



Australian Government
**Australian Transaction Reports
and Analysis Centre**

Parliamentary Joint Committee on the Australian Crime Commission

**Inquiry into the Future Impact of Serious Organised Crime on
Australian Society**

**Australian Transaction Reports and Analysis Centre (AUSTRAC)
Submission**

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Introduction

1. This submission is made by the Australian Transaction Reports and Analysis Centre (AUSTRAC).
2. This submission includes comment on AUSTRAC's role in detecting and countering organised crime now and in the future. Further to this, the submission will also discuss legislation relevant to AUSTRAC and most importantly, how AUSTRAC assists the Australian Crime Commission and other partner agencies to continue to detect, deter and disrupt serious and organised crime.

About AUSTRAC

3. AUSTRAC is Australia's anti-money laundering regulator and specialist financial intelligence unit, originally established under the *Financial Transaction Reports Act 1988* (FTR Act) and continued in existence by the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (AML/CTF Act). AUSTRAC's purpose is to detect and counter money laundering and the financing of terrorism.
4. In its regulatory role, AUSTRAC oversees compliance with the requirements of the FTR Act by a wide range of financial services providers, the gambling industry and others. AUSTRAC also oversees compliance with the AML/CTF Act, which received Royal Assent on 12 December 2006 and contains provisions that are being progressively implemented over a two year period.
5. In its intelligence role, AUSTRAC provides AUSTRAC information¹ to Australian Government law enforcement, revenue, national security and social justice agencies, and to State and Territory law enforcement and revenue agencies. AUSTRAC also provides AUSTRAC information to International Financial Intelligence Units (FIUs) as permitted under the AML/CTF Act. AUSTRAC closely monitors and examines money laundering techniques and adapts its financial intelligence unit capabilities to meet new challenges.

Future trends in serious and organised crime activities, practices and methods and their impact on Australian society

6. The fundamental driver of serious and organised crime is the desire to generate financial gain. The laundering of the proceeds of crime is an intrinsic element of serious and organised criminal activity and empowers criminal groups.
7. The Organisation for Economic Cooperation and Development's Financial Action Task Force on Money Laundering (FATF)², International Monetary Fund (IMF) and World Bank all evaluate anti-money laundering systems when rating a country's performance against internationally accepted standards. These groups, and others such as the United Nations, place significant emphasis on a country's ability to counter organised crime and money laundering because there is such a wide range of adverse consequences that impact on society.

¹ 'AUSTRAC information' is defined in section 5 of the AML/CTF Act, and it includes financial transaction reports information.

² The FATF is an inter-governmental body which sets international standards and promotes policies to combat money laundering and the financing of terrorism. For further information, refer to the FATF website at <http://www.fatf-gafi.org>

8. The consequences of organised criminal activity and money laundering may range from the obvious - corruption of public officials and promulgation of illicit drugs - to the less obvious, for example, the impact on the economy when legitimate business is forced to compete with the unethical business practices of those with a financial advantage gained through crime. The attached electronic journal extract by John McDowell and Gary Novis of the Bureau of International Narcotics and Law Enforcement Affairs in the United State's Department of State at Appendix A provides some useful insight into the potential economic consequences of global money laundering by organised crime.

9. Money laundering provides a cloak of legitimacy to wealth derived from crime and provides a funding base from which further criminal activity can be financed; a cycle that can ultimately corrupt society incrementally if unchecked. A further consequence of this can be the legitimisation of criminally derived wealth as well as the criminal behind the wealth, enabling criminals to operate freely and exert their influence throughout the legitimate economy and making the task of discerning criminal proceeds from legitimate proceeds more difficult for authorities.

10. Effective changes to proceeds of crime legislation around the world, initiatives to enable more effective international cooperation in criminal matters and a global push to combat money laundering have all increased risks for criminal entrepreneurs. It stands to reason that, confronted with increased risk, criminal entrepreneurs like any other entrepreneur, will take steps to mitigate risk.

11. Ultimately, criminal groups will continue to seek money laundering methods that offer anonymity, opacity and liquidity:

- Anonymity enables criminal groups to distance themselves from the proceeds of their criminal activities. This can be achieved in a number of ways but may involve for example: the use of false and stolen identities; recruitment of unrelated parties to undertake transactions on behalf of the group; and the use of financial products that require little or no identification.
- Opacity shields criminal proceeds from detection by authorities and can also be achieved in a number of ways. For example, corporate structures and trusts can be facilitated by professional intermediaries using international jurisdictions to facilitate non arms-length transactions.
- Liquidity is important so that criminal proceeds can be readily used to finance further crime or be invested in assets as a store of wealth or used to fund lavish lifestyles.

The rapid development of technologies that limit the transparency of financial activity will offer money launderers opportunities in these key areas.

12. Australia benefits immensely from globalisation but the same benefits are also available to criminal groups. Instantaneous electronic transfer of funds across national borders through the global financial system offer criminal groups the advantage of both obfuscating financial trails and making the recovery of proceeds of crime by authorities protracted.

13. The internet and mobile telecommunications continue to develop as effective and convenient tools to transfer value across borders and between people. Digital currencies backed by precious metals are also increasingly being used to transact through these telecommunication systems and

provide few consumer safeguards. The providers of these services may often be physically located off-shore, which again provides criminal groups the advantage of obfuscating the money trail resulting in protracted investigations for authorities.

14. There is also an increasing availability of products that allow funds to be stored on debit cards that are not linked to a person's name or account and that can be easily transferred between people and across borders.

15. Although there is little evidence to suggest widespread adoption of these methods by organised crime groups in Australia, these technologies together with the growth in identity fraud and identity theft will continue to present opportunities for organised crime and significant challenges for authorities in combating organised crime and money laundering.

16. Criminal groups will no doubt continue to use the established financial sector and other traditional means to launder the proceeds of crime, but this may become more difficult for them in the future as international regulation becomes more stringent. There is a risk that this will lead to attempts by organised crime to infiltrate sections of the financial sector or particular enterprises to assist with the laundering of criminal proceeds and this risk should not be underestimated. The movement of billions of dollars from the Former Soviet Union through the Bank of New York's correspondent accounts with the aid of Bank of New York senior personnel is a good example of this risk exposure. Similarly, in Australia the use of remittance businesses to transfer the proceeds of crime has been of particular concern, and the remittance sector represents a particularly high risk.

Strategies for countering future organised crime

17. A key strategy for governments around the world will continue to be effective anti-money laundering programs. These programs will need to continue to deliver financial intelligence to local and international authorities and harden enterprises against the risk of money laundering, through effective regulation. Enhanced financial investigation skills of investigators coupled with effective proceeds of crime confiscation legislation and effective information exchange domestically and internationally, provide a potent threat to the activities of serious and organised crime.

18. Communication and information sharing are critical in the fight against serious and organised crime. A co-ordinated and strategic multi-agency approach is critical to effectively investigate cross-jurisdictional organised crime. In this regard, AUSTRAC (and many other policing and intelligence agencies) have access to the Australian Crime Commission Law Enforcement Intelligence Network (ALEIN) and the Australian Criminal Intelligence Database (ACID). The intelligence value of ACID is limited in that only a small number of law enforcement agencies within Australia place intelligence onto the system. The potential intelligence value of a central nationwide repository would be considerable. AUSTRAC is currently considering the Heads of Commonwealth Operational Law Enforcement Agencies (HOCOLEA) initiative for all law enforcement and intelligence agencies to feed criminal intelligence into the ACID system. It would be of significant value to Australia if this initiative was adopted by all States and Territories.

19. In a similar vein the increased use of multi-agency and multi-disciplinary teams has proven to be an effective means for authorities to achieve major operational outcomes. The ACC's Financial Intelligence Assessment Team (FIAT) Task Force is currently under review by the ACC and other participating agencies with the view to reconstituting the group and securing adequate resources and commitment from the participating agencies. Formerly operating under the National Crime Authority as the Agio Task Force, the unit had identified and/or developed a significant number of

major criminal networks and other activities of national importance, including the alleged activities being investigated by the ACC's Gordian Task Force and the Australian Taxation Office's Project Wickenby. The multi-agency and multi-disciplinary approach to combat serious and organised crime is an important strategy that should continue to be fostered as it enhances communication, develops inter-operability of resources and encourages debate and consensus on the most effective measures to investigate illegal activity.

20. The rapid development of technology in the financial sector was discussed earlier as a catalyst for potential negative impacts resulting from serious and organised crime. To effectively combat serious and organised crime, technology must also be embraced by government. Proving a person's identification is critical both in protection against crime and also proving crime. Advancements in biometric identification should continue to be investigated.

21. Agencies also need to continually look at advancing information technology systems to allow for greater mining of the data for anomalies and linkages to increase the value of data matching between agencies both private and public. AUSTRAC is currently in the process of reviewing its monitoring systems to enable the greater detection of hidden networks within large data sets.

The economic cost of countering future organised crime at a national and state and territory level

22. The Government has agreed to increase appropriation to fund anti-money laundering and counter-terrorism financing (AML/CTF) reforms. AUSTRAC's total departmental appropriation funding for 2006-07 is \$36.693 million. AUSTRAC's total approved departmental budget appropriation for 2007-08 is \$59.274 million. AUSTRAC appropriation for 2008-09 will be \$54.928 million and \$56.136 million for 2009-10.

23. Increased funding to AUSTRAC will fund the agency's expanded regulatory function. The funding will enable AUSTRAC to prepare Anti-Money Laundering and Counter-Terrorism Financing (AML/CTF) rules, to provide assistance to industry in its transition to compliance with the new legislative obligations and to enhance and extend the agency's audit and inspection program to a significantly increased number of regulated entities now captured under the new legislation.³

24. AUSTRAC's existing financial intelligence unit function will continue to provide analysis and intelligence support services to AUSTRAC's domestic partner agencies and the 47 financial intelligence units of countries with whom intelligence exchange instruments have been agreed.

The adequacy of legislative and administrative arrangements, including the adequacy of cross-jurisdictional databases, to meet future needs

Anti-Money Laundering and Counter-Terrorism Financing Act 2006 (AML/CTF Act)

25. Australia's anti-money laundering and counter-terrorism financing program places obligations on financial institutions and other financial intermediaries. Those obligations are contained in the FTR Act, as well as the AML/CTF Act.

³ The AML/CTF reforms are discussed in more detail in the following section.

26. The FTR Act requires ‘cash dealers’⁴ to report to the AUSTRAC CEO:

- suspicious transactions;
- cash transactions of A\$10,000 or more or the foreign currency equivalent; and
- international funds transfer instructions.

27. As mentioned earlier, the AML/CTF Act received Royal Assent on 12 December 2006, and forms part of a legislative package that will implement the first tranche of reforms to Australia’s AML/CTF regulatory regime.

28. The AML/CTF reforms are a major step towards ensuring Australia’s financial sector remains hostile to criminal activity by providing law enforcement, security, social justice and revenue agencies with valuable sources of information to investigate and prosecute serious organised crime and terrorist activity.⁵ They also bring Australia into line with international standards, including standards set by the FATF. The FATF has agreed to Forty Recommendations on Anti-Money Laundering and Nine Special Recommendations on Counter-Terrorist Financing (the FATF Recommendations) which provide a comprehensive framework of measures for combating money laundering and the financing of terrorism. On 17 October 2005, the FATF published a Mutual Evaluation Report on its evaluation of AML/CTF measures in place in Australia. The evaluation report identified strengths and weaknesses in Australia’s system.

29. The AML/CTF reforms address key issues raised in the evaluation report, such as the strengthening and modernising of procedures for businesses to identify their customers, requirements for businesses to develop AML/CTF programs to deal with specific risks and maintaining and building on Australia’s existing ‘suspicious transaction’ reporting requirements.

30. The AML/CTF Act covers a range of services provided by the financial sector, gambling sector, bullion dealers and other professionals or businesses (‘reporting entities’) that provide particular ‘designated services’⁶. The Act will be implemented in stages over two years in order to allow industry to develop necessary systems in the most cost efficient way.

31. The two-year staggered implementation means that a number of provisions came into effect upon Royal Assent (1st phase) - 13 December 2006, and other provisions take effect after 6 months (2nd phase) – 12 June 2007, 12 months (3rd phase) – 12 December 2007 and 24 months (4th phase) – 12 December 2008.

32. A second tranche of reforms will be necessary to fully realise Australia’s commitment to combating money laundering and the financing of terrorism in areas involving real estate agents, jewellers and professionals such as accountants and lawyers.

⁴ Cash dealers are defined in section 3 of the FTR Act. Some examples of cash dealers include: banks, credit unions and building societies; insurance companies and insurance intermediaries providers; casinos and gambling houses, and; persons who collect, hold, exchange or remit currency on behalf of other persons.

⁵ Refer to the Attorney-Generals Department AML Fact Sheet, *Why are the anti-money laundering and counter-terrorism financing reforms required?*, http://www.ag.gov.au/www/agd/agd.nsf/Page/Anti-moneylaundering_Factsheets at 19 February 2007

⁶ Designated services are outlined in section 6 of the AML/CTF Act.

Use of AUSTRAC Information

33. AUSTRAC information is an intelligence resource for the Australian Taxation Office (ATO) and 'designated agencies' defined in section 5 of the AML/CTF Act to include various regulatory and law enforcement agencies, such as the ACC. Designated agencies can only use that information in accordance with the secrecy and access provisions specified in Part 11 of the AML/CTF Act and the laws that govern the taking of any investigation or prosecution or regulatory compliance action by that individual agency.

34. Access (and the limitations on that access) to AUSTRAC information is controlled by an Instrument of Authorisation signed by the AUSTRAC CEO under section 126(1) of the AML/CTF Act, together with a Memorandum of Understanding between the AUSTRAC CEO and the Chief Executive of each of the 29 designated agencies with whom AUSTRAC has signed an MOU with.⁷ The number of personnel who are permitted to have online access to the AUSTRAC database is also set out in the authorisations.

35. The information stored in the AUSTRAC database is extensive. As at February 2007 there were approximately 80 million reports available to AUSTRAC and its partner agencies. The reports contain a wide range of useful and valuable information that has been used to initiate and support criminal and other investigations. The information contained within these reports has proven to be an important source of intelligence, both financial and otherwise, and often provides investigators with information not previously known.

36. Types of investigations assisted through the use of AUSTRAC information include:

- Money laundering
- Tax offences
- Organised crime
- Paedophilia
- People smuggling
- Structuring
- Homicide
- Duty evasion
- Drugs (production, importation and distribution)
- Fraud
- Armed robbery
- Child pornography
- Terrorism financing
- White collar crime
- Corporate fraud and scams
- Internet fraud and phishing scams

37. AUSTRAC offers an extensive range of services to its partner agencies to assist in their investigations of organised and other serious crime. These services are outlined in the paragraphs below.

⁷ Note that there are 33 designated agencies under the AML/CTF Act, with 4 new agencies yet to sign an MOU with AUSTRAC.

Online Search Facility

38. AUSTRAC provides its partner agencies with both general and specific access to the information it collects. The general access, governed by Instruments of Authorisation and Memoranda of Understanding, is by way of controlled online access to the data and, where appropriate, by extracts of parts of the data holdings. This allows partner agencies to add AUSTRAC's financial intelligence on particular matters to their intelligence holdings, so giving them a better understanding of the activities under their consideration.

Alerts

39. AUSTRAC's alert facility provides online users with the ability to be automatically alerted when a report is matched against a specified set of criteria.

Macro Searches

40. AUSTRAC has developed a range of macro-analysis tools that allow online users to obtain a comprehensive view or picture of specified financial activity. For example, data can be extracted and summarised by reporting areas such as financial institution, occupation code, postcode and/or country.

Data Mining

41. Data mining is an information extraction activity used to discover hidden facts and/or patterns within a database. Using a combination of machine learning, statistical analysis, modelling techniques and database technology, data miners are able to find patterns and subtle relationships in massive data sets and infer rules that allow the prediction of future results and/or behaviour. Data mining tools provide AUSTRAC staff with an ability to deliver advanced analysis to meet a variety of operational needs, including:

- High level querying capabilities to solve complex analytical requirements;
- Network analysis on large data sets using visual representation tools; and
- Predictive modelling to highlight emerging trends and deploy this knowledge to the operational level to improve decision making.

Automated Monitoring System

42. AUSTRAC's automated monitoring system is designed to identify patterns of unusual and suspicious financial activity that may be indicative of money laundering, tax evasion and other serious crime.

Financial Intelligence

43. Through a dedicated group of analysts, AUSTRAC disseminates financial intelligence information to relevant partner agencies. There are two methods in which information is disseminated. Firstly, utilising output from the automated monitoring system, matters are selected for in-depth analysis and a Financial Intelligence Assessment is compiled and proactively disseminated to a partner agency or agencies for investigation or for intelligence value. The second method, which is increasingly important for partner agencies, is the reactive request for financial analysis to be produced on individual targets under investigation.

On Site Support

44. AUSTRAC has an onsite presence in a number of law enforcement agencies, including the ACC. These AUSTRAC representatives provide extensive analytical support and advice to those agencies in relation to the fight against money laundering, terrorist financing, tax evasion, organised and major crime.

Conclusion

45. From a purely financial perspective there is no greater harm that can be inflicted on serious and organised crime than attacking the motivation for their activities: the profits generated from crime.

46. Following money trails has not only assisted in recovering criminal proceeds but perhaps even more importantly, it has led to the discovery of groups and activities previously unknown and assisted in the investigation of predicate offences, and will undoubtedly lead to the securing of more and more money laundering convictions, putting a disincentive in place for those that would otherwise willingly launder the proceeds of crime.

47. Although the number of money laundering convictions to date has been minimal, with authorities preferring to prosecute predicate offences and use proceeds of crime legislation to attack the financial base of crime, authorities have now signalled their conviction to pursue the offence of money laundering in the wake of the review by the FATF.

48. This strategy will assist to address the concerns of the FATF and raise Australia's international credentials in combating money laundering and the financing of terrorism; criminal activities that are vigorously enforced in many parts of the world. The strategy will also provide the opportunity for more severe custodial sentences to be imposed on organised crime figures and money launderers and enhance the opportunity for Australian authorities to coordinate their activities with international colleagues, using alleged money laundering as the basis for mutual assistance and possibly even extradition.

49. Attack organised crime's money and assets and criminals will struggle to gain the credibility and financial means to operate effectively in the criminal and legitimate economies.

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THE CONSEQUENCES OF MONEY LAUNDERING AND FINANCIAL CRIME⁸

*By John McDowell, Senior Policy Adviser, and Gary Novis, Program Analyst,
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Money laundering has a corrosive effect on a country's economy, government, and social well-being, two State Department officials say.

The officials -- senior policy adviser John McDowell and program analyst Gary Novis of the Bureau of International Narcotics and Law Enforcement Affairs -- say the practice distorts business decisions, increases the risk of bank failures, takes control of economic policy away from the government, harms a country's reputation, and exposes its people to drug trafficking, smuggling, and other criminal activity.

Given the technological advantages money launderers now employ, they say, a high level of international cooperation is necessary to keep them in check.

Money laundering is the criminal's way of trying to ensure that, in the end, crime pays. It is necessitated by the requirement that criminals -- be they drug traffickers, organized criminals, terrorists, arms traffickers, blackmailers, or credit card swindlers -- disguise the origin of their criminal money so they can avoid detection and the risk of prosecution when they use it.

Money laundering is critical to the effective operation of virtually every form of transnational and organized crime. Anti-money-laundering efforts, which are designed to prevent or limit the ability of criminals to use their ill-gotten gains, are both a critical and effective component of anti-crime programs.

Money laundering generally involves a series of multiple transactions used to disguise the source of financial assets so that those assets may be used without compromising the criminals who are seeking to use them. These transactions typically fall into three stages: (1) placement -- the process of placing unlawful proceeds into financial institutions through deposits, wire transfers, or other means; (2) layering -- the process of separating the proceeds of criminal activity from their origin through the use of layers of complex financial transactions; and (3) integration -- the process of using an apparently legitimate transaction to disguise illicit proceeds. Through these processes, a criminal tries to transform the monetary proceeds derived from illicit activities into funds with an apparently legal source.

Money laundering has potentially devastating economic, security, and social consequences. It provides the fuel for drug dealers, terrorists, illegal arms dealers, corrupt public officials, and others to operate and expand their criminal enterprises. Crime has become increasingly international in scope, and the financial aspects of crime have become more complex due to rapid advances in technology and the globalization of the financial services industry.

Modern financial systems, in addition to facilitating legitimate commerce, also allow criminals to order the transfer of millions of dollars instantly using personal computers and satellite dishes. Because money laundering relies to some extent on existing financial systems and operations, the criminal's choice of money laundering vehicles is limited only by his or her creativity. Money is laundered through currency exchange houses, stock brokerage houses, gold dealers, casinos, automobile dealerships, insurance companies, and trading companies. Private banking facilities, offshore banking, shell corporations, free trade zones, wire systems, and trade financing all can mask illegal activities. In doing so, criminals manipulate financial systems in the United States and abroad.

Unchecked, money laundering can erode the integrity of a nation's financial institutions. Due to the high integration of capital markets, money laundering can also adversely affect currencies and interest rates. Ultimately, laundered money flows into global financial systems, where it can undermine national economies

⁸ *Economic Perspectives*, Vol.6, No.2, May 2001, at <http://usinfo.state.gov/journals/ites/0501/ijee/state1.htm> at 6 March 2007

and currencies. Money laundering is thus not only a law enforcement problem; it poses a serious national and international security threat as well.

Exposed Emerging Markets

Money laundering is a problem not only in the world's major financial markets and offshore centers, but also for emerging markets. Indeed, any country integrated into the international financial system is at risk. As emerging markets open their economies and financial sectors, they become increasingly viable targets for money laundering activity.

Increased efforts by authorities in the major financial markets and in many offshore financial centers to combat this activity provide further incentive for launderers to shift activities to emerging markets. There is evidence, for example, of increasing cross-border cash shipments to markets with loose arrangements for detecting and recording the placement of cash in the financial system and of growing investment by organized crime groups in real estate and businesses in emerging markets. Unfortunately, the negative impacts of money laundering tend to be magnified in emerging markets.

A closer examination of some of these negative impacts in both the micro- and macroeconomic realms helps explain why money laundering is such a complex threat, especially in emerging markets.

The Economic Effects of Money Laundering

Undermining the Legitimate Private Sector: One of the most serious microeconomic effects of money laundering is felt in the private sector. Money launderers often use front companies, which co-mingle the proceeds of illicit activity with legitimate funds, to hide the ill-gotten gains. In the United States, for example, organized crime has used pizza parlors to mask proceeds from heroin trafficking. These front companies have access to substantial illicit funds, allowing them to subsidize front company products and services at levels well below market rates.

In some cases, front companies are able to offer products at prices below what it costs the manufacturer to produce. Thus, front companies have a competitive advantage over legitimate firms that draw capital funds from financial markets. This makes it difficult, if not impossible, for legitimate business to compete against front companies with subsidized funding, a situation that can result in the crowding out of private sector business by criminal organizations.

Clearly, the management principles of these criminal enterprises are not consistent with traditional free market principles of legitimate business, which results in further negative macroeconomic effects.

Undermining the Integrity of Financial Markets: Financial institutions that rely on the proceeds of crime have additional challenges in adequately managing their assets, liabilities and operations. For example, large sums of laundered money may arrive at a financial institution but then disappear suddenly, without notice, through wire transfers in response to non-market factors, such as law enforcement operations. This can result in liquidity problems and runs on banks.

Indeed, criminal activity has been associated with a number of bank failures around the globe, including the failure of the first Internet bank, the European Union Bank. Furthermore, some financial crises of the 1990s -- such as the fraud, money laundering and bribery scandal at BCCI and the 1995 collapse of Barings Bank as a risky derivatives scheme carried out by a trader at a subsidiary unit unraveled -- had significant criminal or fraud components.

Loss of Control of Economic Policy: Michel Camdessus, the former managing director of the International Money Fund, has estimated that the magnitude of money laundering is between 2 and 5 percent of world gross domestic product, or at least \$600,000 million. In some emerging market countries, these illicit proceeds may dwarf government budgets, resulting in a loss of control of economic policy by governments. Indeed, in some cases, the sheer magnitude of the accumulated asset base of laundered proceeds can be used to corner markets -- or even small economies.

Money laundering can also adversely affect currencies and interest rates as launderers reinvest funds where their schemes are less likely to be detected, rather than where rates of return are higher. And money laundering can increase the threat of monetary instability due to the misallocation of resources from artificial distortions in asset and commodity prices.

In short, money laundering and financial crime may result in inexplicable changes in money demand and increased volatility of international capital flows, interest, and exchange rates. The unpredictable nature of money laundering, coupled with the attendant loss of policy control, may make sound economic policy difficult to achieve.

Economic Distortion and Instability: Money launderers are not interested in profit generation from their investments but rather in protecting their proceeds. Thus they "invest" their funds in activities that are not necessarily economically beneficial to the country where the funds are located. Furthermore, to the extent that money laundering and financial crime redirect funds from sound investments to low-quality investments that hide their proceeds, economic growth can suffer. In some countries, for example, entire industries, such as construction and hotels, have been financed not because of actual demand, but because of the short-term interests of money launderers. When these industries no longer suit the money launderers, they abandon them, causing a collapse of these sectors and immense damage to economies that could ill afford these losses.

Loss of Revenue: Money laundering diminishes government tax revenue and therefore indirectly harms honest taxpayers. It also makes government tax collection more difficult. This loss of revenue generally means higher tax rates than would normally be the case if the untaxed proceeds of crime were legitimate.

Risks to Privatization Efforts: Money laundering threatens the efforts of many states to introduce reforms into their economies through privatization. Criminal organizations have the financial wherewithal to outbid legitimate purchasers for formerly state-owned enterprises. Furthermore, while privatization initiatives are often economically beneficial, they can also serve as a vehicle to launder funds. In the past, criminals have been able to purchase marinas, resorts, casinos, and banks to hide their illicit proceeds and further their criminal activities.

Reputation Risk: Nations cannot afford to have their reputations and financial institutions tarnished by an association with money laundering, especially in today's global economy. Confidence in markets and in the signaling role of profits is eroded by money laundering and financial crimes such as the laundering of criminal proceeds, widespread financial fraud, insider trading of securities, and embezzlement. The negative reputation that results from these activities diminishes legitimate global opportunities and sustainable growth while attracting international criminal organizations with undesirable reputations and short-term goals. This can result in diminished development and economic growth. Furthermore, once a country's financial reputation is damaged, reviving it is very difficult and requires significant government resources to rectify a problem that could be prevented with proper anti-money-laundering controls.

Social Costs

There are significant social costs and risks associated with money laundering. Money laundering is a process vital to making crime worthwhile. It allows drug traffickers, smugglers, and other criminals to expand their operations. This drives up the cost of government due to the need for increased law enforcement and health care expenditures (for example, for treatment of drug addicts) to combat the serious consequences that result.

Among its other negative socioeconomic effects, money laundering transfers economic power from the market, government, and citizens to criminals. In short, it turns the old adage that crime doesn't pay on its head.

Furthermore, the sheer magnitude of the economic power that accrues to criminals from money laundering has a corrupting effect on all elements of society. In extreme cases, it can lead to the virtual take-over of legitimate government.

Overall, money laundering presents the world community with a complex and dynamic challenge. Indeed, the global nature of money laundering requires global standards and international cooperation if we are to reduce the ability of criminals to launder their proceeds and carry out their criminal activities.