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Evolution of Money Laundering Schemes

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ABSTRACT: *Money laundering is a global concern for governments and banking systems around the world. Banking regulations have been put in place in most of the developed economies to try and combat the problem. This paper will discuss money laundering schemes both past and present. It will also discuss some reasons why money laundering can still occur today despite the worldwide attempts to prevent it.*

KEYWORDS: *fraud, illegal activities, money laundering, forensic accounting*

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I. INTRODUCTION

Money laundering is defined as making illegal gotten funds appear to have come from legitimate sources through any method possible. It typically consists of three stages: placement, layering and integration. In the placement stage the funds are placed into the global financial system. In the layering stage the unlawful origins of the funds are obscured through a variety of means so that the funds appear to be from legitimate sources and can be used in the legal economy. In the integration phase funds are invested in the legal economy (Soudijn, 2016, Unger (2007)).

II. PAST PRACTICES

Money Laundering is a major global problem associated with fraudulent and illegal activities. It has been estimated that illicitly obtained funds in the U.S. amount to approximately \$300 billion annually. The majority of the illicitly obtained funds are likely to be run through money laundering schemes. Money Laundering is of great concern as it costs legitimate businesses money and is a source for the financing of terrorism (Abel & MacKay, 2016).“Money laundering is fundamentally an exercise in deception” (Sterling, 2015).

A number of money laundering schemes are in existence. The first major scheme is cash smuggling which involves the proceeds from crime being moved across a border or borders through stealthy means. This can be accomplished by hiding the money in vehicles or through hiding it in other items crossing the border, such as bodies or large business items. Once across the border the money is deposited in banking institutions, paid to acquire real estate or invested to establish legitimate businesses (He, 2010). This type of scheme is widely used by drug cartels. The drug networks generally will have the smaller amounts of cash from localized areas brought to a larger metropolitan area where it is consolidated for transport across the border by a trusted person (Simser, 2013). The laundering of cash transactions is also a major financial factor in human trafficking and the smuggling of migrants (Kluczynski, 2013).

The next major scheme involves money laundering through banking or financial institutions. One way this method is used is by using underground banks in lesser developed nations as the initial depository for the illegally gotten funds. The funds are then transferred to accounts in respected banking financial institutions. The accounts in the underground banks will generally be in a name different from that at the respected institution and the original account usually has a company name associated with it (He, 2010). This type of money laundering is sometimes accomplished through the use of subsidiaries. In this case money comes into the subsidiary and then is transferred to the parent company. When this method is used companies may try to hide this through the use of loan documents. This can be difficult to identify since the loan documents may look reasonable. Identification may be possible through following the entire loan process. Loans can be made for legitimate reasons but they can be identified by set repayment dates that are reasonable in terms of time frame, in the documents, and that repayments along with interest payments are made on time according to the documents.

Money can also be laundered through insurance companies. In this case the illegally gotten funds are invested in an insurance policy with a cash value. The policy will be held for a few months and then will be cashed in for the value which has now made the funds appear to be legitimately obtained (He, 2010).

The next scheme is through real estate. In this scheme illegally gotten gains are invested in real estate. After a period of time the real estate is resold thus hiding the nature of the original source of the funds. If real estate in the given market is appreciating then many investors may be flipping properties thus making the transaction seem less suspicious (He, 2010).

Money laundering can also be done through the use of a front or shell company. In this case there are several companies that exist as parents and subsidiaries. Money is deposited in the accounts of the parent company then transferred to the accounts of the subsidiary companies and from there it is distributed to the people who obtained the funds illegally in the first place (He, 2010).The methods described above are some of the major traditional methods for money laundering.

III. PRESENT METHODS

In addition to the past practices, there are some new methodologies that are expanding. These include trade based money laundering. In one of the most famous cases of this type of money laundering Columbian cartels over invoiced the prices for emeralds. Orders were filled with inferior stones but invoiced at the price for high grade stones. The cartels would infuse oil into the stones to make them appear as better quality stones to customs officials. The proceeds were then hidden through a series of transfers and the illegally obtained funds were available for use by the cartels (Simser, 2013).

The second major evolving scheme has to do with prepaid access cards. These types of schemes are sometimes called new payment methodologies. In these schemes the cards could be phone cards, merchant cards or even prepaid Master-card or Visa cards. The illegal funds are deposited in a pool and the cards are issued against the pool and do not carry a specific value with the account. Normal prepaid cards carry a value on the card but not so with this type of scheme. Any card can be used to access the pooled funds as long as there are sufficient funds in the pool. This method makes the money hard to trace to individuals (Simser, 2013).

A new evolving scheme involves the use of licensed professionals (e.g. attorneys). The scheme works when one of the licensed professionals in a firm has association with individuals or organizations that are obtaining funds illegally. The licensed professional bills the individual or organization where the placement of funds has placed the funds. These billings are then paid and the fees become legitimate funds that can be used in the legal economy with the parties who originated the funds. Usually the firms have one legitimate partner and are small. The legitimate partner is kept in the dark about the clients of the other partner(s) and distribution of profits follows the partnership agreement.

IV. PREVENTION

Money laundering can be prevented by investigating all suspicious transactions. Authorities can identify suspicious transactions when financial institutions file suspicious transaction reports. Generally, these reports are prepared only for large cash deposits (amounts of $10,000 or more in the U.S.) but could be expanded (Simser, 2013). Another way that money laundering could be prevented is by analyzing business trends, especially in real estate, that involve large cash transactions of large wires across borders that are suspicious.

Certified Public Accountants (CPAs) are involved with the prevention of money laundering through a variety of engagements. These can include: auditing, tax preparation and forensic accounting engagements. The basis for the first two types in that due professional care must be exercised in the performance of the engagement which can involve significant work on compliance with laws and regulations. In forensic accounting engagements CPAs may be specifically attempting to uncover money laundering activities (Abel & MacKay, 2016). A forensic accounting engagement involving money laundering would focus on back tracing the funds from the integration stage, through the layering stage identifying all of the layers back to the placement stage where the laundering began.

Since there are constantly evolving and emerging money laundering schemes there also have to be constantly evolving detection methods. These methods need to be able to link the many different types of schemes currently in use and those that are evolving (Mehmet, Wijesekera & Buchholtz, 2013).

V. REASONS WHY MONEY LAUNDERING STILL WORKS TODAY.

While most of the economically developed countries have enacted laws that are meant to eliminate money laundering those laws can be circumvented because the criminals involved in the illegal activities know the laws as well. In addition many developing countries do not have the resources to attempt to prevent money laundering through their banking systems. The number of banking transactions carried on through the global economy in a single day is staggering and the volume makes it difficult to attempt to identify suspicious transactions.

The global nature of business today creates major obstacles for banking officials who wish to prevent money laundering. Most money laundering activities come to light through other types of investigations and usually involve law enforcement personnel rather than banking personnel.

VI. CONCLUSION

Money laundering schemes have existed for decades and continue to exist today. Countries have enacted banking laws to attempt to prevent money laundering and law enforcement agencies continually try to identify these activities. This is a problem that increases as the global economy expands and business crosses more borders. The problem continues and evolves as business evolves and expands. The sheer volume of economic transactions makes it essentially impossible to wipe out money laundering. This volume makes it more difficult to trace transactions in order to identify gains from illegal activities.

The evolution and diversity of money laundering schemes adds to the difficulty in identifying illegally obtained funds. In turn the difficulty in tracing transactions increases the need for highly trained forensic investigators and accountants. As techniques for identifying money laundering activities become more sophisticated the money laundering schemes also become more sophisticated.

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