

## Modernising Drug Law Enforcement Report 5

# Drug Law Enforcement and Financial Investigation Strategies

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### Key Points:

- Since the 1980s, there has been a major push in rhetoric and institution-building, emphasizing the centrality of attacking the financial lifeblood of drug trafficking networks and organised economic crimes. Much progress has been made in legislation and the creation of financial intelligence units. However, easier guidance is needed on how to get information overseas, and delays in international cooperation lead to under-exploitation of financial investigation opportunities.
- Financial investigation is often mistakenly seen only in the context of proceeds confiscation rather than in revealing forensically the financial relationships in drug networks.
- Financial investigators – whether police, civilian or trained accountants – need to be embedded with operational and intelligence units, so that they are brought in early enough to help the investigation as well as to take away proceeds of crime.
- Criminal finance analysis and UK post-conviction Financial Reporting Orders can be used fruitfully to target the most harmful networks – local, national and international – but this needs to be mainstreamed.
- More focus should be given to the appropriate making and use by the authorities of suspicious activity reports.
- Little is known systematically about the impact of (a) seizure and (b) confiscation of criminal assets on the organisation of drug markets and on price/supply – other than that it upsets offenders who find it harder to regain reputation afterwards.
- The term ‘money laundering’ may conjure up too vague and unspecified an image to fit the reality. ‘Crime money management’ may be a productive alternative. Many drugs traffickers and dealers ‘offend to spend’ and this needs to be factored into more realistic estimates of national and global money laundering *and savings from crime* as measures of what financial measures against drugs are capable of achieving.

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- Financial investigation and proceeds confiscation/recovery can impact upon public reassurance and the behaviour of financial intermediaries as well as drug offenders – but these goals need to be separated out and evaluated, not just asserted.
- The money laundering risk assessments and the focus on effectiveness in the Financial Action Task Force (FATF) Methodology 2013 provide a welcome incentive and opportunity to re-appraise financial investigation strategies and concrete practices, in the context of drug trafficking, economic crimes, and the increasing trend towards poly-crime activities of crime networks.

## Introduction

'If money laundering is the keystone of organized crime, these recommendations can provide the financial community and law enforcement authorities with the tools needed to dislodge that keystone, and thereby to cause irreparable damage to the operations of organized crime'.

*The Cash Connection*, US Presidential Commission on Organized Crime (1986, p.63)

It is decades since the Reagan Commission used these words to end its call for a new focus on financial measures to attack criminal syndicates. In the course of that period, one might have expected a strong evidence base to develop to guide law enforcement today. If so, one's expectations would be dashed. What governments include in the category of 'financial crime' expands ever wider – from drug trafficking to 'all crimes' as predicate offences for money laundering charges; to financing first terrorism and later proliferation of weapons of mass destruction; and to corruption and tax fraud. Criticisms are regularly (and justifiably) made that the private sector is not doing enough to combat these crimes. However, the importance of the issues has not been matched by the underlying analysis that would tell us 'what works' or even 'what does not work', either in the private sector

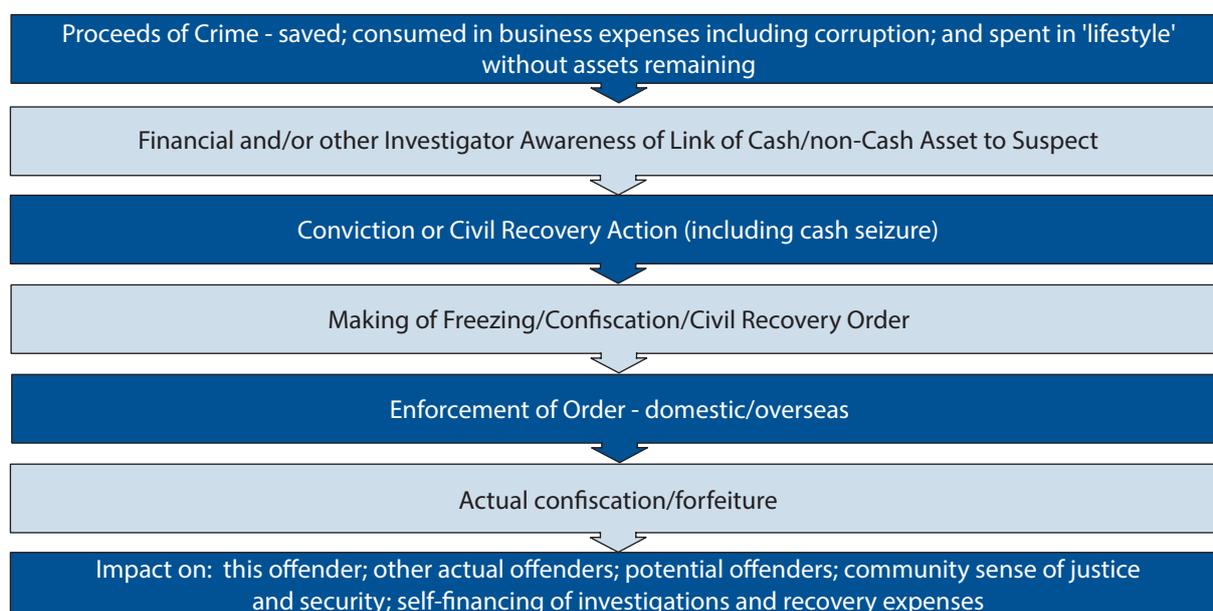
or in the public sector. Nor is there any coherent 'theory of change' that predicts what levels of financial investigation and asset recovery will have what impacts on drugs or other criminal markets under which circumstances.

There are volumes of commentary and legal analysis, but almost nowhere in the world is there any systematic analysis of law enforcement or criminal justice inputs or outputs, let alone of outcomes in terms of reduced crimes of any kind or reduced harms arising from the 'organised' nature of crime.<sup>1</sup> This is so whether crimes are committed by Mafia-type organisations or by the much looser and lower level 'criminal networks' that still can be labelled as 'transnational organised crime' by the modest requirements of the UN 'Palermo' Transnational Organised Crime Convention 2000.<sup>2</sup> Instead, there is a compelling narrative established initially by the use of tax evasion charges to jail Al Capone that has informed law enforcement since the Reagan Commission recommended a national strategy 'to unite a wide range of law enforcement agencies in an effort to strike at the economic heart of organized crime'. It runs as a theme within the recommended use of financial investigation techniques as part of the core forensic process for all 'serious' crimes for gain and to establish the formal and *de facto* ownership/control of proceeds of crime and other assets for the purpose of confiscation or civil recovery proceedings – which can become an end in itself. It also lies behind the global pressures to

increase the burdens on the private sector to better identify risks of financial crimes – both those committed against them and, especially, other crimes whose proceeds *may* be run through them – and to report them to the public authorities, i.e. Financial Intelligence Units (FIUs). FIUs are variously located in the police, administration or judiciary, with implications for their embeddedness and liaison with enforcement, despite global membership of the Egmont Group of FIUs that aims to improve collaboration and standards, whatever their format. This is based implicitly upon enhancing the *potential* for ‘capable guardianship’, in the language of situational crime prevention, as are current G20 proposals to require the better identification of the beneficial owners of corporations and other legal entities, i.e. those who actually control it (see, for example, the proposed Levin-Grassley [Incorporation Transparency and Law Enforcement Assistance Act 2013](#)<sup>3</sup>). However, testing and converting information about ownership and suspicions into intervention action of any kind is far from automatic, so the effects of these measures need to be analysed carefully.

Hitherto, the march of the international anti-money laundering (AML) process has appeared to be remorseless, and it has been extraordinarily successful in attracting support from most

constituencies apart from libertarian<sup>4</sup> and far left groups, offering all of them the prospect of greater purchase on their favoured crime problems. However, analysing the impact on investigative resources ‘on the ground’ and then of AML on levels of crime and – a separate issue – on how crimes are organised<sup>5</sup> has received far more modest attention, conceptually and empirically. A key problem for reviewing the macro impact of financial investigation and associated measures like confiscation is that at one end of the scale, proceeds of crime are ‘estimated’ in their trillions globally, but proceeds of crime actually confiscated are in the very low billions globally, creating an *annual* deficit of trillions of dollars.<sup>6</sup> Looked at in this way, the challenge of getting interventions to reach out and stop such vast sums is so great that the temptation is to give up and opt for the celebration of modest operational successes, or the promotion of radical alternatives such as taxing and regulating the illegal drugs market; but irrespective of views about that, depenalising other organised crime activities such as corruption, fraud, people trafficking and robbery does not seem to be a serious alternative, and those particular problems will not go away of their own accord. So this report makes no claim to be offering a certain route to success: merely an overview of some better and some false steps on the way to whichever goal is specified.



To assist the reader, a set of processes was mapped out above to show the various decision stages involved – these may occur out of the sequence depicted here. For example freezing orders or simple seizures of cash and financial documentation may (and probably should) occur earlier on before the assets are dissipated; and if the offenders are under surveillance, this may be because of financial investigation or other tracking mechanisms.

## The international framework

The Italians might claim that their efforts to get banks to record cash deposits to deal with crimes to finance the *brigata rosse* began the process in the 1970s. But the AML movement started in earnest in 1985 with national efforts in the USA to deal with domestic drugs and organised crime, followed closely by the UK in 1986, and morphed rapidly into the Vienna Convention in 1988,<sup>7</sup> the 'temporary' establishment of the Financial Action Task Force (FATF) in 1989, and the Council of Europe Strasbourg Convention 1990 (revised in the Warsaw Convention 2005).<sup>8</sup> Good accounts of the history exist elsewhere,<sup>9</sup> and there is no need to repeat it here. What is rarer is to examine analytically what the system aims to do and how the operative mechanism actually or even plausibly works. The theories underlying the expected impact of financial crime controls usually assume that drugs traffickers and dealers exercise rational choice (narrowly defined) and that broad situational prevention and targeted enforcement can reduce opportunities and motivation. More broadly – and setting aside other penal principles such as punishing criminals for bad actions because they deserve it – AML controls rest on five foundations:<sup>10</sup>

- **Individual prevention** relies on due diligence by business, and on the passing on of (a) transaction data (CTRs) in some jurisdictions and (b) regulated bodies' suspicions (STRs or SARs) in all jurisdictions

to stop criminals from either 'predicating' criminal activity (e.g. where laundering is part of the original crime, such as some embezzlements and corporate (tax) fraud) or laundering funds, because they will be unable to open accounts or because there is too high a risk of identification from account-monitoring processes before they have got away with their crimes and/or funds.

- **Individual incapacitation** occurs by freezing and confiscating the illegitimately acquired assets of suspects and convicted offenders, which in turn deprives them of capital to commit further crimes, thereby reducing their criminal capability. *Properly enforced*, the criminal must repay their gains – whether from laundered funds, licit funds, or by any other means. This is in addition to any incapacitative impact of custody or even of conviction *per se*, i.e. people and companies requiring licenses as 'fit and proper persons' can no longer practice legally upfront.<sup>11</sup>
- **Individual deterrence** occurs when criminals fear a high risk of exposure if they open up accounts, and/or, if they use corporate fronts or buy other assets from the regulated sector. Consequently, they limit crimes beyond their capacity for personal/group lifestyle consumption and physical storage. This overlaps with individual prevention.
- **Group deterrence** occurs when AML punitive sanctions suppress organised crime, partly because a sufficient number of individuals who might otherwise act as enablers are deterred. Collectively, if there is a level-playing field, this reduces their ability to use different national regimes or institutions within a national regime to find a weak link.
- **Community support for the rule of law and government** is engendered when an AML/confiscation system enhances 'just deserts' by stripping offenders of their ill-gotten gains and is seen as lessening the

attractiveness of certain crimes to others, e.g. drug dealers or generalist crime entrepreneurs are no longer seen as role models. The public face of AML (and of civil asset recovery) may reduce public anxiety about the impunity of evil-doers and contributes to the public's sense of justice. The sense that crooks should not be allowed to benefit from the fruits of crime is an important policy driver and a motivation for financial investigation.

Thus, in the FATF Methodology 2013,<sup>12</sup> Immediate Outcome 7 (prosecutions, etc.) discusses the 'Characteristics of an effective system' and asserts: 'Ultimately, the prospect of detection, conviction, and punishment dissuades potential criminals from carrying out proceeds generating crimes and money laundering'. Immediate Outcome 8 (confiscation) asserts: 'Ultimately, this makes crime unprofitable and reduces both predicate crimes and money laundering'.

The regulatory system is intended to operate by using prospective criminal/regulatory sanctions and regulatory monitoring to pressure and to persuade into greater social responsibility an expanding range of otherwise legitimate institutions that are categorised as 'gatekeepers' or potential 'enablers' of crime:<sup>13</sup>

- (1) to identify and monitor their potential and actual clients and customers far more rigorously than they did in the past, turning away those who do not pass identification and prudential requirements (and perhaps deterring some from applying for accounts);
- (2) to develop systems for identifying patterns of behaviour that are likely (or are believed to be likely) to be associated with various forms of crime.

What is known about the effects of the AML measures that are based on these theories and assumptions? Very little is publicly

known about how difficult drugs or other offenders nowadays find it to launder money, let alone about their detailed risk perceptions of different modes of laundering; the only available studies cover a narrow set of offenders in the Netherlands and the UK.<sup>14</sup> Fairly recent British and Dutch research based on interviews with imprisoned traffickers (of drugs and/or people) suggests that they had modest money laundering sophistication and did not find the system problematic to bypass. As in 'fencing' stolen goods, one might expect knowledge by people willing to offend to act as a constraint upon the development of criminal careers. Much depends on how plausible it is that the sources of funds can be represented as being licit when saving or investing: but a global, well-advertised set of financial intermediaries exist upon whom to experiment, and expectations of being reported following failed attempts may be quite low. Judging from the continued involvement of major banks in negligently or actively facilitating a variety of suspected illicit activities, and the relative impunity of institutions that are 'too big to be prosecuted', normal risk perceptions of relevant parts of financial institutions are not nearly high enough to deter *all* serious non-compliance to AML regulation, though without increasing perceived and/or actual detection risks and reducing elapsed time to action, raising sanctions alone may not work.

Indeed, without doing compliance 'mystery shopping' *internationally* to examine the true state of due diligence and reporting – which I proposed two decades ago in the UK – it is difficult to single out particularly reckless institutions except in the aftermath of scandals that, for example, engulfed Wachovia and HSBC for their role in laundering proceeds of drug trafficking on the Mexico-US intersection.<sup>15</sup> Thematic inspections by the former Financial Services Authority and by World Bank funded experimental exercises have revealed the poor state of compliance in the UK and among some financial intermediaries elsewhere, at least as regards 'Politically Exposed Persons' who

may be involved in drug trafficking.<sup>16</sup> However although infiltration and undercover work by 'cooperating witnesses' have been used, 'Sting operations' have not been tried against elite mainstream financial institutions, though controversially they were against Mexican banks in the DEA's Operation Casablanca in 1998, creating conflict with the Mexican authorities as it seemed clear that they were committed without domestic authorisation or communication on Mexican territory. Whether Mexican banks were especially badly behaved compared with US ones is not a matter of public knowledge, and may not have been a factor in the decision-making as to which institutions to target.

For AML as a whole, the evidence to date offers little that could guide judgments about the optimal balance between financial investigation and other tools for criminal investigation, and between prosecutions for money laundering/financing of terrorism and prosecutions for other offences. There is also no evidence regarding the supply side and demand side effects of convictions of either primary offenders (e.g. drug traffickers) or intermediaries on the market for money laundering other than self-laundering. Thus it is difficult to judge the extent to which the law enforcement and criminal justice component of AML may properly be assessed on a continuum from effective to ineffective. There has been no coherent assessment of what success looks like in drugs AML beyond fewer drug problems, etc., and linking such 'outcomes' later to the AML efforts would not be easy.

Nevertheless, the recent FATF guidance states:<sup>17</sup>

'(13) Countries should ensure that financial investigations become the cornerstone of **ALL** major proceeds-generating cases and terrorist financing cases and that their key objectives include:

- Identifying proceeds of crime, tracing assets and initiating asset confiscation

measures, using temporary measures such as freezing/seizing when appropriate.

- Initiating money-laundering investigations when appropriate.
- Uncovering financial and economic structures, disrupting transnational networks and gathering knowledge on crime patterns'.

## Models of organised crime and corruption

When working out a strategy for enforcement, a key question is working out what kind of problem you are dealing with. This was the cornerstone of Judge Falcone's approach to dealing with the Italian Mafia. Here we confront clearly the theory mistake of 'one size fits all' and the dangers of using the same term 'organised crime' to fit a vast range of formats from the Mafia, Irish paramilitaries and Latin American (mis-labelled) 'cartels' at one end to three burglars and a window cleaning business at the other end of an organisational spectrum. There is a need to allow in our models of how crimes are organised for variations in both (a) the financial arrangements needed to keep the people and activities going and (b) the strategies to impact on their activities and – where this itself constitutes a serious threat – on the people committing them. The link with corruption is also salient. In some developing countries, transnational bribery, law enforcement corruption and major organised crime are connected and are concentrated politically.<sup>18</sup> In other societies, politicians are not heavily involved but law enforcement and criminal justice corruption may be rotten apple or rotten barrel, sufficient to reduce risks of apprehension, conviction and asset confiscation, depending on the risk appetite and connections of the offenders and the control environment in which they find themselves.

## Implications for policing and criminal justice strategies

The models of how serious and organised crimes are put together rationally should affect control strategies, though the action imperative of needing to feel and show that one is doing *something* should never be ruled out. Corruption affects targeting opportunities locally and transnationally. Elsewhere I have examined critically what can be expected from FIUs in developing countries in dealing with Grand Corruption.<sup>19</sup> Can one reasonably expect much more in more *developed* countries (since developed-developing is a spectrum)? In the developed world, NGOs such as the Basel International Centre for Asset Recovery (ICAR), the Francophone SHERPA, and the World Bank's Stolen Assets Recovery (StAR) group have been active against corrupt kleptocrats, some of whom are also involved in drug trafficking and other activities by granting 'protection'/extortionists and/or as co-organisers of drugs and other crime networks. However, such activist groups calling for standalone money laundering charges and international asset-freezing are seldom to be found acting against 'drug traffickers' alone. Thus, in addition to expensive surveillance, action against drugs finances depends largely upon information held in the private sector and available to law enforcement only (a) as routine or suspicious activity reports passed on to FIUs, and (b) as a result of court orders which vary according to powers granted separately in each country, depending on their preference for balancing privacy against investigations. The EU has been particularly active in the mutual cooperation field, via the Camden Assets Recovery Inter-Agency Network (CARIN) – of which the USA is also a full member – and the European Asset Recovery Offices. To increase the speed of investigations, some member states have centralised bank registers, and information about the beneficial ownership of those accounts – i.e. the people who ultimately own the assets – should also be obtainable,

though major traffickers are unlikely to reveal themselves by their personal names.

Nevertheless, moving to effectiveness as well as efficiency, it is not always obvious what people mean in practice by using a network to attack (and to disable or just to disrupt?) another network, and what role can financial investigation play in that, and under which conditions? If we look seriously at confiscation and financial settlements, it is difficult or even impossible to strip out penalties against financial intermediaries from those against 'primary offenders' like traffickers. Perhaps that is not the point: intermediaries may be more vital than individual primary offenders – even 'kingpins' – to the *system* of crime, if any system can be identified. But how do we know what the general or even specific deterrent effect is of the sorts of sanctions against intermediary institutions like Wachovia and HSBC, beyond increasing their compliance departments and cost base, and exiting clients (including possible drug traffickers and their allies) who might attract the wrath of regulators and prosecutors in the future?<sup>20</sup>

Organised crime and drugs enforcement have traditionally been engaged in the search for Mr. Big. Kingpin strategies may reassure the public with dramatic arrests; they may even frighten some talented criminals off aiming for leadership positions (though their need to assert their masculinity may pressure them in the opposite direction). But they do not reduce the level of criminal activities unless that 'kingpin' has unique or hard-to-replace technical and/or brokerage network skills, or unless there is some actual demonstration effect of action against them on the supply of drug dealers at the local, regional or national level, which may take time to become manifest. 'Follow the money' strategies have been critiqued for distorting enforcement priorities,<sup>21</sup> especially when they become an end in themselves. Conversely, they can be attacked for closing their eyes to the vast gap

that exists between current recoveries and even the most conservative estimates of the profits of organised crime and corruption. The latter risks being a policy of despair, since no plausible set of investigations could recover that volume of criminal assets, even setting aside sums spent on 'lifestyle'.

In an earlier era before asset seizure law was tightened, Blumenson and Nilsen<sup>22</sup> found that 80 per cent of US asset seizures (by volume) were unaccompanied by any criminal prosecution. Baicker and Jacobson<sup>23</sup> use data from the Drug Enforcement Administration's System to Retrieve Information from Drug Evidence and other sources, showing that the average price paid for heroin is significantly greater in locations where the police are more active with asset forfeitures. Worrall and Kovandzic<sup>24</sup> conclude, 'police agencies rationally elect to pursue the most lucrative avenues for asset forfeiture, availing themselves of generous state laws'. They found no clear evidence that a greater amount of forfeiture was used in states that permit the police to receive the largest part of the proceeds, though measurement difficulties may have affected this result. They also learned that in states that place limits on what the police can derive from forfeiture, local law-enforcement agencies work around such restrictions by teaming up with federal agencies to mount 'adoptive forfeitures' which pay them based on their part in the enforcement process. States that allow the police to keep all or most forfeiture funds were predictably found to have less recourse to adoptive forfeitures. They note (p. 239) that 'Our study offers some preliminary evidence that forfeiture turns policing into policing for profit. Whether this practice is bane or boon for law enforcement we cannot say... Waging war on drugs is time consuming and expensive, and forfeiture revenues are often pumped right back into drug task forces, undercover investigations, payment of informants, and so on. It is difficult to fault

law-enforcement agencies for exploiting legal arrangements that maximize their potential to offset the high costs associated with America's war on drugs'. The latter perspective is critiqued by Skolnick<sup>25</sup> on ethical grounds, partly because – though this is not articulated – it encourages specialised agencies to become addicted to drug proceeds confiscation. This echoes an earlier study – based on covert participation – which concluded that 'Before asset forfeiture policies were established, narcotics cases were assigned priority by the amount of drugs involved and the level of threat to society posed by suspects. The observations made here, however, show that asset seizure has become the primary objective of drug enforcement'.<sup>26</sup>

While arguing for more financial investigation, Levi and Osofsky<sup>27</sup> questioned the assumption that confiscation would always deter and incapacitate offenders, arguing that it was plausible that some offenders would be motivated to recover their pre-confiscation financial position. Furthermore, to the (disputable) extent that drug traffickers extend credit to purchasers deemed trustworthy or vulnerable to their pressure, large amounts of financial capital may not be needed to begin business again. One can overdo such scepticism – there are instances where criminals struggle to regain their criminal standing. Furthermore, as the re-imprisonment in 2011 of London gangster Terry Adams for failing to report his finances accurately demonstrates, post-conviction Financial Reporting Orders (for up to 10 years) under Sections 76 & 79-81 of the UK Serious Organised Crime and Police Act 2005 can be highly impactful on serious offenders and perhaps on 'the serious crime community', if not on drug price and availability.<sup>28</sup> However the community reassurance component of the 'criminal asset degradation ceremony' – though not formally measured yet – can be a significant benefit, even if it does not raise by much the 'spirit level' of social equality.<sup>29</sup>

As Geis<sup>30</sup> (p. 216) noted, 'It is notable that forfeiture is employed primarily against drug traffickers and customers of streetwalking prostitutes. Neither group enjoys high social approval; nobody proposes forfeiting the private company jet in which the corporate vice president flew off to a meeting with competitors at which prices were fixed in violation of the antitrust laws'. This is less true now, as corrupt insider dealing has become a major target for the US Attorney (Southern District of New York) and for the Securities and Exchange Commission, and a range of organised crime investigative techniques has been deployed against them. Nevertheless, drugs-related cases remain internationally a central feature of organised crime investigations and forfeitures throughout the world. They triggered the Irish and British civil recovery regimes, and predominate in European national and cross-border investigations.

However when reviewing financial investigation, it would be a mistake to focus on assets ordered to be confiscated or actually confiscated as *the* key output indicator. Given the ubiquity of recorded financial transactions to identify geo-location, interactions with others, and motivations, financial investigation has an important role to play in mainstream serious crime policing, from non-domestic homicides to crimes for financial gain, including corruption by public officials. A Thematic Review in Scotland concluded in 2009: 'In contrast to the central position occupied by the SMLU [Scottish Money Laundering Unit] in SCDEA [the Scottish Crime and Drug Enforcement Agency], force financial investigation units (FIUs) were typically situated in peripheral positions in their forces. This seemed to reflect the peripheral position of financial investigation and POCA [Proceeds of Crime Act 2002] generally'.<sup>31</sup> Recent interviews by this author suggest that some of the more enlightened UK and Dutch policing units are using financial investigations in an integrated way, to the limited extent that their resources

(and prosecutor skills and enthusiasms) allow. This brings us to the issue of the practice of financial investigation.

## Financial investigations in practice

International evidence suggests that with increased levels of organised crime come increased levels of corruption,<sup>32</sup> though the sequencing is not self-evident. Buscaglia and van Dijk further argue that the more resources in the form of specialist units that are employed in curbing crime, the more effective they are in fighting corruption. However this omits the issue of Potemkin Villages of apparent institutional activity,<sup>33</sup> which are used for international window dressing or can be deployed aggressively against political opponents: a downside of the trend towards greater financial transparency, and one that is most apparent in some former Soviet countries but can happen elsewhere.

It is worth separating out the objectives of enhancing financial investigation from increasing the level of financial penalties from proceeds of crime investigation *and enforcement*. The absence of research on financial investigation in most countries means that this section relies largely on UK and Dutch research.<sup>34</sup>

### Increasing proceeds of crime confiscation

The global leader in aggressive administrative, civil and criminal asset forfeiture traditionally has been the USA. It sets out its mission thus:

'The primary mission of the Department of Justice (DOJ or the Department) Asset Forfeiture Program... is to prevent and reduce crime by disrupting, damaging, and dismantling criminal organizations through the use of the forfeiture sanction. This is accomplished by

means of depriving drug traffickers, racketeers, and other criminal syndicates of their ill-gotten proceeds and instrumentalities of their trade'.<sup>35</sup>

The Net position (taking away compensation to Madoff and other fraud victims), an indicator of the Assets Forfeiture Fund's future capability to support ongoing operations, decreased to US\$1,620.4 million in Financial Year 2012. But neither it nor the Strategic Plan<sup>36</sup> give any details of effectiveness beyond some examples of activities, nor any methodology by which we could evaluate that impact. The reports give information about the new victim-focused approach to returning confiscated assets – a clear public good – but this is not relevant to drug trafficking. Good process guides are publicly available,<sup>37</sup> as well as other law enforcement-only manuals; and the UK has sought to professionalise proceeds of crime and financial investigation skills learning. However, no literature can be found that has examined seriously the impact of financial forfeitures on drugs markets or on more general social harm.

After a slow start in the 1990s,<sup>38</sup> in the first decade of the 21<sup>st</sup> century, the UK adopted a target culture toward asset recovery, providing incentives to chief officers to adopt that same mind-set with the promise of a percentage of cash rewards from the assets recovered. Showing the motivational benefits of incentivisation, the number of financial investigators deployed increased, as did assets recovered by forces and likewise the rewards to forces; the Labour government published the assets recovered in a form of league table with rankings comparable against other forces.<sup>39</sup> Since then, the negative effects of targets have been recognised and targets have been abandoned, but incentives remain. For cash seizure, half of the funds are retained by the Home Office, and the other half given to the law enforcement body responsible for the seizure. For other asset confiscation,

half is retained by the Home Office, 18.75 per cent given to law enforcement, a further 18.75 per cent is given to the prosecutor, and 12.5 per cent of assets seized is given to the courts (though HM Courts and Tribunals Service charge law enforcement bodies for every cash seizure they bring to court, so their actual 'take' is greater). Nevertheless, financial investigations are overall significantly more costly than the amounts returned to the police, so it might be more accurate to describe this not as 'policing for profit' but as mostly 'policing for less financial loss'.<sup>40</sup> England and Wales confiscations totalled £161.3 million (US\$250.28 million) in 2010/11 – the highest in the last decade – almost a third of which was cash seizures. The great majority of these are low value cases, which currently have to be expensively adjudicated in Crown Courts.

The Scottish Government allocated £500,000 (US\$775,850) to the police service over 3 years, which was match funded by the forces involved, to recruit an additional 19 financial investigators (FIs). The success of this led to approval of an additional £625,000 (US\$969,690) to continue funding the FI posts over a further 2 years, running until the end of 2013-14. In 2012-13, £12 million (US\$18.6 million) were taken from people involved in activities such as drug dealing, human trafficking and benefit fraud with around £8 million (US\$12.4 million) coming from convicted criminals; the remaining £4 million (US\$6.2 million) came from cash and assets seized through civil court orders. Altogether, in the decade since the Proceeds of Crime Act 2002<sup>41</sup>, the Scottish government stated that it received £80 million (US\$124.1 million) from asset recovery: the data show that a significant proportion of this was obtained from corporate crimes rather than from drugs, though the cases highlighted in its *Serious Organised Crime Strategy Spring Update 2013*<sup>42</sup> are mostly drugs cases that show only intermittent evidence of being financial investigation driven. In Wales, £46

million (US\$71.35 million) were recovered from criminals in the past decade (BBC Wales, 21 Mar 2013), the total for England being 10 times higher.

Elsewhere, there is more information about legislation and processes in the Detailed Assessment Reports compiled under the AML regime than there is about effectiveness or even end-to-end efficiency in practice: effectiveness is expected to be assessed in the Fourth round of the FATF AML regime commencing in 2014. One model is to offer incentives of asset sharing and, more rarely, even personal incentives. At one stage, the Thai government was inspired by international pressures to offer personal bonuses to staff to increase the confiscation of assets, and this may have had the effect of reducing the willingness to accept (or demand) bribes, as well as increasing confiscation levels. Whether it led to any human rights abuses is not known. This policy has now been abandoned. Consistent with the UN Convention Against Corruption 2005<sup>43</sup> (with 140 signatories and 167 parties as of July 2013), the World Bank has focussed heavily on criminalising illicit enrichment and the legislative and monitoring processes that underlie that, the aim being to attack the support infrastructure of drug trafficking as well as to deter and prevent bribery.<sup>44</sup> However good the technical assistance offered – a major growth area – much needs to be done to stimulate internal commitment as well as mutual legal assistance for financial investigation, asset freezing, and asset recovery: and not only in developing countries. Cross-border assistance needs stimulation, and a distinction needs to be made between the ability to confiscate proceeds of crime held abroad and their return to the trial jurisdiction: confiscation abroad may need to be incentivised and if its aim is to have an impact upon offending (rather than mainly on the public sense of justice), it does not matter where the proceeds end up.

### **The risks involved in an increased focus on proceeds of crime confiscation**

The dangers in a focus on recovering proceeds of crime as a method of financing law enforcement are noted in several jurisdictions:

- Chasing the ‘low hanging fruit’ – obtaining money from a lot of small cases (e.g. money couriers) could lead to a lack of understanding of the methods or social/financial systems involved
- A focus on income generation instead of criminal justice outputs and outcomes – this can lead to a reluctance to prosecute or even use as witnesses good sources of cash seizures
- A failure to recognise that improved investigations and prosecutions are a prerequisite for presenting a realistic estimate of criminal assets in court and taking the assets from criminals
- The creation of the ‘asset recovery’ culture has had some negative effects on appreciation of the wider benefits of financial investigation. This culture is difficult to break even in the UK, where the financial targets have been abandoned as counter-productive.<sup>45</sup>

Especially when resources are few, law enforcement often resorts in practice to cash seizures and relatively ill-concealed assets domestically held – such as are found in drugs rather than fraud cases.<sup>46</sup> The creation of a national asset recovery agency (ARA) in the UK led to very few cases being referred to it by law enforcement,<sup>47</sup> before it was closed down early after audit reviews found it was costing far more than it recovered – a likely outcome in early years in any part of the world, given the legal challenges and attrition that are commonplace in complex cases. The rate of ‘wealth evaporation’ is fairly high among crime-entrepreneurs: on-going Dutch

research shows that around 10 per cent of the attempted recovery cases have had to be written off. Moreover attrition between initial assessment and final recoveries is common: the Dutch Organized Crime Monitor 2012<sup>48</sup> shows that an initially assumed amount of more than €60 million (for 102 offenders, US\$79.9 million) shrinks dramatically in the course of the various court stages and in the end, only about €10 million (US\$13.3 million) are received by the authorities.<sup>49</sup> This expectation of delayed (and probably reduced) benefits needs to be factored into reforms to avoid disillusionment. Especially in times of austerity, law enforcement agencies with targets to meet want to keep some rewards of their labours. This is one reason why the USA has organised itself into Federal/State Task Forces, to reduce institutional and social barriers among local and state police to joint working.

### **Financial investigation not tied to confiscation**

Assisted by the infrastructure of AML, financial investigation generates both leads for and tests of investigation hypotheses in a variety of fields, including police and governmental corruption, some of which is connected to drug trafficking. An experienced forensic accountant in public service, advocating for greater attention to be given to the financial relationships involved in crime networks, noted: 'The cash spine provides the first stage in developing a model for the OCG [organised crime group] business process. The business command structure that emerges from this can, in turn, provide a structure for considering the application of anti OCG legislation based around the crime of directing serious organised crime, such as now exists in Scotland'.<sup>50</sup>

In community impact terms, low financial value cases may still be important in taking out local nuisance groups who may be 'criminal upcomers'. Targets were never imposed in Scotland, but before the UK government was

persuaded that targets in England and Wales were counter-productive, forces never seemed to meet them, creating pressure to further resource them<sup>51</sup> or to abandon them by default of not prioritising them. Conversely, whilst an increasing range of potential 'enablers' in the financial industry and the professions were compelled to make suspicious transaction reports, proportionately these reports were little used during investigation processes.

A study in England and Wales by Brown et al<sup>52</sup> notes that financial investigations were rarely used to identify organised criminality in the first instance. Financial investigation techniques were applied in more than half of the cases studied during the pre- and post-arrest investigation and the case-building phase. Where used, in addition to identifying organised criminality, financial investigation contributed to investigation and case building through:

- identifying the extent of an organised crime group
- locating assets
- identifying ownership and use of properties
- evidencing offenders' lifestyles
- tracking movements
- placing people at particular places at particular times, linking them to criminality
- identifying additional offences and offenders.

In 30 out of the 60 cases assessed, financial investigation was judged to be 'essential' in determining the case outcome: in 14 cases a conviction would not have been achieved; in 17 cases the role of the offender was discovered; in another eight cases the role of others was identified; and in a further eight cases, further offences were identified, with the consequence that offenders were prosecuted for more offences than otherwise they would have been, reflecting the seriousness of their conduct.

These are not judgements about the inherent limits of financial investigation – simply products of the limited resources available which have to be rationed.

## Conclusions: Paths to follow?

The term ‘money laundering’ conjures up imagery of criminal financial exotica requiring specialist skills for very serious cases only. Yet due to the extension of money laundering legislation globally to cover self-laundering and to almost anything criminals do with proceeds of crime except spending it modestly in immediate consumption,<sup>53</sup> it is a ubiquitous part of the criminal landscape. A more suitable term might be ‘crime money management’, which might make it easier to mainstream financial investigation by demystifying it somewhat, recognising the large spectrum of crime money management practices. In some jurisdictions, to reduce the risk of poor knowledge leading to mistaken approaches to financial institutions, only trained people on the approved FI list are permitted access to the suspicious activity report databases. This is a good practice, both in terms of skills enhancement and to generate greater accountability: otherwise, financial intelligence could be used for extortion from drug traffickers or from semi-legitimate businesspeople, or to sell to the private sector. However, looking for, and using evidence of, drug offender assets does not always require specialist skills, and even the term ‘financial investigation’ ranges from basic ways of thinking about money and assets to deprive criminals to far more complex accountancy skills. Sometimes, the simple juxtaposition of suspects’ lifestyle expenditures with their official incomes can tell an important story, especially if the investigator has access to tax data and it is admissible in court.

I have adopted a tone of cautious scepticism in this review because I consider that what is needed is fewer grand claims and more of an analytical

focus on the end-to-end processing of financial investigation to conviction and/or to deprivation of proceeds of crime. Historically, the AML movement has been suffused with evangelism in spreading the message to every sector of the political economy and the globe. Enthusiasm is good, but sometimes greater analysis is also needed. The new FATF methodology of 2013 heralds a more prosaic world of national risk assessments and prioritisation, which is to be welcomed, in order to replace earlier pressures to create similar laws and institutions to make it look as if one is doing something effective. The difficulty is knowing whether, as part of an end-to-end process of cutting off crime opportunities and disincentivising a ‘career’ in drugs, financial investigation has not succeeded because it has not really been tried in a sustained fashion; or whether it is just another component of drugs enforcement that offers the illusion of impact. Unless there are some transformative shifts in the number of financial investigators and reforms of the court processing of confiscation cases and substantive offences, there can be no step change in the use of financial data in criminal investigation and/or no major increases in proceeds of crime recovery. Research needs to enable clear judgments to be made about what is working and what is not. Before research can accomplish that, there needs to be proper case and data access (as exists in the Netherlands). Therefore, we have to be prepared to shift major resources in that direction or abandon the pretence that financing of crimes and laundering the proceeds are central issues that drive crime and should drive enforcement. We also have to take more seriously the criminal motivations of ‘offend to spend’ rather than wrongly assume that more than a minority of criminals are ‘Protestant Ethic’ entrepreneurs aiming to save and integrate all or most of their income from crime. This has implications for the amount of proceeds that are plausibly available for seizure and confiscation, though it remains important to sort out transnational financial investigation powers and cooperation in dealing with assets, both from criminal and

civil recovery investigations. The European Union (EU) is currently seeking to progress this issue, but mutual legal assistance for financial intelligence, asset freezing and recovery needs to be broader-based than Europe.<sup>54</sup>

Thus far, we have discussed the situation in advanced economies, among whom trust is relatively high. However, the AML movement is global, and the Egmont Group currently (2013) contains 131 FIUs from a vast range of countries. With the right support and independence of investigation, prosecution and trial, financial investigation can be used against elite corruption, drug trafficking and economic crimes: but such support is politically fragile, as the lack of extensive prosecutions following the collapse of the Kabul Bank demonstrates.<sup>55</sup> Regional organisations, periodic international evaluations of AML and mechanisms such as the International Narcotics Control Strategy Report<sup>56</sup> act as bulwarks protecting such independence up to a point, though they may push foreign policy agendas which can inhibit alternative approaches to drug control. But there are strong reasons why a 'one size fits all' model of AML is inappropriate and costly for less developed economies, unless it is needed (to protect other countries) because a less developed country is offering global financial services and serving as a criminal money haven for drug traffickers and economic criminals elsewhere.<sup>57</sup> Trust mechanisms must therefore be developed between the private sector, FIUs and criminal investigators and prosecutors, and this is easier to do in some jurisdictions than in others.

To date, we have only a modest evidenced insight into what the benefits of financial investigation are to weigh against what little is known about the costs of enforcement.<sup>58</sup> This is true of AML generally. Lamenting the poor state of the evidence about costs and benefits of asset forfeiture in the USA, Baumer argues that 'if policy makers are committed to making informed decisions, then it would be wise to invest in activities that

could generate the requisite information'.<sup>59</sup> For once, these reflections on the USA do apply globally. Let us not underestimate the difficulties of linking outputs and outcomes to crimes and to financial investigation inputs.<sup>60</sup> That methodology remains to be developed. However there needs to be a much stronger focus on understanding the evolution and/or stasis of patterns of laundering, how and when financial investigation is actually delivered and used by law enforcement and prosecutors, and the use made of suspicious activity reports, and actual cooperation between Asset Recovery Offices and courts internationally, if any of the grand ambitions and claims made in political gatherings and annual reports are to be grounded in real resources on the ground. Some economists test revealed preferences by 'willingness to pay' models, and our willingness to pay for more *public* resources has been quite modest: many of the costs are transferred (perhaps correctly) to the 'financial polluters' in the private sector, but the private sector alone – whether an enthusiastic or, in some cases, a very reluctant partner – cannot deliver a full package to keep any type of crime under a 'satisficing' level of control.

Historically, criminal justice has been about 'pursue' rather than 'prevent' strategies, and in that framework, using financial investigation more efficiently to prosecute 'bad' people and deliver justice by taking away their liberty and their benefits from crime is itself a good thing. Alongside visibly controlling tax evasion and social security fraud, consumer fraud and environmental waste dumping, showing the public that others do not benefit from crime *could* influence their behaviour as well as being popular. But on current evidence, the contribution of financial investigation to the 'prevent' strand of crime reduction policy is unproven. No-one could rationally think that AML controls in general or financial investigation in particular will 'solve' the drugs problem completely or eliminate high-level drug trafficking: to achieve that, there would need to

be a step change in transparency and effective action against high-level corruption along all possible supply chains. However more progress on these will facilitate interventions against the more harmful individuals, networks and crime enablers. The less complex financial activities of local drug-dealing gangs can be intervened against, without needing international cooperation or familiarity with sophisticated money laundering typologies. There will always be tensions between different interests and rights, and sometimes, vigorous efficiency in the pursuit of some rights produces global bads as well as goods. But there is no point in having a strategy if one has no road map for how to get from here to there.

## Recommendations

With this in mind, a number of recommendations can be made, which apply more readily to developed economies:

- Consideration needs to be given to the more routine mainstreaming of financial investigation and confiscation, and to its impact at different levels of criminal organisation, including local and regional networks – but this requires a sea change in supervisory attitudes and, in some countries, prosecutor and judicial training; and independent monitoring needs to be built into such developments to avoid goal displacement
- The term ‘money laundering’ may conjure up too complex and vague an image to fit the reality, and ‘crime money management’ may be a productive alternative term

- Many criminals ‘offend to spend’ and this needs to be factored into the realism of the large guesstimates of national and global money laundering *and savings from crime* as measures of what financial measures against drug dealing/trafficking are capable of achieving
- More focus should be given to understanding the evolution of patterns of laundering, how financial investigations are deployed, and the appropriate making and enforcement use of suspicious activity reports
- Financial investigation and proceeds confiscation/recovery can impact upon public reassurance and safety; on the behaviour of financial intermediaries, and on both the behaviour and criminal capacity of drug offenders – these goals need to be separated out
- The money laundering risk assessments and the focus on effectiveness in the FATF Methodology 2013 should be used to re-appraise financial investigation strategies and concrete practices, in the context of drugs trafficking, economic crimes, and the increasing trend towards poly-crime activities of crime networks.

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## **Modernising Drug Law Enforcement Project**

***A project by IDPC, with the participation of the International Security Research Department at Chatham House and the International Institute for Strategic Studies***

Drug law enforcement has traditionally focused on reducing the size of the illicit drug market by seeking to eradicate drug production, distribution and retail supply, or at least on the stifling of these activities to an extent that potential consumers are unable to get access to particular drugs.

These strategies have failed to reduce the supply of, or demand for, drugs in consumer markets. Given this reality, and a wider policy context where some governments are moving away from a 'war on drugs' approach, drug law enforcement strategies need to be adjusted to fit the new challenge – to manage drug markets in a way that minimises harms on communities. A recognition that law enforcement powers can be used to beneficially shape, rather than entirely eradicate, drug markets is being increasingly discussed.

The objective of this project is to collate and refine theoretical material and examples of new approaches to drug law enforcement, as well as to promote debate amongst law enforcement leaders on the implications for future strategies.<sup>61</sup> For more information, see: <http://idpc.net/policy-advocacy/special-projects/modernising-drug-law-enforcement>.

## Endnotes

- 1 Though the United Nations Office on Drugs and Crime (2011), *Estimating illicit financial flows resulting from drug trafficking and other transnational organized crime* (Vienna: United Nations) shows that the drug market did not shrink while the prices of most commodities declined. Discussion of the effectiveness of controls on financing of terrorism and WMD proliferation is not within the scope of this essay.
- 2 Available at: <http://www.unodc.org/unodc/treaties/CTOC/>
- 3 Available at: [www.levin.senate.gov/download/?id=10975287-7e5b-4753-ae48-5232de062a58](http://www.levin.senate.gov/download/?id=10975287-7e5b-4753-ae48-5232de062a58)
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- 5 We can attack criminal organisations without reducing levels of crime – indeed, after disturbances in established organisations, violence may be expected to increase as rivals jockey for dominance
- 6 Once such guesstimates are published and uncritically accepted, it becomes difficult politically to produce a lower figure, even if that is much more accurate/analytically plausible. Dubourg, R. & Prichard, S. (eds.) (2009), *Organised crime: Revenues, economic and social costs, and criminal assets available for seizure* (London: Home Office) estimated the amount of UK proceeds of crime available in the UK for confiscation at £2 billion, a tenth of the lower band figure of the UK estimate for organised crime costs. An earlier UK study had estimated proceeds of property crime to be £1.497 billion in 1992 with the much more modest figure of £460 million 'open to confiscation' (Levi, M. & Osofsky, L. (1995), *Investigating, freezing and confiscating the proceeds of crime* (London: Home Office, p. 6). Readers should note that it is a mistake simply to contrast harm figures with laundering or with confiscatability figures, since harm is usually far greater than proceeds of crime (depending, of course, on what view one takes of the harm of consensual prohibited activities). Proceeds of crime are gross turnover data, and to generate a 'realisable benefit' figure need to be reduced to take account of lifestyle expenditures as well as criminal business costs including corruption, staff, and transport. For more information, see: Levi, M., Innes, M. & Reuter, P. (forthcoming 2013), *The economic, financial & social impacts of organised crime in the EU* (European Parliament)
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- 9 Gilmore, W. (2012), *Dirty money*, 3<sup>rd</sup> ed. (Strasbourg: Council of Europe)
- 10 See: Halliday, T., Levi, M. & Reuter, P., (2013), *Assessments of anti-money laundering and combating the financing of terrorism*, (Chicago: American Bar Foundation); Levi, M. & Reuter, P. (2006), 'Money Laundering', in M. Tonry (ed.), *Crime and justice: A review of research*, **34**: 289-375, (Chicago: Chicago University Press)
- 11 Though criminal record flows across borders are often uneven, and the reluctance to prosecute corporations even in those jurisdictions that have corporate criminal liability means that there are often only administrative records of 'corporate criminal careers'. Flows of administrative records across jurisdictions are also uneven
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- 53 In US Federal law, even spending for immediate consumption can constitute money laundering if the party has the requisite knowledge that the funds and proceeds of crime
- 54 For an early thoughtful discussion of process issues in an international context, grounded in acute observation, see: Kennedy, A. (2006), 'Designing a civil forfeiture system: An issues list for policymakers and legislators', *Journal of Financial Crime*, **13**(2): 132-163
- 55 See: Levi, M. (2012), 'How well do anti-money laundering controls work in developing countries?' In: Reuter, P. (ed.), *Draining development? Controlling Illicit flows from developing countries* (Washington DC: World Bank Press), pp. 373-414, n. 19; Ribadu, N. (2010), *Show me the money: Leveraging anti-money laundering tools to fight corruption in Nigeria* (Washington DC: Center for Global Development), <http://siteresources.worldbank.org/EXTPUBLICSECTORANDGOVERNANCE/Resources/Showmethemoney.pdf?resourceurlname=Showmethemoney.pdf>. This IDPC report does not deal with Grand Corruption that is not specifically connected with illicit drugs, though many systemically corrupt countries may serve as attractors for the drug trade. The Independent Joint Anti-corruption Monitoring and Evaluation Committee conducted a major investigation into the collapse of the Kabul Bank, but this revealed that it was more the result of elite embezzlement/insider loans of US\$900 million – little of it recovered – than about specific drug money laundering. Two senior bankers received five year prison sentences in 2013, but it was widely felt that the prosecutions were too narrowly drawn
- 56 U.S. Department of State (2013), *2013 International Narcotics Control Strategy Report, Volume II: Money laundering and financial crimes*, <http://www.state.gov/j/inl/rls/nrcrpt/2013/vol2/index.htm>
- 57 See: Halliday, T., Levi, M. & Reuter, P., (2013), *Assessments of anti-money laundering and combating the financing of terrorism* (Chicago: American Bar Foundation)
- 58 Sproat, P.A. (2009), 'Payback time? To what extent has the new policing of assets provided new assets for policing', *Journal of Money Laundering Control*, **12**(4): 392-405, at p. 401
- 59 Baumer, E. (2008), 'Evaluating the balance sheet of asset forfeiture laws: Toward evidence-based policy assessments', *Criminology & Public Policy*, **7**(2): 245-256, at p. 252
- 60 See Halliday, T., Levi, M. & Reuter, P. (2013), *Assessments of anti-money laundering and combating the financing of terrorism* (Chicago: American Bar Foundation), n. 53
- 61 Dave Bewley-Taylor is the editor of the Modernising Drug Law Enforcement project publication series

The International Drug Policy Consortium (IDPC) is a global network of NGOs and professional networks that promotes objective and open debate on the effectiveness, direction and content of drug policies at national and international level, and supports evidence-based policies that are effective in reducing drug-related harms. IDPC members have a wide range of experience and expertise in the analysis of drug problems and policies, and contribute to national and international policy debates.

Since the 1980s, there has been a major push in rhetoric and institution-building, emphasizing the centrality of attacking the financial lifeblood of drug trafficking networks and organised economic crimes. Much progress has been made in legislation and the creation of financial intelligence units. However, easier guidance is needed on how to get information overseas, and delays in international cooperation lead to under-exploitation of financial investigation opportunities. This report makes no claim to be offering a certain route to success, but is offering an overview of some better and some false steps that have been undertaken in the field of drug law enforcement and financial investigation strategies.

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