

## Card tricks

By David Malamed

Illustration: Blair Kelly



### Drug traffickers, terrorists and other criminals have found a simple and ingenious way to launder their dirty money

Ronnie had too much cash under his bed. Literally. A small-time drug dealer, he had been storing the considerable profit from his illegal activities in a compartment he had built under the bedframe. About six-inches deep, spanning the length and width of his queen-sized bed, it was jammed with dollar bills, mostly 20s, 10s and fives. (Ronnie is a fictitious character and the scenario is a composite of cases.)

An MBA graduate, who discovered he loathed the corporate office environment, Ronnie came up with the idea of delivering marijuana directly to customers after listening to several middle-class friends complain about how hard it was to obtain the drug without putting themselves into dangerous situations, such as trying to buy on the street.

Ronnie sold only to people he knew well or who were referred to him by someone he trusted. He obtained his product from two cousins who grew pot on farmland in an isolated area. He bought a small van that looked like a delivery vehicle and wore a nondescript uniform, including a shoulder sack that made him look like someone dropping off a courier package.

People appreciated the convenience of having their drugs brought to their home or workplace. Within a year of launching his business he had built up a client list that kept him driving throughout the city up to 10 hours a day, five days a week. The cash quickly accumulated and he realized he needed to find a way to launder it.

Ronnie knew he could deposit up to \$10,000 in cash into his bank account without it being reported to the Financial Transactions and Reports Analysis Centre of Canada (FINTRAC). Set up in 2000, the independent government agency was established to detect and prevent money laundering and terrorist financing. But Ronnie also sensed that a canny bank employee could figure out that a customer who regularly deposited large amounts of cash might be up to no-good. He couldn't, and wouldn't, take that risk.

Then he had a eureka moment. A newspaper article about the boom in prepaid debit and loyalty cards, also known as stored value cards (SVC), suggested a safe solution. The cards, he read, could be purchased from banks, cheque-cashing companies, Western Union, casinos and other sources without any identification and without any paper trail back to him. The article spoke directly to him: "They are also being used by drug dealers, terrorists and others who need to launder dirty money," it pointed out, citing a dark side to the otherwise convenient and popular cards.

Ronnie visited outlets throughout his city and the surrounding areas that sold prepaid debit cards. Using cash, he loaded them with various amounts, usually less than \$3,000, occasionally more. Without much effort he could launder \$50,000 in a two-day period, if so inclined. He then used the cards to pay for most of his day-to-day transactions. For large-scale purchases, he would build the balance on one card until he had enough for whatever he wanted to buy. He also used the cards to pay for the pot. Although it took some effort, the process gave Ronnie a peace of mind that he considered well worth the time involved.

The drug dealer was not the only person on the wrong side of the law to find prepaid cards an attractive way to launder money. "Criminals like them because they potentially offer a high degree of anonymity, are easy to transport and have some similar qualities to electronic wire transfers," says Mario Possamai, a certified anti-money laundering specialist and Toronto-based anti-money-laundering compliance and fraud consultant. "The more people legitimately use SVCs, the easier it is for money launderers to hide their illicit activities among them. It's reminiscent of Mao

Tse-Tung's famous quote about guerrilla warfare: 'The guerrilla must move among the people as a fish swims in the sea.' "

The sea that is the prepaid card industry is a vast expanse. No one is certain of how large it is, although industry assessments make it clear the number is huge and growing. In a March 2008 report, FINTRAC estimated that the prepaid card market would grow to almost US\$300 billion in the US by the end of 2010 and Visa International estimated it will grow to US\$2 trillion worldwide by 2010. Eighty-two per cent of Canada's largest retailers offered prepaid cards, including gift cards, to clients in 2005, up from 53% in 2003. Network-branded prepaid cards, such as Visa or MasterCard, are currently the fastest growing card-based financial product. Since that report was produced the numbers have kept rising.

The appeal of prepaid cards to criminals is that they are not considered monetary units (cash, share certificates, travellers cheques, money orders, etc.) and, therefore, not subject to anti-money-laundering reporting legislation. Often no identification, and therefore no paper trail, is required when buying the cards.

Currently it is legal for individuals to enter Canada or the US with countless cards in their possession no matter how much money is stored in each card's magnetic stripe. Needless to say, drug traffickers and those involved in financing terrorist activities have found this loophole appealing.

Testifying before a US Congressional hearing last March, FBI chief Robert Mueller said: "Recent money laundering investigations have revealed a trend on the part of criminals to use stored-value devices such as prepaid gift cards and reloadable debit cards in order to move criminal proceeds. This has created a shadow banking system." The Federal Financial Institutions Examination Council Bank Secrecy Act/Anti-Money Laundering InfoBase, a US federal banking agency, had also made this point in 2007, noting that "drug dealers have been known to load currency onto prepaid cards and send the cards to their drug suppliers [as payment] outside the country."

Prepaid cards, especially gift cards, can also be fenced for up to 80% of their value, according to FINTRAC. Popular sites such as eBay, Craigslist and various card-exchange sites have made "e-fencing" an incredibly easy way to launder dirty money for about a 20% cost, much less than what traditional, human fences would charge. FINTRAC cites one ring of thieves who were caught in Florida in 2007 after buying US\$24,000 worth of gift cards from one Wal-Mart and US\$18,000 from another Wal-Mart.

FINTRAC also reports that British experts allege that prepaid cards have been used to move terrorist funds around the world and finance terrorist attacks.

The popularity of prepaid cards among both retailers and consumers is easy to understand. Retailers who sell the credit cards — in reality the cards don't provide credit; they store an amount of money the purchaser has already paid to the seller but give the appearance of being a credit card, especially those that are affiliated with Visa and MasterCard — obtain a fee, either per card or on an annual basis. There is no risk of the card users failing to pay. The prepaid debit cards also engender fees to the user with no risk to the provider. Many of the cards can be applied for online.

For consumers who are overburdened with debt, unable to obtain a traditional credit card or want to ensure they don't amass credit debts they can't manage, the cards provide the appearance of having credit or can be used to self-regulate their spending habits.

The prepaid credit and debit cards are known as open-loop cards, meaning they can be used virtually anywhere and for any type of purchase. Closed-loop cards are those issued by one business (or, say, a specific shopping mall) and can only be used in locations sanctioned by the issuer. Typically, these are prepaid phone cards or gift cards. Retailers find the latter extremely attractive because recipients of the cards often use them to pay for items that are more expensive than the value on the card. Most open- and closed-loop cards are reloadable, another enticing characteristic to retailers.

The 2008 FINTRAC report notes examples of closed-loop cards. "Hudson's Bay in Canada offers prepaid gift cards that are reloadable in any amount. The Wal-Mart Canada website also says they offer reloadable prepaid cards for use in their stores. Casinos in Quebec offer electronic Texas Hold'em cards. Money is added to the card at the cashier's cage and winnings are automatically added to the card. To cash out,

individuals have to go to the cashier's cage. Closed-loop casino cards also exist in South Africa, the United States and Europe."

In some instances, banks fund prepaid cards without the consumer being aware of their involvement. "One example is the MiCash/The Home Depot Card, which is being marketed to Latinos in Tampa, Fla., and Washington, DC, as a reloadable debit card that can also be used as an ATM card, or as a phone card, and can be sent to a relative in another country," wrote Steve Cocheo, executive editor of the ABA Banking Journal. "The cards are issued in pairs, and include PIN and password. This jointly branded card is actually issued for the two companies by MetaBank, a US\$494.6-million assets savings bank headquartered in Storm Lake, Iowa. Meta Financial Group, Inc., the parent company, issues prepaid cards in more than 500 programs as a business line under its Meta Payment Systems operation."

Although law enforcement organizations are well aware criminals are using prepaid cards, legislation has yet to be developed to deal with the problem effectively. In a March 2010 Reuters article it was pointed out that US senators Joseph Lieberman and Susan Collins had "authored an amendment to close the stored-value card loophole" in 2009. Lieberman was the chairman of the Senate Committee on Homeland Security and Governmental Affairs and Collins was one of its members.

The amendment "became part of an act on credit-card accountability and disclosure President Barack Obama signed into law on May 22 last year," Reuters reported. "[It] stipulated that the Treasury Department work out regulations on the sale, issuance, redemption and international transportation of stored value cards within 270 days. The deadline lapsed on February 16 [2010]. It's not clear whether the delay is due to bureaucratic inertia, overwork in a Treasury Department busy with a deep financial crisis, or, as money laundering expert Charles Intriago put it, 'a manifestation of the unhealthy power of big money, financial institutions and their lobbyists.'"

It seems inevitable, however, that some degree of legislative change will occur, and likely soon. Possamai looks to the US Financial Crimes Enforcement Network (FinCEN), also part of the Treasury Department, to lead the way. In July 2010, FinCEN released a proposed rule that would revise the Bank Secrecy Act requirements currently applicable to money-services businesses with regard to stored value products and services. Intended to address regulatory gaps that have resulted from the proliferation of prepaid innovations over the past 10 years and their increasing use as an accepted payment method, the proposed rules would, among numerous specific measures, place "registration requirements on providers of prepaid access and suspicious activity reporting, customer information record keeping, and new transactional record keeping requirements on both providers and sellers of prepaid access." At the same time, FinCEN's new rules would exempt certain categories of prepaid access products and services posing lower risks of money laundering and terrorist financing from certain requirements. Another proposal would be to revise the Bank Secrecy Act to call stored-value cards "prepaid access" cards. At the time of writing the proposed changes, which had been sent out for comment, had not been implemented.

Currently no such legislation is being considered in Canada, according to a FINTRAC spokesperson. If the US goes ahead with new rules, Canada will likely follow suit at some point, says Possamai. "Over time, this will likely have a ripple effect and lead to other countries having similar regulatory regimes — in the way that crossborder currency controls were first introduced in the US and then spread to other jurisdictions, including Canada. However, this won't necessarily eliminate the money-laundering potential of SVCs, just as tighter controls over crossborder movements of cash have not eliminated its use in the illicit economy. As long as SVCs have qualities that make them attractive to criminals, they will find innovative new ways to use them to further their illicit schemes."

Although the current state of affairs regarding prepaid cards favours criminals who want to misuse them, there are limits imposed on their usage, both by countries and individual issuers. The Australian Institute for Criminology notes, for example, "the Travelex Cash Passport card in Australia has a maximum card balance value [at any one time] of A\$10,000; a maximum amount that can be loaded onto the card during any 12-month period of A\$45,000; a 24-hour ATM withdrawal limit of A\$6,000; and up to two cards able to be issued per Cash Passport fund." Western Union in Canada limits the daily loadable amount to \$950 per card. The Bank of Montreal prepaid Travel MasterCard allows a maximum of \$10,000 on the card at any time.

For someone such as Ronnie, any anti-money-laundering legislation regarding prepaid cards changes will likely not affect him or her. He or she can keep buying

them, in even smaller amounts, without attracting suspicion. But for large-scale drug criminals or terrorist financiers, new rules could have an impact. They will look for new ways to circumvent them, and most probably will, but that's how the money-laundering war is fought, one initiative at a time. Money laundering will never be stopped. But slowing it down or making it harder to do is a victory of sorts and one that has to be seen as the right thing to do by all involved, including law enforcement and through compliance to new rules, retailers.

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