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Foreword | *In order to transfer money, people in Western societies have, for many years, relied on conventional banks and other financial institutions. In addition to ordinary banking, however, money and other forms of value can be transferred through the use of so-called remittance services which have operated for hundreds of years in non-Western societies. Until recently, these alternative systems have been largely unregulated with users and providers of services relying on trust and community ties to ensure reliability and efficiency in moving funds between countries. Since the terrorist attacks of 11 September 2001, however, governments have increased regulation of the formal banking sector and extended these controls to alternative remittance providers. This paper examines the operation of alternative remittance systems in Australia and considers the risks that they entail for illegal movement of the proceeds of crime and financing of terrorist activities. It suggests measures that could be put in place to address these risks, including increased contact between the Australian Transaction Reports and Analysis Centre and the remittance providers, and the possible role which communities could play in facilitating this contact and in maintaining a degree of informal supervision of the alternative remittance industry.*

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Alternative remittance systems in Australia: Perceptions of users and providers

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People and businesses wishing to transfer money between parties can make use of a variety of procedures. In addition to using simple cash transactions, most money transfers in Western societies take place using conventional banks and other financial institutions. In addition to ordinary banking, however, money and other forms of value can be transferred through the use of so-called remittance services. Originating in southeast Asia and India, and known by terms such as *hawala*, *hundi*, *fei-ch'ien*, *hui* and *phoe-kuan* (Passas 2005), users of these systems transfer funds through the use of agents who enter into agreements with each other to receive money from people in one country (such as overseas workers) and to pay money to specified relatives or friends in other countries without having to rely on conventional banking arrangements. Funds can be moved quickly, cheaply and securely between locations that often do not have established banking networks or modern forms of electronic funds transfers available.

Because such systems operate outside conventional banking systems, they are known as 'alternative remittance', 'underground' or 'parallel banking' systems. They are legitimate and legal in many countries, although concerns have arisen in recent years that they could be used to circumvent anti-money laundering and counter-terrorism financing (AML/CTF) controls that now operate across the global financial services sector. Particular risks arise from the irregular forms of record-keeping which are often adopted and the possibility that the laws of every country in which they operate may not be fully complied with.

The heightened awareness of how terrorist activities are financed has led governments in developed countries to include alternative remittance systems/service(s) (ARS) within the regulatory controls that apply to conventional banks. In Australia, for example, the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (Cth) (AML/CTF Act) classifies the provision of alternative remittance as a designated service which requires providers to not only report suspicious matters to the Australian Transaction Reports

and Analysis Centre (AUSTRAC), but also to register with AUSTRAC before designated remittance services can be provided. This legislation places remittance providers under the same obligations as other reporting entities. This includes obligations to adopt anti-money laundering and counter-terrorism financing programs, submit transaction and suspicious matter reports, and file annual compliance reports with AUSTRAC.

It is important, however, to achieve a balance between regulating the remittance sector in an attempt to reduce the flow of illicit funds and permitting its continued use as a legitimate alternative to the conventional banking system—especially for those in less-developed countries who may suffer from under-developed financial sectors or poor governance. Remittance systems provide many ethnic communities with the ability to send money and/or goods back to their country of origin, usually to their families who remain there, and who may be dependent on receipt of such transfers. Remittance systems are also used for a variety of other commercial and social reasons. The remittance industry in Australia includes corporate remitters such as Western Union and large remitters such as Dahabshill, that service a particular country or region and maintain a large number of agents and sub-agents, and other remitters (including sole traders) that service a particular region or country. Many small remitters run businesses such as grocery stores or DVD stores and provide ARS as an adjunct to their main business.

This paper provides a review of the operation of ARS in Australia and an examination of the risks that they entail for illegal movement of the proceeds of crime and financing of terrorist activities. It also examines the measures being used to regulate such systems around the world and whether these are effective in reducing risks of criminality. This paper considers possible measures to increase both AML/CTF compliance by the remittance sector and how to address consumer concerns relating to issues such as fraud within the sector.

The alternative remittance process

The basic process for an alternative remittance transaction is simple. For example:

- Person A in Australia wishes to send \$10,000 to Person B in India.
- Person A pays the \$10,000 to an ARS provider in Australia and is given a code or number to relay to Person B.
- The Australian ARS provider instructs a counterpart in India to pay \$10,000 to Person B upon receipt of the code.
- The funds are paid in India to Person B, although money has not left Australia.

The Australian ARS provider now owes the Indian ARS provider a debt, which can be paid in a number of ways such as under- or over-invoicing, a transfer of funds through a bank account or cash payment through a courier. Passas (2005) has noted that ARS involve varying degrees of contact with the formal banking system with many ARS providers using bank accounts.

The reality is far more complicated, however, as there are often multiple transactions involved as well as various intermediaries.

Regulation

As a result of the terrorist attacks of 11 September 2001, alternative remittance has come under scrutiny due to concerns that it may be used for illegal activities such as money laundering or financing of terrorist activities. Risks of misuse may be enhanced due to the formal banking sector experiencing increased regulation in recent years.

In 1989, the G7 heads of state and the President of the European Commission, established the Financial Action Task Force (FATF), to study and monitor the impact of money laundering and to produce guidelines for its control. Forty initial recommendations were issued in 1989 and a further nine Special Recommendations concerning the financing of terrorism were added between 2001 and 2004 in response to the events of 11 September 2001 (FATF 2004).

Special Recommendation VI (SR VI), which deals specifically with alternative remittance, recommends that both the 40 Recommendations and the Special Recommendations be applied to those who provide ARS, that jurisdictions take measures to ensure that those who transmit money or value be registered or licensed and that providers be subject to administrative, civil and criminal penalties if they do not abide by the regulatory regimes in place. FATF noted that these recommendations should be introduced to ensure they impose the minimum burden necessary on both providers and users of ARS. Further, that jurisdictions should be mindful of both the benefits provided by the alternative remittance industry and the undesirability of driving the remittance industry underground (FATF 2003a).

Countries have responded in a variety of ways to SR VI and current regulatory arrangements include registration through a federal law combined with possible licensing at the state level (United States), registration combined with a fit and proper person test for owners and managers of an ARS (United Kingdom) and registration (Australia and Canada). The success of these arrangements is still being assessed.

Using the 40 Recommendations and the nine Special Recommendations as benchmarks, FATF conducted a mutual evaluation of Australia's financial arrangements in 2005 and found that Australia's anti-money laundering regime was inadequate in a number of areas. As a result, new legislation, the AML/CTF Act, introduced the requirement that remittance providers register with Australia's financial intelligence unit and AML/CTF regulator, AUSTRAC, that they introduce programs to train their staff in AML/CTF issues and that they take greater responsibility for monitoring the behaviour of their customers throughout the business relationship.

Remitters are required to register with AUSTRAC and are placed on the Provider of a Designated Remittance Service (PoDRS) Register. PoDRS are the only providers of designated services who are obliged to

register with AUSTRAC. As at 4 February 2010, there were 5,891 PoDRS registered with AUSTRAC (AUSTRAC unpublished data).

On 4 November 2009, AUSTRAC issued its first remedial direction to an ARS provider. This arose because of non-compliance with AML/CTF legislation by failing to have an effective AML/CTF program in place. Under the terms of the remedial direction, the non-compliant provider was required to submit to AUSTRAC an AML/CTF program that assessed its exposure to AML/CTF risks and by doing so, took account of issues such as the types of customers dealt with, the services offered, its methods of delivering these services and the foreign countries it deals with in the course of its business. The remedial direction stipulated that the provider perform background checks on staff and train staff regarding relevant AML/CTF risks and that the business address customer identification and verification requirements (AUSTRAC 2009b).

The current research

The Australian Institute of Criminology (AIC) has conducted research to examine the manner in which ARS operates within Australia, the extent to which such systems are used and why, the factors that may inhibit or enhance compliance with regulatory requirements, whether ARS is used to facilitate money laundering or terrorism financing and how the risks of abuse can be minimised.

Methodology

Research was conducted with representatives of the Somali, Samoan, Vietnamese, Indian and Filipino communities in Australia. These communities were selected on the basis of factors such as their size, the length of time they have been present in Australia and the degree to which they are involved in the payment of remittances.

The research was undertaken by independent consultants in Sydney and Melbourne and involved conducting individual interviews with the providers

of alternative remittance and a mixture of individual interviews and focus groups with users. Thirty-three out of 5,891 ARS providers who have registered with AUSTRAC since December 2006 and 134 community members were interviewed for the research. The relatively small number of participants suggests that only tentative conclusions should be drawn from the findings.

Results

Extent of usage

It is difficult to quantify the size of the world remittance industry because it uses both formal channels (such as Western Union) and informal methods, which are often under-reported. The World Bank calculated that recorded remittances flowing from the developed to the developing world in 2007 amounted to at least US\$240b and that there was a substantial amount of under-reporting. The World Bank suggested that the 2007 figure represented more than double the level of use in 2002 (Ratha et al. 2007). However, in November 2008, the World Bank revised its 2007 estimate to US\$265b, while also commenting that remittance flows were starting to slow in the third quarter of 2008 (Ratha et al. 2008).

Use of the remittance industry

The AIC research demonstrated that the five communities all considered remittance to be an important and legitimate practice, but reported using different kinds of remitters. The Indian community largely used corporate remitters such as Western Union. The Vietnamese and Filipino communities used ARS providers, who, particularly in the case of the Filipino community, were members of the same community as their customers. The Somalis used a variety of remittance providers (many of them non-Somali in origin) and the Samoans also used a variety of remitters.

ARS users noted that ARS was faster, cheaper and more reliable than either banks or corporate remitters and was used by groups and individuals within the community. The amount of value remitted, the frequency with which remittances were sent and the

reasons for using ARS differed between individuals and groups. One Vietnamese participant who used a Vietnamese provider commented:

These [ethnic-specific providers] are reliable. When we become regular customers, we can even phone them to ask for a transfer and pay them later on our next shopping trip. There are no questions asked and there's no more paperwork required.

The most common reason for sending remittances was support of family (close and extended) in the country of origin, and, to a lesser extent, support of local communities. Some users (particularly Vietnamese and Indian) employed ARS to send value for business purposes. It was common for remittances sent by first generation Australians to be substantially lower than that of their parents and a number of first generation participants expressed concern that their parents sent excessive sums of money overseas.

Alternative remittance and crime

Very few users of ARS reported any difficulties when they used ARS providers, although a number cited either general concerns about the process (such as what would they do if money did not reach its destination) or had heard anecdotes about ARS users who had been cheated. Their comments suggested a number of factors that may militate against ARS being abused. These included the fact that the supplier and the user often know each other and that the user can often contact their family overseas to ensure that the money has arrived. Commentators have noted that this emphasis on trust and personal contact may both dissuade people from trying to infiltrate the system and act as a deterrent to providers who might be tempted to send money of dubious or unknown origins. The effectiveness of these countervailing factors is debatable and would depend upon the number and personal knowledge of the individuals involved (Passas 2008, 2005). There have been cases in both Australia and overseas where ARS providers and users have used ARS for criminal activity.

Case 1: *Liaquat Ali, Akhtar Hussain and Mohsan Khan Shahid Bhatti v R* [2005] EWCA Crim 87. In this case, 11 people were sentenced to imprisonment in 2008 following convictions on charges of money laundering relating to the use of three travel firms based in Bradford, United Kingdom. An investigation conducted by Her Majesty's Revenue and Customs found that these firms had used alternative remittance mechanisms to illegally launder millions of pounds, much of which had been derived from drug trafficking. The investigation relied on evidence from a range of sources, including reports from financial institutions reporting large transactions by the three businesses and surveillance showing large sums of cash being dropped off at the firm's branches in Yorkshire. Estimates of the amount of money involved ranged up to £500m. Some of the defendants argued, in part, that there was little understanding of how much money a legitimate money value transfer business could generate and that the amount involved did not, of itself, demonstrate any wrongdoing. They also commented that the cash had been accumulated by intermediaries and that they had no idea of the money's origins or how it had been raised.

Case 2: *A Ansari v R, H Ansari v R* [2007] NSWCCA 204. In this case, the Ansari brothers ran a Sydney-based remittance business called Exchange Point, which received cash deposits from Australian customers and placed them in a cash pool. The Ansaris would then instruct associates to make equivalent sums available to these Australians when they travelled overseas.

The Ansaris simultaneously received instructions from overseas customers regarding the payments of funds into Australian accounts. They used the cash pool to make these payments, which were often in sufficiently small amounts to avoid Australian reporting requirements. The negotiations on these transactions were conducted over mobile phones and no records were kept. The Ansari brothers were convicted of offences under the *Criminal Code 1995* (Cth) relating to money laundering.

Case 3: On 17 December 2009, seven people were sentenced in the County Court of Victoria to terms of imprisonment ranging up to 12 years for attempting to launder up to \$68m dollars through the Long Than Money Transfer Company and associated cash remittance businesses in Sydney and Melbourne.

AUSTRAC has produced a number of typologies based on cases in which ARS customers and providers have been involved in illegal activity (AUSTRAC 2009a, 2008, 2007). The AUSTRAC *Typologies and Case Studies Report 2009* identified eight cases related to large-scale criminality committed through remittance (AUSTRAC 2009a).

Alternative remittance and terrorism financing

An important finding of the AIC research was that the evidence regarding misuse of ARS largely relates to criminal activities. There is little evidence of systematic use for the financing of terrorism, although the lack of reporting in this area makes it difficult to estimate ARS involvement. However, in the course of focus groups and interviews, ARS users raised concerns about their liability when remittances are sent overseas and then used for, or in support of, terrorist actions. They demonstrated little knowledge of current Australian legislation on this issue, and stated that they would appreciate guidance on how the law operates in this area and under what circumstances senders of remittances could be subject to prosecution.

The vulnerabilities of alternative remittance

Other potential vulnerabilities of ARS as it operates in Australia often appear to relate more to a lack of knowledge than deliberate misconduct. Many users expressed general support for the proposition that ARS providers should be subject to some form of government regulation, and assumed that such regulation was in place, although they often had little idea of the form it currently took. Users generally saw regulation as a positive development because they perceived it would provide them with a

degree of protection against fraudulent behaviour and did not understand that the Australian AML/CTF regime is concerned with protecting the remittance sector from AML/CTF activity and not consumer protection.

Very few of the user participants had any understanding of the current registration system applying to ARS providers and thus had not ascertained whether their provider had registered with AUSTRAC or not. One Filipino user participant commented:

Sometimes we know the person but we don't feel we can ask them if they are registered because it might offend. It is a matter of trust. We are not culturally open to asking questions. We just want to know that the money will get through.

As would be expected, both the corporate remitters and ARS providers who participated in the study, were generally more familiar with the registration requirements than many users. They were also aware of the reporting requirements imposed by AUSTRAC relating to matters such as overseas or suspicious transactions and those over certain monetary limits. However, they often had little knowledge of how the overall remittance industry functioned even when they were agents for a larger remittance organisation. They stated that they complied with current registration requirements because they wished to abide by Australian law, but could see no positive benefits to registration. Overwhelmingly, they said they would not transfer money if illegality was involved, but they had mixed views on whether they would report such a request to authorities. Their reluctance was based on a fear of potential harm to their businesses and the possibility of making enemies.

Both providers and users of ARS had some knowledge of local remittance practices, particularly with regard to ARS. Providers were aware of competitors who had not registered or did not fulfil reporting obligations and resented the possibility that such competitors could offer lower fees because they did not have to outlay resources on compliance arrangements.

Users were aware to some extent of those providers considered unreliable and tended to avoid them. Community media outlets are regularly used to obtain information on the behaviour and reliability of ARS providers. One Filipino user participant commented that:

We will check by trying them out with a small sum of money because they are usually referred by word of mouth. When we know that the money will get to our family we can send larger amounts.

Some users commented that agents and sub-agents of larger organisations did not always behave ethically, which raises the issue of how effectively many principal agents supervise the training and behaviour of sub-agents. Users expressed support for the introduction of a mechanism by which they could report providers whom they believed were not in compliance with regulatory requirements or otherwise acting wrongly, anonymously if necessary. Such a mechanism could also be used by other providers.

It appears that there are several strands of ARS operating simultaneously, with the large majority of legitimate transactions conducted through honest providers and a smaller number of transactions conducted by providers who are aware that the transactions they process are criminal in nature. Such remitters may simply be fronts for criminal activity.

However, the extent to which many providers are prepared to deal with both sorts of transactions is not clear. There is concern that some providers maintain two sets of records and charge two different rates of commission depending upon the character of the transaction. Innocent ARS providers are potentially vulnerable to a criminal ARS user who employs a number of different remitters and/or banks.

The AML/CTF Act is intended to address these concerns by placing a greater onus on providers to monitor the behaviour of their customers. Some ARS providers emphasised that many providers may need assistance to satisfy the increased level of regulation, and that such assistance

could take the form of initiatives such as assistance to obtain new monitoring software.

Engaging the community

AUSTRAC is currently undertaking an education program which involves providing information sessions to ARS providers. Although it's currently beyond AUSTRAC's mandate, it may be productive for AUSTRAC or others to widen educational measures to include ARS users. It is clear that the remittance user community has little understanding of the regulatory system currently applied to ARS. The user community is strongly protective of the remittance system, yet appears to support the need for regulation. Many users expressed interest in obtaining more information about current regulatory arrangements and the policies and legal obligations and responsibilities relating to the remittance system. Some communities could, initially, be hesitant in dealing directly with government representatives and that to engage successfully with communities, culturally-tailored approaches, which may vary from community to community, would need to be employed. Verbal communication is likely to be more effective than written guidance material, arguably, and independent third parties with knowledge of particular communities should be used to act as intermediaries and facilitators in any consultation process.

It also appears that providers have varying degrees of knowledge of current regulatory requirements. Anecdotal evidence suggested that at least some providers may struggle to satisfy these requirements and that providers would welcome assistance from the regulator in obtaining both greater knowledge of their obligations and practical assistance in meeting them. This assistance would need to be provided in a culturally-sensitive way to communities.

While many users had considerable trust in their providers, they took precautions such as contacting recipients in their countries of origin to ensure that remittances had been received. Although they had some

mechanisms for researching the behaviour of providers, their lack of knowledge of regulatory requirements meant they had no knowledge of whether their provider was at risk of prosecution for failing to register as required as a PoDRS and had fulfilled relevant regulatory requirements.

Feedback from providers suggested that the most effective way to influence provider behaviour is through community pressure. Others have identified the difficulty of persuading providers to take part in research or a public function such as a conference (Passas 2005).

Given that comments from users suggested that they have expectations regarding the need for providers to abide by relevant legislation and regulations, one approach that may prove effective is to educate the community as to the standards ARS should meet. As one ARS provider participant commented:

You could focus on providers but the real emphasis should be on the community. They are a very powerful force. If they think you are not doing the right thing by them, then they will make sure everyone in the community knows about this. This means that the business will eventually dry up. The problem is when it's not about the quality of the service but the fact that the person hasn't registered. So you really do need to start within the community.

Another ARS provider suggested:

If you could show these providers who haven't registered that the community is becoming more aware of the law, then it's easier to be saying to them that it makes good business sense to comply with these new rules and regulations.

Conclusion

A number of countries including Australia have adopted AML/CTF regulatory regimes for remittance providers, at least partly

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in response to the lack of compliance with FATFs recommendations. Regulatory regimes in this sector are relatively new and their effectiveness is still being evaluated. These regulatory regimes are intended to prevent certain kinds of conduct, rather than to protect or foster the remittance system. Yet the communities that use ARS see the practice as important and legitimate, and as superior in performance to the formal banking system. It is possible that a greater level of community involvement may be a very valuable adjunct and, in some cases, perhaps could be seen as an alternative to other regulatory systems such as registration, licensing and 'fit and proper' person tests. Another possible initiative could be to establish a public list of registered ARS providers.

The evidence relating to misuse of ARS regarding money laundering, the financing of terrorism and risks of fraud, is fragmentary. It is apparent that there has been some misuse (more commonly by criminal rather than terrorist elements) but it is difficult to quantify how much. To varying degrees, the current regulatory framework in many countries imposes a burden on ARS providers and runs the risk of criminalising a large number of them if they do not comply with regulatory requirements.

It is apparent that the ethnic communities who use ARS in Australia are highly supportive of regulation but have very little knowledge of Australia's current AML/CTF regulatory regime. However, they expect a certain level of conduct and service from ARS providers. Evidence from both users

and providers of ARS suggests that the most effective way of increasing the compliance of providers with current AML/CTF regulatory arrangements is to interact with the communities that use their services. This contact will need to involve approaches that emphasise verbal rather than written communication, including forums or roundtables and intermediaries with specific knowledge of the structure and culture of the communities involved, and it may also need to involve consideration of initiatives such as reporting systems and publicly available lists of PoDRS to increase consumer protection for ARS users.

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