

## Money laundering: beyond cash-stuffed briefcases

By Ron Pol

Discussions with lawyers, accountants and real estate agents – all subject to legal obligations to report suspicious transactions – reveal persistent myths and misunderstandings about application of anti-money laundering legislation to their day-to-day work, what money laundering is, how it occurs, how it can affect their businesses, how to identify it, and what it represents in terms of the reality of serious crimes which produce criminal funds flowing through legitimate businesses.

One of the most pervasive myths is that money laundering affecting professional services firms mostly involves cash transactions.

### Obligation to report suspicious transactions

Many so-called “gate keeper” professionals – the lawyers, accountants and real estate agents who structure, implement and facilitate hundreds of thousands of financial transactions each year – understand that they are required to report suspicious transactions.

Although temporarily exempt from the more onerous obligations of the Anti-Money Laundering and Countering Financing of Terrorism Act 2009 (AML/CFT Act), these professionals remain subject to its predecessor, the Financial Transactions Reporting Act 1996 (FTRA) and its core obligation to report suspicious transactions.

The real issue then is not that such obligations exist, but exactly *what* these professionals should be looking for in their own businesses.

### If we look out for cash, we'll be fine, right?

Most professionals would rightly be concerned about large sums of cash. Briefcases stuffed with foreign currency to settle transactions and banknotes smelling of drugs (yes, both still happen) are obvious indicators.

Yet in various discussions recently, some professionals have flatly denied that money laundering even occurs in a non-cash situation.

One lawyer expressed it chillingly plainly: *“If money is transferred from a bank, the bank will have spotted anything untoward. They are ‘clearing houses’, so if the funds for any transaction come from a bank, they’re clean; no lawyer could possibly have any residual obligation even to ask questions, and there’d be nothing to report.”*

This assumption, however, is **just plain wrong**.

The reality is that criminal money laundering often happens in non-cash situations and especially when professionals like lawyers, accountants and real estate agents are involved.

Indeed, it is often only the least sophisticated criminals who use cash in their dealings with professionals. This means that they are obvious not only because they use cash. They may also be exceptionally brazen, or naive; or hope your staff might be.

In any event, they are easy to spot; and may as well be wearing a name badge “Hi, I’m a criminal” (or the traditional patch on their back) – in effect exclaiming exactly where the funds are likely to have originated.

### Are we OK then if we ask the client to deposit the cash first?

If a client arrives with a large sum of cash, or seeks to make frequent cash transactions, a natural response might be to place the onus back on the client to bank the money directly.

In many cases, this may be appropriate. If you know that the client is completely legitimate and the funds lawfully obtained, the reason for your concern may have related solely to the firm’s cash handling security risk.

However, if your concern related to the legitimacy of the client or source of funds, and the transaction itself seemed suspicious, in effect asking a bank to act as your “clearing house” will not absolve a lawyer’s own anti-money laundering responsibilities.

Asking “suspicious” clients with cash-filled

briefcases to deposit the cash themselves before proceeding with a transaction also risks affecting lawyers’ banking relationships; the banks may not view kindly any perception of freeloading their anti-money laundering systems or loading more risk onto their businesses.

Nor would you even necessarily know if the client subsequently deposited the cash anyway, or bypassed the bank’s systems in other ways.

There are literally dozens of ways to circumvent the rules. For example, a series of small transactions, ostensibly from buying and selling goods – like countless legitimate TradeMe customers – can quickly build a bank account balance. Commingling unlawful funds through a cash-intensive business such as a restaurant is another method. (A few trips overseas to a jurisdiction whose banks are less wary can also see the funds returned electronically to a New Zealand bank).

An increasing number of overseas cases illustrate how legitimate professionals can inadvertently be drawn into a morass of risk. For example:

- failure to report an attempted cash transaction may breach obligations to report suspicious transactions – the FTRA applies even to transactions not concluded;
- failure appropriately to resolve concerns raised during the initial attempted cash transaction may generate a second breach if the transaction is later conducted or sought to be conducted with funds which later appeared electronically in the firm’s trust account; and
- in certain circumstances, advising clients to deposit cash themselves so that the transaction can proceed may constitute more serious offences; such as structuring transactions to avoid application of anti-money laundering requirements, aiding and abetting, or possibly even direct breach of the criminal anti-money laundering provisions themselves. (See *Failure to identify suspicious transactions can be serious*).

So, if a 25-year-old unemployed client with no fixed abode, no known means of income and prior dishonesty and drugs convictions returns to the office after the firm declined to accept a large cash deposit, the intended \$1 million house purchase may be no less suspicious if instead the credit later appeared electronically in the firm’s trust account.

But real life is seldom so clear cut. There is some evidence emerging that New Zealand has its own share of professional money launderers; and they would almost certainly not present any of the same obvious markers – nor typically use cash in their dealings with professional services firms in the first place.

The key message for lawyers, accountants and real estate agents is clear. Any attempt to use the firm's services which exhibits any signs of potential wrongdoing should fully and immediately be investigated; and if the funds for a transaction are "from the bank", it would be a mistake to assume they're "clean". If the transaction "smells", ask why.

*This is the first of a two-part article. In part two, Ron Pol outlines why criminal entrepreneurs and their professional money launderers seldom use cash when they use the services of lawyers, accountants and real estate agents.*

*Ron Pol is a lawyer, consultant, and principal at amlAssurance.com and TeamFactors.com, and is currently undertaking doctoral research on the money laundering vulnerabilities of lawyers, accountants and real estate agents.*

## Failure to identify suspicious transactions can be serious

**FAILURE TO IDENTIFY CASH AND NON-CASH** money laundering transactions which any reasonable professional should have noticed may involve serious breaches.

Offences include failing to report suspicious transactions, helping structure transactions that avoid anti-money laundering legislation, and a variety of aiding and abetting offences.

In extreme cases, failure to spot obvious red flag indicators may be even more serious. Although the legislation is unnecessarily complex and cumbersome, "enabling" and "assisting" others, and being "reckless" as to the source of funds, are components of potential charges under the Crimes Act that may apply to professionals who help design, structure and facilitate financial transactions.

Although this is an area in which New

Zealand's enforcement authorities currently seem reluctant to venture, in an increasing number of jurisdictions overseas, lawyers and other professionals have been prosecuted.

In many of those cases, initial assertions of "unwitting involvement" (suggesting that red flag indicators had been "merely" missed or misunderstood) have also been found by the courts more accurately characterised elsewhere on a continuum of involvement, including:

- "wilful blindness" (in which obvious questions were not asked, and suspicious transaction reports not lodged);
- "being corrupted" (involving persistent wilful blindness); and even
- "complicit" (with actual knowledge of the underlying criminality).

The outcomes for lawyers, accountants and real estate agents whose businesses have been found to have been used in transactions involving criminal funds have included disciplinary action, fines, forfeiture, and imprisonment.

Although the risks for New Zealand professional services firms are also increasing, they can readily be mitigated and even the simplest awareness and vigilance measures may be sufficient for most firms.

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## Money laundering: *Beyond cash-stuffed briefcases*

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### PART ONE ADDRESSED

a pervasive myth that money laundering affecting professional services firms mostly involves cash transactions. In part two, I outline why criminals and their professional money launderers seldom use cash when they use the services of lawyers, accountants and real estate agents.

As reported in *Stop criminals misusing legal services, LawTalk 824*, and *Mitigate risks for business advantage, LawTalk 825*, lawyers' trust accounts and other sources have become more attractive to criminal entrepreneurs laundering at least \$1.5 billion of organised crime proceeds annually, and it has also become more difficult for lawyers to avoid becoming implicated when suspicious transactions occur from time to time.

There are also some early indications that enforcement agencies may follow their overseas counterparts in more closely investigating businesses and professions that are used, often inadvertently, to help facilitate transfers of criminal funds and asset purchases (see *NZ Police on cusp of extending early crime disruption strategies?*)

As an important section of the justice community – and to protect their own businesses from inadvertently being misused – lawyers and other professionals should not limit their scrutiny of unusual transactions to those involving cash.

This article briefly explains why non-cash transactions may be equally suspicious.

### Multi-level analysis reveals real areas of professional services risk

A simple analysis beyond the basic cash/non-cash divide – for example by types of criminals, levels of money laundering, and the classic money laundering phases – helps illustrate some of the areas in which professional advice and assistance is beneficial – or may even be necessary – for criminal entrepreneurs laundering the proceeds of

their unlawful activities.

### Only some types of criminals involve professionals

Financial crime can be analysed according to a hierarchy of criminal sophistication:

- Unorganised criminal activity, such as opportunistic burglary, produces criminal funds which often requires third party involvement (receivers of stolen goods), yet this seldom extends to professional services firms.
- As with their legitimate counterparts, organised criminal businesses – involving ongoing criminal activity for profit by a cohesive organised group, such as drug dealing – often *benefits* from the involvement of lawyers and accountants; for example helping manage the operational and investment activities of associated businesses, many of which may appear legitimate.
- Organised criminal networks, undertaking some of the most serious and often international criminal activities such as corruption and drugs and arms trafficking, often *require* the services of a range of professionals.

In New Zealand, in the absence of extensive empirical research (notwithstanding some evidence of organised criminal networks, notably in drugs trafficking), it is believed that a significant proportion of at least \$1.5 billion of criminal funds laundered each year is generated from the middle tier – organised crime.

### Levels of money laundering illustrate when professionals are useful or necessary

The literature also sometimes distinguishes three levels of money laundering: basic, elaborate and sophisticated.

- Basic money laundering typically involves simple cash transactions in which professional services firms are seldom used.
- For elaborate money laundering – involving substantial sums, investment schemes and electronic funds transfers – there are

often considerable *benefits* for criminal entrepreneurs using the services of lawyers, accountants and real estate agents.

- Sophisticated money laundering *requires* the services of a range of specialist professionals, and may involve a combination of unwitting professional services firms and complicit professionals; the former sometimes instructed by overseas or domestic “colleagues” fully aware of the criminal nature of their activities.

Again, although data is scant, in New Zealand there appears little evidence (beyond some possibly curious currency exchange positions) of the most sophisticated money laundering which circumvents national regulations and capabilities. Most domestic money laundering likely appears within the first and second categories.

### Money laundering phases also reveal when professionals more likely to be involved

Of the three classic phases of money laundering, cash appears mostly in the first stage – placement – when criminal funds enter the financial system.

Although there is evidence of lawyers,

### Anti-Money Laundering and Countering Financing of Terrorism Conference 2014

This conference will be held at Te Papa, Wellington on 10 and 11 July. Those attending will learn about:

- legal obligations to identify and report suspicious transactions;
- recent law changes making banks less susceptible to money laundering may have changed lawyers' vulnerabilities and risks; and
- extensive new compliance obligations due to be extended to lawyers, accountants and real estate agents.

Sessions include:

- organised crime and money laundering in the real estate industry;
- lawyers, accountants and real estate agents – engaged to launder money through banks' back doors? and
- outsourcing and reliance on agency/third party arrangements.

See [www.ACAMS.org.nz](http://www.ACAMS.org.nz).

accountants and real estate agents being used in this initial phase (for example, buying a house fully or partly with cash), research suggests that these professionals are *more often* used in the second and third phases of money laundering, both of which typically involve funds “from the bank”:

- the layering stage includes a range of sometimes complex transactions that camouflage the illicit source of funds – such as electronic transfers for a variety of seemingly legitimate reasons, including invoice payments and intercompany loans, to give two examples.
- the integration stage includes the acquisition of assets – such as buying a house with funds “from the bank”.

The skills of lawyers and accountants closely match the arrangements and transfers involved in “layering”; and those of lawyers, accountants and real estate agents match the “integration” phase.

In a modern economy, the vast majority of these transactions do not involve cash at all. They are typically electronic payments and transfers. (And for some criminal activity, such as fraud and cybercrime, cash may never be involved. Criminal funds begin their journey as bank funds).

This means that when criminal entrepreneurs use lawyers, accountants and real estate agents in the secondary and tertiary “layering” and “integration” phases, it involves helping obscure the source of, and investing, criminal funds that are already within the financial system.

Similarly, the main contact point with professional services firms may not be an obvious thug or criminal mastermind. At the levels at which organised crime groups interact with professional services firms, the literature suggests that it will often be a smart, well presented intermediary. The apocryphal

## Funds ‘from the bank’ are not necessarily ‘clean’

cash-filled briefcase may never appear.

**Criminals and their laundry service mostly use bank funds when they use professional services**

The *real* issue for any lawyer, accountant or real estate agent is, therefore,

not so much the blatant use of cash but ensuring that their business systems meet legal obligations to identify clients who use their services in the process of laundering the proceeds of serious crime when using funds already deposited in banks.

There are many well known – and some new and evolving – methods and techniques involved with each phase, but any professional services firm looking only for cash transactions will almost certainly miss sometimes obvious red flag indicators involving non-cash transactions; and may do so even when there is a positive obligation to report suspicious transactions.

The key messages for professional services businesses are clear:

- Funds “from the bank” are not necessarily “clean”. Whether cash or non-cash, if it “smells”, ask why.
- And if there are legal or ethical obligations to report suspicious transactions, better to do so – and protect your business – than subsequently trying to defend not having done so sometimes years later when traditional enforcement methods eventually catch up and seize assets it later transpires your firm inadvertently helped criminal entrepreneurs accumulate.

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## NZ Police on cusp of extending early crime disruption strategies?

Notwithstanding overseas developments focused on increasingly earlier disruption of the means with which criminal entrepreneurs launder funds during the course of their criminal careers – including their use of professional services firms – New Zealand enforcement priorities still seem mostly fixed on so-called predicate serious crimes; typically drug dealing.

Nonetheless, initial “follow the money” strategies – reducing the benefits of crime and disrupting criminals’ capacity to recapitalise their businesses on release from prison – are proving successful; yet remain mostly focused on seizing assets that drug dealers have accumulated over sometimes many years of criminal activity.

The next transition in enforcement sophistication will see New Zealand authorities following their overseas counterparts; and more effectively using the full range of tools which, for the most part, are already part of an extensive legislative toolkit enabling earlier disruption of serious crime.

Because it helps advance existing high-level objectives to reduce serious crime and its associated victimisation at earlier stages, it is almost inevitable that the New Zealand Police will ultimately extend their enforcement capabilities; provided of course they also have the necessary leadership, resources and capabilities enabling them actually to do so.

In an operational sense, effective frameworks could then readily be developed to help identify, investigate and, in appropriate cases, either collaborate with or prosecute professionals whose businesses and services may be used to help facilitate transfers of criminal funds and asset purchases during all phases of criminal entrepreneurial activity.

And for professional services firms themselves, establishing simple and effective systems and training will help meet existing obligations to report suspicious transactions; and stay well outside the crosshairs when enforcement capabilities expand. Good systems will also help prepare for the more onerous legal obligations due to be extended to lawyers and other professionals within the next few years.



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