

Trade-Based Money Laundering: Trends and Developments

This joint FATF-Egmont report aims to help public and private sector with the challenges of detecting trade-based money laundering. Using numerous case studies from around the FATF's Global Network, it explains the ways in which criminals exploit trade transactions to move money, rather than goods. It highlights recommendations to address the trade-based money laundering risks. These include using national risk assessments and other risk-focused material to raise awareness with the public and private sector entities involved in international trade, improving information-sharing of financial and trade data, and cooperation between authorities and private sector, including through public-private partnerships.

Introduction

The report takes stock of current TBML risks, including the exploitation of new or existing methods of introducing illicit cash into the financial system. Despite the growth in technology-enabled payment methods, case studies highlight the reliance on Black Market Peso Exchange (BMPE). The report also notes other forms of illicit cash integration, such as the exploitation of surrogate shopping or the infiltration of legitimate supply chains

- Surrogate shoppers can act on behalf of wealthy individuals, who might face restrictions in purchasing higher-value goods because of stringent currency controls. One such example of this is known as Daigou (which literally means surrogate shopping) whereby individuals or syndicated groups of exporters outside Asian countries purchase mainly luxury goods for customers in those countries.
- This infiltration may not necessarily result in the subsequent growth of 'common TBML techniques. In some instances, nothing about the trading relationship changes, other than an increase in illicit cash integrated into the importing company. This and the exploitation of surrogate shopping are explored in more detail in the TBML risk and trends section of the report.

While there can be significant intersection between TBML or TBTF schemes and exploitation of shell or front companies, they do not feature in all TBML/TF schemes. When they are used, they can support the integration of funds, while providing an additional benefit of hiding the beneficial owners.

The report notes the continued occurrence of third-party intermediaries, often as part of the financial settlement process. These third-party intermediaries, linked to the OCG, PML or terrorist financier, can quickly integrate into the transaction chain, creating additional distance between their activities and the TBML or TBTF scheme.

While financial institutions were aware of the risks associated with third-party intermediaries, the report acknowledges that others in the supply chain, such as legitimate importers or

exporters, or those with an oversight role, such as auditors or accountants, may not question why an entirely unrelated third-party is involved in the payment settlement process.

The report aims to present complex issues in an accessible, easy-to-understand way. It has relevance to countries with already well-developed systems and processes to identify and disrupt TBML or TBTF, and to those starting on that journey because they have noted a growth in suspicious activity linked to trade transactions. It provides a toolkit of ideas and initiatives that have delivered impact in combatting TBML and TBTF schemes and these can be adapted by jurisdictions to suit their domestic circumstances. For example, if there are restrictions on the extent to which public and private sectors can share actionable ML or TF intelligence, any PPP can focus more on establishing a meaningful dialogue on strategic threat and risk understanding.

The overarching theme of the report is one of vigilance, with competent authorities, private sector institutions, and other participants in global supply chains encouraged to use the report as a guide.

Given the diversity of tradable goods and services, the involvement of multiple parties, and the speed of trade transactions, trade-based money laundering remains a profound and significant risk.

The report also provides fresh insight into TBTF to build awareness and understanding of how terrorist financiers can and do exploit trade processes.

Definitions and trade financing activities

The aim of trade-based money laundering is not the movement of goods, but the movement of money, which the trade transactions facilitate.

Trade-Based Money Laundering (TBML) is “the process of disguising the proceeds of crime and moving value through the use of trade transactions in an attempt to legitimise their illegal origin or finance their activities”.

Trade-Based Terrorist Financing (TBTF) is “disguising the movement of value through the use of trade transactions in an attempt to finance terrorism, whether from legitimate or illegitimate sources”.

Trade process and financing

Open account transactions - TBML schemes frequently involve this method because FIs have a reduced role, meaning less oversight than for the documentary collection process. FIs can struggle to accurately or consistently assess the legitimacy of the customer’s operations, whether through automated or manual transaction monitoring.

Documentary collections - In documentary collection, the exporter requests payment by presenting shipping and collection documents for the traded goods to its FI. The FI then forwards these documents to the importer's FI, who then transfers the funds to the exporter's FI, who will subsequently credit those funds to the exporter. FIs role is limited and documents are not always standardised, increasing the risk of TBML exploitation through fictitious or false invoicing.

However, TBML could be spotted by:

- Use of a personal email address in lieu of a legitimate business email
- Recycling of previous documentation with few or no edits, including something as basic as the date
- Lack of any trading presence of the exporter, following research by the FI

Risk-based approach to trade-based money laundering

Every country in the world is involved in trade. TBML or TBTF can therefore occur anywhere. Contributors noted that TBML/TF enabling activities – such as the misuse of corporate structures – can occur in a wide range of jurisdictions. Organised Crime Groups, Professional Money Launderers, and/or terrorist financiers exploit any potential loopholes or gaps.

Jurisdictions should adopt a risk-based approach to supervision and in the context of TBML, this might mean FIs with large trade finance divisions or significant cross-border payment activity require additional oversight from supervisory bodies to ensure the effectiveness of any threat mitigation strategy. Jurisdictions with specialist company formation sectors, in addition to accountancy service providers, should also consider the potential for these firms to be exposed to TBML or TBTF, again ensuring the robustness of any threat mitigation strategy.

Criminals exploit sectors, products, or businesses prone to gaps in, or the inconsistent application of, customer due diligence and know your customer processes across jurisdictions, which can be exacerbated by a nascent or limited understanding of TBML risk.

A handful of common themes conducive to TBML exploitation were identified:

- Goods with wide pricing margins;
- Goods with extended trade cycles (i.e., shipping across multiple jurisdictions);
- Goods which are difficult for customs authorities to examine

The following business activities are highly vulnerable to ML/TF risks. Enhanced Due Diligence (EDD) should be undertaken to mitigate TBML/TBTF risks.

- Gold, Precious Metals & Minerals
- Auto parts and vehicles
- Agricultural products and foodstuffs
- Clothing and second-hand textiles
- Portable electronics (mobile phones, laptops, etc.)

Types of businesses at risk of trade-based money laundering

As with sectors, the types of businesses at risk of TBML exploitation are varied. Small or medium-sized businesses featured in multiple TBML schemes, but some investigations involved large multinational companies, often through overseas subsidiaries that have more fluid trading relationships in distributing products into newer markets.

Specific business indicators to note include:

- Rapid growth of newly formed companies into existing markets;
- Evidence of consistent and significant cash payments, including those directed towards previously unknown third-parties. These businesses may also receive unexplained third-party payments;
- Unnecessarily complicated and complex supply chains, involving multiple transshipments;
- Previously established companies specialising in one sector that unexpectedly pivot into an entirely unrelated sector. One example provided noted an IT company quickly established a foothold in the acquisition and distribution of bulk pharmaceuticals;
- Companies simultaneously involved in more than one unrelated sector

The following are the tools used by criminals in TBML/TBTF schemes:

- Shell and front companies
- Freight forwarders and customs brokers (verify custom invoices and bill of lading)

Common trade-based money laundering techniques

The FATF 2006 report identified several techniques that form the foundation of TBML and still remains relevant:

- Over-invoicing and under-invoicing of goods and services
- Over-shipment and under-shipment of goods and services
- Multiple invoicing of goods and services
- Falsely described goods and services
- Phantom shipping
- Black Market Peso Exchange

Assessment of current trade-based money laundering risks

- **Illicit cash integration** - given the prevalence of TBML as a process for laundering the proceeds of illegally smuggled commodities, OCGs and PMLs need a way of successfully integrating illicit cash into the financial system. Another variation of illicit

cash integration is the exploitation of surrogate shopping networks and the infiltration of legitimate supply chains.

- **Third-party intermediaries facilitating invoice settlement** - in penetrating legitimate supply chains and sourcing goods without any misrepresentation, the OCG may pay for those goods by involving a previously unknown third-party (usually the company responsible for integrating criminal cash) into the transaction. Shell or front companies i.e. these third-parties may be based in locations with beneficial ownership secrecy provisions

Trade-based terrorist financing (TBTF)

In practice, TBTF schemes can and do rely on the common TBML techniques. They can also feature legitimate firms and transactions right through the supply chain, until the funds are eventually diverted to terrorist organisations.

Services-based money laundering (SBML)

Services-based money laundering (SBML) is not TBML, and is included here for reference as it is recognised as an increasing risk, including through open source reporting. However, the fundamental difference between the two is that SBML schemes rely on exploiting the trade in services or other intangibles to disguise and justify the movement of illicit proceeds.

The following services and sectors were identified as vulnerable to SBML:

- Gambling, particularly online gambling service providers;
- Software providers, including gaming and business software, such as electronic point of sale services;
- Financial services, including virtual asset wealth management;
- Consultancy and advisory services;
- Trademarks and similar intangible items such as intellectual property rights.

Challenges to countering trade-based money laundering

- **Lack of understanding and awareness** - Law-abiding organisations involved in the supply chain, see a piece of the puzzle, but not all of them are sufficiently aware of the signs of trade-based money laundering.
- **Domestic co-ordination and co-operation** - Domestic co-ordination and co-operation is one of the fundamental pillars of an effective AML/CFT regime.
- **International co-operation** - Money launderers often use front companies registered in one jurisdiction and transfer relevant funds and ship goods between others.
- **Investigation and prosecution** - As for any other type of ML, prosecuting TBML requires the need to prove that the laundered funds or assets are the proceeds of crime and that the defendant knew this.

- **Challenges from the private sector perspective** - Trade-based money laundering is highly adaptive and can exploit any sector or commodity. FIs need to identify TBML schemes by estimating the “fair price” of a traded commodity.

Measures and best practices to counter trade-based money laundering

- **Increasing the understanding of trade-based money laundering** - Jurisdictions may use different sources of information to develop an understanding of TBML schemes across the public and private sectors. One source is the NRA, as it typically summarises the available information on ML/TF risks present in the jurisdiction, sometimes with a breakdown by specific sectors.
- **Financial intelligence collected by financial intelligence units** - STRs submitted by DNFBPs, FIs and from other sectors, such as commercial entities engaging in international trade can be a useful tool for detecting TBML.
- **FIU analytical approaches to trade-based money laundering** - FIUs should analyse corporate structures, registration details, alleged company purposes, corporate banking profiles, and the relationship between corporate networks, such as common representatives, overlapping ownership structures, identical registration addresses, and joint bank accounts.
- **Role of customs in countering trade-based money laundering** - Close collaboration between customs agencies and FIUs greatly enhances the collective capacity to identify TBML by linking suspicious trade activity with suspicious financial activities.
- **Interagency groups and co-ordination bodies** - Given that a TBML investigation can involve multiple agencies, establishing a co-ordination mechanism or a working group – whether under the umbrella of one agency or as a separate platform – can lead to increased efficiency.
- **Public-private partnerships** - PPPs may be a useful way to increase communication between the involved sectors and even contribute to a broader dialogue.

Reference

<https://www.fatf-gafi.org/media/fatf/content/Trade-Based-Money-Laundering-Trends-and-Developments.pdf>

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