



FATF REPORT

# **Money laundering / terrorist financing risks and vulnerabilities associated with gold**

July 2015





The Financial Action Task Force (FATF) is an independent inter-governmental body that develops and promotes policies to protect the global financial system against money laundering, terrorist financing and the financing of proliferation of weapons of mass destruction. The FATF Recommendations are recognised as the global anti-money laundering (AML) and counter-terrorist financing (CFT) standard.

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## GLOSSARY OF TERMS AND ACRONYMS

|                        |                                                                         |
|------------------------|-------------------------------------------------------------------------|
| <b>AML</b>             | Anti-money laundering                                                   |
| <b>APG</b>             | Asia/Pacific Group on Money Laundering                                  |
| <b>ASM</b>             | Artisanal or small-scale mining (ASM)                                   |
| <b>DNFBPs</b>          | Designated non-financial businesses and professions                     |
| <b>EAG</b>             | Eurasian group on combating money laundering and financing of terrorism |
| <b>FIU</b>             | Financial intelligence unit                                             |
| <b>FSRB</b>            | FATF-Style Regional Body                                                |
| <b>Gold Bullion</b>    | Refined gold, valued by weight                                          |
| <b>Gold Ingot</b>      | Block of gold, usually in the shape of a bar                            |
| <b>HSI</b>             | Homeland Security Investigations (United States)                        |
| <b>Investment gold</b> | Particular class of gold with a specific purity                         |
| <b>LEA</b>             | Law enforcement agency                                                  |
| <b>LSM</b>             | Large-scale or medium-scale mining                                      |
| <b>MENAFATF</b>        | Middle East & North Africa Financial Action Task Force                  |
| <b>ML</b>              | Money laundering                                                        |
| <b>STR</b>             | Suspicious transaction report                                           |
| <b>TBML</b>            | Trade-based money laundering                                            |
| <b>TF</b>              | Terrorist financing                                                     |

## EXECUTIVE SUMMARY

This joint FATF–Asia/Pacific Group on Money Laundering (APG) research project into the gold sector arose as a result of the apparently natural transition or displacement of money laundering (ML) and terrorist financing (TF) from the formal financial sector and the cash market to the gold market, as regulators and law enforcement harden those environments.<sup>1</sup>

**Chapter 2** identifies the features of gold that make it attractive to criminal organisations as a mechanism to move value.

**Chapter 3** maps the nature, source and scope of gold production, markets and trade, to assist practitioners to recognise the common predicate offences (such as theft, smuggling, fraud, illegal schemes and tax evasion) that occur in the gold market. A good understanding of how these activities operate is required to recognise the ML and TF activity that is being perpetrated.

**Chapter 4** builds a library of ‘red flag’ indicators that could assist designated non-financial businesses and professions (DNFBPs), financial institutions and others in identifying and reporting suspicious activities associated with ML and TF in the gold sector.

The key findings of this report are intended to promote effective risk mitigation and preventative measures or encourage further work on areas requiring further investigation.

### Key findings:

- Gold is an extremely attractive vehicle for laundering money. It provides a mechanism for organised crime groups to convert illicit cash into a stable, anonymous, transformable and easily exchangeable asset to realise or reinvest the profits of their criminal activities.
- The gold market is a target for criminal activity because it is highly lucrative. Understanding the various stages of the gold market continuum, and the types of predicate offending that can occur in each stage, is critical in identifying money laundering and terrorist financing risks emanating from this industry.
- Further research is required to establish the impact of regulation on detecting and discouraging criminal activities in the gold market, and the potential links between the gold market and terrorist financing. Such research into the correlation between financial flows and the gold market will also lead to a better understanding of how criminals use gold and gold products to launder money.

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<sup>1</sup> See also, *Money Laundering and Terrorist Financing through Trade in Diamonds* Report, FATF (2013a).

## 1. INTRODUCTION

Gold has been used in various cultures since antiquity as a medium for exchange or payment. Historically, governments minted coins out of a physical commodity such as gold, or would print paper money that could be redeemed for a set amount of physical commodity (Gold standard). Most modern paper currencies are referred to as ‘fiat currencies’. They have no intrinsic value and are used solely as a means of payment. Even with the modern use of fiat money, precious metals remain an alternative means of payment due to their high intrinsic value and ease of exchangeability.

Recent shifts in the global economy have resulted in an increased demand for stable-value investments and commodities. Gold is a universally accepted currency that has remained stable in spite of fluctuations in global financial markets. Internationally enforced anti-money laundering (AML) measures are influencing a shift in criminal behaviours towards methodologies with lower law enforcement visibility, which makes gold very attractive. Further, gold is an integral part of the cultural heritage of many countries, like China and India, where it features heavily in religious and social exchanges.

As with the diamond sector, the gold sector (via dealers in precious metals) is covered under the FATF Standards by Recommendation 23 - Designated Non-Financial Businesses and Professions (DNFBPs). However, like the diamond sector, it is different from other DNFBPs.

This paper is not intended to describe the various elements of the gold market continuum - it is complex and there are a number of papers that cover this topic comprehensively. In order to effectively understand gold market vulnerabilities, this report should be read in conjunction with, for example:

- *The Direct Economic Impact of Gold*<sup>2</sup> - written by PriceWaterhouseCoopers and commissioned by the World Gold Council which is working diligently to improve governance and compliance of the entire gold industry. This paper provides a unique look at the entire gold value chain.
- *The Gold Paper*<sup>3</sup> authored by the British Jewellers’ Association and the National Association of Goldsmiths.

In addition to reviewing existing literature on the gold sector, this report is the result of extensive consultation with the international public and private sector via:

- *Survey responses from public and private sector participants involved in the gold market.*  
Separate questionnaires were directed at both the Government and private sectors, circulated through FATF, APG and other FATF-Style Regional Body (FSRB) jurisdictions, for completion by relevant bodies. Analysis of these responses assisted in identifying or confirming commonalities amongst various jurisdictions regarding the challenges in understanding and tackling the vulnerabilities of the gold market to ML and TF.

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<sup>2</sup> PricewaterhouseCoopers (2013), ‘The Direct Economic Impact of Gold’. Hereafter referred to as the ‘PWC Report’.

<sup>3</sup> British Jewellers’ Association (BJA) and National Association of Goldsmiths (N.G.A) (2013), ‘The Gold Report’. Hereafter referred to as the ‘Gold Paper’.

■ *Case studies provided by law enforcement agencies.*

This report uses the limited number of case studies that were reported to illustrate the operating environment and to help develop 'red flags' to identify ML and TF activity.

## 2. GOLD AS A VEHICLE FOR MONEY LAUNDERING – SIGNIFICANT VULNERABILITIES

There are two broad characteristics of gold and the gold market which make it enticing to criminal groups. The first is the nature and size of the market itself which is highly reliant on cash as the method of exchange. The second is the anonymity generated from the properties of gold which make tracking its origins very difficult to do. These factors make gold highly attractive to criminal syndicates wishing to hide, move or invest their illicit proceeds.

### THE GOLD MARKET IS CASH INTENSIVE

The regulatory characteristics of the gold market in a number of countries make it attractive for organised crime groups to own cash-for-gold businesses in order to place and integrate illicit proceeds. Given the limited level of industry oversight and licencing requirements, cash-for-gold businesses have the potential to provide criminal groups with a continuous supply of untraceable gold commodities from various sources. Furthermore, this supply is purchased at below market cost, directly from the general public—who do not have to prove that they own the second-hand gold presented for sale.

The high-volume, low value transactions conducted through these cash-intensive businesses can be easily falsified or co-mingled with the proceeds of crime, while the purchased gold can be used to make untraceable gold-based payments for illicit goods and services. Because much of the recycled material is purchased in cash, large numbers of transactions are undertaken anonymously.

Individuals who have a need to launder cash, especially those involved in organised crime, are very willing to participate in the cash-for-gold business because there is a high propensity to make a profit and in most jurisdictions there is little governance or oversight of this type of activity. People with no criminal history are also prepared to undertake this activity even if they suspect that the underlying purpose of the activity is ML.

Trade in recycled gold, both legal and illegal, requires little start-up capital and therefore operations can be very itinerant, opening and closing with little difficulty. This adds to the difficulty for regulators to monitor these activities.

Case study 1 illustrates how cash from the sale of drugs is exchanged for gold and smuggled internationally by a third party money laundering syndicate.

#### Case study 1. **Third party gold smuggling syndicate used to launder proceeds of illegal drug sales**

In early 2014, the French police uncovered an international money-laundering network, used to launder the proceeds of the sale of cannabis in the Paris region of France. This case study summarises the findings of the French law enforcement investigation. Moroccan dealers smuggled hash to France and sold it at street level. An Indian national (who was subsequently arrested in

March 2014) organised the collection of the proceeds from the street sales. This money collection (called '*amana*' by the syndicate) was undertaken by so-called '*salafs*' (mules) who were aware that they were dealing with the proceeds of the crime, but not of the crime itself. This was an intentional decision by the group to put some distance between the predicate criminal activity and the *salafs*. This segregation of roles makes it difficult to demonstrate that the money is the proceeds of a specific predicate offence, which is necessary in a number of jurisdictions to prove money laundering.

In this case study, the *salafs* took their orders from the Moroccan drug dealers and supplied the money to the Indian national. The investigation estimated that in a six-month period the *salafs* collected well in excess of EUR 10 million. Whilst the Indian national kept a very low profile in France (he had no official income apart from his wife's social allowances, and lived in social housing in the suburbs of Paris), he held a number of valuable assets in India.

On receipt of the money, the Indian national arranged the transportation of the cash by car to Belgium where it was used to purchase gold and jewellery. The bulk of the cash was deposited in cash into the different accounts of companies associated with an identified gold trader and used to purchase gold from a wholesaler. False invoices generated by the Indian national (in the name of companies set up by him) were used to support the transactions on the gold coins and ingots as well as gold certificates, whenever authorities would question the holder of the gold.

The investigation established two main routes used to move the gold to India.

First route: Both the jewellery and the gold were sent to Dubai using false invoices and fake companies in the UAE. If the transactions were completed without intervention these false invoices were destroyed and if not, then they were used to support the activity. The investigation established that the gold trader kept official records for the sale of 190 kilograms of gold in 11 months with a value of approximately EUR 6 million. However, the investigation calculated the need for gold by the syndicate was closer to 20 kilograms of gold per week. Details of this shortfall of gold were not established.

The Indian national used relatives to transport the gold to India and the UAE with one of the relatives travelling more than 200 times to India and the UAE from 2008 to 2014 (two to three times a month) The head of the India syndicate controlled a travel agency in India which provided flight tickets to the mules and sometimes fake invoices for the purchase of gold. According to information, the gold was not smuggled to Dubai but officially exported and declared to customs, using the false invoices as a cover.

In the first instance the gold was transported to Dubai where it was sold to local people or Indian nationals (via a *hawaladar*). On the sale of the gold the Moroccan drug dealers were paid via controlled foreign exchange operations in Dubai. The physical gold was then smuggled into India, in this instance with the assistance of an employee of a travel agency based in Dubai who recruited mules to undertake the work for a small fee amounting to approximately EUR 220. The investigations identified, couples, elders and on one occasion the use of a 'toddler' to undertake this activity.

A jeweller transformed the gold to make it easier to conceal including mixing gold flakes with coffee,

nickel electrolysis of jewels, and 100 g gold drops for internal concealment.

Second route: An alternate route to transport the gold from Belgium to India was via the international airports of Bangkok and Singapore to a professional Burmese smuggler. The gold was then conveyed through Myanmar to India where it was sold.

Irrespective of the route used, from the moment the money was collected off the streets in France, it took five days for the money launderers to pay back their Moroccan silent partners.

The Indian syndicate's profit was based upon the conversion and resale of gold. By smuggling gold and avoiding taxes, the Indian syndicate was able to sell it competitively and still make a profit. The gold in question was purchased at EUR 31 per gram in Belgium and resold for EUR 36.32 per gram in Dubai or India. The Belgium gold trader received a fee of EUR 325 per kilogram which equated to a profit of EUR 5 000 per kilogram for the syndicate.

This system used by the Indian syndicate was so profitable that the Indian gave up his normal commission of 2.25% on the money laundered. His only desire was to channel as much *amana* as possible in order to buy the gold again and again. Thus he offered the unique opportunity for his Moroccan partner to launder his money at no cost.

*Source: French National Judicial Police (DCPJ)*

Case study 2 below illustrates how buying gold for cash can allow criminal organisations to place, layer and integrate funds into the formal financial sector.

#### **Case study 2. Trading in gold to legitimise the proceeds of drug trafficking**

The United States Homeland Security Investigations (HSI) uncovered a scheme where illicit proceeds from a drug trafficking organisation were being used to purchase gold.

A criminal organisation in the US was buying gold from various precious metals retailers using illicit proceeds from narcotics sales. The gold was then sold to a precious metals broker who then sold it to other businesses.

The proceeds of the sale were then wired to a third party out of the US with links to the drug trafficking organization, thus completing the money laundering cycle.

*Source: US-HSI*

### **GOLD CAN BE TRADED ANONYMOUSLY AND TRANSACTIONS ARE DIFFICULT TO TRACE AND VERIFY**

As the following case study from Belgium illustrates, many transactions involving gold occur anonymously, with little to no record identifying the seller, or purchaser, of gold. This means that law enforcement agencies have little to assist them to identify what the source of the gold is or the identity of the person who sold it. It may be difficult to refute false claims about the source of gold due to the challenges in correctly identifying gold.

**Case study 3. Buying and selling gold anonymously**

A wholesaler in precious metals (wholesaler A), held various bank accounts in Belgium. Analysis of these accounts showed that the wholesaler mostly paid suppliers of precious metals in cash. Over the period of one year a total amount in excess of EUR 800 million was withdrawn in cash. The account mainly received payments from a Belgian bank for purchases of bullion gold.

Company/trader B supplied used gold to wholesaler A and is paid in cash. Company/trader B also pays its gold suppliers in cash. In its financial records, company/trader B records the supplying companies as private individuals, without any form of identification. Company/trader B is suspected to be a cover for the owners' illegal activities, i.e. laundering proceeds of crime by exchanging money.

Wholesaler A was known to the police to engage in money laundering. Its customers are apparently mainly shops selling gold in Antwerp, private individuals and intermediaries that were all recorded as "private individuals" in the accounts. Wholesaler A did not ask its customers for any identification nor did he inquire into the origin of the gold. Enquiries established that much of this gold was said to have come from the 'black market' (jewellery theft) as well as from criminal organisations linked to prostitution and drugs. Wholesaler A paid for the gold in cash, larger quantities of gold were split up so the price would never be more than EUR 15 000, the threshold for anti-money laundering / countering the financing of terrorism (AML/CFT) reporting of cash transactions.

Apart from company/trader B, other suppliers of wholesaler A's were also known to the police. This lead to suspicion that wholesaler A was being used to launder criminal proceeds. Providing anonymity and cash payments attract customers from a criminal environment.

*Source: Belgium Financial Intelligence Unit (FIU)*

## **GOLD IS A FORM OF GLOBAL CURRENCY AND ACTS AS A MEDIUM FOR EXCHANGE IN CRIMINAL TRANSACTIONS**

Due to the inherent value of gold, and its worldwide exchangeability, retail gold is often seen as a viable alternative to cash to settle debts and distribute profit from criminal activity. Particular ethnic groups operating international *hawala* networks have been found to use gold as a medium to settle outstanding balances (although such use of gold is not an illegal activity in itself)<sup>4</sup>. Case study 4, highlights that a syndicate leader, who was a former bank manager and had intimate knowledge of the formal banking sector, strategically identified gold as a way to launder money and pay his criminal associates for their services. Similarly, in case study 5, a corrupt official seeks to distort the link between himself and a bribe by asking for the bribe to be paid in gold to his wife.

<sup>4</sup> *Hawala* (and other similar service providers such as *Hundi*) are defined as money transmitters, particularly with ties to specific geographic regions or ethnic communities, which arrange for transfer and receipt of funds or equivalent value and settle through trade, cash, and net settlement over a long period of time (FATF (2013b), *The role of hawala and other similar service providers in money laundering and terrorist financing*).

**Case study 4. Major drug syndicate paid workers in gold**

An investigation into a well-organised and resourced drug syndicate identified a former bank manager as the head of the operation. Allegedly, the suspect was involved in financing and facilitating the multi-million dollar cannabis and amphetamines production operation and was linked with several well-known criminals.

The head of the operation was suspected of laundering the proceeds from the drugs syndicates through the purchase and sale of gold, the purchase of cattle and through gambling. Authorities believe the suspect used cash to purchase gold from prospectors at a reduced price and then sold the gold to unrelated businesses and declared it as legitimate revenue. Police located a large quantity of gold nuggets and AUD 161 000 cash hidden by the syndicate.

Those involved in the operation were paid well, and some received bonus payments in drugs and gold. One worker was paid a total of AUD 250 000 in cash, drugs and gold in the four seasons he was involved in the operation. Syndicate chiefs were paid more than AUD 300 000 each harvest, as well as being paid in gold bullion.

Commonwealth proceeds of crime action was taken against the offenders and resulted in the restraint of over AUD 4 million worth of assets, including rural properties, cattle, machinery, AUD 220 000 cash and a large quantity of gold. The law enforcement operation led to the arrest of number of syndicate members, who were subsequently charged and jailed for lengthy periods of time.

*Source: Australian FIU*

**Case study 5. Gold used to exchange value in corruption deals – no banking transactions linking the perpetrators**

Chairman A is the head of an Indian public entity responsible for awarding contracts for industrial work. Person B is the Managing Director of a company that has applied for a contract with the public entity. Person B approaches Chairman A's friend, Person C, to broker a deal to obtain the contract with a bribe of INR 2 million (Indian rupees).

Chairman A directed Persons B and C to contact his wife for the details on how the money was to be exchanged. Chairman A's wife asked for the cash to be converted into gold and handed over to her. Once the gold was provided to her by Person B, she deposited the gold into a bank locker.

Acting on a tip off, the Central Bureau of Investigation registered a case against Chairman A and conducted searches at his premises and lockers and recovered the gold.

The Central Bureau of Investigation charged the offenders for the predicate offence under Prevention of Corruption Act, which is a scheduled offence under Prevention of Money Laundering Act of India and 10kg of gold was restrained as part of a money laundering investigation.

*Source: Enforcement Directorate of India*

## INVESTMENT IN GOLD PROVIDES RELIABLE RETURNS

In the money market, gold as an asset is used to reduce risk and stabilise return on investment. The predominant reason for this is that for the average investor, the gold trade is more easily understood and gold is trusted more than complex financial instruments. Further, gold is less volatile than most commodities and equity indices which allow account managers to better balance investment portfolios because it gives them greater ability to manage risk associated with volatility. For these same reasons, there is a bias for money laundering syndicates to prefer cash or precious metals such as gold when conducting transactions especially international transactions. Case study 6 illustrates that criminals are willing to invest in, and stockpile gold, to distance themselves from the predicate crime, even as a medium-term investment.

### Case study 6. Investing in gold to realise the proceeds of crime at a later date

A Swiss financial intermediary, which offers a complete set of services related to melting, refining, sourcing and trading of precious metals, received a business proposition via e-mail from a person with an Asian-sounding name. The intermediary did not know the person nor the e-mail address (through a commercial provider).

In this e-mail message, the sender indicated that a large sum of gold was to be put up for sale. Attached to the e-mail message was a letter, including letterhead, from a company in Switzerland. In this letter, the company confirmed that it had been asked by a second company to locate potential buyers and serve as the clearing agent for the gold transaction. The letter claimed that this second company was also domiciled in Switzerland and had been contacted directly by a bank, which was the actual seller of the gold. The bank in question, however, was not mentioned. The business proposition was referred to as “a major gold deal” and that the sale price would be 4% below the London Gold Fix rate.

The reporting financial intermediary suspected foul play as such large gold transactions are usually handled by professional dealers and yet the bank seeking to sell the gold was not mentioned in the offer. In addition, the reporting financial intermediary suspected that neither of the two companies mentioned were licensed to act as financial intermediaries.

A report was made to the Swiss FIU and as a result of a search of the FIU database; it became apparent that a representative of one of the companies involved had been convicted in a fraud case abroad several years before. The financial intermediary surmised that perhaps some of the illicit gains from this fraud had been used to buy gold. This gold would then have been hoarded somewhere and now that the gold price had risen; the moment to sell had come.

The Swiss FIU contacted the partner FIU abroad to find out whether all of the assets in question had been seized at the time of sentencing. The foreign FIU replied that there was the suspicion of fraud and the person in question had been investigated by the responsible police. He was also known under his first name and under an alias name. However, records were no longer available. For this reason, a possible link between the gold and illicit gains from fraudulent activities could not be explored further and the suspicious transaction report (STR) could not be forwarded to a law

enforcement authority.

*Source: Switzerland FIU*

## **GOLD IS EASILY SMUGGLED AND TRADED – BOTH PHYSICALLY AND VIRTUALLY**

The survey responses for this report indicate that the majority of money laundering and predicate offences relating to the gold market are associated with international and domestic trading.

In the physical sense, it is easy to melt gold bullion and convert it into different forms to disguise the fact that it is gold. For example, there have been media reports about the interdiction of gold shipments between North and South America where the gold was disguised as American souvenirs. The case studies below, give examples of gold being reshaped into cones and common items such as wrenches, nuts, bolts and belt buckles. Gold in these forms is easier to conceal from border authorities and its value can be considerably understated on the Bills of Lading.

### **Case study 7. Gold reshaped into common objects to avoid detection by customs**

The United States Homeland Security Investigations (HSI) and Internal Revenue Service-Criminal Investigation (IRS-CI) uncovered a scheme related to gold being reshaped and exported as common objects like cones. From December 2001 through May 2003, Jaime Ross, owner of Ross Refiners, a gold refining business in Manhattan's Diamond District in New York, was selling bulk quantities of gold to an undercover agent posing in an undercover operation as a narcotics money launderer.

Ross would sell the gold knowing that the currency used allegedly came from narcotics sales. Ross would recast the gold into cones and alter the colour of the gold to avoid detection while being smuggled to Colombia. Ross was arrested on 4 June 2003 and charged with money laundering and failing to file IRS Forms 8300, declaring the cash transaction relating to the sale of gold.

*Source: US-HSI*

### **Case study 8. Gold reshaped into common objects like wrenches, nuts, bolts, belt buckles etc.**

Under 'Operation Meltdown', The United States Homeland Security Investigations (HSI) investigators uncovered a carousel scheme in which jewellers were converting the proceeds from drug sales into the equivalent value in gold.

The scheme involved a criminal organization with links to gold suppliers in the New York area that were laundering millions of dollars in drug proceeds. The HSI investigation disclosed that the exported gold from Colombia was described as 'gold pigments' and upon importation into the United States the same merchandise was then described as 'gold bullion'.

The gold bullion was then transported to New York, where jewellers who were cooperating with drug trafficking organisations disguised the gold into a wide range of common objects like

wrenches, nuts, bolts, belt buckles and trailer hitches. These items were exported back to Colombia at a declared value far below the worth of their weight in gold. Upon arrival in Colombia, the same gold was recast into bullion and exported again to the US as 'gold pigment'.

The investigation of this case resulted in the arrest of 23 jewellers charged with money laundering and others arrests along with the seizure of 140 kg of gold, more than 100 loose diamonds, USD 2.8 million, 118 kg of cocaine, 6 guns and two vehicles.

*Source: US-HSI*

Because the exact amount of gold harvested from recycling activity is difficult to identify, smuggling is an ideal method of moving it from one location to the next either domestically or to international jurisdictions where it can then be refined.

Criminals may recruit couriers to carry gold across borders both legally and illegally (smuggling). This allows the criminals to remain anonymous and distance themselves from the transfer.

The classification and description of gold as an excuse to move value are techniques used by the criminal organizations to give the appearance of legality to the flow of funds of licit or illicit origin and also allow the gold itself to be transferred to places more conducive to their ongoing criminal activity. This usually occurs through routes that do not have strong governance over the tracking of the movement of gold or the gold is smuggled to avoid detection.

In some cases due to the nature of the market, the gold does not have to exist or be moved physically to be traded. Rather, citing 'gold' as the traded good on an invoice can be used to justify large movements of money, either domestically or across borders.

This is a form of trade-based money laundering (TBML) which is actually promoted by the market itself; the movement of value without the movement of the underlying commodity was created to reduce the cost of physically moving a risky, high valued commodity. TBML is 'the process of disguising the proceeds of crime and moving value through the use of trade transactions in an attempt to legitimise their illicit origins.'<sup>5</sup>

As indicated, the gold sector includes depository and certificate products which provide legal title to gold bullion which is stored on behalf of the owner. These certificates provide another mechanism for criminals to launder money whilst distancing themselves from the asset. These certificates can be purchased or traded by third parties.

<sup>5</sup> FATF (2006), *Trade Based Money Laundering*, p. i.

### 3. OPPORTUNITIES FOR GENERATING ILLICIT PROFIT IN THE GOLD INDUSTRY

This chapter outlines some of the many opportunities available for criminal groups to exploit the gold market for profit. As with the mining of other precious materials, the journey of gold, from production to the consumer and investor, consists of several stages. There are two main sources of ‘new’ gold put on the market each year – the first is gold that is mined and the second is gold that is recycled. Mining accounts for two thirds of ‘new’ gold production each year and recycling accounts for the remaining one third.<sup>6</sup>

This section gives an overview of the type of predicate offending that can occur in the gold market continuum to assist practitioners to better understand the related money laundering and terrorist financing risks. This is intended to provide practitioners with a starting point as there is limited knowledge of the financial flows associated with the gold industry.

Practitioners should also be aware that criminal organisations may choose to infiltrate this industry to easily access mechanisms to place, layer and integrate their illicit proceeds with the proceeds of legitimate activity in the gold industry.

#### LARGE-MEDIUM SCALE MINING

Large scale or medium scale industrial mining (LSM) covers formalised extraction processes using industrial and mechanised methods.<sup>7</sup> This sector is dominated by large corporate companies such as Anglo Gold Ashanti, Rio Tinto and Newmont.<sup>8</sup> LSM operations require significant capital which may be sourced privately or publically. Projects of this kind have high barriers to entry. Research by PricewaterhouseCoopers in 2012, identified China, Australia, the United States, Russia, Peru, South Africa, Canada, Mexico, Indonesia, Ghana, Uzbekistan, Brazil, Papua New Guinea, Argentina and Tanzania as the world’s largest gold producers (in order of significance).<sup>9</sup>

- *Corruption*: Due to the high barriers to entry, including obtaining the necessary environmental and regulatory permission of LSM projects, these activities are susceptible to corruption of a large scale. The capacity to obtain the necessary clearances through corruption maximises the benefits and minimises the costs associated with mining, to the detriment of other businesses and individuals.
- *Theft of mined ore*: As the concentration of gold ore extracted from the ground can only be estimated, there is potential for organised crime groups to infiltrate the production supply chain, siphon off mined ore and have it refined, then sold, to generate income.

<sup>6</sup> PWC Report, p. 12.

<sup>7</sup> Gold Paper, p. 7.

<sup>8</sup> Gold Paper, p. 7.

<sup>9</sup> PWC Report, p. 3.

- *Fraud and other scams involved with mining gold:* Due to the broad appeal of gold to a large sector of the population and the speculative nature of mining start-up companies, the gold market is highly susceptible to fraudulent schemes and other scams, such as Ponzi schemes, which provide fertile ground for organised groups to generate illicit funds.

## ARTISANAL SMALL-SCALE MINING

Artisanal or small-scale mining (ASM) is usually informal or semi-formal gold collection using basic hand tools or simple mechanised equipment. It is often carried out by individuals, sometimes seasonally or as a nomadic activity, or by groups. This form of collection accounts for about 12% of global mine supply and provides income to significant numbers of people, especially in less developed or emerging economies.<sup>10</sup>

- *Illegal mining:* Due to the challenges of governing this sporadic form of mining and the low barriers to entering the sector, there is significant scope for organised crime groups and terrorist groups to harvest gold ore from ASM operations. Similar to LSM mining, corruption can also assist to facilitate illegal ASM activities. Case study 9, illustrates the lucrative nature of illegal mining. Case study 10 explains how a narco-terrorist group used the proceeds of illegal gold mining to support their operations.
- *Smuggling:* Gold that is illegally mined will often need to be smuggled into another jurisdiction to be refined. This is because gold refineries are not necessarily located in the same jurisdiction that the gold ore is mined. Sophisticated smuggling syndicates are engaged to transport the illegally mined ore across borders. Case study 11 provides an example of ASM and gold smuggling in Ecuador.

### Case study 9. Example of gold smuggling and laundering from Zimbabwe

The Zimbabwe FIU commenced an investigation based on a suspicious transaction report (STR) from a financial institution in Zimbabwe (Bank A). This STR reported that the subject, a holder of a personal bank account, attempted to make a cash deposit of ZAR 4.1 million (South African rand, equivalent to about USD 410 000) into his account and sought to immediately withdraw the money in US dollars.

Prior to the attempted transaction, his account had been overdrawn, thereby raising suspicion regarding the source of the substantial cash deposit. The bank was not satisfied that the funds were from a legitimate source, and it declined to accept the deposit and immediately filed an STR with the FIU.

The FIU conducted an interview with the individual who explained that the money was proceeds

<sup>10</sup> PWC Report, p. 17.

from the sale of gold which he had purchased from small-scale miners and illegal dealers who operate in and around Kwekwe, one of Zimbabwe's gold producing regions. The Kwekwe region is dominated by small-scale licensed miners as well as illegal gold "panners" who prefer to make a quick sale and, therefore, sell to buyers such as the subject who pay cash on the spot. It was also asserted that gold buyers such as the subject, offer the small-scale and illegal miners, not only cash on the spot, but also offer a more attractive price than the state licensed buyer, which withholds a percentage as a statutory levy.

The subject told the FIU that he smuggled the gold to South Africa (with which Zimbabwe shares a border), where he would sell the gold to different buyers, including licensed gold millers. The subject indicated that his buyers, in turn, smuggled some of the gold from South Africa to Asia where they sold it to jewelers. The subject added that the attempted deposit was intended to enable him to exchange the South African rand (which he gets upon disposal of the gold in South Africa) for US dollars, which he would use to purchase more gold on the black market and continue the cycle. The US dollar is the currency acceptable to the gold suppliers.

On being asked how he disposed of his ZAR4.1million, after his bank had declined to accept his deposit, the subject revealed that he exchanged the South African rand through black market currency exchangers in Harare.

This case is one of many similar STRs which the Zimbabwean FIU has received and processed. While a few of the illegal gold dealers change their South African rand to US dollar, through banks, many others prefer to change the South African rand on the foreign currency black market to avoid detection.

*Source: Zimbabwe FIU*

#### Case study 10. **Mining and commercialising of gold to finance terrorism - Colombia**

A narco-terrorist group takes control of a territory where a gold mine is in production. To gain control of the mine the narco-terrorist group extorts the owners by way of violence and forcing the community to transfer the ownership titles to the group.

This narco-terrorist group uses the mine illegally where part of the gold from the mine is sold to a legal business and the transaction is paid in cash. The cash is then used to buy equipment, munitions, medicines, and other supplies needed to continue with their terrorist activities. The remaining gold is safely kept for future transactions.

*Source: GAFILAT*

**Case study 11. Illegal mining in Ecuador**

In 2010, approximately 20% of the Ecuadorian territory was registered as mining territory. However, the informal and sometimes illegal nature of the mining sector in Ecuador has impeded the ability of Ecuador and its neighbouring countries to identify how much gold is being mined and leaving the country illegally.

Ecuador estimates its annual production to be approximately 15 to 20 tonnes of gold.

Artisanal mining produced approximately six tonnes of gold in the 2012 equalling approximately USD 9.5 million in revenues for the State. Of the total of six tonnes produced, approximately two tonnes were dedicated to internal consumption (for jewellery) and the four remaining tonnes were legally exported, returning approximately USD 160 million during 2012.

The illegal mining is calculated to amount to between six and eight tonnes of gold every year. A significant amount of this production is smuggled over the border. This is due to the fact that it is easier in the neighbouring countries to sell the gold because, unlike in Ecuador, permits are not required.

*Source: Ecuador FIU*

**RECYCLING**

Recycled gold accounts for about one third of new gold introduced to the market each year.<sup>11</sup> Sources of recycled gold include industrial equipment, scrap generated from retail manufacturing, or jewellery. Recycling of gold is more likely to occur in areas of high gold consumption and is not tied to areas where gold is mined. In 2012, the United States, Italy, China, India, the United Arab Emirates, Turkey, the United Kingdom, Mexico, Egypt and Indonesia were the top source countries for the supply of gold for recycling purposes in order of quantity supplied. The supply of recycled gold is more responsive to demand than gold from mining where lag-time in development and other barriers limit rapid responses.

- *Theft:* Many jurisdictions identified jewellery theft as a significant form of predicate offending that occurs in the gold market. Cash-for-gold businesses provide criminals with the opportunity to convert stolen gold into cash without having to prove ownership over the second-hand gold presented for sale.

**SMELTING/REFINING**

All gold, both mined and recycled, is required to go through a refining process, referred to as smelting, to bring it up to what is referred to as 'investment quality'. Refineries may or may not operate in the same jurisdiction where the gold is mined, and in the majority of cases they do not.

<sup>11</sup> PWC Report, p.1.

- *Smuggling*: As mentioned in the section on ASM, illegally mined gold will often need to be smuggled to a refinery to be smelted. Whilst some enforcement action has been undertaken against smelting operations, anecdotal evidence indicates that the smuggling of gold from both legal and illegal mine sites is widespread.
- *Misrepresentation/fraud*: Organised crime groups can misrepresent the purity, weight, origin and value of gold to create profits or to justify the instrument or proceeds of crime. As demonstrated in case study 12, misrepresentation can also aid in tax fraud.

#### Case study 12. **Fraudulent claims to earn tax credits – Australia**

Criminals can exploit jurisdictional tax schemes in relation to precious metals by combining trading and refining activities. In this case, ‘syndicates’ utilised inter-related transactions with associate entities to conceal the true nature of the transactions in order to fraudulently obtain tax refunds or avoid paying the Australian goods and services tax (GST). This process is also known as a ‘missing trader’ fraud.

Investigations suggest that gold bullion is cycled through gold refining entities, with claims that the bullion is broken down into a taxable form prior to being ‘reconstituted’. It is then sold GST-free to a precious metal dealer after GST credits have been fraudulently claimed on the purchase by misrepresenting the nature and status of the transactions. Tens of millions of Australian dollars in GST payments are made on fraudulent claims.

Broadly, the criminal activity occurs through:

- Claiming GST credits on acquisitions of gold which were GST free and no entitlement exists.
- Incorrectly claiming GST credits under the special rules in relation to acquiring second-hand goods where gold is specifically excluded from the definition of second-hand goods under the GST Act.
- Incorrectly treating some supplies of gold bullion as GST free where the product does not meet the criteria under the Act.
- Individuals receiving payments emanating from the proceeds of the GST claims which are not being reported as income in the respective income tax returns.

Participants at the end of the supply chain are making GST-free sales (on the assumption gold has changed form) and claiming income tax credits on acquisitions from associated suppliers. Further, individuals within the syndicates are benefiting from the receipt of payments generated by the GST fraud which are not declared as income in the appropriate income tax returns.

*Source: Australian Taxation Office*

## RETAILING

Retailing of gold is a significant market internationally, and as indicated below there is some understanding of the predicate offending that occurs in this sector, but there is little understanding of the financial flows in the trade. In 2012, the highest consumption demand came from India, China, the United States, Turkey and Thailand (listed in order of the size of the demand).<sup>12</sup>

- *Fraud*: As gold ownership has deep-rooted cultural significance, criminal organisations have developed a range of schemes to profit from the fraudulent sale of processed gold. These schemes can range from misrepresentation of jewellery pieces, to more complicated activities involving false identities and fraud committed online. For example, a jurisdiction who contributed to this report identified a scam involving a gold dealer looking for an interested partner to purchase gold from a royal family. Fake contact details and websites were created to project an appearance of professionalism in order to attract unsuspecting victims.
- *Exploitation of gold incentive schemes*: Due to the overall demand for gold-based commodities, many jurisdictions see the trade in gold as beneficial to their economy. For this reason a number of jurisdictions have incentive programs usually in the form of tax incentives to help promote the trade. Arbitrage between countries on the different schemes provides opportunities for organised crime to exploit these vulnerabilities by sourcing illegal payments from these jurisdictions for perceived legitimate activity.

## INVESTMENT

Investment gold is a particular class of gold with a specific purity. Gold can act as a financial instrument through online gold trading services which provide loans and credit. The traders and recipients receive a right in gold without the actual physical exchange of gold.

- *Tax fraud*: As gold is easy to obtain and conceal, it often forms the basis of tax fraud where gold commodity is purchased and stored legally in foreign jurisdictions. Whilst stored in foreign jurisdictions, markets are set up to sell the value locally. This allows cash to be drawn on the value of the stored gold without actually accessing the gold.

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<sup>12</sup> PWC report, p. 29.

## 4. RED FLAGS

### ML/TF ACTIVITY (AND UNDERLYING PREDICATE CRIME ACTIVITY)

#### CUSTOMER BEHAVIOUR

- Established customer (including bullion dealers) dramatically increasing his purchase of gold bullion for no apparent reason.
- Foreign nationals purchasing gold bullion through multiple transactions over a short time period.
- Bullion transferred among associates using bullion accounts (including family members) for no apparent commercial purpose.
- Occupation inconsistent with customer's financial profile. For example, the customer may list their occupation as 'student' or 'truck driver' yet transfer large values of funds to bullion accounts.
- Customer buying gold bullion and using a General Post Office (GPO), or private service provider, mail box as their address, without listing a corresponding box number.
- Unusual pattern of bullion transactions and the nature of the transactions are inconsistent with the customer profile.
- A previously unknown customer requesting a refiner to turn gold into bullion.

#### COMPANY BEHAVIOUR

- Non-reporting to the FIU by the gold industry organisations (where there is an obligation to report).
- Changes to business name of entities registered to deal in gold.
- Registration of a trading company in a tax haven even though its business relates to another jurisdiction.
- Movement of abnormally large sums of money in various accounts of the individuals and companies which are not related to the nature of their business.
- Unusual deposits i.e. use of cash or negotiable instruments (such as traveller's cheques, cashier's cheques and money orders) in round denominations (to keep below reporting threshold limit) to fund bank accounts and to pay for gold. The negotiable instruments may be sequentially numbered or purchased at multiple locations and may frequently lack payee information.

- Numerous sole proprietorship businesses/private limited companies set up by seemingly unrelated people (proxies) but controlled by the same group of people. False addresses are used to register such businesses.
- Use of a corporate structure of shell companies located across the jurisdictions.
- Significant number of companies registered to one natural person.
- Commercial activities are not easy to track as the companies are registered elsewhere.
- No clarity of how the company transports the merchandise it has bought.

#### **TRADE-BASED BEHAVIOUR (ALSO RELATED TO TRADE-BASED MONEY LAUNDERING)**

- Cash payments for high-value orders are an indication of trade based money laundering (TBML) activity.
- Misclassification of gold purity, weight, origin and value on customs declaration forms.
- Gold is shipped to or from a jurisdiction designated as 'high risk' for money laundering activities or sensitive / non co-operative jurisdictions.
- Gold is transhipped through one or more such high risk / sensitive jurisdictions for no apparent economic reason.
- Consignment size or type of commodity being shipped appears inconsistent with the scale or capacity of the exporter or importer's having regard to their regular business activities or the shipment does not make economic sense i.e. there is no reasonable explanation for the client's financial investment into the shipment.
- The transaction involves the use of front or shell companies. Both shell and front companies can be used to facilitate TBML but in different ways. A shell company has no real operating activity and is used to hide money laundering activity and the identities of individuals involved so as to obscure the money trail. If activity is traced to the company it is literally an empty shell.

#### **PRODUCT DIFFERENTIATION**

- The bullion has physical characteristics that are inconsistent with industry standards.
- Gold prices higher than those of the local gold market.

#### **PAYMENT BEHAVIOUR**

- A number of affiliated entities in the payments chain.

- Transit movement of funds and changes in purposes of payments.
- Payments to shell companies with further withdrawals.
- Granting of loans (with zero interest rates) to foreign companies.
- Granting of loans (with zero interest rates) to natural persons.
- Natural person or business sells gold saying that it comes from a place with no extraction license or from places with no gold mines.
- Large amount of funds transferred internationally and then withdrawn very quickly.
- International transfers to countries where the company is not registered.
- Significant cash withdrawals from bank accounts by participants within the gold trading industry.
- Division of funds in cheques and smaller cash transactions to pay for merchandise.
- Purchase of gold bullion with bank cheques may be an attempt to conceal the source of the funds and underlying ownership.
- The use of cash to purchase bullion, especially when there are multiple purchases in a short timeframe, or when large amounts are purchased at once, or when there are structured cash deposits into an account to finance a single gold bullion purchase.
- Original source of funds to buy gold bullion cannot be established. The transaction involves the receipt of cash (or by other payment methods, including cheques or credit cards) from third party entities that have no apparent connection with the transaction or front or shell companies or wire instructions / payment from parties which were not identified in the original letter of credit or other documentation. The transactions that involve payments for goods through cheques, bank drafts, or money orders not drawn on the account of the entity that purchased the items also need further verification.
- Transactions between domestic buyers and sellers with sales proceeds sent to unknown third parties overseas.

## PREDICATE CRIME ACTIVITY

### GOLD MINING BEHAVIOUR

- Production and commercialisation of gold by a person or business without a license.
- An ethnic community hires a third party for the entire operation of the mine.

- Licensed mines where the production has decreased with no apparent explanation.
- The development of mining activities using machinery and equipment that is not in accordance with the characteristics of the licensed small or artisanal mining.
- The development of mining activities without compliance with the administrative, technical, social and environmental regulation.
- The development of mining activities in prohibited areas.

## CONCLUSION

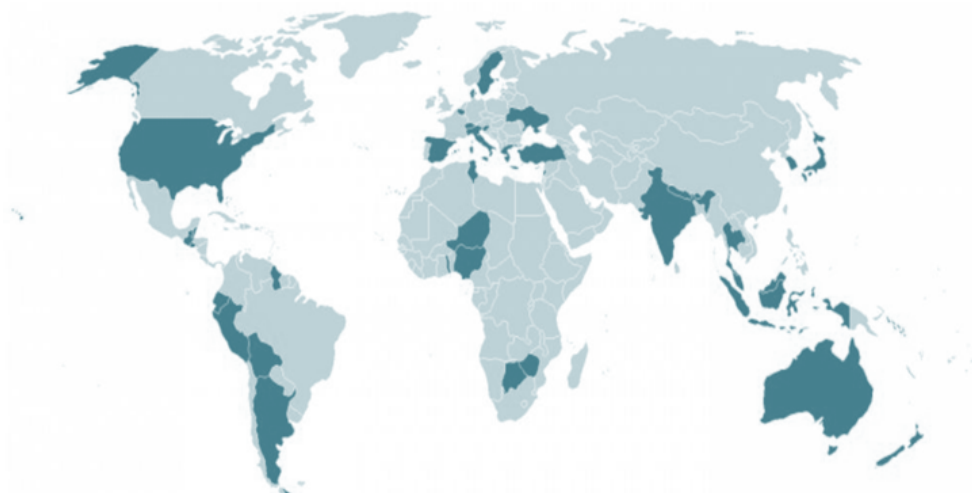
The main finding of this report is that the characteristics of gold make it both attractive for, and vulnerable to, exploitation by criminal organisations that need to legitimise assets. Gold has intrinsic value, is easily smuggled and exchangeable worldwide and can be traded anonymously. Not unlike other precious stones and metals, gold's widespread historical and cultural significance, as well as its potential to legitimise illicit cash, create opportunities for its misuse.

This report has also identified a range of profit-making opportunities for criminals in the gold market continuum. The report also sets out a range of red-flags to identify predicate offences that could occur in the mining, recycling, refinement, retail and investment of gold. While the techniques employed to launder these profits may not be specific to the gold industry, it is important to note that criminal organisations are likely to benefit from infiltrating the gold market continuum due to the inherent value of gold and the ability to use gold to combine aspects of the placement-layering-integration process.

These are important findings, but further work needs to be done to identify any trends or patterns within jurisdictions and internationally in relation to money laundering and terrorist financing in the gold sector. While this report includes one case study on the abuse of the gold market by a terrorist group, it would be worthwhile considering to what extent terrorist groups are moving or raising funds through the gold sector. In addition to the financial flows, more information is required on the commodity flows.

Further work also needs to be done to map the regulatory controls relating to all aspects of the gold continuum, including formal and informal activity, to provide law enforcement agencies with an overview of starting points for regulatory information on gold production, wholesale, distribution and retail. Approximately one third of companies that responded to the questionnaire provided to the private sector revealed that they are not regulated by any Government or statutory authorities. While no conclusive statement can be drawn from this, it would be useful to undertake further study on how the gold industry is regulated both locally and internationally. A key question for this research is whether the gold industry is collecting relevant information, including financial information or customer details, to assist in the investigation of money laundering or terrorist financing and how this information is impacting on investigations.

**Graph 1. Respondent countries to the questionnaire**



- Mining sector: Sixteen companies in six countries
- Refining sector: Seventeen companies in seven countries
- Financial gold products sector: Ten companies in three countries
- Gold trade sector: Forty companies in nine countries

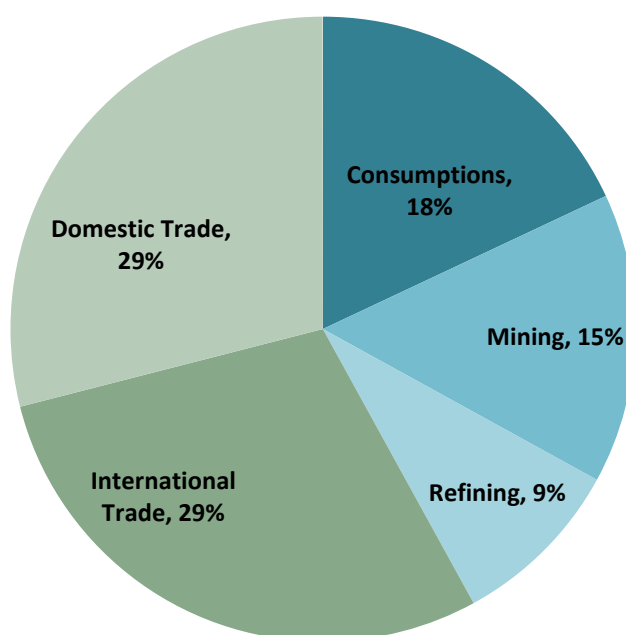
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## SUMMARY OF KEY FINDINGS OF THE QUESTIONNAIRE

In view of the limited sample size, the findings of the analysis of the questionnaire results are tentative. However, the tentative findings corroborate the observations which have been made in this Report on the basis of case studies, presentations made during APG Annual Meetings in Shanghai and Macau, the APG/Eurasian group on combating money laundering and financing of terrorism (EAG) Typologies Workshop in Mongolia and Joint Experts' Meeting in Doha.

The questionnaire results reveal that significantly high ML/TF risks and vulnerabilities arise in the domestic and international trade of gold. This is clearly demonstrated by the fact that jurisdictions have reported the highest number of predicate offences relating to gold, and ML cases related to gold, in the sectors relating to international and domestic trade of gold. The responses from the policy makers illustrate that besides the mining sector, the international trade sector is the most highly regulated. It is not clear whether that regulation relates to money laundering or whether, more broadly, international trade is a form of economic activity which is regulated in a lot of jurisdictions.

Graph 2. **Predicate offences and money laundering cases relating to gold**



*Source: responses to questionnaire to policy makers*

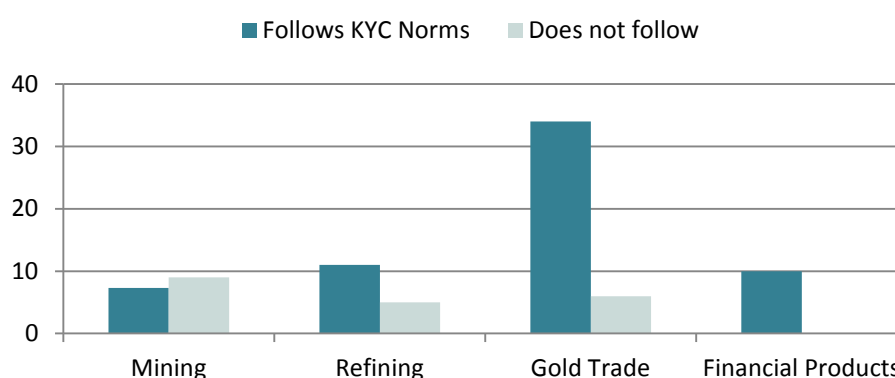
The questionnaire responses indicate that imported gold is a major source for the refinement and domestic consumption of gold. This supports findings of the literature review that gold is often not refined in the country where it is mined. These findings present vulnerabilities and risks arising from trade-based money laundering related to gold. The details provided on reported predicate offence and ML cases indicate that while the absolute number of such cases may be low, the amount involved is substantial. Hence, even low volume of gold movement across border can transfer substantial value. The predicate offences relating to money laundering offences of gold are serious

in nature ranging from smuggling, fraud, corruption to narcotics trade. The statistical findings do not support commensurate international cooperation required to prevent and combat risks and vulnerabilities arising out of the gold trade.

Responses from the gold industry reveal that overwhelmingly the activities relating to mining, refining, trade and financial products of gold are carried out by the private sector. Most of the mining companies do not refine the gold which they mine and the refining companies also refine gold other than ore, in particular scrap gold. Most of the refining companies which have responded do not mark the gold that they refine. On the other hand, companies which are predominantly trading in gold do have quality marking norms for measuring the purity of gold.

The majority of companies in all four gold sectors (mining, refining, retailing and financial products) are subject to government regulation and laws but it is not clear how closely these controls relate to anti-money laundering or counter-terrorist financing. The majority of the companies in all four sectors settle their transactions through formal banking channels. Except for the mining sector, the majority of the companies in the other three Sectors follow know-your-customer (KYC) norms. Except for the financial gold product sector, the majority of the companies in the other three sectors do not claim to be operating in more than one country. Again apart from the financial gold products sector, the majority of the companies in the other sectors are affiliated to international/domestic associations.

**Graph 3. Application of KYC norms per sector**



*Source: questionnaires responses*

*Note:* the graph above illustrates that all of the companies in the financial gold products sector which responded to the Questionnaire follow KYC norms. Similarly, the majority of companies in the gold trade, also claim to follow KYC norms.

While the responses above indicate that there are measures in place to address the risks and vulnerabilities arising from gold production and trade, it is important to note that these responses are from the organised sectors of the gold market and the results may be very different for organisations operating in the sector in an informal or unorganised manner.

## APPENDIX B – FURTHER CASE STUDIES ON MONEY LAUNDERING OR PREDICATE CRIME INVOLVING GOLD OR THE GOLD INDUSTRY

### Case study 13. **Smuggling/undervaluation scheme using scrap gold**

The United States Homeland Security Investigations (HSI) uncovered a smuggling/undervaluation scheme with scrap gold upon entry to the United States (US). From January 2012 to November 2013, a US importer (ultimate consignee) was smuggling scrap gold into the US from countries in Central America at undervalued prices and subsequently providing payments to the exporters at overvalued amounts.

During this time frame two Central American companies sent scrap gold with a total declared value of approximately USD 6.4 million to the US importer yet during that same period wire transfers valued at approximately USD 24 million were sent back to the Central American companies for those imports. The owners of the US business were arrested and charged with conspiracy to commit money laundering using customs violations as a predicate offence.

*Source: US-HSI*

### Case study 14. **Gold mines operated by family alleged to be involved in drug trafficking**

The reporting financial intermediary is a privately held group of international companies which has been operating since the 19th century and whose business is precious metals. The activities of the group are executed by its companies in Switzerland and in the USA.

Two mining companies were reported by the reporting entity on June 2007. Since the establishment of a business relationship between the reporting entity and the two mining companies, all obligations of due diligence according to the Swiss Anti Money Laundering Act and the US legislation in this field had been complied with.

The two companies sent gold from the mines for refining to the reporting intermediary. Once the transaction had been executed, the proceeds of the sale were transferred to the bank accounts of the companies. However, in March 2007, a magazine article about the owner family of the two mines was published. It claimed that the family had been involved in drug trafficking and had gained its fortune through trade in firearms. In the 1980s, one family member, who was close to the actual shareholders of the two mining companies, was prosecuted for drug trafficking but was later acquitted, only to be murdered a few years later. It seemed that during the processing of the Suspicious Activity Report (SAR) the owner family of the two mining companies was in court proceedings with a Canadian company in connection with the purchase of a mine in Peru.

As there only had been press articles and no entries in the police data bases, the Swiss FIU asked the financial intermediary for further information concerning the allegations in the press articles and their accuracy. As there had been no established connection to a predicate offence or money

laundering, the SAR at that stage could not be forwarded to the Law Enforcement Authority for action. However, the Swiss FIU made a request concerning the involved persons to a foreign FIU. The Swiss FIU was promptly informed that there was an ongoing criminal proceeding against one member of this family for embezzlement.

In November 2007, there had been a further SAR from the same financial intermediary. The financial intermediary had done some additional research and established that the press articles were false. Local barristers of the group of the financial intermediary had communicated to the financial intermediary that according to their current knowledge there had been no legal proceedings raised officially in relation to the two companies and its representatives.

After receipt of the second SAR, the Swiss FIU made another request to the foreign FIU concerning the two companies and its representatives. The reply was that there was a formal criminal investigation carried out by the Public Prosecutor regarding the companies and members of the owner family. The predicate offence alleged against the family was drug trafficking.

Due to this new information, the SAR was forwarded to the office of the Attorney General of Switzerland. The assets were seized by order of this competent law enforcement authority.

*Source: Switzerland FIU*

#### Case study 15. **Proceeds of alleged fraud involved in the gold market**

A financial intermediary operating in refining and trading of precious metals sent a suspicious transaction report (STR) to the Money Laundering Reporting Office Switzerland (MROS), the Swiss FIU, in April 2014.

The reporting financial intermediary is one of the world's largest processors of precious metals and is considered among the top three in Switzerland. Behind the decision of the financial intermediary to send an STR, was the publication of 'open source' information indicating that a client had been arrested following an investigation relating to fraud, forgery of documents, drug trafficking and money laundering. After undertaking due diligence, the financial intermediary could not exclude the possibility that the assets (i.e. the gold that was to be refined) were the proceeds of crime.

The STR related to the CEO and representative of a Spanish company specialising in buying retail gold with a turnover of more than EUR 1100 million in 2013. The company described itself as a very professional trading company for gold investments. A US private equity firm specialising in buying and building companies controlled at 51% of the company. The remaining 49% belonged to a European fund, of which the CEO and the representative of the Spanish company held 49%. The company was active in the sale of gold bullion and, more recently, in acquiring jewellery and other gold pieces in order to refine and transform them in gold bullion. In 2009, its turnover was less than EUR 150 million while the following year, in 2010, it was more than EUR 500 million. In 2012, the turnover doubled from that of 2010 and was approximately 1000 million.

The Swiss financial intermediary and the company were bound by a contract, which provided for both the refining of gold and the marketing and sales on behalf of the company. Based on the

information provided by the financial intermediary and information held by the Swiss FIU, there was a question as to whether there were reasonable grounds to suspect that the concerned assets (i.e. the gold) were the proceeds of crime.

In order to receive more information MROS sent two information requests to foreign FIUs. Unfortunately, only one foreign FIU answered the information request. The other FIU, the most important from the point of view of the relevance of the information, did not respond. Finally, the STR was forwarded by MROS to the competent law enforcement authority (LEA) in Switzerland. Before starting a preliminary investigation, the LEA waited on the results of the information request and, in particular, on more information about the investigation conducted on-site and about the reliability of the information concerning the alleged crimes. Meanwhile, the aforementioned company went through bankruptcy proceedings.

*Source: Switzerland FIU*

**Case study 16. Source of the commodity is often not revealed and therefore a significant conduit for stolen commodity**

The United States Homeland Security Investigations (HSI) uncovered a scheme where a jewellery businessman hired a burglary ring to rob clients of previously purchased jewellery.

The jewellery businessman would sell jewellery to clients and then hire an organized burglary ring and provide them the details of the jewellery to be stolen. The information provided by the jewellery businessman contained detailed product descriptions including the residential address of the customers. The burglary ring would then target both the jewellery the customer recently purchased as well as other items of value.

During an HSI undercover operation, the jewellery businessman purchased allegedly stolen jewellery from an undercover agent and indicated that the jewellery would need to be melted and sold as scrap.

The jewellery businessmen was arrested and charged with money laundering and sale of receipt of stolen goods.

*Source: US-HSI*

### Case study 17. **Sale of gold used as justification for movement of funds to another jurisdiction – Costa Rica**

A company operating in country A frequently sent representatives to country B offering services to buy gold, jewellery and precious stones / metals above local market prices. As a consequence of this activity, high quantities of funds were transferred from country A to country B with the reason given that the funds will be used to buy gold. The funds were then withdrawn from financial institutions in country B as either cash or cheques very soon after the funds transfer were made. Little was known about the movement of the merchandise purchased.

The same organisation organised a significant event held at a luxurious hotel in country B, advertising an intention to buy gold. However, few clients were present at the event. Monies (of unknown source) said to be surplus to the cost of holding the event were then sent back to country A or sent to other countries where the company did not operate, with the argument that they would be used for similar events.

*Source: Costa Rica FIU*

### Case study 18. **A Gold Smuggling Case of Bangladesh**

A smuggler used air route for this crime. He came from Riyadh in Saudi Arabia to Dhaka, Bangladesh by Saudi Airlines.

The smuggler's luggage was scanned and found to contain items consistent with metal goods. After opening the luggage, two bottles of a well-known soft drink were found in a carton. Each bottle contains 6 gold bars of investment quality; each gold bar was wrapped with foil paper.

The luggage also contained two 135 gr bars of luxury soap, each soap contained a gold bar weighing 100 gr. In the smuggler's trouser pocket, were 77 gold chains and 2 gold earrings with a total weight of 240 gr.

The authorities did not receive intelligence on this event prior to the detection. The smuggler was passing the 'green' channel. The duty officer scanned his luggage as a routine check and found the presence of the gold.

Bangladesh has a unique operating environment when it comes to the gold market. In recent times no gold has been legally imported into Bangladesh but still the gold market is operating. The smuggling of gold, either for domestic consumption or as a transit point for other countries, has replaced the lack of legal importation. This is despite the possibility of the death sentence for smuggling gold. *Hundi* or *hawala*<sup>13</sup> are the most practiced method of moving value in the country in relation to the movement of gold.

Analysis by Bangladesh Law enforcement concerning the movement of gold has established that Dubai, Mascot and Riyadh are the primary wholesale markets of gold. The gold is purchased from

<sup>13</sup> See footnote 4 for a description of *hawala* or *hundi*.

those markets and smuggled to Bangladesh, or via Bangladesh to other parts of the world. It has been established that, on occasion, such gold is used in the barter for arms or drugs. The money used to purchase the gold is sent either by currency smuggling or Hundi however little is known about the people responsible for this.

On occasions it has been established that gold is smuggled to Bangladesh as a final payment to legal businesses where the partial payment owing has been undertaken legally. On other occasions people would smuggle gold to Bangladesh for purely economic reasons, in order to profit from the different market prices of gold globally.

*Source: Bangladesh Law Enforcement (Police)*

#### Case study 19. **A gold smuggling and money laundering case - Zimbabwe**

The Tunisian FIU received a Suspect Transaction Report (STR) related to a person X whose bank account registered a large amount of funds by means of cash remittances in short period of time and sought to withdraw the money in form of US dollar cash. Information gathered by the FIU as part of its analysis revealed that person X was linked to a network of gold smuggling.

In country A, gold is a regulated sector overseen by the Central Bank. Enquiries established that person X procured gold by different illicit ways, particularly gold smuggled through land frontiers and robbery.

Person X refined the gold into ingots and gave it to air hostess A. Air hostess A had access to all the airport zones and was able to avoid the customs and police controls. Air hostess A left the ingots supplied to her in a toilet near the gates and made a telephone call to smuggler/gold courier Y and told him where she had placed the ingots.

Smuggler/gold courier Y retrieved the ingots and flew to country T. Once there, smuggler/gold courier Y delivered the ingots to person Z in return he received payment and returned to country A where he shared the profits derived from gold smuggling with person X.

A month later the Tunisian FIU received additional information on person X. On this occasion person X had used the account of a company which he owned to try and disguise his identity. This was a more sophisticated scheme to conceal the nature of the transaction however the bank was able to detect the transaction because they had already flagged his name after the first STR. Person X had deposited an amount of ZAR 2.39million (approximately USD 239 000) into his company's account where, soon thereafter a converted US dollar amount was transferred to a third party telecommunications company.

Investigations by the FIU revealed that, after depositing the South African rand into his company's account instead of seeking to withdraw the amount in the form of US dollar cash, as he had wanted to do in his earlier activity; he instead transferred the amount, in batches, over a few days, to the telecommunications company to purchase mobile air-time in bulk quantities.

Investigations revealed that person X was purchasing bulk airtime on behalf of airtime vendors in

and around Kwekwe (Zimbabwe) and that person X made the purchases using the funds that he deposited as South African rand into his company's account, and which could now be transferred as US dollar. Person X would deliver the airtime to the airtime vendors in Kwekwe, who gave him instant cash, in US dollar. Through this method, person X had achieved his objective, to convert a large amount of South African rand cash into US dollar.

Person X would then use the USD cash to make gold purchases, which he smuggled and sold outside the country.

*Source: Zimbabwe FIU*

#### **Case study 20. Using a third party account to facilitate gold smuggling and money laundering**

A Suspect Transaction Report (STR) was received by the FIU relating to person Z from bank B. Bank B had become suspicious after person Z had made several large cash deposits, in South African rand, into the bank account of a company that he owned and controlled. The deposits were followed by withdrawals of the amount in US dollars. The total amount involved was USD 6.6 million.

Investigations by the Zimbabwe FIU revealed that person Z had been conducting the transactions on behalf of a well-known gold dealer, in return for a commission. Person Z's friend person Y, was known to be involved in illegally buying gold from illicit suppliers and then smuggling the gold for re-sale out of the country. Estimates based on the amount of USD 6.6 million involved in this case, suggests that over one tonne of gold was illegally acquired, and smuggled out of the country.

*Source: Zimbabwe FIU*

#### **Case study 21. Pakistan Gold Trade – A Need for a Temporary Ban on the Import of Gold Initiative**

The Gold initiative was an initiative of the Pakistan Government to diversify exports by promoting the export of value-added gold jewellery. For this purpose, special schemes were in operation to support jewellery exporters whereby they are able to import gold without payment of any duty on the condition that the same gold was re-exported after converting it into value-added jewellery.

These schemes were referred to as the "Entrustment" and the "Self Consignment" schemes. The Entrustment Scheme provides for the export of gold jewellery and gold articles. Under the scheme, the quantity of gold exported must equal the quantity of gold imported less the wastage that occurred in the manufacture of the items to be exported. The scheme allows foreign buyers, exporters or an authorized representative to send the gold by air/sea cargo or bring gold into Pakistan personally. The Self-Consignment Scheme regulates the export of gold jewellery and gemstones taken out by authorized representative of an exporter on self-consignment basis. Stringent conditions apply under both schemes, including measures that allow authorities to

monitor and oversee all relevant shipments.

As these schemes matured, there were reports that some of the importers of gold were circumventing the procedures under the schemes to smuggle gold in and out of Pakistan. The Pakistani rupee exchange rate also came under pressure.

The Pakistani Government then took immediate steps to prevent further damage to the national economy. It decided to impose a short-term, temporary ban of 30 days on the duty-free import of gold under these special schemes. This allowed time to restructure these schemes to remove loopholes and deficiencies while still facilitating exporters of gold jewellery to contribute to the national objective of increasing exports. These reforms included limits to the amounts of gold that can be imported by a single party, a shortening of the maximum period within which the gold must be exported in the form of value added gold jewellery, and a stricter control by Pakistan's authorities of all relevant shipments. Also, the Government of Pakistan started auditing all the duty free imports of gold for export purposes in order to ascertain the misuse of the facility.

*Source: Pakistan*

#### Case study 22. **Smuggling of gold and jewellery from Special Economic Zones**

Special Economic Zones (SEZ) are designated areas that have been created to enhance trade and in particular increase exports for the purpose of earning foreign exchange. Imports into a Special Economic Zones are allowed duty free. However due to the relaxed rules governing SEZ, these zones are also vulnerable to money laundering and tax evasion activity.

Background: Directors of the companies identified in this case study were operating in the SEZ and had extensive contacts in the gold trade in India for more than 25 years. They had previously been investigated for gold smuggling and were also known to have committed customs/foreign exchange and income tax violations. One of the directors was also the owner of a gold manufacturing and trading company operating in Dubai.

Modus Operandi: Companies A and B located inside a SEZ were authorised to manufacture and to trade in gold jewellery. This involved importing gold in either bullion form or as semi-finished jewellery from foreign jurisdictions. Generally, due to the special nature of SEZ there is no examination made by the authorities when the goods are imported or exported. These companies had opted for self-certification of the export goods as long as the activity met certain conditions.

Representatives of companies X and Y (mostly run by families) would travel abroad and select jewellery in demand in the Indian market. This jewellery would be paid for at the time of purchase in the foreign jurisdiction in which it was bought. It would then be imported into the SEZ by the companies operating there recorded as jewellery for either scrapping or further finishing.

After customs clearance the goods would be moved from the airport to SEZ (a distance of 20 km). On the way, either the employees of the relevant company or one of the directors replaced the sealed imported packets with certain other sealed packets containing brass, scrap metal or other imitation jewellery. The jewellery that had been imported was then taken and sold to customers in

legitimate gold markets.

The sealed packets containing the brass, scrap metal or other imitation jewellery was self-certified as gold and studded jewellery and subsequently exported. These exports were to their own related companies with remittances being received as required by law. This scheme was made possible due to the absence of even random checks on exports of jewellery from SEZ.

The Directors would charge their customers in INR 25 (Indian rupees) per gram of gold as a delivery charge and also offered commission of INR 5 per gram to the people coordinating the buyers in India.

Magnitude: During the investigation DRI (Directorate General of Revenue Intelligence, India) seized 79 kg of gold jewellery valued at approximately USD 3 million. Examination of intercepted export consignments declared to contain 190 kg gold jewellery with a value of USD 7 million were found to contain scrap metal. DRI seized cash close to USD 100 000. Further 30 kg gold jewellery belonging to a related company was seized valued at USD 1.2 million. A total volume of doubtful imports covered were USD 100-120 million. The total quantum of customs duty evasion amounted to USD 10 million in addition to evasion of other taxes.

*Source: Enforcement Directorate of India*

### Case study 23. **international funds transfers in relation to gold business**

The Financial Intelligence Centre (FIC; the FIU of South Africa) obtained information that a subject, person A, received an inflow of USD 129 995.17 from the US in August 2012.

FIC investigations revealed that person A maintained four different accounts in one bank. All accounts were dormant prior to the transaction. Person A had established a company but could not provide evidence to support his gold business, although he alleged that he had been in the business for four years.

Person A claimed inflows were from his partners in the US who had jewellery shops in Europe. Person A indicated that he bought the gold from the black market and sent it to the USA. Web searches revealed person A to be among several foreign investors who had been duped by fake gold dealers. He was featured in a video filmed by Ana's Aremeyaw Anas (an Investigative Journalist) and broadcasted by Al-Jazeera.

*Source: South Africa FIU*

**Case study 24. Fraud relating to the export of gold jewellery**

A strategic consultant for jewellery making companies and senior employee of trading company A conspired to commit a fraud so that jewellery would be exported in the name of trading company A but other activities would be handled by the conspirators.

According to the agreement, 80% payment was to be made by trading company A to jewellery making companies after the jewellery was exported, and the remaining payment was to be made on realisation of the export proceeds which, as per terms of the agreement, was 170 days from the date of export.

In the first year of operation, all export payments were realised from overseas buyers. In the second year, while export turnover doubled, only 15% of exports proceeds were realised. On the export of the gold jewellery consignments, the conspirators would present the proof of export documents to trading company A, which paid 80% of the value of the exports immediately to the jewellery makers. In order to bridge the gap of 170 days credit, trading company A got the export bills discounted with a bank. Trading company A failed to get the export proceeds from the importers located abroad. The bank and trading company A had to thus bear the losses due to non-realisation of export proceeds. The conspirators in collusion and on behalf of jewellery makers defrauded the trading company A and the bank.

Investigation conducted by the Enforcement Directorate revealed that exports were made to companies abroad that were related to the jewellery makers. The jewellery exported by them, to related importers abroad, was sold for their gain. The advance payment received by the jewellery makers from trading company A was laundered into other businesses, such as real estate. The Enforcement Directorate traced and attached the laundered assets. The overseas investigations are in progress.

*Source: Enforcement Directorate of India*

**Case study 25. Ghanaian gold scam**

In August 2011, a lawyer and a self-styled traditional chief used the internet to lure a businessman from a country in the Middle East to Ghana with the offer of a supply of gold from a criminal syndicate. In this transaction, the lawyer represented both the buyer and the seller.

The buyer wired USD 3.5 million to an established bank in Ghana (bank A) and was subsequently cashed. As a result of the wire transfer, 1% of the agreed quantity of gold was supplied. When the buyer demanded the balance of the supply the criminal syndicate commenced intimidation and also solicited the help of corrupt police to chase the businessman out of the country.

The FIC commenced an investigation seeking particulars of suspects from various banks and information relating to the lawyer from other jurisdictions. This information was then disseminated to a law enforcement agency (LEA) who subsequently arrested the Lawyer and chief who were remanded in custody for two (2) weeks.

A review of the case by the office of the Attorney General found a number of flaws in the evidence which have not yet been resolved and the matter has not progressed.

*Source: Ghana FIU*

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## SPECIAL RECOGNITION

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This report identifies the features of gold and the gold trade that have made it an alternative means for criminals to transfer value and generate proceeds. Gold is anonymous, has a stable value and is easily transformable and transportable, which have made it an attractive alternative for criminals to store or move and generate value as regulators implement stronger anti-money laundering / counter terrorist financing (AML/CFT) measures to protect the formal financial sector from abuse.

This report provides a series of case studies and red flag indicators to raise awareness, particularly with AML/CFT practitioners and companies involved in the gold industry, of the key vulnerabilities of gold and the gold market.