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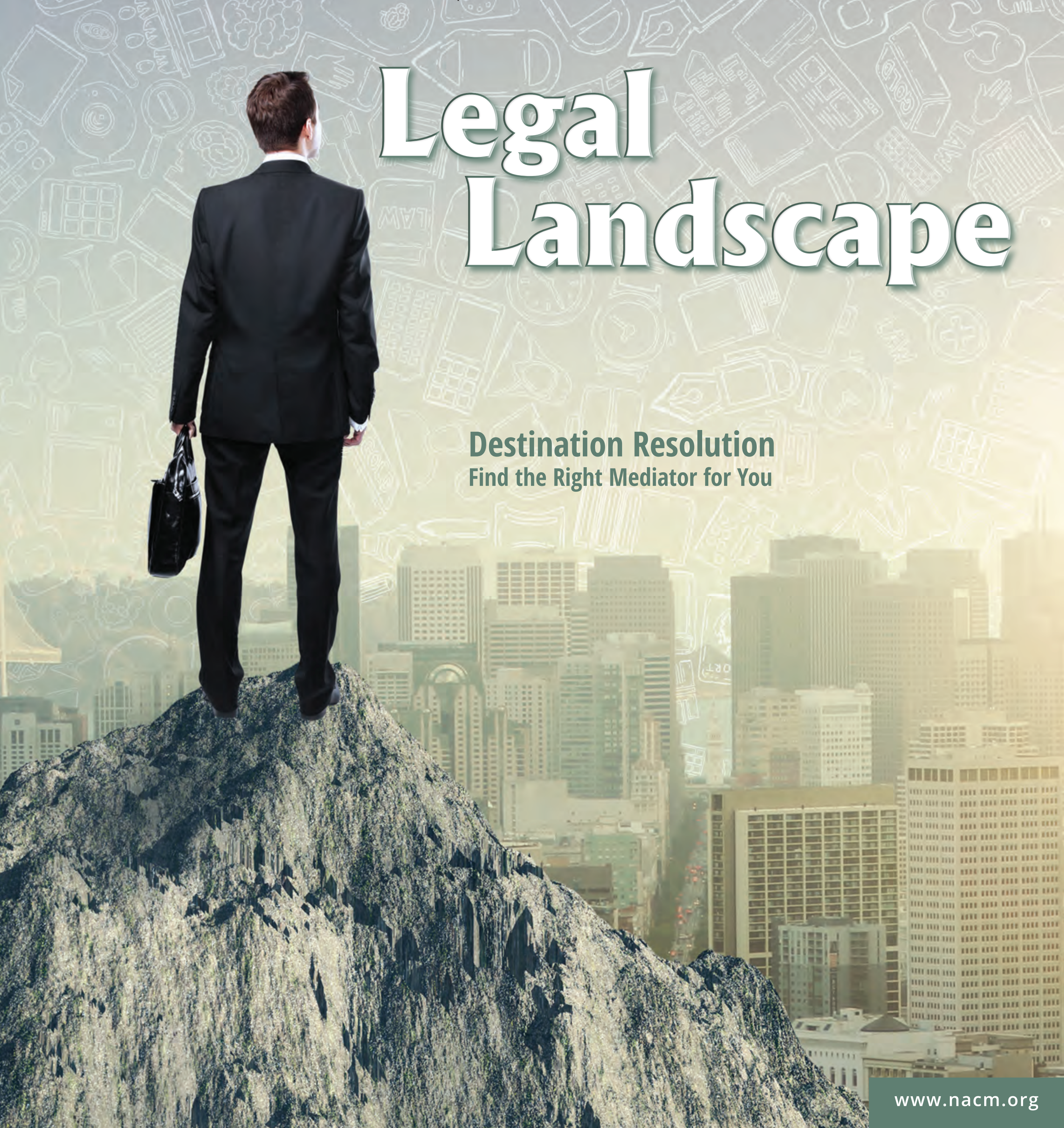
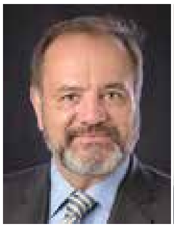


Legal Landscape

Destination Resolution
Find the Right Mediator for You

Dr. Thomas Voller, Esq. and Matthew Wales, Esq.



Prevention of Money Laundering: European Approach

The prevention of money laundering and financing of terrorism is one of the most important subjects in compliance today. No company that trades goods can ignore this and continue in business without an analysis of their own risks and the rules needed to minimize them. Anti-money laundering is as important as the avoidance of bribes, corruption, violation and theft of intellectual property.

Money laundering means simply the act of making money that comes from an illegal source "A" look like it comes from a legal source "B." Criminals try to disguise the origins of money obtained from illegal activities by placing it into a legal business or on an account, executing various trades as layering steps in order to make the money seem like it's coming from legal sources. A drug dealer selling cocaine will hide the fact that his money comes from drug dealing. To achieve this, the drug dealer will invest it in some legal business. The dirty money, which has been "invested," becomes washed money.

Criminals try to disguise the origins of money obtained from illegal activities by placing it into a legal business or on an account.

History

This practice of criminals is certainly as old as money itself. The term "money laundering" received its name from Al Capone. He owned a large chain of Laundromats and all the money, which came from the business, was white. Nobody could control whether the money was put into the Laundromats by a customer or simply put into the shop by Capone. Therefore, the money he earned from illegal alcohol, drugs, prostitution, etc. was clean when it came out of the Laundromat and could be invested in all sorts of legal activities. He was never convicted for money laundering because there was no law against it, but he was convicted of tax evasion.

Following this, Meyer Lansky perfected the act of money laundering. He transferred his illegal money to anonymous accounts in Switzerland, started the casino business in Cuba and Las Vegas, and even established a bank. Laws against money laundering came into being worldwide at the end of the 1980s.

The fight against money laundering, which started on an international basis, was motivated by the fight against drug abuse. The first step was the Vienna Convention of the United Nations on Dec. 20, 1988. This was a convention against the illegal trade with drugs, and part of it was the prevention of money laundering. An important step was the foundation of the Financial Action Task Force on Money Laundering (FATF). The FATF, which is still in existence, was set up in Paris, France in June 1989. One task was to analyze the various money laundering methods. The European Union had its first common Directive in June 1991, which was amended in 2001 and 2005. It was completely revised by the Fourth Anti-Money Laundering Directive (EU) 2015/849 (AMLD), which has been binding for all member states of the EU since June 26, 2017.

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Applicability

But what does this have to do with credit managers? Doesn't this subject apply only to banks and financial institutions since they are always in the press for being fined for money laundering? Or, is it a subject for chartered accountants and lawyers as John Grisham describes it in his novel, *The Firm*?

Article 2, 1 (3)(e) Anti-Money Laundering Directive (AMLD) stipulates that this directive shall apply *inter alia* to the following obliged entities:

> "Other persons trading in goods to the extent that payments are made or received in cash in an amount of EUR 10.000,00 or more, whether the transaction is carried out in a single operation or in several operations which appear to be linked."

This means that everybody (natural persons and legal entities) who sells something can be obliged under the AMLD.

The problem is one regulation applies to all different parts of business sectors. Basically, the same rules are applicable for banks, financial institutions, auditors, lawyers, trusts and estate agents as well as a company that is trading goods. However, the 89 articles of the Directive are applicable only in small part to trading companies—often they are exempted. The major part applies only to banks and similar institutions.

As part of a minimum legal harmonization, each EU member state is obliged to transpose the AMLD into national law. The result is that all EU member states have similar anti-money-laundering laws, but there are different interpretations from country to country. In Germany, for example, the "Geldwäschegesetz" is a binding national law. In Austria, the rules are part of more than six different laws, such as the Austrian Trade Law. These are civil rules pertaining to money laundering. In addition, there are criminal rules, which can lead to imprisonment for up to several years and fines for individuals. In Ireland, it would be the Criminal Justice Act 2013, which has led to fines of up to several million euros in recent years.

The Process

It is very difficult to say how much black money is in this world, but the United Nations estimates it is between 3% and 5% of the gross national product worldwide. In Germany, the estimation is approaching 100 billion euros. The scheme is always the same:

- **Placement:** The money launderer inserts the dirty money into a legitimate financial institution. This can be payments in cash on a bank account. Under the anti-money-laundering laws, the banks are obliged to report high-value transactions, so it is normally done in small portions, below 10,000 euros.
- **Layering:** This is when money is sent through various financial transactions via different continents and from country to country. It is difficult to follow. During this procedure, the money can be invested in high-value items such as boats, houses, race horses, diamonds and expensive cars. The purpose is to make the original dirty money as difficult to trace as possible.
- **Integration:** This occurs when the money re-enters the ordinary economy appearing to be coming from a legal transaction. Now, it's invested in shares, apartments or any sort of legal business.

The longer the procedure takes, the more difficult it is to recognize the dirty money.

Recognizing the Risk

For ordinary trading companies that do not wash dirty money on purpose, the risk is that criminals like to invest into their business as the third step of integration. This can be done by paying invoices for other parties. If a credit manager recognizes that party "A" bought a product, but party "C" pays for it from an address in the British Virgin Islands or Cayman Islands, the minimum he or she has to do is ask why it's coming from there. There can be a simple explanation. It could be cash pooling within a holding structure. On the other hand, there could also be no explanation, or you might hear, "Be glad that your invoice is being paid." If there is any suspicion of illegal activity, the payment should be returned and the authorities informed about possible money laundering.

There could also be the option to invest money directly in a company for better conditions than those offered in a bank loan. It is very rare that a company trading products wants to be active in money laundering, but every company may be abused by criminals without its knowledge.

In the United States, there are several laws preventing money laundering, such as the 1986 Money Laundering Control Act, the 1994 Money Laundering Suppression Act and the 2001 U.S. Patriot Act. These are in direct relation with the rules set up by the Financial Action Task Force, which issues recommendations on a regular basis. These are the Anti-Money-Laundering standards. The Directives of the European Union are also based on these recommendations.

It is in the best interest of the companies trading goods to obey these rules because if they do not, there are various risks to keep in mind:

- **Risks based on law:** The violation of the Anti-Money-Laundering laws includes administrative law, criminal law and civil law.
- **Financial risk:** A company can be fined up to several million dollars.
- **Operational risk:** Competent authorities are authorized to audit an obliged company, whether or not there is an Anti-Money-Laundering System. This may cause delays and additional work.
- **Risk of loss of reputation:** This is by far the most important risk. It can be illustrated by the banks, which dramatically lost their reputations during the last few years because of permanent accusations for money laundering. It is a disaster if a company is accused of being part of a money-laundering system. It will lose a lot of orders. Under European law, it can be blacklisted and will not receive any further public orders.

Evaluating the Risk

The question is, what does such a trading company have to do under the European rules?

The first step is to evaluate its own risks—the risk assessment. This should be done in writing and organized by management. It must be approved by the board of directors. The confidential documentation should stay with management in case the authorities request it, which they can do. In this analysis, the company has to evaluate the risks associated with the products it sells, the structure of the company, the customers, the distribution channels and how the goods are normally paid. A company producing and selling weapons has a completely different risk factor than a producer of shirts and trousers. A company taking cash has a completely different risk compared to a company accepting only bank transfers. Customers in high-risk countries (for example, Nigeria, Iran, etc.) present a different risk compared to customers in the seller's country. A large international business carries a different risk than a local shop.

Company Policy Defined

The analysis is the basis for a document, which needs to be prepared by the company. The money laundering prevention rules are the set of internal procedures on how the legal requirements are being understood and fulfilled.

Part of this is the obligation to identify a person paying for goods in cash valued at more than 10,000 euros. This includes finding out the real beneficiary of the deal. There can be a problem of clear transparency about the natural and beneficial ownership for companies. With the 4th Directive, there is an obligation for all the member states of the EU to have a central registry containing the necessary information about the real, natural owner of a company. This information is available to the national authorities and obliged entities. It all goes back to KYC—knowing your customer.

Another obligation is that in case of a suspicion of money laundering or financing of terrorism, an employee has to inform the person in their company who is responsible for the prevention of money laundering. This could be the money laundering reporting officer, if the company has one. The company also has to inform the authorities about the suspicion.

According to the 4th Directive, the cooperation and exchange of information between the Financial Intelligence Units (FIU) from the different member states will be facilitated. It should, therefore, be easier to prevent and detect crime or terrorist activities.

European Rules

Within the European Union, the fight against money laundering and terrorist financing is more or less unified. All the member states are bound by the same rules via the AMLD. All EU member states transferred these rules into their national laws, so they are almost identical. Companies dealing with European business partners have to be aware that these rules exist. If an American company has an affiliated company in Europe, it must make sure that there is a system implemented that prevents abuse for money laundering purposes. Today, this problem is taken very seriously. Violation of Anti-Money-Laundering laws carries extreme consequences, so the management has to make sure there is no violation of the existing rules.

The minimum a European trading company needs is the analysis of risk. This will vary from company to company based on the types of products, customers, countries and transactions. Employees should be trained within the company and there should be constant supervision. There should be a clear understanding of how suspicions or questions should be reported. There should also be a designated person to get in contact with the authorities, if necessary.

In the U.S., it is not unusual to be confronted with the prevention of money laundering, especially after 9/11. Even if the Europeans took a bit longer with their legislation in this area, the rules are just as strict and clear as in the United States.

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