



THE USE OF FINANCIAL INSTRUMENTS BY CRIMINAL ORGANISATIONS FOR THE PURPOSE OF MONEY LAUNDERING

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Notkun glæpasamtaka á mismunandi fjármálagjörningum til peningaþvættis.

Grunnhugmyndin að baki þessarar rannsóknar er að lýsa hvernig peningaþvætti fer fram með því að útskýra tengslin á milli skipulagðrar glæpastarfsemi og fjármálastofnana. Í fyrsta hlutanum mun ég skilgreina hugtakið peningaþvætti sem fjármálaglæp. Þá mun ég gera grein fyrir núverandi aðgerðum gegn alþjóðlegu peningaþvætti, löggjöf og viðeigandi dómaframkvæmd. Hluti þessarar ritgerðar fæst líka við að bera saman regluverk gegn peningaþvætti á Evrópu, Íslandi og Ítalíu. Aðhafast Ítalir og Íslendingar nóg til að berjast gegn skipulagðri glæpa- og svikastarfsemi? Þá mun ég útskýra hvernig skuggabankakerfi virkar með því að greina algengustu aðferðir glæpamanna til að þvo ólögmætan ágóða í gegnum bankakerfið. Í öðrum hluta mun ég gera grein fyrir raunhæfu dæmi, lýsa bakgrunni þess og hvernig yfirvöld framfylgdu reglum gegn peningaþvætti. Ég mun einnig nefna nokkrar mögulegar lausnir til að takmarka sviksamleg viðskipti með tilkomu fjórðu tilskipun ES um peningaþvætti, með þróun siðsamlegrar bankastarfsemi og siðareglna fyrir banka og stofnun alþjóðlegs fjármáladómstóls og fullnustuviðmið til að koma í veg fyrir peningaþvætti milli landa. Niðurstaða þessarar ritgerðar er að frá ákveðnum sjónarhóli - þrátt fyrir lög og reglur gegn peningaþvætti – fyrirfinnst svik og fjármálaglæpir hvarvetna þó viðleitni stjórnvalda sé bæði umfangsmikil og flókin. Þessi niðurstaða er byggð á þeirri staðreynd, að það er verulegum vandkvæðum bundið að auðkenna rætur fjármálaglæpa, sem út á við eru lögmæt en eru samt í eðli sínu ólögmæt. Sem slík hefur ólögleg starfsemi vafalaust meiri efnahagsleg, stjórnmálaleg og félagsleg áhrif, sem er meiri en við getum ímyndað okkur vegna þess að hún er tengd í gegnum hin margvíslegustu svið daglegs lífs.

Abstract

The use of financial instruments by criminal organisations for the purpose of money laundering

The basic idea behind this study is to describe the features of money laundering, explaining the link between organised crime and financial intermediaries. In the first part, I will define the concept of money laundering as a financial crime, and I will identify the main structural factors of this phenomenon, providing an account of the current global AML regime, legislation and related case law. A comparative study between the European, Icelandic and Italian anti-money laundering regulations is also part of this thesis. Are Italy and Iceland doing enough to combat organised crime and their fraudulent activities? Furthermore, I will analyse the most common financial instruments and methods used by criminals to launder illicit proceeds through the banking system. In the second part, I will take real study-cases and anti-mafia operations in Italy, describing the background of the crime committed and how the authority enforced the anti-money laundering rules. I will also give some possible solutions to limit fraudulent transactions, through the upcoming EU Fourth Money Laundering Directive, the development of ethical banking, the establishment of an international financial criminal court, and the enforcement of measures to prevent money laundering between nations. The conclusion of this thesis indicates that from a certain standpoint - in spite of anti-money laundering laws and regulations - fraud and financial crimes are everywhere, although authorities' efforts are large and complex. This conclusion is based on the fact that there is a real substantial difficulty identifying the criminal origin of an economic activity, outwardly entirely legal, but characterized by a hidden delinquency. As such, illegal enterprises undoubtedly have an economic, political and social power that is bigger and higher than imagined, because they are linked in the most varied sectors of everyday life.

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LIST OF ABBREVIATIONS

AML	Anti-Money Laundering
AMLD	Anti-Money Laundering Directives
BCBS	Basel Committee on Banking Supervision
CDD	Customer Due Diligence
EBOCS	European Business Ownership and Control Structures
ECJ	European Court of Justice
ECtHR	European Court of Human Rights
Egmont Group	Egmont Group of Financial Intelligence Units
EP	European Parliament
EU	European Union
FAIS	FinCEN Artificial Intelligence System
FATF	Financial Action Task Force
FINCEN	Financial Crimes Enforcement Network
FIU	Financial Intelligence Unit
GPML	Global Programme against Money Laundering
ICC	International Criminal Court
ICJ	International Court of Justice
IFCC	International Financial Criminal Court
INTERPOL	International Criminal Police Organization
IT	Information Technology
LSE	London Stock Exchange
MEPs	Members of the European Parliament
OECD	Organisation for Economic Cooperation and Development
KYC	Know Your Customer
SBS	Shadow Banking System
SIV	Structured Investment Vehicle
UNODC	United Nation Office on Drugs and Crime

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European Court of Justice

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Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime (adopted 8 November 1990, entered into force 1 September 1993) European Treaty Series, No. 141.

European Convention for the Protection of Human Rights and Fundamental Freedoms (adopted 4 November 1950, entered into force 3 September 1953) as amended by Protocol No. 11, Nov. 4, 1950, 213 U.N.T.S. 221 [hereinafter ECHR].

International Convention for the Suppression of the Financing of Terrorism (adopted 9 December 1999, entered into force 10 April 2002) United Nations, Treaty Series, vol. 2178, p. 197.

United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances (adopted 19 December 1988, entered into force 11 November 1990) United Nations, Treaty Series, vol. 1582, p. 95.

United Nations Convention against Transnational Organized Crime (adopted 15 November 2000, entered into force 29 September 2003) United Nations, Treaty Series, vol. 2225, p. 209.

TABLE OF LEGISLATION AND PREPARATORY LEGISLATION

Iceland:

Act on measures against money laundering and terrorist financing, No. 64/2006 as amended by Act No. 77/2008, Act No. 116/2009 and Act No. 41/2012 (Official Translation).

Italy:

Legislative Decree 231/2007, implementation of Directive 2005/60/EC on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing, published in *Gazzetta Ufficiale* no. 290 of 14 December 2007- Ordinary Supplement no. 268/L (Official Translation).

EU Directives:

Council Directive 91/308/EEC of 10 June 1991 on prevention of the use of the financial system for the purpose of money laundering, OJ L 166 28.06.1991 p. 77–83.

Directive 2001/97/EC of the European Parliament and of the Council of 4 December 2001 amending Council Directive 91/308/EEC on prevention of the use of the financial system for the purpose of money laundering, OJ L 344, 28.12.2001, p. 76–82.

Directive 2005/60/EC of the European Parliament and of the Council of 26 October 2005 on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing, OJ L 309, 25.11.2005, p. 15–36.

Spain:

Law 19/1993 on specific measures for preventing money laundering (*Ley 19/1993 sobre determinadas medidas de prevención de blanqueo de capitales*) of 28 December 1993 (BOE No 311 of 29 December 1993, p. 37327).

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1. INTRODUCTION

Over the past few years, the international financial market has undergone important changes, characterized by the exponential growth of new trading techniques and innovative banking products. More specifically, banks have developed original and complex instruments - like prime bank guarantees, debentures, bonds and other securities - to meet the specific needs of borrowers; nevertheless the complicated nature of these agreements tends to help those wishing to make fraudulent transactions. In parallel, criminal organisations have adapted very quickly to the socio-economic changes of the last decades, being able to take advantage of new dynamics resulting from the global finance market.

In such an intricate situation, the money laundering operation plays paramount role in the transformation of liquidity of illicit origin. The recycling phase is the crucial moment of contact between honest and dishonest business, and for this reason, the financial system has to proceed in order to eliminate the possibility of these illegal operations, working jointly with governments for a better and fairer economic future. In general, it must be said that the proceeds derived from illegal activities, and recycled with sophisticated techniques, ensures huge profits to organised crime. In order to conceal a fraudulent activity, money launderers use different tools, often finding a path without obstacles through intermediaries and offshore companies in countries with permissive laws.

As a consequence, unlawful schemes raise an extremely significant matter with regard to prevention, detection and prosecution,¹ because the boundaries between legal and illegal economy have become much less obvious than before. The lines of demarcation between white collar crime and organised crime can also be blurred,² as both involved illegal activities through enterprises. However, the main difference between the two is that „white-collar criminals try to profit off of legitimate businesses in a nonviolent method of action, while organised crime seeks profits through illegal schemes and frequently employs physical intimidation and violence”.³ As a matter of fact, we are facing a new reality, where the difference between the previous models of gangsters is substituted by those of highly-

¹ Paul Allan Schott, *Reference Guide to Anti-Money Laundering and Combating the Financing of Terrorism* (Second Edition, The World Bank 2006) I-1.

² David O Friedrichs, *Trusted Criminals: White Collar Crime in Contemporary Society* (4th ed, Wadsworth Cengage Learning 2010) 199.

³ JRank Articles, 'White-Collar and Organized Crime' <<http://law.jrank.org/pages/12381/White-Collar-Organized-Crime.html>> accessed 27 August 2014.

educated criminals supported by financial experts. Besides that, the *financialization* of the economy⁴ - which refers to a „finance-dominated” accumulation regime of capital market without any legal basis⁵ - has favoured the strengthening of white-collar crimes.

Therefore, the laundering and the use of funds, goods or assets of unlawful origin constitute a real danger for a plurality of reasons. The fight against economic crimes needs cooperation from both financial institutions and governments, because, in recent years, the proceeds of illegal activities had worryingly significant implications for the integrity of the banking system. Eliminating money laundering could compromise organised crime groups in their vital stage; consequently, it is only using special investigative techniques that it will be possible to prevent fraud and to trace illicit financial transactions. The importance of anti-money laundering in current international relations has grown considerably in the last 20 years. Therefore, the development of a common approach is now an important issue for the global financial integrity, bearing in mind that it is very difficult to prevent organised crime activities. When the money launderers corrupt the banking system, they also slowly destroy the world's economy; as demonstrated by the investigative experience, it is a complex crime that is not easily identified immediately.

Although terrorist financing is also a topic that concerns money laundering, in this thesis, it will not be treated but only rarely mentioned within the measures taken by the international community.

⁴ Gerald A Epstein, *Financialization and the World Economy* (Edward Elgar 2005) 3.

⁵ Martin H Wolfson and Gerald A Epstein, *The Handbook of the Political Economy of Financial Crises* (Oxford University Press 2013) 12.

2. MONEY LAUNDERING ISSUES

2.1 Introduction

In this chapter, some important concepts related to money laundering will be defined. The aim is to describe the nature and the negative effect on economic development of such fraud, and to illustrate some of the structural points related with these issues. Although, the direct and indirect effects of this crime are sometimes difficult to estimate, here certain factors favouring the spread of fraudulent activities will be discussed in more details. This is a multidisciplinary topic, because money laundering covers many different subjects, such as: the globalisation of crime; the political regulatory, social, criminological, anthropological and economic aspects;⁶ and the link between the shadow banking system and offshore centre. Undoubtedly, it is one of the most alarming crimes across economically advanced nations. The need to prevent and respond to this offence arises from purely social needs, but also to prevent the economic destabilization, because money laundering can alter the allocation of resources, or it can create a wide spectrum of market malfunctioning, including unfair competition. As mentioned above, the *financialization* on the economy has provided increased options for illegal activities such as white-collar crimes. Further, the longstanding practice of laundering the huge sums of money generated by illegal enterprises, classified as a white-collar crime itself, obviously requires some complicity on the part of banks, which benefit from these large deposits.⁷

The financial system in general and banks in particular play an important role in this mechanism. In order to deal with that situation, the cooperation between governments and banks is the focal point both in the fight against money laundering, both in the discussion that revolves around the related legislation. On this basis, banks' internal control systems are increasingly sophisticated, creating an effective regulator tool to fight this practice, but they did not go far enough. Generally, there is a confusing lack of uniformity on the international anti-money laundering requirements which standardize the entire system. Therefore, the importance of combating this phenomenon becomes more and more essential; for this reason, banks should no longer operate just to avoid their involvement in accepting money from illegal sources or from criminal business, but they also have to contribute actively by providing a concrete cooperation with the financial and judicial supervisory authorities.

⁶ Brigitte Unger and van der Linde Linde, *Research Handbook on Money Laundering* (Edward Elgar Pub 2013) 3.

⁷ Friedrichs (n 2) 199.

2.2 Money laundering definitions

This preliminary overview cannot proceed without explaining what the law intended with the term *money laundering*. Article 6 of Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime, which states as following, gives a legal definition of money laundering:

Each Party shall adopt such legislative and other measures as may be necessary to establish as offences under its domestic law, when committed intentionally: (a) the conversion or transfer of property, knowing that such property is proceeds, for the purpose of concealing or disguising the illicit origin of the property or of assisting any person who is involved in the commission of the predicate offence to evade the legal consequences of his actions; (b) the concealment or disguise of the true nature, source, location, disposition, movement, rights with respect to, or ownership of, property, knowing that such property is proceeds; and, subject to its constitutional principles and the basic concepts of its legal system; (c) the acquisition, possession or use of property, knowing, at the time of receipt, that such property was proceeds; (d) participation in, association or conspiracy to commit, attempts to commit and aiding, abetting, facilitating and counselling the commission of any of the offences established in accordance with this article.⁸

Generally, it is a procedure which consists of a set of illegal actions designed to hide, conceal or otherwise obstruct the investigation about the illicit origin of the resources or assets used in a financial transaction. According to this definition, the cash obtained through an unlawful activity enters with a *lawful semblance* in the economic cycle. In practice, it is the act of investing the proceeds of criminal business in legitimate activities, and it is one of the phenomena on which rests the submerging economies. Consequently, it constitutes an offense for which a criminal indictment is expected; therefore, its criminalization is seen as a tool in the fight against organized crime. Self-money laundering is another aspect of the crime and it can be punished by law; therefore, it is the case where the criminal may also have committed the predicate offence, laundering his "own proceeds". Third-party money laundering, instead, is more common, as the crime is committed by a person other than the author of the offence.⁹ In most cases, it usually occurs in three stages: 1) in the *placement stage*, cash generated by criminal activity is deposited into financial institutions, removing the capital from its place of origin; 2) in the *layering stage*, the funds are transferred to further obscure their illicit origin

⁸ Council of Europe: Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime (adopted 8 November 1990, entered into force 1 September 1993) European Treaty Series, No. 141. <<http://conventions.coe.int/Treaty/en/Treaties/html/141.htm>> accessed 30 September 2014.

⁹ Neil Boister, *An Introduction to Transnational Criminal Law* (1st ed, Oxford University Press 2012) 105–106.

and hamper the audit trail,¹⁰ disassociating the cash from its source; 3) in the *integration stage*, the funds are reintroduced into commerce in such a way that there is a legitimate explanation for them,¹¹ bringing the laundered money back into the legal economy.¹² As a result, these performances can harm parts of the banking system and undermine normal governance; once bank managers or supervisors have become corrupted or intimidated by the massive amounts of money involved in the process, non-market behaviour can be introduced into operating areas other than those directly related to the money laundering, which creates risks for the safety and integrity of the bank, or it can reduce the effectiveness of supervision.¹³ However, not all fraudulent transactions involve just these three stages, but there are cases where the phases are much more complex and stratified. Nonetheless, the doctrine uses this classification because it is an easy way to explain what often can be an intricate process. The three-stage process involved in money laundering will be discussed more in detail in Chapter Four, where I will explain the way in which the Italian organised crime launders dirty money.

2.2.1 Organised crime and illicit financial flows

The European Parliament (EP) has stated that organized crime consists of the following characteristics: it is a criminal conspiracy with an organizational structure, like an entrepreneurial company, aimed at the commission of crimes, from which derive financial income to be transferred into the legal economy.¹⁴ More precisely, as stated in the Framework Decision (2008/841/JHA) on the fight against organised crime:

criminal organisation means a structured association, established over a period of time, of more than two persons acting in concert with a view to committing offences which are punishable by deprivation of liberty or a detention order of a maximum of at least four years or a more serious penalty, to obtain, directly or indirectly, a financial or other material benefit.¹⁵

¹⁰ Steven Mark Levy, *Federal Money Laundering Regulation: Banking, Corporate, and Securities Compliance* (1st ed, Aspen Publishers 2003) 2–5.

¹¹ Steven Mark Levy (n 10) 2–5.

¹² Frank G Madsen, *Transnational Organized Crime* (Routledge 2009) 106.

¹³ Peter Alldridge, *Money Laundering Law: Forfeiture, Confiscation, Civil Recovery, Criminal Laundering, and Taxation of the Proceeds of Crime* (Hart Pub 2003) 35.

¹⁴ European Parliament: Special committee on organised crime, corruption and money laundering, *Working document on organised crime* (1 October 2012).

<http://www.europarl.europa.eu/meetdocs/2009_2014/documents/crim/dt/913/913961/913961en.pdf> accessed 27 October 2014.

¹⁵ Official Journal of the European Union, *Council Framework Decision 2008/841/JHA*, 24 October 2008.

<<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2008:300:0042:0045:EN:PDF>> accessed 27 October 2014.

Thus, it is important to track the profile of those that launder criminal money, keeping in mind that this process can involve several subjects, because a person that conceals the illegal income is not necessarily the one that commits predicate offenses. However, in most jurisdictions, anyone who helps a criminal organization, like notaries or real estate agents, is a money launderer himself, unless he is unaware of the fact that his professional knowledge is helping mobsters to better launder their illegal proceeds. Furthermore, those who are engaging in this crime generally operate according to business logic and therefore cannot avoid the general rules of the global economy; such as the profit maximization through an efficient allocation of resources. For this reason, *launderers* are in tune with the evolution of economic and financial systems, which, in a context characterized by the globalization and technological evolution, requires the adoption of a multinational approach. As is well known, illicit cash flows are often run by organised crime.¹⁶ Nevertheless, it is hard to provide a complete description of all possible entities and methods developed for the laundering of illicit profits. Generally, these types of crimes are in the collective thought linked to organized crime, especially Mafia-type organizations. Accordingly, my analysis will focus on their economic criminal activities.

2.3 Structural factors of money laundering

It can be said that criminals need money laundering in order to efficiently use the huge amounts of illegally obtained funds, which are generated from their fraudulent activities. Hence, it is broadly prohibited by law since it generates unacceptable distortions in the economic cycle, altering the normal mechanisms of capital accumulation and funding sources for enterprises. It has a negative impact on the long-term economic development, because it reduces productivity by diverting international trade and capital flows, and it promotes crime and corruption, which in turn depress economic growth itself. Sometimes, even successful enterprises are transformed by criminals into unproductive activities for the purposes of hiding ill-gotten money. Furthermore, money laundering has a more direct negative effect whenever organised crime redirects resources to less-productive assets or luxury imports, such as real estate, jewellery, and automobiles. Generally, the economic impact also concerns unfair competition between legitimate and illegitimate actors, distortions between asset prices, negative effects on private investment, and eventually the crowding out effect on the

¹⁶ Guy Stessens, *Money Laundering a New International Law Enforcement Model* (Cambridge University Press 2000) 9–10 <<http://dx.doi.org/10.1017/CBO9780511494567>> accessed 26 August 2014.

growth of honest business.¹⁷ Besides that, it can generate entrepreneurial phenomena that, because of the ease of capital retrieval, are more competitive than others, despite an unprofitable activity or any financial liabilities accumulated. Therefore, criminals distort the natural mechanisms of market competition, keeping prices down and causing unemployment. Although authorities' efforts are large and complex, the negative effects of such activity are many and difficult to quantify.

In this environment, organised crime has a large sphere of influence, which also creates a negative effect on social development because of the methods, the organisational structures that it adopts and the huge amount of financial resources at its disposal. Hence, social effects include increases in corruption, because laundering needs accomplices and helpers, so more and more people are drawn into criminality, attracted to the benefits of being a member of a criminal organization.¹⁸ As regard the political effects, criminal influence can undermine democratic systems, especially in developing nations, eroding the integrity of banks, non-bank financial institutions and equity markets. Consequently, all of these institutions are vulnerable to corruption due to the massive flow of money; under such conditions, the impact can be extremely disproportionate, because the bribery of government and bank officials can lead to poverty and unemployment.

The global strategy adopted is basically geared to prevent and deal with the accumulation of illicit capital flows and the traceability of the investments made through criminal activities. By contrast, the adoption of strict anti-money-laundering policies can reinforce the development of these critical points, and it can deter such fraud in future. Unfortunately, offshore financial centres and some governments are very slow in putting in place effective policy measures; on the contrary, their administrative and criminal penalties are not strict enough to stop organized crime.

2.3.1 Money laundering and globalisation

Among the structural factors of money laundering, it is import to isolate four points which are of particular significance: 1) the globalisation of markets and the continuing integration also with those of emerging economies; 2) the adoption of the common currency in the European context; 3) the technological advances in the field of communication through Internet and other online systems; 4) the increasing sophistication of financial products and services.

¹⁷ Unger and Linde (n 6) 4.

¹⁸ Unger and Linde (n 6) 4.

Thanks to globalisation, the geography of crime expands exponentially, and the task of combating money laundering became absolutely imperative, necessary and urgent.¹⁹ As a consequence, criminals use the globalisation of the banking sector to quickly convert funds into various products and with the appearance of legitimacy. Therefore, they are primarily focused on generating illicit profits which are then hidden from police investigation. In practice, there has been a rapid development in financial information systems, which allow capitals to move anywhere in the world more easily.²⁰ In a context of new international opportunities, local criminal organisations can instantly transfer enormous amounts of money through personal computers and satellite dishes.²¹ As soon as illicit financial flows get into the international banking system, the more difficult it is to identify their origin; furthermore, due to the hidden nature of these types of transactions, it is hard to estimate the total amount that goes through the laundry cycle.²² In fact, globalisation has created an increasingly interdependent world,²³ which gives transnational organised crime a significant and growing power in the global economy. As we will later see, although the European Union (EU) and the United Nations (UN) have established special bodies and regulations to combat money laundering, the lack of coordination and cooperation between countries, the inconsistent application of international treaties and accords,²⁴ and the exponential growth in the intensity of financial globalisation seem to favour this process.²⁵ Criminal organisations have strategic business objectives, and, apparently, they are like any other legal enterprises, investing everywhere in the world. The new model followed is to invest the proceeds of illegal activities abroad, establishing business ventures between foreign and local crime. Undoubtedly, the integration into the world economy has created opportunities for crime and criminality, contributing to the weakening of the rule of law.²⁶ Therefore, the global governance is still not able to stop this transnational phenomenon that negatively affects our

¹⁹ Arthur M Mitchel, *Manual on Countering Money Laundering and the Financing of Terrorism* (Asian Development Bank 2003) 10.

²⁰ Arthur M Mitchel (n 19) 10.

²¹ Howard Abadinsky, *Drug Use and Abuse: A Comprehensive Introduction* (Eighth edition, Wadsworth/Cengage Learning 2014) 252.

²² Mitchel (n 19) 10.

²³ Sheila L Croucher, *Globalization and Belonging: The Politics of Identity in a Changing World* (Rowman & Littlefield 2004) 13.

²⁴ James R Richards, *Transnational Criminal Organizations, Cybercrime, and Money Laundering: A Handbook for Law Enforcement Officers, Auditors, and Financial Investigators* (CRC press 1999) 277.

²⁵ David Held, *Global Transformations: Politics, Economics and Culture* (Stanford University Press 1999) 234.

²⁶ Mats R Berdal and Mónica Serrano (eds), *Transnational Organized Crime and International Security: Business as Usual?* (Lynne Rienner Pub 2002) 34.

societies and economies; but it also erodes the independence of some countries and their ability to follow a path of development.

2.3.2 Criminal finance in the European and global economies

The most disastrous consequences of money laundering are to be considered with special regard to the European and global economies. The fight against organised crime groups involves many things that have to be done to face these challenges with the appropriate tools. Money launderers are some of the most important and the largest financial players in our economic system, and their strategies are progressively affecting the way financial institutions deal with national policies. Furthermore, the advent of the euro has contributed to the increase of criminal opportunities.²⁷ With the entering into force of the common currency, the exchange of huge amounts of funds within the European Union has certainly been facilitated; accordingly, the phenomenon of money laundering has reached alarming proportions in a short period of time, which has generated an estimated turnover of millions of euros.

For a very long time, the U.S. dollar has been the preferred currency for illegal transactions, because of its large domestic market for goods and services, its ready convertibility into gold or other precious metals, and its spread around the world. The newly unified currency has become a rival to the American dollar for financial fraud activities, thanks to a general use in all the nations that are interested in doing business in Europe, and to all the international trade of European Union Member States. The euro simplifies the process of money laundering, because „it eliminates the need to transfer a certain amount of money into another national currency” before changing into US dollars.²⁸ In the past, if a crime brought French francs, there was the need to *pre-wash* that amount of money into another national currency, like Italian lire, as the main objective of criminals is to split the currency from the crime and where it occurred. Today, there are fewer steps because the euro is already the second reserve currency in the world.

Consequently, the need for actions aimed at combating this process cannot be postponed; subsequently, the EU member countries have started to harmonize national legislation and to adapt their own regulations to the common goal of countering money laundering activities. Therefore, the intent is to establish an active partnership with banking intermediaries, which

²⁷ D.M.P. McCarthy, *An Economic History of Organized Crime: A National and Transnational Approach* (Routledge 2011) 34.

²⁸ D.M.P. McCarthy (n 27) 34-35.

are also the actors most involved by criminal organisations to hide the money's illegal origin. However, the absence of global appropriate measures to counter this crime has prompted the European Union to issue directives concerning the fight against money laundering, such as 2005/60/EC.²⁹ Unfortunately, this still doesn't seem enough to ensure the uniform treatment of this offense, as the Directive leaves to Member States the choice of appropriate regulations.

2.3.3 Advances in communication technology and their impact on financial fraud

New IT systems are increasingly being used for both money laundering violations and initiatives against them; as a consequence, the advances in communication technology imply positivity, freedom and democratic processes on one hand, and lend themselves to critical, negative and illegal uses on the other. All banking and financial transactions are treated, stored and transmitted through telematics systems, capable of providing significant contribution to speed up the transfer of money and capital investment. For this reason, fraudulent activities need to be viewed considering a number of different factors such as: 1) the telecommunications revolution; 2) the possibility to convey information and messages of all kinds in real time and in any part of the world; 3) the advent and popularization of information technologies; 4) the global Internet usage that does not take into account the geographical boundaries of legal jurisdictions.

In recent years, the investigative experience has shown that the most determined and sophisticated criminal organisations use information technologies in their illegal business. For example, the use of electronic funds transfer systems raises important questions, as money launderers can send money via online banking to offshore companies, to then redirect the cash flow to the country of origin in the form of loans or payments to their own enterprises. As a result, they are able to recover a massive amount of capital through their financial intermediaries, insofar as criminal organisations have no difficulty in hiding the identity of the last beneficiary, complicating the process with multiple transactions, or using incompressible stratified schemes. Finally, because there are dozens of intermediate steps, it becomes very hard to ascertain the real initiator of the electronic funds transfer. It must be added to this scenario that too many governments, *tax havens*, offshore banks and nonbank

²⁹ Directive 2005/60/EC of the European Parliament and of the Council of 26 October 2005 on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing, OJ L 309, 25.11.2005, p. 15–36. <<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2005:309:0015:0036:en:PDF>> accessed 1 October 2014.

financial institutions (like exchange houses, brokerage houses or check-cashing services) still refuse to give information about suspicious transactions, which could facilitate international investigations.³⁰

2.3.4 Increasing sophistication of financial products and services

Money laundering has become a big issue for the world's economy, damaging the authority and credibility of the banking system. This problematic area arises from a variety of factors because the impact varies considerably in different contexts. Generally, the presence of organised crime in many societies is a considerable risk to the stability of markets and their development, especially in underdeveloped nations. Often, the recycling of *dirty money* flourishes in economies with a weak banking system, a large underground economy, a poor institutional quality, or a low corporate governance.³¹ Criminals regularly attempt to launder their illicit proceeds in order to place them with the appearance of legitimacy beyond the reach of the law enforcement and prosecution authorities, utilizing the complexity of financial products and services to their benefit. In this respect, the use of banks can also allow them to convert or transfer funds into various entities - such as bank drafts, wire and telegraphic transfers, electronic payment systems, loan back schemes, and correspondent or offshore banking accounts.

As a consequence, financial institutions are making an effort to track illegal asset transfers, and to improve their anti-money laundering regimes, so that they can prevent or limit such fraud in future. Because international criminal organisations know how to avoid controls and investigations, banks should be able to recognize unusual transactions and behaviours by monitoring them through internal data management. The most effective solution here is probably to immediately hit the financial resources of the Mafia groups; as soon as a criminal entity decides to launder money, it is also the right time to combat and prevent the crime. Sometimes, even analysing the entire data set could not be enough to identify suspicious patterns, as there may be missing or incorrect information. Moreover, transnational criminal organisations spend a lot of money to pay highly educated people, to make sure that as soon as authorities are investigating a suspicious activity, they stop using the old scheme, coming up with new ways to hide illegally obtained gain.

³⁰ Pierre-Laurent Chatain (ed), *Preventing Money Laundering and Terrorist Financing: A Practical Guide for Bank Supervisors* (World Bank 2009) 256.

³¹ Guillermo Calvo, *Unlocking Credit: The Quest for Deep and Stable Bank Lending*. (Inter-American Development Bank ; Distributed by the Johns Hopkins University Press 2004) 246
<<http://site.ebrary.com/id/10089227>> accessed 30 August 2014.

In the next paragraphs, therefore, the acts of various international bodies will be reviewed, such as the UN Conventions, the Basel Committee on Banking Supervision (BCBS), the Council of Europe, and the Financial Action Task Force on Money Laundering (FATF). In addition to this, an overview of the deficiencies related to anti-money laundering (AML) will be given, analysing some of the methods employed by the organised crime.

2.4 International anti-money laundering regulatory framework

This paragraph discusses the various international regulatory frameworks and special bodies established to combat money laundering practices. In particular, the United Nations has been the first international organization to undertake concrete actions through the Global Programme against Money Laundering (GPML), carried out by their Office on Drugs and Crime (UNODC). Indeed, the GPML provides governments and financial institutions with common strategies, expert advices and cross-border co-operation against this white collar crime.³² In addition, it is designed to increase the level of awareness among the states, to promote the same legal approach between civil and common law systems, and to create a database for monitoring all financial crime activities. Generally, international treaties or conventions have the force and effect of law in a country that has signed, ratified and implemented them. For this reason, the United Nations conventions are all binding multilateral treaty, because without an agreement of states, the international legal system has no authority to implement binding legislation.³³ Thus, the Vienna Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances (1988)³⁴ has exhorted countries for the first time to criminalize money laundering activities, and it has established a basis for the confiscation of illicit proceeds.³⁵

The Palermo Convention (2002)³⁶ is a major step in order to combat transnational organised crime, which has specifically obligated each ratifying country to establish regulatory regimes to deter and detect all forms of money laundering, such as record-keeping procedures, customer identification requirements and suspicious transaction reports.³⁷ Furthermore, the

³² Schott (n 1) III–6.

³³ Jack Goldsmith and Daryl Levinson, 'Law for States: International Law, Constitutional law, public law' (2009) 122 Harvard Law Review, 1806–1807.

³⁴ United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances (adopted 19 December 1988, entered into force 11 November 1990) United Nations, Treaty Series, vol. 1582, p. 95.

³⁵ Schott (n 1) III–2.

³⁶ United Nations Convention against Transnational Organized Crime (adopted 15 November 2000, entered into force 29 September 2003) United Nations, United Nations, Treaty Series, vol. 2225, p. 209.

³⁷ Schott (n 1) III–3.

Palermo Convention authorizes the exchange of information among law enforcement and other authorities, and it promotes international cooperation through the establishment of a financial intelligence unit. Of course, another concern is the international financing of terrorism, which gave rise to the International Convention for the Suppression of the Financing of Terrorism (1999) and to a variety of Security Council Resolutions.³⁸ All these measures are therefore aimed to criminalize terrorism, and to outlaw forms of financing for subversive groups.

Finally, the Basel Committee on Banking Supervision (BCBS) (also known as Basel Committee) is an international organization established by the central bank governors of the ten most industrialized countries in the world (G10).³⁹ The purpose of the Committee is to promote cooperation among central banks and other financial institutions, in order to achieve the monetary and economic stability. In addition, it coordinates the allocation of supervisory responsibilities among national authorities, to implement a global effective control over banking activities. Principally, the Basel Committee aims to enhance the security and reliability of the financial system, to establish a minimum standards relating to prudential supervision, to promote best practices for banking regulations, and to ensure international cooperation in the field of anti-money laundering. Nevertheless, it operates through guidelines, standards, recommendations and agreements. In addition to other important definitional aspects, the BCBS confirms the tendency to limit the use of cash, by increasing the number of subjects required to report suspicious transactions to the authorities. The Council of Europe is also cooperating with the Financial Action Task Force in order to set and implement common standards in the form of Conventions and recommendations.

2.5 Financial Action Task Force on Money Laundering (FATF)

The Financial Action Task Force (FATF) is an intergovernmental organization, created after the 15th G7 Summit (Paris, 1989), which has the purpose of promoting policies to combat money laundering, terrorism financing and illicit proliferation funding of weapons of mass destruction.⁴⁰ The FATF aims to create legal instruments that can effectively combat the criminal use of the financial system. Through 40 recommendations, that have been recognized and ratified by several other international organizations, the FATF has created a body of reference for the national laws of its 34 member countries to promote cooperation

³⁸ Schott (n1) III-4.

³⁹ Schott (n 1) III-13.

⁴⁰ Schott (n 1) III-7.

and information exchange between financial authorities.⁴¹ Among other things, these recommendations include the adoption of preventive measures. Recommendation number 10 is about *customer due diligence*:

Financial institutions should be required to undertake customer due diligence (CDD) measures when: (i) establishing business relations; (ii) carrying out occasional transactions: above the applicable designated threshold (USD/EUR 15,000); or that are wire transfers in the circumstances covered by the Interpretive Note to Recommendation 16; (iii) there is a suspicion of money laundering or terrorist financing; or (iv) the financial institution has doubts about the veracity or adequacy of previously obtained customer identification data.⁴²

Another important recommendation, number 11, disciplines *record keeping*:

Financial institutions should be required to maintain, for at least five years, all necessary records on transactions, both domestic and international, to enable them to comply swiftly with information requests from the competent authorities. Such records must be sufficient to permit reconstruction of individual transactions (including the amounts and types of currency involved, if any) so as to provide, if necessary, evidence for prosecution of criminal activity.⁴³

Recommendation number 20 requires a financial institution to report suspicious transactions.

If a financial institution suspects or has reasonable grounds to suspect that funds are the proceeds of a criminal activity, or are related to terrorist financing, it should be required, by law, to report promptly its suspicions to the financial intelligence unit (FIU).⁴⁴

Other objectives are to monitor the implementation of regulatory and organizational principles of anti-money laundering,⁴⁵ through a process of mutual evaluation and report on new techniques or trends,⁴⁶ and to verify the effectiveness of those rules in the participating jurisdictions.⁴⁷ The longstanding debate about the criminalisation of money laundering leads many to wonder whether this should include only drug trafficking related offences, serious fraud or all type of financial crimes. Hence, it is essential to clarify these issues to act without

⁴¹ The full document can be downloaded at: <http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF_Recommendations.pdf> accessed October 9, 2014. The document is: *International standards on combating money laundering and the financing of terrorism & proliferation. The FATF Recommendations, February 2012.*

⁴² The FATF Recommendations (n 41) 14.

⁴³ The FATF Recommendations (n 41) 15.

⁴⁴ The FATF Recommendations (n 41) 19.

⁴⁵ The FATF Recommendations (n 41) 11.

⁴⁶ The FATF Recommendations (n 41) 25.

⁴⁷ The FATF Recommendations (n 41) 26.

limits against the organized crime. In this context, the enforcement of KYC and CDD requirements could improve the security around transactions and beneficiary owner identification, creating a durable bank-client relationship. It should be a mandatory duty for private sector institutions, through a system of record keeping, reporting unusual activities and transactions to law enforcement bodies or public prosecutors.

2.5.1 The Egmont Group of Financial Intelligence Units (FIUs)

The Egmont Group of Financial Intelligence Units (Egmont Group) is an informal international organisation, which brings together specialized authorities, called Financial Intelligence Units (FIUs). Thanks to the work of research carried out by the FATF, the idea of combating money laundering has been developed in financial terms through networks capable of identifying and tracking the flow of illegal proceeds. In fact, among the recommendations developed by the Financial Action Task Force, there are three in particular (FATF Recommendations 15, 23 and 32) that provide for the creation of a structure of independent units, which centralize functions of retention and analysis of suspicious transaction reports. Recommendation number 15 requires countries and financial institutions to promote the use new technologies.

Countries and financial institutions should identify and assess the money laundering or terrorist financing risks that may arise in relation to (a) the development of new products and new business practices, including new delivery mechanisms, and (b) the use of new or developing technologies for both new and pre-existing products. In the case of financial institutions, such a risk assessment should take place prior to the launch of the new products, business practices or the use of new or developing technologies. They should take appropriate measures to manage and mitigate those risks.⁴⁸

Recommendation 23 disciplines non-regulated entities, and in accordance with paragraph (a):

Lawyers, notaries, other independent legal professionals and accountants should be required to report suspicious transactions when, on behalf of or for a client, they engage in a financial transaction in relation to the activities described in paragraph (d) of Recommendation 22. Countries are strongly encouraged to extend the reporting requirement to the rest of the professional activities of accountants, including auditing.⁴⁹

Recommendation number 32 is about *Cash couriers*.

Countries should have measures in place to detect the physical cross-border transportation of currency and bearer negotiable instruments, including through a declaration system and/or disclosure system. Countries should ensure that their

⁴⁸ The FATF Recommendations (n 41) 17.

⁴⁹ The FATF Recommendations (n 41) 20.

competent authorities have the legal authority to stop or restrain currency or bearer negotiable instruments that are suspected to be related to terrorist financing, money laundering or predicate offences, or that are falsely declared or disclosed. Countries should ensure that effective, proportionate and dissuasive sanctions are available to deal with persons who make false declaration(s) or disclosure(s). In cases where the currency or bearer negotiable instruments are related to terrorist financing, money laundering or predicate offences, countries should also adopt measures, including legislative ones consistent with Recommendation 4, which would enable the confiscation of such currency or instruments.⁵⁰

In June 1995, the delegations of Belgium and the United States became promoters of a meeting in order to study stable forms of collaboration. This is how the Egmont Group has been created, and accordingly its main task is to promote and foster cooperation between the Financial Intelligence Units. In essence, the Group is an international network of national agencies, specialized in combating money laundering, which also works to promote cooperation through a mutual exchange of information and knowledge related to possible fraudulent transactions. With regard to the Financial Intelligence Units, it is necessary to reiterate that individual states have essentially attributed to a single body the duties of retention and analysis of suspicious transaction reports, and the exchange of information relating to them. In some countries (such as Australia, Belgium, France, Italy, the Netherlands and the United States), these authorities have an administrative nature; in others, they were built as specialized departments of the police force (UK and Slovakia for example) or incorporated as a part of the judicial authority (the case of Iceland). However, in order to avoid obstacles for cooperation between FIUs, given their different nature, the Egmont Group has determined the common elements that should characterize such bodies' activities. Basically, the FIU should serve as a connector between different national authorities involved in money laundering detection. To this end, it must coordinate both the internal activity and the international cooperation with other FIUs. Finally, it has to perform financial analysis of suspicious transactions, verifying all the reports it receives.

2.6 Conclusions

As reviewed in this chapter, it is acknowledged that money laundering is one of the most alarming crimes across economically advanced nations. The need to prevent and respond to this offence arises from purely social needs, but also to prevent the economic destabilization,

⁵⁰ The FATF Recommendations (n 41) 25.

because money laundering can alter the allocation of resources, or it can create a wide spectrum of market malfunctioning, including unfair competition. It constitutes an offense for which a criminal indictment is expected; therefore, its criminalization is seen as a tool in the fight against organized crime. Generally, this process can involve several subjects, because a person that conceals the illegal income is not necessarily the one that commits predicate offenses. The global strategy adopted is basically geared to prevent and deal with the accumulation of illicit capital flows and the traceability of the investments made through criminal activities. Among the structural factors of money laundering, I have isolated four points which are of particular significance: 1) the globalisation; 2) the adoption of the euro; 3) the technological advances in the field of communication; 4) the increasing sophistication of financial products and services. As we have seen, through the Global Programme against Money Laundering and together with other initiatives, the United Nations has been the first international body to undertake concrete actions against criminal proceeds. Nevertheless, there is a confusing lack of uniformity on the international anti-money laundering requirements to which standardize both onshore and offshore jurisdictions. However, the FATF has created a body of reference (the forty recommendations) for the national laws of its member countries. In virtue of these recommendations, many states have established a central authority for reporting unusual activities, as a result of the perceived necessity to start an international co-operation between them. There are five factors that could give rise to a better financial system: 1) the global criminalisation of money laundering; 2) the confiscation and forfeiture of criminal proceeds; 3) the creation of a reporting system; 4) the enforcement of *Know Your Customer* (KYC) and *Customer Due Diligence* (CDD) regulations for service providers; 5) the reinforcement of international cooperation and mutual assistance between nations.

3. EU FRAMEWORK AGAINST MONEY LAUNDERING

3.1 Introduction

As we have seen above, thanks to the globalisation of the economy, organised crime knows no national boundaries or barriers, and this requires uniform regulations at the European and international level. Many proposals and measures have therefore taken place, and an important action against money laundering is carried out by the European Union. In most cases, the purpose of anti-money laundering policy is to hit criminals in their business, and to protect the integrity of the financial system. The current EU legislation, such as the third money laundering Directive, is therefore based largely on the FATF recommendations. For this reason, already by the end of the eighties, a common strategy has been designed to tackle this problem effectively. The aim of this chapter is to describe the EU legal framework, as well as the three EU directives issued on the risks of money laundering. A comparative study between the Italian and the Icelandic anti-money laundering regulations is also part of this chapter. I will also provide an account of the related case law of the European Court of Human Rights (ECtHR) and the European Court of Justice (ECJ).

3.2 First European AML Directives

As is well known, EU member countries have started to harmonize national legislation and to adapt their own regulations with the common goal of countering fraudulent activities. The European Union, since 1991, has been very active against money laundering; in fact, three different directives have been issued. The first one is the Council Directive 91/308/EEC on prevention of the use of the financial system for the purpose of money laundering, which was the first step at EU level in the fight against this type of crime. The First Directive defines the concepts of credit institution, financial institution and money laundering; in addition, it focuses on drug-trafficking related to dirty money. According to Article 6:

Member States shall ensure that credit and financial institutions and their directors and employees cooperate fully with the authorities responsible for combating money laundering: - by informing those authorities, on their own initiative, of any fact which might be an indication of money laundering, - by furnishing those authorities, at their request, with all necessary information, in accordance with the procedures established by the applicable legislation. The information referred to in the first paragraph shall be forwarded to the authorities responsible for combating money laundering of the Member State in whose territory the institution forwarding the information is situated. The person or persons designated by the credit and financial institutions in

accordance with the procedures provided for in Article 11 (1) shall normally forward the information. Information supplied to the authorities in accordance with the first paragraph may be used only in connection with the combating of money laundering. However, Member States may provide that such information may also be used for other purposes.

Subsequently, Member States have to ensure cooperation and information exchange between the institutions and persons subject to this Directive and the authorities responsible for combating money laundering. Hence, they are obliged to report suspicious transactions and to monitor the fulfilment of these provisions; accordingly, they are required to verify that credit and financial institutions have ascertained the identity of their clients, unless the customer is itself a credit or a financial institution. According to Article 3 (paragraphs 1, 5, 6 and 8):

Member States shall ensure that credit and financial institutions require identification of their customers by means of supporting evidence when entering into business relations, particularly when opening an account or savings accounts, or when offering safe custody facilities. In the event of doubt as to whether the customers referred to in the above paragraphs are acting on their own behalf, or where it is certain that they are not acting on their own behalf, the credit and financial institutions shall take reasonable measures to obtain information as to the real identity of the persons on whose behalf those customers are acting. Credit and financial institutions shall carry out such identification, even where the amount of the transaction is lower than the threshold laid down, wherever there is suspicion of money laundering. Credit and financial institutions shall not be subject to the identification requirements provided for in this Article where the customer is also a credit or financial institution covered by this Directive.

Therefore, at the international level, the reference texts on that subject are the 40 recommendations of the Financial Action Task Force (FATF). The First AML Directive implemented these recommendations within the competencies of the EC Treaty. However, unlike the FATF standards, this Directive made for the first time the reporting of suspicious transactions an obligation and not just an option. Consequently, under this provision, banking secrecy has to be suspended in case of suspected money laundering offences, and the operation has to be reported to the FIUs.

The Second Directive of the European Parliament and Council (2001/97/EC) amends the previous Council Directive (91/308/EEC), which did not specify the competent authorities of the Member State that are obliged to receive details of suspicious transactions. In accordance with this Directive:

'Competent authorities' means: the national authorities empowered by law or regulation to supervise the activity of any of the institutions or persons subject to this Directive.

Nevertheless, the Second Directive represented the best international practice in protecting the financial sector from the risk of money laundering. It extends the Community framework to all types of crime, such as corruption, and it also contains information on those who have the duty to report anomalous transactions, including enhancements to the requirements for customer due diligence. It also clarifies that currency exchange offices, money transmitters and investment firms can be susceptible to money laundering transactions linked to criminal activities. The European Council extended the provisions of the Directive to lawyers „participating in financial or corporate transactions”. Thus, in accordance with paragraph 16:

Notaries and independent legal professionals, as defined by the Member States, should be made subject to the provisions of the Directive when participating in financial or corporate transactions, including providing tax advice, where there is the greatest risk of the services of those legal professionals being misused for the purpose of laundering the proceeds of criminal activity.

However, the rules of lawyer confidentiality were not violated because the provision was not extended to the reporting information related to judicial proceedings. In fact, paragraph 17 states as follows:

However, where independent members of professions providing legal advice which are legally recognised and controlled, such as lawyers, are ascertaining the legal position of a client or representing a client in legal proceedings, it would not be appropriate under the Directive to put these legal professionals in respect of these activities under an obligation to report suspicions of money laundering. There must be exemptions from any obligation to report information obtained either before, during or after judicial proceedings, or in the course of ascertaining the legal position for a client. Thus, legal advice remains subject to the obligation of professional secrecy unless the legal counsellor is taking part in money laundering activities, the legal advice is provided for money laundering purposes, or the lawyer knows that the client is seeking legal advice for money laundering purposes.

To better understand the scope of this exception, in the next paragraph, I will discuss the case of *Michaud v. France*, where the ECtHR held that the obligation on lawyers to report suspicious transactions does not interfere disproportionately with the principles of protection of lawyer-client relations, since they are not subject to the requirement when defending litigants.

3.3 European Court of Human Rights: *Michaud v. France*

In July 2007, the French National Bar Council provided the legislation that disciplinary actions should be taken against lawyers in case of non-compliance with the EU requirements in the field of AML. In the present case, the European Court of Human Rights (ECHR) is asked to clarify the limits between the lawyer's duty of professional secrecy and the obligation to report suspicious transactions.⁵¹ In particular, the applicant, Mr. Patrick Michaud, a French lawyer, considered the European legislation in the field of anti-money laundering detrimental to his profession. According to him, the reporting obligation is disproportionate to the Financial Intelligence Unit (*Tracfin* in France), especially when a lawyer just assisted a client in the preparation or execution of real estate contracts. The applicant complained that the concept of *suspicious transactions* is too vague and he asked the European Court of Human Rights to decide whether the reporting obligation is compatible with the right to respect for private life contained in Article 8 of the European Convention of Human Rights.⁵²

The Court notes that within the scope of this article, there is undoubtedly the right to the privacy of correspondence between individuals. Then, the protection for the confidentiality of such communications is one of the areas included in the most general concept of privacy. In the opinion of the Court, the requirement to submit suspicious transactions reports can be considered as interference by public authority in the correspondence between private citizens. However, the Court recalls that the prohibition is not absolute, but exists unless the interference is prescribed by law. In this case, the interference is justified as a measure to combat the phenomenon of money laundering, which pursues one of the purposes mentioned in Article 8(2), precisely the prevention of disorder or crime. The lawyer's duty of professional secrecy has significant importance for the proper administration of justice; nevertheless, it should be a fair balance between the attorney-client privilege and the fight against money laundering. In the opinion of the Court, the reporting requirement does not apply when lawyers give advice in judicial proceedings. Accordingly, the obligation to report suspicious transactions does not affect the essence itself of defending a client, which is the

⁵¹ Michaud v. France (2012) App no 12323/11 (ECtHR, 6 December 2012). Full document available at: <[http://hudoc.echr.coe.int/sites/eng/pages/search.aspx?i=001-115377#{"itemid":\["001-115377"\]}](http://hudoc.echr.coe.int/sites/eng/pages/search.aspx?i=001-115377#{)>, accessed 9 October 2014.

⁵² European Convention for the Protection of Human Rights and Fundamental Freedoms (adopted 4 November 1950, entered into force 3 September 1953) as amended by Protocol No. 11, Nov. 4, 1950, 213 U.N.T.S. 221 [hereinafter ECHR]. Full document available at: <http://www.echr.coe.int/Documents/Convention_ENG.pdf>, accessed 9 October 2014.

basis of the lawyer's duty of professional secrecy. The Court states that France did not violate Article 8, as the obligation to report suspicious transactions is not a disproportionate interference with the lawyer's duty of professional secrecy.

3.4 Third Money Laundering Directive: 2005/60/EC

The third AMLD is Directive 2005/60/EC on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing. This provision has introduced a new approach to the prevention of large amounts of illicit money from entering the banking system. Indeed, it is based on an active collaboration between banks, financial institutions, insurance companies and anti-fraud experts. Furthermore, this communitarian legal act encourages maximum coordination and cooperation between Member States. The European Commission is now aware of the fact that „flows of dirty money can damage the stability and reputation of the financial sector”.⁵³ Subsequently, Article 1 describes money laundering as the following intentional conduct:

(a) the conversion or transfer of property derived from criminal activity to conceal or disguise its illicit origin; (b) the concealment or disguise of the true nature, source, location, disposition, movement or ownership of property known to have been derived from criminal activity; (c) the acquisition, possession or use of property known to have been derived from criminal activity; (d) the participation, or assistance, in the commission of any of the activities above.

The Directive has one of the key points in the requirements for customer due diligence with particular reference to the professionals, when carrying out occasional transactions amounting to EUR 15 000 or more. However, lawyers must file a suspicious transaction report when there is suspicion of money laundering, regardless of any exemption or threshold. There are cases in which simplified CDD standards may be used, especially in relation to national public authorities. Nevertheless, whenever there is a high risk of fraudulent activity, these entities are required to apply enhanced CCD, and to verify the documents supplied by the customers. In conformity with Article 22:

1) Member States shall require the institutions and persons covered by this Directive, and where applicable their directors and employees, to cooperate fully: (a) by promptly informing the FIU, on their own initiative, where the institution or person covered by this Directive knows, suspects or has

⁵³ Augier, De Rynck and Dunne, 'European Commission - Anti-Money Laundering: Stronger Rules to Respond to New Threats' (5 February 2013) <http://europa.eu/rapid/press-release_IP-13-87_en.htm> accessed 3 December 2014.

reasonable grounds to suspect that money laundering or terrorist financing is being or has been committed or attempted; (b) by promptly furnishing the FIU, at its request, with all necessary information, in accordance with the procedures established by the applicable legislation.

2) The information referred to in paragraph 1 shall be forwarded to the FIU of the Member State in whose territory the institution or person forwarding the information is situated. The person or persons designated in accordance with the procedures provided for in Article 34 shall normally forward the information.

The Directive therefore requires European countries to establish a Financial Intelligence Unit (FIU), which serves as a centre for receiving, analysing and disseminating to the national competent authorities suspicious transaction reports and other information regarding potential fraud offenses. Subsequently, Article 24 states that:

Member States shall require the institutions and persons covered by this Directive to: (a) inform the FIU of the suspected commission (or attempted commission) of money laundering or terrorist financing provide the FIU on request with all necessary information; (b) provide the FIU on request with all necessary information.

Furthermore, each Member State has a supervisory role and it must require the local FIU to monitor compliance with this Directive. Therefore, Article 37 establishes that:

Member States shall require the competent authorities at least to effectively monitor and to take the necessary measures with a view to ensuring compliance with the requirements of this Directive by all the institutions and persons covered by this Directive. Member States shall ensure that the competent authorities have adequate powers, including the power to compel the production of any information that is relevant to monitoring compliance and perform checks, and have adequate resources to perform their functions.

For this reason, the entities and persons concerned must be held responsible for any violation of the AML policy; and the penalties must be effective, proportionate and dissuasive (Article 39).

3.5 European Court of Justice: *Jyske Bank Gibraltar Ltd v. Administración del Estado*

The following judgement of the European Court of Justice (Case C-212/11) gives a better understanding of the Directive. In fact, the ECJ has ruled that Article 22(2) does not preclude the legislation of a Member State from requiring credit institutions to forward information necessary for combating money laundering direct to the Member State authorities rather than through mutual cooperation routes. In *Jyske Bank Gibraltar Ltd v. Administración del*

Estado,⁵⁴ the European Court of Justice (ECJ) gives some important clarifications on the relationship between national law and Community legislation in the field of combating money laundering and terrorist financing. The Supreme Court of Spain (*Tribunal Supremo*) has asked the ECJ to rule on the interpretation of Article 22(2) of Directive 2005/60/EC. This article deals with the duty to cooperate and exchange information among the subjects indicated by the Directive and the Financial Intelligence Unit. *Jyske Bank Gibraltar Ltd* is a Danish credit institution based in Gibraltar, and it operates in Spain under the freedom to provide services, namely without being established in the Spanish territory. In particular, the bank is doing an activity consisting of granting mortgages and secured loans for the purchase of property in Spain. On 30 January 2007, the Spanish FIU (*Servicio Ejecutivo*) has communicated to *Jyske* that since it has not appointed an agent authorized to negotiate with them, it would have to begin an investigation in relation to the activities carried out by the Danish bank. According to the report of the local Financial Intelligence Unit, there is a very high risk that the bank is used for money laundering. As we have seen, Directive 2005/60/EC imposes certain disclosure obligations, requiring each Member States to forward information about suspicious transactions to the FIU. Therefore, the bank refused to furnish information requested by *Servicio Ejecutivo*, provided in accordance with a Spanish legislation on money laundering in force at that time (Law n. 19/1993).⁵⁵ As a result, the Spanish Council of Ministers (*Consejo de Ministros*) has fined the Danish bank for failure to disclose some documents and information relating to the identity of some customers, suspected of potential money laundering offences. For this reason, the *Tribunal Supremo* has completed the reference for preliminary ruling to the ECJ in order to know whether the Spanish legislation (which extends the reporting requirements also to credit institutions operating in Spain under the freedom to provide services) is in conformity with Directive 2005/60/EC. The ECJ stated that Article 22(2) of Directive 2005/60/EC does not preclude, in principle, the possibility for a Member State to require credit institutions, operating under the freedom to provide services, to communicate information requested by the local FIU. Furthermore, the principle of freedom

⁵⁴ Case C-212/11 *Jyske Bank Gibraltar Ltd v. Administración del Estado* (25 April 2013). Full document available at:

<<http://curia.europa.eu/juris/document/document.jsf?jsessionid=9ea7d0f130d55a39b8e1c47f4f589e6ac1721ff6cb3b.e34KaxiLc3eQc40LaxqMbN4Ob3yOe0?text=&docid=136784&pageIndex=0&doclang=EN&mode=req&dir=&occ=first&part=1&cid=87491>> accessed 9 October 2014.

⁵⁵ Drafted in Spanish, the full document can be downloaded at:

<<http://www.sepblac.es/espanol/legislacion/prevbcap/pdf/ley19-93.pdf>> accessed 9 October 2014. The document is: *Ley 19/1993 de 28 de diciembre, sobre determinadas medidas de prevención de blanqueo de capitales* [Law 19/1993 on specific measures for preventing money laundering of 28 December 1993, BOE No 311 of 29 December 1993, p. 37327].

to provide services may be restricted by national legislation, whenever it falls in an area not fully harmonized with EU law. The judgement is of particular importance because it reaffirms the principle that fundamental freedoms of the European Union (like the freedom to provide services) are subject to certain conditions and limitations in case of overriding reasons of general interest, such as the fight against money laundering. In any case, these restrictions apply in accordance with the principle of proportionality.

3.6 Icelandic anti-money laundering legislation

In Iceland, the parliament (called *Alþingi*) has adopted Act No. 64/2006 on measures against money laundering and terrorist financing to harmonise the national regulation with the European Directive 2005/60/EC. The purpose of Act No. 64/2006 is to prevent money laundering by obligating financial intermediaries to know the identity of their customers and their activities, and to notify the competent authorities if they become aware of any suspicious transaction. Article 264 of the Icelandic General Penal Code no. 19/1940 criminalizes money laundering and it states as follow:

Any person who accepts, makes use of or acquires gains, for himself or for others, by violation of this Act, or by punishable violations of other statutes, or who, amongst other things, converts such gains, transports them, sends them, stores them, assists with their delivery, or conceals them or information concerning their origin, nature, location or manner of disposal, shall be imprisoned for up to 6 years.

A person who commits the original offence, and also commits an offence under the first paragraph of this Article, shall be subjected to the same punishment as is provided for in that paragraph. In such cases, Article 77 of this Act shall apply as appropriate.

In cases involving gains resulting from violations of Article 173 a of this Act, punishment of up to 12 years' imprisonment may be imposed. If an offence under the first paragraph of this Article is committed through negligence, it shall be punished by a fine or up to 6 months' imprisonment.⁵⁶

According to this legislation (Act No. 64/2006):

The offence applies to those who intentionally or negligently engage money laundering. Under the basic concepts of Icelandic law, intention can be inferred from objective factual circumstances. Knowledge, according to the explanations provided, encompasses direct intention, probable intent, and also

⁵⁶ Article 264 of the Icelandic General Penal Code no. 19/1940, available at: <<http://www.logreglan.is/upload/files/Peninga%FEv%E6ttissk%FDrsla%202009-2010%20%E1%20ensku%20lok.pdf>> accessed 9 October 2014. Page 9.

wilful blindness and *dolus eventualis*. Criminal liability of legal persons exists for money laundering related to corruption, but otherwise is too narrow.⁵⁷

However, the participation in a criminal organisation is not separately criminalised. Article 254 of the Icelandic General Penal Code is another important provision and it is a special rule in regard to Article 264. It „criminalizes the retaining of valuables unlawfully acquired by means of an enrichment offence as well as the assistance in retaining and the participation in the gain derived from a predicate offence”.⁵⁸ Article 254 (1) is as follows:

In case a person unlawfully retain, without his/her act being subject to the provisions of Art. 244, 245 or 247 – 252, an article or other valuables from the owner and which have been acquired in a manner referred to in these Articles, participates in the gain derived from such an offence, assists another person in retaining such gain or promotes in another manner the maintenance of the unlawful consequences of the offence, he/she shall be punished by up to 4 years imprisonment. Penalty may, however, consist of [imprisonment for up to 1 year] 1) or fines in case the accused party has originally obtained by honest means the valuables which had been acquired by means of an enrichment offence.⁵⁹

An enrichment offence is very often the original offence in a money laundering case. However, there is also a stronger tradition for the use of this article because it is an older provision than Article 264. For this reason few judgements have been pronounced for offences committed after the passing of this article. In the past years, there have been a limited number of indictments and convictions for money laundering offences, but the amendment of Article 264 is likely to significantly increase prosecutions for these types of crimes. In case S-500/2010,⁶⁰ the Reykjavík District Court has convicted two men of money laundering in connection with a drug trafficking offence for having imported from Spain 1544 grams of cocaine. Subsequently, they were found guilty for money laundering and self-laundering according to Article 264. In addition to the above, in case no. 495/2010,⁶¹ the

⁵⁷ Financial Action Task Force, 'Third Mutual Evaluation Report Anti-Money Laundering and Combatting the Financing of Terrorism - Iceland' (2006) 5 <<http://www.fatf-gafi.org/media/fatf/documents/reports/mer/MER%20Iceland%20full.pdf>> accessed 14 October 2014.

⁵⁸ 'MONEY LAUNDERING - Information-Money-Laundering.pdf' <<http://www.vidraedur2009-2013.is/media/ESB/samningskaflar/04/Information-Money-Laundering.pdf>> accessed 4 December 2014.

⁵⁹ Article 254 (1) of the Icelandic General Penal Code no. 19/1940, available at: <<http://www.logreglan.is/upload/files/Peninga%FEv%E6ttissk%FDrsla%202009-2010%20%E1%20ensku%20lok.pdf>> accessed 9 October 2014. Page 13.

⁶⁰ 'Héraðsdóms Reykjavíkur, 23. júlí 2010 í máli nr. S-500/2010' <<http://www.domstolar.is/domaleit/nanar/?ID=S201000500&Domur=2&type=1&Serial=1&Words=>>> accessed 20 November 2014.

⁶¹ 'Héraðsdóms Reykjavíkur 17. maí 2010 í máli nr. S-250/2010' <<http://www.domstolar.is/domaleit/nanar/?ID=S201000250&Domur=2&type=1&Serial=1&Words=>>> accessed 20 November 2014.

District Court of Reykjavík found three person guilty of money laundering for having obtained proceeds amounting to ISK 1,200,000 with the sale and distribution of an unspecified quantity of drugs. These crimes, however, were qualified as grave breaches and violations of both the new and the previous money-laundering provisions of Article 264 with subsequent amendments.

The new regime has therefore a wider scope. It includes rigorous CDD standards, comprehensive record-keeping duties and a direct mandatory obligation to report suspicious transactions. The purpose is to prevent the crime by obligating parties - such as financial undertakings, life insurance companies, pension funds or attorneys - to know the identity of their customers and their activities, and to notify the competent authorities if they become aware of such illegal activities. Consequently, local financial institutions have started a campaign to promote awareness of the importance to verify client's identity, and of gathering information about the transaction's intent at the beginning of a new business relationship. The Icelandic Financial Intelligence Unit is a member of the Egmont Group (an international network of financial intelligence units), and it is part of the Economic Crime Unit of the National Commissioner of the police (*Ríkislögreglustjórnin*). This organ is the central authority for reporting suspicious transactions, and for this reason it has access to a wide range of information. Besides that, it has a network of relationships within the banking sector and other financial intermediaries. The fact that the Icelandic Financial Intelligence Unit is part of the Economic Crime Unit at the National Commissioner of the police does not inhibit its ability to exercise the investigative function in an independent and efficient manner.

According to Article 22 of Act no. 64/2006, the financial undertakings are obliged to appoint a person responsible for applying all the measures to prevent fraudulent activities, and for dispatching reports on suspected transaction to the police or directly to the FIU officer. The following text is a transcription of Article 22 on the designation of persons who perform the above AML functions:

Persons under obligation to report are responsible for compliance with this Act and rules and regulations issued pursuant to this Act. They shall nominate a specific person of managerial rank to be generally responsible for notification pursuant to Articles 17 and 18 that has unconditional access to customer due diligence information, transactions or requests for transactions, together with any documents which may be relevant to notifications. The police shall be informed of the nomination of such responsible person. Such responsible

person shall ensure the development of co-ordinated practices which support the sound implementation of this Act.⁶²

The FIU officer is the person responsible for AML within the Financial Intelligence Unit. He is a detective chief inspector, monitoring all suspicious transaction reports that are submitted from entities under the above obligation. There are others regulators, such as the Special Prosecutor (*Sérstakur saksóknari*) and the Ministry of the Interior (*Innanríkisráðuneytið*), working in coordination and cooperation with the Financial Intelligence Unit. The Ministry of the Interior's main areas of responsibility are justice, human rights, transport and communications, while the Special Prosecutor is responsible to direct the function of public investigation and prosecution. Act No. 135/2008 regulates therefore the office of the *Sérstakur saksóknari*, and it is his duty to investigate suspicions of money laundering. Where the Special Prosecutor knows or suspects a case of criminal actions connected to activities of financial undertakings or individuals, he can „follow up on these investigations by bringing charges in court against those concerned”.⁶³

3.7 Italian anti-money laundering legislation

An anti-money laundering regulation in Italy has developed through a complex system of sources at the international, European and national level. The fight against money laundering is of particular importance, due to the presence of Mafia organizations which result in lack of economic development. According to Article 648 *bis* of the Italian Criminal Code, the laundering of illicit proceeds is a criminal offense and the first paragraph states that:

This crime arises if a person substitutes or transfers money, goods or other benefits resulting from an unpremeditated crime, or carries out other transactions in relation to these assets, in such a way as to hinder their identification as the proceeds of a crime. The crime is punishable by four to twelve years' imprisonment and a fine from 1,032 to 15,493 euros. The punishment is increased if the crime is committed during the exercise of a professional activity.⁶⁴

⁶² 'Act on Measures against Money Laundering and Terrorist Financing, No. 64/2006 as Amended by Act No. 77/2008, Act No. 116/2009 and Act No. 41/2012 | Nr | Laws and Regulations | Atvinnuvega- Og Nýsköpunarráðuneytið - EN' <<http://eng.atvinnuvegaraduneyti.is/laws-and-regulations/nr/nr/7389>> accessed 19 November 2014.

⁶³ 'Special Prosecutor | English | Sérstakur Saksóknari' <<http://www.serstakursaksoknari.is/english/special-prosecutor/>> accessed 3 December 2014.

⁶⁴ Article 648 bis of the Italian Criminal Code, which defines money laundering, available at: <<http://www.terna.it/LinkClick.aspx?fileticket=xVrvxNvtxU%3D&tabid=474&mid=10614>> accessed 9 October 2014.

At a national level, the Italian money laundering legislation has been supplemented by the Legislative Decree 231/2007,⁶⁵ which transposes the European Directive 2005/60/EC and entrusts the Bank of Italy with regulatory tasks with regard to: 1) adequate customer verification; 2) recording of data; 3) organizational, procedural and internal control; 4) reporting suspicious transactions. Accordingly, banks, financial intermediaries, insurance companies and various categories of professionals are required to comply with this specific provision. Nevertheless, the anti-money laundering framework has been progressively extended beyond the traditional segment of banks and financial intermediaries towards other entities, that are carrying out activities particularly exposed to the risk of money laundering (such as lawyers, notaries, accountants, as well as certain categories of non-financial such as antique dealers, casinos, and real estate agents).

Besides that, the Legislative Decree 231/2007 introduces stringent obligations of cooperation, prevention and information between financial authorities. However, there are two different types of cooperation: 1) a passive collaboration directed to ensure a thorough knowledge of the customer, requiring the retention of documents relating to the transactions; and 2) an active collaboration aimed to the identification and report of suspicious or unusual transactions. The Legislative Decree 231/2007 also imposes obligations of Customer Due Diligence to determine the type of relationship between the client and the bank, and the future behaviour (on the basis of the information provided). The information required will vary depending on the type of relationship. For example, when the customer has to open a basic current account, he must clarify the purpose for which it is made; while additional information will be required for loans and credit lines. Moreover, the law provides that all data collected are listed in an archive that every bank must keep.

The archive can be accessed at any time by the Financial Information Unit (*Unità di Informazione Finanziaria*) established at the Bank of Italy, the headquarters of all the activities for prevention on money laundering carried out in this country. As provided for by the Legislative Decree 231/2007; among the many tasks of the Italian FIU are to get all

⁶⁵ Drafted in Italian, the full document can be downloaded at: <<https://www.bancaditalia.it/UIF/prev-ricic/sara/norm-sara/norm-naz/dlgs-2007-231.pdf>> accessed October 10 2014. The document is: *D.Lgs. 21 novembre 2007, n. 231 - Attuazione della direttiva 2005/60/CE concernente la prevenzione dell'utilizzo del sistema finanziario a scopo di riciclaggio dei proventi di attività criminose e di finanziamento del terrorismo nonché della direttiva 2006/70/CE che ne reca misure di esecuzione e successive modificazioni e integrazioni*. [Legislative Decree 231/200, implementation of Directive 2005/60/EC on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing, published in Gazzetta Ufficiale no. 290 of 14 December 2007- Ordinary Supplement no. 268/L].

reports of suspicious transactions, and to exchange information between supervisors and law enforcement agencies (*Guardia di Finanza* and *Direzione Investigativa Antimafia*). Given that the Italian FIU is doing excellent informative and investigative work, in several cases, as reported in the FATF Mutual Evaluation, inspections showed that some intermediaries had not properly implemented CDD standards and other obligations.⁶⁶

As seen above, the Bank of Italy plays an important role in implementing AML policy and it has the merit of having promoted the use of new technologies for detecting suspicious transactions. The GIANOS (*Generatore Indici di Anomalia per Operazioni Sospette*, namely Generator of Abnormality Indexes for Suspicious Transactions) is an anti-money laundering computer procedure, made in Italy, for the monitoring and identification of potentially suspicious transactions.⁶⁷ More in detail, the procedure automatically identifies, for each customer, all the operations considered unexpected, namely which do not appear in line with the normal behaviour of the customer, as assessed by analysis of his past activity. The operating rules of the software were developed by a permanent committee of legal, informatics and banking industry experts, including representatives of banks. Thus, this software, linked to a centralised computer archive, has supported financial institutions in identifying abnormality indexes since 1995, evidencing all unusual transactions that may not be consistent with the customer profile.

Accordingly, all Italian banks have a centralised computer archive, introduced by Legislative Decree 231/200, enclosing information on their customers. This single computerized data base is called *Archivio Unico Informatico*, containing information about: date, reason and total amount of a transaction; name, surname, date and place of birth of persons carrying out transactions.⁶⁸ Therefore, financial intermediaries use GIANOS to better evaluate a transaction, because they are not always able to distinguish if an operation hides illicit financial flows or not. However, most suspicious transaction reports to the Italian FIU are identified by GIANOS, which properly records the data in the centralised computer archive, using standard criteria for evaluating potential money laundering behaviour. Finally, it must be said that the use of GIANOS is an aid and not a substitute for fulfilling the obligations to

⁶⁶ Financial Action Task Force, 'Italy FATF Mutual Evaluation, Second Biennial Update. Report from Italy' (Financial Action Task Force 2013) <http://www.fatf-gafi.org/media/fatf/documents/reports/mer/Second_Biennial_Update_Feb2013_Italy.pdf> accessed 14 October 2014.

⁶⁷ Chatain (n 30) 64–65.

⁶⁸ Ibid.

detect and report suspicious transactions.⁶⁹ In fact, this procedure does not relieve all the activities that the human element must continue to make. It is only a useful analytical tool, ensuring the correct application of the provisions aimed at highlighting possible fraudulent activities and to ensure uniform behaviour within the lending institutions.

3.8 Comparative legal analysis

In this paragraph, I analyse the Icelandic and the Italian AML regulations through a comparative legal analysis of Article 264 of the Icelandic General Penal Code and Article 648 *bis* of the Italian Penal Code. Because the protection of the banking sector is inextricably connected to transnational capital flows, AML is one of the most harmonized fields of EU law. As I have explained in the previous paragraphs, three EU directives on AML have been adopted. Subsequently, my comparative analysis can undoubtedly play an important role in this process of harmonization. The Icelandic and the Italian AML rules have been respectively supplemented by the Act No. 64/2006 and the Legislative Decree 231/2007, which transpose the European Directive 2005/60/EC in their national legal order.

In 2009, the Icelandic parliament passed a new money laundering provision (Article 264), which takes into consideration the observations of the FATF mutual evaluation report of October 2006. This article defines the offence with special wording on the methods of the conduct, focusing on Article 6 of the Palermo Convention, which is one of the most important features of this treaty since it provides for the criminalisation of money laundering. More specifically, Article 6 (1) of the Palermo Convention states as follows:

Each State Party shall adopt, in accordance with fundamental principles of its domestic law, such legislative and other measures as may be necessary to establish as criminal offences, when committed intentionally: (a) (i) The conversion or transfer of property, knowing that such property is the proceeds of crime, for the purpose of concealing or disguising the illicit origin of the property or of helping any person who is involved in the commission of the predicate offence to evade the legal consequences of his or her action; (ii) The concealment or disguise of the true nature, source, location, disposition, movement or ownership of or rights with respect to property, knowing that such property is the proceeds of crime; (b) Subject to the basic concepts of its legal system: (i) The acquisition, possession or use of property, knowing, at the time of receipt, that such property is the proceeds of crime; (ii) Participation in, association with or conspiracy to commit, attempts to commit and aiding,

⁶⁹ Financial Action Task Force, 'Mutual Evaluation Report on Anti-Money Laundering and Combating the Financing of Terrorism. Italy.' (2006) 54
<<http://www.fatf-gafi.org/media/fatf/documents/reports/mer/MER%20Italy%20full.pdf>> accessed 14 October.

abetting, facilitating and counselling the commission of any of the offences established in accordance with this article.

Under the Icelandic criminal law, the main objective in making money laundering punishable is to attack the roots of offences by eliminating their primary incentive (namely the proceeds they may generate). Money laundering refers therefore to gains or proceeds from predicate offences mentioned in the Icelandic General Penal Code, but also to punishable offences by other laws. The Supreme Court of Iceland gives in case no. 200/2001⁷⁰ an interpretation of Article 264(1), which states as follow:

Article 264, paragraph 1, of the General Penal Code contains a condition of a gain deriving from an offence, according to said act. Considering the nature and purpose of the provision, however, a requirement is not made as to exactly what kind of offence this pertains to. It must be considered in light of the circumstances in every instance whether it has been sufficiently proven that a gain is not of a lawful origin; instead that it derives from a violation of the act.⁷¹

The main point here is that the money laundering offence is extended to offences criminalized in other laws besides the General Penal Code. Hence, this provision applies to all kinds of assets, such as real estate, liquid assets or financial valuables, as well as documents or data that are deemed as being certificates for assets or financial valuables. Self-laundering is now dealt with in paragraph 2, which establishes that a person who commits the predicate offence and also commits an offence under the first paragraph of Article 264 (money laundering offence) shall be subject to the same penalty as provided for therein (self-laundering offence). Considering that money laundering and self-laundering constitutes two independent offences, the provision highlights that Article 77 of the Icelandic General Penal Code on simultaneous offences prevails as appropriate.

As regards the definition of money laundering stated under Article 648 *bis* of the Italian Penal Code, the offence is extended to any type of criminal proceeds, without specifying whether the article extends to assets which are not the direct gains of crime, like for example income derived from investments. One difference with Article 264 of the Icelandic General Penal Code is that Article 648 *bis* does not cover negligence. Though the concept of predicate

⁷⁰ 'Hæstiréttur Íslands, 8. nóvember 2001 í máli nr. 200/2001'

<<http://www.haestirettur.is/domar?nr=2220&leit=t>> accessed 20 November 2014.

⁷¹ Ríkislögreglustjórnin - National Commissioner of the Icelandic Police, 'Financial Intelligence Unit, FIU Iceland: Report for 2009-2010' (2011) 10

<<http://www.logreglan.is/upload/files/Peninga%FEv%E6ttissk%FDrsla%202009-2010%20E1%20ensku%20lok.pdf>>.

offence is extended to any crime committed intentionally, Article 648 *bis* therefore excludes crimes by negligence. Another difference is about self-laundering. Although this offence is contrary to fundamental principles of domestic law, it is still not punished under the Italian legal framework. This differs from the Icelandic law, which considers money laundering and self-laundering two independent offences. In fact, under Article 268 *bis*, money laundering offence does not apply to criminals who laundered their own proceeds. The use and concealment of crime proceeds by the person who committed the crime generating such illegal gains (drug trafficking for example) are not considered as punishable after the fact. As a consequence, the activities carried out by the author of the predicate offence are punishable when they are not directly consequential to the predicate offence. However, in order to stay in step with the EU AML legislation, the Italian Parliament is going to introduce the crime of self-laundering, which will also punish a person who may be the author of the offence, and anyone that has laundered own proceeds.

3.9 Conclusions

In concluding this chapter, it is interesting to point out the fact that the European Union has set up a complex legislation through three different directives, promoting the harmonisation of national AML regulations to the common goal of fighting money launderers and organised crime. The Third AML Directive (2005/60/EC) has introduced a new approach within the competences of the EC Treaty, based on an active collaboration between banks, financial institutions, insurance companies and anti-fraud experts. This is the result of a modern vision, and it takes into account the problem of contrasting the economic basis of organized crime groups, but also of terrorist movements.

As a result of the financial crisis, Iceland has therefore strengthened even more the efforts toward the path of compliance with the international standards on this matter, taking into account the risks related to money laundering. As reported by the last FATF mutual evaluations report, the Icelandic AML legislation is comprehensive and generally compliant with the 40 Recommendations, but there are concerns about the system's effectiveness, that can lead to insufficient structural independence and to a lack of resources. It appears that penalties for money laundering are low, and measures are not effectively implemented, probably because there have been a limited number of prosecutions and convictions. In general, the level of crime in Iceland is very low, but the situation may be changing with growing presence of foreign criminals, especially from Eastern Europe.

As I have explained, money laundering consists of a set of activities intended to reinvest in the legal economy those financial resources or assets of illicit origin. Indeed, the criminal intent is to hide, conceal or otherwise obstruct the investigation process of the sources from which the "cleaned" goods come from. It can be said that money laundering is a phenomenon that affects the whole world, but it is particularly alarming in Italy. In the Italian legislation, there are still weaknesses related to the cooperation between administrative and judicial level, the identification of the beneficiary owner, and the diligence measures and procedures for the application of such obligations. The history of Italy has been marked by a high level of criminality thus far, especially by organized crime groups such as the *Camorra* in Naples, *'Ndrangheta* in Calabria and *Mafia* in Sicily. As it will be explained further below, mobsters are able to always come up with new fraudulent schemes, more and more sophisticated.

4. CORPORATE VEHICLES AND FINANCIAL INSTRUMENTS USED BY CRIMINAL ORGANISATIONS

4.1 Introduction

The intent of this chapter is to provide an account of the different financial instruments used by criminal organisations to avoid AML rules, as well as to discuss about some certain cases to better understand the role of banks in this matter. The following paragraphs will also provide an overview of the deficiencies related to anti-money laundering (AML), analysing some of the methods employed by the organised crime. First, how the *shadow banking system* works will be shown, which tends to help, especially through corporate vehicles, those wishing to make fraudulent transactions. Certain of these money-laundering techniques, such as *structuring*, *smurfing*, *loan-back schemes* and *back-to-back loans*, are described in some detail. Another objective is to focus on enterprise financial crimes involving *mortgage schemes* and other securities. Nevertheless, a growing number of Western countries also choose an offshore financial centre in order to receive economic benefits. This is clearly demonstrated for example by the fact that the majority of offshore bank accounts domiciled in the Caribbean Islands belong to Western corporations. However, the aim here is to demonstrate that offshore entities are a great opportunity for organized criminal networks, as they provide to their customers a high degree of confidentiality, anonymity, tax advantages, limited legal liability, and ease of transfer. Accordingly, there are undoubtedly deficiencies that the financial system and the international community have to review as soon as possible, because all these factors can facilitate those wishing to make fraudulent transactions.

4.2 Corporate vehicles and shadow banking system

Corporate vehicles are legal persons which have often been found to be misused for illicit purposes, in order to hide the financing related to transnational criminal networks. Indeed, it is a common practice to conceal the beneficial owners of an asset, or the origin of proceeds, among tax havens with a reputation for banking secrecy. Therefore, fraud schemes can be facilitated by those financial institutions benefiting from the so-called bank secrecy, unless a criminal complaint has been filed. This system makes it possible for organised crime to expand opportunities for profit and risk reduction, and to reinvest dirty money in legal enterprises.

Besides that, the *shadow banking system* (SBS) is the set of non-bank financial intermediaries, providing services similar to traditional commercial banks, that includes credit hedge funds, money market funds and structured investment vehicles (SIV). Sometimes, these types of services tend to favour money-laundering activities in the global stage, since there is the possibility to be exempt from reporting rules, and to make transactions in a way that are not visible to investors. In particular, hedge funds fit well into money laundering procedures, because they are private investment partnerships with the objective of getting higher returns. To achieve this goal, they can offer an easy way to place large sums of money into secret offshore bank accounts.

The shadow banking system flourishes within a network of offshore areas in countries with less stringent banking regulations and asset verification requirements, such as Aruba, the Bahamas, Barbados, Hong Kong, the Isle of Man, Jersey, Liberia, Lichtenstein, Nauru, the Netherlands Antilles, Nevis, Panama, and Switzerland.⁷² Criminals are using the anonymity of offshore companies to hide illicit proceeds associated with illegal activity, taking advantage of the fact that there is not enough control by the financial system. In such a situation, bankers frequently succumb to their duty of secrecy, saying that more often than not they are aware of the questionable origin of customer's deposit. Accordingly, managers or supervisors can be corrupted or intimidated by the massive amounts of money involved in the process; sometimes, they prefer to not intervene, as the transactions have already gone through multiple transfers before arriving at the end recipient bank.⁷³

4.3 Offshore banks and regulated global finance

An *aura of mystery* surrounds the offshore banks and the relationship that connect them to the regulated global finance; although the exact volume of money laundering is not easily measured, fraud experts at *Ernst & Young* estimate that organised crime earns about \$2 trillion annually,⁷⁴ and a significant portion of it is most likely being transferred to a third country through bank accounts, prime bank guarantees, bonds and other securities. In this context, tax havens have contributed to the lack of control over illegal enterprises and their business; despite that, it is necessary to ensure a minimum set of rules in terms of financial transparency. It seems interesting to put the spotlight on the mechanisms and effects resulting

⁷² Lyubov Grigorova, *Crime-Terror Alliances and the State: Ethnonationalist and Islamist Challenges to Regional Security* (Routledge 2013) 13.

⁷³ Lyubov Grigorova (n 71) 13.

⁷⁴ Tracy Kitten, 'How Organized Crime Uses Banks' (2012) <<http://www.bankinfosecurity.com/interviews/how-organized-crime-uses-banks-i-1408>> accessed 28 August 2014.

from this situation, which have represented one of the elements that have increased the spread of money laundering, certainly complicating the investigator's job.⁷⁵ The bottom line of this system is the separation between form and substance. Consequently, it is enough to add in a transaction one more formal operation (like the purchase of a financial product) - involving a company based in tax havens - that such a step ensures complete confidentiality for those involved. Generally, tax havens have two main attractive characteristics for transnational criminal networks: firstly, the rate of taxation and the monetary regulatory apparatus are practically nil; secondly, offshore banking customers have the option to carry out corporate, banking, securities, and other financial transactions⁷⁶ in complete anonymity. As a result, there are a number of criteria that a money launderer would look for when choosing an offshore bank, which, if present, create beneficial conditions for illegal enterprises activities; however, it is useless to make a list of these factors, as it could not be exhaustive. Even in the European Union, where the EU Parliament has participated actively in the development of a complex anti-money laundering legislation, a large number of financial centres can be qualified as tax and banking havens. So far there are around twenty active areas, in Luxembourg and the City of London for example, which are contributing somehow to the increase in financial fraud. In this way, globalised crime is able to avoid national regulations and controls, since cash flows are hidden in these territories where the law is more tolerant. Consequently, it is not surprising that these offshore centres can adversely affect even virtuous countries, gradually aligning themselves with these types of deregulated financial activities, which can cause a levelling down of legal provisions. Unfortunately, they are considered role models because they are not used only by professional criminals, but they also serve large enterprises, corrupt politicians and businessman for their financial operations of dissimulation of proceeds. Besides that, these options can inadvertently help fraudulent practices to contaminate the entire international economy. However, the European Parliament is trying to stem this trend with more stringent laws and regulations, because inadequacies in AML regulations represent a serious threat to the international financial system and global economy.

4.4 General schemes of money laundering

Financial crimes are often associated with structuring, smurfing, loan-back schemes, back-to-back loans, mortgage schemes and other securities, because launderers' intent is to project an image of normalcy. These frauds are notable for the variety of forms used to carry them out,

⁷⁵ John Madinger, *Money Laundering: A Guide for Criminal Investigators* (3rd ed, Taylor & Francis 2012) 136.

⁷⁶ Richards (n 24) 78.

and some of these instruments are potentially susceptible to various abuses related to money laundering. As already said in previous paragraphs, it is not easy to identify the type of schemes used by transnational criminals to reintroduce into the legal economy the proceeds of crime. In order to reach their objective, they use different tools to hide illicit proceeds associated with illegal business. Accordingly, they have developed original instruments and incompressible stratified schemes, which, due their complicated nature, facilitate the success of fraudulent transactions. Previous cases have shown that when financial authorities take action against certain techniques of money laundering, organised crime tends to change to other methods. This study has identified the instruments that are more used by criminal enterprises; anyhow more details of some of these sophisticated techniques are given as follow.

First of all, it should be immediately clarified that *structuring* and *smurfing* are two different types of money laundering systems. Even though there is not a clear delineation between these two genres, both techniques are a tiny variation of the same crime. Structuring is the act of executing financial transactions in a specific pattern calculated to avoid a mandatory reporting and a consequent creation of certain records required by law. Smurfing, by contrast, is the act of using cash from illegal sources to make multiple deposits into multiple accounts of apparently unrelated individuals, in such a way that it is possible to avoid a currency transaction report. For example, if a criminal needs to move moderate amounts of illicit proceeds, the simplest way without detection is to use anonymous helpers to split a transaction into small parts. Another popular fraud is the *loan-back scheme*, where a company essentially borrow money from itself. Accordingly, the illegal gains are transferred to the company's activities as a business loan; once the loan is executed, the criminal enterprise begins repayment, including the interest rate, with funds consisting of dirty money.⁷⁷ Furthermore, loan-back transactions are also used to buy properties through the purchase of shares in property investment funds; generally, criminals lend themselves money with the purpose to give an appearance of legitimacy and to hide the true identity of the parties.

As the previous schemes, the *back-to-back loans* are another way to launder large amount of cash. In this case, an investment organisation lends money based on the sum of money posted by the borrower in the usual way, then borrowing back that same amount of money in the

⁷⁷ Howard Silverstone, *Forensic Accounting and Fraud Investigation for Non-Experts* (3rd ed, Wiley 2012) 135.

participating bank. When the collateral posted is not specified in the loan agreement, as well as the nature, location and value of the transaction, it is very difficult to recognize the back-to-back loan. Finally, *mortgage schemes*, which constitute one of the main assets on the balance sheets of banks, are used by organized crime to promote laundering through a material misrepresentation or omission of information with the intent to deceive or mislead a lender. Therefore, the techniques used by criminal enterprises to carry out their mortgage fraud are difficult to detect for the following reasons: 1) the use of family members to move money; 2) the transfer of funds overseas; 3) the use of shell companies; 4) the use of multiple bank accounts; 6) the use of an import/export business. In the case of residential real estate for example, organised crime groups have two different options as they can continue to make regular and timely payments on the loan to integrate their illicit proceeds, or they can ask the bank for a new mortgage to buy a more expensive property, affording greater laundering possibility.

4.5 Financial instruments and warning signs to detect potential money laundering

Criminal organisations often smuggle financial instruments during the *layering* stage. The following are some of these instruments used by money launderers to conceal illegal activity proceeds: checking and savings accounts, certificate of deposit, wire transfer, insurance policy, fiduciary business, securities trading, foreign trade business or user transactions. According to a report by UNODC, there are warning signs to detect potential money laundering offences through financial instruments. It could be a warning sign „the opening of several checking accounts under one or more names, all with the same person authorized to sign checks; or the consecutive opening of several savings accounts under different names through sharing similar characteristics”⁷⁸ (such as family relationship or economic activity), but money launderers give the appearance of not knowing each other.

A checking account is a contract through which an individual or a company, known as the account holder, deposits, withdraws or consigns money to a bank in order to make use of its balance.⁷⁹ A savings account is a contract by means of which a person, either natural or legal, known as the saver, either delivers, orders or deposits sums of money to a financial entity in order to make use of the balance.⁸⁰

⁷⁸ UNODC, ‘Risk of Money Laundering through Financial Instruments, Users and Employees of Financial Institutions’ (2010) <<http://www.osce.org/eea/88254?download=true>> accessed 21 November 2014.

⁷⁹ UNODC (n 78) 11.

⁸⁰ UNODC (n 78) 23.

With regard to certificate of deposit, a warning sign could be an attempt to bribe bank officers to get them to accept partial or false information.

A Certificate of Deposit (CD) or Time Certificate of Deposit (TCD), is a financial investment product, generally short-term, offered by commercial banks and other financial institutions. A Certificate of Deposit (CD) is a time deposit that produces interest.⁸¹

An international wire transfer can be also a financial instrument used to clean up illegal proceeds, especially in cases of fractioned transfers of unlawful money.

International wire transfers are a specialised mechanism used to make electronic transfers of money from or to a given country through certain financial institutions.⁸²

In case of insurance policy, it is an alarming factor when applicants record the same address, telephone number or occupation as other people with whom they have no apparent relationship.

An insurance policy is a financial instrument that covers a risk or event, generally in the short term, renewable annually, offered by insurance companies.⁸³

Another suspicious behaviour, it could be the opening of several fiduciary lines of business by different companies all of which share the same managers or legal representatives.

A fiduciary business is a financial instrument that enables many commercial operations that a fiduciary group carries out on behalf of an individual or a legal entity.⁸⁴

Finally, warning signs regarding receipt for acceptance of money or securities are also deposits released on the same date and for similar or equal amounts in different country offices, in which the client does not have business offices or agencies. Unfortunately, money laundering methods are notable for the variety of forms used to carry them out, which can involve the complicity of the most respected bank or unsuspecting people as well. Sometimes, a financial institution can provide services to borrowers with apparently impeccable credentials and reputation,⁸⁵ as the investigative experience has shown that the use of nominees is commonly practiced by the most determined criminal organisations.

⁸¹ UNODC (n 78) 36.

⁸² UNODC (n 78) 47.

⁸³ UNODC (n 78) 57.

⁸⁴ UNODC (n 78) 73.

⁸⁵ Peter Reuter, *Chasing Dirty Money: The Fight against Money Laundering* (Institute for International Economics 2004) 25.

Nevertheless, an illegitimate scheme can involve either an international transaction or purely domestic laundering.

4.6 Money laundering cases through banks

The international case studies on money laundering show an increasing number of proceedings concerning corruption or complicity in fraudulent activities between organised crime and banks.⁸⁶ In this paragraph, I will discuss some meaningful cases that will explain the extent of this fraud. The complexity of the banking system allows organised crime to hide their illegal funds. It turns out that not only offshore banks are involved in law enforcement investigations, but also both European and American financial institutions. For example, in recent years, some large American banks have contributed to clean the illicit proceeds of criminals in Colombia and Mexico. The Wachovia Bank (now Wells Fargo) and American Express Bank International have handled illicit funds on behalf of drug cartels in money-laundering operations through currency exchange or holding companies. In the Wachovia Bank case, the ruse used by corrupt bankers consisted of transferring huge amount of money as salary payments from a Mexican currency-exchange house (*Casa de Cambios*) to that US bank. Accordingly, this was undoubtedly a suspicious monetary transaction, which significantly exceeds normal parameters and missing adequate identifying information. From a legal standpoint it can be said that these transactions, involving deposits of travellers' cheques in euros, were suspicious for lack of Know Your Client (KYC) information and AML requirements.

In the other case, two bankers were convicted for laundering illegal income belonging to a Mexican drug cartel through a Cayman Islands holding company.⁸⁷ Although, the launderers used proper structured investment vehicles (such as mortgage and other collaterals) to buy art, real estate and a Blockbuster Video franchise, the intent was just to conceal the origin of illegally obtained proceeds. In both cases, the US Custom (an agency of the U.S. Department of Homeland Security) was able to identify those accounts and to arrest corrupt bankers; furthermore, the two banks have been fined for failures in anti-money laundering controls because their measures were inadequate.⁸⁸ However, often the fines are not sufficient to prevent the involvement of financial institutions, because criminal organizations pay very well, much more of the amount of an administrative penalty. In many cases, banks can pay

⁸⁶ Richards (n 24) 91.

⁸⁷ Richards (n 24) 91.

⁸⁸ Richards (n 24) 92.

the fines without admitting their guilt, and corrupt bankers seldom go to jail, despite their direct involvement in the movement of large amounts of money in favour of the drug cartels or Mafia organizations around the world.

The British bank HSBC, the largest European financial services company, was also accused of money laundering on behalf of drug cartels and other entities banned from the American financial system; in fact, between 2007 and 2008, its subsidiary bank had transferred about 7 billion dollars belonging to the Mexican drug cartels.⁸⁹ As a consequence of a U.S. Senate investigation,⁹⁰ which demonstrates the evidence of money laundering activities and the vulnerability of the American banking system, HSBC have apologised and promised to continue to strengthen its compliance policies and procedures.⁹¹ Not one banker was prosecuted. Nevertheless, these are just some of the cases involving the banking system, which is one of the most important vehicles used by organised crime for money laundering.

4.7 Conclusions

In this chapter corporate vehicles and financial instruments used by criminal organisations have been reviewed. Corporate vehicles are generally exploited in criminal schemes as a source of legal income, but they are able to run undiscovered because they carry out perfectly legitimate business (real estate for example) which gives them an appearance of legality. In most cases, the use of corporate vehicles is facilitated if companies are entirely controlled or owned by criminals. However, the level of misuse could be reduced, if the data concerning the real owner, the source of assets and the business plan of the enterprises are easily available to the financial authorities. In this scenario, offshore companies play an important part in money laundering transactions, because beneficial owners also have the advantage of extra protection in the form of bank secrecy. As said before, money laundering is one of the most alarming issues for economically advanced nations. It is not only an economic problem, but also a matter of criminal policy. Indeed, transnational organized crime can now create complex fraudulent banking schemes, using several types of financial instruments (like

⁸⁹ Saurav K Dutta, *Statistical Techniques for Forensic Accounting: Understanding the Theory and Application of Data Analysis* (FT Press 2013) 101.

⁹⁰ The full report can be downloaded at:

<<http://www.hsgac.senate.gov/subcommittees/investigations/hearings/us-vulnerabilities-to-money-laundering-drugs-and-terrorist-financing-hsbc-case-history>> accessed 15 October 2014. The document is: *U.S. Vulnerabilities to Money Laundering, Drugs, and Terrorist Financing: HSBC Case History* (Carl Levin and Tom Coburn, United States Senate, Permanent Subcommittee on Investigations, 2012).

⁹¹ Dutta (n 89) 101.

shares, futures contracts or investment fund), and different methods (such as structuring, currency exchanges or real estate investing) to conceal illegal activity proceeds. Accordingly, the global trading environment has facilitated committing financial and white-collar crimes, and it has provided further opportunities for mobsters. Despite the global efforts, it is very difficult to stop this process as illegal enterprises are often able to circumvent the rules, and to hide their fraudulent activities in new ways. In recent years, the transnational dimension of the phenomenon has increased the involvement of international organizations. Subsequently, the international community is developing an ever increasing standard of better laws to contrast money laundering activities. Indeed, there have been different initiatives which have targeted all the offshore jurisdictions that are offering limited financial regulation. In the next chapter, real study-cases and police operations will be analysed to better understand the process used to clean up illegal proceeds, describing the background of the crime committed and how authorities applied the AML rules.

5. OPERATIONS AGAINST MONEY LAUNDERING OFFENCES IN ITALY

5.1 Introduction

It is a fact that drug trafficking and arms trade are all activities that procure illegal income to criminal organisations, which need to be cleaned with sophisticated methods before it can be spent. During the 1980s the Italian government intervention against the “mob” became more determined through the creation of a special task force, the *Antimafia Pool*. Therefore, it was a group of investigating magistrates like Giovanni Falcone and Paolo Borsellino, both murdered by Mafia bombs in 1992. As a result of their investigations, the police came to the conclusion that there was a real parallel banking system in Italy, which could rely on an extensive network of distribution. Furthermore, massive flows of cash, which were beyond all control, could be used for example to sustain the election campaign of corrupt politicians, or to finance other illegal activities. In this chapter, the way in which Italian organised crime launders dirty money will be explained. In order to achieve a better understanding of the problem, real study-cases and anti-mafia operations are used to identify the three classic phases, namely placement, layering and integration. I have personally translated from Italian some acts of judges and courts that have dealt with restrictive measures against organized crime.⁹² Basically, in the Italian system, the structure of the judiciary comprises three tiers: Court of first instance, Appellate Court and Court of Cassation. In most of these cases, investigations are still ongoing, in others the trial stage has just begun. However, in this way, I was able to make a deep analysis of all the intricate mechanisms behind the phenomenon of money laundering.

5.2 The three-stage process involved in money laundering

As previously mentioned, the laundering process is generally divided into three stages. The first phase *placement* consists of the repositioning on the legal financial system of illegal profits, necessarily characterized by the separation of these proceeds from their places of origin or from the person that has generated them. A subject who has the physical possession of the goods, cash flow or other benefits from a crime has an interest in getting rid of them as quickly as possible, safeguarding both him and the illegal gain. Then, the scope is to transform this material wealth into positive cash balance through financial intermediaries.

⁹² Please note as well that some documents are not in the public domain, but they have been made “public” on the web. Many newspapers and websites indicate that they have seen copies, and used them as a basis of their reports.

Accordingly, the placement can be performed through various operators, such as banks, insurance companies or brokers, and non-traditional financial institutions like money exchange, casinos or illegal offshore banking. Furthermore, it can be done in connection with providing direct market access for the purchase of goods, or transferring the criminal proceeds between accounts in different countries. Unfortunately, the banking sector has been used for the reallocation of the proceeds of certain criminal activities, especially in countries where the controls are not very effective.

Often, to avoid detection, criminals make transactions that do not exceed the traffic limits and the threshold beyond which accounts are selected for a report of suspected fraud. Sometimes, the underground banking system (or private lending) allows organised crime to move a large sum of money through simple and informal transactions. This is the case of the *havala system*, used to circumvent currency restrictions in some countries such as China, Pakistan and India.⁹³ With this method, there are no written records because the transactions are based solely on trust.⁹⁴ Indeed, a criminal organization gives dirty money to a local *hawala* brokers who will contact his counterpart at the destination country. Accordingly, the broker gives dispositions to his counterpart about the funds, without actually moving them, promising to pay off the debt at a later date.

In my opinion, this method is similar to the *Provenzano's pizzini*, consisting in small pieces of paper used for high-level communications by Bernardo Provenzano, the head of the *Corleonesi* (a Mafia faction), on which he wrote encrypted messages that could be decoded by the intended receivers. Often, these techniques (*havala* and *Provenzano's pizzini*) are linked to money laundering activities, because, unlike IT form of communication, are hand delivered and thus less likely to be intercepted at the placement stage.

The second phase is called *layering*, consisting of different types of commercial and financial operations that are intended to make the illegal proceeds disappearing without a trace. During this stage, criminals perform multiple transactions aimed at concealing and disguising the illicit origin of the money. Therefore, this is possible thanks to the electronic funds transfer, the use of off-shore countries, or the creation of a false paper trail to disguise the true source of the capital. In the chain of money laundering this is usually the time when organised crime gets the highest value added, which is often involved with the entrance of outside

⁹³ Madinger (n 75) 177–178.

⁹⁴ Madinger (n 75) 177–178.

professionals of various kinds. At this stage, the use of Internet banking is taking on increased importance, which is an obstacle to AML regulations as it makes it more difficult to track suspicious transactions around the world, especially in countries with offshore jurisdictions. Indeed, the web is an element of dramatic improvement for *recyclers* and a consequent alarm for the authorities that are responsible to apply anti-money laundering rules. In particular, several investigations have identified four areas of risk that could be easily exploited by criminals: 1) financial institutions providing asset protection and private banking services, principally based on extreme confidentiality; 2) online banking in countries with restrictive laws on banking secrecy and imperfect implementation of customer identification; 3) electronic commerce with internet; 4) online casinos.

The *integration* phase is the last part of this infringement, since the re-use is the final intent of the launders. On the contrary, this third phase will develop in those countries experiencing stable economic conditions and efficient financial markets. The amounts invested are back to the criminal organization that has started the process. Therefore, the money that has been cleaned up through the previous stages is now an apparently valid transaction into the legal economy. As a result, organised crime makes the reuse of dirty money in different ways, through nominees, legal entities, institutions involved in financial transactions, lawyers, notaries, banks, insurance companies, entrepreneurs, and so on.

5.3 Operation *Fulcro*

The following are some of the anti-money laundering operations carried out in recent years in Italy. In the Italian judicial system, once a public prosecutor (*Pubblico Ministero*) or a member of the police have received a crime report, they are obliged to start the preliminary investigations, involving inspections, searches, seizures, or monitoring of conversations or communications. Operation *Fulcro*⁹⁵ (*Core*) was a police operation conducted in accordance with the Court of Naples in December 2012 by the Italian anti-mafia investigations department (*Direzione Investigativa Antimafia*) targeting money laundering, with special attention to activities relating to real property, supermarkets and grocery stores. According to the Icelandic Code of Criminal Procedure (No. 19/1991) and the Regulations on custody (No. 179/1992), the person in charge of the investigation (generally the police) takes the initial

⁹⁵ Drafted in Italian, the full document, about the Court of Naples decision on pre-trial detention, can be downloaded at: <<http://www.gruppoantimafiapiolatorre.it/sito/download/atti/ordinanze-di-custodia-cautelare/finish/12-ordinanze-custodia-cautelare/29-occ-fulcro.html>> accessed 23 October 2014. The document is: *Operazione "Fulcro", Tribunale di Napoli, Ufficio del giudice per le indagini preliminari, VIII sezione, ordinanza di misura cautelare personale -art. 272 e ss.cpp-*.

decision regarding the placing of a person in a pre-trial custody. Under Article 272 of the Italian Code of Criminal Procedure, the public prosecutor (not the police) requested the competent judge to issue a pre-trial custody order against the members of the *Fabbrocino* clan to prevent further offences of money laundering. In the Italian system, the public prosecutor has the monopoly on criminal prosecutions; in fact, under Article 112 of the Italian Constitution, he has the obligation to constitute criminal proceedings.

Consequently, the investigations led to the confiscation of assets, such as real estate and companies, belonging to this criminal organisation, a Neapolitan *Camorra* clan. Therefore, a clarification is necessary here. The *Camorra* is another mob organization founded in Campania, a region in southern Italy. Unlike other Italian crime syndicates, it has its origins in the urban context and lowest social stratum. Furthermore, it has a pyramidal structure, composed of different groups and clans. However, a clan (or *family*) is a criminal association that relies on the strength of intimidation and the associative link between affiliates. According to the Italian police, the clan has committed the following crimes: usury, bid rigging, extortion, bankruptcy fraud, possession of offensive weapons in a public place, false registration of assets in favour of third parties, and especially money laundering. As a result, it has been able to cleverly conceal the illegal proceeds of its criminal activities for a long period, and at the same time to maintain a strong leadership over the Neapolitan area.

In the *placement stage*, it has placed and used 112 million euros⁹⁶ of illegal proceeds to buy real properties around Italy. The authorities started investigating these suspicious transactions, because it is during this stage that criminals are the most vulnerable to being caught. According to investigators, this was *a large washing machine* of dirty money into the legitimate financial system, as they have found that these apparently legal activities can earn over three thousand euros a week, and more than one hundred million euros a year. The *Fabbrocino* clan is characterized mainly by the fact that all affiliates perform stably in their entrepreneurial activity, particularly in the clothing industry and the trade of food, with a great ability to infiltrate even away from their territory. During the *layering stage*, the *Fabbrocino* clan has transferred funds overseas to elude investigators, taking advantage of delays in international police cooperation. Therefore extortion, fine-grained control over the

⁹⁶ Leandro Di Natta, 'Usury: The Bank System of Camorra' (European Strategic Intelligence and Security Center ESISC 2012) 3 <<http://www.esisc.org/upload/publications/briefings/usury-the-bank-system-of-camorra/Bank%20system%20of%20Camorra.pdf>>.

territory and vote trading are some of the elements that constitute the investigative framework borne by all members of the clan.

Finally, in the *integration stage*, white-collar workers, such as notaries and lawyers, have helped the clan to fully integrate these proceeds into the financial system, offering legal advice and political connections to be able to continue money laundering transactions without drawing attention. It is obvious that, this organization is a typical example of efficient money launderers, which can count on a widespread code of silence, a dense network of collusion and a hierarchical structure. Hence, all of the members of the *family* are fully aware of the role that has been granted and, accordingly, they are respectful of hierarchies. Therefore, one of the main factors that has enabled the organization to operate for such a long time in criminal activities, is the ability to provide constant economic assistance to all imprisoned members and their families. The clan economic power derives from the proceeds of unlawful activities and profits arising from conduct of entrepreneurial activity managed through the Mafia's methods. Thanks to this economic capacity, and despite the imprisonment of its leading representatives, the clan has never collaborated with the Italian justice system. Accordingly, this demonstrates the compactness and strong bond that has always linked all the *family* members. Nevertheless, the investigations have not yet come to trial.

5.4 Operation *Crimine-Infinito*

The *'Ndrangheta* is another Italian criminal organization, located in the Calabria region, which provokes a deep social conditioning based on the force of arms and on the economic role achieved through intimidation and violence. Therefore, operation *Crimine-Infinito* (*Crime-Infinity*) is a maxi-operation against this group, which was carried out by the anti-mafia investigations department of the Courts of Reggio Calabria and Milan in July 2010. Notwithstanding the trials are still ongoing, the investigation culminated in the arrest and subsequent conviction of more than two hundred people. Thanks to money laundering of proceeds of crimes (like corruption, prostitution, extortion and usury), the Calabrian Mafia is one of the world's richest criminal organizations;⁹⁷ as a matter of fact, this activity has allowed the organization to control a large segment of the economy, such as trade and agriculture, often with the connivance of administrative officials and politicians. Actually,

⁹⁷ Peter Lilley, *Dirty Dealing: The Untold Truth about Global Money Laundering, International Crime and Terrorism* (Fully rev and updated 3rd ed, Kogan Page 2006) 24–25.

this operation is divided into two different strands, operation *Crimine*⁹⁸ (focusing on Calabria) and Operation *Infinito*⁹⁹ (highlighting the stable presence of the 'Ndrangheta in Milan), but they both converge because investigations led to the same criminal network. However, the inquiry focuses more on targeting the structure of the organisation, trying to understand interconnections between criminals and power hierarchies.

During the *placement stage*, the anti-mafia investigations department found out that the Calabrian Mafia has created a whole infrastructure of companies in the northern area of Italy only for being able to clean up the illegal proceeds. Generally, these businesses were in the construction industry, and carried out by hundreds of workers, but the criminals have never paid them any social security contributions. Accordingly, this demonstrates that there was no long-range planning strategy, but only the intention to avoid a police investigation. Furthermore, modern slot machines - which were completely altered in order not to transmit any information about suspicious transactions to the state authorities - were also used to launder cash in the placement stage. This led to a finding of violation of Article 55(9) of Legislative Decree 231/2007, which provides that:

Anyone who with the intention of profiting for him/herself or for others, makes improper use, not being the legitimate holder, of credit or payment cards or any other similar kind of document permitting cash withdrawal or purchase of goods or provision of services, shall be punished with 1 to 5 years' imprisonment and a fine of from €310 to €1,550. The same penalty shall apply to anyone who, for the purpose of profiting for him/herself or for others, falsifies or alters credit or payment cards or any other similar kind of document permitting cash withdrawal or purchase of goods or provision of services, or who holds, transfers or purchases such cards or documents from an illegal source or in any case that have been falsified or altered, as well as payment orders produced with them.¹⁰⁰

In the *layering phase*, funds were transferred through bank drafts on accounts in San Marino or Luxemburg, and from there, using a trust company with headquarters in the Cayman Islands, to other financial institutions in Switzerland. Nonetheless, the wiretaps played an

⁹⁸ Drafted in Italian, the full document, about the Court of Reggio Calabria decision on pre-trial detention, can be downloaded at: <http://www.genovaweb.org/volume_primo_definitivo.pdf> accessed 23 October 2014. The file is extremely large. The document is: *Operazione "Crimine", Procura della Repubblica, Presso il Tribunale di Reggio Calabria, Direzione Distrettuale Antimafia, Decreto di Fermo di indiziato di delitto- artt. 384 e segg. c.p.p.* -

⁹⁹ Drafted in Italian, the full document, about the Court of Milan decision on pre-trial detention, can be downloaded at: ><http://www.stampoantimafioso.it/wp-content/uploads/2011/07/operazione-infinito.pdf>> accessed 23 October 2014. The file is extremely large. The document is: *Operazione "Infinito", Tribunale Ordinario di Milano, Ufficio del giudice per le indagini preliminari, ordinanza di applicazione di misura coercitiva con mandato di cattura, - art. 292 c.p.p.* -

¹⁰⁰ Legislative Decree 231/2007 (n 65) 39.

important role in understanding the method used to launder capitals. For example, it has been established that a mobster can drive a car in a short time from northern Italy to Luxembourg, where illicit financial flows disappear through regular bank transactions. Most of the time, the same operation is also carried out with financial institutions of San Marino. In that way, the clan has accumulated in the *integration stage* a portfolio of over sixty million euros, consisting of buildings, garages, warehouses and other forms of wealth.

5.5 Operation *Phuncards-Broker*

In this case, there are many different actors such as the Calabrian Mafia, telecommunications providers, brokers, offshore companies, businesspeople and corrupt politicians, who are all involved into a money laundering and tax-evasion scheme. Although preventive custody and house arrest warrants were issued after allegations of money laundering, at the time of writing, the trial is still ongoing. As a result, two parallel investigations were conducted in concert with the national military police (*Carabinieri*) and the special force responsible for financial crimes (*Guardia di Finanza*), which joined their forces to carry out operation *Phuncards-Broker*¹⁰¹.

The investigation began when an attempted bribery of police officers lead to the same offshore company, called *Broker Management Ltd.*, that had been identified as the recipient of suspicious transactions related to the sale of international phone cards and VoIP termination services. In the *placement stage*, there was an attempt by criminals to transfer funds from illicit activities (here the phone cards were not real, and the VoIP termination services were not provided to end-users) in the circuit of the legal capital market. Thus, the Rome District Anti-Mafia prosecutors had detected a complex scheme to launder large amounts of money through different companies, based on Italian, Panamanian, Luxembourgish, Finnish, British and French laws.

The large sums of illicit money came from various fictitious transactions of wholesale telecommunications services that occurred with the widespread knowledge of the directors of two Italian telephone companies, *FastWeb* and *Telecom Italia Sparkle*. According to the prosecutor of Rome, the headquarters of this transnational criminal organization was a luxury villa in Antibes (France) where the fraud was prepared, but developed in two other EU

¹⁰¹ Drafted in Italian, the full document, about the Court of Rome decision on pre-trial detention, can be downloaded at: <http://www.genovaweb.org/doc/ord_BROKER-1pt.pdf> accessed 23 October 2014. The document is: *Operazione "Phuncards-Broker," Tribunale Ordinario di Roma, Sezione Distrettuale dei giudici per le indagini preliminari, Ufficio 40, Procedimento N. 6429/2006 R.G.*

countries (UK and Italy). The scheme is characterized by two circular flows that were equal and opposite at the same time: the financial flow was real and the commercial flow was fictitious, because they were covered by false billing. This included, among recipients, companies domiciled in non-EU territories (Panama and the British Virgin Islands), and known as tax havens. Therefore, in the *layering stage*, complacent senior officials have used dummy corporations with the sole objective to justify, through the use of invoices or other documents for non-existent transactions, the cash flows generated from the proceeds of criminal activities.

The amount of money laundered is quantified only in rough terms; nevertheless, the authorities focused more on the methodology of this complex global fraud, which led to the arrest of 52 people. However, in the *integration stage*, fraudsters were able to reinvest this capital in order to gain an additional profit, because they had the capacity to transfer and clean huge flows of money, using a classical organized crime structure.

5.6 Operation *Fort Knox*

Operation *Fort Knox*¹⁰² was a law enforcement operation, conducted by the *Guardia di Finanza*, targeted at dismantling an organization devoted to money laundering, handling stolen goods, tax fraud and misuse of the gold trade. Therefore, police forces have discovered in the course of the investigations, as is often the case, that since the beginning of the economic crisis many cash-for-gold shops are in collusion with organized crime. As stated in a report by the Italian Senate of the Republic,¹⁰³ 60 percent of this type of business is subjected to Mafia infiltration and is related to criminal phenomena such as money laundering. The investigation, coordinated by the public prosecutors of Arezzo and Naples, has uncovered a complex money laundering scheme. More specifically, the public prosecutor of Arezzo found that this criminal organisation has infringed Article 49 on the limitations on the use of cash and bearer instruments of Legislative Decree 231/2007. Paragraphs 1 and 2 of Article 49 provide that:

¹⁰² Drafted in Italian, the document about *Operation Fort Knox* and a search warrant issued by the Court of Arezzo can be downloaded at:

<https://www.senato.it/application/xmanager/projects/leg17/attachments/documento_evento_procedura_commissione/files/000/001/212/2014_04_08_Presentazione_audizione_GdF.pdf> accessed 28 October 2014.

¹⁰³ Drafted in Italian, the full report about the spread of cash-for-gold shops in Italy can be downloaded at: <https://www.senato.it/application/xmanager/projects/leg17/attachments/documento_evento_procedura_commissione/files/000/000/882/2014_01_23_-_AIRA_-_Dossier_mercato_oro.pdf> accessed 29 October 2014. The document is: *Dossier sulla diffusione dei negozi Compro oro sul territorio nazionale AIRA - ANOPO, aprile 2012*.

1. It is forbidden for any reason to transfer cash or bank or postal bearer deposit instruments or bearer instruments in euro or foreign currency between different persons when the value of the transaction, even if subdivided, is €1000 or more in total. Transfers may however be made through banks, electronic money institutions and *Poste Italiane S.p.A.*

2. Transferring cash by means of persons referred to in paragraph 1 must be done according to an order accepted in writing by such persons, after prior delivery to them of the cash. From the third working day following that of such acceptance, the beneficiary shall have the right to obtain the payment in the province of domicile.¹⁰⁴

This article prohibits the transfer of money in cash (or divided into several tranches) of more than 1000 euros. Beyond this amount, the seller has to use checks or credit cards, which are traceable instruments. The gold buying stores involved in this operation have paid the jewels in cash, which were often in excess of the above limit. According to this inquiry, criminals were able, in the *placement* and *layering stages*, to launder large amounts of stolen gold through a network of cash-for-gold shops, located over a large portion of the Italian territory. In essence, exemplifying the scheme of this parallel system, it was found that all trades were done taking as a basis the official price of precious metal as investment fixed daily by the London Stock Exchange (LSE).

In the *integration stage*, the plan was intended to bring the illegal gold back in the international trading market once in the Swiss territory. Thus, the precious metals, mainly of dubious origin, were transformed into ingots and subsequently marketed in the Swiss gold market. Basically, the precious metal was likely the loot of stolen goods, such as robbery or theft in apartments. The boss of this organization, having a pyramidal structure, is an Italian citizen living in Switzerland. He made use of his Italian counterparts in order to direct the collection and delivery of gold. Accordingly, intermediaries had bargained this precious metal with gold buying stores. In particular, they used cars equipped with sophisticated double bottoms which can be activated electronically; and on other occasions they concealed the gold, to be commercialized in Switzerland, in anonymous luggage trolleys. Finally, this criminal network has shown in just 8 months of activity a significant increase in its turnover, because it has collected and marketed 4390 kg of illegal gold, with a laundered income of more than 175, 620, 000 euros.¹⁰⁵ However, there is not yet a final judgment but only the end of the preliminary investigations.

¹⁰⁴ Legislative Decree 231/2007 (n 65) 33.

¹⁰⁵ Operation Fort Knox (n 102) 3.

5.7 Conclusions

This chapter, based on real study-cases and anti-mafia operations, has examined the way in which Italian organised crime launders dirty money. Therefore, the laundering of criminal proceeds is the essence of organized crime business, because any illegal activity needs a cleaning process for the wealth produced. Whenever criminals invest to clean up their own money, they also gain from the investment. Sometimes normal entrepreneurs and mobsters reach an agreement to launder illicit funds, distorting the dynamics of the free market.

Through speculative transactions on the secondary market for listed securities, targeted investments, or the sale of securities at a loss, they can generate capital gains that are difficult to track down. In addition, the part of the internet that is not indexed by search engines, called *deep-web*,¹⁰⁶ is one of their favourite platforms used to transfer money or to sell illegal material. Moreover, organized crime creates companies that are formally legal, which are able to obtain loans from banks due to persuasive methods used (like financial corruption or other forms of intimidation). Since the end of the Second World War, there have been numerous investigations against the *Cosa Nostra* (translated as "our thing"); notwithstanding that, it is still one of the most powerful criminal organisations. Over the years police forces have been involved in a series of operations, all composing the law enforcement aspect of the complex fight against the mob. On the basis of the Latin saying *pecunia non olet* ("money doesn't stink"), banks are more often than not providing their investment services to organised crime because illicit financial flows are attractive. Indeed, in the last few years, all around the world numerous cases of Mafia's presence in financial structures have emerged. Thence, it is imperative to fight corruption because it allows the financial Mafia to survive. Despite obstacles, authorities continue to give a strong signal that such crimes are not tolerated.

¹⁰⁶ Jannis Kallinikos, *The Consequences of Information Institutional Implications of Technological Change* (Edward Elgar 2006) 166 <<http://www.books24x7.com/marc.asp?bookid=22383>> accessed 27 October 2014.

6. NEW EFFORTS, IDEAS AND TOOLS TO PREVENT MONEY LAUNDERING

6.1 Introduction

In this chapter new efforts and solutions to prevent and combat money laundering are discussed. The aim is to provide an overview of the new measures and tools that can be adopted to avoid the fraudulent use of the financial system. I have made a note of the international dimension of money laundering activities and the high presence of white-collar workers who use complex schemes to conceal the origin of the proceeds of a crime. For this reason, the new way to deal with this criminal phenomenon is to adopt common measures to ensure the integrity and stability of banks, along with confidence in the financial system as a whole. As explained in previous sections, the legal basis to harmonise the legislation at EU level is determined by Directive 2005/60/EC. Furthermore, the FATF Recommendations are the guidelines at international level for the financial intermediaries and governments to ensure that organised crime cannot transfer illicit financial flows through fraudulent schemes and transactions. In this context, the strategy is a new approach to increase cooperation between countries, implementing transparency requirements and data protection, facilitating the identification of beneficial owners of securities, and avoiding confusion on reporting obligations.

6.2 Upcoming Fourth AML Directive and EU-wide register of beneficial ownership

The Fourth Directive on money laundering should be an example of harmonization of criminal law in the European Union. Subsequently, the European Commission issued two different legislative and complementary proposals, with the intention of updating the discipline with a new directive. As regards to the context of this proposal:

The main objectives of the measures proposed are to strengthen the Internal Market by reducing complexity across borders, to safeguard the interests of society from criminality and terrorist acts, to safeguard the economic prosperity of the European Union by ensuring an efficient business environment, to contribute to financial stability by protecting the soundness, proper functioning and integrity of the financial system. These objectives will be achieved by ensuring consistency between the EU approach and the international one; ensuring consistency between national rules, as well as

flexibility in their implementation; ensuring that the rules are risk-focused and adjusted to address new emerging threats.¹⁰⁷

As it will be explained further below, there is also a plan to build up a public trust register to be able to finally break away the practice of hidden company ownership, and to gain an outcome of more transparency around EU countries. The proposed Fourth AML Directive is therefore aiming to increase transparency across the Member States. For this reason all enterprises will have to perform due diligence analysis and to hold data on the ultimate beneficial owners for the identification of corporate banking customers. In particular, they will be required to maintain records as to the identity of those who stand behind the company in reality. According to paragraphs 1 and 2 of Article 12 of this new provision:

1. Member States shall require that the verification of the identity of the customer and the beneficial owner takes place before the establishment of a business relationship or the carrying-out of the transaction. 2. By way of derogation from paragraph 1, Member States may allow the verification of the identity of the customer and the beneficial owner to be completed during the establishment of a business relationship if this is necessary not to interrupt the normal conduct of business and where there is little risk of money laundering or terrorist financing occurring. In such situations these procedures shall be completed as soon as practicable after the initial contact.

In addition, the upcoming Directive will permit banks to perform high standards for AML and to strengthen the cooperation with the national Financial Intelligence Units. In fact, as it stated in Article 32:

1. Member States shall require obliged entities, and where applicable their directors and employees, to cooperate fully: (a) by promptly informing the FIU, on their own initiative, where the institution or person covered by this Directive knows, suspects or has reasonable grounds to suspect that funds are the proceeds of criminal activity or are related to terrorist financing and by promptly responding to requests by the FIU for additional information in such cases; (b) by promptly furnishing the FIU, at its request, with all necessary information, in accordance with the procedures established by the applicable legislation. 2. The information referred to in paragraph 1 of this Article shall be forwarded to the FIU of the Member State in whose territory the institution or person forwarding the information is situated. The person or persons designated in accordance with the procedures provided for in Article 8(4) shall forward the information.

¹⁰⁷ 'Proposal for a Directive of the European Parliament and of the Council on the Prevention of the Use of the Financial System for the Purpose of Money Laundering and Terrorist Financing' (2013) <<http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52013PC0045&from=EN>> accessed 4 December 2014.

As result, they will have a broader ability to consider the outsourcing of due diligence processes. However, the European Parliament is yet to vote on the Fourth AML Directive and it is possible that there will be additional changes to these proposals.

During the end of the winter of 2014, the European Parliament condemned the use of shell companies to hide the operations of money laundering or tax fraud. Accordingly, they voted to introduce an EU-wide register where ultimate owners of companies would have to be listed.¹⁰⁸ This register will be used to immediately detect fraudulent transactions to offshore accounts, and it will also contribute significantly to limit tax evasion. With this vote, the Parliament provides for the establishment of a centralized register in each country of the EU, with public information regarding the owners of corporations, foundations, trusts and holding companies. Finally, this centralized register will be based on three points: 1) verification of customers; 2) archiving and cataloguing of relationships and transactions; 3) identification and reporting of suspicious transactions. In particular, the Parliament has targeted the whole system of the so-called "Chinese boxes", behind which organised crime conceals the illegal operations. The idea is to create an EU-wide register of who really holds companies to make sure that once data is collected, it's usable to identify the ultimate owners. It may certainly be an important step in the fight against the long-standing practice which ensures offshore companies the opportunity to hide their financial dealings thanks to anonymity. The draft rules want to make sure that if done deliberately, activities such as concealing, disguising, converting, transferring or removing source and ownership, in a member state or in the third country, would be considered fraud. This could represent a positive beginning as the register can provide a tool for financial institutions and law enforcement bodies to prevent the abuse and to look directly into the ultimate beneficiaries of companies.

However, the records will be used only to identify beneficial owners, because it is also important to guarantee data protection. Indeed, there are a number of safeguards to protect privacy by ensuring that it will be disclosed in the register only essential information. Nevertheless, beneficial ownership registers will be available throughout the European Union, with an on-line registration, previous identification of the person seeking access to the data. As a result, banking and financial institutions, accountants, lawyers, notaries, tax advisers and real estate agents will be required to be enrolled in the register.

¹⁰⁸ Dorata Kolinska and Isabel Teixeira Nadkarni, 'Money Laundering: MEPs Vote to End Anonymity of Owners of Companies and Trusts' (20 February 2014) <<http://www.europarl.europa.eu/news/en/news-room/content/20140210IPR35562/html/Money-laundering-MEPs-vote-to-end-anonymity-of-owners-of-companies-and-trusts>> accessed 6 November 2014.

6.3 European Business Ownership and Control Structures (EBOCS)

In January 2014, the Directorate-General of the European Commission funded a new project of eighteen months' duration called European Business Ownership and Control Structures (EBOKS). It consists of the development of new IT services to facilitate financial investigations in the fight against money laundering. Therefore, EBOKS has created a search engine to provide simplified and unified access to data on business ownership and control structures, whenever information come from various company registers in Europe. The benefit of implementing IT services is an increase in the level of transparency on legal entities during financial analysis and investigation purposes. In the past, accessing all enterprise registers across EU countries would have been impossible; instead, EBOCS allows law enforcement and financial intermediaries - subjected to Anti-Money Laundering regulations and customer due diligence measures - to carry out faster and more effective investigations. In this first phase, the European Business Ownership and Control Structures have initiated his activities in five pilot countries (Italy, Ireland, Romania, Estonia and Latvia). This network is coordinated by the European Business Register (EBR), with the participation of different IT Service Providers at European level: the Irish Enterprise Registry Solutions, the Italian *InfoCamere*, the Estonian *Registrite ja Infosusteemide Keskus*, the Romanian *Oficiul the National Registrului Comertului* and the Latvia's Financial Intelligence Unit.

Today, the use of new technologies is fundamental in the fight against money laundering and organised crime activities. To this end, significant developments have occurred in the field of artificial intelligence, computer graphics and statistical computing. Accordingly, these technologies can improve wire transfers fraud detection, as well as the monitoring and identification of potentially suspicious transactions (like the GIANOS procedure). At the same time, financial operations move through large computer networks and each wire transfers can hide fraudulent activities. Unfortunately, the speed with which suspicious transactions can be completed makes their identification difficult. Indeed, the development of new digital technologies and the advent of globalization, as we have seen, while it has certainly opened up new opportunities for the growth of enterprises and the detection of criminal schemes, on the other hand have simultaneously increased the risks associated with the concealing of illegal proceeds across national borders. As a result, the task of identifying suspicious transactions is certainly not easy, but every financial intelligence units have their own systems.

For example, the Financial Crimes Enforcement Network (FINCEN), a bureau of the U.S. Treasury Department, has developed a system based on the use of artificial intelligence, called FAIS (FinCEN Artificial Intelligence System). This system is currently used to investigate reports that the U.S. Treasury Department receives under the provisions of the Bank Secrecy Act.¹⁰⁹ The FAIS procedure is able to process any transfer of funds through American financial intermediaries. Furthermore, this procedure is equipped with special software of artificial intelligence that allows operators to conduct cross-searching of the activities of companies or banks under investigation. It is also programmed to scan tens of millions of currency transactions and automatically report anomalies and suspicious manoeuvres. The main feature of this technology lies in the fact that it is continually updated to reflect changes in money laundering techniques. The system is available only to American investigations agencies but, thanks to an agreement with the Egmont Group,¹¹⁰ the Financial Crimes Enforcement Network is authorized to pass certain personal information to the foreign FIUs. Accordingly, these data can be shared with the other Financial Intelligence Units in the course of a large-scale investigation.

6.4 Code of conduct and ethical banking

Broadly speaking, the mechanisms used by financial speculators in order to obtain the most profitable investments are similar to those used to commit crimes such as money laundering. In economics and finance there is a huge "grey zone" between legal and illegal operations. In fact, there are opportunities provided by offshore countries and tax havens characterised by the total lack of transparency regarding transactions and AML regulations. As a result, the huge profits of the criminal organisations can easily move there, while financial intermediaries can offer the perfect way to launder money. The fight against tax havens and offshore countries is therefore a matter of collective economic interest. For this reason, it is essential to intervene at the legislative level to put an end to the fraudulent practices permitted or tolerated in those areas. In this context a code of conduct can regulate comprehensively the behavior of banks and other financial intermediaries.

¹⁰⁹ Bank Secrecy Act of 1970, H.R. 15073, 91th Cong. § 91-508 (1970). Available at: <https://fraser.stlouisfed.org/scribd/?title_id=1025&filepath=/docs/historical/congressional/bank-secrecy-1970.pdf> accessed 7 November 2014.

¹¹⁰ 'The Egmont Group of Financial Intelligence Units' <<http://www.fincen.gov/international/egmont/>> accessed 7 November 2014.

The Core Principles,¹¹¹ adopted by the Basel Committee, are probably the starting point. Indeed, they highlight the increasing risk of involvement in the banking and financial system of money laundering offences, and they outlines a sort of code of conduct for financial intermediaries. This text is devoid of cogency, but it is not without values along the lines of moral suasion¹¹² towards credit institutions. The Core Principles have four objectives, the pursuit of which is seen as being very important for banks and national supervisors.

1. The necessity for identifying the customer and, in parallel, for maintaining internal documentation of the transactions.
2. The necessity to facilitate strict observance of laws and regulations.
3. The necessity to facilitate cooperation with law enforcement officials conducting investigations.
4. The adoption of policies that are consistent with the Declaration, ensuring that staff understand these standards and are informed enough to implement them.¹¹³

An ethical bank is also an interesting initiative to be encouraged, because it is a sustainable institution which operates on the financial market with moral guidelines. Accordingly, ethical banks provide their customers with the normal banking services, but they apply specific criteria in the selection of investments on which to place the savings collected. Sometimes, they are also offering microcredits¹¹⁴ to customers in particularly difficult situations (in typical cases where a client cannot use the traditional financial channels), providing them with low-interest loans. Another objective is that a banking operation involves the transparency guarantee on the types of investments offered. Therefore, among the requirements of an ethical bank, there are the following:

- 1) Ethical initiatives: the funds collected are used only to support moral initiatives. Accordingly clients can choose the sector on which they want allocate their savings.
- 2) Self-determination of the rate: indeed, the customer can choose the interest rate charged on its deposit between a minimum and maximum range of values.

¹¹¹ Basel Committee on Banking Supervision 'Core Principles for Effective Banking Supervision' (Bank for International Settlements 2012) <<http://www.bis.org/publ/bcbs230.pdf>> accessed 3 December 2014.

¹¹² Moral suasion means: „the attempt to coerce private economic activity via governmental exhortation in directions not already defined or dictated by existing statute law." See: J.T. Romans, "Moral Suasion as an Instrument of Economic Policy," *The American Economic Review* (American Economic Association) 56, no. 5 (December 1996): 1220-1226.

¹¹³ Basel Committee on Banking Supervision, 'Core Principles for Effective Banking Supervision' (n 110).

¹¹⁴ Microcredit is a useful tool for combating poverty and financial exclusion, which provides access to banking services (like loans) for indigent people.

- 3) Interpersonal relationships: the investor is always identified and there are no forms of bearer deposit note.
- 4) Transparency: savers must be informed of the specific use of their funds.

Although, mobsters are able to find new ways to conceal their illegal proceeds, in my opinion the promotion of ethical initiatives and the use of a strict code of conduct can at least make the banking system less attractive to the Mafia.

6.5 Blacklist and new agreement to end bank secrecy

Generally, a blacklist is a register compiled by the Organisation for Economic Cooperation and Development (OECD), which indicates countries that have special tax regimes and strict banking secrecy regulations. In regard to the prevention of money laundering, the Financial Action Task Force (FATF) published in 2000 the first blacklist of countries that do not conform to international standards, identifying 25 criteria that allow detecting non-cooperative behaviours. The FATF has analysed the weaknesses in control systems to prevent fraudulent activities in countries with international financial markets, and in particular, offshore centres. However, the blacklist only includes those countries monitored that are not respecting the principles set out in the forty recommendations. In particular, it refers to tax havens that are explicitly opposing any type of dialogue with the international community.

The register is updated regularly and it has not only an informative character - in fact, it is a valid tool that enables, for example, the Interpol to perform more accurate investigations against criminals and those who help them. In addition, it is a deterrent to encourage offshore countries to adapt their legislation to more effective AML regulations in line with the required standard. Nevertheless, the blacklist has dwindled rapidly as many countries have adapted, at least formally, to the measure requested, and returned as full participants in the global financial community after a short period of quarantine. Unfortunately, the global offshore network is also used by the same actors that are demanding in international fora for greater transparency and security in financial transactions. Despite official condemnation and a solemn commitment to combat money laundering, these countries are accompanied by a total laxity in regards to enforcement of the rules they have helped to promote. The reason being that the size of the illegal economy is such that the acquisition of the flow of 'dirty money' becomes an important geopolitical matter. Indeed, tax havens compete against each other to absorb shares of criminals' capital within their national banking and financial systems.

The end of banking secrecy could be another important step towards greater transparency of financial transactions. The Multilateral Competent Authority Agreement, signed by 51 countries, moves in this direction. Beginning in 2017, finance ministers of the OECD member countries will have access to data concerning illegal transfers abroad as well as income held outside local tax jurisdictions. The major EU countries (like Germany, France and United Kingdom) and several well-known tax havens (such as the Cayman Islands, Bermuda and Liechtenstein) are among the signatories of this agreement sponsored by the Organization for Economic Cooperation and Development. The new mechanism for data exchange between OECD member countries will allow automatic share of information on an annual basis regarding bank accounts, taxes, assets, and underwriting income generated by insurance policies. Therefore, these data should be provided primarily by banks but also by brokers, insurance companies as well as some collective investment vehicles. Following several cases of money laundering offences and under international pressure, Switzerland, Austria and Luxembourg will end banking secrecy and also join the initiative by 2018.

6.6 The establishment of the CRIM

The European Parliament has established on 14 March 2012 a Special committee on organised crime, corruption and money laundering (CRIM).¹¹⁵ It is a special task force to prevent and counteract criminal activities conducted at national, European and international level through legislation or other initiatives. Indeed, the EU has realized that these criminal phenomena have a negative impact on the security of citizens and the interests of European companies. The establishment of the CRIM is also a measure consistent with the new and important responsibilities conferred to the European Parliament by the Treaty of Lisbon in the field of police and judicial cooperation against organised crime. According to the Title V of the Treaty:

Police and judicial cooperation in criminal matters takes the form of: 1) cooperation between national police forces; 2) cooperation between national customs services; 3) cooperation between national judicial authorities.

However, the committee has a one-year term, renewable for a further year and has the power to make on-site visits, holding hearings with EU and national institutions from all over the world. Furthermore, the MEPs can meet representatives of business and civil society, families

¹¹⁵ Federico De Girolamo, 'Organised Crime, Corruption and Money Laundering: MEPs Table Crackdown Hit List' (17 September 2013) <<http://www.europarl.europa.eu/news/en/news-room/content/20130916IPR20026/html/Organised-crime-corruption-and-money-laundering-MEPs-table-crackdown-hit-list>> accessed 4 December 2014.

of Mafia victims or judges, involved in the daily fight against organized crime. The CRIM performs two main tasks: the monitoring of Mafia-type organisations, and the processing of a joint plan at the European level to combat corruption and money laundering. It certainly is an effective tool, but it has to be supported by harmonisation of the criminal law procedure of the EU member states, and to further development of the legislation through the upcoming Fourth Anti-Money Laundering Directive. According to the CRIM, many criminal groups have a network structure characterized by high levels of flexibility and mobility, accompanied by a remarkable capacity for infiltration and corruption. As a result, this leads to the ability to take advantage of a 'grey area' of collusion with other parties, such as government officials, politicians, banks, professionals and so on, with whom they have mutually profitable business relationships. The Special committee on organised crime, corruption and money laundering has presented a plan for 2014-2019 that aims at attacking organized crime through a series of actions. As an essential remedy, the CRIM proposes the elimination of tax havens, the introduction of the offense of vote trading and the disqualification from holding public office for at least five years for anyone who has been convicted of corruption offenses or money laundering. The creation of a common anti-mafia legislation, integrated and harmonised to all states, is still a long way off. Nevertheless, the awareness and early action by the member states, as well as the establishment of a body like the CRIM, bodes well.

6.7 Establishment of an International Financial Criminal Court

Due to jurisdiction complications, governments face the inability to prosecute money laundering offences from anywhere - both when it comes to Mafia-type organizations or white-collar criminals. The question arises as to whether it should be established an International Financial Criminal Court (IFCC) with power to take legal action to counteract fraudulent activities. This type of jurisdiction can be created to reduce the lack of implementation in the fight against organized crime and to more effectively prevent international money laundering. Accordingly, the creation of the IFCC would be a functional tool for several reasons. Firstly, it can be a valid judicial body which can end impunity for cases of corruption and financial crimes, since violations of AML regulations have to be punished worldwide. Secondly, the Court will act whenever local justice institutions are unable to properly prosecute a suspected money launderer, especially in offshore countries or in economies with a weak banking system. Thirdly, it can be a deterrent to discourage or prevent future money laundering activities once it is clear that white collar crimes will no

longer go unpunished under this universal jurisdiction. Finally, an International Financial Criminal Court would allow legal action to be taken in every country and would start an investigation process independently with a staff of experts and prosecutors. Therefore, the centralisation of investigative powers into a single judicial body could certainly reduce the fragmentation of the global justice. In my opinion, there are already some candidates, among the existing international judiciary, for taking jurisdiction over global money laundering offenses. The first of these judicial bodies is the International Criminal Court (ICC), which prosecutes individuals accused of „the most serious crimes of international concern, namely genocide, crimes against humanity and war crimes”.¹¹⁶ The International Court of Justice (ICJ) could be another legitimate alternative. As evident, there is not the will to improve the current state of affairs. It seems that the international justice is just a process intended to condemn dictators and criminals overtaken by history, since it would have been enough to extend the mandate of one of the above bodies (ICC and ICJ) also to money laundering offenses.

6.8 Conclusions

The ideas discussed in this chapter have shown that there are different usable solutions to efficiently combat and punish suspected money launderers. The new global strategy for money laundering detection aims to transform financial intermediaries in effective anti-money laundering supervisors. It imposes on them a number of obligations to cooperate with local or supranational authorities having jurisdiction in financial crimes. In particular, operators are required to make a due diligence investigation of their customers in order to quickly identify their economic profile. In light of a better performance, the introduction of an EU-wide register - where ultimate owners of companies would have to be listed - could be a solution to ensure more transparency around EU countries. In regard to the monitoring and evaluation of non-cooperative behaviours, the existence of a blacklist represents a deterrent to encourage offshore countries to implement their AML regulations. I also found that the use of new technologies (like artificial intelligence, computer graphics and statistical computing) has certainly opened up new opportunities to conduct cross-searching of the activities of companies or banks. This means that through a link analysis for example, it is possible to represent the probabilistic relationships between criminal networks and financial transactions,

¹¹⁶ 'ICC - International Criminal Court' (*About the Court*) <http://www.icc-cpi.int/en_menus/icc/about%20the%20court/icc%20at%20a%20glance/Pages/icc%20at%20a%20glance.aspx> accessed 3 December 2014.

providing law enforcement with a graphical model to discover, examine and rebuild possible fraudulent practices. Probably, the promotion of ethical alternatives and the creation of a code of conduct could make the banking system less attractive to criminals. Therefore, the centralisation of investigative powers into a new judicial body (like an International Financial Criminal Court) or into an existing international judiciary (ICC or ICJ) could certainly reduce the fragmentation of the global justice.

7. CONCLUSION

This thesis, based on my research, has examined the use of financial instruments by criminal organisations for the purpose of money laundering. The conclusion of this investigation indicates that from a certain standpoint - in spite of anti-money laundering laws and regulations - fraud and financial crimes are everywhere, although authorities' efforts are large and complex. This conclusion is based on the fact that there is a real substantial difficulty identifying the criminal origin of an economic activity, outwardly entirely legal, but characterized by a hidden delinquency. As such, illegal enterprises undoubtedly have an economic, political and social power that is bigger and higher than imagined, because they are linked in the most varied sectors of everyday life. It is interesting to point out the fact that, thanks to globalisation and other structural factors, the integration into the world economy has created opportunities for crime and criminality. In addition to the above, the lacks of coordination between supranational structures, and the possibility to use heterogeneous banking products to launder money, add to the complexity of these issues.

Today, criminals have large funds of illicit origin, which are fraudulently returned to the circuit of lawful economic activity. Unlike criminal organisations - which have branched out their national borders, taking advantage of the current globalisation trends - governments are not yet fully aware of the problem, since they do not have developed effective measures of global contrast. Theoretically, this debate - on the different financial instruments used by criminals to conceal the origin of illegally obtained proceeds - can continue indefinitely, because organized crime needs constantly new schemes. Therefore, they use highly sophisticated techniques, provided by the shadow banking system and the offshore financial centres, to be able to use efficiently the huge amounts of illegally obtained funds. Correspondingly, cooperation between governments, banks and the global financial system represents a crucial aspect of protecting and enforcing AML regulations.

The current legal regime rests on prevention, enforcement and compliance,¹¹⁷ but there is still a significant gap between legal systems with traditional commitments to bank secrecy. For example, in many offshore financial centres, *Know Your Customer* and *Customer Due Diligence* regulations are insufficient for the compliance function, as they are frequently superficial and not adequate. However, these standards are not intended only to protect clients or financial institutions, but their role is especially to safeguard the stability and

¹¹⁷ Daniel Adeoyé Leslie, *Legal Principles for Combatting Cyberlaundering* (Springer 2014) 120.

integrity of the global economy. Despite that, all governments and banks play a key role in ensuring: 1) the development of stricter rules on the subject of *Know Your Customer* and *Customer Due Diligence* regulations; 2) the adoption of more appropriate measures of control and identification; and 3) the achievement of effective collaboration between financial institutions and those authorities involved in AML compliance. Therefore, financial intermediaries need to fulfil these provisions to bring them into closer alignment with all FATF Recommendations.

The analysis also researched the legal basis of the Italian and the Icelandic anti-money laundering regulations and how Italy and Iceland have implemented the Directive 2005/60/EC. The following question has been considered: are Italy and Iceland doing enough to combat organised crime and their fraudulent activities? After a thorough analysis of the two AML regimes, I have reached a stage where it can be asserted that both Iceland and Italy have made significant progress. In spite of the fact that Iceland and Italy have a different economic and financial development, the Icelandic AML legislation performs quite similar elements with the analogous Italian regime, as both disciplines reflect the principles developed by the FATF Recommendations and the third EU Directive 2005/60/CE. As regards to the local conditions, there is a persistent Mafia presence in Italy, while there are no cases of money laundering activities linked to organised crime in Iceland. Despite the fact that the recent financial crisis has hit Iceland particularly hard, the rapid rise of the banking system should be seen by the international community as an example of virtue; in particular, there were healthy parliamentary inquiries and legal proceedings, which have been important factors in the national economic recovery. The main countermeasures that Icelandic authorities have used to combat the crisis were the enforcement of strict capital controls, the activation of a sovereign debt package for the support of the finance budget deficits, and the activation of a minimum deposit guarantee repayment loans for the repayment of foreign account holders (having lost their savings due to the bankruptcy of the banks).

Furthermore, the Italian National Anti-Mafia Directorate (*Direzione Investigativa Antimafia*) shows an alarming picture of the alleged links between the Mafia and some banks; therefore, there are many reports about business relationship among these two entities. In addition, some of the money earned from illegal profits are laundered through local enterprises or other

financial intermediaries, and especially reinvested in construction projects.¹¹⁸ Moreover, through shell companies, Italian criminals are able to get loans without collateral, or to clean up illicit proceeds through investment in disparate business. In this context they are able to complete fraudulent activities of high performance with lower risk. Another option is to set up finance companies to lend money at usurious rates of interest, in part as a means of clean up *dirty money* or to unfairly enrich the Mafia. Nevertheless, the effort to target money laundering and financial crimes is enormous, and law enforcement operations shown in the above chapter are just a few of the thousands investigations carried on in recent years by the Italian police.

I have observed how organised crime is able to easily change its field of action: from drug trafficking to usury, from international trade in fake phone cards to obstruction of the exercise of the right to vote, or from money laundering to handling stolen goods. As we have seen, the Mafia phenomenon affects the Italian political structure and economic system, leading to corruption, tax evasion or illegal work. Notwithstanding all this, the Mafia must be seen as a historical phenomenon that, like all historical phenomena, had a beginning and an end. Some of the remedies available are easily enforceable, but it seems what is still missing is the will to improve the current state of affairs, especially at regional and local levels. However, I have noticed that, despite these complications, AML policies are increasingly interconnected across jurisdictions as a result of a continuously evolving regulatory framework. Therefore, the proposed Fourth AML Directive could be an exemplary model for future harmonization of criminal law in the European Union.

¹¹⁸ Michael Dunford, *After the Three Italies: Wealth, Inequality and Industrial Change* (Blackwell Publishing 2005) chap 3.

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