

Alternative remittance systems distinguishing sub-systems of ethnic money laundering in Interpol member countries on the Asian continent

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Abstract

Traditional methods of money movement on the Asian continent, called alternative remittance systems, have been discovered as efficient methods of laundering criminal proceeds in the wake of international legislative efforts aimed at laundering in the conventional banking system. A lack of information and understanding regarding the structure and operation of these systems has thus far precluded the criminal justice community from responding to their laundering activities.

The existing body of literature on ethnic banking systems does little to alleviate the confusion regarding their composition and aspects of operation. Estimates concerning the overall structure of alternative remittance in the Asia/Pacific range from one, uniform system of operation to the existence of multiple regional sub-systems. Further, although six different operational aspects are identified in the remittance process, the literature addressing systemic operational characteristics is riddled with contradiction.

A study of 31 Interpol member countries in the Asia/Pacific is conducted by questionnaire and telephone interview to test the hypothesis that two dominant and distinct alternative remittance systems prevail in the region; the first encompassing the Asian-oriental countries and the second covering the Indian sub-continent. The data set is comprised of the 21 Interpol countries reporting the presence of ethnic banking inside their borders.

Observational trends in operational aspects within each system lend support to the hypothesized existence of two distinct ethnic banking systems in the region. The hawala/hundi system and Asian-oriental system are distinguished from each other primarily through the type of funds laundered, the presence or absence of factors influenced by exchange controls, and the methods used to settle debts between ethnic bankers. A third group of Interpol member countries in the region are identified as hosts to the two primary systems, and do not appear to have indigenous systems of their own.

Introduction



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The ethnic or "underground" banking systems of the Asia/Pacific region, used for centuries as legitimate banking services in the region, have emerged as effective, efficient vehicles for laundering money. The very nature of these alternative remittance systems (ARSs) makes them uniquely able to conduct sizable currency transactions unhindered by current worldwide anti-money laundering efforts. Any attempt to formulate effective countermeasures must therefore flow from an understanding of the intricacies of their nature.

This study, conducted in concert with the International Criminal Police Organization Interpol, constitutes an effort to better understand the operation of alternative remittance systems. Comprehension of the basic characteristics of ARSs generates an understanding of their popularity as a money laundering method. A detailed knowledge of their unique characteristics may provide the insight necessary to combat their activities.

▲ **Alternative Remittance Systems**

The most basic, underlying characteristic common to the long-standing ethnic banking systems of the Asia/Pacific region is a strong cultural sense of honor and trust. A powerful sense of community and familial identity underscores many of the region's cultures, and translates to an ethnic sense of affiliation and obligation in both the home communities and in immigrant communities abroad. These cultural ties are the pillars of every transaction.

Ethnic bankers are often members of old, established banking families and are well known, powerful, and respected within their community (Nove, 1991). They are connected through a network of similar bankers in corresponding ethnic communities around the globe. Each banker enjoys a private reserve of cash, from either personal wealth or involvement in a cash-intensive business. Alternative remittances (see Figure 1) essentially involve one ethnic banker delivering money from his private reserve at the request of an ethnic banker in another country who is serving a client.

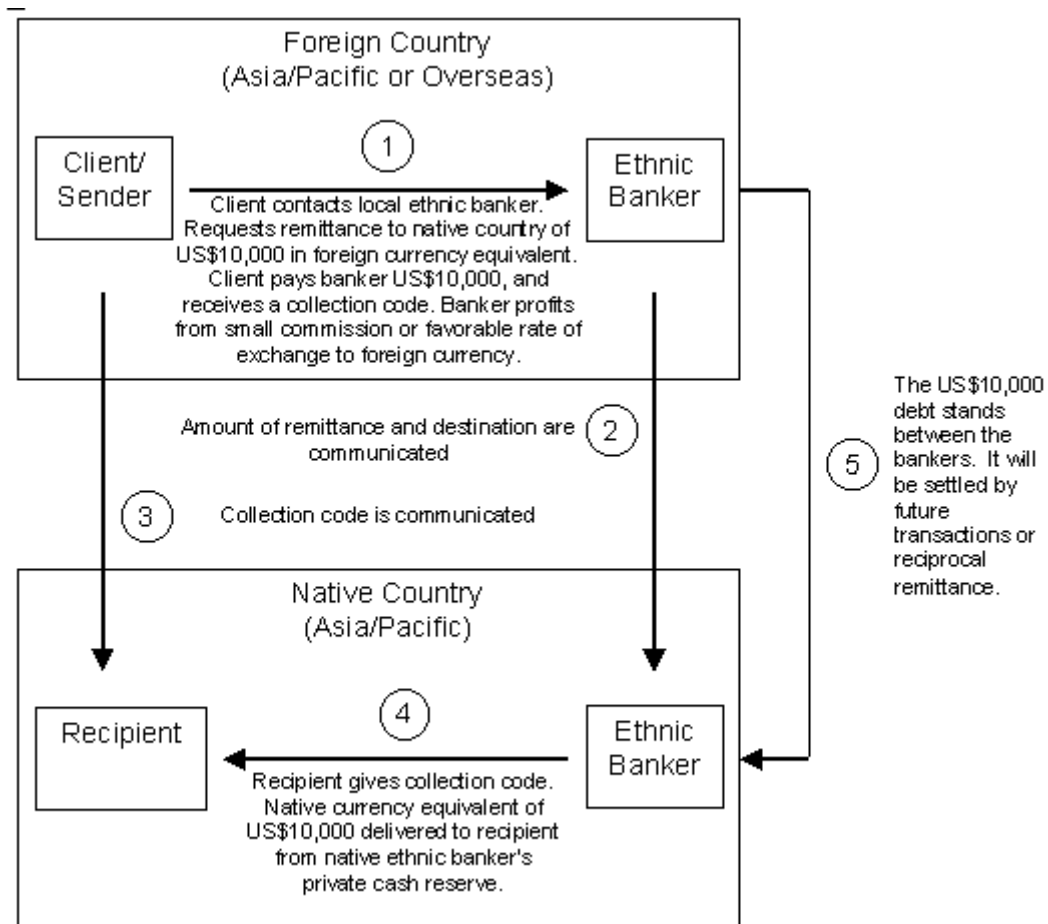


Figure 1. Basic sequence of communication and payment in an alternative remittance

Although the client wishes money be sent to a distant location, no money crosses a border physically and no money enters the conventional banking system. The transaction rests upon a single communication between bankers and is often not recorded or guaranteed by written contract. The trust between the two bankers secures the debt and allows the debt to stand, with no legal means of reclamation. In some cases, the trust between client and banker allows the money to be delivered to its destination even before payment is requested of the sender.

The debt between the two bankers is eventually cleared, either by remittances requested in the reciprocal direction or through a variety of money movement methods. Payment is guaranteed, however, because a broken trust is tantamount to community ostracism-- which constitutes economic suicide for an ethnic banker.

▲Emergence as a Money Laundering Method

Extensive emigration from the Asian continent has resulted in a worldwide network of ethnic communities. Although overseas, these immigrants retain strong ties with their home countries. Often these ties translate to a sense of obligation to support relatives back home (Cassidy, 1990). Many of these immigrants also bring with them a fundamental mistrust of central government and central banking systems that has been fostered over years of foreign occupation and political turmoil (Willoughby, 1990). Consequently, instead of the conventional or "Western" banking system, ethnic banking systems are relied upon to remit their earnings to relatives in the home nation.

Alternative remittance systems function in an entirely legal capacity when they remit the legitimate earnings of immigrant communities. For centuries these systems have

provided legitimate remittance and banking services for the peoples of the Asia/Pacific (Cassidy, 1990; Jost 1997). Whereas the systems themselves remain legal, they are increasingly being used in tax evasion and to provide growth capital and money laundering services for the criminal economy (Drug Enforcement Administration [DEA], 1994).

The popularity that ethnic banking enjoys with the criminal economy is due to several important factors. The first is the abundance of cash-intensive criminal proceeds found in the Asia/Pacific region. Cheng (1995) notes that the "golden triangle" and "golden crescent" of opiate/methamphetamine production combines with Asian-oriental organized criminal activity to produce large amounts of cash in need of laundering. The second and most compelling reason is that traditional avenues for laundering these proceeds have become increasingly restricted. Recent worldwide legislative efforts have made it slightly more difficult to launder large amounts of cash in the conventional banking system. The U.S. Bank Secrecy Act of 1970, Money Laundering Act of 1986, and 1998 Swiss Loi sur de Blanchiment d'Argent require reporting of large or suspicious transactions, identification of the source of funds and the economic beneficiary, and also provide for asset forfeiture. In contrast, alternative remittance systems are not regulated and can handle large cash transactions without leaving a paper trail. Ethnic banking systems are also popular because of their ability to serve remote Asian locations. Their ability to remit back to isolated villages works to the advantage of drug producers wishing to transfer funds out of those same areas. Finally, the DEA (1994) reports that alternative remittance systems are proving to be faster, cheaper, and more secure than laundering through conventional banking or physical smuggling.

▲Scale of the Problem

There are no known estimates of the current size and extent of money laundering through ARSs. The International Monetary Fund estimates the total criminal economy at US\$500 billion per year (Quirk, 1996), but there is no indication of what portion of that economy is laundered by alternative remittance systems. The DEA (1994) has named the underground banking system as the primary money movement method for drug proceeds in some areas of the world, and a sub-system as the principal method of movement for heroin profits and operating funds within Asia.

It is apparent that alternative remittance systems are functioning on a grand scale to launder the proceeds from a wide range of criminal activities, facilitate tax evasion, and provide a conduit for flight capital. These systems remain untouched by legislation aimed at curbing such activities in a recorded banking sector, and therefore offer an escape from enforcement measures.

▲Purpose of the Study

Very little information presently exists on the subject of alternative remittance systems. Few original studies have been conducted, reflecting the fact that reliable, first-hand information on ethnic banking is well guarded within immigrant communities and, to varying degrees, by the countries of the Asia/Pacific and the Middle East (see Appendix A for regional sub-divisions). As a result, the existing literature contains contradictory information regarding the operation of ethnic banking.

Further, there is a tendency in the literature to group all alternative remittance systems together. There is some indication, however, that the Chinese and Indian sub-continent systems share similar characteristics, lending the appearance of two prominent approaches to alternative remittance (DEA, 1994; Interpol, 1991). The existence of multiple regional sub-divisions could also be inferred from subtle variations between as well as within these two systems.

The purpose of this study is to delineate the operational characteristics of alternative remittance systems, and, in doing so, to discover whether distinctive sub-systems exist. Probing for these variations uncovers defining areas where each system may be vulnerable to efforts by the law enforcement community.

▲Overview of the Study

This study attempts to bring together all the available works on alternative remittance systems in combination with original information gathered from the Asia/Pacific region. The written material is first collated to provide a picture of what is presently known about alternative remittance systems and to illuminate areas of ambiguity and confusion. Some clarification is obtained by an Interpol written survey of the member countries of the region and telephone interviews of regional experts and national delegates to the Asia/Pacific Group on Money Laundering.

Although a similar 1991 Interpol survey was met with reluctance on the part of many member countries, regional governments since have demonstrated an increased willingness to deal with the problem of money laundering and to cooperate on an international level. The present study encountered a more positive response; and whereas some nations are still unable or unwilling to provide estimates and figures, enough information exists to conduct a qualitative analysis.

Information gathered in the survey is combined with the existing literature in order to form a conclusion as to how many types of alternative remittance systems are in existence and which characteristics define each type. This information will be provided to [Interpol's 179 member countries](#) and may serve as a useful tool in formulating a law enforcement response to the problem of money laundering in alternative remittance systems.

Review of the Literature

[Money Laundering](#)

[Criminal Justice Response to Money Laundering](#)

[Money Laundering in Asia](#)

[Money Laundering through Alternative Remittance Systems](#)

[The Structure of Alternative Remittance Systems](#)

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[Clientele - Profits - Trust and Payment - Receipts and Paper Trails - Debt Settling - Illegal Activities](#)

[Summary](#)

An examination of the available material reveals that although an extensive collection of work exists on the subject of money laundering, alternative remittance systems is an area little explored in the literature. Existing sources generally represent the efforts of individuals in law enforcement and state agencies. To date, few attempts have been made to combine these varied perspectives into a depiction of the overall structure of ethnic banking.

A review of the literature begins by placing alternative remittance systems within the context of money laundering. This is by no means intended to constitute a thorough review of the existing literature on money laundering, but rather to provide an overview of money laundering through the conventional banking system for the purpose of

comparison. A brief treatment of the criminal justice response to conventional money laundering follows. The unique instance of Asian money laundering is then discussed, with an emphasis on the effectiveness of the criminal justice response in the region. Alternative remittance systems are presented as an alternative to money laundering through the conventional banking system.

Following a review of money laundering, the existing literature on alternative remittance systems is examined. This section begins by addressing the overall structure of ethnic banking and concludes with a review of the operational aspects attributed to each system. Areas where the structure of the system is uncertain are identified, thereby defining the purpose and scope of the study.

▲ Money Laundering

The Interpol definition of Money Laundering as adopted in the General Assembly of 1995 is: Any act or attempted act to conceal or disguise the identity of illegally obtained proceeds so that they appear to have originated from legitimate sources. It is done both to evade detection by law enforcement authorities and to enable the criminal to use the profit generated by illegal activities. Although the need to conceal and convert the proceeds of crime is not new, the [Financial Crimes Enforcement Network \(1992a\)](#) cites a steady escalation in money laundering activity over the past few decades that coincides with the rapid growth of the drug trade. Just as money laundering activity has increased, so have attempts to understand the many and varied methods employed by the launderer.

Money laundering methods are broadly grouped into the three general areas of placement, layering, and integration. [Möbius \(1993\)](#) points out that these three categories, and the money laundering techniques they encompass, are simply variations on the single theme of "hiding the source of the income through a series of financial transactions".

Money laundering begins with the placement of the criminal proceeds in the legitimate financial system. Care must be taken not to raise suspicion about the size or source of the initial deposit. Large deposits are broken down into multiple smaller deposits and placed in several different financial institutions: a process known as structuring or "smurfing." Criminal profits can also be mingled with the deposits of a legitimate business and represented as income from that business. Often, when there are large volumes of cash to be laundered, the money will first be physically smuggled to a destination free of money laundering safeguards in the banking system, in order to facilitate easy placement. Smuggled cash can be carried personally, sent by courier, swallowed, or stowed inside hollow merchandise for shipment. Illicit profits can also be converted into other financial instruments, exchanged for higher denomination bills, or used to buy goods. Non-traditional financial institutions such as casinos, check cashing and postal services, currency exchanges, and precious metals brokers are often used for that purpose ([Financial Crimes Enforcement Network, 1992a](#)). The wealth is then transported to another jurisdiction in the form of money orders, traveler's checks, and luxury items to be sold or redeemed and deposited.

The layering stage in the money laundering process involves a series of financial transactions where the money is "moved" to generate distance from its original source. Once established in the conventional banking sector, the funds can be passed by electronic or wire transfer through a combination of front companies, banks, and shell corporations operating in financial tax havens. The goal is to obfuscate the trail of the money and ensure that any efforts to trace its origin are hindered by a complex trail and bank secrecy laws ([Rider 1992](#)).

The funds are ultimately made available for use through integration. At this stage, the money laundered through the financial sector is returned to the launderer and given the appearance of legitimate income. It may reappear as profit from a shell corporation or it may mix with the profits of a genuine enterprise. The launderer may receive the funds as a loan from an offshore bank, and re-pay the loan from an account containing the laundered money. Banking secrecy laws make it difficult for authorities to confirm the legitimacy of the loan or international income.

The [Financial Crimes Enforcement Network](#) (1992a) notes that, although placement, layering, and integration provide the basic framework for money laundering activity, money laundering schemes are complex and can involve combinations of techniques from each stage of activity. Structuring is employed both as a placement technique and as a tool for layering, and front companies serve to place illegal revenue in the banking system as well as to repatriate it as profits. Stages in the process may also recur out of sequence to further complicate the trail.

[Rider](#) (1992) acknowledges the stages involved in the money laundering process, but views them as parallel and interlocking rather than as progressive layers. This concept of transactions creating a web of mutual obligations highlights the fact that the money trail is most vulnerable to detection at its initial point of entry into the banking system.

▲Criminal Justice Response to Money Laundering

The criminal justice response at the national and international levels concentrates primarily on combating laundering activity in the conventional banking sector. U.S. measures to counter money laundering have focused specifically on the placement stage, targeting suspicious deposits ([Financial Crimes Enforcement Network, 1992a](#)). The Bank Secrecy Act mandates Currency Transaction Reports (CTRs) be filed for transactions exceeding US\$10,000 and records be kept of transactions between US\$3,000 and US\$10,000. Under the Act, financial institutions dealing with currency, traveler's checks, and money orders must report the identity particulars of individuals making large or suspicious transactions ([Financial Crimes Enforcement Network, 1992b, 1993](#)). The Money Laundering Act of 1998 extends that definition of financial institutions to include foreign banks, and requires that account holders justify holdings where the presumption of illegitimacy exists ("Foreign banks," 1998).

Similarly, recent Swiss legislation focuses on identifying the customer as well as the beneficial owner of funds ([Bosworth-Davies, 1998](#)). An obligation to clarify exists where the economic background and purpose of a transaction appears unusual or where links to criminal activity are suspected.

Money laundering activity in the conventional banking sector is also the target of inter-governmental and international activity. In his compilation of initiatives undertaken by such organizations as the Financial Action Task Force, the United Nations, Interpol, the European Community, and members of the Commonwealth, [Gilmore](#) (1992) comments that solutions thus far have featured two primary components. The first is an increased preventative role for the financial sector, making laundering through the banking system more difficult to accomplish. The second is a strengthening of criminal laws where money laundering activities are concerned. These components are well illustrated in the Forty Recommendations produced by the [Financial Action Task Force](#) (1990), as 22 of the 40 recommended anti-money laundering measures deal specifically with the role of the financial system and several others call for an increase in legislative activity and mutual legal assistance.

▲Money Laundering in Asia

Several unique factors in the Asia/Pacific region combine to manufacture high demand for money laundering services in the area. Political and economic instability in many nations of the region creates a desire to move currency abroad to more stable economies (Interpol 2000; MacDonald, 1994a). Rigid national policies regulating exchange and trade can also be a contributing factor.

Illicit proceeds are further produced by criminal activity in the area. Central Asia, the Golden Triangle, and the Golden Crescent are major centers for the manufacture of heroin, opium, marijuana, and methamphetamine (DEA, 1994). Revenue from the drug trade must be moved out of the area and laundered, or redistributed to other areas of production to cover operating costs. Criminal income is also generated by Asian-oriental organized criminal involvement in prostitution, human traffic, gambling, kidnapping, extortion, and drug trafficking (Cheng, 1995).

In addition to the abundance of criminal proceeds, Cheng (1995) cites three aspects of the Asia/Pacific region that combine to create a money laundering boom in Asia. The first is the presence of several major financial centers, notably Hong Kong and Tokyo, which provide access to banking facilities, communications, and financial markets. Secondly, some of the territories of the region lack regulatory controls over their financial sectors and legal provisions against money laundering, allowing laundering activities to continue unhindered. Finally, Cheng a need for hard currency in countries undergoing economic reform that leads to a welcoming, "no questions asked" policy regarding foreign cash investments.

Provisions against money laundering that do exist in the region mirror Western and international efforts, focusing on the tracking and seizure of assets in the conventional banking system (INTERPOL/FOPAC, 1996). Existing laws deal mainly with financial investigations involving the laundering of drug proceeds, with money laundering itself not specifically a crime (DEA, 1994; Lee, 1998; MacDonald, 1994b). Thus far, these regional legislative efforts at curbing money laundering in the conventional banking system have proven unsuccessful. The U.S. Department of State (1997), in a recent assessment of the global money laundering situation, rated 14 of the 32 Interpol countries included in this survey as areas of "Primary Concern," and a further five as areas of "Concern." The strength of the rating constitutes a measure of a country's vulnerability to money laundering, notwithstanding the effect of any countermeasures, and of the severity and nature of their money laundering situation.

One reason that money laundering continues to plague the region, despite an increased legislative response, is the presence of alternative remittance systems. ARSs provide an avenue for money laundering that circumvents laws aimed at detecting laundering in the financial sector and undermines the deterrent effect of any asset forfeiture provisions (DEA, 1994).

▲ Money Laundering through Alternative Remittance Systems

Florez and Boyce (1990) examine the difficulties and risks inherent in the process of money laundering through the conventional banking system. They find that physical smuggling of cash to areas of low regulation has the disadvantage of being bulky and carries a high risk of loss. That risk can be minimized through conversion to other monetary instruments and by placing the money directly into the banking system using structuring to avoid reporting requirements, but these techniques are time consuming. Moreover, use of the conventional banking system at any stage in the process creates a paper trail and leaves the activity vulnerable to detection by authorities.

Money laundering through alternative remittance systems, in contrast, does not carry the risks associated with laundering through the financial sector. Interpol (1991) reports that

ethnic banking is essentially no different than banking through conventional channels: in neither system is money actually transported, only debited and credited through the communication of data. The difference with ARSs is that little or no record of the communication remains, so the launderer leaves no trail. Furthermore, problems of risk, speed, and cumbersome sums of cash are not present in the ARS transaction. ([Interpol 2000](#)).

Sandhu ([Interpol 2000](#)) points out that alternative remittance systems function at all levels of the money laundering process. Placement is facilitated by incorporating criminal profits as the legitimate business deposits and expenses of an ethnic banker. Multiple remittances can occur in a layering process, or alternative remittance can be employed as a layering technique in a conventional money laundering scheme. Lastly, integration is accomplished again through the business front; as investment or disguised in the invoicing of imports and exports.

Alternative remittance systems function as dependable, efficient tools for laundering criminal proceeds in the Asia/Pacific region. In some ways they mirror the money laundering process in the conventional banking sector, and yet they function outside of the scope of law enforcement provisions designed to curb that process.

▲The Structure of Alternative Remittance Systems

The existing body of literature on alternative remittance systems reflects a diverse array of opinions regarding their composition and operation. To begin a review, literature on estimations of the overall structure of alternative remittance systems is presented. Assessments range from the existence of a single, universal system to the presence of multiple unique ethnic systems.

Nove (1991) and the [Commonwealth Secretariat](#) (1998) both view ethnic banking in its most simple systemic form, though they differ in their perceptions of its operations. Although Nove recognizes different regional labels given to alternative remittance systems, these differences are reported as a matter of nomenclature rather than an indication of systemic divisions. Chinese banking is referred to as "chop shop" and Indian sub-continent terminology includes "chiti", "hundi" and "hawala." In reference to operational details, Nove represents ethnic banking as a single, trust-based system, which he terms hawala. A report by the [Commonwealth Secretariat](#) (1998) also finds that the various terms used in reference to underground banking are interchangeable, and uses hawala to refer to the entire system. However, the Commonwealth Secretariat describes the hawala system as an organized system, with worldwide office branches under the control of single hawala bankers and a hawala council presiding to fix rates. Both Nove and the Commonwealth Secretariat emphasize a component of threat in the hawala system, reinforcing the trust element with fear.

A 1991 study by Interpol distinguished between two types of alternative remittance systems; grouping hawala/hundi banking and the chiti/chop shop system. Although "chiti" comes from the Indian language Hindi, it was introduced into China by the English and is thus used with chop shop to denote the Chinese system of alternative remittance. Interpol attributes the hawala/hundi system to the Indian sub-continent. Both systems are considered trust-based in nature and consist of networks of immigrant communities; the networks of the chiti/chop shop system extending throughout China, Southeast Asia, and North America, and the larger hawala/hundi system covering the Indian sub-continent, Southeast Asia, Europe, the Middle East, Africa, and North America. Interpol further identifies Thai and Vietnamese systems of underground banking which have adopted one or both of the larger systems and adapted the banking methods to incorporate their traditions and expertise. The Thai system, called "poey kuan", is said to have extended the remittance process to include intermediaries.

In Asian money movement methods (1994), the DEA identifies the Chinese and the hawala or hundi underground banking systems as the two primary systems. These systems are "identical in their adherence to trust, confidentiality, and efficiency" but exhibit some characteristic differences which are recognized by movers of drug money within Asia. The Chinese system is based in Hong Kong and Thailand and known as fei ch'ien, chop shop, hui kuan, and phoei kwan. It is based on ethnic trust, strengthened regionally and locally by bonds of ethnic subgroups, and as such, it is the preferred method for moving operating funds and profits within Asia. However, the DEA contends that the Chinese system is not as prominent internationally. As few Chinese systems exist in North America, remittances through the Chinese banking system lack convenience and the element of trust guaranteed by a large, interdependent network. They found that the hawala system, with its prevalence in North America, is regarded among the Chinese heroin traffickers as a more trusted network and therefore used as the primary overseas movement method for Chinese heroin profits.

Quite the contrary, [Willoughby](#) (1990) acknowledges the presence of a large Vietnamese system within the United States that is used extensively by the Vietnamese community for both legal and illegal remittances. The [DEA](#) (1994) mentions the Vietnamese system in stating that "most ethnic groups worldwide have an underground banking system of some form" , but does not mention whether these systems are thought to differ from the two main systems.

[Carroll](#) (1995), in a report on alternative banking in the Australian context, recommends a distinction between four types of alternative remittance systems based upon the services provided in each system. Carroll distinguishes these alternative remittance systems from underground banking in that they originated as remittance and lending services not specifically designed for illegal purposes. The first system, hawala/hundi, transfers money or value between locations without using conventional banking channels. This system exists in countries with direct connections to Asia and is distinctive in that it honors verbal commitments based on the honesty and trust of its bankers. The second and third systems are distinguished from the previous system in that they involve the issuance of a receipt as proof of a transaction. Both systems refer to ancient Chinese practice that evolved to eliminate the inconvenience of carrying goods or money over long distances. In the fei ch'ien system, southern traders would surrender the profits from their sales in the capital to a regional representative, in return for a certificate representing cash in the home province. Similarly, in the chit/chop shop system, a banker issued a receipt for deposit that could be removed to a foreign country and exchanged for local currency. A commission was charged for this service. The fourth system, hui, refers to a Vietnamese term for borrowing and lending. Unlike the preceding systems, hui is more a rotating loan association than a remittance method. Members of an ethnic community contribute to a general fund, which is loaned back to each contributor on a rotating basis. Also referred to as a mutual financing association ([Cassidy, 1990](#)), it often constitutes the only available source of financing for individuals and businesses unable to obtain assistance through the conventional banking sector.

[Interpol](#) (2000; see also [Mirza, 1996](#)) shares the vision of a distinct alternative remittance system in India and Pakistan, and use the terms hawala and hundi interchangeably in reference to that system. Contrary to other systems, the hawala system makes little use of negotiable instruments as "the components of hawala that distinguish it from other remittance systems are trust and the extensive use of connections" . [Interpol](#) (2000) further distinguishes the hawala system by emphasizing that alternative remittance is only part of its larger, overall operations. The banking function of the hawala system is intertwined with gold smuggling and money movement through import/export invoicing manipulation, forming a symbiotic relationship. Hawala is therefore portrayed by Jost as a multi-faceted enterprise, where opportunities for profit exist at each of the three stages in the relationship.

There is little indication that the Chinese system, or any of its regional offshoots, serve such a variety of functions. [Interpol](#) (1991), in an exploration of the Japanese system, describes a system that resembles the Chinese branch of ARS more so than the system of the Indian sub-continent. The Japanese system is focused specifically on remittance, indeed with closer ties to the conventional banking arena than any system previously described. Similarly, [McDonnell's](#) (1991) description of Vietnamese and Chinese systems operating within Australia, although termed hawala in the document, mirrors the Chinese system on the Asian continent in respect to reliance on receipts or chits.

▲Operational Aspects of Alternative Remittance Systems

Just as there are different views on the number of distinct alternative remittance systems and sub-systems, confusion exists as to the exact mechanics of operation within each system. This section explores the different operational aspects of the alternative remittance process as they are represented in the literature and examines the range of characteristics attributed to specific systems. Prominent aspects of ethnic banking are identified as: type of clientele, means of generating profit, degree of trust and payment sequence, presence of receipts and paper trails, method of debt settling, and extent of illegal involvement.

▲Clientele

The literature presents differing opinions on whether or not ethnic bankers openly advertise their services, as opposed to serving a select clientele. [Interpol](#) (1991) reports that underground bankers "solicit funds by open advertisement in the local vernacular press", but makes no distinction between the use of advertisement in the hawala versus the Chinese system. [McDonnell](#) (1991) relates that hawala dealers advertise their services in developed countries only, and [Interpol](#) (2000) documents instances where hawala is openly advertised in local Indo-Pakistani newspapers, and claim that advertisement is now also conducted on the Internet. Yet, in Nove's account of the hawala system he states that the hawala dealer "could not and would not advertise his services overtly" (1991).

Reporting on the workings of the Vietnamese and Chinese remittance systems, [Carroll](#) (1995) finds that neither system advertises publicly, preferring to restrict access to those within their own network. Similarly, Thai and Vietnamese marijuana suppliers have gained a competitive advantage over their U.S., Australian, and British competitors in the region, because nationals possess the necessary family connections to move and receive operating profits cheaply through the ethnic banking system ([DEA, 1994](#)).

The DEA goes on to report that the Chinese banking system does not have Japanese clientele, with organized crime groups favoring the conventional Japanese banking system. However, Japanese evidently have access to the Chinese system, with at least one major case of its use by the Boryokudan reported ([FOPAC, 1998](#)).

▲Profits

Profit in alternative remittance systems is generated either by charging a commission for remittance or by manipulation of official exchange rates. Many nations in the Asia/Pacific region employ exchange controls to regulate the flow of foreign and domestic currency across their borders. Exchange rates are set by the national central banks, and deviation from such rates is illegal. Ethnic bankers have lower business overhead than banks, enabling them to offer better rates of exchange than the official exchange rates and still profit from the transaction ([Interpol, 2000](#); [Mirza, 1996](#)). Hawala bankers also speculate on the natural fluctuations in currency demand to generate a return on their remittances.

[Interpol](#) (2000) contends that profit is generated in the hawala system by exchange rate manipulation, with hawala bankers able to profit on a 2% margin from official rates. Interpol FOPAC Officer Sandhu adds that exchange rates in a hawala transaction can vary according to continent and type of money remitted. Whereas hawala bankers may offer better-than-official exchange rates in North America, on the Indian sub-continent they can profit from offering lower rates to those willing to lose on exchange in return for laundering services.

[Nove](#) (1991) and the [Commonwealth Secretariat](#) (1998) both speak of one predominant hawala system, but differ on its method of generating profit. Nove says revenue is created through exchange rate differentials, whereas the Commonwealth Secretariat contends that all alternative remittance proceeds come from commissions. They quote a rate of 0.25% to 1.25% for legal remittances and 15% to 20% for illegal transactions. [Saltmarsh](#) (1988) sets the commission rate for hawala transactions between 0.25% and 0.65%.

Concerning alternative remittance in Asian-oriental areas, [FOPAC](#) (1998) finds commissions of 0.5% in Japan, and the Commonwealth Secretariat cites 20% for Vietnam (1998). Transactions in Hong Kong profit from a set fee of HK\$50 plus manipulation of exchange rates ([Carroll, 1995](#)).

▲Trust and Payment

Issues of trust and payment are intertwined in alternative remittance systems. The degree of trust embodied in a system is reflected not only in the relationship between bankers, but also in the relationship with the client. Therefore, trust can determine the point in the remittance where payment by the client is required.

[Interpol](#) (1991) attributes the operation of both the Chinese and hawala systems of ethnic banking to their trust-based networks. [Sandhu](#) (1998) reiterates the importance of the trust component in the hawala system. A strong bond between the hawala system in India and bankers in the Middle East means that the client is able to receive proof of the complete transaction before any payment is requested ([Interpol, 1991](#)).

Still, some of the literature contains skepticism regarding the degree to which trust plays a role in the hawala system. The [Commonwealth Secretariat](#) (1998), in their view of hawala as a centrally-controlled and franchised banking network, states that contracts are adhered to primarily because the parties fear punishment or death. As well, [Nove](#) (1991) mentions that fear acts as reinforcement for trust in the hawala system.

The DEA finds that some of the Asian-oriental systems have strengthened their trust-based nature with familial and regional bonds. Trust can be bolstered by membership in organized crime brotherhoods or by identification with an ethnic sub-group. A breach of that trust amounts not only to community ostracism but also to loss of social identity ([DEA, 1994](#)). [FOPAC](#) (1991) describes an arrangement between Japanese organized crime and the Chinese system on the continent, where funds are delivered to China before the amount of the remittance is deposited in Japan. Trust is likewise augmented with familial and marriage bonds ([McDonell, 1991](#)). One Thai branch of the Chinese banking system is comprised of an entire extended family ([DEA, 1994](#)).

Some systems are less accommodating in their remittances, requiring the client to deposit the entire sum before the transaction takes place. The underground banking system operating in Hong Kong and the Vietnamese and Chinese systems in Australia are cited as examples ([Carroll, 1995](#); [DEA, 1994](#)).

▲Receipts and Paper Trails

Paper trails can be created at several stages in the remittance process, but are generally sparse or non-existent in most systems. Written proof of a remittance system may take the form of banker's diaries, customer receipts, or records of shipping and conventional banking transactions used to settle debts between bankers.

The literature contains little mention of the personal recording practices of ethnic bankers. Cassidy (1990) says record keeping in the Chinese remittance system is nearly non-existent, with most transactions conducted by telephone and facsimile machines. If records are maintained, two sets may exist: one containing legitimate transactions, and a second, hidden "parasitic" account documenting off-the-books transactions. Cassidy advises that law enforcement attempts to decode these records are complicated by the need to distinguish traditional Chinese accounting practices from accounting entries recording illegal activities.

Documentation is also rare in the hawala system (Jost 1997). Remittances recorded by hawala bankers are often insubstantial and encrypted in the banker's personal shorthand. Diaries seized during the Jain hawala case in India consisted merely of jotted initials and numbers, and were difficult to decipher and connect to specific individuals (Kapoor, 1996).

Receipts or chits issued for remittances also create a paper trail. Receipts may take many forms; among them torn bank notes, marked notes, and "chops" (Chinese carved seals used as ink stamps). Although some systems continue to use chits as a regular remittance method, other systems have moved to embrace modern communication methods as an alternative.

The Commonwealth Secretariat (1998) and Nove (1991), in referencing a single hawala system, state that a chop or chit is always given in a transaction. Bank notes and pictures are torn in half, with one half given to the client and the other half sent by mail or delivered to the recipient. The two halves must be matched to complete the remittance. Sandhu claims that this practice is outdated in the hawala system. Mirza (1996) and Interpol (2000) concur that negotiable instruments are used little, if at all, in hawala. Instead, deliveries are placed and confirmed through telephone, facsimile, and e-mail. The hawala system even offers pick-up and home delivery of funds so a trail need not be created between banker and client (Mirza, 1996).

FOPAC (1998) finds use of modern communication predominates in the Japanese system, with no evidence of written receipts. However, according to Cassidy (1990), chops and chits continue to figure strongly in the Chinese system of remittance.

Finally, paper trails exist where ethnic bankers use the conventional banking system or import/export methods to settle their debt. The DEA (1994) and Sandhu (1998) suggest that all underground banking systems use the conventional banking sector at one point or another in the remittance process. Evidence of heavy reliance on conventional financial institutions is present in the case of remittances involving Japan and Hong Kong (FOPAC, 1998; Interpol, 1991). Interestingly, hawala bankers often intentionally create paper trails through invoice manipulation of exports and imports as a means of settlement of hawala dues. These traces of transactions serve to satisfy casual law enforcement inquiries and to authenticate the bankers' business (Interpol, 2000).

▲Debt Settling

Use of the conventional banking system to settle alternative remittance debts is most commonly associated with Asian-oriental banking in the literature. Carroll (1995) reports that the Vietnamese and Chinese communities within Australia telex transfer large sums of money back to their nations after structuring deposits in the banks. Presumably, some

of this money constitutes settlement of debts between ethnic bankers. Carroll comments further on the specific instance of underground banking in Hong Kong, finding that debts are cleared through the financial sector as well as by bulk smuggling of cash. The Chinese affinity for bulk smuggling is confirmed by the [DEA \(1994\)](#), although mention is made that a Thai sub-system prefers settling through banking channels involving known tax havens.

Accounts of the hawala system also evince debts settled in the conventional banking sector ([Saltmarsh, 1988](#); [Sandhu, 1998](#)). Yet, the literature demonstrates that hawala bankers rely to a greater degree on a variety of creative alternatives. As mentioned, in a 1999 presentation, FOPAC Officer Sandhu emphasized the interdependent nature of gold smuggling, invoice manipulation, and alternative remittance in the hawala system. Each of the three components function in a variety of ways: sometimes as the initial transaction, and other times as the method of settlement. The remittance itself may be the primary service, or function to pay for a shipment of smuggled gold. Gold and remittance debts are settled by invoice manipulation, as well. Movement of funds into the Asia/Pacific region is accomplished by importing goods from abroad with under-inflated invoices. The banker sells the merchandise, having paid a fraction of its worth, and keeps the difference as return payment for a remittance. Similarly, payment is made in the other direction. This time, a banker pays for imports at an invoice price that greatly exceeds their actual worth. The over-payment constitutes a transfer of funds out of the region to settle a debt with a banker overseas. This scheme is especially effective in countries with stringent exchange controls, as governments make special exceptions to currency control regulations in the case of payment for trade.

Money is moved through gold smuggling in much the same way. The demand for gold is high on the Indian sub-continent, especially in India, although its import is highly restricted (Jost 1997). Gold can be smuggled into India and sold at a profit, with the money used as a cash surplus to facilitate ethnic banking in the country. Often, the profits remain in India as payment for a remittance or shipment in the other direction.

The use of gold and invoices to settle debts in the hawala system is generally acknowledged in the literature, and frequently combined with mention of drug production and smuggling ([Commonwealth Secretariat, 1998](#); [Nove, 1991](#)). [Mirza \(1996\)](#) reports a strong link in Pakistan between drugs, underground banking, and gold smuggling.

▲Illegal Activities

The issue of illegality in alternative remittance systems arises in the generation of the fund surplus necessary to conduct remittances, as well as in the type of funds moving through the systems. [Interpol \(1991\)](#) lists several methods by which ethnic bankers illegally generate funds, although no method is attributed to a specific system of remittance. The illegality inherent in most of the methods is due to violation of exchange controls, and therefore only applies to components of the system operating under currency restrictions. Along with the aforementioned invoice manipulation, hard currency is generated by conjuring documentation for non-existent shipments in order to obtain foreign exchange releases. Foreign currency is also available from the central bank for the purchase of airline tickets, which are cashed in after the first leg of a journey for partial refund. Ethnic bankers will even corner foreign tourists, offering to pay the expenses in local funds for the duration of their stay, in exchange for their supply of hard currency.

Drug smuggling and traffic in humans and stolen goods can also produce cash surplus. [Interpol \(1991\)](#) mentions that these methods are more likely to be used in the Asia/Pacific, whereas funds are generated in the West by organized crime and fraud, in addition to the legitimate business earnings of bankers.

Illegality also exists in the practice of alternative remittance, as well as in the types of funds laundered in the various systems. [Interpol](#) (2000) points out that hawala itself is illegal in India and Pakistan, as currency speculation or dealings offering any rate other than the official exchange rate are prohibited. Moreover, India's Foreign Exchange Regulation Act of 1976 makes the invoice manipulation component of hawala a violation of customs regulations as well as exchange controls. Illegality in the hawala system also arises in the financing of gold and silver smuggling ([Interpol, 1991](#); [Mirza, 1996](#)), and in the movement of profits from the sale of drugs and armaments ([DEA, 1994](#); [Nove, 1991](#)).

Apart from laundering proceeds, hawala bankers are also in an excellent position to provide loans and operating capital for criminal enterprises ([Nove, 1991](#)). Using their legitimate business status, bankers can obtain short-term loans from the central bank to cover falsified trade bills. The funds are then re-loaned at a highly inflated interest rate to someone requiring operating funds for an illicit enterprise. When the debt is repaid, the banker not only profits on the interest differential but also builds excellent credit with the central bank.

Criminal activity is also facilitated by Asian-oriental alternative remittance systems. Accounts of the Chinese banking system feature the laundering of heroin and other drug profits through the ethnic banking network ([Cassidy, 1990](#); [DEA, 1994](#)). The Japanese system is highly involved in organized criminal activities, and has ties to alien smuggling networks in China ([FOPAC, 1998](#)). Finally, networks operating in the Philippines have become popular vehicles for laundering drug money and ransom ([Dobson, 1993](#)).

▲Summary

The systemic composition and operational characteristics of alternative remittance systems lack clear definition in the literature. Speculation about the structure of the system favors the concept of systemic division, recognizing differences between the Indian sub-continent and the Asian-oriental systems. Yet, accounts of many smaller regional banking networks raise questions regarding the existence of multiple systems or ethnic sub-systems.

Similarly, several different interpretations regarding the operational characteristics of each perceived system make it difficult to define specific systems. Broadly, the hawala system appears to have a wider range of clientele than Asian-oriental systems, possibly due to the use of advertisement. However, uncertainty exists regarding the degree and nature of the trust bond in different systems, and its effect on the remittance process. Profits generated by alternative remittance on the Indian sub-continent are most likely a function of exchange rate manipulation, rather than commission, and the degree to which systems leave proof of their profits and dealings is unknown. Contradictory reports on the subject lend credibility to the theory that regional variations exist. Asian-oriental remittance systems indicate a strong reliance on the conventional banking sector when settling debts between bankers, whereas hawala practices rely to a greater extent on the movement of gold and trade goods. Lastly, it is difficult to distinguish sub-systems in terms of involvement in illegal enterprise. Each systemic interpretation in the literature indicates some tendency to launder the proceeds of drug sales and other illicit activities.

Methodology



Survey Methods

The primary purpose of this study is to determine the structure and operation of alternative remittance systems. Combinations of operational characteristics are identified in an effort to ascertain the existence of specific systems or sub-systems. A survey of the available literature reveals enough significant differences in remittance methods to dismiss the likelihood of a single, overarching system in favor of a more complex systemic structure. Further, although the literature addresses a variety of operations, patterns are visible that suggest remittance methods can be broadly grouped into two general systems. It is hypothesized, therefore, that two dominant systems of alternative remittance exist: one covering the Indian sub-continent and termed hawala, and the other a system with Asian-oriental basis.

A qualitative approach was taken to test this hypothesis, for two reasons. The first reason is a matter of practicality and measurement. Present day attempts to estimate the extent of global money laundering activity and the size of the "black" economy rely on vague indicators like monetary demand, economic activity, and comparisons of tax returns with total income held in national accounts (Gupta & Gupta, 1984). A similar test conducted to determine the size of alternative remittance systems within the underground economy would essentially constitute an extrapolation from these already arbitrary figures. Further, conducting such a measure in an unrecorded banking system is implausible.

The second reason for doing a qualitative study is based on utility. As a matter of function dictating form, Interpol is responding to a need expressed by policy makers and the international law enforcement community. Having already acknowledged that ethnic money laundering constitutes a substantial problem, estimates of the size of the threat are not as necessary to those attempting to counter its effects as an analysis of its nature.

▲Survey Methods

▲Questionnaire

Interpol attempted a survey of "underground or parallel banking" for the first time in 1991. That survey was distributed to 19 Interpol member countries, and among the 7 responses received, 5 were from the Asia/Pacific region. The study provided a useful framework for understanding basic remittances, but unfortunately lacked full representation from the systems in the area.

The present study is a component of a larger study on money laundering in Asia and the Pacific, called project Asia Wash. The research process for the study began in June, 1998, with the distribution of a questionnaire to a purposive sample of nations in Asia, the Pacific, and the Middle East. The sample consisted of all 31 Interpol member countries in the region, who are grouped sub-regionally by Interpol as follows:

1. The Indian sub-continent of India, Pakistan, Sri Lanka, Nepal, and Bangladesh.
2. Iran, the Gulf Co-operation Council countries of United Arab Emirates, Saudi Arabia, Kuwait, Bahrain, Qatar, and Oman.
3. Japan and the Republic of Korea.
4. Association of South East Asian Nations (ASEAN) countries of Brunei Darussalam, Indonesia, Malaysia, the Republic of the Philippines, Singapore, Thailand, and Vietnam.
5. People's Republic of China and Hong Kong, China.
6. The eastern Mediterranean countries of Turkey, Cyprus, Israel, Lebanon, Jordan, and Syria.

7. Australia and New Zealand.

The survey was directed to the Interpol National Central Bureau (NCB) of each country, with a request that the NCB act as a coordinating body for responses. NCBs were asked to distribute the questionnaire to national experts in the fields of policing, law, economics and government.

The questionnaire, drafted by members of Interpol's FOPAC (Funds Derived from Criminal Activities) Branch, contained a one-page overview of alternative remittance systems. Respondents were asked whether alternative remittance systems function within their national borders and, if so, by what name. The survey requested a brief description of the remittance methods used, the currencies involved, and an estimate of the amounts transferred through the system per year. Countries were also asked to provide case examples of investigation and prosecution where money laundering is connected with ethnic banking.

The written survey realized a response rate of 38.7%, with 12 of 31 countries responding to the survey. In addition, two countries provided situation reports through the Asia/Pacific Group on Money Laundering. These reports provided more information than was requested in the Interpol questionnaire, and therefore constitute an increase in the written response rate to 14 of 31, or 45.2%.

▲Interview

Written surveys of the Interpol regional members were followed up by telephone interviews with experts in the region. A follow-up was considered necessary for several reasons. First, Interpol surveys of the region have historically encountered a poor response rate, decreasing the ability to generalize the findings. Second, and closely associated, regional political sensitivities may create a reluctance to comply with a written instrument, where fears may possibly be assuaged through personal communication. Third, bureaucracy can intervene to slow the return of the written instrument beyond the completion of the study, whereas the telephone affords an immediate response. Forth and finally, confusion in question response due to the complexity of the subject matter and linguistic barriers can be communicated and remedied with a telephone interview, providing more accurate and complete results.

Interview questions focused on the identification of specific operational characteristics observed in the ethnic banking systems within an expert's country.

Delegates to the Asia/Pacific Group on Money Laundering typologies workshop on "Underground Banking and Alternative Remittance Systems", March, 1999, chosen to represent their countries as national authorities on ARSs, were the subjects of this purposive sample. Occasionally, "snowball" sampling was used, where respondents provided the identity particulars of another expert in the field not included on the APG roster. Although the initial sampling of delegates for interviews and consequent snowball sampling call for concern regarding the validity and reliability of the information, the sampling methods were necessitated by the nature of the study. Knowledge of alternative remittance systems is globally uncommon, and the difficulty of locating someone learned in the subject is further complicated in a region where linguistic barriers intervene to restrict effective communication. Capable respondents were therefore not likely to be well represented in a random sample of officials in the region.

Telephone interviews were administered to 26 experts, representing 21 of the 31 Interpol countries; resulting in a response rate of 67.7%. Where possible, incomplete data fields were supplemented by an interview with a second expert from the same country.

In total, 25 of the 31 countries sampled participated in the study through at least one, if not both, of the survey instruments, generating an overall response rate of 80.6%. Results from the questionnaire have been combined with the findings from telephone interviews to test the hypothesis that two alternative remittance systems predominate in the Asia/Pacific region. Findings and conclusions are presented in the following two chapters.

Results

Trends in Observed Operational Aspects of ARSs

[Ethnic Bases](#) - [Illegal Activities \(Flight Capital - Laundering\)](#) - [Clientele](#) - [Profits](#) - [Trust and Payment](#) - [Receipts and Paper Trails](#) - [Debt Settling](#) - [Summary](#)

Common Methods of Alternative Remittance

[Hawala and Hundi Systems](#) - [Systems Present in the Middle East and the Gulf](#) - [Systems with Asian-oriental Bases](#)

Response to the survey instruments provided a working sample of 25 Interpol member countries in the Asia/Pacific, 21 of which report some form of alternative remittance system operating within their borders. Countries in the region not reportedly experiencing ethnic banking systems are Brunei, Darussalam, Cyprus, and Jordan. The study finds that alternative remittance systems function within Australia, Bahrain, Hong Kong, China, India, Indonesia, Israel, Japan, Kuwait, Malaysia, Nepal, New Zealand, Oman, Pakistan, the People's Republic of China, the Republic of Korea, the Republic of the Philippines, Sri Lanka, Saudi Arabia, Thailand, Turkey, and Vietnam. The responses of these 21 countries that affirm the existence of ARSs within their national boundaries comprise the data set.

The various operational aspects of the ethnic banking systems described by the 21 Interpol countries have been compared and contrasted in an effort to distinguish predominant systems. The results are presented in two parts: first, aspects are examined individually, and trends in reporting by the countries are revealed; second, these trends are assembled into systems sharing common methods of alternative remittance.

▲Trends in Observed Operational Aspects of ARSs

Observed characteristics of alternative remittance, in the 21 Interpol countries reporting the presence of such systems, are presented in eight sections. The first section, ethnic bases, comprises information regarding specific ethnic characterizations given to national systems or observed in systems operating within immigrant communities. The subsequent sections revisit previously mentioned aspects of remittance, and are entitled illegal activities, clientele, profits, trust and payment, receipts and paper trails, and debt settling.

▲Ethnic Bases

Answers concerning the regional terms used to describe the various remittance systems, the ethnic composition of those systems and their clientele, and the currencies involved in their transactions, divide naturally into three groups. The first group consists of underground banking systems termed hawala or hundi, with 4 of the 21 countries reporting the presence of both systems. India, Pakistan, Sri Lanka, and Nepal report the existence of hundi and hawala, with India and Sri Lanka making some form of distinction between the two systems. India considers the hawala system to be more international when compared to hundi. Hundi is described as a local banking system, issuing certificates of deposit that can be physically carried across India's borders to near-

neighboring countries and exchanged for local currency. The Sri Lankan hundi system is used primarily by the Muslim community as a payment method for imported goods. The hawala system is a conduit for more illegal monies and dealings, and is identified in Sri Lanka with the Tamil community. Each of the four countries denominates both hawala and hundi in rupees.

Another eight countries, although each not specifically naming their system, report its interconnectedness with the currencies and peoples of the Asian-oriental region. The Hong Kong, China "unregulated remittance centers" are reported to be Chinese in origin, serve the local Chinese, Vietnamese, Thais, Indians, Nepalese, and Filipinos, and deal in most South East Asian currencies. Similarly, the Japanese system has Chinese, Korean, Nepalese, Thai, Myanmar, Iranian, and Filipino clientele, and is said to function identically to the systems existing in those nations. Korean alternative remittance has close connections with Japan, as does the Thai system phoe kwan. Ethnic banking in Thailand is also strongly linked to Taiwan and Saudi Arabia. Filipinos, as well as Chinese, patronize the system in the Philippines. Finally, although no specific ethnicity is attributed to the clientele of the Vietnamese system, the Indonesian "bangelap" (dark bank), or the Chinese "di xia qian zhuang" (underground money shop), these national systems appear in the majority of Interpol member countries in the Asian-oriental region.

The final group is located geographically in the Middle East, the Gulf, and the Pacific, and contains the remaining nine countries. These countries do not describe a specific indigenous system, but find one or more immigrant communities within their borders operating their national systems or using these countries as conduits for their systems. Malaysia, Oman, New Zealand, and Saudi Arabia all recognize the hawala system, used by members of their Indian communities. New Zealand also gives the name hawala to the immigrant systems practiced by Somalis and Iraqis, using Jordan as a conduit country, and Saudi Arabia uses the same term for alternative remittance by Pakistanis, Indonesians, and Filipinos within its borders. Israel reports an ethnic banking system operating within their Filipino community but does not associate it with any specific term. Malaysia finds a Chinese system, distinct from the aforementioned hawala system, operating through traditional medicine halls. Its clients are Chinese, Thai, Singaporean, and Indonesian. Likewise, Australia finds "Asian systems" within immigrant communities, specifically Vietnamese and Myanmar. The various Asian national systems present are patronized not only by their own expatriates but also by immigrants from across ethnic lines. Remaining in this group are Turkey, Bahrain, and Kuwait. Alternative remittance in Turkey is practiced by Georgians and Azerbaijanis, and appears to link more closely with Eastern nations than with countries of the Asia/Pacific. Kuwait and Bahrain report the presence of ethnic banking, but can not identify its ethnic composition or any regional connectivity. However, other national experts in the region comment that the Gulf countries function as conduits for most systems, providing the financing necessary for trade and gold smuggling in hawala transactions. Further, national systems within communities of guest workers throughout the Gulf remit the earnings of those workers to families all over the Asia/Pacific region, including India, Kuwait, Lebanon, Hong Kong, Singapore, and other countries in Southeast Asia.

▲Illegal Activities

Thirteen of the 21 Interpol countries experiencing alternative remittance systems find that they function as a money laundering tool. These countries, scattered throughout the region and displaying no apparent pattern, are Hong Kong, China, India, Indonesia, Japan, Nepal, Pakistan, People's Republic of China, the Republic of Korea, the Republic of the Philippines, Sri Lanka, Thailand, Turkey, and Vietnam. Money laundering through alternative remittance systems is considered a possibility in Australia. Two countries, Oman and Bahrain, report that laundering is not a function of ethnic banking. The five remaining respondents were unable to comment on a possible relationship.

Interestingly, countries finding an absence of money laundering activity in their remittance systems, as well as some not offering comment, list capital flight and tax evasion among the services provided in those systems. This implies a distinction in the area of money laundering between money hidden to evade governmental regulations--however illegal such evasion may be--and laundering the proceeds of criminal activity. In order to make this distinction, the illegal activities reported in the various systems are presented as flight capital or laundering.

Capital Flight

The illegality involved in obtaining foreign currency and transporting currency across borders is dependent upon the presence of exchange controls at the national level. Therefore, alternative remittance is in itself criminal in countries where exchange controls exist to regulate the flow of currency across their borders. Exchange controls exist in 12 of the 21 Interpol countries reporting ARSs: Bahrain, India, Indonesia, Kuwait, Malaysia, Nepal, Oman, Pakistan, Sri Lanka, Thailand, Turkey, and Vietnam. However, in many of these countries, the routine remittance activities of ethnic banking systems that predate state-imposed currency restrictions are not policed, but rather are accepted and embraced within society. Some countries on the Indian sub-continent even report that ARSs are used by certain government officials and by businessmen who travel abroad to augment the inadequate foreign currency released to them because of foreign exchange restrictions.

Laundering

Interpol member countries of the Asia/Pacific record a variety of criminal proceeds laundered through their ethnic banking systems. Profits from the drug trade, arms smuggling, gold and gem smuggling, terrorism, corruption and extortion, gambling, and human traffic are laundered through the alternative remittance systems present in the region.

Money associated with the drug trade is laundered through ARSs in Hong Kong, China, India, Indonesia, Nepal, Pakistan, the People's Republic of China, the Republic of the Philippines, Sri Lanka, Thailand, Turkey, and Vietnam. Remittance systems in India, Sri Lanka, and Turkey encounter profits from arms smuggling. The Indian system also launders funds from smuggled gold and precious stones, terrorism, and corruption. Similarly, hundi or hawala is used in Pakistan to move money from gold smuggling and corruption. Sri Lanka makes a distinction between the hundi and hawala systems in that only the hawala system is used to launder the proceeds of illegal activities. Apart from monies derived from arms and drug smuggling, Sri Lankan hawala launders cash connected to terrorism and blackmail. The ethnic banking systems of Hong Kong, China, Indonesia, Japan, and the Republic of the Philippines are used to launder illegal gambling profits, and the proceeds of human traffic, including alien smuggling and ransom, are washed through alternative remittances in India, Japan, the People's Republic of China, the Republic of the Philippines, and Vietnam.

Using the three groups previously derived from the data on national ARS terms and ethnic composition, the sources of laundered funds in the ethnic banking systems of the Asia/Pacific Interpol countries are summarized in Table I. Countries are grouped into those reporting hawala and hundi systems, those connected to Asian-oriental systems, and those without an indigenous system that experience national systems within their immigrant communities or act as conduits for other systems.

Table I

Origin of Criminal Proceeds Laundered through Alternative Remittance Systems in the Interpol Member Countries of the Asia/Pacific

Source of Laundered Funds	Country Group		
	Hawala/ Hundi	Conduit/ Secondary	Asian oriental
Drug profits and operating funds
Arms smuggling	..	.	
Precious stones and gold smuggling	..	.	
Terrorism	..	.	
Corruption, bribery, and extortion
Gambling		
Human traffic

Note. • = One Interpol country of the Asia/Pacific region.

Operating funds and profits from the drug trade, laundered in 11 of the 21 Interpol countries in the region reporting the existence of alternative remittance systems, are distributed primarily between the hawala/hundi group and the group demonstrating interconnectedness between the Asian-oriental countries of the region. Similarly, monies associated with corruption, bribery, and blackmail do not favor one of the three groups. However, examination of the countries laundering funds from smuggling and terrorism uncovers a concentration in the countries reporting hawala and hundi systems, with a lesser presence in the secondary and conduit countries. Conversely, little evidence of the proceeds of human traffic and gambling appears in these countries, with those profits laundered primarily in the Asian-oriental group. Whether patterns suggested by this analysis exist due to tendencies in alternative remittance systems or are simply reflective of regional criminal preponderances is not known.

▲ Clientele

Only 4 of the systems in the 21 countries contributing data use advertisement to attract clientele, whereas 11 report that word of mouth generates select patrons for their ethnic banking systems. Six countries did not comment on the aspect of clientele in their alternative remittance systems. Advertisement is found in the Asian-oriental systems present in Australia, Indonesia, Japan, and the Republic of Korea, but does not necessarily preclude the generation of clientele through referrals.

Systems in Bahrain, Hong Kong, China, India, Malaysia, Nepal, New Zealand, Oman, Pakistan, the Republic of the Philippines, Sri Lanka, and Thailand do not advertise. Although hawala is not advertised openly in India as it violates exchange control regulations, it is advertised in many Indian communities in the West. Indeed, there is a strong correlation between national ARSs who do not advertise and the presence of national exchange controls. Nine of the 11 countries where ethnic banking systems are not publicized enforce currency exchange controls. Similarly, of the four countries in the region known to advertise, only Indonesia has restrictions on currency movement. However, advertisement in Indonesia does not directly mention the underground banking system, but instead makes reference to "improving" money. The close association between the presence of exchange controls and the use of advertisement suggests that caution is required in inferences concerning systemic trends in this aspect of alternative remittance.

▲ Profits

Alternative remittance systems in Australia, Japan, the Republic of Korea, Nepal, New Zealand, Sri Lanka, Turkey, and Vietnam profit by charging a commission. Three countries, India, Pakistan, and Malaysia, profit by both commission and exchange rate

manipulation, although profit by exchange is the most popular method in India. Manipulation of official rates of exchange is the primary method of profit in the remittance systems of Oman and Thailand. The remaining 8 of 21 countries in the data set did not respond.

Reports on the rate of commission range between 0.5% to 5% of the remittance, depending on the situation. Exchange rate differentials on regular ethnic banking transactions fall between 0.5% and 3% of the sum remitted. However, rates in India and the Gulf can be as high as 30% when the demand for hard currency in a transaction is high.

No regional trends are evident in the distribution of profit methods. However, the connection between the method of generating profit and the presence of exchange controls must again be noted. Clearly, profit from manipulation of official rates of exchange is only possible in countries where exchange controls are employed. Each of the five countries that profit through exchange report the presence of such controls. Remittance systems in the region operating on commission demonstrate less of a pattern. Five of the 8 countries where commission is the form of profit in alternative remittance--Australia, Hong Kong, China, Japan, the Republic of Korea, New Zealand--do not have exchange controls. Yet, despite the presence of such controls in Nepal, Sri Lanka, and Turkey, these systems rely on commission for their profits rather than exchange.

▲Trust and Payment

Eight of the 21 countries reporting remittance systems in the Asia/Pacific request payment from the client before the transaction is carried out. Systems in Bahrain, Indonesia, the Republic of Korea, Malaysia, New Zealand, Oman, Pakistan, and Thailand require payment made to the banker or an account at the beginning of the remittance sequence. Payment is generally received before the transaction in Australia, Hong Kong, China, India, Japan, and Nepal, however, on rare occasions, it is accepted after the remittance has been made. In Nepal and Hong Kong, China, this exception is based on the relationship between banker and customer. In India, more practical considerations are weighed, with exceptions in the payment sequence contingent primarily on credit worthiness, and then on the volume involved in the transaction and the banker-client relationship. No observable regional trend exists to distinguish the five countries with systems allowing exceptions to the order of payment from the eight requiring payment before the transaction. The remaining eight countries could not speculate on the remittance sequence.

No evidence was discovered to support the conceptualization of alternative remittance systems as organized, hierarchical networks; indeed, each expert surveyed reiterated the foundation of trust and ethnic networking that underlies these systems. Hong Kong, China found that the element of trust was bolstered by some connection to triads. Further, no evidence was obtained that an element of fear or violence exists to reinforce the remittance process. Every one of the fourteen countries responding to the question dismissed the idea of a violent element in ethnic banking.

▲Receipts and Paper Trails

Little is known about the use of receipts and diaries in the alternative remittance systems of the Asia/Pacific, as evinced by the response of only 9 of the 21 countries. Hong Kong, China reports that transaction diaries are well kept, although in shorthand, and customer identity records are maintained until the remittance is complete. Personal, coded diaries are also used to varying degrees by bankers in the alternative remittance systems of India, Indonesia, Japan, Malaysia, Nepal, Pakistan, Sri Lanka, and Thailand. Banker's

diaries appear to be a part of alternative remittance systems in all regions of the Asia/Pacific.

In the Indian hundi system, the word hundi signifies a receipt for a deposit, much like regular banking. However, unlike conventional banking, no name is written on the receipt such that any bearer can redeem it. These negotiable instruments are used in Indian hundi to transport funds safely over immediate borders, and are honored in local currency in the neighboring country. Chits are also issued in the Pakistani hundi system, as well as in Nepal. Hong Kong, China finds that chits are given in the early stages of a transaction and destroyed afterwards to remove any evidence of the remittance.

The use of receipts or chits seems predominate in the hundi systems of the Indian sub-continent, although caution must be exercised in not extending the generalization to the other systems of the region. There is insufficient data for speculation about the use of receipts in the ethnic banking systems of the Middle East, the Gulf, and the Asian-oriental countries. However, 13 of the 21 Interpol countries in the region note that communication between bankers has evolved with technology to employ the telephone and facsimile machine in place of written communication of remittance, suggesting that chits are no longer popular in the systems of the Asia/Pacific.

▲Debt Settling

Debt settling is carried out in the ethnic banking systems of the Asia/Pacific Interpol member countries through a variety of methods, including reciprocal remittances, gold smuggling, invoice manipulation, conventional banking channels, and physical smuggling of cash across borders. Offsetting remittances are relied on in the hawala and hundi systems of India and Nepal, as well as in the hawala system present in Malaysia and the Asian-oriental system of Hong Kong, China. Gold smuggling is used to settle debts in India and Pakistan. The hawala and hundi systems in India, Nepal, Pakistan, and Sri Lanka also use over- and under-invoiced trade goods, as does the Vietnamese system. Further, the Chinese medicine halls of Malaysia manipulate their supply invoices to settle their remittance accounts.

Use of the conventional banking system occurs in the Asian-oriental systems of Australia, Hong Kong, China, Japan, Korea, and Thailand. Regular banking channels are also mentioned as a rare method of debt settling in Pakistan and Sri Lanka. Finally, accounts between bankers are reconciled by physically repatriating cash in the systems of Hong Kong, China, Pakistan, the Republic of the Philippines, and Vietnam.

For purposes of analysis, the debt settling methods attributed to ARSs of Interpol member countries in the Asia/Pacific are presented in Table II. Country responses are arranged according to their self-identification with the hawala and hundi systems or integration with predominately Asian-oriental systems. As debt-settling methods in countries without their own indigenous systems are reported according to the ethnicity of the immigrant communities, those responses are also included in the appropriate groups to facilitate comparison.

Table II
Debt Settling Methods in Alternative Remittance Systems in the Interpol Member Countries of the Asia/Pacific

Debt Settling Method	Country Group	
	Hawala/ Hundi	Asian oriental
Reciprocal Remittance	...	

Invoice Manipulation	***	.
Gold Smuggling	..	
Conventional Banking		*****
Physical Smuggling of Cash	.	***

Note. • = One Interpol country of the Asia/Pacific region

A clear distinction is present in the methods of reconciliation favored by each regional group. Countries reporting the hawala and hundi systems find that those systems rely primarily on offsetting remittances, trade, and smuggled gold to settle debts between ethnic bankers. In contrast, alternative remittance systems with close connections to the countries and peoples of the Asian-oriental region rely on regular banking channels and the physical transport of cash to remedy debits and credits.

The ability to reconcile debts through the conventional banking system depends to a great extent on the absence of exchange controls in the Asian-oriental Interpol member countries. All but one of the Asian-oriental countries that settle debts through regular banking are free of such economic restrictions. Similarly, every one of the Interpol countries using the hawala and hundi systems are under the influence of national exchange controls. Although it is not possible to determine matters of cause and effect in these relationships, it seems that methods of remittance and national economic policies have adapted to accommodate each other.

▲Summary

The different operational aspects identified in the alternative remittance systems of the Asia/Pacific region vary with respect to their usefulness as systemic indicators. The presence or absence of banker's diaries and the order of the payment sequence provide little systemic indication when the distribution of reporting countries in the Asia/Pacific is plotted. In contrast, strong regional patterns are evident in the type of funds laundered in each system, their methods of debt settling, and the use of receipts in the reporting countries of the Indian sub-continent. Finally, although use of advertisement and method of profit appear to be strong systemic indicators, their usefulness in that capacity is constrained by a close correlation with the presence of exchange controls, suggesting a possible spurious relationship.

▲Common Methods of Alternative Remittance

Like characteristics in the operational aspects of ethnic banking are observed in alternative remittances conducted in the Asian-oriental region, as well as in the systems identified as hawala and hundi. There is no indication in the available data that systems present in the Middle East and Gulf regions possess sufficient unique characteristics to be considered distinctive methods of alternative remittance. The operational aspects of the two recognizable systemic groupings, as well as the characteristics of the systems present in the Middle East and Gulf regions, are summarized in the following sections.

▲Hawala and Hundi Systems

Hawala and hundi systems are the method of alternative remittance in the countries of the Indian sub-continent. Their ethnic base is Indian, Pakistani, Sri Lankan, and Nepalese, and they serve these communities on the continent and abroad. Hawala and hundi systems operate within the Interpol member countries of Malaysia, New Zealand, and Oman, as well as on the European and North American continents.

Some countries report differences in the functions performed by these systems on the Indian sub-continent. Hundi is recognized as a more regional system used to safeguard funds during cross-border travels and to facilitate the purchase of goods, and as such involves the issuance of a written receipt. Hawala is a more international system, does not involve negotiable instruments, and is associated with criminal activities more so than the hundi system. However, distinctions between the hawala and hundi systems are disparate and do not pervade the region.

Although some differences are perceived in the two systems, their methods of remittance appear identical. Each system launders the proceeds of drugs, gold, terrorist activity, and corruption, and engages in the facilitation of flight capital by virtue of the exchange controls present in the national economies of the region. Advertisement is not used to attract clientele. Communication between bankers is conducted by telephone and facsimile machine, with chits used only in regional remittances through the hundi system. Bankers in both systems generally keep coded diaries. Payment in the remittance sequence can occur both before and after the transaction, and profit is generated by exchange rate manipulation and commission at rates indistinct from other systems in the Asia/Pacific. Finally, debts between bankers in hawala and hundi are settled primarily through reverse remittances, gold smuggling, and invoice manipulation.

▲Systems Present in the Middle East and the Gulf

The Interpol countries of the Middle East and the Gulf observed that regional ethnic banking systems tend to launder the profits of the drug trade, gold smuggling, extortion, and terrorism not unlike the neighboring hawala/hundi systems of the Indian sub-continent. However, information regarding the specific operational aspects of the systems within the countries of the Middle East and Gulf regions is not available and may not exist. Experts in neighboring regions report that alternative remittance systems in the Gulf area are used as a conduit and financing mechanism for the gold trade into the Indian sub-continent.

▲Systems with Asian-oriental Bases

Systems in Interpol member countries of the Asian-oriental region--Hong Kong, China, Indonesia, Japan, People's Republic of China, the Republic of Korea, the Republic of the Philippines, Thailand, and Vietnam--evince a great deal of interconnectedness among them. They tend to launder the proceeds of the drug trade, gambling, and human traffic. Most of these systems do not operate under the umbrella of exchange controls, and, consequently, do not facilitate capital flight and are free to advertise their services.

Remittance operations in Asian-oriental systems are conducted by telephone and facsimile machine, with written receipts likely not given. As in the hawala and hundi systems, ethnic bankers generally keep coded journals. Payment is required of the client before the remittance occurs, and bankers profit from the transaction primarily through commission. The Asian-oriental systems differ from the systems of the Indian sub-continent in that debts are settled between bankers principally through conventional banking channels and physical repatriation of currency.

The following chapter summarizes these findings and examines their relevancy in light of the research hypothesis. The study concludes with recommendations for further research, taking into account the strengths and limitations of the present work.

Conclusions



Ethnic banking systems in the Asia/Pacific region began centuries ago with moneychangers and receipts to facilitate the travel of goods and wealth over long distances. Today, they parallel the conventional banking sector and still provide essential banking services for many in the region. However, the very nature of these systems also makes them tremendously capable providers of laundering services for the criminal proceeds that abound in the Asia/Pacific. It is the intent of this study to reveal the nature of alternative remittance in the region, such that anti-money laundering enforcement efforts might effectively be directed at curbing their laundering activity.

A review of the literature reveals a lack of clarity and consensus regarding the regional structure of ethnic banking and the operational characteristics defining each component system. Speculation about the overall composition of the system, and the different operational aspects present, favors a multi-systemic definition of the alternative remittance situation in the Asia/Pacific.

Based on available knowledge of Asia/Pacific ethnic banking systems, a study of 31 Interpol member countries in the region tests the hypothesis that two dominant and distinct alternative remittance systems prevail--one encompassing the Asian-oriental countries and the other covering the Indian sub-continent. Member countries surveyed by written questionnaire and telephone interview produced a sample of 21 countries observing ethnic banking within their borders. Analysis of the data describing the operational aspects of these banking systems supports the hypothesis of two distinct regional methods of alternative remittance. Specifically, the sources of the laundered funds, the means of debt settling, and the methodological impact of national exchange controls are features that distinguish a hawala/hundi system of the Indian sub-continent from an Asian-oriental system.

A final observation derived from the survey regards the degree of cooperation and openness experienced in the region. It is concluded that present efforts to study money laundering in the Asia/Pacific are being met with significantly more enthusiasm and cooperation than those of the past. However, many countries are still reluctant to share knowledge at an international level--a problem certain to hinder future enforcement efforts.

Michel Camdessus, Director of the IMF, states of enforcement efforts that "money being laundered will flow quickly to the weakest point in the international system" (1998,)direct quote. Understanding the nature and operation of the alternative remittance systems in the Asia/Pacific region is a necessary step towards effective measures in an area where laundering has thus far escaped international enforcement efforts.

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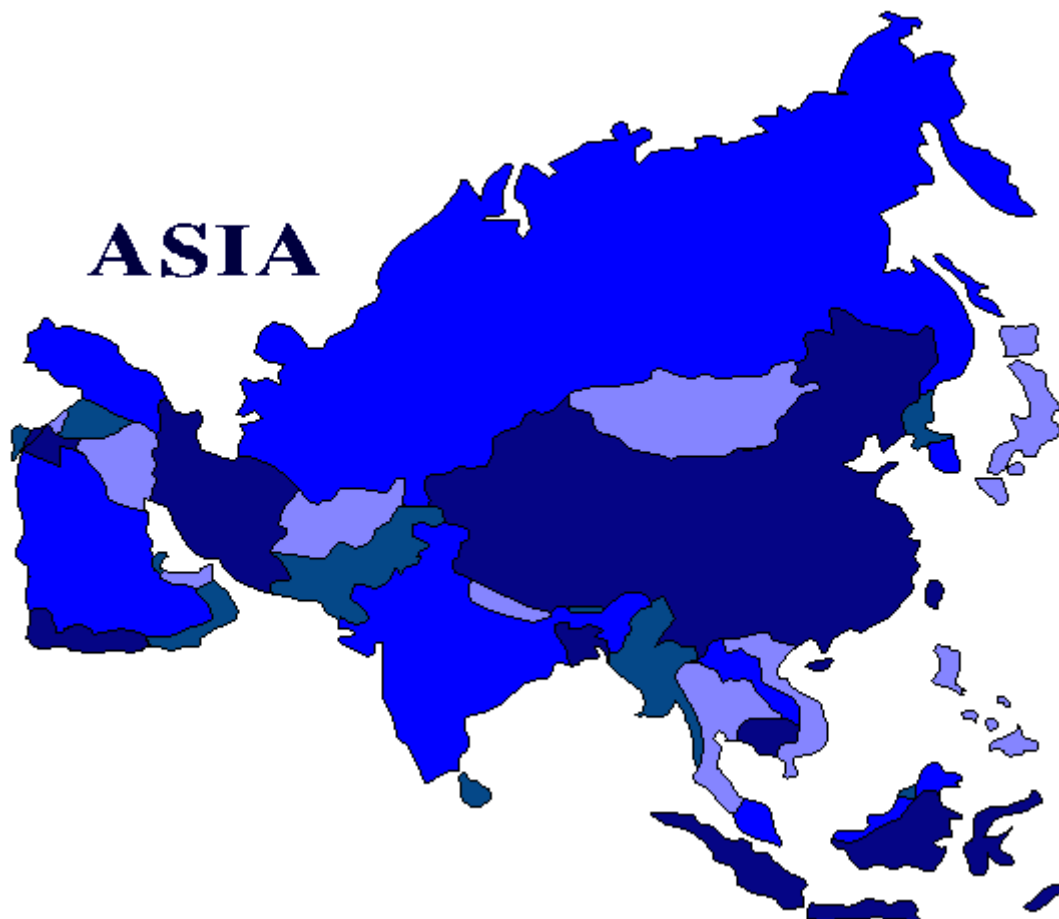
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Appendices

- A Map of the Asia/Pacific Region
- B Alternative Remittance Segment of Interpol Questionnaire
- C Interpol Member Countries of the Asia/Pacific Region and their Response to the Survey Instruments
- D Questions for Telephone Interview

▲Appendix A

Map of the Asia/Pacific Region





▲Appendix B

Alternative Remittance Segment of Interpol Questionnaire

§G-10:

What other methods are used to launder money in [Country]? (e.g. Alternative Remittance Systems/underground banking systems)

By what name(s) are these methods known in [Country]? (e.g. hawala, hundi, chop shop, hui)

Please provide a brief description of how this system works in your country. Include any relevant case examples.

Estimate how much money is transferred through alternative remittance/underground banking systems, per year, in [Country].

What currencies are transferred through alternative remittance/underground banking systems in [Country]?

§B-8:

Does unconventional, parallel or non-traditional banking exist in [Country]?

Yes – No

If yes, is it a major economic factor?

Yes – No

If yes, please provide details:

▲Appendix C

Interpol Member Countries of the Asia/Pacific Region and their Response to the Survey Instruments

ICPO-Interpol Member Country	Questionnaire Response	Interview Response	Reported Existence of ARSs
Australia	Y*	Y	Y
Bahrain	N	Y	Y

Bangladesh	N	N	-
Brunei Darussalam	N	Y	N
Cyprus	Y	N	N
Hong Kong, China	Y	Y	Y
India	Y	Y	Y
Indonesia	Y	Y	N,Y
Iran	N	N	-
Israel	N	Y	Y
Japan	Y	Y	Y
Jordan	N	Y	N
Kuwait	Y	N	Y
Lebanon	Y	N	-
Malaysia	Y	Y	Y
Nepal	Y	Y	Y
New Zealand	Y	Y	Y
Oman	N	Y	Y
Pakistan	Y	Y	Y
People’s Republic of China	N	Y	Y
Qatar	N	N	-
Republic of Korea	N	Y	Y
Republic of the Philippines	N	Y	Y
Saudi Arabia	N	Y	Y
Singapore	N	N	-
Sri Lanka	N	Y	Y
Syria	N	N	-
Thailand	N	Y	Y
Turkey	Y	Y	N,Y
United Arab Emirates	N	N	-
Vietnam	Y*	N	Y
Response Rate (Y)	14/31 45.2%	21/31 67.7%	21/31 67.7%
Overall Response Rate (Y) (Questionnaire or Interview)	25/31 80.6%		
Respondents Reporting ARSs	21/25 84%		

* Situation report provided in lieu of the Interpol survey.

▲Appendix D

Questions for Telephone Interview

Expert contact:

Country:

Telephone:

Time Zone:

- Is alternative remittance illegal in your country?

- Do Alternative Remittance Systems function within your national boundaries?
 Yes ☐
 No ☐
 If Yes:
- What function does alternative remittance serve in your country (ie. repatriation of earnings, money laundering, tax evasion, capital flight, etc.)?
- If laundering occurs through the system, what is the source of the illegal funds?
- What ethnic system(s) are prevalent and how are they regionally termed?
- Is advertisement used to attract clientele?
 Yes ☐
 No ☐
- How would you describe the ARS clientele, in terms of ethnic background and social status?
- How would you describe the ARS bankers, in terms of ethnic background, social status, and occupation?
- Do bankers appear to be joined by any special regional, ethnic, familial, and/or gang connections?
- What is the preferred method of communication within the system?
 Fax ☐
 Telephone ☐
 Chit ☐
 Other (specify)_____
- When is payment requested in the remittance sequence?
- What, if any, records remain as proof of a transaction (ie. receipts, diaries)?
- How are debts settled between bankers?
- Is there any indication that violence is used in the system?
- How is profit generated in the system, and at what rate?