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Money Laundering and Bulk Cash Smuggling: Challenges for the U.S.-Mexico Border  
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### **The Scope of the Problem**

Bulk cash smuggling across the U.S.-Mexico border cannot be viewed in isolation. Rather, the process of illegally moving large quantities of dollars across the border must be viewed as part of the movements in a larger pipeline that flows across the northern tier of South America, through Central America and Mexico and into the United States. The pipeline, fed by many smaller feeder lines, moves products both north and south, and the a significant portion of the violence in Mexico today, as well as among the *maras* in Central America, revolves around disputes over control of portions of that pipeline, its *plazas* and branches. The primary goods flowing northward are cocaine, human traffic, gang members hired by the drug cartels as enforcers, and marijuana. The primary products moving south are large amounts of cash generated from the illicit activities, stolen cars and other goods, and weapons. It is important to understand that all of these products move through the same basic architecture and rely on many of the same facilitators to enable the flow of goods and services.

Historically, Mexico has been the single greatest source of U.S. currency repatriated by a foreign country to the United States. Moreover, documented inflows from Mexico have customarily exceeded outbound reporting linked to legitimate sources such as worker remittances and cross-border commerce, revealing a substantial unexplained gap. The gap, estimated to be between \$11 billion and \$22 billion, can be attributed, in large part, to bulk cash smuggling associated with transnational criminal activity such as drug trafficking and alien smuggling. The March 2007 seizure of \$207 million in cash from drug trafficking proceeds from a Mexico City residence is a dramatic example of the scope of the problem.<sup>1</sup>

Like much else in the drug trade, the current situation with bulk cash shipments is the product of adaptation and evolution by the drug cartels to law enforcement efforts. This means that any analysis of the movement is constantly subject to change. Using the pipeline analogy, products can be rerouted around whatever law enforcement obstacle is

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<sup>1</sup> An example of the differences in estimates, Mexican Attorney General Eduardo Medina Mora, appearing before the Mexican Congress in October 2007, stated that Mexican banks receive about \$1 billion from their U.S. counterparts annually, but return up to \$16 billion, of which about \$10 billion “does not have an explanation ... and could be attributed to the flow of drug trafficking money.” According to Samuel Gonzalez of the Mexican Autonomous Institute of Technology (*Instituto Tecnológico Autónomo de México*—ITAM) drug proceeds laundered in Mexico account for as much as four percent of the country’s GDP, or roughly \$35.7 billion annually. See: “Marching as to War,” *Economist.com*, January 31, 2008. [http://www.economist.com/world/la/displaystory.cfm?story\\_id=10608676](http://www.economist.com/world/la/displaystory.cfm?story_id=10608676)

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raised and a blockage or bottleneck occurs. Globalization and the "dollarization" of the Mexican economy have opened a variety of new fronts for the movement of profits from drug cartels and other transnational criminal organizations.

However, the money derived from the sale of drugs and other illicit activities, and the need to move and place that cash, are vital to the criminal organizations that generate the revenue. This offers significant vulnerabilities that can be exploited by law enforcement and intelligence operations on both sides of the border. The impact of cash seizures is high because it deprives the criminal organizations of both profits (the reason for existing) and operating fund (the source of power and impunity).

### **The Growing Dominance of the Mexican Drug Trafficking Organizations**

The growing dominance of Mexican criminal groups in the U.S. drug trafficking and alien smuggling markets in recent years has generated significantly more cash that has to be moved and integrated into the financial structures. This is due in large part to the decline of the Colombian structures, given the demise of the Medellín, Cali, and Northern Valley cartels and the increased pressure by the Colombian government on the *Fuerzas Armadas Revolucionarias de Colombia* (FARC). As a result of there being no dominant Colombian organization for the first time in three decades, the Mexican cartels have seen their power and wealth grow dramatically in the past two years.

The need to move larger amounts of money has developed at the same time as stronger U.S. anti-money laundering regimes, particularly after the 9/11 attacks, have made other methods (smurfing, layering through banks, and other uses of the formal financial sector) more difficult and risky, and has contributed to a heavy reliance on bulk cash smuggling. At the same time, the cartels need to rely far less on their own money service businesses such as *casas de cambio* and *centros cambiarios* to convert dollars to pesos. There are several reasons for this, including:

- Drug trafficking organizations in Mexico prefer to hold onto their cash in U.S. dollars, as U.S. dollars are considered more stable than the Mexican peso;
- Most bribes and operating expenses paid by Mexican drug trafficking organizations, which are large and continual, are paid in U.S. currency;
- Cocaine sources of supply in South America prefer to be paid in U.S. dollars from Mexican buyers;
- Many businesses in Mexico accept U.S. dollars, thus providing an easy means for drug trafficking organizations to place their illicit proceeds into the formal economy. Among the favorite places to place the dollars are in real estate, luxury vehicles, construction and other cash-intensive businesses. Hoarding cash is also common.

Further adding to the attractiveness of the dollar is that much of the region is officially dollarized, so the dollar can now flow without the need to exchange to local currencies.

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El Salvador, Panama, and Ecuador all officially use the U.S. dollar as their currencies, and other countries in Latin America use the U.S. dollar as an acceptable parallel currency. Of particular concern are Panama (especially the Colón Free Trade Zone) and El Salvador, which have some of the most rapidly growing banking systems in Latin America, while having little visible legitimate means to support such growth.

The revenue generated from drug trafficking and criminal activity is dispersed throughout Mexican society, including the business community, politicians, law enforcement and military personnel, the media, and scores of other individuals. Recent political changes in Mexico have also led to a significant change in corruption patterns and how the criminal organizations distribute their cash. Under the one-party rule of the PRI, corruption was largely top down, that is to say that senior officials could be bribed and distributed the money down the chain of command. With the advent of multi-party rule, most states and towns have several parties that must be paid off at the local level, forcing the criminal organizations to pay less to each party but more overall to ensure continued freedom of operations. This has led to the need to buy into the electoral process earlier, as the winner is no longer guaranteed, spreading the corruption further throughout the body politic.<sup>2</sup>

It is important to note that most of the bulk cash smuggled into Mexico does not stay there. At least a half (some estimates range to 80 percent) of the cash is used immediately to purchase more product and is therefore re-smuggled or sent on to Colombia, often via Panama, Ecuador and El Salvador, because the economies of all three use the U.S. dollar for their currency, making dollar transactions easier than elsewhere.

The expenses of the cartels are also rising in the face of the sustained efforts by the Calderón administration to attack the drug trafficking organizations militarily. This could significantly impact the profits the cartels and their associated criminal organizations earn. The cartels are faced with escalating purchases of ammunition, sophisticated weapons, surveillance equipment, armored vehicles, and bulletproof vests, as well as the recruiting and training of security forces.

### **The Introduction of New Factors in the Laundering Process**

While it is likely that bulk cash shipments will remain important and perhaps of primary method for the drug trafficking organizations to move money from the

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<sup>2</sup> In August 2008, *El Universal* reported that Mexican Defense Secretary Guillermo Galvan stated that 500,000 individuals in Mexico are tied to the illegal drug trade. According to Galvan, this includes 300,000 growers, 160,000 small-time drug dealers or transporters, and 40,000 individuals in leadership positions. These figures may be considerably understated, as private security forces, complicit public officials, and willing members of the business or financial community were not mentioned in Galvan's remarks. See Brendan Walsh, "Mexico Estimates 500,000 Tied to Drug Trade, *El Universal* Says," Bloomberg.com, August 9, 2008; <http://www.bloomberg.com/apps/news?pid=20601086&sid=a2CHFyiv3gn8>.

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United States to Mexico, it is likely that new patterns in money laundering and bulk cash movement will emerge and could already be underway.

One is the growing use of over invoicing or under invoicing of products that are bought in China and shipped to Mexico. There is credible anecdotal evidence that Mexican drug trafficking organizations are buying container loads of cheap plastic products in China, which are shipped to Mexico at a substantially inflated declared value. Many of these containers are never claimed in customs, but the person or company that ordered goods will most likely have successfully laundered the declared value of the products. This means the laundering organizations have moved their money from the point of origin, primarily the United States, to a bank outside of Mexico, and can now move it back through the banking system as clean money. This risk mitigation of this method may lessen the importance of bulk cash shipments.

A second important shift is the growing presence of Russian organized crime in Mexico. These organizations, buying up large amounts of properties on Mexico's west coast--particularly hotels and casinos because they are cash intensive businesses--offer new opportunities for Mexican organizations to launder and move their funds through the formal financial system. If money can be placed into the Russian laundering structures outside of Mexico, they can be delivered in Mexico again as clean cash. Alternatively, if Mexican organizations have large amounts of cash on hand in country, they can launder those funds through the Russians' structures and have those funds delivered either inside or outside the country as clean funds.

Another unintended side effect of the growing controls and regulations placed on the *casas de cambio* and *centros cambiarios* is that many of those companies are going out of business. These companies are being replaced by unregulated money remittance houses, including Western Union and other U.S. based companies.<sup>3</sup>

Other vulnerabilities include the lack of regulation in the registration of used car sales, as well as the purchase and sale of real estate, both favorite ways for drug trafficking organizations to launder and invest cash. A particular vulnerability is the notary public system, where land transactions are registered. They remain antiquated, not computerized, not searchable and unable to communicate with other registries, meaning that land records are virtually impossible to trace. This is important because proceeds from the drug trade are flowing directly into land purchases in Mexico. These purchases allow criminal organizations to establish territorial control, set up training camps and safe havens and expand their influence in significant parts of the country.

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<sup>3</sup>For an interesting look at the new concerns about Western Union, see: <http://www.supreme.state.az.us/opin/pdf2009/WesternUnionOpinion%20FINAL.pdf>; and Josh Meyer, "'Blood Wires' Over the Mexican Border," Los Angeles Times, June 8, 2009, accessed at: <http://www.latimes.com/news/nationworld/nation/la-na-western-union8-2009jun08.0.4162344.print.story>

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Stored value cards, which are essentially pre-paid debit cards, also allow money to flow freely across the border in relatively small quantities. As with Western Union activities, there is anecdotal evidence that the stored value cards are being used to "smurf" cash across the border, meaning that many people are using them to draw relatively small amounts of money so as to not draw attention to themselves, but in aggregate they are able to move significant amount of funds.

### **Facing the Threat**

The multiple and constantly evolving options available to drug trafficking and organized criminal organizations to move and hide their funds highlights the extreme difficulty in combating the flow of illicit funds. As with the movement of drugs, people or weapons, the specific routing and methodology of movement of the commodity can be changed, concentrated or diversified as needed.

On the U.S. side of the border, combating the versatile organizations with rapidly shifting methods are primarily state and law enforcement officials. While receiving some federal aid and training, the local law enforcement units are often operating on their own, with little communication or information sharing with other units. On a federal level, resources and talent in the Treasury Department, particularly FinCen and OFAC, have been taken from the tracking of drug money to trying to track terror finance. In the intelligence community the same trend has prevailed. Only the DEA has managed to keep a sustained focus on drug trafficking organizations, and is now in ongoing turf battles with the Department of Homeland Security (DHS) and other parts of the government. While the trend has reversed slightly in recent months, money movements of organized criminal organizations, unless they are directly linked to terrorism (and more and more are), remain a far lower priority than prior to 9/11.

On the Mexican side, significant strides have been made in creating the legal framework that will allow the Mexican government to more aggressively pursue the illicit proceeds of the drug gangs, but much of the implementing legislation remains to be written, and the governmental and judicial infrastructure is lacking. While the sustained military pressure on the cartels has forced the groups to spend more money in order to continue operations, relatively little emphasis has been placed on cutting off the flow of cash to them.

For example, funding for Mexico's Financial Intelligence Unit (*Unidad de Inteligencia Financiera*—UIF) has been far from adequate. In 2006, the UIF received just 0.3 percent, or \$7.1 million, of the budget allotted to the Ministry of Finance and Public Credit (*Secretaria de Hacienda y Crédito Público*—SHCP), less than the ministry's public relations department. There are indications the situation may be changing. Under the Mérida Initiative the UIF is to receive \$5 million in IT assistance and FinCEN has begun a more intensive relationship with the UIF to modernize and improve its capabilities.

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Like drugs moving south to north, money moving north to south must cross the border if it is physically transported. Bulk cash is much easier to move when it takes up less space and weight. This means that there is a constant demand for \$100 bills, as a way of consolidating the small bills into less bulky larger bills. But even this presents the drug traffickers with significant challenges. For this reason, much of the same architecture for moving bulky drug shipments north is used in moving cash south.

Money is often smuggled in false compartments of trucks and other vehicles, many vehicles are used in order to minimize the loss of an individual busts, to consolidation centers. At the consolidation centers the money is vacuum packed in plastic bags in the highest bills available, usually \$100 bills. Then many smaller loads are sent out, and the same spotters who monitor the border to guide traffickers through border crossing also monitor it to guide the couriers returning. Moving money by human courier by aircraft is also a known method, as are moving cash hidden inside of merchandise on aircraft or ship. Again, often the same groups that move the product north will move the cash south.

### **The Road Ahead**

It is not realistic to think in terms of eliminating or completely blocking bulk cash shipments and other forms of money laundering. Rather, policy options must examine ways of raising the cost of doing business to the cartels and other criminal organizations and creative ways of targeting their most successful types of operations. This requires an understanding that if one method is successfully tackled the cartels will already have several new ones operational. Key to any success is the effective use of human intelligence and financial intelligence, meaning the ability to sift through significant amounts of data for the anomalies that indicate illicit gain. The danger of over-relying on data extraction at the expense of human intelligence is the sheer volume of data makes it impossible to make sign

Of primary importance (and one of the keys to the more successful targeting the FARC and other Colombian organizations) is the creation of vetted units on both sides of the border that can communicate with each other in real time. Only with the ability to compare and share information can the financial side begin to be addressed. The DEA (and recently in Iraq, SOCOM in the Pentagon) have worked, with some success, to track financial structures of criminal and terrorist groups. They have done this by maintaining a concerted focus on finances, including successfully exploiting "pocket litter," telecommunications, and exploiting human intelligence. These lessons need to be studied and applied to the Mexico-U.S. border situation.

On the U.S. side, it is imperative that local and state law enforcement forces be given the training and tools to follow the money. Because the movement of money is often a multi-jurisdictional challenge, coordination among these groups across state lines and with the federal government is imperative. Most border police forces do not

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have the resources to do more than try to keep from being overrun by the flow of drugs, guns and illegal immigrants. Tracing finances is often only done when cash is seized coincidentally as part of an operation. There is not the training or the personnel to do more on the financial front.

Coordination with the federal government is not a small task. The DEA, FBI, FinCEN, DOD, IC and DHS all have equities in tracking illicit finances, particularly if a designated terrorist entity is involved. This comes into play in the Mexico situation because the Mexican cartels deal directly and indirectly with two designated organizations, the FARC and the United Self Defense of Colombia (AUC). In addition, there is growing evidence (part of which was made public in recent Colombian and U.S. statements) that Hezbollah is using the FARC/Venezuelan connection to raise and move money. The territorial disputes, lack of clear jurisdictional guidelines, and inter-agency rivalries make intra-governmental and inter-governmental coordination a daunting task.

On the Mexican side, the endemic corruption, the deep roots already laid down by the drug trafficking organizations, lack of technical training in police and military units and the lack of vetted units all make combating the financial flows particularly difficult. In addition, as describe above, the illicit money seeps into virtually every part of the Mexican national and local state structures, making executing existing laws a daunting task and the effective implementation of the new constitutional reforms on confiscation of properties and other important aspects even more challenging.

The entire process is further hampered by the lack of coordination among the UIF, prosecutors and law enforcement investigators. While information on transactions or suspicious activities can be requested by the UIF, it cannot be required. Requests must still be hand delivered and there is no mechanism to allow the immediate sharing of information that could lead to action. As a result, there have been few (I could find none) cases of money laundering successfully brought against drug traffickers.

In order to significantly increase the cost to the drug cartels of moving bulk cash across the U.S. -Mexico border both nations will need to take several steps together. The opportunity to take these steps in coordination with Central American nations exists because of the joint participation in the Mérida Initiative. These are:

1. Make combating the illicit financial flows a central part of the counter-drug and fight against organized crime on both sides of the border;
2. Create vetted units where language is not an obstacle and where information can be shared freely. This would allow law enforcement to jointly exploit what each side knows about personnel, routes and methods and coordinate activities in real time;



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3. Substantially increase the financial and technical resources available to trace financial networks. This is particularly true in Mexico and at the state and local levels in the United States. This includes modernizing the way the UIF and other organizations in Mexico exchange information, access information and deal with law enforcement;
  4. Develop human intelligence within the drug trafficking organizations specifically targeted at the financial structure with the goal of both identifying routes, but also key facilitators and exploitable weaknesses along the financial pipeline and anticipating future vulnerabilities;
  5. Develop joint regulations on wire and other unrestricted money transfer systems, recognizing that such services are often an important financial lifeline to significant numbers of people, particularly in rural areas. Simply cutting the services or making them unviable would create significant hardship and generate sympathy for the drug traffickers;
  6. Monitor and trace the purchase of land, particularly near the border, in order to anticipate where the cartels are likely to be able to exert significant pressure.

All of these steps would increase the cost of doing business for the organized criminal organizations. The more money they have to spend to move money, they less they have for other activities. Money that is seized deprives the criminal organizations of the final payoff for their activities, and hurts them more than interdicting the drugs or other products. Targeting cash remains one of the most effective ways of significantly hurting criminal organizations, so creative and flexible approaches to doing so are imperative.