>	<ul style="list-style-type: none"> <li>Tax abuse</li> <li>Market/regulatory abuse</li> </ul>
	Under-pricing	<ul style="list-style-type: none"> <li>Shift undeclared (licit) income/profit</li> <li>Shift criminal proceeds out</li> <li>Evade capital controls (including on profit repatriation)</li> </ul>	<ul style="list-style-type: none"> <li>Tax abuse</li> <li>Laundering proceeds of crime</li> <li>Market/regulatory abuse</li> </ul>
Imports	Overpricing	<ul style="list-style-type: none"> <li>Shift undeclared (licit) income/profit</li> <li>Shift criminal proceeds out</li> <li>Evade capital controls (including on profit repatriation)</li> </ul>	<ul style="list-style-type: none"> <li>Tax abuse</li> <li>Laundering proceeds of crime</li> <li>Market/regulatory abuse</li> </ul>
	Under-pricing	<ul style="list-style-type: none"> <li>Evade tariffs</li> <li>(Re)patriate undeclared capital</li> </ul>	<ul style="list-style-type: none"> <li>Tax abuse</li> <li>Market/regulatory abuse</li> </ul>

**Source:** Cobham (2014).

- 21 Boyce J and Ndikumana L (2000), "Is Africa a Net Creditor? New Estimates of Capital Flight from Severely Indebted Sub-Saharan African Countries, 1970-1996", *Economics Department Working Paper Series* 81 at 3.
- 22 Buehn A and Eichler S (2011) "Trade Misinvoicing: The Dark Side of World Trade", *The World Economy Blackwell Publishing Ltd* at 1263.
- 23 De Boyrie, Nelson & Pak (2007) at 475.
- 24 GFI "Trade Misinvoicing", available at <https://gfintegritty.org/issue/trade-misinvoicing/> (visited 15 May 2020).

Figure 1 above provides an overview of the transaction types and illicit motivations involved in TMI. The original table, developed by Alex Cobham and Alice Lépissie of the Center for Global Development, demonstrates the entire breadth of IFF phenomena; for purposes of this paper, it has been narrowed down to motivations for TMI which utilise TBML techniques. Clear clusters are captured, showing the main illicit motivations and the manipulative mechanisms employed.

While there are clear motivations for criminals to launder money through TBML techniques, companies involved in illicit transactions also are driven to launder money for financial gain. In this circumstance, the incentive drives the motivation.

### 2.1.2 Illegal Capital Misinvoicing

Misinvoicing of imports or exports may be divided into illegal capital and legal capital misinvoicing in the context of IFFs. It is internationally understood that illegal capital is illicit flows that are based on the theft of state assets and the proceeds of crime.<sup>25</sup> Theft of state assets entails direct theft by people in positions of power, while proceeds of crime may be derived from such activities as trafficking of drugs, people and illegal goods,<sup>26</sup> fraud in the financial sector, money laundering, stock market manipulation and outright forgery.<sup>27</sup> In the past, the focus was upon these avenues of illegal flows because of the threat terrorism posed after the World Trade Center attacks of September 2001.<sup>28</sup> However, since the 2008 financial crisis, greater prominence has been given to tax and market abuse.<sup>29</sup>

In essence, IFFs converge around the core concept of financial transfers across borders that are related in some way to illegal activity. Because a great number of countries try to process their customs transactions rapidly so that they can increase their economic growth and encourage international trade, it is also easy and low-risk for criminals to engage in TMI.<sup>30</sup>

25 Cobham A & Jansky P (2017a) "Measurement of Illicit Financial Flows" *UNODC-UNCTAD Expert Consultation on the SDG Indicator on Illicit Financial Flows* at 1.

26 Cobham A & Jansky P (2017b) "Illicit Financial Flows: An Overview" *International Group of Experts on Financing for Development* Geneva at 11.

27 AU/ECA (2015) at 31.

28 Cobham & Jansky (2017a) at 7.

29 Cobham A (2014) "Benefits and Costs of the IFF Targets for the Post-2015 Development Agenda" *Illicit Financial Flows Assessment Paper* at 4.

30 Herold Financial Dictionary "What is Trade Misinvoicing?", available at <https://www.financial-dictionary.info/terms/trade-misinvoicing/> (visited 15 May 2020).

### 2.1.3 Legal Capital Misinvoicing

As a rule, IFFs involve the transfer of money earned through various illicit activities. However, such flows may also involve funds that were earned through legitimate means.<sup>31</sup> It is in transferring legitimately earned funds in direct contravention of applicable capital controls that the transfer becomes an illicit flow, even though the funds were earned in a legitimate activity.<sup>32</sup> This is why GFI reminds us that:

Somewhere at its origin, movement, or use, the money broke laws and hence it is considered illicit.<sup>33</sup>

The AU/ECA HLP on IFFs, the World Bank, the IMF, the UN, and the OECD all have defined IFFs within their various contexts. However, the most widely accepted definition is that proposed by GFI, which describes IFFs as “money illegally earned, transferred or utilised”.<sup>34</sup> This description emphasises the illegality across all stages of IFFs, to confirm that a legal act in one geographical location does not nullify the intent and purpose of such outflows, which is to hide money even if it was earned legitimately.<sup>35</sup> A category of misinvoicing motivation is applicable here, especially as regards the commercial activities of private companies.

This aspect of TMI represents a potential brake upon economic growth and development, which accounts for persistent balance of payments deficits and erodes the domestic tax base, thereby affecting income redistribution in underdeveloped countries.<sup>36</sup> Several criminal offences may occur in the process of misinvoicing and the following sections look at how the offence of money laundering is introduced into the process.

## 2.2 Trade-Based Money Laundering

In its landmark TBML Report of 2006, the FATF defined TBML as:

the process of disguising the proceeds of crime and moving value through the use of trade transactions in an attempt to legitimise their illicit origin.<sup>37</sup>

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31 Kar D & Cartwright-Smith D (2009) “Illicit Financial Flows from Developing Countries 2002–2006” *Global Financial Integrity* at 1.

32 Kar & Cartwright-Smith (2009) at 1.

33 Kar D (2010) “Illicit Financial Flows from Developing Countries: The Absurdity of Traditional Methods of Estimation”, available at <https://gfintegrity.org/illicit-financial-flows-from-developing-countries-the-absurdity-of-traditional-methods-of-estimation/> (visited 15 May 2020).

34 GFI (2017) at 1.

35 AU/UNECA (2015) at 23.

36 De Boyrie, Nelson & Pak (2007) at 6.

37 FATF (2006) paragraph iii.

Initially, the 2006 Report excluded the movement of money for tax avoidance, tax evasion and capital flight on the grounds that such movement usually involved the transfer of legitimately earned funds across borders.<sup>38</sup> However, the follow-up Report in 2008 included terrorist financing (TF) within the definition and scope of TBML, on the understanding that licit and illicit funds could be intermingled, giving rise to capital flight and the movement of funds for tax avoidance and evasion purposes.<sup>39</sup> The 2008 Report defined TBML/TF as:

the process of disguising the proceeds of crime and moving value through the use of trade transactions in an attempt to legitimise their illegal origins or finance their activities.<sup>40</sup>

The complex nature of international trade meant that criminals can utilise TBML techniques easily to hide illicit wealth and avoid detection by the authorities.<sup>41</sup> The techniques of TBML traverse a wide range of options, from simple fraudulent invoicing to the sophisticated integration of trade in goods into complicated financial transactions that obscure the origin of funds.<sup>42</sup> They include:

- over- and under-invoicing of goods and services (trade misinvoicing);
- multiple invoicing of goods and services;
- over- and under-shipments of goods and services; and
- falsely described goods and services.

The most common method of laundering money through trade is misinvoicing. Money can be moved from one country to another by under-invoicing the exports or over-invoicing the imports. Similarly, money can be moved into a country from another country by over-invoicing the exports or under-invoicing the imports.

Transnational criminal organisations and terrorist organisations use a variety of money laundering schemes to disguise the origin and destination of their illicit proceeds and to integrate their criminal assets into legitimate financial entities.<sup>43</sup> Figure 2 below shows how the importer and exporter negotiate the terms of the transaction, and how their banks process payment for the transaction,

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38 APG (2012) “APG Typology Report on Trade Based Money Laundering” *Asia/Pacific Group on Money Laundering* at 9.

39 FATF (2008) “Best Practices Paper on Trade Based Money Laundering” at 1.

40 FATF (2008) at 1.

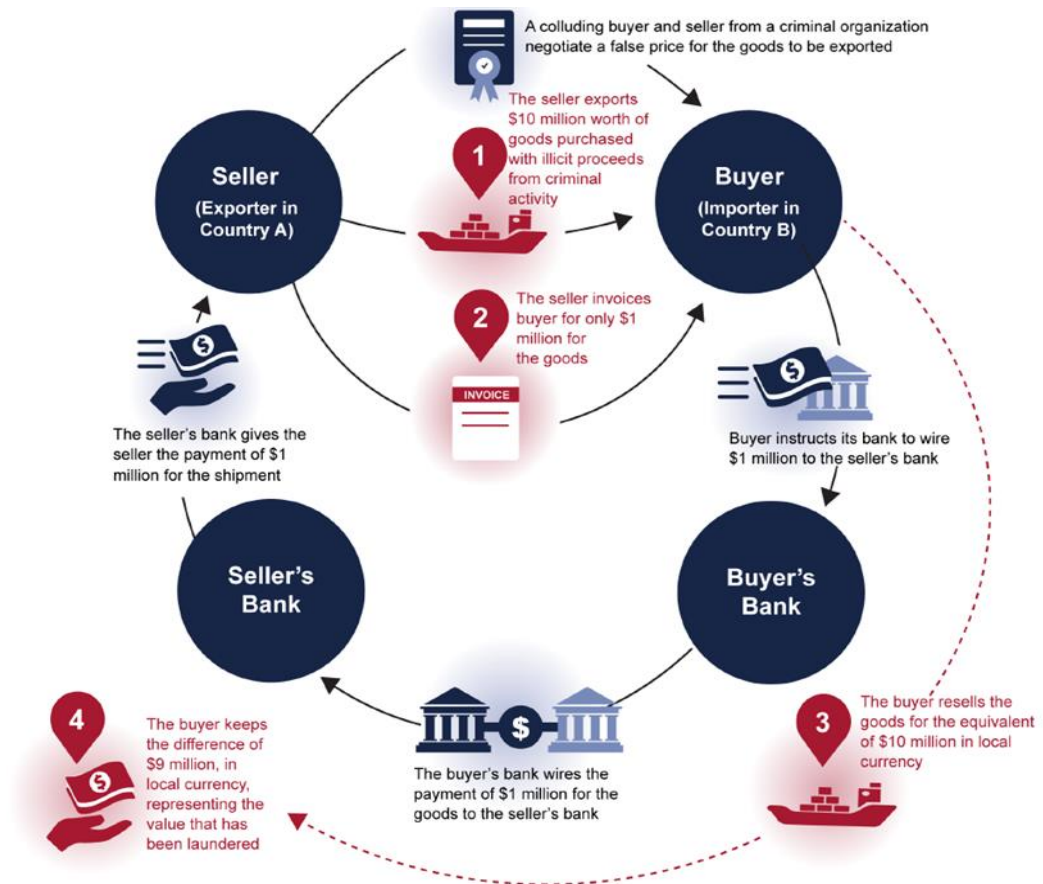
41 FATF (2006) at 2.

42 FATF (2006) at 25.

43 GAO (2020) “Trade-Based Money Laundering: US Government Has Worked with Partners to Combat the Threat, but Could Strengthen Its Efforts” *A Report to Congressional Requesters* GAO-20-333 at 4.



Figure 2: TBML through Open-Account Transactions



Source: United States Government Accountability Office (2019)

often without access to the invoices or documents underlying the transaction.<sup>44</sup> In international trade transactions, generally banks do not review customs documents such as invoices, bills of lading or customs declarations in open-account transactions and those financed by the bank.<sup>45</sup> Hence, money laundering risks through TMI expose the international trade sector to increased financial risk and criminality.

### 2.3 Role of Misinvoicing in the Money Laundering Cycle

Choi & McGauran see TMI as a broader concept than TBML. They suggest that TMI involves a case of illegal transfer of *legally earned profits*, which is the most

44 GAO (2019) "Countering Illicit Finance and Trade: U.S. Efforts to Combat Trade-Based Money Laundering" *Government Accountability Office* GAO-20-314R at 19.

45 GAO (2019) at 15.

representative case of IFFs via TMI.<sup>46</sup> This description is limited because it excludes the motivation to launder money through TMI (property derived from a criminal origin) and focuses only on legal profits that are transferred illegally. GFI gives a broader description and explains that:

trade misinvoicing can be related to, but does not precisely correspond to TBML rather, trade misinvoicing is a mechanism that can be used to engage in TBML.<sup>47</sup>

Thus, it may be deduced that the TMI motivation to launder money is in fact TBML. Like TMI, TBML may be carried out through misrepresentation of the price, quantity or quality of imports or exports through fictitious trade activities and/or through front companies. TBML and TMI coalesce when a criminal or company misrepresents the price on a customs invoice to hide or accumulate money in another jurisdiction. The question is whether money laundering is involved in all incidents of TMI? TMI has other motivations, such as evading tax and duties, avoiding quotas and market manipulation, which cover a spectrum of offences that can be linked to money laundering. Careful analysis and observation of the misinvoicing process suggest that all motivations of TMI that generate criminal proceeds which eventually are concealed or disguised involve money laundering.

### 2.3.1 Trade Misinvoicing and Proceeds of Crime

It is submitted that any motivation of TMI, such as capital flight and tax evasion, entails variants of money laundering, as long as the camouflaging of the nature of the transfer of funds across international borders pertains to the proceeds of crime.

According to both Article 3(1) of the United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances (Vienna Convention) and Article 6(1) of the United Nations Convention against Transnational Organised Crime (Palermo Convention), money laundering is to be criminalised by each state party. Money laundering involves the conversion and transfer of criminally derived property to disguise its illegal origin. In order to secure a conviction for money laundering, prosecutors must show that the accused engaged in a transaction or

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46 Choi Y & McGauran R (2018) "Conceptual Basis of Illicit Financial Flows, Trade Mis-invoicing and Trade Discrepancy" in *Illicit Financial Flows via Trade Mis-invoicing* Study Report: World Customs Organisation at 22.

47 GFI "Trade Misinvoicing" paragraph 3.

international transportation which involved property from a specified unlawful activity.<sup>48</sup> As the International Monetary Fund (IMF) rightly states:

money laundering requires an underlying, primary, profit-making crime (such as corruption, drug trafficking, market manipulation, fraud, tax evasion), along with the intent to conceal the proceeds of the crime or to further the criminal enterprise.<sup>49</sup>

To be sure, not all IFFs are derived from illegal sources or involve proceeds of corruption or other crime. However, with TMI (a component of IFFs), the criminally derived property is generated during the misinvoicing cycle.

The United Nations Convention against Corruption, as well as the United Nations Convention against Transnational Organised Crime, defines proceeds of crime as:

Any property derived from or obtained, directly or indirectly, through the commission of an offence.<sup>50</sup>

Directive 2014/42/EU of the European Parliament and Council of the EU defines proceeds as:

Any economic advantage derived directly or indirectly from a criminal offence; it may consist of any form of property and includes any subsequent reinvestment or transformation of direct proceeds and any valuable benefits.<sup>51</sup>

Offences such as drug smuggling, bribery and theft of state assets involve proceeds of crime *ab initio*. Intermingling such proceeds through trade by over- or under-invoicing of imports or exports would be considered as TBML and would provide a *prima facie* case for adding money laundering charges to a criminal prosecution. The problem is linking money laundering to motivations of TMI in which the source of funds is apparently legitimate. In other words, how may illicit TMI transactions involving funds not adjudged to be derived from proceeds of crime be understood as a form of TBML? Directive 2014/42/EU elaborates upon the concept of proceeds of crime in the following terms:

There is a need to clarify the existing concept of proceeds of crime to include the direct proceeds from criminal activity and all indirect benefits, including subsequent reinvestment or transformation of direct proceeds.

48 Bauer P & Ullmann R (2001) "Understanding the Wash Cycle" 6(2) *Electronic Journal of the US Department of State* 19-23 at 21.

49 IMF "Anti-Money Laundering/Combating the Financing of Terrorism (AML/CFT)", available at <https://www.imf.org/external/np/leg/amlcft/eng/> (visited 25 May 2020).

50 Article 2(e) of UNCAC and Article 2(e) of the Palermo Convention.

51 Article 2(1) of Directive 2014/42/EU.

Thus proceeds can include any property including that which has been transformed or converted, fully or in part, into other property, and that which has been intermingled with property acquired from legitimate sources, up to the assessed value of the intermingled proceeds. It can also include the income or other benefits derived from proceeds of crime, or from the property into or with which such proceeds have been transformed, converted or intermingled.<sup>52</sup>

For example, as an offence, bribery usually brings direct criminal proceeds, whereas the indirect proceeds of bribery typically may include services or advantages derived indirectly from the offence or the appreciation in the value of the direct proceeds.<sup>53</sup> The intermingling of licit and illicit funds implies that the abuse of capital flight and the movement of funds to avoid or evade tax fall within the scope of TBML.<sup>54</sup>

**Figure 3: Example of Trade Misinvoicing**



**Source:** Global Financial Integrity, available at <https://gfintegrity.org/issue/trade-misinvoicing/>.

In Figure 3, the Indian importer illegally moves US\$500 000 out of India utilising a Mauritius intermediary. The importer intends to purchase only US\$1 million worth of used cars from the US exporter but utilises the intermediary to re-invoice the amount up to US\$1.5 million.<sup>55</sup> The scenario does not give us the motivation for re-invoicing the amount by an additional US\$500 000. Reference to Table 1 above suggests that there could be several reasons why the Indian importer

52 Paragraph 11 of the Preamble to Directive 2014/42/EU.

53 OECD (2018) "Confiscation of instrumentalities and Proceeds of Corruption Crimes in Eastern Europe and Central Asia" *Anti-Corruption Network for Eastern Europe and Central Asia* at 25.

54 APG (2012) "APG Typology Report on Trade Based Money Laundering" *Asia/Pacific Group on Money Laundering* paragraph 31.

55 GFI "Trade Misinvoicing" paragraph 6.

overvalued the import from the US exporter, for example, to shift legitimate but undeclared income or profit offshore, to transfer criminal proceeds to another country, or to evade capital controls (including on profit repatriation). Whatever the reason, an economic advantage was derived from the illicit transaction. The most important aspect is that the transaction must constitute a crime and generate illegal proceeds. The US exporter is paid a legitimate US\$1 million, but the remaining US\$500 000 then is diverted to an offshore bank account, constituting an act designed to disguise the unlawful activity. Besides, the Indian importer will not pay taxes or import duties on the US\$500 000, since it does not exist for the Indian customs authorities.

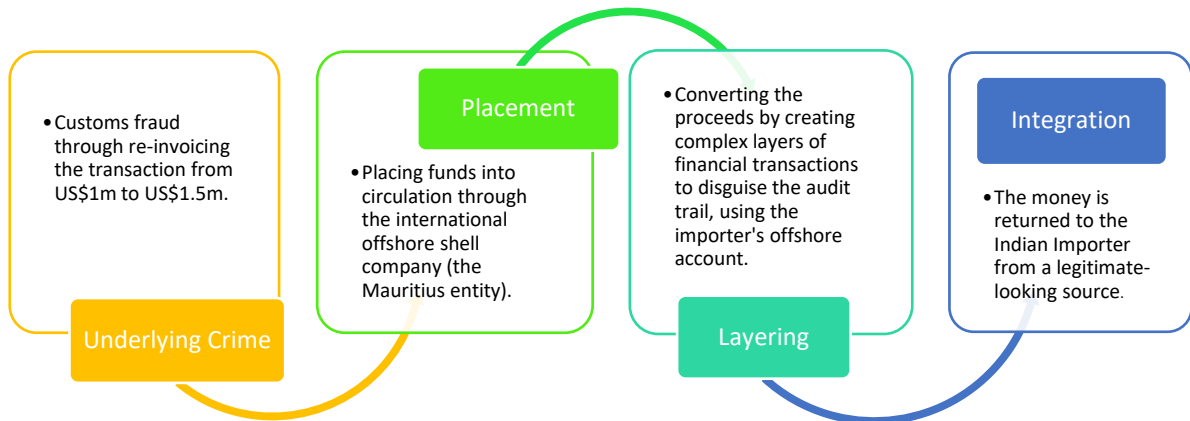
The example illustrated in Figure 3 above presents a legally cognisable theory of money laundering conspiracy because the specified unlawful activity — the customs fraud scheme — allowed the Indian importer to shift the illegal proceeds of US\$500 000 offshore. The intermediary used the process of re-invoicing to disguise the true nature of the original transaction with the US exporter, thereby deriving an economic advantage for the Indian importer and facilitating onward distribution of the money. The Mauritius intermediary helped the Indian importer to commit the predicate offence and to evade the legal consequences of his actions, in contravention of Article 6(1) of the United Nations Convention against Transnational Organised Crime. If the above scenario were to give rise to a money laundering prosecution, proof of the criminal origin of the property would require the testimony of the Mauritius intermediary, as the person with the best knowledge of who perpetrated the fraud which created the criminal proceeds.<sup>56</sup>

Money laundering, including TBML, often involves a complex series of transactions that traverses three phases, namely, placement, layering and integration.<sup>57</sup> Figure 4 below demonstrates how the crime of money laundering eventually was committed in the scenario of TMI presented in Figure 3. Regardless of the stage of the transaction, the underlying crime occurred when the act of fraud was committed by re-invoicing the original transaction from US\$1 million to US\$1.5 million. This transaction will offend against the laws of India concerning

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56 Bell R (2000) "Proving the Criminal Origin of Property in Money-Laundering Prosecutions" 4(1) *Journal of Money Laundering Control* 12-25 at 13.

57 ACAMS (2012) "Study Guide for the CAMS Certification Examination (5ed)" *Association of Certified Anti-Money Laundering Specialists* at 15.

**Figure 4: How Trade Misinvoicing Generated Proceeds of Crime**

**Source:** The author

false declaration and/or false documents.<sup>58</sup> In India, commercial fraud is any offence against statutory or regulatory provisions administered by the Central Board of Indirect Taxes and Customs, which offence is committed in order to:

- evade, or attempt to evade, payment of duties or levies or taxes on movements of commercial goods;
- evade, or attempt to evade, any prohibitions, restrictions or requirements applicable to commercial goods;
- receive, or attempt to receive, any repayments, subsidies or other disbursements to which there is no proper entitlement nor transaction;
- obtain, or attempt to obtain, illicit commercial advantage injurious to the principle and practice of legitimate business competition; and/or
- exploit, or attempt to exploit, commerce for the purpose of transferring proceeds of crime.<sup>59</sup>

So, criminal proceeds and stolen public funds or legitimate income and company profits may be laundered. In other words, money laundering may involve capital adjudged to be either illegal or legal.

This paper accepts that, in relation to TMI, the concept of proceeds of crime encompasses “any property derived from or obtained, directly or indirectly, through the commission of an offence”.<sup>60</sup> The process of misinvoicing, whatever the motivation, involves money laundering because the unlawful activity begins

58 Section 132 of the Customs Act, 1962.

59 This amended definition was agreed by the Working Group on Commercial Fraud, approved by the 27th Session of the Enforcement Committee and adopted by the Council in June 2008. See Nanda A (2017) “Trends in Revenue Fraud: The Indian Customs’ Perspective” *WCO Knowledge Academy* at 2.

60 Article 2(e) of the United Nations Convention against Transnational Organised Crime.

when illicit profits are generated. The illicit origins of the profits are obscured through further layers of transactions designed to make them seem legitimate. The traditional theory of a money laundering scheme is that the illegal proceeds must exist before money laundering is perpetrated. However, money laundering is committed when the launderer intentionally conceals or disguises the true nature of the criminally derived property in order to make it appear licit. Money laundering is a crime of motive rather than activity<sup>61</sup> and should be treated as a means to an end, rather than as an end in itself.<sup>62</sup> At its core:

money laundering involves the proceeds of criminally derived property rather than the property itself.<sup>63</sup>

Through misinvoicing, the underlying crime is committed and the money launderer intentionally and eventually conceals the true nature of the property through a series of other transactions. This debunks the assumption that businesses operating internationally are not used to launder the proceeds of crime.<sup>64</sup>

Figure 5 below shows the capital origin of a quadrant of transactions ranging from illicit to licit and illegal to legal. Now, as regards IFFs, illegality across any stage of outflows in one geographical location does not nullify the intent and purpose of such outflows, which are to hide money, even if legitimately earned.<sup>65</sup> Historically, the focus of anti-money laundering research and policy development has been placed on those transactions where the origin of the capital is illegal, that is, clusters relating to the abuse of power and proceeds of crime such as drug trafficking and terrorism financing. The areas of market and tax abuse which constitute motivations for TMI have been neglected in terms of policy focus, largely excluding the use by private sector actors of trade to launder money, whether intentionally or not.<sup>66</sup>

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61 CEI (2001) "Why the War on Money Laundering should be Aborted", available at <https://cei.org/outreach-regulatory-comments-and-testimony/why-war-money-laundering-should-be-aborted> (visited 25 May 2020).

62 OECD (2018) "Illicit Financial Flows: The Economy of Illicit Trade in West Africa" *OECD Publishing* at 22.

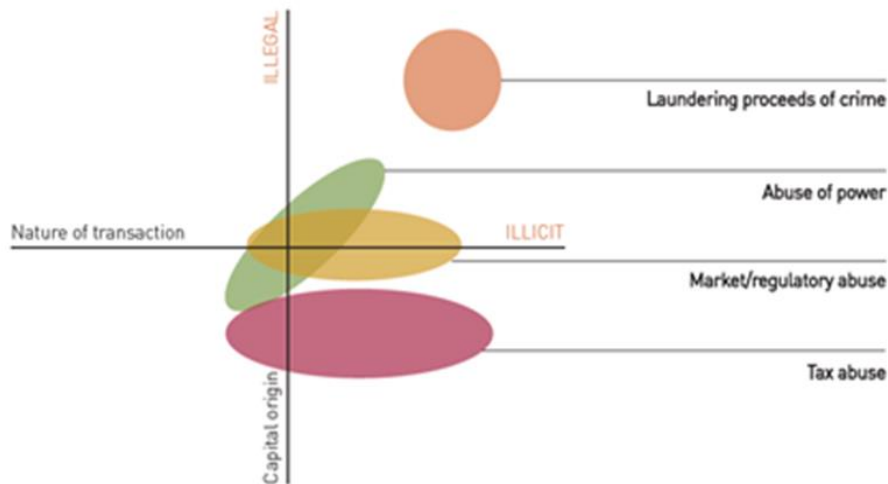
63 Schott P (2006) "Reference Guide to Anti-Money Laundering and Combatting the Financing of Terrorism", *World Bank*, Washington Second Edition and Supplement on Recommendation IX at 1.

64 Cobham & Jansky (2017b) at 9.

65 AU/ECA (2015) at 23.

66 Cobham (2014) at 10.



**Figure 5: Origin of Illicit Financial Flows**

**Source:** AU/ECA Report of the High-Level Panel on Illicit Financial Flows from Africa (2015)

### 2.3.2 Motivations of Trade Misinvoicing as Predicate Offences for Money Laundering

Generally, money laundering has been criminalised globally. Across different jurisdictions, there are variations in the definition and application of predicate offences. Initially, predicate offences were confined to drug trafficking, as defined in the 1988 Vienna Convention. However, countries were encouraged to extend predicate offences to include other crimes. Presently, in some jurisdictions predicate offences are limited to the crime of drug trafficking and a few other crimes.<sup>67</sup> In other jurisdictions, an exhaustive list of predicate offences is embedded in domestic legislation, whereas some countries define predicate offences generically to include all crimes, or all serious crimes, or all crimes subject to a defined penalty threshold.<sup>68</sup>

The FATF Recommendations require countries to criminalise money laundering in terms of the 1988 Vienna Convention and 2000 Palermo Convention, and to apply the crime of money laundering to all serious offences, with a view to designating the widest range of predicate offences.<sup>69</sup>

67 UNODC “Criminalising the Laundering of Proceeds of Trafficking in Persons”, available at [https://www.unodc.org/documents/human-trafficking/Toolkit-files/08-58296\\_tool\\_3-5.pdf](https://www.unodc.org/documents/human-trafficking/Toolkit-files/08-58296_tool_3-5.pdf) (visited 25 May 2020).

68 UNODC “Criminalising the Laundering of Proceeds of Trafficking in Persons” paragraph 4.

69 FATF Recommendation 3.



The United Nations Convention on Transnational Organised Crime states that:

Predicate offence shall mean 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 this Convention.<sup>70</sup>

The crime of money laundering is linked inherently to the underlying predicate offence that gave rise to the criminally derived property. Therefore, the FATF makes the following recommendation:

Countries should apply the crime of money laundering to all serious offences, with a view to including the widest range of predicate offences. Predicate offences may be described by reference to all offences, or to a threshold linked either to a category of serious offences or to the penalty of imprisonment applicable to the predicate offence (threshold approach), or to a list of predicate offences, or a combination of these approaches.<sup>71</sup>

The FATF Recommendations list designated categories of offences<sup>72</sup> considered to be predicate offences for money laundering.<sup>73</sup> Significantly, serious tax crimes, market manipulation, fraud and forgery are among the categories of designated offences<sup>74</sup> which also fall under the motivations of TMI. Any motivation of TMI must generate proceeds of crime and be the subject of an offence, as defined by Article 6 of the Palermo Convention, to be prosecuted for additional charges of money laundering. The only requirement for such a prosecution is that the predicate offence is a crime domestically, even if it was committed in another jurisdiction.<sup>75</sup>

Ultimately, the deliberate misrepresentation of the value of imports or exports in order to evade customs duties and VAT taxes, to launder the proceeds of criminal activity, or to hide offshore the proceeds of legitimate trade transactions<sup>76</sup> is motivated by the importer's or exporter's desire to generate extra profit. TMI always is driven by a financial motive.<sup>77</sup> The use of offshore companies to re-

70 Article 2(h) of the Palermo Convention, 2000.

71 Interpretive Note to FATF Recommendation 3 (Money Laundering Offence).

72 For the complete list, see FATF Recommendations: General Glossary.

73 ACAMS "AML Glossary", available at <https://www.acams.org/aml-glossary/index-d/> (visited 25 May 2020).

74 FATF Recommendations: General Glossary.

75 FATF Recommendation 3.

76 AfricaBusiness.com (2019) "Illicit Financial Flows are Significant and Persistent Drag on Developing Country Economies", available at <https://africabusiness.com/2019/01/29/trade-misinvoicing/> (visited 25 May 2020).

77 UNCTAD (2016) "Trade Misinvoicing in Primary Commodities: The cases of Chile, Côte d'Ivoire, Nigeria, South Africa and Zambia" *UNCTAD/SUC/2016/2* at 7.

invoice trade documents, thereby generating and concealing criminal proceeds, will constitute a *bona fide* case for a money laundering prosecution. The motivations of TMI should be regarded as predicate offences to enable prosecutors to bring additional charges of money laundering against the fraudulent operations of commercial businesses.

If TMI were not profiting the traders financially, it would not have cost some of Africa's largest economies dearly. According to a recent report by GFI, TMI in South Africa for the period 2010–2014 entailed potential loss of revenue to the government of US\$7.4 billion annually, comprising a total of US\$37 billion.<sup>78</sup> In 2014, the potential loss of revenue to the Nigerian government through TMI was approximately US\$2.2 billion.<sup>79</sup> In Kenya, TMI in 2013 involved potential loss of revenue to the government of US\$907 million.<sup>80</sup> And in 2016, the estimated potential tax revenue losses to the Egyptian government were approximately US\$1.6 billion, equivalent to 4.1% of Egypt's total government revenue collections for that year.<sup>81</sup> All in all, TMI comprised an average of 87% of IFFs from developing<sup>82</sup> to the financial institutions of developed countries, such as the US and UK, and tax havens, such as Switzerland, the British Virgin Islands and Singapore.<sup>83</sup>

This does not happen by accident. Many countries and their institutions actively facilitate — and reap enormous profits from — the inflow of massive amounts of money from developing countries.<sup>84</sup>

There is no gainsaying this observation.

78 GFI (2018a) "South Africa: Potential Revenue Losses Associated with Trade Misinvoicing", available at <https://gfintegrity.org/report/south-africa-potential-revenue-losses-associated-with-trade-misinvoicing/> (visited 25 May 2020).

79 GFI (2018b) "Global Financial Integrity Releases New Study on Trade Misinvoicing in Nigeria", available at <https://gfintegrity.org/press-release/global-financial-integrity-releases-new-study-on-trade-misinvoicing-in-nigeria/> (visited 25 May 2020).

80 GFI (2018b) "Global Financial Integrity Releases New Study on Trade Misinvoicing in Kenya", available at <https://gfintegrity.org/press-release/global-financial-integrity-releases-new-study-on-trade-misinvoicing-in-kenya/> (visited 25 May 2020).

81 GFI (2019b) "Egypt: Potential Revenue Losses Associated with Trade Misinvoicing", available at <https://gfintegrity.org/report/egypt-potential-revenue-losses-associated-with-trade-misinvoicing/> (visited 25 May 2020).

82 GFI (2017) at vii.

83 Basquill J (2020) "Trade Misinvoicing a "Real and Immediate Liability", available at <https://www.gtreview.com/news/global/trade-misinvoicing-a-real-and-immediate-liability/> (visited 27 May 2020).

84 Basquill (2020) paragraph 5.

### 3 POLICY IMPLICATIONS

TBML in the international trade sector has implications for anti-money laundering policy at the global, regional and national levels.

#### 3.1 Redefinition of Trade Misinvoicing in International Policy Framework

TMI ought to be redefined in the context of money laundering, not explicitly in legislation but in policy frameworks which can influence a better understanding of the phenomenon and enhance more effective legislative measures to curb money laundering in international trade. In this regard, it is suggested that TMI means misrepresenting the price or quantity of imports or exports in order to launder money to other jurisdictions. The point is that money laundering is one of the inevitable outcomes of TMI. The discussion below attempts to demonstrate this intimate association of TMI with money laundering.

#### 3.2 The US Approach

The US was one of the first countries to criminalise money laundering, and claims to have the world's most comprehensive and effective anti-money laundering and countering the financing of terrorism (AML/CFT) regime.<sup>85</sup>

The criminalisation of money laundering is contained in the Federal Statutory Code 18 USC §1956(a)(1), which states that:

Whoever, knowing that the property involved in a financial transaction represents the proceeds of some form of unlawful activity, conducts or attempts to conduct such a financial transaction which in fact involves the proceeds of specified unlawful activity—

- (A)(i) with the intent to promote the carrying on of specified unlawful activity; or
- (ii) with intent to engage in conduct constituting a violation of section 7201 or 7206 of the Internal Revenue Code of 1986; or
- (B) knowing that the transaction is designed in whole or in part—
  - (i) to conceal or disguise the nature, the location, the source, the ownership, or the control of the proceeds of specified unlawful activity; or
  - (ii) to avoid a transaction reporting requirement under State or Federal law,

shall be sentenced to a fine of not more than \$500,000 or twice the value of the property involved in the transaction, whichever is greater, or imprisonment for not more than twenty years, or both.

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85 US Treasury (2020) "National Strategy for Combating Terrorist and Other Illicit Financing" at 3.

The section goes on to stipulate that:

a financial transaction shall be considered as one involving the proceeds of specified unlawful activity if it is part of a set of parallel or dependent transactions, any one of which involves the proceeds of specified unlawful activity, and all of which are part of a single plan or arrangement.

Predicate offences for money laundering are referred to as “specified unlawful activity” and are defined broadly under the Federal Criminal Statute.<sup>86</sup> The definition encompasses a broad range of white-collar and other crimes, including a list of more than 170 crimes ranging from fraud to tax evasion as predicate offences for money laundering.<sup>87</sup> Also, §1956(a)(2) outlaws the international transportation or transmission of funds with the intent to promote a predicate offence; or knowing that the purpose is to conceal laundering of the funds and that the funds are the proceeds of a predicate offence.<sup>88</sup> Its companion, 18 USC §1957, prohibits depositing or spending more than \$10 000 of the proceeds from a predicate offence and carries a maximum penalty of imprisonment for 10 years.<sup>89</sup>

### 3.2.1 Example 1

The US Homeland Security Investigations uncovered a smuggling and undervaluation scheme involving scrap gold, which operated from January 2012 to November 2013.<sup>90</sup> It was a basic TMI scheme in which a US importer smuggled scrap gold into the US from Central America at undervalued prices and subsequently provided payments to the exporters at overvalued amounts.<sup>91</sup> The two colluding Central American companies sent scrap gold with a total declared value of US\$6.4 million to the US importer, while wire transfers of US\$24 million were made to the Central American companies for those imports.<sup>92</sup> The owners of the US business were arrested and charged with conspiracy to commit money laundering using customs violations as a predicate offence.<sup>93</sup>

86 §1956(c)(7).

87 Cadwalader, Wickersham & Taft LLP “Anti-Money Laundering and Fraud in the USA”, available at <https://www.lexology.com/library/detail.aspx?g=330bdf46-1eb9-4a14-8d7e-9851feb2839e> (visited 29 May 2020).

88 See §1956(a)(2)(A) and §1956(a)(2)(B)(i).

89 See Doyle C (2017) “Money Laundering: An Overview of 18 USC §1956 and Related Federal Criminal Law” *Congressional Research Service RL33315* paragraph 1.

90 FATF & APG (2015) “Money Laundering/Terrorist Financing Risks and Vulnerabilities Associated with Gold” at 28.

91 FATF & APG (2015) at 28.

92 FATF & APG (2015) at 28.

93 FATF & APG (2015) at 28.

In this case, the capital was not proceeds of crime derived from terrorist activity, corruption or drug-related offences. Rather, the proceeds of crime were generated as a result of customs violations, specifically through TMI. According to Kaplan Marino, a white collar criminal defence law firm based in the US, “virtually every criminal offense that derives a monetary gain can be subject to money laundering charges”.<sup>94</sup>

### 3.2.2 Example 2

In *United States v Garcia-Adarme et al*,<sup>95</sup> a federal grand jury indicted five individuals and three companies for conspiracy to smuggle and clandestinely introduce aluminium into the US.<sup>96</sup> The goods were imported from China by passing false and fraudulent invoices and documents through the San Juan CBP customhouse with the intent to defraud the US of approximately US\$26.7 million in lawful anti-dumping and countervailing (ADD/CVD) duties.<sup>97</sup> All defendants were charged with conspiracy to commit money laundering when they attempted to transfer US\$6 907 985.43 from Puerto Rico to Malaysia, with the intent to promote the conduct of a specified unlawful activity.<sup>98</sup>

### 3.2.3 Example 3

In *United States v Chavez et al*,<sup>99</sup> the government showed that it was using traditional civil statutes, such as 19 USC §1592, in conjunction with other civil and criminal statutes in a multi-pronged approach to combat customs violations.<sup>100</sup> Two individuals and their corporations were charged with and found guilty of multiple criminal counts, including conspiracy (18 USC §371), money laundering (18 USC §1956), and entry of goods by means of false statements (18 USC §542).<sup>101</sup> The defendants were charged also with obstruction of justice (18 USC §1519),

94 Kaplan Marino “Money Laundering and Conspiracy”, available at <https://kaplanmarino.com/practice-areas/white-collar-crimes/conspiracy-and-money-laundering/> (visited 22 May 2020).

95 *United States v Garcia-Adarm et al*, Criminal Case No 13-353 (DPR).

96 US DoJ (2013) “Five Individuals Indicted and Arrested for Conspiracy to Smuggle Goods into the United States and Money Laundering”, available at <https://www.justice.gov/usao-pr/pr/five-individuals-indicted-and-arrested-conspiracy-smuggle-goods-united-states-and-money> (visited 1 June 2020).

97 US DoJ (2013) paragraph 2.

98 US DoJ (2013) paragraph 7.

99 *United States v Chavez et al* Criminal Case No 03137 (SDC).

100 Aenlle-Rocha F *et al* (2015) “And Up to Twenty Years in Prison: The Criminalisation of US Customs Violations” *White & Case* at 3, available at <https://gfintegrity.org/white-case-highlights-increased-u-s-scrutiny-of-trade-misinvoicing/> (visited 11 July 2020).

101 Aenlle-Rocha *et al* (2015) at 3.

which, along with the money laundering charges, exposed them to a potential prison term of 20 years.<sup>102</sup>

The US government is expanding enforcement mechanisms from monetary penalties to prison terms, and turning to conventional criminal statutes to enforce customs laws.<sup>103</sup> Thus, 18 USC §1956 and §1957 on money laundering have been used in recent customs violation prosecutions in tandem with the more common statutes deployed in trade matters.<sup>104</sup> These include 19 USC §1592 (entering goods into the US via fraud, gross negligence or negligence), 18 USC §541 (entry of goods falsely classified) and 18 USC §542 (entry of goods by means of false statements).<sup>105</sup> There is an increase of US enforcement in the customs sector, and the cases referred to involve TMI/fraud, a practice which accounts for about 80% of GFI's estimates of IFFs which drained US\$730 billion from developing and emerging economies in 2012.<sup>106</sup>

### 3.3 The Korean Approach

The Korea Customs Service (KCS) discovered that the legal and administrative mechanisms employed to tackle international trade crimes were aimed only at undervaluation of goods, and had little effect in addressing overvaluation.<sup>107</sup> Thus, the KCS revised the Customs Act by criminalising the manipulation of prices of goods itself, irrespective of evasion of taxes.<sup>108</sup> This revision has empowered the KCS to tackle manipulation of prices of import and export goods more actively than ever.<sup>109</sup> In 2013, the KCS investigated 24 price manipulation cases amounting to US\$82 million worth of criminal proceeds, with the total figure of price manipulation investigations from 2013 to 2017 standing at 154 cases involving US\$792 million worth of criminal proceeds.<sup>110</sup>

In a typical overvaluation case, a Korean semi-conductor company set up a shell company in China and pretended to import the goods at overvalued prices

102 Aenlle-Rocha *et al* (2015) at 3.

103 Aenlle-Rocha *et al* (2015) at 2.

104 Aenlle-Rocha *et al* (2015) at 2.

105 Aenlle-Rocha *et al* (2015) at 2.

106 Lowe H (2015) "White & Case Highlights Increased US Scrutiny of Trade Misinvoicing", available at <https://gfintegrity.org/white-case-highlights-increased-u-s-scrutiny-of-trade-misinvoicing/> (visited 1 June 2020).

107 Han C (2018) "Combating Illicit Financial Flows: Practice of Korea Customs Service" in World Customs Organisation *Illicit Financial Flows via Trade Mis-invoicing* Study Report at 140.

108 Han (2018) at 140.

109 Han (2018) at 141.

110 Han (2018) at 141.

directly from its business partner, a company also in China.<sup>111</sup> The Korean importer declared to customs authorities overvalued prices which were manipulated by getting the shell company fictitiously involved in the trade between the Korean semi-conductor company and the Chinese company.<sup>112</sup> Customs officials investigated the Korean company's trade records and determined that the extent of the criminal proceeds generated through overvalued prices, in comparison to the genuine invoices, amounted to US\$16 million.<sup>113</sup> Further analysis led to the discovery that, of said criminal proceeds, US\$6 million were brought to Korea as employees' wages, foreigners' donations and foreign direct investments.<sup>114</sup>

### 3.4 Approach of Global Financial Integrity

GFI suggests that TMI does not correspond precisely to TBML, but is a mechanism that is used to engage in TBML.<sup>115</sup> The implication of this approach, as GFI suggests, is that governments should adopt laws making TMI illegal, along the following lines:

Whoever, in relation to the importation or exportation of goods or in relation to the trade in services or intangible property, deliberately misstates, manipulates, falsifies, or omits a price, quantity, volume, grade, or other material aspect of an invoice for the purpose of (i) evading or avoiding VAT taxes, customs duties, income taxes, or any other form of tax or revenue collected by the Government; (ii) obtaining a tax benefit, export subsidy, or other benefit provided by the Government; or (iii) evading or avoiding [capital or foreign exchange controls]; shall be subject to a civil or criminal fine of up to [specific amount] [or imprisoned for up to [X] year(s), or both].<sup>116</sup>

GFI suggest also that governments should develop the capacity of customs authorities by providing the training and equipment needed to improve the detection of intentional misinvoicing of international trade transactions.<sup>117</sup>

### 3.5 Application of AML/CFT Measures to the International Trade Sector

By widening the coverage of money laundering to fraudulent operations of commercial businesses, policymakers will be able effectively to apply anti-money laundering mechanisms to the international trade sector.

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111 Han (2018) at 142.

112 Han (2018) at 142.

113 Han (2018) at 142.

114 Han (2018) at 142.

115 GFI "Trade Misinvoicing" paragraph 3.

116 GFI (2019a) at 19.

117 GFI (2019a) at 19.



As the main policy-making body in the global fight against money laundering, the FATF would have to generate the necessary political will to bring about national legislative and regulatory reforms in the international trade sector. A new recommendation on TBML should address all those involved in the international trade supply chain, including importers and exporters, freight forwarders, shippers and air couriers companies.<sup>118</sup>

As suggested by Delston & Walls, a forty-first FATF Recommendation on TBML could read as follows:

#### Recommendation 41, Trade-Based Money Laundering

Countries should have measures in place to monitor, detect and prosecute abuses of the international trade system on the basis of the Vienna and Palermo Conventions, and should ensure that one or more competent domestic authorities are authorised to supervise traders. Countries should ensure that effective, proportionate and dissuasive sanctions are available to these authorities to deal with persons who fail to comply with AML/CFT requirements under this Recommendation, fail to declare or make false declarations on customs forms or on any documentation related to the import/export of such goods, including bills of lading, invoices, warehouse receipts, and letters of credit. In cases where the goods or the underlying import/export transactions are related to terrorist financing, money laundering or predicate offences, countries should also adopt measures, including legislative measures consistent with Recommendation 4, that would enable the confiscation of such goods. Domestic authorities should be empowered to inspect shipments with technology commensurate with the risks of money laundering and financing of terrorism, collect and review related documents, collect and analyse information gathered by domestic law enforcement authorities, and monitor trade flows on a real-time basis. Commensurate with the risks identified, countries should implement new inspection technologies relating to the prevention, suppression and disruption of proliferation of weapons of mass destruction. Traders should be required to implement programmes against trade-based money laundering and terrorist financing that encompass the following:

- a) Adequate internal controls, including group-wide training and information-sharing, set out in Recommendation 18;
- b) Customer due diligence and record-keeping requirements consistent with Recommendations 10, 11, 12, 15 and 17 for import and export transactions in an amount equal to or greater than the applicable designated threshold; and

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118 Delston R & Walls S (2009) "Reaching beyond Banks: How to Target Trade-Based Money Laundering and Terrorist Financing Outside the Financial Sector" 41 *Case Western Reserve Journal of International Law* 85-118 at 88.



- c) Report suspicious transactions as set out in Recommendations 20 and 21.<sup>119</sup>

An interpretive note to this new Recommendation 41 could draw heavily from red flags and other issues discussed in landmark policy papers on TBML developed by the FATF.<sup>120</sup>

#### **4 CONCLUSION**

Money laundering rarely is discussed in any depth in the context of TMI. This paper has sought to clarify the linkages between TBML and TMI. It provides an analysis of money laundering in the context of TMI as a means of adding impetus for prosecutors to tackle money laundering activities by commercial businesses in the international trade sector. It concludes that, within the context of TMI, money laundering is the falsification of trade documents to conceal or disguise the true nature of the transaction and to entitle the international trader involved to apparently legitimate possession of the property shifted.

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119 Delston R & Walls S (2012) "Strengthening Our Security: A New International Standard on Trade-Based Money Laundering Is Needed Now" 44 *Case Western Reserve Journal of International Law* 737-746 at 744-745.

120 Delston & Walls (2012) at 745.