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Money Laundering in Brazil

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I – Introduction

Money laundering became an important issue of concern for all nations. They're aware about the risk it represents to the global economic and financial system**.** According to Robinson, "after foreign exchange and the oil industry, the laundering of dirty money is the world's third-largest business" (13).

At the early beginning, the term money laundering was mostly associated with the money generated in drug trafficking activities. Currently, not only criminals use this procedure, but legitimate business that need to disguise the payment of a bribe, or Governments, whether to subvert terrorists or to arm "freedom fighters", as in the case of Iran-Contra.

By the nature of the subject, it is very difficult to obtain a measurement for money laundering. No one knows for certain how much dirty money circles the globe each year, but some guesses range between $200 billion to $500 billion. A consensus range is 2 to 5 percent of global GDP.

The purpose of this paper is to analyze the issue of money laundering, giving a special focus in Brazil's situation after the enactment of Law 9,613 in 1998. It is organized as follows: Section II defines money laundering and the origin of the term, emphasizing the difference between money laundering and tax evasion. Section III explains the whole process of money laundering and some techniques used for this purpose. Section IV presents the international efforts to combat money laundering and also discusses the macroeconomic effects of it. Finally, Section V analyses the situation of Brazil in the implementation of recent counter-measures against money laundering.

II – Money Laundering

A. Definition of Money Laundering

The legal definition of money laundering adopted in the 1988 United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances is:

> *- The conversion or transfer of property, knowing that such property is derived from an offense... , 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 such an offense ... to evade the legal consequences of his actions;*
>
> *- 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 derived from an offense... ;*
>
> *- The acquisition, possession, or use of property, knowing, at the time of receipt, that such property was derived from an offense or from an act of participation in such offense.* (UN Global Programme Aagainst Money Laundering 3)

Money laundering is the process in which profits obtained in illicit activities are converted into legitimate money or usable assets. Money is laundered to hide criminal activity associated with it, including the crimes that generate it, such as drug trafficking or illegal tax avoidance. It conceals the true source of funds so that they can be used freely. It is the support service that allows criminals to enjoy the fruits of their crimes.

The laundering of money is reported to be very expensive. Sometimes, fees of 30 percent or even higher of the amount to be laundered have to be paid or loss-making activities have to be bought.

B. The origin of the term

The term money laundering was originated in the United States, during the 1920s, when street gangs found a seemingly legitimate explanation to justify the money generated by their illegal activities. They used retail service business, like clothes laundries and car washes, to justify the amounts of cash they earned. The reasons to do so were to hide their material success from corrupt police intent on collecting protection payments, or to avoid attracting the attention of envious and brutal competitors. In the 1930s,criminals used money laundering to evade the possibility of tax evasion charges.

The most famous of these criminals was Al Capone who, while operating out of Chicago, managed a large and powerful national crime syndicate. Everyone knew he was a murderer and extortionist, but they could not prove it. He did not need to carry out the criminal acts himself; he would hire others for that.

President Herbert Hoover was frustrated at the inability of the Chicago Police or the new FBI to make a case against “Big Al”. He personally held several meetings to develop a strategy. It was clear that Capone had insulated himself from the criminal conduct that led to his great wealth. However, he did not insulate himself from the profits of the crime, after all, that was what he was in business for. The Untouchables were government law enforcement agents. These agents were accountants with the U.S. tax agency, now the Internal Revenue Service. Al Capone went to prison, not for the crimes he organized, but because he didn’t pay his taxes on their profits.

C. Money Laundering and Tax Evasion

The nature of the laundering process raises important issues of tax enforcement. While illicit money is being earned, criminals will attempt to ensure that it escapes the scrutiny of the authorities, including fiscal ones. Once the money has been laundered, this is no longer necessary. Although tax evasion and money laundering share several techniques and can be mutually supportive, it is important to understand that operationally they are quite distinct processes. In general, tax evasion involves taking legally earned income and either hiding its very existence (if, for example, it is skimmed in cash) or disguising its nature (by making it appear to fall into a non-taxable category). In either event, it turns legal into illegal income. Money laundering does the opposite. It takes illegally earned income and gives it the appearance of being legally earned. In terms of their impact on the fiscal position of a country, evasion and laundering also have quite opposite effects.

Earnings of a legal enterprise can be thought of as falling roughly into two categories. Part of the gross proceeds is used to cover expenses, including wages, material costs and interest payments due to those who lent operating funds. Part is left over as profit, which in turn can be either reinvested or distributed to owners who may consume it or save it.

Though, when illegal goods and services are sold, the results are different. As before, part of the gross proceeds of illegal activity is used to cover expenses of operation and part represents profit, some of which may be reinvested and some distributed to owners, but there is a further division. Regardless of whether earnings are used to cover expenses or to reward owners, some remain in the illegal sector and some may be recycled into the legal one. That which surfaces in the legal economy, part may be used to meet the expenses owed to illegal suppliers while another may go to their counterparts. Another part may become apparently legitimate property of the owners of the business, who, in turn, may reinvest it in illegal or legal business, spend or save it by acquiring legitimate assets. The actual form the laundering process takes will depend at least to some degree on the intended disposition of the funds.

However, one thing remains true. The entire portion of the criminal earnings that appears in the legal economy potentially attracts the attention of the fiscal authorities. Undoubtedly, criminals are as eager as any other entrepreneurs to reduce their fiscal burden, but some such burden is almost inevitable. Tax evaders under-report the earnings of their legal enterprises, thereby paying less in taxes than they legally should. Criminals by contrast, over-report the earnings of any legal enterprises they use for cover, therefore paying more in taxes than their legitimate front companies would normally be required.

This is not to suggest that the state would be fiscally better off if legitimate business shifted to explicitly criminal activity on which some taxes were paid. Clearly, even though criminals will pay some taxes on the portion of their illegal earnings, overall they will evade taxes on as much of their total earnings as possible. The point is that, contrary to the stereotype that sees criminal activity as an off-the-books, unrecorded and untaxed activity, once the money is laundered it becomes at least in part liable to be taxed, albeit with its precise nature disguised.

III. The Process of Money Laundering

A. The Three-stage Process

The most basic problem for a money launderer is to convert large amounts of funds received from illegal activities into more manageable and readily negotiable monetary instruments or other assets, which conceal their illicit origins. It does not matter whether the criminal profits are derived from arson, embezzlement, forgery, fraud, income tax evasion, narcotics trafficking or any other illegal activity. To succeed, criminals must launder their proceeds without leaving a recognizable audit trail.

The process of money laundering, regardless of the degree of complexity, is accomplished in three stages.

1. ***Placement Stage***

   The physical moving of currency or other funds derived from illegal activities and its introduction into traditional or nontraditional financial institutions or into the retail economy.

During placement, the money is most vulnerable to detection and seizure. To assist in the placement stage, the funds may be initially smuggled across a nation's borders and placed into financial institutions located in foreign countries.

2. ***Layering Stage***

The conduct of multiple complex financial transactions, for example, wire transfers or monetary instruments, to make it difficult to trace the proceeds from their illegal source. Layering disguises or eliminates the audit trail of the funds.

3. ***Integration Stage***

This stage provides a legitimate-appearing explanation for illicit financial wealth. For example, integration of these proceeds might include the purchase of real estate, businesses, securities, automobiles, jewelry, etc. Integration places the funds back into economy with the appearance of normal business earnings. It is extremely difficult at this stage to distinguish between legitimate and illicit funds.

There are a wide variety of techniques available today by which money can be laundered. The choice depends partly upon the following criteria:

- *The immediate business environment.* While in principle there is no limit to the fronts through which and forms in which money can be laundered, in practice, launderers try to make their choices reflect as closely as possible the profile of normal business in the area and jurisdiction in which they are operating.
- *The orders of magnitude.* Small sums laundered periodically will require quite different techniques than comparatively large amounts.
- *The time factor.* The technique chosen will likely reflect whether the operation is a once-and-for-all, or sporadic, event or something to be

conducted on an on-going basis. It will reflect as well the degree to which haste is essential.

- *The amount of trust that can be accorded to complicit institutions and individuals.* This requires a judgment about how much potential partners/accomplices have at stake in cooperation or betrayal and where, on the fear-greed tradeoff curve, they happen to be.
- *The record of law enforcement.* Laundering requires time and money. How much energy and expenditure will be put into the effort to multiply levels of cover and obscure the trail will depend on an assessment of how serious and effective police probes are likely to be in the place or places where the process is conducted.
- *The planned long-term disposition of the funds.* Money may be subjected to differing processes depending on whether it is designed for immediate consumption, for savings in visible or invisible forms or for reinvestment (Blum 6).

International treaties recognize a broad range of transactors, instruments and institutions that are potentially involved in laundering the proceeds of illegal activities. Some examples of common money laundering transactions are as follows:

- *Smurfing* involves the use of multiple cash deposits, each smaller than the minimum cash-reporting requirement established by government or banking authorities.
- *Misinvoicing* of exports and falsification of import letters of credit and custom declarations can conceal cross-border transfers of, say, the proceeds of drug trafficking.
- *Barter:* stolen property (e.g., antiques or automobiles) can be exchanged, across national borders or domestically, for illegal substances.

- *Parallel credit transactions* can be used to avoid the formal economy, except for the final use made of the net proceeds of illegal activity to purchase legally marketed goods or services.
- *Interbank wire transfers* may not be subject to reporting on money laundering; bribery of bank officials can thus make it easier to conceal large illegal transfers between accounts.
- *Derivatives* that replicate insider-trading opportunities (e.g., a synthetic version of a company stock subject to merger or takeover) can be used to avoid detection of an unusual change in a listed stock price (Quirk 6).

B. The Money Laundering Cycle in Action

There are four factors common to all money laundering operations.

1. The ownership and source of the money must be concealed. There's no sense in laundering money if everyone knows whom it belonged to and where it originated after it comes out the other end.

2. The form it takes must be changed. Changing the form also means reducing the bulk. No one wants to wash $ 5 million in $20 bills.

3. The trail left by the process must be obscured. The whole purpose of money laundering is defeated if someone can follow the money from beginning to end.

4. Constant control must be maintained over the process. Many of the people who deal with the money while it is being laundered know it is dirty money, and if they steal it, there's little the original owner can legally do.

Figure 1 describes the money laundering cycle. The first step (placement stage) consists in physically placing bulk cash proceeds. The layering stage consists in separating the proceeds from criminal activity from their origins through layers of complex financial transactions, in order to obscure the money trial. The third step, integration stage, is to provide an apparently legitimate explanation for the illicit proceeds. At this point, the money laundered is mixed with legal money, becoming more difficult to separate both.

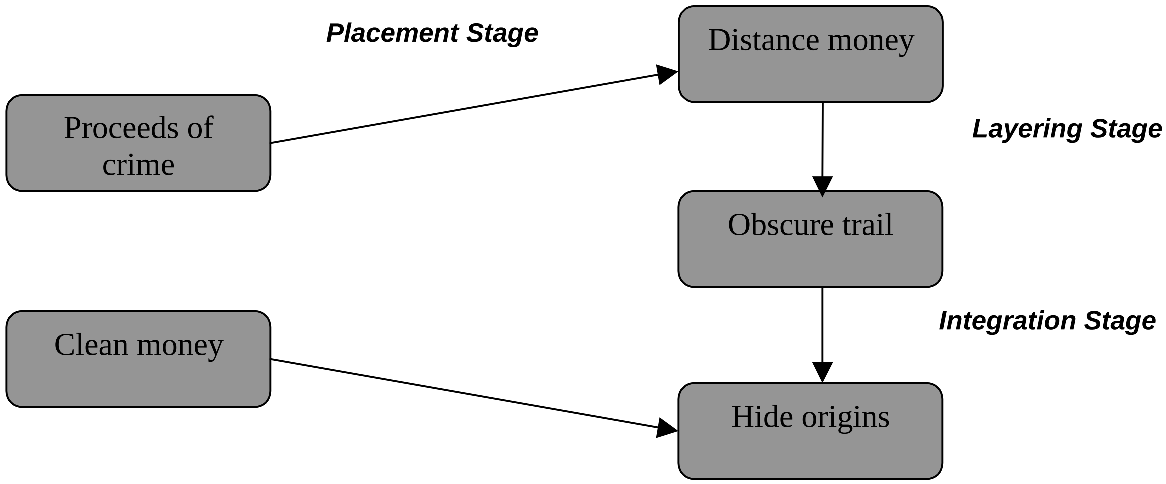

Figure 1 – The money laundering cycle

The cycle is dynamic, and sometimes, due to the complexity of the operations, the three independent steps occur simultaneously, making it impossible to identify each one. Some examples of money laundering operations are described in the following section.

Laundering At Home

The simplest forms of laundering take place strictly within the jurisdiction in which the underlying offence has been committed. If the sums involved are relatively small and/or episodic in nature, there are a number of techniques in which all three stages of the laundering cycle can be neatly combined. Racetracks are classic examples – the launderer simply uses his illegal cash to purchase winning tickets, probably paying the true winner a premium, and then presents the ticket for legitimate earnings from gambling. Much the same can occur with lotteries.

Such techniques are usually employed only episodically and for relatively small sums. To handle on-going flows of criminal money, recourse is usually derived from a cash-based retail service business – car washes and laundries, bars and restaurants have long been favorites. The principle is simple: the illegal money is mixed with the legal and the entire sum is reported as the earnings of the legitimate business.

When the sums become larger and law enforcement in the immediate jurisdiction is seen as particularly dangerous, the laundering process will more likely involve an international dimension. At this point the three stages in the cycle become both logically and chronologically distinct.

Moving the money abroad

The first task is to move the funds from the country of origin. This can be done by either sidestepping or working through the formal banking system. If the decision is made to avoid the system, the most popular method appears to be shipping the money abroad in bulk cash. Sometimes items like diamonds or gold or even precious stamps and other collectibles are also used; the criteria is that they be of high value in relation to bulk, making them physically easy to smuggle as well as relatively easy to reconvert into cash at the point of destination.

Clearly, the problem of currency smuggling will increase as world trade grows, borders become more open to both people and goods and currencies become more convertible.

Various lateral transfer schemes are also used to export money. These work through compensating balances, a simple principle that has long been used in legitimate trade, particularly when dealing with countries that have exchange controls and/or legally inconvertible currencies.

When the decision is made to send criminal money abroad using the formal banking system, additional precautions are required. Large deposits (whether in cash or in checks) with no apparent justification potentially attract attention. Successful money laundering today probably requires working through a front business, one that has a credible explanation for its level of deposits and -something vital when the next stage begins – an equally credible explanation for moving the funds abroad.

Such a company would be one that engages regularly in international trade in goods and/or services. A clever laundering operation would assure that any "payments" it makes to supposed suppliers abroad are in odd rather than round sums and that those sums are not repeated. It might also divide the payments between suppliers in several countries, alternate between wire and written forms of remittance and ensure that the nominal recipients appear to have sound business reputation.

Seeing the world

Once the money is abroad, it is time for stage two of the laundering cycle, moving it through the international payments system to obscure the trail.

Well before a reasonably sophisticated money launderer will attempt to establish a bank account in any haven jurisdiction, there are preliminary steps to be taken. Bank secrecy can often be waived in the event of a criminal investigation. It is for that reason criminal money is normally held not by an individual but by a corporation. Prior to the money being sent to a financial haven, the launderer will probably call on one of the many jurisdictions that offer an instant-corporation manufacturing business. The Cayman Islands and the British Virgin Islands are among the favorites, although there are many others that sell "offshore" corporations that are licensed to conduct business only outside the country of incorporation, are free of tax or regulation and are protected by corporate secrecy laws. Preferably for the launderer, such a company will already have a history of actual activity to increase the appearance of legitimacy. Once the corporation is set up in the offshore jurisdiction, a bank deposit is then made in the haven country in the name of that offshore company, particularly one whose owner's identity corporate secrecy laws protect. Thus, between the law enforcement authorities and the launderer, there is one level of bank secrecy, one level of corporate secrecy and possibly the additional protection of client-attorney privilege if a lawyer in the corporate secrecy haven has been designated to establish and run the company.

In addition, many laundering schemes devise yet a third layer of cover, that of the offshore trust. There are many perfectly legal reasons for the establishment of offshore trusts, some rather dubious one (dodging decisions of tax or divorce courts being the most common) and a few clearly illegal ones. The advantage of a trust is that the owner of assets conveys that ownership irrevocably to the trust and therefore prevents those assets from being seized by creditors. Offshore trusts are usually protected by secrecy laws and may have an additional level of insulation in the form of a "flee clause" that permits, indeed compels, the trustee to shift the domicile of the trust whenever the trust is threatened – by war, civil unrest or even by probes from law enforcement officers. The obvious disadvantage is the nominal loss of control by the owner: in theory a deed of trust is irrevocable, and the former owner can influence, but cannot control, the actions of the trustee.

The offshore asset-protection trust creates another layer of secrecy and security in a money laundering scheme, and it can be complemented by yet more tricks and devices. Companies can be capitalized with bearer shares so there is no owner on record anywhere – the person who physically possesses the share certificates owns the company. There can be multiple systems of interlocking companies, all incorporated in different places, forcing law enforcement officers to proceed from jurisdiction to jurisdiction peeling them away like layers of an onion. There can be multiple bank transfers, again from country to country, where each transfer is protected by secrecy laws that must be breached one at a time. The funds transfer trail can be broken on occasion with the launderer picking up the money in cash from a bank in one place, re-depositing it in a bank somewhere else and then wiring it to yet a third location. The trail can be further complicated if the launderer purchases his own “instant bank” in one of the several jurisdictions that offer such facilities and makes sure that his bank is one of those through which the money passes, then closes the bank and/or destroy the records.

Once the funds have been moved through the international financial system sufficiently to make their origins extremely difficult, if not impossible, to trace, it is time to move them home again, to be enjoyed as consumption or employed as capital.

Heading Home

Many techniques can be used for this stage. Some possibilities are:

- The use of international real estate flips. The criminal arranges to “sell” a piece of property to a foreign investor who is, in fact, the same criminal working through one or several offshore companies. The “sale” price is suitably inflated above acquisition cost, and the money is repatriated in the form of a capital gain on a smart real estate deal. International real estate sham sales can only be used on an occasional basis.
- False capital gains on options trading are preferable to real estate, as it is perfectly normal for someone to trade securities regularly. In fact, frequent securities transactions, each “making” modest capital gains, are less likely to attract unwanted attention than an occasional major gain. The trick is to “buy” and sell a currency, commodity or stock option back and forth between foreign and domestic companies. The onshore company records a capital gain and the foreign one a capital loss. This works even better if the foreign company is incorporated in a place with secrecy laws. Such a laundering trade is perfectly safe since the domestic authorities cannot audit the books of the offshore entity.
- For truly regular income flows, the criminal might arrange to collect the money in the form of income rather than gambling receipts (casinos) or

capital gains (real estate transactions). Personal income is easy to arrange. The criminal simply has one or more of his offshore companies hire him as an employee or, better, as a consultant. In effect the criminal can pay himself a handsome salary or generous consulting fees, as well as possibly a company car or a condominium in a prime location, out of the offshore nest egg. Although this usually results in the highest personal tax rate, it can be partially obviated by having as much of the consulting fees as seems credible paid to cover expenses, which are then deducted from the taxable component of the income.

- The criminal might also choose to repatriate the money as business income. It is merely a matter of setting up a domestic corporation and having it bill an offshore company for goods sold or services provided. If commodities are the chosen vehicle, it is safer when they actually exist and are overvalued (if on the way out) or undervalued (if on the way in), rather than completely fake. It is easier to argue with custom inspectors who might check the shipment about the declared value of a good than it is to try to explain a shipment of empty crates. Once abroad, the goods can be dumped on the black market or into the sea. The same can happen with services, in this case without the need to be bothered with physical inventory.
- The neatest solution of all is to bring the money home in the form of a “loan”. The criminal arranges for money held in an offshore account to be “lent” to his onshore entity. Not only is the money returning home in completely non-taxable form, but also it can be used in such a way as to reduce taxes due on strictly legal domestic income. Once the “loan” has been incurred, the borrower has the right to repay it, with interest, effectively to himself. In effect, the criminal can legally ship even more money out of the country to a foreign safe haven while deducting the “interest” component as a business expense against domestic taxable income. With the employment of various “loan-back” techniques, the money laundering cycle is not merely closed; it can actually be increased in diameter.

C. The Changing Frontier of Money Laundering

The golden rule in successful money laundering is always to approximate, as closely as possible, legal transactions. As a result the actual devices used are themselves minor variations on methods employed routinely by legitimate businesses. In the hands of criminals, transfer-pricing between affiliates of transnational corporations grades into phony invoicing, inter-affiliate real estate transactions become reverse-flip property deals, back-to-back loans turn into loan-back scams, hedge or insurance trading in stocks or options become matched – or cross-trading, and compensating balances develop into so-called underground banking schemes. On the surface it may be impossible to differentiate legal and illegal variants – the distinction becomes clear only once a particular criminal act has been targeted and the authorities subsequently begin to unravel the money trail.

The trend towards institutional commingling is enhanced by three other developments. One, which became evident first with drugs and now is increasingly apparent in other forms of illegal activity, is that criminal entrepreneurs have shifted from serving a set of essentially unrelated regional markets to catering to an increasingly integrated world-wide market. There appears to have been a parallel change in money laundering. There is also some evidence to suggest that, in place of the old pattern of the occasional money laundering institution that was usually linked directly to one or a few criminal entrepreneurs or groups, there has emerged what is virtually an integrated underground global financial system whose relations to criminal entrepreneurs employing its services tend to occur through a series of arms-length commercial transactions. Based on the evidence surfacing in actual cases, money launderers are now more often independent contractors who are as comfortable handling drug money as washing payments for a shipment of embargo-busting arms, as skilled in assisting insider-trading schemes as in moving corporate bribes.

Another aspect is that, whereas in the past the apprehension of a criminal group might well have uncovered the money laundering apparatus along whit it, now there are really two quite distinct targets of investigation and enforcement, which might require two quite separate methodologies. Pursuing transnational crime requires better exchanges of information on particular offenders and improved facilities for transnational investigation and prosecution of particular cases. It remains therefore fundamentally a matter of criminal law. Combating money laundering, however, may require initiatives that might threaten not a particular institution but rather well established systems of banking and financial practices that have a long historical pedigree and that are protected by strong vested-interest groups. It might require actions that particular jurisdictions could well interpret as a direct threat to their very sovereignty. As such, demands for actions must occur in a context of full awareness of the uniqueness of the economic history and practices of each country affected.

A second complication comes from the fact that, while once it was relatively easy to separate the legal and illegal aspects of economic activity because the two existed in a different social and economic space, this is not the case today. Underground activities – either explicitly criminal or merely "informal" – interact with legal ones at many levels. Sweatshops in big cities in the industrialized countries hire illegal aliens who are brought in by smuggling groups that may also deal in banned or restricted commodities, are financed by loan sharks who may be recycling drug money and make cartel agreements with trucking companies run by organized crime families, all in order to sell their goods cheaply to prestigious and eminently respectable retail outlets that serve the general public. The masses of street peddlers in the big urban centers of developing countries sell goods that might be smuggled, produced in underground factories using fake brand-name labels or stolen from legitimate enterprises, thereby violating customs, intellectual property and larceny laws. They pay no sales or income taxes but make protection payments to drug gangs that control the streets where they operate. The drug gangs might then use the protection money as operating capital to finance wholesale purchases of drugs and arms.

The result of these and many similar sorts of interfaces is an economic complex that can no longer be divided into black and white; rather, it forms a continuum of differing shades of gray.

This blurring of traditional frontiers raises new problems of money-laundering control. If economic activity is no longer divisible simply into legal or illegal and if the entire economy is riddled with entrepreneurs who bend this or that rule to and sometimes beyond the breaking point, then the more accepted it becomes for people to violate “small” laws and the greater the probability that others will decide it is permissible to break slightly larger ones, and so on up the scale. Moreover, the greater the degree to which legal and illegal, formal and informal, underground and over ground activities are mixed, the deeper the confusion over the origins of funds, the more difficult the job of exercising due diligence with respect to crimes deemed especially serious and the greater the problems of effective use of suspicious transaction reporting.

The third development, which reinforces the problem, appears at first glance to be a minor statistical technicality, but goes to the heart of modern economic development processes and impacts directly on the problem of policing criminal money flows. Although exceptions exist, economic progress is generally associated with a rise in the percentage of economic activity accounted for by the production of services as opposed to physical goods. As countries increase in wealth and degree of development, the shift in the composition of gross national product (GNP) from tangible goods to intangible services opens up new possibilities for the laundering of criminal money.

The best cover for laundering is a business engaged in legitimate retail trade, especially one that generates large amounts of cash on a regular basis. The higher the service content of the products sold, the greater the potential to use the legitimate retail business to hide the proceeds of crime. It is much easier in services to cloud the audit trail, since there is seldom as clear a relationship between physical inputs and the market value of outputs in a service firm as there is in one supplying physical goods. Tax authorities have long been aware that it is simpler in the services than in the physical goods industries to skim off income and under-report earnings. It is equally easy to do the opposite, to mix illegally earned with legally earned income and report it as if it were legal. A simple rule is: other things being equal, the higher the ratio of services to physical goods' production in a country's GNP, the greater the facility with which its legitimate business firms can be used for laundering money.

This, in turn, has another implication that is potentially dangerous from the point of view of money laundering controls. There is a widely held view that the criminal sector operates overwhelmingly with cash while the legal one uses a mixture of cash and other financial instruments. Indeed, it is common to use changes in the ratio of cash to bank instruments as a tool to estimate the size and growth rate of the underground economy. However, this simple dichotomy may be in the process of becoming obsolete. If the objective is to hide the existence of a criminal money flow or to criminalize legal income after it has been earned (by skimming and hiding) there may be few alternatives to working in cash. But if the objective is to hide the nature of a criminal money flow, an on-going alibi provided by a suitable front company, especially in the retail services field, becomes more important than anonymity. In this case there is nothing that logically precludes the use of cheques or credit cards in conducting retail deals in contraband goods and services.

The blending of legal and illegal actions and the mixing of various degrees and sorts of criminality, along with the attendant difficulty of differentiating between ordinary financial transactions and laundering and between petty and serious crime, has two important consequences with respect to anti-money-laundering measures. The first is that it calls into question much of the enthusiasm about the potential use of artificial intelligence (AI) models and similar devices that are supposed to facilitate the task of sorting through great amounts of financial data. Such models can hardly anticipate all the subtle criminal variations on techniques and methods that appear to be completely innocent in themselves but that are intended to hide illegally obtained money. Artificial intelligence is no substitute for human intelligence. Indeed, it calls into question the very efficacy of imposing ever more severe general reporting requirements. It may well be that all such gross reporting requirements can offer is somewhat better reactive efficiency in following money flows once crimes have already been detected using traditional investigatory techniques, and even this will depend on the particular institutional conditions of the country concerned.

Therefore, it may be unwise to shift significant amounts of limited resources from old-fashioned and less glamorous policing methods to AI models that rely on collecting large amounts of raw information and depend on high-tech solutions.

The second consequence is that not only does the blurring of the frontiers between legal and illegal economy activities, along with the process by which illegal acts become institutionally embedded in legal business firms, make the tracing and unveiling of criminal money much more difficult, but it also raises the cost of doing so. The potential regulatory burden imposed on legitimate business and the degree of disruption of normal transactions flows probably increase more than proportionately. This is especially the case given the rule that the lower the percentage of illegal money running through a particular front, the more respectable that front appears and the more successful that front will be in the long term for laundering.

This implies that at some point Governments must balance the costs of further regulatory complications against the gains measured in terms of crime control. This is, to be honest, quite messy. The costs of the extra regulatory burden are, in some cases, relatively easy to approximate in simple quantitative terms, but assessing the gains in terms of crime control is so complex and so mired in definitional and operational complications that it represents a logical and methodological swamp. Yet it is, unfortunately, one into which everyone concerned with the issue of money laundering will eventually be forced to step.

IV - The International Efforts to Combat Money Laundering

Since the adoption of the Basle Supervisor's Committee Statement of Principles on Money Laundering in 1988, a number of international organizations and regional groups have adopted new rules and regulations against money laundering.

The first international instrument to address the issue of money laundering, and to require States to establish money laundering as a criminal offence, was in the United Nations Convention Against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, adopted in December 1988 in Vienna. In this document, the 185 United Nation Member States declare:

> *The Parties to this Convention,*
>
> *Deeply concerned by the magnitude of and rising trend in the illicit production of, demand for and traffic in narcotic drugs and psychotropic substances, which pose a serious threat to the health and welfare of human beings and adversely affect the economic, cultural and political foundations of society,*
>
> *...*
>
> *Recognizing the links between illicit traffic and other related organized criminal activities which undermine the legitimate economies and threaten the stability, security and sovereignty of States,*
>
> *Recognizing also that illicit traffic is an international criminal activity, the suppression of which demands urgent attention and the highest priority,*
>
> *Aware that illicit traffic generates large financial profits and wealth enabling transnational criminal organizations to penetrate, contaminate and corrupt the structures*

> *of government, legitimate commercial and financial business, and society at all its levels,*
>
> *Determined to deprive persons engaged in illicit traffic of the proceeds of their criminal activities and thereby eliminate their main incentive for so doing, …* (UN, "Money Laundering and the Global Criminal Economy" 3).

Although this was viewed as goodwill declaration, at February 1998, only 145 of a total of 185 Member States of the United Nations had become parties to the Convention. United States officials estimate that only 30 of them had implemented anti-money-laundering measures substantially compliant with the 1988 Convention.

In June 1998 at the twentieth Special Session of the United Nations General Assembly devoted to "countering the world drug problem together", it was adopted a Political Declaration and Action Plan Against Money Laundering.

> *We, the States Members of the United Nations,*
>
> *.....*
>
> *15. Undertake to make special efforts against the laundering of money linked to drug trafficking and, in that context, emphasize the importance of strengthening international, regional and subregional cooperation, and recommend that States that have not yet done so adopt by the year 2003 national money laundering legislation and programmes in accordance with relevant provisions of the United Nations Convention against the Illicit Traffic in Narcotic Drugs and Psychotropic Substances of 1998, as well as the measures for countering money laundering, adopted at the present session* (UN, "Money Laundering and the Global Criminal Economy" 7).

Ten years after the 1988 convention, the General Assembly upgraded and updated it through the adoption of a plan of action, "Countering Money Laundering" to fine-tune and further strengthen the action of the international community against the global criminal economy. This plan of action is the most recent and the most widely accepted set of standards against money laundering. The 185 United Nations Member States have unanimously adopted it.

The General Assembly,

Recognizing that the problem of laundering of money derived from illicit trafficking in narcotic drugs and psychotropic substances, as well as from other serious crimes, has expanded internationally to become such a global threat to the integrity, reliability and stability of financial and trade systems and even government structures as to require counter measures by the international community as a whole in order to deny safe havens to criminals and their illicit proceeds,

......

Aware that the proceeds of illicit drug-trafficking and other illicit activities, which are laundered through banks and other financial institutions, constitute an obstacle to the implementation of policies designed to liberalize financial markets in order to attract legitimate investment, in that they distort those markets,

....

Realizing the importance of progress being made by all States in conforming to the relevant recommendations and the need for States to participate actively in international and regional initiatives designed to promote and strengthen the implementation of effective measures against money laundering,

Strongly condemns the laundering of money derived from illicit drug trafficking and other serious crimes, as well as the use of the financial systems of States for that purpose;

Urges all States to implement the provisions against money laundering that are contained in the United Nations Convention Against Illicit Trafficking in Narcotic Drugs and Psychotropic Substances of 1988 and the other relevant international instruments on money laundering, in accordance with fundamental constitutional principles, by applying the following principles:......... (UN, "Money Laundering and the Global Criminal Economy" 9-10).

The main focus adopted to counter money laundering at the beginning had been to counter the laundering of money related to illegal drug activities, since they concluded that it does little good to attack the criminals while leaving the proceeds untouched. The best results in the fight against the criminals were obtained when they seized the profits obtained in the illegal activity.

The first country to criminalize money laundering was the United Sates. The Money Laundering Control Act of 1986, part of the Anti-Drug Abuse Act of 1986, made money laundering a federal crime.

Until the Vienna Convention, the legislation about money laundering considered just drug trafficking as an underlying offence. Later on, other countries issued legislation considering other crimes like terrorism or extortion through kidnapping as underlying offences. An example of these second generation legislation is the Brazilian money laundering law. Nowadays, the modern legislation about money laundering considered almost all illicit activities as underlying offences. As examples of third generation legislation we have the ones of Italy, France and United States.

A. The International Organizations Created to Combat Money Laundering

FATF – Financial Action Task Force on Money Laundering

The Financial Action Task Force on Money Laundering – FATF, was established at the summit meeting of the Group of Seven major industrialized countries, G-7, in 1989. It's an inter-governmental body whose purpose is the development and promotion of policies to combat money laundering. In April 1990, FATF issued 40 recommendations that cover legal financial regulatory law enforcement and international action that governments should take to combat money laundering. The recommendations are consistent with the Vienna Convention. They also formed the basis of money laundering rules and regulations established by the Caribbean Financial Action Task Force - CFATF, and the Organization of American States.

Those recommendations have become an internationally accepted benchmark in this area. In 1996 the 40 recommendations were revised to take into account the experience gained over the last six years and to reflect the changes that have occurred in the money-laundering problem.

These forty recommendations set out the basic framework for anti-money laundering efforts and they are designed to be of universal application. They cover the criminal justice system and law enforcement, the financial system and its regulation, and international cooperation.

It was recognized from the outset of the FATF that countries have a diverse legal and financial systems and so all cannot take identical measures. The Recommendations are therefore the principles for action in this field, for countries to implement according to their particular circumstances and constitutional frameworks, allowing countries a measure of flexibility rather than prescribing every detail. The measures are not particularly complex or difficult, provided there is the political will to act. Nor do they compromise the freedom to engage in legitimate transactions or threaten economic development.

FATF countries are clearly committed to accepting the discipline of being subjected to multilateral surveillance and peer review. All member countries have their implementation of the forty Recommendations monitored through a two-pronged approach: an annual self-assessment exercise and the more detailed mutual evaluation process under which each member country is subject to an on-site examination. In addition, the FATF carries out cross-country reviews of measures taken to implement particular Recommendations.

The FATF currently consists of 29 countries[1] and two international organizations[2]. Its membership includes the major financial center countries of Europe, North America and Asia. It is a multi-disciplinary body – as is essential in dealing with money laundering – bringing together the policy-making power of legal, financial and law enforcement experts.

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[1] The 29 FATF member countries and governments are: Argentina, Australia, Austria, Belgium, Brazil, Canada, Denmark, Finland, France, Germany, Greece, Hong-kong, Iceland, Ireland, Italy, Japan, Luxembourg, Mexico, the Kingdom of the Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, Turley, United Kingdom, and The United States.

[2] The two international organizations are: the European Commission and the Gulf Coopeation Council.

FIU – Financial Intelligence Unit

Over the past ten years, a number of specialized governmental agencies have been created as countries develop systems to deal with the problem of money laundering. These entities are commonly referred to as “financial intelligence units” or “FIUs”. These units have attracted increasing attention with their ever more important role in anti-money laundering programmes, that is, they seem to provide the possibility of rapidly exchanging information (between financial institutions and law enforcement / prosecutorial authorities, as well as between jurisdictions), while protecting the interests of the innocent individuals contained in their data.

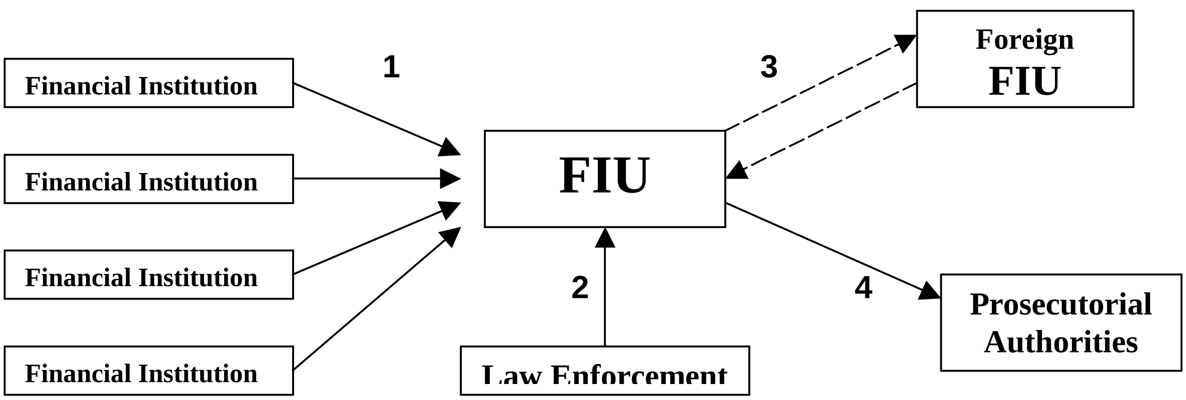
The creation of the FIUs has been shaped by two major influences:

- *Law Enforcement:* Most countries have implemented anti-money laundering measures alongside already existing law enforcement systems. Certain countries, due to their size and perhaps the inherent difficulty in investigating money laundering, felt the need to provide a “clearinghouse” for financial information. Agencies created under this impetus were designed, first and foremost, to support the efforts of multiple law enforcement or judicial authorities with concurrent or sometimes competing jurisdictional authority to investigate money laundering.
- *Detection:* Through the Financial Action Task Force 40 Recommendations and other regional initiatives (European Union and the Council of Europe in Europe; CFATF – Caribbean Financial Action Task Force - and OAS/CICAD – Organization of American States/Inter-American Drug Abuse Control Commission - in the Western Hemisphere), the concept of suspicious transaction disclosures has become a standard part of money laundering detection efforts. In creating transaction disclosure systems, some countries saw the logic in centralizing this effort in a single office for receiving, assessing and processing these reports. FIUs established in this way often also play the role of a “buffer” between the private financial sector and law enforcement and judicial/prosecutorial authorities. With the FIU serving as the honest broker between the private and government sectors, this

arrangement has, in many cases, fostered a greater amount of trust in the anti-money laundering system as a whole.

Over time, FIUs in the first category have tended to add the disclosure receiving function to their list of attributions. Regulatory or oversight authority (with regard to anti-money laundering matters) has also increasingly become a function of a number of FIUs. Since disclosing requirements necessitate that the receiving agency deal with the disclosing institution, it is only logical that some FIUs then become a primary force in working with the private sector to find ways to perfect anti-money laundering systems.

Figure 2 - Basic FIU Concept



1. **Disclosures transmitted to FIU.**
2. **FIU receives additional information from law enforcement.**
3. **Possible exchange with foreign counterpart FIU.**
4. **After analysis, FIU provides case to prosecutor for action.**

The Egmont Group

Despite the fact that FIUs were created in several jurisdictions throughout the world during the first years of 1990s, their creation was still at first seen as isolated phenomena related to the specific needs of those jurisdictions establishing them. Since 1995, a number of FIUs began working together in an informal organization known as the Egmont Group (named for the location of the first meeting at the Egmont-Arenberg Palace in Brussels). The goal of the Group is to provide a forum for FIUs to improve support to their respective national anti-money laundering programmes. This support includes expanding and systematizing the exchange of financial intelligence information, improving expertise and capabilities of personnel of such organizations, and fostering better communication among FIUs through application of technology.

B. The Macroeconomics Effects of Money Laundering

The globalization of the capital market has allowed professional money launderers to exploit differences in controls and regulations far more efficiently and easily than it was possible when capital movements were controlled and restricted within countries. In a way, the freedom of movement of capital, without the necessary steps of leveling controls and regulation, has increased the importance of the differences in controls. Capital movements induced by attempts at laundering money are not promoted by differences in economic fundamentals, such as differences in after-tax rates of return to real investment or, in real interest rates. Rather, they are largely induced by differences in controls and regulations, which make money laundering a safer activity in some countries than in others.

Those who wish to launder money are not looking for the highest rate of return on the money they launder but for the place or the investment that most easily allows the recycling of the criminally or illegally obtained money even when this requires accepting a lower rate of return. Therefore, these movements may well be in directions opposite to those that would be expected on the basis of economic fundamentals. Money may move from countries with good economic policies and higher rates of return to countries with poorer economic policies and lower real or risk-adjusted rates of return, thus seeming to defy the laws of economics. This implies that, because of money laundering, the world capital tends to be invested less optimally than would be the case in the absence of money laundering activities. The world rate of growth is thus reduced not only because of the effects of the criminal activities on the allocation of resources but also because of the allocation of the proceeds from those activities. As a consequence of these counter intuitive capital movements, the policymakers of a country that, in the face of high inflation, overvalued exchange rate, and a large fiscal deficit experienced capital inflow might be less inclined to change their current policies.

If the reported estimates of the proceeds of crime are broadly of the right order of magnitude, the value of all the assets controlled by criminal organizations must be very large. A sizeable share of this value may be invested in countries other than the ones in which reside those who own and control these organizations. Some of these assets may be held in the form of deposits in foreign banks and especially in those that respect bank secrecy; some in shares in foreign enterprises; some in real estate; others in public bonds; others still may be held in cash either domestic or foreign. On the basis of the advice they receive from their financial advisers, those who own and control these assets make the decisions on whether to leave them were they are or to move them to other habitats. These decisions may be influenced more by the attempt to escape controls and to avoid detection than by the search for the highest rate of return. In a way they are still maximizing rates of return adjusted for risk of detection. However, this private maximization is not consistent with an optimal allocation of resources. Therefore, as already mentioned, there may be a large misallocation of world resources associated with the allocation of laundered money in different countries.

Apart from the issue of the optimal or at least the efficient allocation of resources, a large stock of laundered capital may bring some inherent instability to the world economy. The total assets controlled by criminal organizations or criminal elements or by their agents may be so large that the transfer of even a small fraction of them from one country to another could have important economic consequences. If the annual total flow of laundered money is in the hundreds of billions of dollars, and if the stock of all laundered money is even larger, it is not too implausible to imagine that billions of these dollars could be moved around at particular times. These movements could create macroeconomic difficulties for the countries that receive or lose this money and, at least in theory, could have a potentially significant impact on the world economy.

At the national level, large inflows or outflows of capital could significantly influence variables such as the exchange rates and the interest rates, or even the prices of particular assets toward which the money is invested, such as land and houses. In some countries identified with money laundering activities there have been increases in asset prices (land and houses) that often could not be explained by the changes in the countries' policies. When the exchange rate is free to fluctuate, the inflow of large amounts of laundered money into a country would lead to its appreciation and/or to an expansion of the country's monetary base. The appreciation of the exchange rate would encourage more imports. The expansion of the monetary base, in the absence of sterilization, would also put some upward pressure on domestic prices. Faced with this version of the "dutch disease", the policymakers of the country would be forced to tighten its fiscal policy in order to try to create a budgetary surplus to use to sterilize the monetary effects of the capital inflows. A country experiencing a capital outflow would have opposite effects.

These capital movements originating from money laundering activities, especially when they are considered to be of temporary nature, could have internationally destabilizing effects because of the integrated nature of global financial markets. This integration implies that financial difficulties originating in one center can easily spread to other financial centers thus transforming a national problem into a systemic one. The destabilizing effects could arise because these capital movements would not be seen to reflect differences in economic fundamentals across countries. Thus, they send confusing signals to the world economic community. International coordination of economic policy cannot be completely successful without addressing the causes of these perverse capital flows. These causes are, of course, the criminal or illegal activities and, perhaps, as importantly for the international policy coordination, the differences in controls and regulations among countries.

An interesting aspect of international money laundering worth mentioning is the role that American dollar bills play into it. Being the largest market for narcotics, the United States generates a large share of the income produced by this activity. The sale of illegal drugs alone has been estimated to generate as much as US$100 billion a year in the United States. These drugs are imported from Colombia and some other places. When drugs are sold in the streets of the American cities, they are bought with American currency, i.e., with actual dollar bills. These dollars, normally collected in small amounts reflecting the purchases by individual drug users, are used by the local distributors to buy their merchandize from the wholesalers. These in turn use them to pay the distributors who represent the drug lords. These dollar bills are generally smuggled out of the country. As far back as 1984, the U.S. President’s Commission on Organized Crime has estimated that US$5 billion a year in the form of currency was being taken out of the United States through the illegal drug trade. Recent estimates indicate much larger amounts.

Other indirect evidence points to a large stock of U.S. dollars held abroad. For example, there is a great disparity between the total amount of dollar bills known to have been issued by the American authorities, and thus known to be in circulation (about US$350 billion), and the amounts reported to be in the hands of Americans by periodic surveys made by the Federal Reserve System. On the basis of the known quantity of dollar bills issued by the American authorities, each American should be carrying about US$1,500 in cash in his/her pocket. Obviously, this is not the case. Richard Porter, of the U.S. Federal Reserve System has estimated that the amount held abroad is at least US$200 billion out of a total of about US$350 billion. How much of this has left the United States because of money laundering activities is unknown. (Tanzi 9)

Important macroeconomic implications follow from this. First, the holding of these dollars by foreigners implies that an interest-free loan is given to the U.S. government because no interest is paid by it to those who hold them. Second, by reducing the demand for domestic money in the countries where the U.S. dollars are held (that is, through the phenomenon of currency substitution), the holding of dollars abroad raises the rate of inflation in those countries or at least it reduces the seigniorage that the governments of those countries receive from issuing their own money. Finally, it creates some potential instability for the world financial system because of the possibility that at some point (if, say, the value of the dollar were predicted to fall significantly) these dollars could suddenly be unloaded in exchange for other foreign currencies.

The development of an efficient world capital market requires that those who participate in this market have full confidence in it. If this market came to be significantly contaminated by money controlled by criminal elements, this confidence would inevitably be affected. The trust that normal individuals have in the capital market would be reduced. The market would then react more dramatically to rumors and to false statistics thus generating more instability.

The transparency and the soundness of financial markets are key elements in the effective functioning of economies and both may be threatened by money laundering. Criminally obtained money can corrupt some of the officials who make decisions concerning the financial market of countries. If some damage should occur to the financial markets, it could be long lasting because the credibility of markets can be reduced instantaneously but it takes a long time to rebuild. Thus countries that do not make a substantive effort to control money laundering are *de facto* imposing negative externalities on other countries.

It is not farfetched to imagine that, through the use of proxies, criminal elements could intentionally seek to subvert financial markets by corrupting some of the designers and administrators of the laws governing banking, currency, and financial markets in particular countries and the administrators of the financial market. In a worst case and admittedly unlikely, but not impossible, scenario, a cartel of criminal organizations, with control over large financial resources, could attempt to de-stabilize a national economy by intentionally coordinating a transfer of funds (controlled through proxies) out of that economy. They might do this, for punishing the authorities of that country for becoming extra vigilant or for introducing stricter controls. These shifts could create difficulties for some of the countries involved. Of course, these criminal elements may also corrupt the political process of particular countries by financing candidates who may be more likely to let these elements have their way. When the money involved is so large and the pay off to the criminal elements is so significant, it seems realistic to expect that attempts will be made by criminal elements to install more friendly administrations in some countries.

V – Money Laundering in Brazil

The Brazilian government has sought to address the problem of money laundering firstly by building an appropriate legislative framework. The legal framework for the system is contained in the Law 9,613 of 3 March 1998. It defines the offence of money laundering, lays out the principal preventive measures (customer identification, record keeping and suspicious transaction reporting), creates the Brazilian financial intelligence unit (FIU), COAF – Council for Financial Activities Control - and establishes procedures for international co-operation in the areas of confiscation, freezing and seizure of criminal proceeds.

The Council is composed by representatives from Central Bank of Brazil (BACEN), Securities and Exchange Commission (CVM), Superintendent of Private Insurance (SUSEP), Secretariat for Complementary Providence (SPC), Secretariat of Federal Revenue (SRF), Department of Federal Police (DPF), Brazilian Agency of Intelligence (ABIN), Prosecutor General of the National Treasury (PGFN) and the Ministry of Foreign Affairs (MRE).

A. International Cooperation

The 1988 United Nations Convention against Illicit Traffic in Narcotic and Psychotropic Substances (the Vienna Convention) was signed by Brazil in December 20th, 1988. The Legislative Decree 162, from June 14th, 1991, approved the Convention. It was promulgated by the Decree 154, from June 26th, 1991 and came into force in Brazil in October 15th, 1991.

Brazil has actively participated in CICAD/OAS, having an anti-money laundering legislation fully compatible with the Model Regulations of this organization. Furthermore, Brazil, through COAF, integrated the Egmont Group, since its Seventh Plenary Meeting, which took place in Bratislava, Slovakian Republic, in May 1999.

Also, Brazil was an observer member of FATF since September 1999, and was admitted as a full member in June 2000.

B. Money Laundering Situation

With its large and modern financial services sector and its location near some of the major narcotics producing areas of South America, Brazil is an obvious target for money laundering. Up to 1995, the criminal situation in Brazil was strongly influenced by foreign criminal organizations, including Nigerian, Russian, and Korean groups, as well as Italian and Corsican mafias. This influence was largely the result of Brazil's position as a transit country for illegal drug shipments. Since 1995 and because of monetary reforms, it has been more difficult for foreign criminals to find refuge in Brazil, and local groups of varying size now play the most important role in the criminal scene.

There remain some areas of Brazil that are the particular focus of criminal activity, including the border with Colombia (the Tabatinga region) and the tri-border area between Brazil, Argentina, and Paraguay (Foz do Iguaçu). Narcotic trafficking is considered to be the principal source of illegal funds laundered in Brazil, although it is not the only one. Other types of illegal activities, such as trafficking in illegal firearms and stolen automobiles, are also an important source of criminal proceeds, along with illegal gambling, smuggling, bribery, prostitution, tax fraud and theft of government funds.

A large number of fraud cases involving money that has been taken from the Treasury by corrupt government officials has coming to public recently. The missing money has been laundered around the world and the Government is searching for it in the expectation of recovering it.

There's not a measurement for money laundering levels in Brazil, but estimates of illegal funds in circulation range from tens of millions to hundreds of billion of dollars. (Bureau for International Narcotics and Law Enforcement Affairs, 64)

According to the final report of "CPI do Narcotráfico", a commission responsible for the investigation of drug trafficking created in the Congress, the amount of money laundered in Brazil is about US$ 50 billion per year. 50% of this amount is related to drug trafficking. This report was released at the end of November, after one year and a half of investigation. (Marques)

With the recent entry into force of the Brazilian anti-money laundering legislation, it is not yet possible to describe with precision the money laundering typologies derived from Brazilian cases. Nevertheless, according to the Federal Police, the most frequently cited money laundering techniques include:

- the use of current accounts on behalf of front and shell companies;
- transportation and deposit of large amounts of cash;
- exchange houses;
- real estate transactions;
- operations using bingo, lotteries and slot machines as a cover;

- remittance of money through foreign exchange transactions and through deposits to non-resident accounts in Brazil (accounts called CC-5) that are subsequently transferred to offshore centres.

C. Principal Aspects of Anti-Money Laundering Policy and Laws

A key characteristic of the Brazilian anti-money laundering system is its reliance on both a central "competent" authority (the financial intelligence unit - COAF), as well as sector specific authorities, to ensure that money laundering countermeasures correspond to the individual natures of each part of the banking and financial sectors. This means in practice that each financial supervisory authority issues a set of anti-money laundering regulations[3] applicable to institutions, entities, or activities under its jurisdiction and is responsible for ensuring compliance with the measures. Those entities, professions or persons that conduct financial and non-financial activities not covered by one of the already established supervisors fall under the jurisdiction of the Brazilian financial intelligence unit (COAF). The supervisors work with COAF to analyze disclosures of suspicious transactions, along with other information, to detect possible cases of money laundering that are then turned over to investigative authorities.

The money laundering offence covers hiding or concealing illegal proceeds, as well as knowingly using such proceeds in any sort of economic or financial activity. This latter provision would allow Brazilian authorities to prosecute individuals who facilitate laundering operations. "Illegal proceeds", according to the law, are those funds that are generated from a list of underlying offences, including, among others, narcotics trafficking, terrorism, smuggling, other types of trafficking, extortion, corruption, financial crimes and crimes committed by organized criminal groups.

[3] These "administrative regulations" are binding in nature, that is, they have the force of law.

The Brazilian anti-money laundering system also makes the use of a full range of provisional measures, as well as confiscation or forfeiture, as additional tools in combating money laundering. The assets of individuals accused of money laundering may be seized or frozen as part of an investigation, and the law reverses the burden of proof for implementation of such measures. Confiscation of criminal proceeds was already a feature of the Brazilian legal system prior to the enactment of the Law 9,613 of 1998; the legislation merely added money laundering as another crime to which confiscation of assets may be applied.

In the area of international co-operation, Brazilian anti-money laundering legislation authorizes the exchange of information and the sharing of assets through bilateral or multilateral agreements or based on reciprocity. This flexibility is further enhanced by a specific provision authorizing COAF to enter into informal information exchange agreements, such as memoranda of understanding, to facilitate exchanges with counterpart anti-money laundering authorities in other countries.

With regard to criticisms of the Brazilian anti-money laundering system, current secrecy provisions of the banking law pose a significant potential obstacle to the effectiveness of the system. These secrecy provisions apply to all banking information and may only be lifted through judicial authorization. Law enforcement authorities are able, therefore, to obtain such financial information in conjunction with properly authorized investigations. The system for reporting suspicious transactions is affected by the secrecy provisions, however. Some portions of the reports necessarily fall under secrecy restrictions and may not therefore be accessed by COAF. Additionally, the information in these reports that is covered by banking secrecy may not be provided to a foreign jurisdiction unless requested by formal rogatory letter. Brazilian authorities are aware of this potential problem and have proposed modifications to legislation that would maintain the protections of bank secrecy while permitting COAF to obtain access to such information.

The Brazilian legislation is relatively recent, and there have not yet been any prosecutions or convictions for violations of Law 9,613. It is difficult at this point therefore to judge the effectiveness of the law until there has been some experience with it in court. Regarding federal courts, there are not yet judges who specialise in the area of money laundering. COAF is planning a training specially for the judiciary system and have just finished one directed to analysts of various agencies like Central Bank and Federal Police.

While secrecy provisions may, in practice, be a surmountable obstacle for law enforcement investigations, they are a hindrance for the sort of analysis work that is foreseen as part of the mission of COAF. COAF has the role of collecting, recording, analysing, and forwarding information dealing with potential money laundering for investigation by law enforcement. Entities and activities directly subject to COAF's regulations notify COAF directly of suspicious transactions. Financial institutions subject to one of the four other supervisory agencies[4] report their suspicions directly to their respective supervisor, which in turn passes the information to COAF. Due to current Brazilian banking secrecy provisions, the supervisory authorities are not permitted to transmit to COAF the full extent of information they receive from reporting institutions. For example, BACEN may communicate the identity of the customer, the location of the transaction (but not the bank branch), the type of transaction (but not the amount or the account number). CVM may not provide the exact type of securities involved in a suspicious transaction report it receives, and SUSEP may not provide the number of the insurance contract or its nominal amount. In instances where BACEN or another supervisor suspects that a crime has been committed, they may pass the information, again taking into account banking secrecy restrictions, to appropriate law enforcement authorities. Thus banking secrecy is another factor that could over time erode the efficiency of the system. It should be noted as well that BACEN and

[4] BACEN – Central Bank of Brazil, CVM – Securities and Exchange Comission, SUSEP – Superintendence of Private Insurance, or SPC – Secretariat of Complementary Providence.

the other supervisors do not have access to police information, whereas COAF does have the capability to do so.

The Brazilian government has acknowledged the problem of banking secrecy, and it has prepared a bill that would modify the relevant provisions. The proposal would maintain the need for judicial authorisation for lifting bank secrecy but would establish a maximum period of 72 hours after which the tacit deferral of the judge might be presumed. It would permit the supervisory agencies to furnish COAF with the identification data on customers and all information pertaining to suspicious transaction reports. It would furthermore allow BACEN and CVM to sign informal agreements (memoranda of understanding) with foreign counterparts (central banks and financial supervisors) aimed at preventing money laundering. The main obstacle to passage of this legislation is the slow action in the congress, due to focus on other areas, notably the elections last october.

A strong point in this area is the multidisciplinary nature of COAF, the Brazilian financial intelligence unit. Its council consists of representatives of all the major players in the Brazilian anti-money laundering programme, including not only supervisory authorities, but also law enforcement and intelligence agencies. The role of COAF as the focal point of this system is further reinforced by the co-ordination among the members of the council.

VI – Conclusion

Money laundering became an important issue of concern for all nations due to the threat it represents to the global economic, financial and political systems.

The estimates of the amount of money laundered each year in the world are something between 2 to 5 percent of global GDP.

The process of money laundering is conducted in three stages:

1- Placement stage: physically placing bulk cash proceeds.
2- Layering stage: separating the proceeds from criminal activity from their origins through layers of complex financial transactions.
3- Integration stage: providing an apparently legitimate explanation for the illicit proceeds.

Since the adoption of the Basle Supervisor’s Committee Statement of Principles on Money Laundering in 1988, a number of international organizations and regional groups have adopted new rules and regulations against money laundering.

Brazil has started effective anti-money laundering effort by criminalizing money laundering, creating a financial intelligence unit – COAF, and regulating financial and non-financial institutions that are potentially used to the purpose of money laundering.

These institutions must have compliance programs that will ensure their employees are trained, critical records are maintained, transactions monitored and suspicious activity reported to the authorities. These programs must be continuous, in order to update the employees in the new techniques used for money laundering.

As governmental officials are seldom schooled in the intricacies of economic crime and money laundering, (this is particularly true of police, prosecutors and judges who are typically more versed in more traditional criminal behavior), a major effort must be undertaken to develop the analytic, investigative and prosecutive skills to address the unique and complex challenges presented by economic crime. Changes in technology and the globalization of financial services make such efforts difficult, but the training of expertise is essential for well-succeeded investigations and prosecutions.

The composition of COAF is a key point to ensure that the governmental entities work together and share the information. But a problem that Brazil has to address seriously is banking secrecy. It can erode the efficiency of the system.

The relative recent establishment of the Brazilian anti-money laundering system is one of the reasons that there have not yet been any successful prosecutions or convictions for money laundering. The lack of this kind of results at this point in the evolution of the Brazilian system is not yet a matter for concern. However, with slightly more than two years after the passage of Law 9,613 and a year since the first financial sector regulations were issued, the system will soon need to show some successful prosecutions and convictions if it is to be deemed effective and worthy of continued support by law enforcement, the financial sector and the public at large.

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