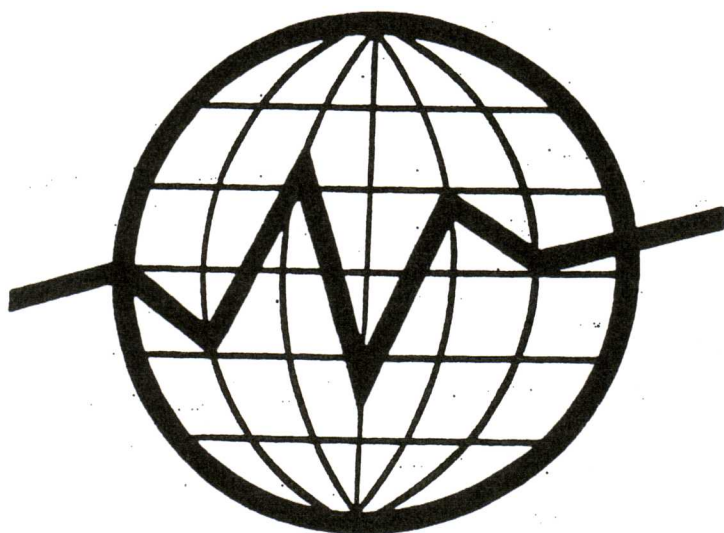


# **REPORT ON MONEY LAUNDERING**



**INTERNATIONAL ORGANIZATION OF SECURITIES COMMISSIONS**

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| <p style="text-align: center;"><b>COMPOSITION OF I.O.S.C.O.</b></p> <p style="text-align: center;"><b>WORKING PARTY N° 4</b></p> |
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## INTRODUCTION

There is a growing international consensus that money laundering<sup>1</sup>, which has a direct relationship to serious crimes, must be treated as a regulatory and enforcement priority. Regulators responsible for various sectors of the economy that could be abused by money launderers are examining their sectors of responsibility, and developing and implementing appropriate measures to detect and combat money laundering. IOSCO and its members are participating in the examination of the securities and futures markets, and are committed to fighting the use of these markets in money laundering schemes. To that end, the IOSCO Technical Committee gave Working Party No. 4 a mandate to prepare a report that could assist all IOSCO members in taking the measures they consider appropriate to combat money laundering<sup>2</sup>.

The present report consists of two parts.

The first part deals with the IOSCO project, including :

- A. Background ;
- B. Observations about the securities and futures markets in the context of money laundering enforcement ;
- C. Goals and achievements of the project.

The second part discusses issues raised by the FATF 40 recommendations that should be considered in combatting money laundering in the securities and futures markets, as follows :

- A. Customer identification ;
- B. Record keeping and the ability to reconstruct transactions ;
- C. Detecting and reporting suspicious transactions ;
- D. Preventing control of securities and futures firms by criminals ;
- E. Monitoring/developing programs for firms to guard against money laundering ;
- F. Use of cash in securities and futures transactions ;
- G. Forms of cooperation.

The conclusion summarizes the main results of the study and makes proposals.

<sup>1</sup> Extensive discussions have been held at the international level concerning the definition of money laundering. For purposes of this Report, IOSCO Working Party No. 4 has adopted the definition of money laundering as set forth in the United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances (the "Vienna Convention"). In the Vienna Convention, money laundering activities are defined as the activities linked with the conversion or transfer of property ; or the concealment of the disguise of the true nature of property, knowing that this property is derived from drug trafficking. The scope of the definition of money laundering, however, ultimately is a matter to be determined by the national authorities of each country, in conformity with their international commitments.

<sup>2</sup> The Working Party's members include : the Australian Securities Commission ; the Ontario Securities Commission, and the Commission des Valeurs Mobilières du Québec of Canada ; the Commission des Opérations de Bourse of France ; the Ministry of Finance of Germany ; the Securities and Futures Commission of Hong Kong ; the Commissione Nazionale per la Società e la Borsa of Italy ; the Securities Bureau of Ministry of Finance of Japan ; the Stichting Toezicht Effectenverkeer of the Netherlands ; the Comisión Nacional del Mercado de Valores of Spain ; the Swiss Bankers Association, and the Federal Department for Foreign Affairs of Switzerland ; the Department of Trade and Industry and the Securities and Investments Board of the United Kingdom ; the Securities and Exchange Commission, and the Commodity Futures Trading Commission of the United States of America.



## I. The IOSCO PROJECT

### A. BACKGROUND OF THE IOSCO PROJECT

IOSCO is the only global association of organizations responsible for regulating the securities and futures markets. As such, it brings a unique perspective to the examination of the principal issues involved in combatting money laundering in the markets its members regulate. In addition, IOSCO provides an important international forum for communication among securities and futures regulators, as well as members of the securities and futures industries, concerning developments in the fight against money laundering. Therefore, IOSCO is well-situated to advance international efforts in this area by evaluating the markets its members regulate in the context of money laundering.

While eager to contribute its singular perspective and platform to the global effort to fight money laundering, IOSCO Working Party No. 4 recognizes and supports the important work done by other groups on this topic, and has endeavored to build upon, rather than duplicate, the efforts of those groups. In particular, the Working Party has looked to the United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances ("Vienna Convention"); the 40 recommendations propounded by the Financial Action Task Force ("FATF")<sup>3</sup>; the European Directive on Prevention of the Use of the Financial System for the Purpose of Money Laundering ("EC Directive"); and the Banking Supervisory Authorities of the Group of Ten Basle Declaration of December 1988 as important building blocks for this project.

IOSCO further recognizes that the states of many of its members (including all the members of the Technical Committee) have, through FATF, made national commitments in the area of money laundering<sup>4</sup>. In addition, some members are subject to additional commitments made through the Vienna Convention and the EC Directives as well as under domestic legislation. Accordingly, this report, and the other initiatives of the Working Party to strengthen the international efforts against money laundering, do not in any way suggest that regulators agree to take measures in connection with money laundering that would be inconsistent with their national commitments.

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<sup>3</sup> The FATF report containing the 40 recommendations is attached at Appendix A.

<sup>4</sup> As of May 1992, FATF has 28 members: Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greece, the Gulf Cooperation Council, Hong Kong, Iceland, Ireland, Italy, Japan, Luxembourg, the Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, Turkey, the United Kingdom, the United States, and the Commission of the European Communities.



## B. OBSERVATIONS ABOUT THE SECURITIES AND FUTURES MARKETS IN THE CONTEXT OF MONEY LAUNDERING ENFORCEMENT

In the course of this project, many members of the Working Party consulted with the national authorities responsible for the investigation and prosecution of money laundering offenses in their respective jurisdictions, in order to determine the extent to which money laundering problems had been observed in the securities and futures markets<sup>5</sup>. The consultations revealed few publicly reported instances of money laundering in these markets.

This scarcity may result from the fact that in many jurisdictions, securities and futures brokers that are authorized to receive and hold customer funds do not, in most cases, accept such funds in the form of cash. For this reason, the securities and futures markets may not lend themselves well to the "placement" phase of money laundering<sup>6</sup>. The volume and liquidity of international securities and futures trading coupled with the increasing complexity of transactions, may render use of the securities and futures markets more attractive at the "layering" and "integration" stages of a money laundering scheme, where it may be more difficult to detect. Therefore, it is unclear whether the absence of a significant number of publicly identified instances of money laundering in the securities and futures markets indicates that it is not occurring in these markets, or reflects the difficulties involved in detecting such activity. In any event, as other financial sectors increase their defenses against money laundering, it will be important to ensure that securities and futures markets do not become a comparatively more attractive alternative for money launderers.

The members of the Working Party also reviewed existing domestic laws and regulations regarding securities and futures transactions that might be relevant in the fight against money laundering. The review indicated that the domestic securities and futures regulatory systems of the Working Party member countries already incorporate elements critical to the detection and prosecution of money laundering. For example, record keeping and the subsequent ability to reconstruct transactions are central features of many securities and futures regulatory systems. Existing regulations in many countries also stress background checks on persons who seek to control brokerage firms. Hence, these systems should facilitate investigations of money laundering practices in the securities and futures markets, and hinder criminals who may seek to use the markets to conceal the true source or ownership of assets.

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<sup>5</sup> As a general matter, IOSCO members are not vested with the authority to prosecute cases of money laundering *per se*. However, as discussed in more detail at section II.C, below, conduct that may violate a country's securities and futures laws (over which a securities or futures regulator generally would have jurisdiction) also may violate its money laundering laws. In addition, certain patterns of transactions in the securities and futures markets that may not violate the securities and futures laws nonetheless may be indicative of money laundering.

<sup>6</sup> In general, money laundering activity may be divided into three stages: 1) placement, which involves the physical placement of cash or other highly liquid instruments derived from illegal activities; 2) layering, which involves disguising and concealing the proceeds of illegal activities, often by creating layers of financial transactions; and 3) integration, during which the proceeds of illegal activities are integrated back into the economy.

### C. GOALS AND ACHIEVEMENTS OF THE IOSCO PROJECT

A principal objective of this project has been to enhance channels for communication about the problem of money laundering in the context of securities and futures markets. In addition to the discussion of this problem among members of the Working Party, IOSCO members already have begun dialogues with their domestic national money laundering authorities. The Working Party also views this project as an opportunity to disseminate the concerns and approaches to combatting money laundering identified by the FATF to IOSCO members from countries that do not belong to the FATF (currently 35 countries). The Working Party believes the further dissemination of the FATF's work is particularly important given the need (as emphasized by the FATF recommendations) to deter and prosecute money launderers effectively through the creation of a net of cooperating authorities across national boundaries. The wider that net is cast, the more difficult it will be for money launderers to avoid it.

Another central theme of this project has been the identification of issues that should be considered by securities and futures regulators and regulatees in applying the FATF recommendations, which, although applicable to the securities and futures markets, appear to have been developed primarily with deposit-taking institutions in mind. Because of the distinct regulatory concerns applicable to the securities and futures markets, IOSCO Working Party No. 4 can play an important role in providing a forum for discussion, analysis and interpretation of the FATF recommendations in the context of these essential financial markets.

IOSCO also has begun to work with other international organizations, such as the FATF, to address how the securities and futures markets fit into money laundering enforcement programs. In this regard, the Working Party has offered its assistance and expertise to the chairman of the FATF Working Group on Financial Matters. In February 1992, the chairman of the Working Party attended a meeting of that FATF Working Group as an observer and was given an opportunity to explain the IOSCO project and to discuss some of the distinctive features of the securities and futures markets. Several other representatives of members of the Working Party also participated in the meeting.

IOSCO looks forward to continuing to promote communication and cooperation, not only among securities and futures regulators, but also among domestic authorities and between international organizations, to protect the integrity of the securities and futures markets against those who would seek to use those markets for money laundering purposes.



## II. ISSUES RAISED BY THE FATF 40 RECOMMENDATIONS THAT SHOULD BE CONSIDERED IN COMBATTING MONEY LAUNDERING IN THE SECURITIES AND FUTURES MARKETS

In considering how best to deter, detect and prosecute money launderers, it is essential to recognize the complexity of the modern, global financial system, including how unique characteristics of each of the various sectors that comprise that system may lend themselves to combatting money laundering. The Working Party has looked to the FATF as a primary source for identifying issues that should be considered in this area. In doing so, a principal goal is to lend support to the FATF's efforts.

The FATF recommendations were designed to create an increasingly fine net across the various sectors of the global financial system to prevent money laundering. In these circumstances, it is important to recognize that different types of financial institutions in the system may play different roles in weaving the net. Indeed, optimal results should be achieved through the implementation of actions in the various sectors of the financial system that complement actions taken elsewhere in the system.

For example, bearing in mind that most of the transactions in the securities and futures markets are settled through checks drawn on or wire transfers from bank accounts, the application of the FATF recommendations by banking institutions should benefit the securities and futures markets by making it more difficult, as a general matter, for money launderers to access the legitimate financial system, and, thereafter, the securities and futures markets.

As with every financial sector, when devising means to combat potential money laundering activities in the securities and futures markets it is important that unnecessary burdens are not placed on legitimate business activities. Striking the optimal balance between the need to deter the operations of money launderers and the need not to inhibit legitimate market activity in these essential sectors requires a detailed knowledge and examination of the operations of securities and futures markets professionals and participants, and of the abusive practices that money launderers may have at their disposal.

Based on the work of the FATF, the Working Party has identified the following central issues that should be considered in developing tools for combatting the use of the securities and futures markets for money laundering: Customer Identification; Record Keeping and the Ability to Reconstruct Transactions; Detecting and Reporting Suspicious Transactions; Preventing Control of Securities and Futures Firms by Criminals; Development of Programs for Intermediaries to Guard Against Money Laundering; Use of Cash in Securities and Futures Transactions; and Cooperation and Coordination Among Domestic and International Authorities<sup>7</sup>. These issues, which draw upon the principal themes in the FATF recommendations, are discussed below<sup>8</sup>.

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<sup>7</sup> The FATF recommendations are organized around four central themes: General Framework of the Recommendations; Improvement of National Legal Systems to Combat Money Laundering; Enhancement of the Role of the Financial System; and Strengthening of International Cooperation. This report deals predominately with the recommendations dealing with Enhancement of the Role of the Financial System, because those recommendations have the most direct ramifications for securities and futures regulators and their regulatees.

<sup>8</sup> Where an issue discussed herein corresponds to one or more FATF recommendations, the FATF recommendations are identified in parentheses at the beginning of each section.



## A. CUSTOMER IDENTIFICATION (12, 13)

The ability to identify customers is crucial to detecting, prosecuting and deterring money launderers. For this reason, the FATF recommendations contemplate that financial institutions will not maintain anonymous accounts, or accounts in names that clearly appear fictitious. Instead, financial institutions would be obligated to identify their account holders by "an official or other reliable identifying document." (Recommendation 12). Moreover, under the recommendations, financial institutions are advised to take "reasonable measures" to ascertain the true identities of account owners when there is any doubt whether the persons who opened the account are the true account owners (Recommendation 13).

In most countries represented by Working Party members, securities and futures brokers must maintain customer identifying information pursuant to national law, securities and futures regulations and/or self-regulatory organization rules. Securities and futures transactions, however, often involve a chain of multiple intermediaries, some of whom may be from different countries. In general, only the immediate client of a securities or futures firm need be considered a "customer" for the purposes of existing customer identification requirements. For example, a financial institution may maintain an omnibus account in the name of a foreign financial institution, and normally would not know the identity of the foreign financial institution's customers. In such a case, the foreign financial institution would be the "customer" as to whom identifying information would be maintained. The foreign financial institution, in countries that have implemented the FATF recommendations, would, in turn, maintain customer identifying information about its clients, i.e., the ultimate beneficial owners of its transactions. Thus, through sharing information among enforcement authorities, customer identifying information could be obtained in an expeditious fashion concerning each link in the chain.

The ability to trace the identity of the ultimate customer should improve as more countries implement the FATF recommendations, since, as long as the information is required at the beginning of the chain, it should be possible to follow the links back to the identifying information. This process, however, can be frustrated when the chain includes countries that have not implemented customer identification requirements and procedures to facilitate sharing customer identifying information.

## B. RECORD KEEPING AND THE ABILITY TO RECONSTRUCT TRANSACTIONS (12-15)

The ability to reconstruct financial transactions is essential to effective detection and prosecution of money launderers, as recognized in the FATF recommendations. For securities and futures markets, this means that firms handling customer funds should: 1) keep records sufficient to verify the movements of such funds in connection with transactions in the securities and futures markets and through accounts related to such transactions; 2) and be able to document fully all aspects of securities and futures markets transactions. Recognizing that investigating and prosecuting financial crimes can be a complex and time-consuming matter, the FATF also recommends that financial institutions maintain the relevant records for a period of five years. Both recommendations are consistent with the regulatory requirements placed on securities and futures firms to ensure compliance with the applicable securities and futures laws and regulations.

Most of the members of the Working Party note that the statutory and regulatory or self-regulatory requirements for their securities and futures firms meet, and in some cases exceed, the requirements recommended by the FATF with regard to record creation and retention. In addition, many members of the Working Party note that such records are required to be provided upon request to the relevant securities or futures supervisory authority.

The similarities between the record creation and retention requirements imposed by securities and futures regulators and self-regulatory organizations ("SROs") and those recommended by the FATF, evidence international consensus on the importance of such requirements in order to investigate and prosecute crimes involving financial transactions.



### C. DETECTING AND REPORTING SUSPICIOUS TRANSACTIONS (15-19)

The cooperation of financial institutions with the appropriate authorities is viewed as an important element in the detection and prosecution of money laundering. For example, the FATF recommendations call for heightened vigilance on the part of financial institutions with respect to "all complex, unusual large transactions" (Recommendation 15). The FATF also recommends that institutions be permitted or required to report to the authorities charged with some or all aspects of detecting, deterring and prosecuting money laundering offenses ("competent authorities"), any suspicions that funds moving through their accounts "stem from a criminal activity" (Recommendation 16).

The monitoring of large or unusual transactions in the securities and futures markets, as indicators of money laundering activity, may be complicated by the complex trading strategies and transactions involving large sums of money that occur frequently in those markets. Moreover, aspects of transactions that appear "unusual" in one financial sector may not be unusual in another, i.e., the transaction may appear unusual to bankers but may be a routine transaction in the securities or futures markets. Further, transactions in one market may no longer appear unusual when considered in conjunction with transactions undertaken in another market.

The challenge for securities and futures firms is to identify types of transactions or patterns of activities that may be, for those markets, indicative of money laundering<sup>9</sup>. Such transactions might include the following :

- The use by a customer of a securities or futures brokerage firm as a place to hold funds that are not being used to trade in securities or futures.
- A customer who deals with a securities or futures broker only in cash or cash equivalents rather than through banking channels.

Money laundering in the securities and futures markets at the layering or integration stages might more likely be detected in circumstances where the suspect transactions also involve possible violations of securities and futures statutes or regulations. For example :

- The entry of matching buys and sells in particular securities or futures contracts ("wash trading"), creating the illusion of trading. Such wash trading does not result in a bona fide market position, and might provide "cover" for a money launderer<sup>10</sup>.
- Wash trading through multiple accounts might be used to transfer funds between accounts by generating offsetting losses and profits in different accounts. Transfers of positions between accounts that do not appear to be commonly controlled also could be a warning sign.

As noted above, one element of the FATF's proposal for involving financial institutions in efforts to combat money-laundering, is to have the institutions report suspicious transactions to the appropriate authorities. In addition to the issue of whether such reporting should be permissive or mandatory, the FATF also raises the issue of how to handle the potential liability of a financial institution which makes such a report (recommendation 16). Approaches to this issue vary, including jurisdictions where financial institutions are required to transmit such information but are provided with legislative protection from lawsuits for breach of confidentiality or from good faith reporting that turns out to be erroneous, and jurisdictions where no protection from liability is provided. The issues of mandatory reporting and protection from ensuing liability raise similar policy questions with respect to all regulated financial institutions, not just securities and futures firms, and therefore may be best addressed on a national basis by each country.

<sup>9</sup> Sources of case studies and hypotheses involving money laundering in the securities and futures markets are listed in Appendix B.

<sup>10</sup> Note, however, that although numerous "wash trading" cases have been brought in the securities and futures area, the laundering of proceeds from other illegal activities has not been shown to be involved in those cases.



#### **D. PREVENTING CONTROL OF SECURITIES AND FUTURES FIRMS BY CRIMINALS (29)**

As recognized in FATF Recommendation 29, it is critical to ensure that money launderers do not infiltrate or gain control of financial institutions for their own ends. Many of the Working Party members indicated that background checks of firms and principals of firms seeking registration or authorization as securities or futures brokers are already routinely performed. These checks may include vetting of applicants' names and other identifying information with criminal investigative authorities, review of any relevant disciplinary history, and requirements that applicants disclose any relevant sanctions or convictions in their past.

Some members have expanded their background checks to include vetting of names with foreign regulatory and criminal authorities. Securities and futures regulators frequently exchange public and non-public information, both informally and pursuant to information-sharing agreements, concerning the disciplinary history of applicants for registration in their respective countries. Such exchanges of information are useful in detecting and preventing the control of brokerage firms by criminals. In addition, all of the Working Party members expressed interest in working with other domestic authorities to find the appropriate way to ensure that past disciplinary information is available for background checks on persons who seek to own or control securities and futures firms.

#### **E. MONITORING/DEVELOPING PROGRAMS FOR FIRMS TO GUARD AGAINST MONEY LAUNDERING (20, 21, 22, 26, 28)**

FATF Recommendation 20 provides an overall model for the internal work of financial institutions in combatting money laundering. In particular, it recommends that financial institutions develop internal policies, procedures and controls, including designation of compliance officers at the management level, adequate screening procedures to ensure high standards when hiring employees, ongoing employee training programs, and audit functions to test the internal systems. Recommendations 21 and 22 specifically focus on the need for vigilance by financial institutions in dealing with organizations operating from non-FATF countries.

Many of the Working Party members have noted that extensive supervisory and audit procedures already are in place with respect to the operations of securities and futures firms. These include, among other things, comprehensive requirements imposed by the relevant securities and futures regulatory authorities as well as by the relevant SROs with regard to the receiving, handling and documenting of customer funds.

In addition, through internal discussions as well as contacts with the FATF Working Group on Financial Matters, members of the Working Party have been made aware of guidance notes for securities and futures firms concerning money laundering promulgated by regulatory and self-regulatory authorities in various countries. These guidance notes exemplify one approach to involving financial institutions in assisting the competent authorities in detecting, investigating and prosecuting money launderers (Recommendation 28). Nonetheless, the Working Party recognizes that implementation of the FATF recommendations concerning internal procedures and policies of financial firms for combatting money laundering is a matter to be addressed in accordance with the particular regulatory structures and policies of each country.



## F. USE OF CASH IN SECURITIES AND FUTURES TRANSACTIONS (25)

FATF recommendation 25 focuses upon the need to encourage the development of modern, secure techniques of money management to replace or limit the number of transactions in cash or cash equivalents.

As already mentioned, information provided by the members of the Working Party indicates that securities and futures businesses generally are not cash-intensive. While these practices make the placement of illegal funds in securities and futures firms for money laundering purposes less likely, members of the Working Party nonetheless note that their regulatory schemes generally impose documentary requirements that should be sufficient to reconstruct deposits of cash or cash equivalents by customers. These requirements can operate as a significant deterrent to the use of these markets for placement of funds for money laundering purposes.

The Working Party also considered the availability, in some countries, of bearer shares or debt instruments, which, if fully transportable, could operate as cash equivalents for purposes of money laundering. It was noted that bearer shares held in recognized depositories and properly recorded may be less susceptible to such abuses.

## G. FORMS OF COOPERATION (14, 28, 31, 32, 34, 36, 37, 38)

The importance of domestic and international cooperation in the field of money laundering has long been recognized by various organizations, including the FATF. At a domestic level, the FATF recommends documents should be made available to the domestic competent authorities in the context of relevant criminal prosecutions and investigations (Recommendation 14); at an international level, the recommendations provide for the development of international cooperation among competent authorities, with the elaboration of bilateral and multilateral agreements, and the use of compulsory measures in providing mutual legal assistance (Recommendations 36, 37, 38). Recommendation 31 indicates that international competent authorities should be responsible for gathering information about the latest developments in money laundering techniques and transmitting the information to the competent domestic authorities. Recommendation 32 encourages each country to make efforts to improve spontaneous or "upon request" international information exchanges relating to suspicious transactions, persons or corporations involved in those transactions between competent authorities.

The FATF recommendations on cooperation are addressed principally to authorities with direct national responsibility for investigating and prosecuting the crime of money laundering. Securities and futures regulators may be able to offer substantial assistance to the competent anti-money laundering authorities investigating conduct that also may violate securities and futures laws. For example, a money laundering investigation may intersect with a cross-border investigation of securities or futures law violations, in which information has been shared by two financial regulators. Access to that information may be granted to the competent anti-money laundering authority, in accordance with the terms on which the information was initially passed between the financial regulators. Indeed, many existing memoranda of understanding between securities and futures regulators contemplate and contain specific provisions that would govern such a transmission. Although not a substitute for formal criminal information sharing channels, such information nonetheless may be useful to competent authorities in their investigative efforts.

Even where no substantive securities or futures violations are indicated, but where transactions on the securities and futures markets are involved, national efforts against money laundering may be advanced by the involvement of securities and futures regulators. The regulators can offer their experience in detecting and investigating illegal activities in the securities and futures markets, their technical expertise on the functioning of those markets, and relevant public or non-public information from their files.



## CONCLUSION

The Technical Committee's mandate on money laundering has provided an opportunity for the members of the Working Party No. 4 to consider the problem of money laundering from the shared perspective of experts in the regulation of securities and futures markets. Informed by the important work of the Financial Action Task Force embodied in its 40 recommendations, as well as by the work of other international organizations, the Working Party has endeavored to identify central issues that should be considered in developing strategies for deterring and combatting money laundering in these essential financial markets.

The Working Party believes that all members of IOSCO would benefit from undertaking their own examinations of these central issues. This would be particularly true for those IOSCO members who currently are not members of the FATF, since all FATF members already have committed themselves to the process of evaluating their implementation of the recommendations. Moreover, for the FATF non-members, such an evaluation would assist them in detecting systemic weaknesses that may be exploited by money launderers.

As noted in this report, and consistent with the FATF Recommendations, each IOSCO member should consider:

- (1) the extent to which customer identifying information is gathered and recorded by financial institutions under its supervision, with a view to enhancing the ability of relevant authorities to identify and prosecute money launderers ;
- (2) the extent and adequacy of record-keeping requirements, from the perspective of providing tools to reconstruct financial transactions in the securities and futures markets ;
- (3) together with their national regulators charged with prosecuting money laundering offenses, the appropriate manner in which to address the identification and reporting of suspicious transactions ;
- (4) procedures in place to prevent criminals from obtaining control of securities and futures businesses, with a view to working together with foreign counterparts to share such information as needed ;
- (5) the appropriate means to ensure that securities and futures firms maintain monitoring and compliance procedures designed to deter and detect money laundering ;
- (6) the use of cash and cash equivalents in securities and futures transactions, including the adequacy of documentation and the ability to reconstruct any such transactions ; and
- (7) the most appropriate means, given their particular national authorities and powers, to share information in order to combat money laundering.

The Working Party also proposes to act as a clearinghouse for information for securities and futures regulators about regulatory or self-regulatory steps that have been taken in IOSCO member countries regarding combatting money laundering in securities and futures markets. For example, at the direction of the Technical Committee, the Working Party will gather, and will make available to IOSCO members upon request, copies of guidance notes issued by securities and futures regulators or SROs with respect to identification of money laundering. In addition, the Working Party proposes to monitor, through informal consultations among its members, technological, operational and regulatory developments in the securities and futures markets that may affect efforts to detect and deter money laundering in these markets.

The Working Party proposes to continue its informal liaison efforts with the FATF Working Group on Financial Matters, including making available its expertise in securities and futures markets. Upon direction from the Technical Committee, the Working Party will provide a copy of this report to the chairman of the FATF Working Group on Financial Matters. Through its continuing efforts, the Working Party hopes to continue to heighten the awareness of IOSCO members about the problem of money laundering, and to increase the sophistication of IOSCO members in taking appropriate steps to protect the integrity of the securities and futures markets and businesses against abuse by money launderers.

**APPENDIX A**

**THE FORTY FATF RECOMMENDATIONS**

**(SYNOPSIS)**



## A - GENERAL FRAMEWORK OF THE RECOMMENDATIONS

1 Each country should, without further delay, take steps to fully implement the Vienna Convention, and proceed to ratify it.

2 Financial institution secrecy laws should be conceived so as not to inhibit implementation of the recommendations of this group.

3 An effective money laundering enforcement program should include increased multilateral cooperation and mutual legal assistance in money laundering investigations and prosecutions and extradition in money laundering cases, where possible.

## B - IMPROVEMENT OF NATIONAL LEGAL SYSTEMS TO COMBAT MONEY LAUNDERING

### Definition of the criminal offense of money laundering

4 Each country should take such measures, as may be necessary, including legislative ones, to enable it to criminalize drug money laundering as set forth in the Vienna Convention.

5 Each country should consider extending the offense of drug money laundering to any other crimes for which there is a link to narcotics; an alternative approach is to criminalize money laundering based on all serious offenses, and/or on all offenses that generate a significant amount of proceeds, or on certain serious offenses.

6 As provided in the Vienna Convention, the offense of money laundering should apply at least to knowing money laundering activity, including the concept that knowledge may be inferred from objective factual circumstances.

7 Where possible, corporations themselves -not only their employees- should be subject to criminal liability.

### Provisional measures and confiscation

8 Countries should adopt measures similar to those set forth in the Vienna Convention, as may be necessary, including legislative ones, to enable their competent authorities to confiscate property laundered, proceeds from, instrumentalities used in or intended for use in the commission of any money laundering offense, or property of corresponding value.

Such measures should include the authority to: 1) identify, trace, and evaluate property which is subject to confiscation; 2) carry out provisional measures, such as freezing and seizing, to prevent any dealing, transfer, or disposal of such property and 3) take any appropriate investigative measures.

In addition to confiscation and criminal sanctions, countries also should consider monetary and civil penalties, and/or proceedings including civil proceedings, to void contracts entered by parties, where parties knew or should have known that as a result of the contract, the state would be prejudiced in its ability to recover financial claims, e.g., through confiscation or collection of fines and penalties.

## C - ENHANCEMENT OF THE ROLE OF THE FINANCIAL SYSTEM

### Scope of the following recommendations

9 Recommendations 12 to 29 of this paper should apply not only to banks, but also to non-bank financial institutions.

10 The appropriate national authorities should take steps to ensure that these recommendations are implemented on as broad a front as is practically possible.

11 A working group should further examine the possibility of establishing a common minimal list of non-bank financial institutions and other professions dealing with cash subject to these recommendations.

### Customer identification and record keeping rules

12 Financial institutions should not keep anonymous accounts or accounts in obviously fictitious names: they should be required (by law, by regulations, by agreements between supervisory authorities and financial institutions or by self-regulatory agreements among financial institutions) to identify, on the basis of an official or other reliable identifying document, and record the identity of their clients, either occasional or usual, when establishing business relations or conducting transactions (in particular opening of accounts or passbooks, entering into fiduciary transactions, renting of safe deposit boxes, performing large cash transactions).

13 Financial institutions should take reasonable measures to obtain information about the true identity of the persons on whose behalf an account is opened or a transaction is conducted if there are any doubts as to whether these clients or customers are not acting on their own behalf, in particular, in the case of domiciliary companies (~~the institutions~~ corporations, foundations, trusts, etc., that do not conduct any commercial or manufacturing business or any other form of commercial operation in the country where their registered office is located).

14 Financial institutions should maintain, for at least five years, all necessary records on transactions, both domestic or 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 behaviour.

Financial institutions should keep records on customer identification (e.g. copies or records of official identification documents like passports, identity cards, driving licenses or similar documents), account files and business correspondence for at least five years after the account is closed.

These documents should be available to domestic competent authorities in the context of relevant criminal prosecutions and investigations.



### Increased diligence of financial institutions

15

Financial institutions should pay special attention to all complex, unusual large transactions, and all unusual patterns of transactions, which have no apparent economic or visible lawful purpose. The background and purpose of such transactions should, as far as possible, be examined, the findings established in writing, and be available to help supervisors, auditors and law enforcement agencies.

16

If financial institutions suspect that funds stem from a criminal activity, they should be permitted or required to report promptly their suspicions to the competent authorities. Accordingly, there should be legal provisions to protect financial institutions and their employees from criminal or civil liability for breach of any restriction on disclosure of information imposed by contract or by any legislative, regulatory or administrative provision, if they report in good faith, in disclosing suspected criminal activity to the competent authorities, even if they did not know precisely what the underlying criminal activity was, and regardless of whether illegal activity actually occurred.

17

Financial institutions, their directors and employees, should not, or, where appropriate, should not be allowed to, warn their customers when information relating to them is being reported to the competent authorities.

18

In the case of a mandatory reporting system, or in the case of a voluntary reporting system where appropriate, financial institutions reporting their suspicions should comply with instructions from the competent authorities.

19

When a financial institution develops suspicions about operations of a customer, and, when no obligation of reporting these suspicions exist, makes no report to the competent authorities, it should deny assistance to this customer, sever relations with him and close his accounts.

20

Financial institutions should develop programs against money laundering. These programs should include, as a minimum :

a) the development of internal policies, procedures and controls, including the designation of compliance officers at management level, and adequate screening procedures to ensure high standards when hiring employees ;

b) an ongoing employee training program ;

c) an audit function to test the system.

### Measures to cope with the problem of countries with no or insufficient anti money laundering measures.

21

Financial institutions should give special attention to business relations and transactions with persons, including companies and financial institutions, from countries which do not or insufficiently apply these recommendations. Whenever these transactions have no apparent economic or visible lawful purpose, their background and purpose should, as far as possible, be examined, the findings established in writing, and be available to help supervisors, auditors and law enforcement agencies.

22

Financial institutions should ensure that the principles mentioned above are also applied to branches and majority owned subsidiaries located abroad, especially in countries which do not or insufficiently apply these recommendations, to the extent that local applicable laws and regulations permit. When local applicable laws and regulation prohibit this implementation, competent authorities in the country of the mother institution should be informed by the financial institutions that they cannot apply these recommendations.

Other measures to avoid currency laundering

23

The feasibility of measures to detect or monitor cash at the border should be studied, subject to strict safeguards to ensure proper use of information and without impeding in any way the freedom of capital movements.

24

Countries should consider the feasibility and utility of a system where banks and other financial institutions and intermediaries would report all domestic and international currency transactions above a fixed amount, to a national central agency with a computerized data base, available to competent authorities for use in money laundering cases, subject to strict safeguards to ensure proper use of the information.

25

Countries should further encourage in general the development of modern and secure techniques of money management, including increased use of checks, payment cards, direct deposit of salary checks, and book entry recording of securities, as a means to encourage the replacement of cash transfers.

Implementation and role of regulatory and other administrative authorities

26

The competent authorities supervising banks or other financial institutions or intermediaries, or other competent authorities, should ensure that the supervised institutions have adequate programs to guard against money laundering. These authorities should cooperate and lend expertise spontaneously or on request with other domestic judicial or law enforcement authorities in money laundering investigations and prosecutions.

27

Competent authorities should be designated to ensure an effective implementation of all these recommendations, through administrative supervision and regulation, in other professions dealing with cash as defined by each country.

28

The competent authorities should establish guidelines which will assist financial institutions in detecting suspicious patterns of behaviour by their customers. It is understood that such guidelines must develop over time, and will never be exhaustive. It is further understood that such guidelines will primarily serve as an educational tool for financial institutions' personnel.

29

The competent authorities regulating or supervising financial institutions should take the necessary legal or regulatory measures to guard against control or acquisition of a significant participation in financial institutions by criminals or their confederates.



## D - STRENGTHENING OF INTERNATIONAL COOPERATION

### Administrative cooperation

#### a) Exchange of general information

30 National administrations should consider recording, at least in the aggregate, international flows of cash in whatever currency, so that estimates can be made of cash flows and reflows from various sources abroad, when this is combined with central bank information. Such information should be made available to the IMF and BIS to facilitate international studies.

31 International competent authorities, perhaps Interpol and the Customs Cooperation Council, should be given responsibility for gathering and disseminating information to competent authorities about the latest developments in money laundering and money laundering techniques. Central banks and bank regulators could do the same on their network. National authorities in various spheres, in consultation with trade associations, could then disseminate this to financial institutions in individual countries.

#### b) Exchange of information relating to suspicious transactions

32 Each country should make efforts to improve a spontaneous or "upon request" international information exchange relating to suspicious transactions, persons and corporations involved in those transactions between competent authorities. Strict safeguards should be established to ensure that this exchange of information is consistent with national and international provisions on privacy and data protection.

### Cooperation between legal authorities

#### a) Basis and means for cooperation in confiscation, mutual assistance, and extradition

33 Countries should try to ensure, on a bilateral or multilateral basis, that different knowledge standards in national definitions - i.e. different standards concerning the intentional element of the infraction - do not affect the ability or willingness of countries to provide each other with mutual legal assistance.

34 International cooperation should be supported by a network of bilateral and multilateral agreements and arrangements based on generally shared legal concepts with the aim of providing practical measures to affect the widest possible range of mutual assistance.

35 Countries should encourage international conventions such as the draft convention of the Council of Europe on confiscation of the proceeds from offenses.

#### b) Focus of improved mutual assistance on money laundering issues

36 Cooperative investigations among appropriate competent authorities of countries, should be encouraged.

37 There should be procedures for mutual assistance in criminal matters regarding the use of compulsory measures including the production of records by financial institutions and other persons, the search of persons and premises, seizure and obtaining of evidence for use in money laundering investigations and prosecutions and in related actions in foreign jurisdictions.

38

There should be authority to take expeditious action in response to requests by foreign countries to identify, freeze, seize and confiscate proceeds or other property of corresponding value to such proceeds, based on money laundering or the crimes underlying the laundering activity. There should also be arrangements for coordinating seizure and confiscation proceedings which may include the sharing of confiscated assets.

39

To avoid conflicts of jurisdiction, consideration should be given to devising and applying mechanisms for determining the best venue for prosecution of defendants in the interests of justice in cases that are subject to prosecution in more than one country. Similarly, there should be arrangements for coordinating seizure and confiscation proceedings which may include the sharing of confiscated assets.

40

Countries should have procedures in place to extradite, where possible, individuals charged with a money laundering offense or related offenses. With respect to its national legal system, each country should recognize money laundering as an extraditable offense. Subject to their legal frameworks, countries may consider simplifying extradition by allowing direct transmission of extradition requests between appropriate ministries, extraditing persons based only on warrants of arrests or judgments, extraditing their nationals, and/or introducing a simplified extradition of consenting persons who waive formal extradition proceedings.



## APPENDIX B

### SOURCES FOR CASES STUDIES AND HYPOTHESES INVOLVING MONEY LAUNDERING IN THE SECURITIES AND FUTURES MARKETS

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