Money laundering involves three steps: placement, layering, and integration. In Encyclopedia of Transnational Crime and Justice

Money laundering is the illegal practice of transferring funds of illegal origin, usually as cash, into legal enterprises in such a way that they appear to be legitimate.

Money laundering is a broad descriptor of numerous techniques to move illicit funds into the legitimate economy. Money laundering can be used to hide foreign profits, avoid taxes, or cleanse the proceeds of crime. It is a crime that supports any level of crime that produces cash that cannot be spent freely.

Criminal enterprises tend to concentrate currency in the hands of one or a few people. Small amounts of cash are easy to blend into the general background of commerce. Large amounts of cash, large enough to amount to wealth, require the services of a financial institution. Anti-money laundering (AML) laws target these institutions with reporting and regulations like the know-your-customer (KYC) laws. Possession of large amounts of cash is not illegal, but the various AML laws and initiatives require identification of the personnel handling the currency and tracking of transactions involving large amounts of currency. Traditionally, AML laws target the concentration of currency, but as electronic funds transfers have become more common, AML laws have adapted. AML laws have recently been adapted to an increasingly international economy and international threat groups seeking to fund their operations.

Money laundering is described in three parts to help target identification and enforcement efforts. The initial step of money laundering is called placement, which occurs when illicit funds are first introduced into the financial system. Depositing illicit cash at a bank or buying money orders with illicit cash is part of placement. The next step is called layering. Layering usually involves multiple transactions to obscure the origin of funds in the financial system. Transferring funds to an offshore, privacy haven bank and transferring the funds back in small increments is an example of layering. There can be overlap between the steps. For example, carrying cash proceeds of a crime into a casino, buying chips, and later cashing the chips in as winnings and even paying taxes on the winnings includes both placement and layering in the same transaction. The final step is called integration. Integration is the point at which laundered funds are returned to legitimate uses. These stages are targeted by the various AML efforts and laws. AML compliance programs also recognize these categories and direct efforts at them specifically.

A Legislative History

In the United States, the Banking Secrecy Act of 1970 (BSA) began efforts to fight money laundering. Banks were required to identify depositors and keep records of financial transactions. The BSA
required all transactions over $10,000 in cash to be accompanied by a Currency Transaction Report (CTR). In 1986, the Money Laundering Control Act made money laundering a federal crime and criminalized structuring of financial transactions designed to avoid CTR reporting requirements. The law also implemented civil and criminal forfeitures for violations. The Anti-Drug Abuse Act of 1988 added businesses with large transactions like auto and real estate sales to financial institutions required to report large currency transactions. The act also required identification of purchasers of financial instruments worth $3,000 or more.

The Annunzio-Wylie Anti-Money Laundering Act of 1992 instituted Suspicious Activity Reports (SARs). SARs allow a financial institution to report activity that may indicate money laundering. For example, a structured set of four money order deposits with identical amounts, on the same day, and with sequential serial numbers may be deemed suspicious because the transactions are clearly related and are apparently structured to avoid reporting.

The Money Laundering Suppression Act of 1994 made it a federal crime to operate an unregistered Money Service Business (MSB). The act required banks to proactively train employees to identify and report suspect transactions. A similar act, the Money Laundering and Financial Crimes Strategy Act of 1998, expanded the training requirement to bank examiners and made structural changes in the government’s response to money laundering. The USA PATRIOT Act of 2001 broadened AML laws to all financial institutions, strengthened identification requirements under previous laws, and increased controls on international transactions. Most recently, the Intelligence Reform and Terrorism Prevention Act of 2004 strengthened requirements on financial institutions making electronic money transfers internationally.

New Orleans, Louisiana, Mayor Ray Nagin takes King Abdullah II Bin Al-Hussein of Jordan on a walking tour of the Ninth Ward on February 3, 2006, to view the devastation caused by Hurricane Katrina. Nagin's own political disaster finally made landfall on January 18, 2013, when he was indicted on 21 counts of corruption, including wire fraud, bribery, and money laundering. If convicted of conspiring to commit money laundering, Nagin faces up to 10 years in prison, a $250,000 fine, and three years of supervised release.

In 2005, the European Parliament issued its third Anti-Money Laundering Directive to member states

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of the European Union (EU). Since the first AML Directive in 1991, the EU has progressively expanded its definition of money laundering and also the list of predicate offenses and has expanded the professions and institutions targeted. Actual laws are implemented by EU member states. Member states are free to enforce AML laws going beyond the directives, but the directives serve as a minimum level of effort and cooperation in the Eurozone. AML efforts in the EU have been primarily directed at prevention rather than criminal penalties. The collective EU countries have only 1 percent of the convictions of the United States in recent years. Much of this can be attributed to a more aggressive definition of money laundering and the United States' substantial use of AML laws in connection with other crimes like drug trafficking.

The Financial Industry and AML Compliance

Both U.S. and European efforts have substantial requirements of the financial services industry to help prevent money laundering activities. A complex, vigorous, international economy helps hide money laundering activities from regulators, so current laws make it incumbent upon the financial service companies to be diligent in not becoming unwitting accessories to serious crimes. To address these concerns, the financial industry has established industry practices that often fall into four categories of response. First AML programs and written policies establish the scope of an organization’s efforts to comply with AML practices. Policies usually include verification of customer identity, reporting requirements, record retention, response to law enforcement requests, licensing, statement of regulatory compliance, and training for employees. AML programs are not limited to these policies, but they illustrate the concept well. Second, designation of a compliance officer makes it the duty of a single responsible individual to ensure that AML policies are followed. Third, ongoing employee training ensures that new and existing employees will not unknowingly allow violations of AML policies. Training also establishes the organization’s efforts to proactively support AML efforts. The fourth and final category of industry response is periodic review of AML policies and actual practices. If a third party is not required by regulation, review by someone outside the normal compliance office is necessary. Review by someone within the compliance office simply duplicates that function.

Know-your-customer (KYC) policies reflect legal requirements to positively identify customers in certain financial transactions and support broader AML compliance. By knowing the customer, an employee or business unit can spot unusual activities that must be reported in an SAR. Some entire business categories place a financial service provider at increased risk. Casinos, check cashing companies, money transmission businesses, and even charities are considered “vulnerable” to use in money laundering. KYC policies help identify these risky customers. Additionally, any business that regularly deals in large amounts of cash may require extra scrutiny. Restaurants, parking garages, and retail stores all have a typical profile with their use of financial services. Deviating from these profiles may signal that additional scrutiny is necessary.

For example, sudden increases in the cash deposits of a small restaurant owner may indicate money laundering or it may indicate a new mobile lunch cart or truck with more cash transactions. A parking garage that suddenly needs significantly more large denomination bills but does not show any other changes may be part of a drug dealer’s efforts to change small bills to more easily transported large-denomination bills. Normally, garages need small bills for change and deposit large bills. Finally, a change in the ratio of credit deposits to cash deposits from a retail store may signal money laundering. These examples are illustrative of concerns that are not unique to a single type of business. KYC policies help financial services companies determine if certain questionable transactions or trends are actually out of

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character for their customer.

Suspicious transactions can be defined by nature or because of the client. Clients refusing to provide required identification or backing out of a transaction when asked questions causes justifiable concerns. Structured transactions that appear intended to avoid reporting or identification are also suspicious. Use of ATMs or other mechanisms that allow a customer to conduct transactions without being asked for identification fall into this category. Finally, transactions with banking privacy havens or Money Service Businesses (MSB) can draw scrutiny. Policies empowering employees to act on such suspicions and training on how to identify them provide meaningful AML efforts.

See Also: Advance Fee Scam; Bank of Credit and Commerce International; Bank Secrecy Act; Campaign Finance; Check Kiting; Currency Fraud; Daisy Chains; Daiwa Bank Ltd.; DeLay, Tom; Federal Gambling Regulation; Financial Crimes Enforcement Network, U.S.; Gambling and Lotteries; Nonprofit Organization Fraud; Offshore Bank Accounts; Organized Crime; Racketeering

Further Readings


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