THE BROOKINGS INSTITUTION
CENTER FOR NORTHEAST ASIAN POLICY STUDIES

THE EFFECTIVENESS OF MONEY LAUNDERING INVESTIGATIONS IN FIGHTING TRANSNATIONAL CRIME:

A COMPARISON OF THE UNITED STATES AND HONG KONG

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Chapter 1
Introduction

For a two-year period between 2008 and 2010, part of my professional responsibilities with the Hong Kong Police was to command the Joint Financial Intelligence Unit[1] of Hong Kong ("JFIU"). One day in mid 2009, just as I was about to leave the office, I received a call from a compliance officer of a bank, who was also a personal friend, asking for my advice on a case which had aroused his suspicions. In short, his staff had identified a pattern involving a group of three nonresidents (from Mainland China in fact) opening personal bank accounts at different branches of the bank in the last couple of days. During routine customer due diligence processes, the group told the bank that the accounts were to be used for the purpose of business (trading). However, they appeared to have some common links and once the accounts were opened, they shared a similar transaction pattern of receiving inward remittances from Taiwan in the range of HK$20,000 – 100,000 (US$2,500 – 12,500).

Though I was not happy about the bank allowing personal accounts to be opened for business purposes, being his friend I was courteous enough to praise his staff for what appeared to be good transaction monitoring. Though experience suggested that something was not right with these accounts, neither the bank nor my unit could do anything about the inward remittances. I advised my friend to file a suspicious activity report as obligated under Hong Kong law so that my unit could look into it.

After the call, I asked one of my team leaders to initiate an investigation into the background of the group once the suspicious activity report had been received. The report came two days later which I regarded as pretty efficient; many reports were filed weeks or months after the transactions in question had taken place. However, when the team leader called the bank for some missing details, he was told that the accounts had received further inward remittances from Taiwan in the last two days and that most of them had been either withdrawn in cash or transferred to a remittance agent. The inward remittances amounted HK$ 1.6 million (US$200,000) in total.

Initially, little could be established as to the background of the account holders as they were nonresidents and had left Hong Kong. The funds transferred to the remittance agency were

[1] Hong Kong's Joint Financial Intelligence Unit ("JFIU") is managed by the Hong Kong Police and is set up in accordance with Recommendation 26 of the Financial Action Task Force ("FATF"), an intergovernmental body comprising 36 financial jurisdictions and organizations. Recommendation 26, titled "Institutional and other measures necessary in systems for combating money laundering and terrorist financing," reads as follows:

> "Countries should establish a FIU that serves as a national centre for the receiving (and, as permitted, requesting), analysis and dissemination of suspicious transaction report (or suspicious activity report) and other information regarding potential money laundering or terrorist financing. The FIU should have access, directly or indirectly, on a timely basis to the financial, administrative and law enforcement information that it requires to properly undertake its functions, including the analysis of STR."

See http://www.fatf-gafi.org/document/44/0,3746,en_32250379_32236920_43730156_1_1_1_1,00.html.

subsequently "wired"[2] through underground remittance networks to two bank accounts in the Mainland. Background checks on the account holders and bank accounts were then conducted with the Mainland and the Taiwanese authorities but experience suggested that we would have to wait weeks or even months for the results. Two days later the remitting bank in Taiwan attempted to recall the remittances from one of the accounts as they were believed to be the proceeds of fraud. Our suspicions were confirmed. The remitting bank alleged that the remittances came from the account of a retiree who was deceived (over the telephone) to believe that his son was subject to a money laundering investigation by the Taiwanese Police and that he needed to transfer all funds in his account to Hong Kong for investigation to prove his son's innocence.

This was not an exceptional case but was one of many which JFIU came across in recent years. This case illustrates, for the purpose of this study, the fact that transnational crimes take place on a daily basis, and that they are not necessarily complex or involve big sums. It also depicts the current landscape of transnational crime where criminals are adept at exploiting jurisdictional boundaries and incompatibilities to ensure a low risk environment for their criminalities; and it exemplifies the relative inefficiency and ineffectiveness of law enforcement response. There were also issues concerning the regulation of financial institutions for the purposes of anti-money laundering and combating the financing of terrorism, but they do not fall within the purview of this study.

Research Objectives

This research seeks to:

(a) Identify emerging trends in transnational crime and the resulting challenges to law enforcement;
(b) Examine the effectiveness of money laundering investigation of the law enforcement agencies of the United States and Hong Kong in addressing these trends and challenges;
(c) Compare the two regimes so as to identify strengths and weaknesses; and
(d) Suggest a way forward in enhancing the effectiveness of money laundering investigation.

Scope and Definitions

This study does not seek to examine the effectiveness of money laundering investigation in interdicting money laundering activities because well-established assessments by international organizations already exist. There are, however, no similar assessments on the effectiveness of money laundering investigation in combating transnational crime or crime in

[2] Cross boundary remittance operations between Hong Kong and Mainland China do not involve actual cross boundary fund transfers through banking systems. Remittance agents in Hong Kong normally join in partnership with underground remittance agents in the Mainland to conduct the cross boundary remittance business. On receiving a remittance instruction from a client in Hong Kong, a remittance agent will pass it to his partner agent in the Mainland, who will then deposit the money into the bank account(s) designated by the client.

general, as little attention has been paid to the fact that the underlying purpose of anti-money laundering is in fact combating crime. Reasons for this interesting phenomenon will be discussed and elaborated in Chapter 3 (pp.10-14).

The study will primarily focus on the practical institutions of the respective law enforcement regimes. However, as policy and legal institutions also impact on practical institutions, they will also be considered as and when necessary.

Two important definitions will further define the scope of this research:

(a) Transnational Crime

The following definition, adapted from the definition of "Organized Crime Group" of the 2000 United Nations Convention against Transnational Organized Crime ("UNTOC"), is used:

> A cross border or cross boundary crime committed by a group of two or more persons, existing for a period of time, working in more than one jurisdiction and acting in concert with the aim of committing the crime in order to obtain, directly or indirectly, financial or other material benefit.

(b) Money Laundering Investigation

Money laundering investigation refers to the operational functions of law enforcement agencies of the jurisdictions under study; and "operational functions" refers to the descriptions[3] used in the recent review of the Recommendations 27 and 28 by the Financial Action Task Force ("FATF") Typologies Working Group, which include:

(i) Analyzing and developing financial intelligence;
(ii) Conducting investigation into suspicious property and persons;
(iii) Interdicting the proceeds of crime;
(iv) Prosecuting the persons; and
(v) Confiscating the proceeds.

Methodology

This study is conducted primarily by interviewing academics and legal and law enforcement practitioners in the United States and Hong Kong. If an interview is not feasible, input is collected by way of a questionnaire. Reference is also made to academic literature and international reports. The observations and experiences of the author during his ten-year engagement in anti-money laundering with the Hong Kong Police and the Hong Kong Government Secretariat form a major source of information of the respective regimes and the relevant issues.

[3] FATF Working Group on Typologies, 2010, *Operation Issues: Recommendation 27 & 28*. Paris, France. 18 Oct 2010. Paris: FATF/OECD.

Comparable and Meaningful?

It is not easy at first glance to conceive how Hong Kong can be *meaningfully* compared with the United States, given the huge difference in size of their economies.[4] Actually, it depends on what the observer is trying to compare. Closer examination of all the relevant facts and statistics suggest that it is not difficult to find many similarities between the United States and Hong Kong. Both jurisdictions are governed by rule of law. While the United States is a highly developed country with a free market economy, Hong Kong is also a very well developed international center for trade, finance, business and communications.[5] Though having a comparatively small GDP, the GDP per capita and GDP per capita based on purchasing power parity of Hong Kong represent 67 percent and 96 percent of those of the United States, which means that their people enjoy similar levels of living standards. Both the United States and Hong Kong rank very high in many international indexes[6] which measure governance effectiveness, competitiveness, economic freedom, etc.

More similarities can be found in the law enforcement regimes of the two jurisdictions. For example, both operate under a common law system despite the fact that U.S. law has diverged somewhat from its English ancestor both in terms of substance and procedure. Both jurisdictions have relatively mature anti-money laundering regimes and well developed competent law enforcement agencies charged with anti-money laundering investigation. Both were rated as "Compliant" in respect of FATF Recommendations 27 and 28, which measure the effectiveness of law enforcement in combating money laundering and terrorist financing. More importantly, law enforcement agencies ("LEAs") in both the United States and Hong Kong are targeting similar and indeed sometimes *the same* transnational crime groups and as a reflection of this there are many joint investigations conducted between the LEAs of the United States and their counterparts in Hong Kong targeting crime groups from all over the world. Geographically, both the United States and Hong Kong are situated in close proximity to some jurisdictions where either law enforcement institutions are not very well developed or corruption is rampant. Both face similar challenges when working with these jurisdictions.

Though the two law enforcement regimes cannot be said to operate under exactly the same institutions and environments, they are nevertheless close enough to have a *meaningful* comparison. Comparing two relatively close regimes can avoid non-law enforcement variables such as political, social or economical, from becoming determinant. The comparison can also be more focused, which enables the respective strengths and weaknesses to be identified for reference by each other.

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[4] The U.S. has a total area of 9.6 million square kilometers with a population of about 307 million, while Hong Kong has an area of about 1,100 square kilometers, which houses seven million people. The U.S. is the largest economy in the world with GDP in 2009 valued at over $14 trillion, whereas Hong Kong's GDP in 2009 was valued at only $205 billion.

[5] Hong Kong operates one of the world's busiest container ports in terms of throughput, as well as one of the busiest airports in terms of number of passengers and volume of international cargo. It is the world's 15th largest banking center in terms of external banking transactions, and the sixth largest foreign exchange market in terms of turnover. Its stock market is Asia's second largest in terms of market capitalization.

[6] For example, the Index of Economic Freedom of the Heritage Foundation; the Global Financial Centre index; the World Governor Indicators; and the GCI Global Competiveness Index.

Chapter 2
Challenges and Law Enforcement Responses

Emerging Trends

In this era of globalization, crime and the associated money laundering activities are inherently transnational in nature, and nomadic by definition. However, incompatibilities arising from differences in political, legal, and social systems present barriers and hence hamper the effectiveness and efficiency of law enforcement efforts. Political ideologies, institutional arrangements, and social settings dictate law enforcement priorities and responses. In jurisdictions of socio-political marginalization and poverty, national security and social stability are priorities; crime, not to mention money laundering, becomes only a secondary concern in such jurisdictions. Criminals are highly efficient at exploiting these incompatibilities to create a low risk environment for their criminalities. It has long been a trend that criminals move their operations to jurisdictions which present a lower risk of enforcement action. LEAs are increasingly encountering criminalities where criminals reside well beyond the jurisdiction(s) in which their crimes are perpetrated.

While globalization makes the jurisdictional borders for criminalities increasingly vague, jurisdictional borders for law enforcement are increasing in relevance with more bureaucracy and protocol required in their dealings as a result of growing public expectations for human rights and governance transparency. Worse still, some of the LEA that the United States and Hong Kong work with, in particular those in Asia and South America, are not particularly well developed for international cooperation in terms of institutions, resources, and skills. As a result they are not very capable of providing the type of assistance required in the pursuit of complex transnational crime. Others simply are not willing to do so because of political reasons, corruption, or other factors, and it is fair to say that there have been frustrations in dealing or working with these jurisdictions. Even with proper mutual legal assistance mechanisms in place, LEAs are very often highly frustrated at the time such requests take and the delays encountered.

The significance of information technology is clear. It enables transnational criminals to function more efficiently and anonymously, and poses great challenges to law enforcement in both their investigative and prosecution endeavors. Use of false or stolen identity has become highly prevalent in the virtual world, which not only facilitates crime, particularly internet-based frauds, but also enables criminals to move their ill-gotten gains quickly and anonymously—for example, via internet based payment methods. The Global Money Laundering and Terrorist Financing Threat Assessment ("GTA"),[7] undertaken under the auspices of FATF in 2009, points out that internet-based frauds and other use of internet technologies in fraudulent activities are notably on the rise globally. GTA also highlights, in respect of trends on money laundering, that methods and techniques most jurisdictions are currently seeing are broadly the same as the ones that have been observed previously; and that while

[7] FATF, 2010. *Global Money Laundering and Terrorist Financing Threat Assessment.* [online] Paris: FATF/OECD. Available at: < http://www.fatf-gafi.org/dataoecd/48/10/45724350.pdf> [Accessed 8 March 2011].

criminals maximize opportunities offered by new technologies, new financial products, and new commercial activities, the abuse of cash in money laundering remains a concern.

Apart from being more secretive and anonymous as a result of globalization and information technology, substantial changes have also been observed in the structure of criminal groups. Europol, the European law enforcement agency, reports that "Criminal groups are getting smaller in size, more fluid in nature, and are increasingly multi-commodity and poly-criminal in their activities."[8] Many now exist in the form of loosely knit networks of cells. In recent years, well structured hierarchies are not common and are only found in less developed jurisdictions where corruption is still a problem.[9] Cells of different expertise and skills will come together for a particular crime and after the crime is perpetrated the network will break; the cells, if new opportunities arise, will net with other cells to form new networks to perpetrate other crimes. Criminals are therefore increasingly opportunistic and decreasingly discriminating, choosing to engage in a wider variety of criminalities. There is no obvious leadership in a network and the network exists transiently; such structural changes are noted to have a significant impact on law enforcement efforts. Law enforcement response needs to be fast as the window in which to collect evidence and develop leads closes quickly. A fast or pre-emptive law enforcement response is achievable through Intelligence-Led Operations,[10] but that is not always possible and in practice is not at all easy.

Despite these significant challenges law enforcement agencies have never been given the full range of necessary resources and powers to do their job. It is fair to say that a level playing field has never existed between law enforcement and crime. On the contrary, law enforcement powers are increasingly restricted as a result of growing public awareness and expectations on rights. The enactment of the Interception of Communications Surveillance Ordinance ("ICO") in Hong Kong in 2006, which seeks to regulate the interception of telecommunications and covert surveillance by authorities, is a prime example of how development in one area of a society restricts performance in another. While many limitations have already been imposed on LEAs over the use of these special investigative techniques as a result of the enactment, legislators still do not consider these sufficient to ensure privacy; efforts to increase these limitations continue, much to the frustration of law enforcement.

A Better Law Enforcement Approach and Focus

Given all these challenges, what should be the approach and focus of law enforcement in order to retain effectiveness and relevancy to transnational crime? Traditional approaches

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[8] EUROPOL, 2011. *Organised Crime Threat Assessment OCTA 2011*. p.5 [online] The Hague: EUROPOL, http://www.europol.europa.eu/publications/European_Organised_Crime_Threat_Assessment_(OCTA)/OCTA_2011.pdf, accessed 12 May 2011.

[9] Corruption is the main facilitator for the establishment and existence of well structured criminal hierarchies.

[10] Intelligence-Led Operations are enforcement operations derived from Intelligence-Led Policing, which is a business model and managerial philosophy where data analysis and crime intelligence are pivotal to an objective, decision-making framework that facilitates crime and problem reduction, disruption and prevention through both strategic management and effective enforcement strategies that target prolific and serious offenders. Source: Ratcliffe, JH (2008) *'Intelligence-Led Policing'* (Willan Publishing: Cullompton, Devon).

tend to target low level operatives, i.e. front men, as LEAs often either find their hands tied in going after the key players and prefer to spend their scarce resources on the pursuit of cases with tangible results. An effective law enforcement approach, however, should target both the "crime" and the "people" behind the crime. "People" means key players, prime offenders or masterminds and does not include front men or low level operatives. There is a common phenomenon amongst LEAs all over the world that focus and efforts have been primarily placed on the "crime." Many law enforcement agents, at frontline and managerial levels alike, are very often complacent regarding, for example, a seizure of a large quantity of drugs or contraband with the arrest of a couple of front men while the prime offenders or masterminds are at large. Goal displacement is another common phenomenon as going after the "people" is neither easy nor rewarding: in some cases even though the law enforcement agents are visionary enough to target both the "people" and the "crime" from the outset, as the investigation develops they would gradually alter their goals and incline their focus and efforts to the "crime" only.

Apart from the "crime" and the "people," law enforcement should also target the "money," It is widely accepted that profit is fundamental to the goals of most crime, and money laundering is a key enabling factor. The ease with which ill-gotten gains can be shifted and laundered amongst groups and across borders is a primary factor facilitating the success of criminalities.[11] To effectively combat transnational crime, law enforcement efforts should target both the predicate crime and the associated money laundering, i.e. to take away the ill-gotten gains. This would not only to remove the incentive for crime but also would prevent re-investment in further crimes. Despite the fact that criminals nowadays are adept at insulating themselves, by following the "money" they can be identified and brought to justice because no matter how far they distance themselves from the crime they orchestrate, their ultimate aim must be to have beneficial control of the proceeds. Please see Case Study 1 below:

Case Study 1

In June 2004 a prolonged joint investigation between LEAs in Australia, Fiji, Hong Kong, Mainland China, and Malaysia culminated in the arrest of six Chinese and a Fijian in an "ice" laboratory in Fiji and the seizure of 800 kilograms of semi-product of the drug ice. The arrested persons were later charged and convicted. When the covert investigation turned overt, the mastermind, a holder of Nauru passport and his wife (a Hong Kong resident), were arrested in Kula Lumpur, Malaysia. However, due to insufficient evidence to link them to the drug laboratory they were later released and deported back to their respective places of residence. However, a parallel financial investigation in Hong Kong revealed that the couple had with US$4M worth of assets in Hong Kong. When the wife was deported back to Hong Kong, she was arrested and charged with money laundering. Despite the absence of evidence to link her and her husband to the ice laboratory in Fiji, she was subsequently convicted on the grounds that they had no legitimate business to account for the accumulated wealth and the ways by which she used the assets were suspicious enough that it was reasonable to believe them to be the proceeds of crime. She was sentenced to 5 years imprisonment. Assets of the couple were also confiscated.

[11] Baker, R., 2005. *Capitalism's Achilles Heel*. New Jersey: Wiley. (p.100)

Given its instability and short lifespan, it is increasingly difficult to fully identify a criminal network or the crime it perpetrates. As Case Study 1 illustrates, an arguably more efficient way to bring these groups to the surface and fully identify them is to follow or trace back the profits generated from the crime. Money laundering investigation serves this purpose very well. Information derived from suspicious activity reports provides law enforcement with valuable clues in this respect. Investigation into the information will help illuminate what suspects are doing and where their assets are hidden, and more importantly, at the end provides us with evidence of their criminalities.

In simple terms, first, international cooperation is important in combating transnational crime as collective efforts will be more advantageous than what any single jurisdiction can achieve individually. However, the feasibility of international cooperation is not always guaranteed and therefore, while endeavoring to foster and enhance closer and more efficient cooperation with other jurisdictions at all fronts, LEAs should always be prepared to cope with the problem on their own in the absence of any such cooperation. Second, law enforcement structures need to be flexible. An over compartmentalized law enforcement structure may result in mismatch of resources and expertise with the problem it is dealing with. Third, LEAs need to be prepared to do more with less. A focus on outcome instead of output, and an approach targeting the "crime," the "people," and more importantly the "money" are the way forward for law enforcement if it wants to retain its effectiveness and relevancy. However, this is not to suggest that money laundering investigation offers a panacea to combating transnational crime, but it does without doubt offer increased opportunities to identify criminalities, to bring those responsible to justice, and to confiscate their ill-gotten gains. Combating transnational crime calls for a holistic approach. Without money laundering investigation any law enforcement efforts will be in vain.

Chapter 3
Money Laundering Investigation Regimes and Measuring Effectiveness

There is strong evidence from both the FATF Mutual Evaluations[12] and overseas law enforcement partners that the respective money laundering investigation regimes of the United States and Hong Kong are relatively well developed and do not have the common deficiencies found in other less developed regimes, such as: (a) poor resources or training; (b) corruption; (c) lack of basic investigative powers to conduct financial investigation; (d) money laundering investigation does not form a routine integral part of a criminal investigation, (e) poor collaboration with Financial Intelligence Unit ("FIU"); or (f) unwillingness or inability to respond to international cooperation.

Money Laundering Investigation Capability of Hong Kong

Given its relatively small size, the law enforcement structure in Hong Kong is simple when compared with that of the United States. There are three primary LEAs in Hong Kong, namely the Hong Kong Police ("HKP"), the Hong Kong Customs and Excise ("HKC&E"), and the Independent Commission Against Corruption ("ICAC"). ICAC is primarily responsible for corruption and bribery investigations, HKC&E is responsible for investigations relating to drug trafficking (importation), intellectual property rights, smuggling of dutiable commodities, etc., while the Hong Kong Police are responsible for all other criminal investigations. In each agency there are dedicated units charged with financial investigation, namely the Financial Investigation Division of the HKP, the Financial Investigation Group of the HKC&E, and the Financial Investigation Section of the ICAC. The latest FATF Mutual Evaluation commends Hong Kong that these units are well trained, sufficiently resourced, as well as highly skilled to pursue money laundering investigations.

The LEAs in Hong Kong are empowered with sufficient investigative powers and tools to pursue money laundering investigations such as production orders, search warrants and witness orders. Moreover, it is legally permissible for them to use special investigation techniques including controlled delivery, interception of telecommunication, and undercover operations, although their uses have been relatively few. These dedicated financial investigation units enjoy close collaboration with the Joint Financial Intelligence Unit ("JFIU"), the FIU of Hong Kong, which enables them to swiftly get hold of financial information derived from suspicious activity reports. In urgent cases, this can take place just within a matter of hours.

The latest FATF Mutual Evaluation notes that between 2003 and 2007, 786 persons were prosecuted in Hong Kong for money laundering ("ML") offenses, of which 465 persons were

[12] FATF, 2006. *Third Mutual Evaluation Report on Anti-Money Laundering and Combating the Financing of Terrorism: United States of America.* [online] Paris: FATF/OECD. Available at: http://www.gafi.org/dataoecd/44/9/37101772.pdf, accessed 8 March 2011; and
FATF, 2008 *Third Mutual Evaluation Report on Anti-Money Laundering and Combating the Financing of Terrorism: Hong Kong, China. [online*] Paris: FATF/OECD. Available at:<http://www.fatf-gafi.org/dataoecd/19/38/41032809.pdf, accessed 8 March 2011.

convicted. The FATF Mutual Evaluation commended that the number of ML prosecutions and convictions for the period under evaluation was reasonably high compared to other jurisdictions, which speaks for the effectiveness of the law enforcement investigative action, in particular the strong role taken by the Hong Kong Police. However, the Mutual Evaluation criticized that, by comparison, Hong Kong has relatively few cases of asset confiscation, and though such cases have been rising as a result of concerted government efforts, they are still not proportionate to the relatively high rate of money laundering conviction.

Money Laundering Investigation Capability of the United States

Unlike Hong Kong with only a few LEAs, the United States law enforcement structure is well known for its compartmentalization, with many LEAs of overlapping and laced with a great variety of multi-agency task forces. This not only serves to confuse overseas law enforcement partners but arguably also serves to confuse internally. It is difficult to find a simplified picture of all agencies and their respective jurisdictions and interactions, but as far as anti-money laundering is concerned they basically include the Federal Bureau of Investigation ("FBI"), Drug Enforcement Administration ("DEA"), Department of Homeland Security - Immigration and Customs Enforcement ("ICE"), and Customs and Border Protection ("CBP"); Internal Revenue Service Criminal Investigation; and the U.S. Postal Service. These agencies either have their own money laundering investigation capability or have designated units that specialize in money laundering investigation. On top of these agencies, there also exist multi-agency task forces spearheaded by different agencies targeting specific crimes. These task forces also possess money laundering investigation capability.

The LEAs in the United States are empowered with sufficient investigative powers to pursue money laundering investigations. Unlike their counterparts in Hong Kong, American LEAs are more willing to use special investigation techniques including controlled delivery, interception of telecommunications, and undercover operations to collect evidence—in particular for money laundering charges—and have achieved good results. The reasons for that will be elaborated in Chapter 4 (p.16).

The Financial Crimes Enforcement Network ("FinCEN"),[13] the FIU in the United States, is not a law enforcement model FIU. Instead of taking an active role in analyzing and disseminating suspicious activity reports, FinCEN entrusts that role to Suspicious Activity Report Review Teams, which are multi-agency teams set up across the country. FinCEN permits LEAs to directly query its database without a need for a formal request; and in addition, most of the LEAs have liaison officers posted to FinCEN to ensure and enhance collaboration with FinCEN. The latest FATF Mutual Evaluation criticized that FinCEN's analytical products do not appear to be particularly suited to LEAs in the United States, and there is a general perception among American LEAs that FinCEN's products are not too helpful to their investigations.

[13] FinCEN is the financial intelligence unit of the U.S., set up under the U.S. Treasury Department, in accordance with FATF Recommendation 26.

According to the FATF Evaluation, over a thousand persons are convicted of money laundering in the United States every year,[14] and the amounts of the assets seized and forfeited[15] are equally substantial.

Measuring Effectiveness

There are two international instruments which may possibly provide valid criteria for measuring the effectiveness of a jurisdiction's capability to interdict transnational crime through money laundering investigation, namely the FATF Recommendations and the articles of the United Nations Convention against Transnational Organized Crime ("UNOTC").

FATF Recommendations specifically require states to have money laundering investigation capability to, inter alia, investigate money laundering activities with a view to prosecution as well as to trace, seize, freeze, and confiscate crime proceeds. As a result, money laundering investigation has become the foci of considerable national and international law enforcement, and nearly every jurisdiction has now developed or is developing its own money laundering investigation capability in accordance with the requirements of the Recommendations. However, FATF Recommendations have attracted considerable criticism from the private sector, academics, rights advocates, and even anti-money laundering ("AML") practitioners. Apart from allegations of having constituted an over-inflated, inefficient, and exceedingly costly tool, in terms of both of the monetary cost to society, and of the non-monetary cost in the resultant severe diminution of citizens' privacy rights,[16] the FATF Recommendations are also criticized as being overly "compliance" based at the expense of a focus on "effectiveness."

While the Recommendations, in their present form and shape, are not perfect, they have nevertheless contributed greatly to moving jurisdictions toward a full harmonization of systems—legal, financial regulation, and law enforcement alike. This is very important and may be considered the first step toward overcoming the incompatibilities exploited by criminal groups and money launderers.

In the latest round of FATF Mutual Evaluations, both the United States and Hong Kong were rated "Compliant" on Recommendations 27 and 28,[17] which relate to money laundering investigation capability. These results reflect, to a certain degree, that both jurisdictions have relatively developed law enforcement regimes for anti-money laundering. However, does it mean that they are also effective in interdicting transnational crime? This may not necessarily be the case. FATF Recommendations have never been specifically designed for combating

[14] According to the Asset Forfeiture and Money Laundering Section of the U.S. Department of Justice, the number of money laundering prosecutions have reached 3,000 in recent years.
[15] FATF Mutual Evaluation Report on the U.S, (p.49): Amounts of proceeds forfeited: US$564.5 million in 2003, US$614.4 million in 2004 and US$767.4 million in 2005.
[16] Madsen, F., 2009. *Transnational Organized Crime*. London: Routledge. (p.103)
[17] The FATF reported a relatively high level of compliance for these recommendations, yet this did not necessarily correspond to a high degree of effectiveness, a disparity which the FATF is attempting to address in its current review of the standards.

crime. In the FATF's mandate, no specific reference has ever been made to combating crime although there appears to be an obvious causal relationship between anti-money laundering and combating crime. People take it for granted that if a LEA is doing well at anti-money laundering, it must also be good at combating crime. Over the years the efforts of the FATF have been inadvertently focused on combating money laundering (and terrorist financing) without paying appropriate regard to the root causes generating the tainted funds. This is understandable because if combating crime becomes part of the mandate of FATF, its works will become overly complex and cumbersome.

However, if sufficient reference is made to the root causes or predicate crimes, the Recommendations and their measuring criteria would encourage going after the key players of a crime, not just money launderers. For example, Recommendations 1 and 2 regarding money laundering offenses could be changed to require a jurisdiction to have money laundering offenses which encourage and enable that jurisdiction to prosecute prime offenders, who control the profits generated from the crime they orchestrate but will never get their hands dirty. In turn this would lead, in the evaluation process, to a more meaningful analysis and evaluation of the money laundering prosecution figures: a clearer picture of the number of key players vs. the number of professional money launderers vs. the number of front men. This is the way forward for FATF Recommendations and its evaluation methodology to evolve. These observations aside, it is generally agreed that FATF Recommendations and their criteria set out minimum requirements for an effective money laundering investigation regime. Apart from the minimum what else do we need to look for? Can UNTOC provide additional criteria?

UNTOC was adopted in 2000. It represented a major step forward in the fight against transnational organized crime. The convention contains 41 articles requiring signatories to put in place institutions and measures to fight against transnational crime including corruption. Similar to FATF Recommendations, UNTOC attempts to achieve a harmonization of institutions and closer international cooperation to prevent, deter, and detect transnational crime including corruption. However, unlike FATF, UNTOC has had little achievement in the implementation of its articles. Signatories of the Convention are still deliberating an implementation review or monitoring mechanism. One can imagine that this will take a very long time. In the absence of a review mechanism and a methodology, which interprets and elaborates the articles, it is difficult to envision this particular convention providing valid criteria to measure the effectiveness of a jurisdiction's money laundering investigation capability in interdicting transnational crime.

Back to Basics

Without valid criteria, how can a jurisdiction's capability to combat transnational crime through money laundering investigation be assessed? This study was originally intended to serve as a quantitative analysis of the enforcement figures of the United States and Hong Kong. The enforcement figures contained in their respective FATF Mutual Evaluation reports seem to suggest that both jurisdictions are doing quite well in netting money launderers. However, as argued in the preceding paragraphs, the FATF Recommendations may not provide the most relevant benchmark for the purposes of this study. On this

assumption, instead of spending time on collecting and analyzing statistics (or devising valid precise accessing criteria) a more valid approach may be to return to basics.

All the interviewees in this study unanimously agree that, in simple terms, an anti-money laundering investigation regime's ability to interdict transnational crime is effective *only if* the prime offenders or the masterminds—"the people"—can be prosecuted *and* their assets—the "money"—is forfeited as a result of the prosecution. This statement of effectiveness has a premise that there is strong will at the government level to combat transnational crime and law enforcement agencies are given sufficient resources to do so without fear of unnecessary political or corrupt interference. Both the United States and Hong Kong do not appear to have any problems with this premise. The words "*only if*" and "*and*" are italicized to emphasize two things. First, LEAs' efforts against crime are bound to fail if they do not go after the "people" and the "money," but equally there is no guarantee of success if they do so. Second, either prosecution or forfeiture alone is not enough. They have to take place together though not necessarily simultaneously.

Chapter 4
Strengths and Weaknesses

The statement of effectiveness highlighted in Chapter 3 contains two legal instruments, namely the criminalization of money laundering and the forfeiture of the proceeds of crime. An examination of these two instruments in the contexts of the United States and Hong Kong will be useful.

Money Laundering Offenses

There is a common criticism that money laundering offenses in many jurisdictions are unnecessarily complex, creating over-high burdens and tests that are very difficult to prove, which either deter investigators and prosecutors from targeting resources on it if they already have sufficient evidence to prove the predicate crime, or more commonly perhaps, they simply ignore it.[18] This is especially the case where the predicate crime takes place overseas and only the proceeds of the crime are dealt in the jurisdiction.

The United States criminalized money laundering in 1986 (Title 18 USC 1956 and 1957, Money Laundering Control Act of 1986, Pub. L. 99-570). Sections 1956 and 1957 criminalize four different types of money laundering: (a) basic money laundering [s. 1956(a)(1)]; (b) cross border money laundering [s.1956(a)(2)]; (c) money laundering in undercover operation [s.1956(a)(3)]; and (d) spending greater than US$10,000 in criminal proceeds (s.1957). To prove basic money laundering, it is necessary to prove:

(a) knowledge[19] of the proceeds of some form of unlawful activities;
(b) guilty intent to promote illegal activities, to conceal or disguise the proceeds of specified unlawful activities, etc.;
(c) the fact that property is indeed derived from specified unlawful activities; and
(d) the actus reus which must involve a financial transaction.

Aside from the fact that knowledge and intent are not ordinarily easy to prove, the laundering must also involve a "financial transaction," which either "in any way or degree affects interstate foreign commerce" or "involves the use of a financial institution." That means simply possessing or concealing illicit proceeds cannot be captured by this offense.[20]
For cross border money-laundering, in which criminal proceeds are moved in or out of the U.S., it is also necessary to prove the knowledge or intent of the accused, as well as the fact that the property is indeed the proceeds of specified unlawful activities. For offenses of

[18] Ringguth, J., 2002, Money Laundering – The Criminal Dimension, *"Stop Money Laundering Conference."* London, 26 February 2002. London: London Corporate Training Limited.
[19] Knowledge can be inferred by proof of willful blindness, deliberate ignorance, or conscious avoidance, please see *United States v. Flores*, 454 F.3d 149, 2 55-56 (3rd Cir.200) - willful blindness; United States v.Puche, 350 F.3d 1137, 1147 n.4, 1149 (11th Cir. 2003) – deliberate ignorance; and United States v. Hoffler-Riddick, 2006 WL 2381859, at *5 (E.D. Va.2006) – conscious avoidance.
[20] Please see *United States v. Garza,* 118 F.3d 278, 284-5 (5th Cir.1997) and *United States v. Ramirez,* 954 F.2d 1035, 1040 (5th Cir.1992): simple possession of criminal proceeds is insufficient to show there was a "transaction" under USC 1956 and 1957 offenses.

money laundering through undercover operations, though there is no need to prove the property is indeed the proceeds of specified unlawful activities, there is still a need to prove that the accused, knowing the property represented the proceeds of specified unlawful activities, conducted a financial transaction with intent to promote the specified unlawful activities, or to conceal or disguise the proceeds. As for the spending offense, apart from knowledge of the illicit nature of the property and the fact that it is indeed derived from specified unlawful activities, it is necessary to prove that the transaction must be a monetary transaction which is narrowly defined as a transaction conducted by, to, or through a financial institution. The maximum penalty for the first three categories is a fine and/or imprisonment for not more than 20 years. The maximum penalty for the spending offense is a fine and/or imprisonment for not more than 10 years.

It is plain enough that the money laundering offenses of the United States are complex. Some observers might conclude that the qualifications of the offenses render them unnecessarily limited in scope and difficult to prove. Although American prosecutors argued in the last FATF Mutual Evaluation that the gaps in the offenses were not significant and in reality there were few scenarios which would fall through the net, with the requirements of proving the knowledge and intent and other qualifications, it is easily conceivable that the offenses, in their present form, will not be effective in netting prime offenders or masterminds who are so good at insulating themselves. Apart from cases of undercover operations as per s.1956(a)(3), there are few prosecutions with only money laundering charge(s) because the evidence required for proving the money laundering charge is very often as much as that required for proving the predicate charge. This partly explains why U.S. law enforcement agencies are more enthusiastic to mount money laundering undercover operations and use special investigative techniques in their money laundering investigations. This overall situation is likely to impact collaboration between U.S. law enforcement and their overseas counterparts: one could doubt the ability of the United States to net a criminal who orchestrates crime abroad but hides his ill gotten gains in the United States, especially when overseas evidence of the crime is not available for one reason or another.

Very different from the U.S. offenses, the definition of money laundering offenses in Hong Kong are extremely simple and wide in scope. The offenses are respectively contained in section 25(1) of the Organized and Serious Crimes Ordinance ("OSCO") and the Drug Trafficking (Recovery of Proceeds) Ordinance ("DTROPO"), which read,

> "A person commits an offence if, knowing or having reasonable grounds to believe that any property in whole or in part directly or indirectly represents any person's proceeds of an indictable offence/drug trafficking, he deals with that property."

The term "indictable offense" is sufficiently broad for purpose and covers all serious offenses. "Dealing with" is also very wide and it includes receiving, concealing, disposing, bringing into or out of Hong Kong, or using the property in anyway. Proving an accused person's knowledge is not easy and it normally requires the accused's own admission, or evidence of an undercover operative or accomplice. To circumvent this, an objective element – "having

reasonable grounds" is included in the offenses. The phrase of "having reasonable grounds to believe" was explained by *HKSAR v. SHING SIU-MING & others, CA 415/97*.[21]

The offenses also contain an overseas provision, which reads,

> "…..references to an indictable offence include a reference to conduct which would constitute an indictable offence if it had occurred in Hong Kong."

This means that if someone brings in property derived from a crime in an overseas jurisdiction, whoever deals in the money locally commits an offense. The offenses, though framed in simple terms, are wide and generally all-embracing. It is not necessary to prove the commission of an indictable offense, nor is it necessary to prove the property is actually derived from an indictable offense. It is the "belief" rather than the "property," which matters;[22] and the belief is not that of the accused but that of a reasonable man. Moreover, unlike the money laundering offenses of the United States and many other jurisdictions,[23] money laundering offenses in Hong Kong contain no element of guilty "intent" or "purpose."[24] With such elements of "intent" or "purpose" the application of ML offenses may in some circumstances be circumscribed. The maximum penalty for the offenses is a fine and/or imprisonment for not more than 14 years.

There are recent cases where drug traffickers stored their proceeds in cash in their houses. This has yet to be become a trend but there is evidence, collaborated by the findings of the FATF Threat Assessment 2009, suggesting that criminals are increasingly aware of the risk of putting their ill gotten gains in banks.[25] There are also transnational cases where evidence of overseas predicate crime is not available for one reason or another. The applicability of the money laundering offenses of the United States in these scenarios is extremely limited. In

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[21] HKSAR v. SHING SIU-MING & others, CA 415/97, "..... This phrase, we are satisfied, contains subjective and objective elements. In our view it requires proof that there were grounds that a common sense, right-thinking member of the community would consider were sufficient to lead a person to believe that the person being assisted was a drug trafficker or had benefited therefrom. That is the objective element. It must also be proved that those grounds were known to the defendant. That is the subjective element ....."

[22] HKSAR v. LI Ching, CA 436/1997, "……We are satisfied if the Organized and Serious Crimes Ordinance is read as a whole that it was the intention of the legislature to concern itself with the Applicant 's belief. It is accordingly framed in wide terms. It is clear from the Reasons for Judgment of the Court that the Applicant had such a belief. There is nothing in section 25 to indicate that there is a requirement for the prosecution to prove the commission of the indictable offence referred to. What is required is to prove that the defendant had reasonable grounds to believe that the property represented any person's proceeds of an indictable offence. It is not necessary to prove the commission of the offence. ……."

[23] For example, the UK money laundering offenses require the subject property constitutes or represents a person's benefit from criminal conduct. The Australia money laundering offences requires the subject money or property to be proceeds of crime even though it is not necessary to prove a particular offence was committed in relation to the money or property; or a particular person committed an offence in relation to the money or property.

[24] For example, the money laundering offences of Ireland contain an element of "for the purpose of avoiding prosecution," the New Zealand money laundering offence contain en element of "for the purpose of concealing the property or enabling another person to conceal the property"; and that of the Canadian contains an element of "intent to conceal or convert property or proceeds."

[25] For a brief discussion of some of the implications of this trend, see Han Chang-Ryung, "Korea-U.S.-Cooperation against Bulk Cash Smuggling," The Brookings Institution, December 7, 2010, http://www.brookings.edu/papers/2010/1207_us_korea_smuggling_han.aspx.

fact, many money laundering prosecutions against prime offenders in Hong Kong would not have been possible if the scope of money laundering offenses were as limited in Hong Kong as they are in the United States. Please see Case Study 2 below:

Case Study 2

In an anti-triad operation, Hong Kong Police arrested a senior member of the targeted triad but failed to put together sufficient evidence against him for any triad-related offense. However, during a search of his residence, cash in the amount of of HK$1.7 million (US$217,000) wrapped in a brown package was found under the bed of the master bedroom. Under caution, he stated that the money was a loan from a friend but refused to disclose the identity of the friend or the purpose of the loan. Subsequent investigation revealed that the suspect had not ever filed any income tax return to the tax authority in the preceding five years, nor did he have any legitimate business which could account for the possession of large amount of cash in his residence. He was subsequently charged with money laundering; and was convicted after trial. The court was satisfied that the accused had reasonable grounds to believe that the funds represented the proceeds of crime. The grounds included the concealment of large amount of cash at residence, the nil tax return and the implausible excuse for loan while not being in debt. (Ref: NB RN 06000347).

There is argument that if a criminal is found to have significant unexplained wealth in the United States and there is insufficient evidence to charge him with a predicate or money laundering offense, he can be tried for tax evasion for the illicit wealth and the illicit wealth can be taken away by civil forfeiture – for example the famous Al Capone case. This to some extent compensates for the shortcomings in the scope of money laundering offenses in the United States – but sentences for tax evasion convictions are normally much lighter than money laundering convictions as the sentences would be based, according to the U.S. Sentencing Commission Guidelines, on 28 percent of the unexplained wealth (equal to the assumed tax loss for the U.S. government) instead of the total illicit wealth. There are also other remedies, such as the offenses of bulk cash smuggling and structuring, etc., but again sentences for these offenses are lighter than for money laundering offenses.

The treatment of money laundering offenses in Hong Kong is not without criticism. Though the offencss are well prosecuted and carry a maximum sentence of 14 years, the sentences awarded upon conviction, for most cases, are comparatively low. The heaviest sentence ever awarded was 10 years and most of the cases, even involving several millions (US$) in crime proceeds only result in sentences of 4 to 7 years. The Hong Kong Department of Justice and the Hong Kong Police should work together to assist the courts in Hong Kong to develop a sentencing guideline for money laundering convictions, which can reflect the different roles played by masterminds, professional money launderers and stooges, and can lead to heavier sentences for the former two groups of offenders.

Asset Forfeiture

Regarding asset forfeiture, the very significant difference between the United States and Hong Kong is that the U.S. enjoys both criminal and civil forfeiture regimes whereas Hong Kong only has criminal forfeiture. The asset forfeiture regimes of the United States are considered to be very well developed. American civil forfeiture laws have been enacted for a considerable period and have been increasingly utilized to good affect since the 1970s-1980s. Since the 1990s, other countries have recognized the benefits of both regimes and started to introduce civil forfeiture laws such that it has become a global trend, in particular for forfeiting terrorist funds and property. It is however noted that there has yet to be any international standard mandating a jurisdiction to have civil forfeiture.

In layman's terms, civil forfeiture is basically to put the property (i.e. the proceeds of crime), not the criminal, on trial. (In a criminal forfeiture, the conviction of the criminal is a perquisite for the forfeiture proceedings.) The prosecution only needs to prove, on the balance of probabilities, that the property is the proceeds of crime, thus shifting the onus of proof to the respondent, e.g. the owner of the property, without need to have any conviction of an accused. Apart from civil and criminal forfeitures, the United States also has administrative forfeiture which applies to uncontested cases and can be undertaken by a federal LEA as an administrative matter without a judicial proceeding. In fact, the vast majority of forfeitures in the United States are administrative forfeitures. As shown from the results of the latest FATF Mutual Evaluation on the U.S., the number of cases and the total amounts of forfeiture were impressive, speaking to the effectiveness of its asset forfeiture regime. Asset forfeiture has long been institutionalized in the United States as an integral part of criminal investigations into profit-generating crime.

As for Hong Kong, with the exception of drug trafficking-related cash found at the border and terrorist property, there is no general provision in Hong Kong laws for civil forfeiture of tainted property. Hong Kong basically has only criminal forfeiture. The primary asset forfeiture provisions of Hong Kong are set out in OSCO, DTROP and the Prevention of Bribery Ordinance.

The most recent comprehensive study of Hong Kong forfeiture and confiscation regimes, which was also the first of its kind, was the Hong Kong Civil Forfeiture Project ("HKCFP") led by Professor Simon Young of the Faculty of Law, University of Hong Kong.[26] The project aimed at identifying the most effective laws and policies to eliminate and deter profit-making crime in Hong Kong by means of interdicting the proceeds of the crime with reference to the experiences of some overseas jurisdictions including Australia, Canada, China, Ireland, South Africa, the United Kingdom, and the United States. The Project argues that the Hong Kong criminal forfeiture laws are underused and law enforcement actions against proceeds of crime are not satisfactory.

[26] Young, Simon N.M., ed., 2009.*Civil Forfeiture of Criminal Property: Legal Measures for Targeting the Proceeds of Crime.* Massachusetts: Edward Elgar Publishing.

This criticism is collaborated by the findings of the latest FATF Mutual Evaluation on Hong Kong.[27] The primary reason for the "unsatisfactory performance," of Hong Kong's LEAs and DOJ was that most of the profit-generating crimes in Hong Kong involved victims, e.g. theft, deception, fraud, etc., and the authorities would not initiate asset forfeiture proceedings where the victims were contemplating civil avenues of recovery. Victims of crime have to do so in case their losses have been transformed into other forms of property or co-mingled with other funds, as existing forfeiture laws give the courts no leeway to compensate them. Another possible contributory factor, based on experience, has been a relatively weak asset tracing and forfeiture culture. The Hong Kong Police are noted to have begun a series of initiatives in recent years to remedy this and the results remain to be seen.

There are also other deficiencies in Hong Kong asset forfeiture regimes. First, apart from low numbers of domestic forfeitures, the number of outgoing requests to overseas countries for enforcing forfeiture orders is relatively low, which again suggests that LEAs and DOJ in Hong Kong do not have a strong asset tracing and forfeiture culture. The other deficiency concerns asset sharing. The existing forfeiture laws of Hong Kong only facilitate sharing of assets confiscated pursuant to an external forfeiture order. Hong Kong can enforce an external forfeiture order issued by another jurisdiction under DTROP or the Mutual Legal Assistance in Criminal Matters Ordinance ("MLAO"). External orders enforceable in Hong Kong under DTROP include orders issued by Mainland China, but they must be related to drug proceeds. On the other hand, external orders enforceable under MLAO exclude orders from Mainland China, but are applicable to proceeds of all crimes.

In respect of assets forfeited pursuant to a domestic forfeiture order under DTROP or OSCO, currently there is no legal mechanism facilitating asset sharing with another jurisdiction even though the jurisdiction has provided substantial assistance to Hong Kong in the prosecution and forfeiture. The proceeds of realization of forfeited assets are all to be paid to the general revenue. This gap is certainly unsatisfactory from the perspective of international cooperation and fails to meet the growing international aspirations about asset sharing though there exists no international standard or obligation requiring Hong Kong to do so.

It is widely agreed by academics, law enforcement practitioners and prosecutors in Hong Kong that there exists a strong case for reforming the asset forfeiture laws of Hong Kong given its many deficiencies. At the same time, many in the legislative, legal and the private sectors have criticized Hong Kong's anti-money laundering laws for being draconian. Any attempt to further expand the scope of the regime, or powers of LEAs, etc., encounters barriers at several levels which the relevant policy bureaux appear unable to fully manage or address. This in part explains why the anti-money laundering laws and regime of Hong Kong has remained relatively static for years.

Is civil forfeiture absolutely necessary for Hong Kong? Many jurisdictions, including the United States, introduced civil forfeiture based on the rationale that it is often impossible to bring the masterminds to justice and civil forfeiture can be an important alternative to ensure

[27] FATF Mutual Evaluation Report on Hong Kong (p.44): No. of asset confiscation orders in Hong Kong between 2004 and 2007 are: 28 (2004), 19 (2005), 37 (2006) and 41 (2007).

that criminals cannot enjoy their ill-gotten gains. However, there is an argument that this rationale may not be appropriate to Hong Kong on the grounds that, given the robustness of its money laundering offenses, the evidence required to succeed in a civil forfeiture proceeding would have been sufficient to prove the money laundering offenses against the person possessing or in control of the property and criminal forfeiture will follow, so there is no need for civil forfeiture. This argument is correct to a certain extent, but would this always be the case? Can hearsay evidence, which is admissible in civil forfeiture proceedings, be admissible in hearings on a money laundering charge? Civil forfeiture does provide an alternative and sometimes more efficient way of going after the proceeds of crime, e.g. without first requiring a criminal conviction. This is particularly the case when criminals are becoming more adept at insulating themselves by exploiting globalization and technology. Put simply, the robustness of the Hong Kong money laundering offenses, upon which the regime relies, may not last indefinitely. It is time for policy makers to seriously consider the introduction of civil forfeiture if Hong Kong's legal and law enforcement institutions are to retain their effectiveness and relevancy to combating transnational crime.

After examining the respective primary legal instruments of the two regimes, let's now turn to their respective practical institutions. This study finds that LEAs in both the United States and Hong Kong possess similar investigative powers, practices and procedures for money laundering investigations. There are however a few relevant and significant differences in the following areas:

(a) Interdiction of the Proceeds of Crime
(b) Use of Special Investigative Techniques
(c) Domestic Collaboration
(d) International Cooperation

Timely Interdiction of Crime Proceeds in Transit

In the era of information technology, in which anonymity is easily achievable and funds can be transferred across jurisdictions in a minute through internet banking, it is imperative for any effective money laundering investigation regime to interdict proceeds of crime before their disappearance into the night – or another jurisdiction. This is not a matter of "efficiency." It remains a matter of "effectiveness" as proceeds of crime can only be forfeited if they can be traced and more importantly, stopped in a timely fashion. Once the proceeds of crime change their forms, e.g. from funds in a bank account to a cash withdrawal, or even worse once they leave a jurisdiction, substantial difficulties and barriers are added to the investigation.

Asset forfeiture normally comes with a restraint mechanism, which is a temporary judicial measure to prevent assets in question from being dissipated before a final decision on its disposal is made. Restraint mechanisms and proceedings are, however, equally complex and onerous. It takes weeks if not months for a judicial order to be issued. In Hong Kong there is a temporary administrative way of "holding" suspicious assets. After a reporting entity (such as a bank) has filed a suspicious activity report ("SAR") on suspicious assets, it needs to wait for the consent of the Joint Financial Intelligence Unit ("JFIU") for it to continue to deal with

the assets otherwise the reporting entity will run the risk of being prosecuted for money laundering if the assets are later confirmed to be the proceeds of crime. If the JFIU considers that the assets in question require to be investigated or may be subject to judicial restraint or forfeiture (including overseas forfeiture), it will withhold the consent and disseminate the SAR to an appropriate investigating unit for investigation or action. In practice, the JFIU will issue a "No Consent Letter" to the reporting entity. A "No Consent Letter" is not a court order and the reporting entity is not obliged to follow it. However, if the reporting entity disregards it and continues to deal with the assets, as detailed above, it may be liable to prosecution.

Therefore, reporting entities normally treat a "No Consent Letter" as a warning and will not deal further with the assets. The law is silent about the qualifications for JFIU to issue the "No Consent Letter." JFIU normally only issues the "No Consent" if it is satisfied that this course of action is *reasonable* and *proportionate* to the circumstances taking into account, inter alia, (a) the gravity of the case; (b) the impact on prevention and detection of crime if the assets are not "interdicted"; (c) the prospect of seeking a judicial restraint order within a reasonable period of time; and (d) the prospect of the victim seeking an injunction within a reasonable period of time. This arrangement conveniently provides LEAs with a means of holding suspicious assets pending investigation or application for a judicial restraint or forfeiture order.

In the United States, there is no similar administrative power for the Financial Crimes Enforcement Network ("FinCEN") or LEAs to "warn" reporting entities or temporarily "freeze" suspicious assets except that administered by the Office of Foreign Assets Control ("OFAC") of the U.S. Department of the Treasury, which basically enforces sanctions against targeted countries and regimes, terrorists, international narcotics traffickers, those engaged in activities related to the proliferation of weapons of mass destruction, and other threats to the national security, foreign policy or economy of the United States. Apart from that, U.S. LEAs can only seize suspicious assets with a seizure warrant judicially sanctioned and supported by "probable cause." Though it may only take a couple of days for a warrant to be applied and issued, it is long enough for the flight of suspicious assets.

Investigative Techniques

LEAs in the United States and Hong Kong share similar powers and techniques for money laundering investigation. There is however an interesting phenomenon that while special investigation techniques – such as controlled operations, sting operations, and interception of telecommunications – are commonly used U.S. money laundering investigations, they are used relatively less frequently in Hong Kong. This may be attributable to the robustness of Hong Kong money laundering offenses which makes special investigative techniques comparatively less significant for collection of evidence. Moreover, in Hong Kong admissibility of intercepts of telecommunications as evidence is explicitly prohibited by law and such inadmissibility to some extent diminishes the usefulness of telecommunications interception in combating crime and therefore discourages its use by LEAs in money laundering investigations.

The telecommunications interception law of Hong Kong was enacted in 2006 after a controversial legislative process amidst a spate of public criticisms. In a brief to the Legislative Council,[28] the Security Bureau reasoned that it had long been the policy of Hong Kong to not use telecommunications intercepts as evidence in legal proceedings in order to minimize the intrusion into the privacy of innocent third parties, as the intercepts would be subject to disclosure during legal proceedings. This explanation is hardly convincing, in particular when products of covert surveillance, video and audio alike – which are equally intrusive and which are regulated under the same ordinance – are admissible. Overseas experience also indicates that there has not been any issue over third party privacy when such intercepts are used as evidence; and more importantly there are abundant numbers of overseas investigations demonstrating beyond a doubt that evidence of telecommunications interception can prove to be the key element in the conviction of prime offenders and masterminds. The inadmissibility of telecommunications intercepts has to a great extent reduced the value of this investigative technique.

Domestic Collaboration

As a result of its compartmentalized and often confusing structure, the U.S. law enforcement regime is characterized by its many interagency task forces, permanent and ad-hoc alike. These task forces serve to pool together expertise from different agencies to achieve synergy in tackling specific problems, though most of these task forces are equipped with money laundering investigation capabilities. Such arrangements seek to minimize duplication of efforts, as well as to maximize intelligence and investigative capabilities. These task forces are particularly important for a large jurisdiction with complicated law enforcement structures like the U.S. Hong Kong's simple law enforcement structure does not initially appear to make them a necessity. However, criminals are becoming more opportunistic and are clearly becoming more indiscriminate regarding their choices of criminalities. Given the ease with which organized crime groups commit a wide spectrum of offenses, be they in the field of drugs (Police), pirated goods (HKC&E), corruption and/or bribery (ICAC), and tax fraud (Inland Revenue Department), it is surprising that interagency cooperation in Hong Kong, even at a working level, has been so limited. LEAs in Hong Kong need to be more receptive to the formation and use of interagency task forces as and when necessary.

Collaboration between Financial Intelligence Units ("FIUs") and LEAs is equally important for an effective money laundering investigation regime as an FIU is one of the primary sources of financial information and intelligence for LEAs. The Joint Financial Intelligence Unit of Hong Kong ("JFIU") is a law enforcement-model FIU. It is primarily staffed and operated by the Hong Kong Police, and is under the same command structure of the Financial Investigation Division ("FID") of the Hong Kong Police. There are certain advantages to this set up, as it ensures a very close working arrangement between the JFIU and FID, particularly with respect to sharing, analyzing and developing financial information; it offers assurance that each case disclosed by the JFIU will be assigned a higher priority for investigation than might be the case if the JFIU and FID were totally separate; and it avoids duplication of efforts in responding to international requests for assistance. Unlike JFIU, the

[28] Security Bureau, 2006. *Proposed Legislative Framework on Interception of Communications and Covert Surveillance* (CB(2)997/05-06(01)) Hong Kong: HKSAR.

Financial Crimes Enforcement Network ("FinCEN") of the U.S., is totally independent from LEAs but it has put in place measures to ensure collaboration with LEAs. For example, U.S. federal LEAs can directly access the FinCEN's database at their own terminals; LEAs also have liaison officers seconded to FinCEN to act as bridges between FinCEN and LEAs.

International Cooperation

LEAs in the United States and Hong Kong face similar difficulties in international cooperation, arising from non-harmonization of laws and judicial systems, differences in language, and law enforcement priorities. To circumvent these problems, U.S. LEAs have an extensive international legal attaché network (commonly known as "legat") to broker collaboration with international law enforcement agencies to drive investigations into transnational crime and support bilateral or multi-lateral cooperation; collect and exchange criminal intelligence in support of international law enforcement efforts; and enhance the capacity and the capability of international law enforcement agencies to combat transnational crime. For example, the FBI currently has 60 fully operational legat offices and 15 sub-offices, with more than 250 agents and support personnel stationed around the world.

Unlike the U.S., Hong Kong does not have a similar law enforcement legal attaché program. Hong Kong Police currently has two overseas liaison officers, one in Lyon and the other in Bangkok, but they actually work (on secondment) for Interpol, not the Hong Kong Police. It is recognized that "legats" can play an important role in narrowing down the differences between jurisdictions. They understand the limitations of the host jurisdictions in operational and practical terms and can reflect them to colleagues back home, and vice versa. They can discuss problems with their counterparts face-to-face, facilitating a quicker resolution. By understanding the differences and respective limitations, they can assist in developing an effective law enforcement response and investigative approach to transnational crime. Experience suggests this system ensures fast, efficient and effective cooperation because of the personal element that will always trump an electronic request from an unknown entity. While other international law enforcement partners like the US have found the benefits of "legat" network and are expanding in this way, it is an opportune time for the Hong Kong Police to consider introducing a similar network in strategically important jurisdictions in the region.

Over the years much has been done by both the United States and Hong Kong, at both government and agency levels, to foster international cooperation in (a) training and technical assistance; (b) intelligence exchange and operation; as well as (c) legal assistance in the areas of sharing of evidence, surrender of fugitives, and asset recovery. While impressive results have been seen at the first two levels of cooperation, cooperation at the level of legal assistance still leaves much to be desired as a result of the many deficiencies of the Mutual Legal Assistance ("MLA") arrangements. MLA is by nature a time consuming process and, at least from the perspective of the admissibility of evidence obtained, often a complicated process.[29] People are well aware of the many deficiencies of MLA but few bother to critically

[29] Cuthbertson, S., 2001. Mutual Legal Assistance in Criminal Matters Beyond 2000. *Australia Law Journal,* 75(5), p.326.

evaluate them and enact change. It is undisputable that MLA agreements often fail to keep up with the pace with which transnational crime develops and evolves. Simplifying request protocols, streamlining internal clearance procedures and lowering standards for admissibility of evidence are some of the ways to enhance the efficiency of MLA agreements. Prosecutors, law drafters, investigators and policy makers should now start working together to reengineer the MLA arrangements to ensure they remain fit for purpose.

Financial Intelligence Capability

The last thing to discuss is the financial intelligence capabilities of the U.S. and Hong Kong AML regimes. The LEAs on the two sides have very similar investigative powers and capabilities which enable them to cultivate, collect, collate and develop financial intelligence from various sources. One of the main differences of the two regimes lies on their financial intelligence units ("FIU"), i.e. the Financial Crimes Enforcement Network ("FinCEN") of the United States and the Joint Financial Intelligence Unit ("JFIU") of Hong Kong. FinCEN and JFIU were set up in accordance with the FATF Recommendations whose functions are to, inter alia, receive and analyze suspicious activity reports filed by reporting entities; as well as disseminate pursuable reports to LEAs for investigation. However, as previously discussed, unlike JFIU, FinCEN is not a law enforcement-model FIU and as such it does not have the investigative and intelligence capability of a law enforcement agency for intelligence development, in particular tactical intelligence development. Therefore, there are some reservations about its ability to add intelligence value to a suspicious activity report. Moreover, FinCEN relies wholly on LEAs – through SAR Review Teams set up by LEAs for reviewing incoming suspicious activities reports ("SARs") – to see whether the SARs are worthy of further investigation. It does not play any part or take any role in analyzing incoming SARs or deciding which SAR should be disseminated to LEAs for further investigation. FinCEN appears to fall short of the requirements of FATF Recommendation 26 in respect of analyzing and disseminating SARs.

The other difference between the two regimes is that there is both suspicious activity reporting and threshold reporting (reporting on transactions of US$ 10,000 or more) in the United States, whereas Hong Kong only has suspicious activity reporting. Threshold reporting is not a requirement under the FATF Recommendations; and there have been a lot of debates on its pros and cons. There are arguments that,

(a) It can enrich an FIU database but can also overload an FIU with raw information;
(b) While screening and analyzing suspicious activity reports has already stretched the resources of an FIU to the limit, an FIU simply does not have spare resources to manage the vast volume of raw information from threshold reporting;
(c) Threshold reporting information serves little tactical intelligence purpose but is good for data mining, trends and patterns identification;
(d) Threshold reporting can give LEAs more financial information about certain individuals just in case the information is needed but that does not seem to satisfy the "reasonably necessity and proportionality test" from a personal data protection perspective; and

(e) From a reporting entity's perspective, threshold reporting incurs substantial cost to a compliance system at the expense of resources for suspicious activity reporting.

These two differences explain the observations that the JFIU is good at tactical analysis and its analytical products are generally more welcomed by LEAs in Hong Kong, while FinCEN is rather weak in tactical analysis of SAR but has been more productive in typologies studies and strategic analysis.

Chapter 5
Conclusion and Recommendation

While both regimes have their respective strengths and weaknesses, as highlighted in the table shown below, this study is not able to draw any firm conclusions as to which regime is superior:

	United States	Hong Kong
Money Laundering Offenses	• Relatively narrow in scope and difficult to prove	• Wider in scope and easy to prove
Asset Forfeiture	• Comprehensive with administrative, civil and criminal forfeitures	• Limited with only criminal forfeiture
Interdiction of Crime Proceeds	• Court Order is required	• Crime proceeds can be interdicted rapidly by administrative means
Special Investigative Techniques	• Frequent use	• Less frequent
Domestic Collaboration	• Complex and compartmentalized law enforcement structure • Collaboration amongst LEAs is characterized by multiagency task forces • Collaboration between LEAs and FinCEN is achieved by liaison officers and SAR Review Teams	• Simple law enforcement structure • Close collaboration amongst LEAs and with JFIU
International Cooperation	• Overseas liaison officers help bridging transnational gaps	• Absence of overseas liaison officers
Financial Intelligence Capability	• Good at strategic intelligence analysis	• Good at tactical intelligence analysis

In brief, the U.S. money laundering investigation regime may be considered as very effective in going after the "money" though not necessarily the "people," whereas the Hong Kong regime is good at going after the "people" but not necessarily the "money." Despite the respective weaknesses, this study is restrained from concluding that either of the two regimes is *ineffective* in combating transnational crime because the enforcement figures and the

findings of the case studies do not seem to substantiate such a conclusion. However, given the fast changing environment and the challenges arising, it can be said with some degree of certainty that the effectiveness of the regimes would quickly be questioned if these respective weaknesses, as clearly identified for some period of time, are not addressed. Below are recommendations that the U.S. and Hong Kong authorities should seriously consider if they want their LEAs to retain their effectiveness and relevancy to combating transnational crime:

United States	(1) Simplify the definition of money laundering offenses, with reference to definitions in Hong Kong. (2) Introduce administrative measures to interdict crime proceeds with reference to the Hong Kong experiences. (3) Review FinCEN's roles in analyzing and disseminating suspicious activity reports and its capability in tactical intelligence analysis.
Hong Kong	(4) Develop a sentencing guideline for money laundering convictions. (5) Conduct a review of its asset forfeiture and sharing regimes with reference to U.S. experiences. (6) Consider to allow products of telecommunications interception admissible as evidence in criminal trials. (7) Be prepared ready to form multi-agency task forces to proactively target transnational crime groups. (8) Consider posting liaison officers at a small number of strategically important overseas locations to enhance cooperation with overseas jurisdictions.

At the multilateral international level, there are both general and specific recommendations:

General	(9)	Streamline the protocols and procedures, and lower the standards for admissibility of evidence associated with and required for Mutual Legal Assistance in Criminal Matters.
FATF	(10)	Consider to mandate jurisdictions to simplify and widen the scope of their money laundering offenses.[30]
	(11)	Consider to mandate jurisdictions to introduce civil forfeiture.[31]
	(12)	When formulating and reviewing its Recommendations and the Evaluation Methodology, pay sufficient regard to combating the underlying crimes in addition to anti-money laundering.
	(13)	When evaluating a jurisdiction's compliance with Recommendations 1 and 2, examine money laundering prosecution and conviction figures in a better perspective.[32]
UNTOC	(14)	Put in place without delay a mechanism similar to the FATF Mutual Evaluation to evaluate the implementation of the articles of the Convention by the signatories.

[30] Consider to incorporate an "objective mental element" into the offences and do away with the "element of intent", for example, amending Essential Criteria 2.1 of FATF Recommendation 2 as follows:

> *"The offence of money laundering should apply at least to natural persons that knowingly engage or having reasonable grounds to believe being so engaged in ML activity, without a need to prove any illicit intent.."*

[31] Consider to make Additional Element 3.7 of FATF Recommendation 3 an Essential Criteria.

[32] Apart from the total figures, it is important to examine the breakdown of the figures, e.g. number of prime offenders vs. number of professional launderers vs. number of stooges. The breakdown can clearly show the effectiveness of the money laundering offenses of a jurisdiction in going after the prime offenders and professional money launderers.

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