ANTI-MONEY LAUNDERING

Hot property, even hotter money

A Regulatory Intelligence Special Report

This Regulatory Intelligence investigation looks into China's efforts to use private sector "bounty hunters" in bid to track down illicit assets being parked in Australian real estate

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SPECIAL REPORT: ANTI-MONEY LAUNDERING

The bounty and the hunt: Tensions flare amid Chinese-Australian capital flight, laundering

By Nathan Lynch, Thomson Reuters

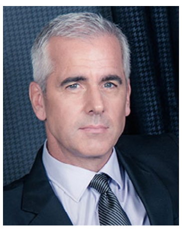
Chinese law enforcement agencies have resorted to the use of private sector "bounty hunters" to track down assets in Australia that are linked to Mainland corruption, as diplomatic tensions flare over money laundering and capital flight. Australia is growing increasingly concerned about the use of civil asset recovery agents, or private "bounty hunters", to bypass official channels for mutual legal assistance in these matters.

Beijing, meanwhile, perceives Australia as offering a safe haven for kleptocrats and other financial criminals, including those who have absconded with the proceeds of Mainland investment fraud. Chinese officials are frustrated with Australia's failure to crack down on the laundering of funds through real estate, lawyers and accountants, according to Bill Majcher, a civil asset recovery expert who works closely with the Chinese Ministry of Public Security.

A documentary on ABC's flagship current affairs show Four Corners will show the "thin line" these asset recovery agents walk under Australian law. It will also demonstrate the vulnerability of Australian real estate for money laundering, with suspected proceeds of crime being moved via companies with nominee directors to be parked in property investments.

The documentary explores cases involving Queensland real estate agents, accountants and law firms, which have been arranging complex deals on behalf of high-profile Chinese nationals. On the other side of the ledger, it also explores the activities of contractors who are tracking down these assets on behalf of Mainland authorities.

Chinese organised criminals, money launderers and legitimate investors view Australia, New Zealand and Canada as property "safe havens". This perception is fuelled by the countries' stable economies, lax anti-money laundering (AML) oversight for real estate purchases, strong rule of law and tough extradition requirements. It is difficult for gatekeeper professions, which do not have AML/CTF obligations, to differentiate between legitimate and illicit funds that flow through their business accounts.



Bill Majcher, a civil asset recovery expert with EMIDR in Hong Kong

"Gun for fire"

Majcher, who has spent his career working as a police and private sector anti-money laundering operative, said interest in commercial recovery services had surged under operations Sky Net and Fox Hunt. Chinese government agencies had grown impatient with the glacial pace of Western criminal law enforcement, Majcher said.

They were trying to accelerate that process by using lawful civil recoveries to obtain criminal assets, as well as targeting legitimate assets that have been moved out of the country in breach of capital controls.

"The Ministry of Public Security (MPS) definitely appears frustrated. From my perspective, the legal system in the West is rooted in the principle that an accused is innocent until proven broke. I have shared that viewpoint with some individuals in the MPS and received no disagreement," he said.

Some of the people China is pursuing in Australia were employees of state-owned enterprises with annual incomes of around A$30,000 who have amassed fortunes of up to A$500 million during their careers, Majcher said.

"I've advocated to the Chinese that in many cases, civil asset recovery litigation is the most efficient way to proceed as the criminal justice system is heavily slanted in favor of lawyers and criminals regardless of their origin."

Civil asset recovery operations have their critics, however. Some bounty hunters have been accused of using heavy-handed tactics to intimidate Chinese nationals or dual-citizens living in Australia. People have also received "knocks on the door" from bounty hunters claiming to be acting on behalf of the Chinese MPS.

Asset recovery agents were operating in a "very grey area", said Neil Jeans, an AML expert based in Melbourne.

"I think their activities would be viewed very dimly by Australian authorities, " Jeans said.

End-to-end laundering pipeline

Australia, Canada and New Zealand are among the favoured jurisdictions for criminals and corrupt politicians who want to invest in property overseas. Majcher, a former organised crime investigator for the Canadian government, said there were pockets in Australia where money laundering through real estate had reached "systemic and epidemic proportions".

"An elaborate 'cottage industry' for laundering has taken root in Australia. This has blinded many Australian gatekeepers — to the point where they've lost sight of their professional responsibilities," he said.

Australia has been a known target destination for the proceeds of Mainland Chinese corruption for many years. The problem has worsened significantly in recent years, Jeans said.

The existence of strict Chinese capital controls has also made the task of Australian AML/CTF teams and law enforcement agents harder when dealing with fund flows from places such as Hong Kong and Macau. China limits outflows of yuan to US$50,000 per citizen each year. As a result, people are using money laundering techniques to spirit lawfully obtained assets into Australia.

Evasion of Chinese capital controls is not a predicate offence under Australia's money laundering laws.

"It's very hard for Australian authorities to differentiate between what we view as a legal movement of funds and money laundering. The challenge is finding out the source of funds in China, which can take up a lot of time and law enforcement resources," Jeans said.

Chinese banks with Hong Kong branches often use back-to-back loans to allow Chinese nationals to invest in real estate abroad despite the Mainland capital controls. These cross-border loans allow Mainland investors to take out a yuan-denominated facility to buy assets overseas. The sheer volume of these money flows makes it very difficult for Australian authorities and banks to identify bad actors.

"Collateralised loans are made by Aussie lenders to Chinese customers. They show up in Australia without any jobs or declared income, but they can show blocked funds of unknown ownership or origin sitting in a bank in China. The Australian bank accepts the Chinese funds as collateral to secure loans to buy property in Oz," Majcher said.

Casinos, travel junket operators, high-value goods dealers, remittance agents, education providers and trade-based finance are all popular with Mainland money movers. Traditional banks are also playing a key role by inadvertently facilitating trade-based money laundering (TBML).

"You need a comprehensive AML/CTF regime to equip and obligate these gatekeeper professions to detect, deter and disrupt serious financial crime," Jeans said.

Fox back in the hole?

Despite the tsunami of hot Chinese money entering Australia, operations Fox Hunt and Sky Net have gone "very quiet" in recent months, sources said. Civil recovery agents are understood to be getting fewer mandates in a challenging geopolitical environment.

Diplomatic tensions surrounding the arrest in Canada in December of Meng Wanzhou, chief financial officer of Chinese telecoms giant Huawei, have added another layer of complexity to Beijing's efforts to repatriate funds. China has also arrested a number of Canadian nationals on espionage charges but denies these are linked to the Huawei case.

At the same time, the Australian Federal Police (AFP) have become more visible in their efforts to seize assets linked to Chinese criminal activity. Late last year the Criminal Assets Confiscation Taskforce seized more than A$15 million in real estate, jewellery, wine and assets that are suspected to have been bought with the proceeds of crimes perpetrated in China, including investment fraud.

The crackdown is the result of a two-year investigation partnership between the AFP and the Chinese MPS. The AFP has insisted it is working closely and collaboratively with the Chinese government through official mutual assistance channels.

"This operation further highlights the AFP's relationship with the MPS and ongoing close collaboration under the Joint Agency Arrangement on economic crime cooperation," the Federal Police said in a statement.

Assistant Commissioner Bruce Hill, the AFP's head of organised crime, said there was a need for strong enforcement and international collaboration to tackle cross-border money laundering.

"This kind of activity, where significant criminal proceeds are moved into Australian assets, can erode the level playing field for Australian homebuyers and small business owners," he said.

The Australian Criminal Intelligence Commission estimates organised crime costs A$36 billion each year. Professional facilitators were increasingly being used to launder the proceeds of crime, it said in a declassified report last year.

Of needles and haystacks

The identification of illicit funds flows within the vast majority of legitimate transactions is extremely challenging, for both banks and law enforcement agents. The cross-border nature of modern organised crime aims to exploit this complexity.

"Cross-border investigations are time consuming and require significant cooperation between agencies. This is compounded by the fact that many of the gatekeeper professions sit outside the purview of Australian financial intelligence agents," Jeans said.

The challenges are compounded when there are vastly different legal systems in countries that need to cooperate on investigations. Issues of trust, privacy and judicial fairness can often hamper major international AML operations.

"This can make cooperation problematic, particularly when a crime in one country is not recognised in the other or there are different standards of evidence required for agencies dealing with the request to lawfully act in their country," Majcher said.

Despite these challenges, Majcher said if Australia failed to deal with this problem it would undermine confidence in the economy and possibly even the legal system.

"This tsunami of unexplained wealth has had a corrosive effect on the average law-abiding Australian, who is playing by the rules and yet falling further behind," he said.

Project Dragon, reported by Mark Willacy, airs on Monday 18 February at 8.30pm on ABC Four Corners.

Chinese laundering allegations put pressure on Australia to close AML loophles

By Nathan Lynch, Thomson Reuters

The revelations about Chinese asset recovery agents operating covertly in Australia will put pressure on the Department of Home Affairs to introduce law reforms ahead of the May general election. The government is sitting on "Phase 1.5" legislation that will prepare Australia for the introduction of the long-awaited Tranche 2 AML/CTF laws.

This transitional legislation is understood to have been shelved late last year amid a gridlocked federal parliament.

The federal government will be under pressure to be seen to act, however, before the arrival of the Financial Action Task Force (FATF) for an assessment visit later this year. The international standard setter will want to see evidence Australia has acted upon the weaknesses set out in its 2015 mutual evaluation report. Chief among these was the failure to regulate lawyers, accountants and real estate agents.

Late last year the AFP's Criminal Assets Confiscation Taskforce seized more than A$15 million in real estate, jewellery, wine and assets that are suspected to have been bought with the proceeds of crimes perpetrated in China, including investment fraud.

AML practitioners said it was unsurprising that the assets in the AFP's recent seizures all sit outside the Australian AML regime. The seizures demonstrated the importance of extending the country's AML regime to include "tranche two" entities, they said.

Neil Jeans, an AML consultant with Initialism, said the role of designated non-financial businesses and professions (DNFBPs) in complex money laundering schemes had been well understood and accepted in Australia for two decades.

"The regulation and supervision of DNFBPs is a fundamental requirement of the FATF, which sets the international standards for AML/CTF," he said.

"Australia, despite warnings from the FATF and government reports highlighting the failure to bring lawyers, accountants and real estate agents into the AML/CTF regime, has been slow to act. This represents a significant hole in Australia's AML/CTF regime, which we know domestic and international criminals are exploiting."

On the drawing board … still

The Tranche 2 laws have been on the drawing board in Australia for more than 12 years, despite having bipartisan support. The federal government had committed to pass laws to capture DNFBPs by 2018, following the critical report from the FATF in 2015. Australia had fallen well behind in its international obligations to protect the country's economy from criminal abuse, the report said.

The "phase 1.5" stepping-stone legislation has been drafted jointly by the Department of Home Affairs, the Attorney-General's Department (AGD) and with input from the Australian Transaction Reports and Analysis Centre (AUSTRAC).

A Home Affairs spokesman said there was no fixed timetable for the Phase 1.5 laws, which will be tabled "subject to the parliamentary schedule".

The next stage will be to work on "the process of simplifying and streamlining Australia's AML/CTF regime and to improve compliance with the international standards set by the FATF."

"The government is considering options to extend AML/CTF regulation to 'tranche 2' entities, such as lawyers, accountants and real estate agents," the spokesman said.

Tranche warfare

This reform would be crucial for Australia to have any hope of turning back the tide of dirty money, said Bill Majcher, an AML expert and former undercover agent based in Hong Kong.

"Lawyers, realtors, and immigration agents are, in my view, the most engaged parties facilitating these dirty money channels," he said.

Drug manufacturers operating out of Southern China have been targeting Australia with lab-produced drugs, such as methamphetamine and precursor chemicals. After selling their product on the black market in Australia they have what's known colloquially as a "cash problem". They need to find a way to place and conceal those funds in the financial system.

The drug syndicates in China have exploited the fact that there are many people in China who want to get their money out of the country. Money laundering facilitators will take these illicit funds, place them in the financial system, then use them to buy hard assets, including real estate.

Often these purchases are made in the name of offshore companies. The underlying shares can be transferred to new owners without needing to alter the title to the property.

All of the key players in these transactions are outside the AML regime. The Tranche 2 legislation, when passed, will capture the lawyers, real estate agents, accountants and trust and company service providers who facilitate this illegal activity.

"The real estate purchasers in China are paying the laundering syndicates with yuan. They may not even be aware that the house they're buying was originally purchased with the cash generated from drug sales in Australia by Chinese-linked drug dealers," Majcher explained.

"Typically, some offshore corporate entity owns the real estate assets. So the shares in the company change hands but, on the property title, the corporate owner stays the same."

China’s global hunt for ‘big crocs’ flounders amid geopolitical tensions

By Nathan Lynch, Thomson Reuters

China’s high-profile global crackdown on corrupt oligarchs, or “big crocs”, has begun to flounder as geopolitical tensions rise between the Mainland and the West. Sources said cooperation between Chinese and Western governments had become especially difficult following the arrest of Meng Wanzhou, chief financial officer of Chinese telecoms giant Huawei, in Canada in December.

China has retaliated by arresting a number of Canadian nationals on espionage charges, although it denies officially that these are linked to the Huawei case.

Bill Majcher, a civil recovery expert who hunts down assets for governments and large organisations, said the frosty geopolitical climate was clearly hampering initiatives such as Sky Net and Fox Hunt.

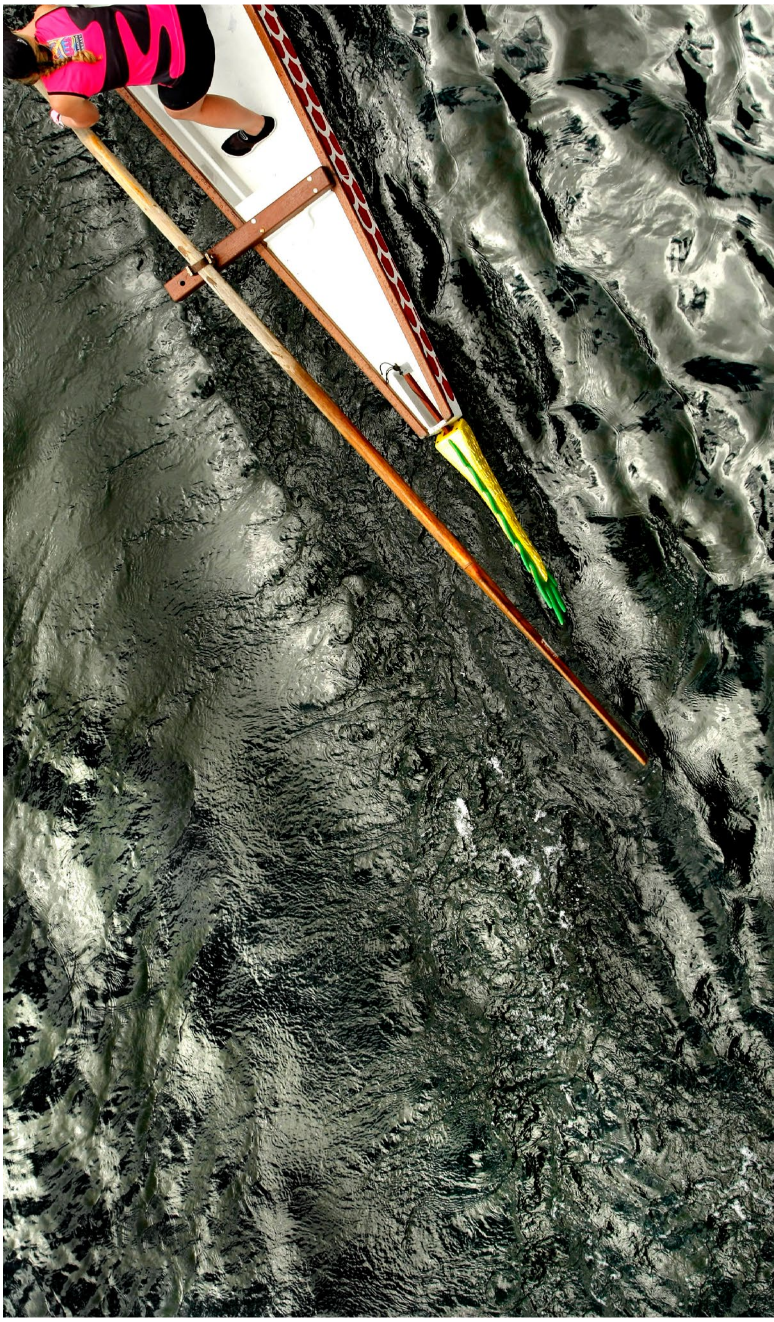
“Fox Hunt and Sky Net, in my estimation, have not been as successful as the Chinese would like. As big as China is, it still only has finite resources at its disposal with the ability to interface with the outside world,” Majcher said.

“The ascendancy of President Xi has caused some security ripples in China. This has been compounded by the US-China trade war, One Belt One Road growing pains, and the growing containment of global Chinese technology firms competing for 5G globally. All of this has taken some of the focus off Fox Hunt and Sky Net.”

Despite these challenges, and the diplomatic distractions facing Beijing, wealthy Chinese nationals living abroad are being very careful in the current environment. The fallout has also had an impact upon legitimate business people who have made fortunes in China and then left to live abroad.

Some expats are using international law firms to manage everything from their financial assets to their travel itineraries in the present climate. A source said some of China’s early tech tycoons, who had since moved abroad, were being particularly careful to avoid travel to a destination where China may be able to force an extradition. Even Hong Kong is off limits to some, at present.

“These people haven’t done anything wrong. They’ve just fallen out of favour with Beijing, as they’re perceived to be too closely aligned to the West. The early tech tycoons in China, for instance — they were all linked to Silicon Valley,” a source said.



Sky is not falling

Over the longer term, Majcher is confident that President Xi Jinping will mend bridges with the West and continue to tighten the noose around corrupt officials. He said China's oligarchs have collectively embezzled billions from the country's coffers and private investors.

"I believe those who have plundered the wealth of China and its citizens should not confuse government distraction with capitulation," he said.

Beijing has had some major successes in repatriating stolen funds through Sky Net. In July last year the country's anti-corruption agency secured $485 million from the U.S., in the proceeds from a major corruption and bank fraud case.

The recovery involved assets stolen by Xu Chaofan, the president of Bank of China's sub-branch in Kaiping, in the southern province of Guangdong.

Xu fled to the United States in 2001. He was detained in 2003 following a cooperative effort between the law enforcement officials in both countries. He was convicted in the U.S. and sentenced to a 25-year prison term in 2009. Xu has since been repatriated to China, following pressure applied on him by U.S. and Chinese authorities.

China has ramped up pressure on corrupt officials, which the country's media refers to as "big crocs". It is known to use agents in foreign countries as well as pressure on relatives on the Mainland, in addition to securing cooperation from foreign law enforcement agencies. In some cases, China has released personal details of its targets publicly, including their foreign addresses.

China says it has had limited success in securing cooperation from Western countries such as Australia, Canada and the United States, where many of the most wanted individuals have taken up residence. Western governments, meanwhile, have complained about a lack of transparency and due process in China's judicial system.

Additional reporting by Lusha Zhang and Se Young Lee, Reuters, in Beijing.

CASE STUDY: LAUNDERING TRADECRAFT

China: Trade-based money laundering

Money laundering is a global operation and each criminal or group may launder their money slightly differently. For cases in which the Chinese financial system is used, dirty money is often passed through multiple accounts around the world, either through an exchange or through a criminal's accounts, and ultimately ends up in a Chinese account. From there, the funds are sometimes used to purchase goods. These goods may be sold in China at inflated prices and the invoices used to legitimize the funds, which are then transferred to the launderer's account outside of China. In other cases, the purchased goods are shipped to the country or region of the launderers, often with inaccurate shipping invoices to lower fees. Upon arrival, an importer sells the goods to legitimize the funds.

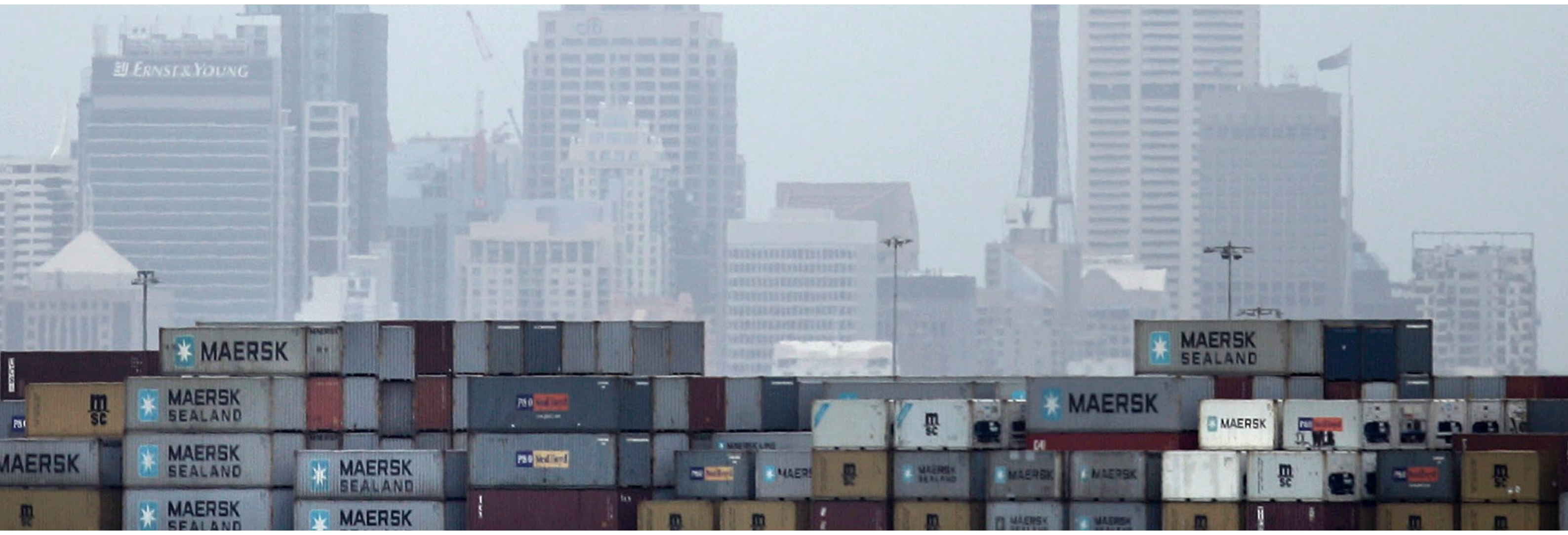
Trade-based money laundering (TBML) is also commonly used by launderers operating through the Chinese financial system. In many cases, dirty money is sent to accounts in China, often first crossing several borders via wire transfer companies, casinos or other accounts in small amounts before eventually being deposited into a mainland account.

At the same time, a company connected with the scheme in the United States or elsewhere offers money exchange and import/export services to legitimate companies seeking to import goods from China. Taking advantage of the competitive exchange rates offered, the lawful companies use the exchange company as a middle man.

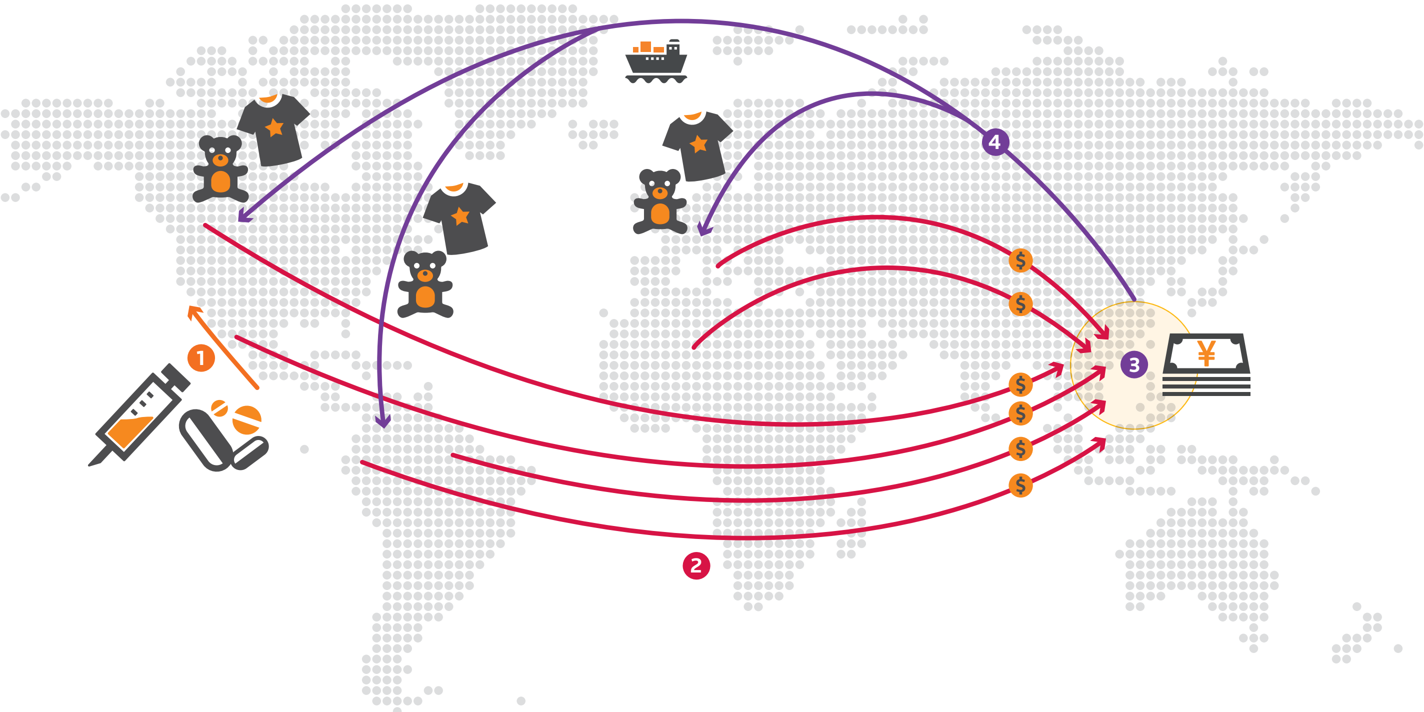
The illicit money in the Chinese bank – the origin of which is often unclear as a result of account layering – is used in mainland China to purchase goods, such as toys or clothing, to send to the importer. The "clean" cash paid to the exchange company by the importer is then paid to the criminal group behind the money laundering scheme.

A case in point involved three Colombians based in Guangzhou, who used TBML through China to launder over US$5 billion for Spanish and Mexican drug smugglers.[1] The Guangzhou Enterprise passed the dirty money through bank accounts in Hong Kong and China to fund purchases of counterfeit goods in China, which were then shipped to Colombia (and elsewhere) and sold.[2]

This case highlights an important issue, namely that foreigners opening bank accounts and businesses in China can create weak points that can be exploited by criminals. While a select few banks have access to extensive global risk information, many Chinese banks are only accessing local or country-level data. Thus, previously convicted criminals or suspects may still be able to open accounts in China and participate in TBML and other illicit activities.



1. http://readingeagle.com/ap/article/ap-investigation-china-launders-cash-of-foreign-criminals
2. https://justice.gov/usao-edny/pr/three-members-international-organization-money-launderers-largest-drug-cartels-arrested



1. Drugs from Latin America and the Caribbean are trafficked to the United States and sold.

2. Proceeds from these transactions are passed through multiple accounts around the world before being sent to Hong Kong and finally, China.

3. The funds are often withdrawn in cash by exporters and used to purchase goods such as clothes and toys.

4. Goods are sent to Latin America or the United States and are sold. The now-legitimate profits are used to pay for the trafficked narcotics.

About the Author

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Nathan Lynch is an experienced writer, public speaker and policy analyst in the fields of Financial Crime Intelligence, Anti-Money Laundering, Counter-Terrorism Financing and Regulatory Risk. At Thomson Reuters Regulatory Intelligence he takes a thought leadership role in relation to emerging threats, typologies, solutions and commercial opportunities in the financial crime and risk field.

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