



CLIENT ALERT /// July 6, 2020

## FATF Plenary Outcomes and Illegal Wildlife Trafficking Report

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### FATF Plenary Outcomes

On June 24, 2020, the Financial Action Task Force (“FATF”) held its plenary meeting **virtually**. It was the final plenary of China’s presidency of FATF; Germany will now begin its two-year term. As part of the plenary outcomes, FATF released several documents, including a new report on the illicit financial networks that support illegal wildlife trafficking (“IWT”), described in detail below. The outcome statement and accompanying reports include:

- **China’s End of Presidency Statement:** Xiangmin Liu, the outgoing FATF President, acknowledged the unprecedented challenge to FATF and its member-states posed by the COVID-19 pandemic.<sup>1</sup> The pandemic response has led FATF to temporarily postpone mutual evaluation procedures, deadlines for follow-up, and updates on high-risk and other monitored jurisdictions. The FATF plenary, however, has continued its work on a strategic review of the FATF assessment process as a whole, including how to augment the processes for mutual evaluation, follow-up, and the International Co-operation Review Group (ICRG), which oversees the identification and monitoring of jurisdictions with strategic anti-money laundering/countering the financing of terrorism (“AML/CFT”) deficiencies.<sup>2</sup>

In summarizing the accomplishments of the Chinese presidency, Liu touted FATF efforts to address the challenges that new technologies present to AML/CFT and the countering proliferation financing (“CPF”). Of note, the FATF extended its standards to virtual assets and virtual asset service providers (“VASPs”) and published an accompanying non-binding guidance paper.<sup>3</sup> The FATF also published important guidance on digital identity.<sup>4</sup>

- **Announcement of a Public Consultation Period on Amending Recommendation 1:** FATF Recommendation 1 states that countries should “identify, assess, and understand the money laundering and terrorist financing risks” for the country and respond to those risks using a risk-based approach. In response to the efforts of some countries, including the United States, to prioritize CPF efforts, FATF is seeking public comment on whether to update Recommendation 1 and its accompanying Interpretive Note to include CPF.<sup>5</sup> The proposed changes are narrowly tailored to focus on preventing the breach of targeted financial sanctions related to proliferation rather than calling on additional vigilance measures to target a wider range of proliferation-related financial activity.<sup>6</sup>
- **Priorities of the German Presidency of FATF:**<sup>7</sup> Each incoming presidency of FATF publishes a document outlining its priorities for its term. The FATF Plenary approved Germany’s priorities for its presidency, which include:



- Continuing to aid the international community to achieve consistent and coordinated AML/CFT action during the COVID-19 pandemic.
- Exploring how AML/CFT/CPF efforts could be strengthened through the adoption of new digital tools. Methods such as artificial intelligence and machine learning could make AML/CFT/CPF practices more efficient if developed and deployed in a coordinated way. As part of this effort, the FATF will convene a high-level roundtable with key groups such as data protection authorities and technology developers.
- Studying the illicit finance threats from ethnically or racially motivated terrorism, migrant smuggling, the nexus between illicit arms trafficking and terrorist financing, and environmental crimes.
- **Additional reports:** FATF released two reports on new financial technologies and their impact on AML/CFT/CPF priorities, highlighting how it plans to monitor the evolving risks from virtual assets:
  - The first report is the “12-month Review of the Revised FATF Standards on Virtual Assets and Virtual Asset Service Providers.”<sup>8</sup> The review notes that jurisdictions and the private sector have made some progress in implementing the FATF Standards with respect to virtual assets and VASPs, particularly regarding the “travel rule,” but highlighted the need for further guidance from jurisdictions on virtual assets and VASPs. The FATF will continue private sector outreach through its Virtual Assets Contact Group, prioritizing technology providers, technical experts, and academics. FATF agreed to undertake another 12-month progress review, to be published in June 2021. Separately, FATF will publish a report on red flag indicators and cases studies on virtual assets in October 2020.
  - The second report is a study requested by the G20 to examine how “so-called stablecoins”—the term used by the FATF to describe a class of cryptocurrencies backed by an asset or group of assets in order to maintain price stability—may have implications for AML/CFT risks.<sup>9</sup> While the report to the G20 stated that the FATF Standards did not need to be amended in order to address so-called stablecoins, it recognizes that this is a “rapidly evolving area” and countries should pay close attention to potential developments. The report acknowledges that developers and governance bodies of so-called stablecoins are responsible for determining: 1) how the so-called stablecoin will function; 2) who can access the so-called stablecoins; and 3) to what extent compliance measures are built into the arrangement. Provided this role, the report stresses that those developers and governance bodies will have a critical role to play in implementing AML/CFT obligations. The FATF also flagged as particular concerns anonymous peer-to-peer transactions of so-called stablecoins



conducted through unhosted wallets. The FATF will also release further guidance on so-called stablecoins as part of its overall effort to highlight illicit finance risks from virtual assets.

## The Money Laundering-IWT Nexus

### 1. *Understanding the Nature of the Threat*

**On June 25, 2020, FATF published a report on the illicit financial risks arising from the illegal wildlife trade (“FATF IWT Report”).**<sup>10</sup> The financial channels that enable IWT are an important-but-poorly-understood driver of money laundering and corruption. Although estimates of the magnitude of this illegal activity are inexact, FATF suggests that IWT generates billions of U.S. dollars per year.<sup>11</sup>

The FATF IWT Report makes some high-level conclusions about the need for a more robust international response:

- **How the IWT threat has evolved.** The FATF IWT Report outlines how the scope of the trade has expanded, with networks engaging in a range of illegal activities and in jurisdictions far from the sources of the wildlife products themselves. These networks engage in bribery, fraud, and tax evasion, and their activities bleed into other illicit activity such as smuggling and arms trafficking.
- **How countries should respond.** Given the threat that IWT poses to the integrity of the international financial system, FATF encourages jurisdictions to prioritize combating IWT, using the FATF Standards as a framework to detect and disrupt the financial aspects of this activity. To date, financial investigations into these criminal entities have lagged behind efforts to physically seize the contraband. FATF recommends that the public sector needs to do a better job furnishing the private sector with information about typologies and suspicious actors and that authorities facilitate information sharing through existing and new public-private partnerships.
- **How the private sector can contribute.** The private sector has a critical role to play, both on its own and in close coordination with relevant government authorities. Financial institutions and certain designated non-financial businesses and professions (“DNFBPs”), which include real estate agents, lawyers, accountants, trust and company service providers, and dealers in luxury goods, are the first line of defense in identifying suspicious activity. However, many private sector actors struggle to recognize the red flags and risk indicators that would help identify IWT-specific financial flows, in part because efforts to detect and disrupt IWT have not been commensurate with the risk that it poses.

**IWT is a global problem. The illicit actors that traffic in these goods operate in countries that have substantial biodiversity (and thus are ripe for exploitation) and are in well-known transit or financial hubs that enable this trade.**<sup>12</sup> The FATF IWT Report identifies common



methods that illicit actors and networks engaged in IWT use to launder the proceeds. These include:

- **Misuse of the formal financial sector:** IWT networks embrace typical money laundering schemes, including the placement and layering of funds through the formal banking system. Transactions done through cash deposits, e-banking platforms, money or value transfer systems (“MVTs”), or wire transfers are typical, often structured in a way to deliberately keep individual transactions below applicable reporting thresholds.
- **Front companies and the co-mingling of licit and illicit financial flows:** Like many illicit actors, IWT syndicates use front and shell companies to access the financial system and hold and move money. They use these companies to camouflage IWT-derived proceeds by mixing them with funds from licit business. IWT networks often use companies that provide goods or services related to the wildlife sector as fronts, such as taxidermists, farms, breeding facilities, pet shops, and zoos.
- **Purchases of real estate and luxury goods:** To launder the proceeds of IWT, criminal networks purchase high-value goods such as real estate, vehicles, jewelry, and artwork, often using cash. FATF emphasized that these methods underscore the importance of DNFBPs, such as real estate agents, understanding their AML/CTF obligations.
- **Informal or unregulated money or value transfer systems:** Illicit networks use informal or unregulated non-bank settlement methods that take advantage of family or community linkages among IWT network operators. Examples of these channels include hawala, China-based fei chen (known as “flying money”), or India-based hundi, which facilitate the distribution of their products and the collection of revenue without needing to move the money underlying those transactions across physical borders.<sup>13</sup>
- **Role of new technologies:** Alongside these traditional ways to move and launder money, IWT networks have also embraced a suite of new technologies to move money and find customers for their products. Social media, encrypted messaging apps, e-commerce websites, mobile banking, and prepaid debit cards have all figured prominently in IWT networks’ schemes. Although there are few examples of use of virtual assets being used in IWT schemes, FATF suggests that it is possible, and that jurisdictions and financial institutions should remain vigilant.

## **2. Implications for the Private Sector**

**FATF emphasizes the important role that the private sector—particularly financial institutions, DNFBPs, and companies involved in global trade—has to play in combating IWT and encourages the private sector to take the threat more seriously.** To that end, as part of the drafting process for the FATF IWT Report, FATF surveyed 15 financial institutions about their experiences addressing the financial risks from IWT. From their answers, FATF highlighted a



series of steps that the private sector should take to help address the threat of IWT-derived financial flows:

- **Broaden financial institution risk assessments to include specific high-risk sectors:** FATF recommends that risk assessments pay particular attention to clients or customers in high-risk sectors affiliated with IWT networks, including farms, zoos, breeders, and import-export firms. All but one of its survey participants had incorporated IWT into their institutional risk assessments, either through identifying specific risk indicators or methods for gathering open source information to identify emerging risks.
- **Incorporate IWT-specific information in customer due diligence and transaction monitoring as a best practice:** FATF identified best practices for continuous monitoring of customers and transactions for activity that may suggest links with IWT based on the report. These include automated alerts, targeted investigations, or regular reviews of information provided by external resources. In the case of IWT, external resources include governments but also non-profit organizations that work to address environmental or wildlife crimes.
- **Include more IWT-related flags in suspicious transaction or suspicious activity reporting (“STR/SAR”):** FATF encourages more financial institutions to incorporate potential IWT activity in their transaction monitoring scenarios and STR/SAR filings while acknowledging that further progress will at least in part be a function of the degree to which governments can share relevant intelligence with the private sector. FATF found that many financial institutions failed to specifically target IWT through transaction monitoring and STR/SAR filing.
- **Improve on existing information-sharing and public-private partnerships:** To support private sector efforts to combat IWT, there needs to be increased information sharing between governments, between governments and the private sector, among private sector entities themselves, and between the private sector and civil society. FATF faults many jurisdictions for not taking IWT seriously enough and ensuring that their legislative and regulatory frameworks appropriately address the risks. As jurisdictions take the threat more seriously, they can prioritize informing the private sector of typologies and red flags. Current examples of successful information-sharing methods FATF cites include:
  - The United for Wildlife (“UfW”) Financial Task Force,<sup>14</sup> founded in 2018, brings together more than 30 financial institutions with civil society subject matter experts. They conduct regional workshops to train public and private sector representatives, share red flags and risk indicators, and provide financial institutions with specific lead intelligence.
  - Financial institutions have also leveraged the efforts of non-governmental organizations (“NGOs”) like Environmental Investigation Agency,<sup>15</sup> Liberty



Shared,<sup>16</sup> and TRAFFIC,<sup>17</sup> which routinely provide financial institutions with names of suspected IWT network participants, based on their own open-source research.

- For U.S. financial institutions, legal tools like the USA PATRIOT Act 314(b) provision allow bank-to-bank information sharing, which could focus on IWT.

The FATF IWT Report provides useful case studies of how financial institutions have put these practices into place and actively participated in the disruption of IWT networks. What these examples and this study overall demonstrate is that IWT is a global threat, undermining the integrity of not only the jurisdictions in which these animals are hunted or sold, but the entire financial system.



### 3. Red Flag Indicators

Appendix A of the IWT Report offers indicators of money laundering associated with IWT. The below table highlights some, but not all, of the important indicators identified by FATF. FATF stresses that one indicator on its own may not be actionable evidence of illicit activity. A combination of factors, however, alongside other information available to financial institutions, may point to actors in an IWT syndicate.

Client Profiles	Corporates	<ul style="list-style-type: none"> <li>Involved in import-export, freight-forwarding, custom clearance, and logistics, particularly those located in transit or demand countries for illegal wildlife.</li> <li>These firms tend to be re-used by different IWT networks.</li> <li>Involvement of legal wildlife entities: zoos, breeders, exotic pet stores, safaris, and pharmaceutical companies that contain wildlife by-products.</li> </ul>
	Individuals	<ul style="list-style-type: none"> <li>PEPs, wealthy individuals, particularly those who own businesses involved in the wildlife, environment, game, or forestry sectors and are located in transit or demand countries for illegal wildlife.</li> <li>Account holders or beneficial owners of corporate entities located in jurisdictions that are prominent source or transit points for IWT.</li> <li>Negative news coverage implicating individuals in wildlife or environmental crimes.</li> </ul>
Transactions and Client Activity	Corporates	<ul style="list-style-type: none"> <li>Anomalous loans originating between trading or import/export companies in IWT source or transit countries.</li> <li>Payment activity between companies using IWT products and wildlife traders. Special attention should be paid to payments purported to be related to gold trading, which is a common cover for IWT.</li> <li>Large dollar wire between wildlife farms and firms operating in inconsistent lines of business, especially firms that may be involved in cover activities (like trade in coffee, tea, agricultural products, or clothing).</li> </ul>
	Individuals	<ul style="list-style-type: none"> <li>Large cash deposits or irregular financial activity by government officials working in wildlife protection agencies, border control, customs and revenue agencies, forestry agencies, or wildlife management authorities.</li> <li>Known wildlife traffickers will often make wire transfers to their relative's accounts, claiming that such transfers are for tuition, allowance, or family support payments.</li> <li>Airline travel to high-risk IWT routes paid for in cash or by third parties.</li> </ul>



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## Endnotes

<sup>1</sup> Financial Action Task Force, “Xiangmin Liu’s End of Presidency Statement,” (June 30, 2020), available at <http://www.fatf-gafi.org/publications/fatfgeneral/documents/chinese-presidency-outcomes.html>.

<sup>2</sup> This review, which focuses on how to make evaluation timelier and embrace the risk-based elements of the assessment progress, will inform revisions to the methodology for FATF assessments beginning in 2021.

<sup>3</sup> Financial Action Task Force, “Guidance for a Risk-Based Approach to Virtual Assets and Virtual Asset Service Providers,” (June 21, 2019), available at <http://www.fatf-gafi.org/publications/fatfrecommendations/documents/guidance-rba-virtual-assets.html>.

<sup>4</sup> Financial Action Task Force, “Guidance on Digital ID,” (March 6, 2020), available at <http://www.fatf-gafi.org/publications/fatfrecommendations/documents/digital-identity-guidance.html>.

<sup>5</sup> Financial Action Task Force, “Public consultation on FATF’s Recommendation 1 and its Interpretive Note,” (June 30, 2020), available at <http://www.fatf-gafi.org/publications/fatfrecommendations/documents/consultation-recommendation-1.html>. The relevant text of the proposed addition to Recommendation 1 is:

“Countries should also identify, assess, and understand the proliferation financing risks for the country. In the context of Recommendation 1, ‘proliferation financing risk’ refers strictly and only to the potential breach, non-implementation or evasion of the targeted financial sanctions obligations referred to in Recommendation 7. Countries should take commensurate action aimed at ensuring that these risks are mitigated effectively, including designating an authority or mechanism to coordinate actions to assess risks, and allocate resources efficiently for this purpose. Where countries identify higher risks, they should ensure that they adequately address such risks. Where countries identify lower risks, they should ensure that the measures applied are commensurate with the level of proliferation financing risk, while still ensuring full implementation of the targeted financial sanctions as required in Recommendation 7”.

<sup>6</sup> FATF’s non-binding guidance on proliferation financing, for example, says that an effective CPF approach would require measures beyond targeted financial sanctions. Financial Action Task Force, “FATF Guidance on Counter Proliferation Financing,” (February 2018), available at <http://www.fatf-gafi.org/media/fatf/documents/reports/Guidance-Countering-Proliferation-Financing.pdf>.

<sup>7</sup> Financial Action Task Force, “Priorities for the Financial Action Task Force (FATF) Under the Germany Presidency: Objective for 2020-2022,” (July 1, 2020), available at <https://www.fatf-gafi.org/media/fatf/documents/German-Presidency-Priorities.pdf>.

<sup>8</sup> Financial Action Task Force, “12-Month Review of the Revised FATF Standards on Virtual Assets and Virtual Asset Service Providers, (June 2020), available at <http://www.fatf-gafi.org/media/fatf/documents/recommendations/12-Month-Review-Revised-FATF-Standards-Virtual-Assets-VASPS.pdf>.

<sup>9</sup> Financial Action Task Force, “FATF Report to the G20 Finance Ministers and Central Bank Governors on So-called Stablecoins,” (June 2020), available at <https://www.fatf-gafi.org/media/fatf/documents/recommendations/Virtual-Assets-FATF-Report-G20-So-Called-Stablecoins.pdf>.



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<sup>10</sup> Financial Action Task Force, “Money Laundering and the Illegal Wildlife Trade,” (June 25, 2020), available at <https://www.fatf-gafi.org/media/fatf/documents/Money-laundering-and-illegal-wildlife-trade.pdf>.

<sup>11</sup> The intermingling of IWT with legitimate wildlife trade makes revenue estimates difficult. The FATF report provides a range from \$7 to \$23 billion per year. *Ibid.*, pg. 13.

<sup>12</sup> In a FATF survey of forty-five member-states, twenty-two considered themselves “source” countries for wildlife-related crime. Eighteen considered themselves “transit” countries and fourteen “destination” countries. *Ibid.*, 14.

<sup>13</sup> FATF Recommendation 14 deals directly with MVTs, and FATF has published guidance on risks arising from the sector. Financial Action Task Force, “Guidance for a Risk-Based Approach for Money or Value Transfer Services,” (February 2016), available at <https://www.fatf-gafi.org/media/fatf/documents/reports/Guidance-RBA-money-value-transfer-services.pdf>.

<sup>14</sup> The United for Wildlife Financial Task Force website is available at <https://unitedforwildlife.org/projects/financial-taskforce/>.

<sup>15</sup> The EIA website is available at <https://eia-global.org/>.

<sup>16</sup> The Liberty Shared website is available at <https://libertyshared.org/>.

<sup>17</sup> The TRAFFIC website is available at <https://www.traffic.org/>.