REGULATING MONEY LAUNDERING IN THE UNITED STATES AND HONG KONG: A POST 9-11 COMPARISON

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I. INTRODUCTION

China announced in September 2005 that it is "stepping up work on laws to counter money laundering and [the] financing of terrorist

operations" with the aim of entry into the Financial Action Task Force (FATF).[1] The FATF has been the most successful international entity at encouraging countries to combat money laundering. However, only after the terror attacks of September 11, 2001 (9-11), did the organization begin to specifically target terrorist financing.[2] One of the recent FATF Special Recommendations addresses underground banking networks, a method of transferring money that avoids formal financial institutions.[3]

This Note will compare how post 9-11 money laundering legislation in two FATF member countries, the U.S. and Hong Kong, applies to underground banking.[4] This comparison reveals that a huge discrepancy exists among current standards for dealing with underground banking.[5] However, the FATF is currently more concerned with gathering information than forcing countries to enact specific regulations. As China's spokesman said, the "anti-money laundering campaign calls for international co-operation between all regions and countries."[6] However, targeting underground banking is not currently required.

A note on terminology. Underground banking encompasses a number of terms.[7] The FATF uses the term "Alternative Remittance Systems" (ARS); the U.S. uses the term "Informal Value Transfer Systems" (IVTS); and Hong Kong uses the term "Unregulated Remittance Centers" (URC). To avoid confusion, I will use the term "underground banking" to refer to the phenomenon generally, "IVTS" to refer to systems targeted by the U.S., and "URCs" to refer to the systems targeted by Hong Kong.

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1. *China Working on Laws to Counter Laundering*, CHINA DAILY, Sept. 24, 2005, http://www.chinadaily.com.cn/english/doc/2005-09/24/content_480548.htm (last visited Sept. 24, 2005). China was granted observer status in the Financial Action Task Force (FATF) in January 2005, but it cannot receive member status until regulations are passed. FIN. ACTION TASK FORCE, ANNUAL REPORT 2004–2005, at 7 (June 10, 2005), *available at* http://www.fatf-gafi.org/dataoecd/41/25/34988062.pdf [hereinafter FATF 2004–2005 ANNUAL REPORT].

2. FIN. ACTION TASK FORCE ON MONEY LAUNDERING, SPECIAL RECOMMENDATIONS ON TERRORIST FINANCING (Oct. 22, 2004), *available at* http://www.fatf-gafi.org/dataoecd/8/17/34849466.pdf.

3. *Id. See* Part VI.

4. Specifically, this Note will compare the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act (USA PATRIOT Act), Pub. L. No. 107-56, 115 Stat. 272 (2001), with the United Nations (Anti-Terrorism Measures) Ordinance, (2004) Cap. 575. (H.K.), *available at* http://www.legis.gov.hk/yr04-05/English/subleg/sub_0172.htm.

5. The USA PATRIOT Act better conforms to Special Recommendation VI than Hong Kong's United Nation's (Anti-Terrorism Measures) Ordinance. *See* FIN. ACTION TASK FORCE ON MONEY LAUNDERING, *supra* note 2, Part IV.

6. Jiang Zhuqing, *Laundering Legislation to Spread Net Wider*, CHINA DAILY, (Sept. 30, 2005), *available at* http://www.chinadaily.com.cn/english/doc/2005-09/30/content_482018.htm, *quoting* Cai Yilian, Deputy Director of the Anti-money Laundering Bureau under the People's Bank of China (PBOC).

7. *See infra* note 10.

II. BACKGROUND AND HISTORY

A. The Money Laundering Process

Money laundering is defined as "the process that disguises illegal profits without compromising the criminals who wish to benefit from the proceeds."[8] According to estimates, as much as $1 trillion of funds are laundered internationally per year.[9] The process usually involves three stages: placement, layering, and integration.[10]

In the placement stage, funds are removed from the criminal act by placement in a bank.[11] Because the money at this stage is in the form of cash, it is bulky and difficult to transport.[12] Money at this stage is most vulnerable to being lost, stolen, destroyed, or detected.[13] U.S. legislation has primarily targeted this stage by focusing on financial institutions.[14] Criminals respond by attempting to avoid these institutional regulations.[15]

In the second stage, layering, the launderer distances the illegal money from the crime through a series of complex financial transactions. This is the most international stage, as launderers often utilize offshore financial institutions to conceal funds.[16] The purpose of creating such a complex trail is to so obscure the connection between the money and the crime that detection by law enforcement becomes impossible.[17]

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8. U.N. Office on Drugs and Crime, *The Money Laundering Cycle*, *available at* http://www.unodc.org/unodc/en/money_laundering_cycle.html (last visited Oct. 30, 2005) [hereinafter *The Money Laundering Cycle*].

9. Wendy Chamberlin, Introduction, *The Fight Against Money Laundering*, ECONOMIC PERSPECTIVES, May 2001, at 2, http://usinfo.state.gov/journals/ites/0501/ijee/ijee0501.pdf (last visited Jan. 22, 2006).

10. Paul Bauer & Rhoda Ullmann, Commentary, *Understanding the Wash Cycle*, ECONOMIC PERSPECTIVES, May 2001, at 19, http://usinfo.state.gov/journals/ites/0501/ijee/ijee0501.pdf.

11. Lester M. Joseph, *Money Laundering Enforcement: Following the Money*, ECONOMIC PERSPECTIVES, May 2001, at 11, http://usinfo.state.gov/journals/ites/0501/ijee/ijee0501.pdf.

12. Bauer & Ullmann, *supra* note 10.

13. *The Money Laundering Cycle*, *supra* note 8.

14. Andres Rueda, *International Money Laundering Law Enforcement & the USA Patriot Act of 2001*, 10 MSU-DCL J. INT'L L. 141, 174 (2001).

15. *Id.*

16. Offshore financial institutions with tax havens, strict bank secrecy rules, or lax statutory enforcement are preferred. *The Money Laundering Cycle*, *supra* note 8. Other techniques include Shell banks (banks with no real address or location, sometimes existing solely on the internet), "loan-backs" (where the criminal transfers his money to an offshore entity that he owns and then transfers it back), "double invoicing" (keeping two sets of books), and the purchase of big-ticket items (that are bought and then resold). *Id.*

17. *Id.*

The final stage, integration, occurs when the funds are fully assimilated into the mainstream economy and become available to the criminal for any purpose.[18]

B. Avoiding Detection

Because money is most vulnerable at the placement stage, U.S. legislation has focused here by regulating financial institutions.[19] Regulations including "Know Your Customer" identification requirements, Currency Transaction Reports for amounts over $10,000, and Suspicious Activity Reports aim at destroying criminal anonymity and detecting illegal funds.[20]

In response, criminals attempt to structure their transactions in ways that avoid these regulations. For example, keeping transactions just under $10,000 skirts the Currency Transaction Reporting requirement.[21] Other avoidance techniques include mixing the illegal cash with legitimate funds through a cash-intensive business, such as a restaurant, hotel, or casino,[22] or using insurance companies, currency smuggling, real estate or gold transactions, and non-bank financial institutions such as bureaux de change and money remitters.[23] Yet another alternative is to avoid financial institutions altogether by using IVTS.

C. Informal Value Transfer Systems (IVTS)

The U.S. uses the term IVTS because it is more accurate than other terms.[24] The term "underground banking" is inaccurate because "[i]t is not always underground; banking is rarely involved, if ever; and it is not a single system."[25] The terms "alternative banking" and "alternative remittance systems" are inaccurate because these systems predate the

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18. *Id.*
19. Rueda, *supra* note 14, at 174.
20. *The Money Laundering Cycle*, *supra* note 8.
21. This is called the "smurfing syndrome." Petrus van Duyne, *Medieval Thinking and Organized Crime Economy*, *in* TRANSNATIONAL ORGANIZED CRIME: MYTH, POWER, AND PROFIT 42 (Emilio C. Viano, Jose Magallanes, Laurent Bridel eds., Carolina Academic Press, 2003).
22. Bauer & Ullmann, *supra* note 10, at 20.
23. NIKOS PASSAS, INFORMAL VALUE TRANSFER SYSTEMS AND CRIMINAL ORGANIZATIONS: A STUDY INTO SO-CALLED UNDERGROUND BANKING NETWORKS 3 (1999), http://usinfo.state.gov/apgml.org/frameworks/docs/8/Informal%20Value%20Transfer%20Systems%20-%20Passas.pdf.
24. Other terms for underground banking include "informal banking, unregulated banking, quasi-banking, alternative banking, alternative remittance systems, and parallel banking." *Id.* at 9.
25. *Id.*

conventional banking systems of many countries and in some places still remain more prevalent than formal banking systems.[26]

Another misconception regarding IVTS is that these systems arose to subvert legal financial institutions or government restrictions.[27] In fact, the two precursors of modern IVTS arose in India and China primarily as ways to transfer money through more secure and convenient systems than physical transport.[28] These systems were, in essence, "centuries old . . . low-tech Western Union[s]"[29] that "facilitated legitimate trade or other transactions, while protecting against robbery and theft [on] highways."[30] As these ethnic groups emigrated outside Asia, they established IVTS abroad and relied on these systems to send money back home.[31]

Today, IVTS exist on every continent. While there are multiple variations,[32] IVTS are derived from three basic types: the Chinese system

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26. *Id*. at 11.

27. *Id*. at 13.

28. For "[t]he most authoritative and original study on the beginnings and mechanics of indigenous banking in India" see L.C. JAIN, INDIGENOUS BANKING IN INDIA (1929). PASSAS, *supra* note 23, at 13.

> According to Akse (1996), the origins of the system are located in the North-South rice trade, when traders sought to avoid the physical transportation of money. . . . In the second half of the T'ang dynasty, a growing tea commerce between the south and the imperial capital created the need for a convenient means of exchange. As a result, 'flying money' (fei-ch'ien) evolved. As Cassidy (1994:2-3) notes, 'Provincial governors maintained 'memorial offering courts' at the capital. Southern merchants paid the money they made from the sale of goods at the capital to these courts, which then used it to pay the tax quotas due from the Southern provinces to the central government. In return, the courts issued the merchants with a [sic] certificate. When the merchant returned home, he presented this certificate to the provincial government and was paid an equivalent sum of money. Thus . . . both the merchant and the local government avoid[ed] the risk and inconvenience of carrying quantities of copper or silk.'

Id. at 16 (citing A.T. Akse, Geldstromen Onder N.A.P.: Ondergrondsbankieren in Nederland, Amsterdam, FINPOL, KLPD\dCRI, 1996 and W.L. Cassidy, Fei-Chien or Flying Money: A Study of Chinese Underground Banking (WLR Cassidy & Associates), 1994, http://users.deltanet.com/~wcassidy/wlrc/Flyingmoney.html).

29. *Stefan A. Riesenfeld Symposium 2003: International Money Laundering: From Latin America to Asia, Who Pays?: The Transnational and Sub-National in Global Crimes*, 22 BERKELEY J. INT'L L. 59, 85 (2004) [hereinafter *Symposium*].

30. PASSAS, *supra* note 23, at 2.

31. *Id.* at 14.

32. FIN. ACTION TASK FORCE, MONEY LAUNDERING & TERRORIST FINANCING TYPOLOGIES 2004–2005, at 14–26 (June 10, 2005), *available at* http://www.fatf-gafi.org/dataoecd/16/8/35003256.pdf [hereinafter FATF TYPOLOGIES REPORT]; Walter Perkel, *Money Laundering and Terrorism: Informal Value Transfer Systems*, 41 AM. CRIM. L. REV. 183, 187 (Winter 2004); *Symposium*, *supra* note 29, at 74; PASSAS, *supra* note 23, at 11–12; Lisa C. Carroll, *Alternative Remittance Systems Distinguishing Sub-systems of Ethnic Money Laundering in INTERPOL Member Countries on the Asian Continent* (INTERPOL), Sept. 22, 2005, http://www.interpol.com/public/financialcrime/moneylaundering/ethnicmoney/defualt.asp. *But see* PASSAS, *supra* note 23, at 13 (quoting FinCEN officer, Joseph W. Myers: "true underground banking is practiced in only two

(*fei-quien*),[33] the Indian system (*hawala*),[34] and the American system (the Black Market Peso Exchange).[35]

IVTS are preferred over formal money transfer systems because they are cheaper and more pleasant, have lower transaction costs and increased confidentiality.[36] In some countries, IVTS are a "desperately needed service" because "the absence of adequate infrastructure and banking facilities" make the formal transfer of money impossible.[37]

In a typical IVTS transfer, no money actually crosses national borders. For example,

> [t]he client approaches a hawaladar (hawala operator or broker) to request the transfer of a certain value to country X. The banker will call or fax the details to his counterpart in that country and payment will be made within hours to the requested party . . . . The client will hand over to the local broker the amount she wishes to transfer . . . and the broker and his counterpart will settle their debt in a subsequent transfer.[38]

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cultures, the Indian (including Pakistan and Bangladesh) and the Chinese. It is only within these two cultures that social rules have evolved sufficiently to insure the trust essential to completion of a banking transaction.").

33. *Fei-quien* translates to "flying money." This system mostly involves one-way transfers and is found predominantly in China (under the names "chop shop," *di xia qian zhuang*, *hui k'uan*, and *ch'iao hui*), Hong Kong (*Nging sing kek*), Thailand (*poey kwan*, *phoei kwan*), Vietnam (*hui*, *hui kwan*), Indonesia (*bangelap*), The Philippines, Japan, and among these immigrant groups in North America and Australia. PASSAS, *supra* note 23, at 11–12; Carroll, *supra* note 32.

34. The *hawala*-based system is also called *chiti* and *hundi*. This system is larger and often involves bilateral transfers. It is the major system of Pakistan and India and is also found in Southeast Asia, Europe, the Middle East, Africa, and North America. *See* PASSAS, *supra* note 23, at 11–12; Carroll, *supra* note 32.

35. The Black Market Peso Exchange is the largest system in the western hemisphere. It is used by Columbian drug cartels in South America and Mexico. Terms include "stash house," *casas de cambio*, and *centros cambiarios*. PASSAS, *supra* note 23, at 23–24; Carroll, *supra* note 32; Panel Discussion, *Money Laundering, Cybercrime and Currency Manipulations*, 11 U.S.-MEX. L.J. 219, 226 (2003) [hereinafter Panel Discussion]; DON LIDDICK, THE GLOBAL UNDERWORLD: TRANSNATIONAL CRIME AND THE UNITED STATES 68 (2004).

36. *See* Fletcher N. Baldwin, Jr., *Organized Crime, Terrorism, and Money Laundering in the Americas*, 15 FLA. J. INT'L L. 3 (2002) (quoting an immigrant who patronized a Hong Kong based IVTS: "The Bank of China took three weeks, charged a bad foreign exchange rate, and delivered the cash in yen. Sister Ping delivered the money in hours, charged less, and paid in American dollars. It was a better service.").

37. PASSAS, *supra* note 23, at 22. For example, in Afghanistan, even aid agencies use the IVTS systems to transfer funds. *Symposium*, *supra* note 29, at 80.

38. PASSAS, *supra* note 23, at 14.

> [If the client wishes] to pick up the money herself in the other country . . . a code will be given to the client for reference to the "banker" in the country where the pick-up is to take place. This code will be communicated in the meantime by fax or telephone to the hawaladar responsible for the payment . . . . The client will hand over to the local broker the amount she

The lack of a paper trail, strong cultural ties, and emphasis on trust and confidentiality make these systems especially difficult for governments to regulate. IVTS were generally left alone until the U.S. launched its "war against terror" in the wake of 9-11.[39]

III. POST 9-11 LEGISLATION APPLYING TO IVTS

In response to the 9-11 attacks, the United Nations Security Council called upon all member states to "redouble their efforts to prevent and suppress terrorist acts"[40] and take measures to prevent terrorist financing.[41] Another international body, the Financial Action Task Force (FATF) issued Nine Special Recommendations on Terrorist Financing.[42] Also in 2001, the U.S. passed the USA PATRIOT Act,[43] the country's most overarching anti-money laundering legislation yet.[44] In 2005, Hong Kong passed the United Nations (Anti-Terrorism Measures) Ordinance, Chapter 575.[45]

> wishes to transfer either in advance or, in some cases, when assurance is given that the money has been received on the other end.

Id. For further discussion of Hawala mechanics, see Nikos Passas, *Hawala and Other Informal Value Transfer Systems: How to Regulate Them?*, http://usinfo.state.gov/eap/Archive_Index/Hawala_and_Other_Informal_Value_Transfer_Systems_How_to_Regulate_Them.html (last visited Jan. 22, 2006).

39. It wasn't until the war on drugs and anti-money laundering movement that Western countries began to see IVTS as a problem. PASSAS, *supra* note 23, at 3.

40. S.C. Res. 1368, U.N. SCOR, 4370th mtg., U.N. Doc. S/RES/1368 (Sept. 12, 2001), *available at* http://www.un.org/News/Press/docs/2001/sc7143.doc.htm.

41. S.C. Res. 1373, U.N. SCOR, 4385th mtg., U.N. Doc. S/RES/1373 (Sept. 28, 2001), *available at* http://www.un.org/News/Press/docs/2001/sc7158.doc.htm.

42. FIN. ACTION TASK FORCE ON MONEY LAUNDERING, *supra* note 2. In addition to the Special Recommendations focusing solely on terrorism, the FATF edited the 2003 version of the Forty Recommendations to delete specific references to drug offenses, thus expanding the application of the Forty Recommendations. Allison S. Bachus, *From Drugs to Terrorism: The Focus Shifts in the International Fight Against Money Laundering after September 11, 2001*, 21 ARIZ. J. INT'L & COMP. L. 835, 859–60 (2004); Joseph Wheatley**,** Comment, *Ancient Banking, Modern Crimes: How Hawala Secretly Transfers the Finances of Criminals and Thwarts Existing Laws*, 26 U. PA. J. INT'L ECON. L. 347, 371 (2005).

43. *See supra* note 4.

44. Panel Discussion, *supra* note 35, at 222 (quoting Charles Blau, former Chief of Narcotic and Dangerous Drug Section in the Criminal Division of the U.S. Department of Justice, "I think [the USA PATRIOT Act] was a compilation of items on the wish lists of the Justice and Treasury Departments that would never be passed in any normal setting . . . . There are many things in this Bill which are there because of 9/11 or the incidents following 9/11."). Even though "[t]he evidence in the 9-11 attacks shows that most of the funds received by the hijackers reached the US [sic] through formal financial institutions (e.g., wire transfers, credit card use)," PASSAS, *Hawala and Other Informal Value Transfer Systems: How to Regulate Them?*, *supra* note 38, the United States began, through the USA PATRIOT Act, to target IVTS as a major vehicle of terrorist financing. *Id.* (citing M. Ganguli, *A Banking System Built for Terrorism*, TIME MAGAZINE, Oct. 5, 2001).

45. *Supra* note 4, pmbl.

This part of the Note first discusses the anti-money laundering legislation of both the United Nations and the FATF. Second, this part explores how the domestic legislation of the U.S. and Hong Kong compares with the international requirements and recommendations.

A. International

There are many international groups active in the fight against money laundering. These include INTERPOL,[46] Europol,[47] the Basel Committee,[48] the Bank for International Settlements,[49] the Egmont Group,[50] and the International Chamber of Commerce.[51] There are also a number of FATF-style regional bodies that have observer status with the FATF.[52]

The Council of Europe,[53] the European Union,[54] and the Organization of American States[55] have also taken steps in the fight against money

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46. INTERPOL is an International Criminal Police Organization whose membership includes almost all states of the world. INTERPOL "exchanges and analyzes information, supply national police forces with data and analyses to recognize international criminal structures and connections, provides the tools that enable them to work together when something international has to be dealt with." Fulvio Attina, *Globalization and Crime: The Emerging Role of International Institutions* (Univ. of Catania Dep't of Political Studies, Jean Monnet Working Papers in Comparative and International Politics, JMWP07.97, 1997), *available at* http://www.fscpo.unict.it/EuroMed/jmwp07.htm (last visited Jan. 22, 2006).

47. Europol was established by the Maastricht Treaty Art. K.1.9 and is governed by the Europol convention. Europol requires every country to set up national intelligence service.

48. The Basel Committee includes eleven major industrialized nations and Luxembourg. In 1988, the Committee issued a Statement of Principles with advice to banks including a "know your customer" rule. In 1992, the Committee issued new Minimum Standards regarding government supervision and regulation of international banks and sanctions. Madelyn J. Daley, *Effectiveness of United States and International Efforts to Combat International Money Laundering*, 2000 St. Louis-Warsaw Trans'l 175, 185.

49. Basel Comm. on Banking Supervision, Customer Due Diligence for Banks (Oct. 2001), *available at* http://www.bis.org/publ/bcbs85.pdf.

50. The Edgmont group is a global enforcement mechanism linking Suspicious Activity Reports received by financial intelligence agencies in eighty-four countries. Bachus, *supra* note 42, at 855. For more information, see http://www.egmontgroup.org.

51. The International Chamber of Commerce issued a *Guide to Prevention of Money Laundering* in 1998. *See* Anti-corruption conventions and treaties, http://www.u4.no/document/treaties.cfm#3.

52. *See* FATF-GAFI, http://www.fatf-gafi.org (follow "About the FATF" hyperlink; then follow "Members and Observers" hyperlink) [hereinafter FATF Members and Observers) (listing FATF-style regional bodies, including the Council of Europe Select Committee of Experts on the Evaluation of Anti-Money Laundering Measures, the Eurasian Group, the Eastern and Southern Africa Group, the FATF in South America, and the Middle East and North Africa FATF); *see also* Money Laundering Website, http://www.anti-moneylaundering.org/ (last visited Jan. 22, 2006) (including links to domestic anti-money laundering legislation in over ninety jurisdictions); Bachus, *supra* note 42, at 853 (discussing the Caribbean FATF); Caribbean Financial Action Task Force, http://www.cfatf.org/default.asp (last visited Jan. 22, 2006).

53. The Council of Europe (an international organization formed in 1949 that currently has forty-

laundering. This part focuses on the United Nations and Financial Action Task Force.

1. United Nations

The United Nations first began to address the problem of money laundering through its efforts to combat the international drug trade and sales of illicit arms.[56] Through the Office of Drug Control and Crime Prevention, the United Nations established a Global Program Against Money Laundering with the aim "to help member states introduce

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seven member states) signed the Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime on November 11, 1990. The Convention requires signatories to implement domestic legislation criminalizing money laundering-related offenses in a variety of contexts. However, countries are not required to criminalize money laundering if doing so would conflict with the nation's constitution or legal system. Daley, *supra* note 48, at 187. Because the Convention specifies a mens rea of knowledge, it is difficult to apply the Convention to IVTS.

54. "The first concrete reference to money laundering within the European Union can be traced to the European Parliament Resolution of October 16, 1986, which urged the Council of Ministers, the EU's main decision-making organ, to take concerted action against all aspects of drug trafficking, including money laundering." Reuda, *supra* note 14, at 154. In 1991, the European Union (also called the Commission of European Communities) issued a directive requiring members to implement anti-money laundering legislation. Council Directive 91/308/EEC, Prevention of the Use of the Financial System for the Purpose of Money Laundering, 1991 O.J. (L 166).

55. The Organization of American States (OAS) references money laundering in its Inter-American Convention Against Terrorism. Inter-American Convention Against Terrorism art. 4, June 3, 2002, 42 I.L.M. 19 (2003).

56. Paul Kennedy, *Watching the Clothes Go Round: Combating the Effects of Money Laundering on Economic Development and International Trade*, 12 CURRENTS: INT'L TRADE L.J. 140, 146 (2003) (citing John Evans, *International Efforts to Contain Money Laundering* (Int'l Ctr. for Criminal Law Reform and Criminal Justice Policy, Vancouver, Can.), Apr. 8, 1997, http://www.icclr.law.ubc.ca/Publications/Reports/MoneyLaundering.PDF (last visited Aug. 15, 2007)). The 1988 United Nations Drug Convention acknowledges the importance of attacking the proceeds of criminal activity as a method of attacking the activity itself. Daley, *supra* note 48, at 182–83 (discussing United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, Dec. 20, 1988, 28 I.L.M. 493 (1989) (entered into force Nov. 11, 1990) [hereinafter U.N. Drug Convention]). Today there are more that 150 signatories to the Convention. Daley, *supra* note 48, at 184. The Convention imposes an obligation on parties to enact domestic legislation criminalizing money laundering activity but applies to the drug context only. Money laundering activity is defined as:

> 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;
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> 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;

U.N. Drug Convention art. 3(1)(b). For a detailed discussion of the U.N. Drug Convention, see Daley, *supra* note 48, at 182–85.

effective anti-money laundering legislation."[57] Among other things, the Global Program coordinates an International Money Laundering Information Network, which seeks to develop tools and mechanisms to combat money laundering, and enables member states to implement money laundering legislation by receiving aid.[58]

The 1999 United Nations Convention for the Suppression of the Financing of Terrorism (the "Convention") broadened the definition of money laundering offenders to include anyone who "unlawfully and wilfully, provides or collects funds with the intention that they should be used or in the knowledge that they are to be used" for certain terrorist activities.[59] The required mens rea of willful intent limits the application of the Convention in the IVTS context, where confidentiality is strongly respected.[60]

United Nations Resolution 1373 (adopted seventeen days after 9-11) imposed an obligation on all states "to respond to the global threat of terrorism."[61] The U.S. responded to the U.N. Resolution's requirement to "report back within 90 days on the steps taken to implement the resolution" by creating the USA PATRIOT Act.[62] Hong Kong's response came a little later, with the United Nations (Anti-Terrorism Measures) Ordinance, Chapter 575.[63]

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57. Kennedy, *supra* note 56, at 146. The developing world has a larger say in the UN than the FATF. *Id.*

58. *See* UNODC-Global Programme Against Money Laundering, http://www.unodc.org/unodc/money_laundering.html.

59. United Nations International Convention for the Suppression of the Financing of Terrorism art. 2, para. 1, Dec. 9, 1999, 39 I.L.M. 270 (2000) [hereinafter Convention for the Suppression of Terrorism Financing]. Other activities specified in the annex include: seizure of aircraft, acts against the safety of civil aviation, acts against internationally protected persons, hostage taking, acts against the protection of nuclear materials, violence at airports, acts against the safety of maritime navigation (piracy), acts against the safety of fixed platforms (oil and gas rigs), and terrorist bombings. *Id.* at annex. For further analysis of the Convention, see Baldwin, *supra* note 36, at 10–11.

60. However, the Convention for the Suppression of the Financing of Terrorism reiterates that the United Nations has "called upon all States to take steps to prevent and counteract, through appropriate domestic measures, the financing of terrorists and terrorist organizations, whether such financing is direct or indirect" and to consider adopting regulatory measures. Convention for the Suppression of Terrorism Financing, *supra* note 59, at pmbl.

61. *See* S.C. Res. 1368, *supra* note 40 (condemning 9/11 attacks and calling for global response to terrorism); S.C. Res. 1373, *supra* note 41 (calling for member states to take measures to prevent terrorist financing, creating a U.N. Counter-Terrorism Committee, and authorizing Security Council action to enforce the Resolution's objectives under Chapter 7 of the U.N. Charter).

62. Baldwin, *supra* note 36, at 12 (discussing paragraph 6 of Security Council Resolution 1373). The United Kingdom's Anti-Terrorism Crime and Security Act of 2001 was similar to the U.S. response to Resolution 1373. *Id.*

63. United Nations (Anti-Terrorism Measures) Ordinance, (2004) Cap. 575, pmbl. (H.K.).

2. Financial Action Task Force (FATF)

The FATF is an inter-governmental policy-making body "whose purpose is the development and promotion of national and international policies to combat money laundering and terrorist financing."[64] The FATF was established in 1989 by the G-7 Summit in Paris.[65] A year later, the FATF issued a set of Forty Recommendations, providing a comprehensive plan of action for combatting the problem of money laundering.[66] FATF membership has since expanded to include thirty-one countries and territories and two regional organizations.[67]

While the FATF recommendations are not legally binding, the Forty Recommendations are "the crown-jewel of soft law."[68] The effectiveness of the FATF recommendations stem from its penalties, which include severe trade consequences for uncooperative countries.[69]

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64. Financial Action Task Force (FATF), http://www.fatf-gafi.org (last visited Aug. 23, 2007) [hereinafter FATF Homepage]. The FATF is an investigative branch of the Organization for Economic Cooperation and Development (OECD). Perkel, *supra* note 32, at 186.

65. Financial Action Task Force (FATF), http://www.fatf-gafi.org (follow "About the FATF" hyperlink). In 1989, the G-7 consisted of the United States, United Kingdom, France, Germany, Italy, Japan, and Canada. Also involved in the Summit were the Commission of European Communities and eight other countries (Sweden, The Netherlands, Belgium, Luxembourg, Switzerland, Austria, Spain, and Australia). FIN. TASK FORCE ON MONEY LAUNDERING, REPORT 3, http://www.fatf-gafi.org/dataoecd/20/16/33643019.pdf.

66. Financial Action Task Force (FATF), http://www.fatf-gafi.org (follow "40 Recs" hyperlink). The Forty Recommendations "encourage countries to adopt various provisions with regard to financial institutions, including increased due diligence requirements, reporting of suspicious transactions, and mutual assistance with other nations regarding money laundering investigations." G. Scott Dowling, *Fatal Broadside: The Demise of Caribbean Offshore Financial Confidentiality Post USA PATRIOT Act*, 17 TRANSNAT'L L. 259, 283 (2004).

67. Financial Action Task Force (FATF), http://www.fatf-gafi.org (follow "About the FATF" hyperlink; follow "Members and Observers" hyperlink). The two regional organizations are the European Commission and the Gulf Co-operation Council. *Id.*

68. Bachus, *supra* note 42, at 848 (citing GUY STESSENS, MONEY LAUNDERING: A NEW INTERNATIONAL LAW ENFORCEMENT MODEL 11 (James Crawford & David Johnson eds., 2000)). Bachus continues that the FATF is "widely recognized by governments and international organizations as the world's preeminent counter-laundering body, and its policies are looked to as a source of customary international law." Bachus, *supra* note 42, at 848 (citing Jesse S. Morgan, *Dirty Names, Dangerous Money: Alleged Unilateralism in U.S Policy on Money Laundering*, 21 BERKELEY J. INT'L L. 771, 782 (2003)).

69. *See* FIN. ACTION TASK FORCE, ANNUAL AND OVERALL REVIEW OF NON-COOPERATIVE COUNTRIES OR TERRITORIES (June 10, 2005), http://www.fatf-gafi.org/dataoecd/41/26/34988035.pdf (blacklisting non-cooperative countries). For further discussion on the ability of the FATF to coerce offshore jurisdictions into adopting its recommendations through disastrous effects on their economies, see Vaughn E. James, *Twenty-First Century Pirates of the Caribbean: How the Organization for Economic Cooperation and Development Robbed Fourteen CARICOM Countries of their Tax and Economic Policy Sovereignty*, 34 U. MIAMI INTER-AM. L. REV. 1 (2002) and G. Scott Dowling, *Fatal Broadside: The Demise of Caribbean Offshore Financial Confidentiality Post USA PATRIOT Act*, 17 TRANSNAT'L L. 259, 281 (2004).

After 9-11, the FATF issued a set of "9 Special Recommendations on Terrorist Financing."[70] Special Recommendations VI applies the Forty Recommendations to IVTS.[71] Specifically, the "Know Your Customer" identity requirements,[72] record keeping requirements,[73] and licensing and registration requirements[74] now apply to IVTS. In addition, jurisdictions may impose sanctions on those who fail to comply.[75] The goal of these requirements is to enhance the integrity and transparency of IVTS.

However, "[it] remains to be seen whether this approach, treating [IVTS] as though they were formal financial institutions . . . will produce the desired results."[76] According to INTERPOL, there is "no evidence . . . to support the conceptualization of [IVTS] as organized, hierarchical networks."[77] Most countries have been reluctant to accept the Special Recommendations in full. Enforcers are questioning whether transparency and accountability are desireable. "Who wants it?"[78] The reform efforts of Khalid Mirza, Pakistani Securities and Exchange Commission Chairman, "led to street protests by brokers who accuse him of being an 'American Agent.'"[79]

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70. *See* S.C. Res. 1368, *supra* note 40. FIN. ACTION TASK FORCE ON MONEY LAUNDERING, SPECIAL RECOMMENDATIONS ON TERRORIST FINANCING (Oct. 22, 2004), *available at* http://www.fatf-gafi.org/dataoecd/8/17/34849466.pdf. In addition to the Special Recommendations focusing solely on terrorism, the FATF edited the 2003 version of the Forty Recommendations to delete specific references to drug offenses, thus expanding the application of the Forty Recommendations. Bachus, *supra* note 42, at 859–60; Wheatley**,** *supra* note 42.

71. *See* Fin. Action Task Force, Interpretative Note to Special Recommendation VI: Alternative Remittance, http://www.fatf-gafi.org/dataoecd/53/34/34262291.PDF [hereinafter FATF Interpretative Note] (last visited Jan. 22, 2006). In particular, IVTS are subject to the Special Recommendations, as well as Recommendations 10 to 21 and 26 to 29 of the Forty Recommendations. The FATF Forty Recommendations on Money Laundering cover "know your customer" reporting requirements in Recommendation 10. *See* FIN. ACTION TASK FORCE ON MONEY LAUNDERING, THE FORTY RECOMMENDATIONS 4–5 (June 20, 2003), http://www.fatf-gafi.org/dataoecd/7/40/34849567.PDF [hereinafter FORTY RECOMMENDATIONS].

72. Recommendation 10. FORTY RECOMMEDATIONS, *supra* note 71, at 4–5.

73. Recommendation 12. *Id*. at 5.

74. Recommendation 23. *Id*. at 7.

75. FATF Interpretative Note, *supra* note 71, at 1. Countries with IVTS that fail to comply with the required FATF Recommendations or operate without a license or registration will be blacklisted as non-cooperative countries. *Id*.

76. *Symposium*, *supra* note 29, at 92.

77. *Id.* (quoting Carroll, *supra* note 32).

78. *Id.* (quoting Richard Behar, *Kidnapped Nation*, FORTUNE, Apr. 29, 2002, at 84).

79. *Symposium*, *supra* note 29, at 92.

B. United States

1. Background: Pre 9-11 Legislation

The 1986 Money Laundering Control Act was limited in scope.[80] It criminalized financial transactions involving proceeds from specified illegal activities and penalized the "transfer" of laundered money across U.S. borders.[81] The first comprehensive congressional money laundering legislation, the 1970 Bank Secrecy Act (BSA),[82] introduced three required forms. Together, these forms created a paper trail from which law enforcement officials could trace money laundering activity.[83] Suspicious Activity Reports (SARs) were introduced in 1996.[84] "Know Your Customer" reporting requirements were introduced and then abandoned in 2000.[85] Prior to 9-11, "anti-money laundering proposals were at a virtual standstill in Congress due to strong lobbying by the banking industry."[86]

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80. 18 U.S.C. § 1956(a)(2). The Money Laundering Control Act is codified at 18 U.S.C. § 1956-7. To fall under the requirements of the Money Laundering Control Act, currency transactions must meet three requirements: the money must come from "criminally derived property"; the amount must exceed $10,000; and the money must cross a U.S. border. Daley, *supra* note 48, at 189.

For a detailed discussion of the Money Laundering Control Act, see Helesa K. Lahey, *Money Laundering*, 42 AM. CRIM. L. REV. 699 (2005). The reporting requirement for U.S. businesses taking in more than $10,000 cash was first instituted in 1984. IRS Form 8300; I.R.C. § 6050I (1984). *See also* Internal Revenue Service Overview-Money Laundering, http://www.irs.gov/compliance/enforcement/article/0,,id=112999,00.html (last visited Jan. 22, 2006); Panel Discussion, *supra* note 35, at 219–22.

81. The penalized legal activities included embezzlement, narcotics, and fraud.

82. Internal Revenue Service History-Money Laundering, http://www.irs.gov/compliance/enforcement/article/0,,id=113001,00.html (last visited Jan. 22, 2006) [hereinafter IRS Money Laundering]; Panel Discussion, *supra* note 35, at 219–22.

83. IRS Money Laundering, *supra* note 82. The first required form is the Currency Transaction Report (Int. Rev. Form 4789). The Currency Transaction Report identifies owners and parties in interest of the account and the type of currency. Under the Bank Secrecy Act, banks are required to file Currency Transaction Reports for transactions over $10,000. 31 U.S.C. § 5313 (2000). Currency Transaction Reports extend to "hybrid hawala dealers" but not to normal IVTS. Perkel, *supra* note 32, at 197.

The second required form is the Report of International Transportation of Currency or Monetary Instruments (Int. Rev. Form 4790). This form requires reporting to U.S. Customs when more than $10,000 crosses U.S. borders.

The third required form is the Report of Foreign Bank and Financial Accounts (FBAR, Form TD F90-22.1). This form requires filing for customers who own an active foreign bank account. 31 U.S.C. § 5314 (2000). Since 1976, U.S. case law has enforced a mens rea for lawyers supporting money laundering transactions of willful blindness. Under the willful blindness standard, "if you close your eyes to the facts that should have alerted you, you can be convicted of having the requisite knowledge." Panel Discussion, *supra* note 35, at 224 (citing United States v. Jewell, 532 F.2d 697 (9th Cir. 1976), *cert. denied*, 426 U.S. 951 (1976)).

84. Rueda, *supra* note 14, at 167. "The Treasury Department must process between 60,000 and 80,000 of these reports each year." *Id.*

85. Under the "Know Your Customer" regulations, banks were required to

establish the true identity of their customers (including beneficial owners); determine the

2. Post 9-11 Legislation: The USA PATRIOT Act

Title III of the USA PATRIOT Act[87] ended the anti-money laundering legislative standstill by introducing "the most significant package of anti-money laundering measures in more than a decade."[88] It codified the International Money Laundering Abatement and Anti-Terrorist Financing Act of 2001 and dealt primarily with banks.[89]

Title III is also significant for being the first piece of U.S. legislation to address IVTS. Section 359

> (a) extends recordkeeping and reporting requirements to IVTS businesses;[90]

> customer's source of funds; determine the customer's normal and expected types of transactions; monitor customer transactions to determine whether they are consistent with the customer's 'profile'; and determine whether a transaction is unusual and suspicious and requires the filing of a SAR.

Id. The "Know Your Customer" regulations were abandoned "after receiving 200,000 negative public comments. . . . However, the September 11 events muted industry criticism," and the "Know Your Customer" rules were revived in the USA PATRIOT Act. *Id. See also* 31 U.S.C. § 5318.

86. Bachus, *supra* note 42, at 857 (citing Jackie Johnson, *11th September, 2001: Will It Make a Difference to the Global Anti-Money Laundering Movement?*, 8 J. Money Laundering Control 9, 10 (2002)).

87. Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act (USA PATRIOT Act), Pub. L. No. 107-56, 115 Stat. 272 (2001).

88. David R. Sahr & Daniel Morales, *U.S. Anti-Money Laundering Legislation*, 8 NAFTA L. & BUS. REV. AM. 583, 584 (2002).

89. "About 90% of the Act deals with banks and the manner in which currency is financially handled." Panel Discussion, *supra* note 35, at 222. For an in-depth discussion of the USA PATRIOT Act's application to financial institutions, see Sahr & Morales, *supra* note 88. The Act holds U.S. banks to a higher standard for gathering and keeping information about clients. *Id.* The Act extends the BSA requirements from only banks to insurance companies, mutual funds, broker-dealers, shell banks, pass-through and correspondent accounts, and a "host of other entities that are considered to be financial institutions for various purposes." Panel Discussion, *supra* note 35, at 222 (citing USA PATRIOT Act § 321); 31 U.S.C. § 5312(2)(E) (2000); Rueda, *supra* note 14, at 183; Sahr & Morales, *supra* note 88. The Act also expands criminal statues to cover additional money laundering offenses, such as bribing foreign officials.

90. This is done by including IVTS in the definition of "financial institution." The recordkeeping and reporting requirements are specified in 31 U.S.C. § 5318. They include Suspicious Activity Reporting Requirements under 31 U.S.C. § 5318(g), and additional record-keeping and reporting requirements for transfers over $3,000 and $10,000. Perkel, *supra* note 32, at 194. 31 U.S.C. § 5312(a)(2) defines "financial institution" for subchapter II "Records and Reports on Monetary Instruments Transactions" as

> a licensed sender of money or any other person who engages as a business in the transmission of funds, including any person who engages as a business in an informal money transfer system or any network of people who engage as a business in facilitating the transfer of money domestically or internationally outside of the conventional financial institutions system.

31 U.S.C. § 5312(a)(2)(R) (2000).

(b) requires IVTS businesses to register information with the Secretary of the Treasury;[91]

(c) establishes penalties for unauthorized participation;[92] and

(d) resolves to reconsider the issue in one year.[93]

3. Jurisdiction, Mens Rea, and Enforcement

IVTS are subject to U.S. jurisdiction where "(a) the investigation which gave rise to the summons is being or has been carried on; (b) the person summoned is an inhabitant; or (c) the person summoned carries on business or may be found, to compel compliance with the summons."[94] IVTS may also be subject to extraterritorial jurisdiction.[95]

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91. This is done by including IVTS in the definition of "money transmitting business." A "money transmitting business," for the purposes of section 5330 registration requirements, includes any business that

> provides check cashing, currency exchange, or money transmitting or remittance services, or issues or redeems money orders, travelers' checks, and other similar instruments or any other person who engages as a business in the transmission of funds, including any person who engages as a business in an informal money transfer system or any network of people who engage as a business in facilitating the transfer of money domestically or internationally outside of the conventional financial institutions system.

31 U.S.C. § 5330(d)(1)(A) (2000). 31 U.S.C. § 5330(b) requires money transmitting businesses to register their name, location, information about each of their agents, and other information with the Secretary of the Treasury. All money transmitting business are required to register with FinCEN and comply with existing banking regulations. *Id.*

Additionally, the prohibition of unlicensed money transmitting businesses in 18 U.S.C. § 1960 now applies to IVTS. "Whoever knowingly conducts, controls, manages, supervises, directs, or owns all or part of an unlicensed money transmitting business, shall be fined in accordance with this title or imprisoned not more than five years, or both." *Id.*

A five-year penalty is imposed for operating an unregulated currency transaction business. USA PATRIOT Act § 373, 18 U.S.C. § 1960(a) (2000). It appears that the rules under the Bank Secrecy Act applying to "money transmitting businesses" could now also apply to IVTS via this section.

92. The penalty is a fine up to $1,000,000 or five years imprisonment. USA PATRIOT Act § 359 extends the applicability of rules promulgated under the Federal Deposit Insurance Act, 12 U.S.C. § 1829b, to such persons. *See also* 31 C.F.R. § 103.41 (2000).

93. Congress will consider the need for additional legislation and whether or not to lower the suspicious transaction reporting requirements. USA PATRIOT Act, Pub. L. No. 107-56, § 359(d), 115 Stat. 272 (2001) (cross-referencing to 31 U.S.C. § 5318(g) specifying suspicious transaction reports). *See* 31 U.S.C. § 5311 (2000) (deadline).

94. 31 U.S.C. § 5318(e)(2) (2000). Under the Money Laundering Control Act of 1986, long-arm jurisdiction extends over U.S. citizens "world wide, regardless of whether any part of this transaction ever touched the U.S." Panel Discussion, *supra* note 35, at 236 (citing 18 U.S.C. § 1956(f) (providing extraterritorial jurisdiction over U.S. citizens and national jurisdiction for transactions over $10,000)). The USA PATRIOT Act provides for long-arm jurisdiction over foreign money launderers and extraterritorial jurisdiction. Section 317 of the USA PATRIOT Act amended 18 U.S.C. § 1956(b)(2) to provide for jurisdiction over a foreign person who

> (A) . . . commits an offense . . . involving a financial transaction that occurs in whole or in

To convict an offender of money laundering, the government must prove four elements: "(i) knowledge, (ii) the existence of proceeds derived from a specified unlawful activity, (iii) a financial transaction, and (iv) intent."[96] The mens rea of intent or knowledge is relaxed to "willful blindness" in some circuits.[97]

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part in the United States;

(B) the foreign person converts, to his or her own use, property in which the United States has an ownership interest . . . ; or

(C) the foreign person is a financial institution that maintains a bank account at a financial institution in the United States.

Thus, "funds illegally obtained in the U.S. or that have been transformed into an asset in the U.S. or laundered through a U.S. financial institution" are subject to U.S. jurisdiction. Rueda, *supra* note 14, at 189. USA PATRIOT Act § 377 amended 18 U.S.C. § 1029 to extend long-arm jurisdiction over "access devices" affiliated with U.S. entities and where some part of the transaction touches the territorial jurisdiction of the United States. "Access devices" are defined as

> any card, plate code, account number, electronic serial number, mobile identification number, personal identification number, or other telecommunications service, equipment, or instrument identifier, or other means of account access that can be used, alone or in conjunction with another access device, to obtain money, goods, services, or any other thing of value, or that can be used to initiate a transfer of funds (other than a transfer originated solely by paper instrument).

18 U.S.C. § 1029(e)(1) (2000).

95. If the IVTS definition of "financial institution" also extends to the use of the term in 18 U.S.C. § 1029(h)(1) ("the offense involves an access device issued, owned, managed, or controlled by a *financial institution*, account issuer, credit card system member, or other entity within the jurisdiction of the United States" (emphasis added)), then

> [a]ny person who, outside the jurisdiction of the United States, engages in any act that, if committed within the jurisdiction of the United States, would constitute an offense under subsection (a) or (b) of this section regarding counterfeit access devices, shall be subject to the fines, penalties, imprisonment, and forfeiture provided in [title 18] . . . .

18 U.S.C. § 1029(h) (2000).

96. Lahey, *supra* note 80, at 706 (citing 18 U.S.C. §§ 1956–57 (2002)).

97. The plain language of the Money Laundering Control Act requires knowledge of the offender. This knowledge can be either knowledge of "a monetary transaction in illegally derived property" or "knowledge of a specified unlawful activity." *Id.*

However, some circuits have allowed a "willful blindness" standard, assuming that Congress intended the definition of knowledge to be so broad. *Id*. at 707 (citing 18 U.S.C. §§ 1956–57 (2002)). These circuits include the First, Second, Fourth, and Eighth. *Id*. at 707–08.

Applied to IVTS, the requirements of the 1986 Act raise several issues: "unlawful activity," mens rea of knowledge or intent, and "proceeds." *See* Perkel, *supra* note 32, at 191.

> The IMLAFA [USA PATRIOT Act Title III] amendments did not explicitly change any of the elements required to prove a money laundering offense, and no court has cited the IMLAFA amendments in interpreting the required elements of a money laundering offense. However, the enhanced reporting requirements imposed by the IMLAFA amendments might be construed by future courts as setting a new bar in determining willful blindness. In particular, courts may allow a failure to comply with reporting requirements to constitute circumstantial evidence of illicit financial activity.

Lahey, *supra* note 80, at 708.

U.S. enforcement is conducted by the U.S. Department of Treasury's financial intelligence unit, called the Financial Crimes Enforcement Network (FinCEN).[98]

C. Hong Kong

1. Background: Pre 9-11 Legislation

Money laundering was criminalized in Hong Kong in 1989.[99] Hong Kong uses the term "Unregulated Remittance Centers" (URC) to describe the local equivalent of IVTS.[100] As late as 1999, no URC had been charged with money laundering violations, primarily due to the high mens rea, requiring proof that the agent "knew or believed" that the money came from an illegal source.[101] Most URCs carry out transactions without inquiring into the source of the money and thus do not meet this high mens rea. Generally, "URCs are used by money launderers, rather than being money launderers themselves."[102] Attempts to get URCs to conform to tax laws and administrative guidelines, "such as customer identification, record-keeping and reporting of suspicious transactions" have largely failed.[103]

2. Post 9-11 Legislation: HK Chapter 575

In 2005, Hong Kong adopted Chapter 575, the United Nations (Anti-Terrorism Measures) Ordinance (HK Chapter 575), in response to U.N. Security Council Resolution 1373, as well as other international terrorist

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98. Rueda, *supra* note 14, at 163. FinCEN operates the world's largest computerized financial transaction system. *Id.* at 162. Only Australia has a comparable system. *Id*. at 192. Other enforcement mechanisms include Mutual Legal Assistance Treaties. Daley, *supra* note 48, at 193; Rueda, *supra* note 14, at 169 (citing U.S. Dep't of State, *Mutual Legal Assistance Treaties and Other Agreements*, http://travel.state.gov/mlat.html (last visited Jan. 22, 2006)).

Sting operations have generally been quite successful. They are key to enforcement but are subject to some limitations, such as the entrapment defense. Rueda, *supra* note 14, at 193–94. "Operation Green Quest," a multi-agency financial enforcement initiative, operates through the U.S. Treasury and coordinates law enforcement among "the Federal Bureau of Investigation, the Central Intelligence Agency, the U.S. Secret Service, the Customs Service, the Internal Revenue Service Criminal Division, and the Department of Justice." Perkel, *supra* note 32, at 186.

99. PASSAS, *supra* note 23, at 60.

100. *Id.*

101. *Id.*

102. *Id.* at 61.

103. Proposed legislation suggests imposing a duty on URC agents to identify customers and keep proper records with a fine for non-compliance, on-site inspections by the Hong Kong police, and possibly amending the wording of the legislation to use terms other than "know" or "believe." *Id.*

treaties "to implement certain of the Special Recommendations on Terrorist Financing of the Financial Action Task Force."[104]

Section 7 of HK Chapter 575[105] prohibits providing or collecting funds, "directly or indirectly" with intent or knowledge that the funds will be used to commit a terrorist act.[106] Section 8 prohibits making funds available, directly or indirectly, to anyone the transmitter "knows or has reasonable grounds to believe is a terrorist or terrorist associate," but is not yet in operation.[107]

3. Jurisdiction, Mens Rea, and Enforcement

Violators of section 7 or section 8 (when it comes into force) are subject to territorial and national jurisdiction.[108]

While section 7 does not specifically target URCs, the criminalizing of any "indirect" provision of funds suggests that URCs could also be found to be in violation of the statute. However, the high mens rea of "intention" or "knowledge" in section 7 is similar to the old standard of "knew or believed" that failed to effectively monitor URCs. Since URCs are infamous for respecting customer confidentiality, they are unlikely to "knowingly" or "intentionally" transfer funds. Thus, URC businesses that do not question the source or use of the money they transmit are effectively shielded from liability. Section 8 contains a more relaxed mens rea standard of "knows or has reasonable grounds to believe;" however, section 8 is not yet in force.

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104. United Nations (Anti-Terrorism Measures) Ordinance, (2004) Cap. 575, pmbl. (H.K.), *available at* http://www.legislation.gov.hk.eng/index.html.

105. Section 7 is titled "Prohibitions relating to Terrorists, Terrorist Associates and Terrorist Property." *Id.* § 7.

106. The language reads: "(a) with the intention that the funds be used; or (b) knowing that the funds will be used, in whole or in part, to commit one or more terrorist acts (whether or not the funds are actually so used)." For the definitions of "terrorist," "terrorist associates," "terrorist property," and "terrorist acts," see section 2. For an inclusive list of funds, see schedule 1 of the United Nations (Anti-Terrorism Measures) Ordinance.

107. Section 8 reads:

> No person shall, except under the authority of a licence granted by the Secretary, make any funds or financial (or related) services available, directly or indirectly, to or for the benefit of a person who the first-mentioned person knows or has reasonable grounds to believe is a terrorist or terrorist associate.

Id. § 8.

108. Offenses under sections 7, 8, 9, 10, 11B, and 11F subject to jurisdiction as provided in section 3 of the Ordinance covering "(a) any person within the HKSAR [Hong Kong Special Administrative Region]; and (b) any person outside the HKSAR who is (i) a Hong Kong permanent resident; or (ii) a body incorporated or constituted under the law of the HKSAR." *Id.* § 3.

HK Chapter 575, which was enacted to implement "certain," but not all of the FATF Special Recommendations, does not appear to include Special Recommendation VI.[109] Therefore, targeting URCs under the current statutory system would be difficult.

Although Hong Kong's legislation does not target URCs, Hong Kong is not ignoring the problem. [110] Hong Kong has identified a "noticeable immigration/ethnic related underground sector," and had registered 1373 URCs as of March 2005.[111] Hong Kong's enforcement agency, the Financial Intelligence Unit (FIU), has been authorized to check criminal records and conduct on-site visits. Transactions over HKD 20,000 (USD 2500) are subject to reporting requirements, including Suspicious Transaction Reports. Such records are kept for six years.[112] Sanctions include warnings and prosecution. Money transmitters who use formal banking channels are required to register details of the bank accounts utilized.[113]

IV. COMPARING U.S. AND H.K. ANTI-MONEY LAUNDERING LEGISLATION AS APPLIED TO IVTS, CONSIDERING FATF SPECIAL RECOMMENDATION VI

Although U.S. legislation and H.K. legislation were both enacted to combat terrorist financing, the U.S. legislation is more comprehensive and farreaching. To show this in the IVTS context, I compare the USA PATRIOT Act and HK Chapter 575 with reference to three specific points: (1) the application of such legislation to underground banking systems (IVTS/URCs); (2) jurisdiction over money laundering offenses; and (3) the mens rea of the crime. While the USA PATRIOT Act closely adheres to FATF Special Recommendation VI, HK Chapter 575 does not.

A. IVTS-Specific Legislation

Compared to HK Chapter 575, the USA PATRIOT Act is more comprehensive. Section 359 of the USA PATRIOT Act addresses underground banking systems specifically, extending obligations that include recordkeeping, reporting, and registration requirements while

109. *Id*. pmbl.
110. *See* FATF TYPOLOGIES REPORT, *supra* note 32, at 3–40.
111. *Id.*
112. Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act (USA PATRIOT Act), Pub. L. No. 107-56, § 359, 115 Stat. 272 (2001).
113. *Id.*

imposing sanctions of fines and imprisonment for noncompliance. While the definitions of specific terms in Title III and Special Recommendation VI differ slightly,[114] these measures are closely in line with the three core elements underlying FATF Special Recommendation VI on Alternative Remittance.[115]

In contrast, HK Chapter 575 does not specifically mention underground banking. Theoretically, URCs could be charged under the general scheme of providing funds to terrorists; however, the high mens rea allows URCs to remain unaffected. The suggestion of a lesser mens rea for the offense of making funds available to terrorists in section 8 is not yet in force.[116] Even if Hong Kong were to enact comprehensive legislation requiring record-keeping or reporting requirements, the majority of URCs would not comply with such regulations.[117] HK Chapter 575 does contain sanctions, but without URC charges, these sanctions do not apply.

B. Jurisdiction over IVTS Offenses

Title III of the USA PATRIOT Act has a broader jurisdictional reach than HK Chapter 575 because it extends extraterritorial jurisdiction over

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114.

> *Money or value transfer service* refers to a financial service that accepts cash, cheques, other monetary instruments or other stores of value in one location and pays a corresponding sum in cash or other form to a beneficiary in another location by means of a communication, message, transfer or through a clearing network to which the money/value transfer service belongs. Transactions performed by such services can involve one or more intermediaries and a third party final payment.

FATF Interpretative Note, *supra* note 71, at 1. "Alternative remittance services" is defined as

> [a] money or value transfer service [that] may be provided by persons (natural or legal) formally through the regulated financial system or informally through non-bank financial institutions or other business entities or any other mechanism either through the regulated financial system (for example, use of bank accounts) or through a network or mechanism that operates outside the regulated system. In some jurisdictions, informal systems are frequently referred to as *alternative remittance services* or *underground* (or *parallel*) *banking systems.*

Id. at 1–2. "Licensing" is defined as "a requirement to obtain permission from a designated competent authority in order to operate a money/value transfer service legally." *Id*. at 2. "Registration" is defined as "a requirement to register with or declare to a designated competent authority the existence of a money/value transfer service in order for the business to operate legally." *Id*. The FATF Special Recommendations do not require that jurisdictions "impose a separate licensing/ registration system or designate another competent authority in respect to persons . . . already licensed or registered as financial institutions . . . ." *Id.*

115. The first core element requires licensing or registration for IVTS businesses. The second element seeks to enforce the FATF Forty Recommendations and Eight Special Recommendations against IVTS, and the third core element imposes sanctions on IVTS that fail to comply. *Id*. at 2.

116. *See supra* note 106 and accompanying text.

117. PASSAS, *supra* note 23, at 61.

specified offenses.[118] HK Chapter 575 only covers territorial and national jurisdiction.[119] If the definition of "financial institution" does not apply equally to multiple sections of the U.S. Code (specifically Title 31 and Title 18),[120] then IVTS under the USA PATRIOT Act section 359 are only subject to territorial and national jurisdiction under Title 31, with language almost identical to Hong Kong's Ordinance section 3.[121]

C. Mens Rea

Finally, the mens rea required by U.S. and Hong Kong anti-money laundering legislation both discuss "intent" and "knowledge." However, the language of HK Chapter 575 reads intent *or* knowledge and the U.S. language reads intent *and* knowledge.[122] The proposal to lower the mens rea in HK Chapter 575 to "knows or has reasonable grounds to believe"[123] is similar to the "willful blindness" standard used by some U.S. circuit courts.[124] A lower mens rea would help Hong Kong target URCs, especially in the absence of a statutory scheme specific to URCs, in a way comparable to that under the USA PATRIOT Act section 359.

V. ANALYSIS: WHILE U.S. LEGISLATION BEST CONFORMS WITH FATF RECOMMENDATION VI, SUCH A HIGH STANDARD IS NOT CURRENTLY REQUIRED INTERNATIONALLY

Both the United States and Hong Kong enacted new anti-money laundering legislation in response to a heightened awareness of the dangers of terrorist financing after 9-11. However, the U.S. legislation is more comprehensive than Hong Kong's legislation in several ways. First, the USA PATRIOT Act specifically addresses IVTS, while HK Chapter 575 does not mention underground banking at all. Second, the USA PATRIOT Act has a broader jurisdictional reach. Third, the USA PATRIOT Act uses a different standard for mens rea.

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118. *See supra* note 94 and accompanying text.

119. United Nations (Anti-Terrorism Measures) Ordinance, (2004) Cap. 575, § 3 (H.K.).

120. *See supra* note 94 and accompanying text (discussing the IVTS definition of "financial institution").

121. *Compare* 31 U.S.C. § 5318(e)(2) *with* United Nations (Anti-Terrorism Measures) Ordinance § 3.

122. It also requires the existence of proceeds and a financial transaction. 18 U.S.C. §§ 1956–57.

123. United Nations (Anti-Terrorism Measures) Ordinance § 8.

124. *See supra* note 122 and accompanying text. Circuits include the First, Second, Fourth, and Eighth. *See also* Lahey, *supra* note 80, at 707–08.

The approach taken by the United States is closely aligned with that of the FATF. This approach is the highest international standard for regulating underground banking. Although Hong Kong has not met this high standard, Hong Kong still maintains the FATF membership that it has held since 1990 and has not been blacklisted. Evidently, the FATF is not demanding that current members strictly comply with all of its standards but rather allows a discrepancy.[125] Domestic legislation that closely follows the FATF approach toward underground banking is currently the exception rather than the rule.[126]

Furthermore, prospective members are not required to enact comprehensive legislation.[127] The requirements for China to convert their FATF status from observer to member do not include the enactment of legislation to target underground banking.[128]

VI. CONCLUSION

Following the 9-11 attacks' graphic demonstration of the dangers of terrorist financing, the world began to first address the long ignored phenomenon of underground banking. The U.N. called upon member states to take steps to respond to "the global threat of terrorism."[129] The FATF introduced 9 Special Recommendations on Terrorist Financing.

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125. It is important to note, however, that Hong Kong is not ignoring the problem of money laundering. *See* FATF TYPOLOGIES REPORT, *supra* note 32, at 38.

126. *See supra* note 97.

127. To be admitted to the FATF, a country must

> be fully committed at the political level to implement the Forty Recommendations within a reasonable time frame (three years) and to undergo annual self-assessment exercises and two rounds of mutual evaluations; 2) be a full and active member of the relevant FATF-style regional body; 3) be a strategically important country; 4) have already made the laundering of the proceeds of drug trafficking and other serious crimes a criminal offense; and 5) have already made it mandatory for financial institutions to identify their customers and to report unusual or suspicious transactions.

JAMES K. JACKSON, CRS REPORT FOR CONGRESS, THE FINANCIAL TASK FORCE: AN OVERVIEW (2005), *available at* http://www.fas.org/sgp/crs/terror/RS21904.pdf.

128.

> The final membership requirement is that China undergo an FATF mutual evaluation in which it demonstrates satisfactory compliance with key FATF Recommendations relating to the criminalization of money laundering and terrorist financing (Recommendation 1 and Special Recommendation II), customer identification and due diligence (Recommendation 5), record keeping (Recommendation 10) and suspicious transaction reporting (Recommendation 13 and Special Recommendation IV). The date for China's mutual evaluation has not yet been set.

FATF 2004–2005 ANNUAL REPORT, *supra* note 1, at 7; *see also* PASSAS, *supra* note 23, at 61 ("IVTS bring value into China, rather than the other way round.").

129. *See* S.C. Res. 1373, *supra* note 41.

Special Recommendation VI promotes a set of specific measures to target underground banking; however, enacting these measures is not required for FATF membership.[130] Because there is no binding international law on underground banking, it is currently up to individual countries to determine their own standards for regulating the problem. The United States and Hong Kong have both enacted legislation to respond to "the global threat of terrorism," but only the U.S. legislation addresses underground banking. The U.S. strategy is closely aligned with the FATF, but may not be effective. [131] Thus, while countries like Hong Kong and China should not be required to adopt the FATF Recommendation word-for-word, neither should they ignore the problem.[132] Underground banking is a significant vehicle for terrorist financing and only if countries work together can a global solution be reached.

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130. However, the FATF is not ignoring the problem of IVTS. In 2004–2005, the FATF dedicated resources to evaluating and analyzing the problem. In the *FATF Typologies Report*, the FATF dedicates much of the report to evaluating the IVTS problem. This includes monitoring the activities of current members in relation to IVTS. Included in this research is an analysis of the status of various countries on money laundering. The FATF's lack of pressure on countries to enact specific measures targeting IVTS suggests that the FATF is currently more concerned with information gathering than enforcing specific compliance. The FATF seems to recognize that monitoring ARS is a new phenomenon that may require further exploration to determine the best methods to combat the problem. FATF TYPOLOGIES REPORT, *supra* note 32.

131. There is no way to definitively know what works or how big a problem underground banking is. The FATF recognizes this and therefore is not demanding compliance with its recommendation.

The U.S. strategy to target IVTS has been to extend the regulations that have formerly applied to financial institutions. These regulations include currency transaction reports, customer identification requirements, and suspicious transaction reports. When applied to financial institutions, these regulations target the placement stage of the money laundering process (when funds are moved into a bank). However, it is unknown if these methods effectively transfer to IVTS. It remains to be seen if the U.S. and FATF guidelines are effective at targeting IVTS. For a discussion of recent USA PATRIOT Act cases, see Alicaia L. Rause, *USA PATRIOT Act: Anti-Money Laundering and Terrorist Financing Legislation in the U.S. and Europe Since September 11th*, 11 U. MIAMI INT'L & COMP. L. REV. 173, 176–77 (2003).

132. Instead, it would be wise for such countries to heed the main emphasis of the *2004–2005 Typologies Report* by staying informed of FATF reports and suggestions. In beginning to develop a strategy to target IVTS, countries should first seek to identify IVTS and assist with international cooperation on intelligence and investigation. The next step is to establish regulations and supervision that apply to IVTS. Countries should be prepared to enact legislation when the FATF determines what kind of legislation is effective, and what legislation it needs to require.

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