Trade Based Money Laundering

An Overview…

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WHAT IS TBML?

Trade-based money laundering (TBML), originally defined by FATF in 2006 as "the process of disguising the proceeds of crime and moving value through the use of trade transactions in an attempt to legitimize their illicit origins."

The FATF recognized TBML as one of the three main methods by which criminal organizations and terrorist financiers move money for the purpose of disguising its origins and integrating it back into the formal economy.

TBML is based on abuse of trade transactions and their financing. The 2006 FATF Study highlighted the increasing attractiveness of TBML as a method for laundering funds, as Controls on laundering of funds through misuse of the financial system (both formal and alternate) and through physical movement of cash (cash smuggling) become tighter.

DISTINGUISHING FEATURES

Opportunities to take advantage of differences in legal systems of various jurisdictions. Such as free trade zones and less stringent AML-setups

Cross border transactions

Intermingling of the trade sector with the finance sector

Lack of cross-referencing of trade-data with that of trade-finance essential when investigating TBML

Trade dominated by internationally accepted currencies, the conversion of currency at market determined exchange rates enhances scope for criminals to launder

Vulnerabilities of the foreign exchange market

Long supply chain

The long supply chain makes Trade sector more vulnerable, starting from manufacturer, trader, consigner, consignee, notifying party, financier

TBML METHODOLOGIES

TBML schemes are often accomplished through custom fraud violations, such as:

1. Over and under shipment of goods & services
2. Over and under invoicing of goods & services
3. Multiple invoicing or false invoicing of goods & services
4. Falsely described goods & services
5. Related party transactions or use of shell companies as front
6. Black market exchange

TBML TYPOLOGIES

Techniques

Over Invoicing

- By misrepresenting the price of the goods in the invoice and other documentation (stating it at above the true value) the seller gains excess value as a result of the payment

Under Invoicing

- By misrepresenting the price of the goods in the Invoice and other documentation (stating it at below the true value) the buyer gains excess value when the payment is made

Multiple Invoicing

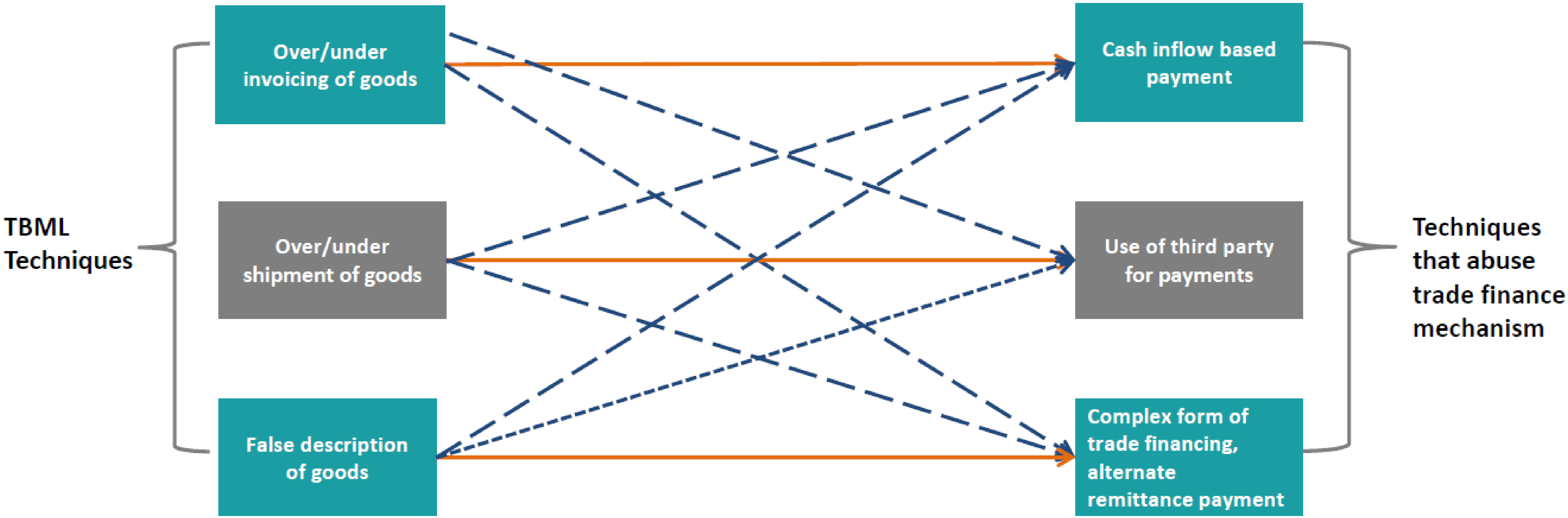
- By issuing more than one invoice for the same goods a seller can justify the receipt of multiple payments. This is harder to detect if the colluding parties use more than one Financial Institution to facilitate payments/transactions

TBML TYPOLOGIES

Techniques

Short Shipping	Over Shipping	Obfuscation of type of goods	Phantom Shipping
• The seller ships less than the invoiced quantity or quality of goods in the documents. The effect is similar to over invoicing	• The seller ships more than the invoice quantity or quality of goods thereby misrepresenting the true value of goods in the documents. The effect is similar to under invoicing	• Parties may structure a transaction in a way to avoid alerting any suspicion to FIs or to other third parties which become involved. This may simply involve omitting information from the relevant documentation or deliberately disguising or falsifying it.	• No goods are shipped and all documentation is completely falsified

COMPLEX TBML TECHNIQUES



PARTS OF THE TBML SOLUTION

Solutions

- **Vessel Screening:** Organizations must screen against not only Vessels listed by OFAC, but all vessels associated with any sanctioned country.
- **Payment Routing** – SWIFT/BICs of all sanctioned banks should form the part of the screening database.
- **Companies & Organizations** – Database must also have companies owned by sanctioned governments and additional locations and subsidiaries of designated companies
- **Goods** – Banks should possess comprehensive list of dual-use goods and controlled goods based on latest internationally agreed dual-use controls
- **Country Details** – Database must provide principle cities, towns, airports, and seaports of all fully sanctioned countries
- **People** – PEP DATABASE should always be updated.
- **Ongoing Monitoring** - What was originally scanned during the issuance of the letter of credit versus what is to be scanned when the shipping documents are presented can literally be a world apart in terms of sanctions obligations.

KEY GAPS IN TBML CYCLE

1. Few cases of TBML reported
2. Lack of reliable statistics relating to TBML
3. Lack of awareness and training on TBML among various jurisdictions
4. No current standardization with regard to practice of collection and maintenance of data on TBML
5. Most jurisdictions do not distinguish between TBML and other forms of ML
6. Trade related data available with custom authorities needs to be used for detecting TBML

KEY RISKS & ISSUES

Risks

Trade Finance has become a popular instrument for Money Laundering as:
— The **tremendous volume of trade** makes it easy to hide individual transactions
— The **complexity that is involved in multiple foreign exchange/cross border** transactions
— The **limited resources available to agencies** wanting to detect money laundering

Issues

- Lack of clear policy & inconsistent approach to risk assessment with no specific trade finance money laundering risk assessment
- Inability to demonstrate that money laundering risk had been taken into account when processing particular transactions
- Trade processing staff do not make adequate use of CDD information gathered by relationship managers or trade sales teams
- Little or no management information on financial crime risks in the trade finance business
- No specific trade finance financial crime training for relevant staff
- Inadequate systems and controls over dual-use goods

RED FLAGS

Red Flags relating to Jurisdiction

- Commodities shipped from and to destinations categorized as “high risk”
- Commodities trans-shipped through one or more jurisdictions
- Unusual shipping routes or trans-shipment points
- Customers involved in businesses in high-risk jurisdictions

Red Flags relating to Goods

- Discrepancies arising from description of goods, actual goods shipped, value of commodity reported on the invoice bill
- Shipment – inconsistency in the size of shipment, location, packaging
- Misrepresentation of type of goods
- Carousel transactions: repeated importation and exportation of same high-value goods

Red Flags relating to Corporate Structure

- Transactions involving the use of front (or shell) companies
- Obscuring the true nature of transactions through the introduction of corporate entities by using an unnecessarily complex transaction structure
- Companies or Money Exchange Bureaus in third countries used as intermediaries for transfer of money

Red Flags relating to Trade Finance

- Transactions involving amended or frequently extended letters of credit
- Customer’s inability to produce appropriate documentation
- Phantom shipping: no goods shipped and falsified documents for moving funds
- Sudden payments typically wire transfers

WAYS TO COUNTER TBML

Any strategy to prevent and combat TBML needs to be based on TBML structures while allowing general trade to occurred unfretted

- Inter-agency co-ordination & international co-operation
- Strategy that takes account of sectoral peculiarities, jurisdictional frameworks & agency specialization
- A common format of reporting and maintaining trade-relevant statistics
- Co-relate trade data with foreign exchange data to detect TBML

- **TBML focused training for competent authorities** such as Customs, FIUs, Tax Authorities and Regulators
- **Cross-referencing of trade data and trade finance** can be a starting point for risk-based approach to identifying TBML

TRADE FINANCE INSTRUMENTS

Instruments	Documents	Vulnerability
Bills of Exchange	Transport Document, Commercial Invoice, Insurance Document , Certificate of Origin, Packing List, Weight Certificate	• Undertaken and paid for without any form of due diligence by an intermediary in the supply chain because the parties are complicit • Phantom trade may be the cause of unrealistic timeframes or short supply chains
Counter-trade	It exists where economies face the problem of limited foreign exchange holdings, encompassing the idea of subjecting the agreement to purchase goods or services to an undertaking by the supplier to take on a compensating obligation in lieu of a cash settlement. The seller is required to accept goods or other instruments of trade in partial or whole payment for its products. Types : Barter, counter-purchases, buy-back	• Vulnerability arise in determination of exchange ratios for goods to be counter-traded, such ratios may often be determined as a process of negotiation rather than being market determined, giving way to TBML
Documentary Credit	Letter of credit - Generally the exporter requires an importer to prepay in cash for goods shipped. The importer naturally wants to reduce risk by asking the exporter to acknowledge through documents that the goods have been shipped. The importer's bank assists by providing a letter of Credit (Documentary credits) to the exporter (or the exporter's bank) providing for payment upon presentation of certain documents, such as a bill of lading either immediately or at a prescribed date.	• Even in this simple form the true value of goods transferred between countries can be masked through misrepresentation of price, quantity and quality. Letters of Credit may be generated to create a veneer. • The documentation generated in the process leaves a paper trail which money launderer may rely upon to disguise illegal proceeds.
Open Account Facilities	Open account transactions can be described as 'buy now, pay later' and are more like regular payments for a continuing flow of goods rather than specific transactions.	• Open account facilities have caused a disconnect between the movement of the underlying trade and the money used to finance it.

BEST PRACTICES

- Capacity building and **increased awareness of TBML through training modules**
- **Identifying red flag indictors for each sector**. A Risk based approach with target orientation has been strongly recommended
- **Cooperation among various authorities** as often data is dispersed over more than one agency
- Encouraging international cooperation
- Access of trade data and trade finance databases to investigators through secure databases
- Strengthening current measures so that there is extensive use of available data in the form of case studies and red flag indicators of TBML
- Automation - A system that can perform **background checks through leveraging partnership** with the recognized data providers
- Stopping proliferation – Engagement and **partnerships with the private sector** can be the first line of defense against trade based money laundering
- Trade related **due diligence**
- **Know Your Customer" (KYC) Policies** and Procedures are imperative to identifying and evaluating the risk associated with each customer

Q&A