

China in Our Backyard: How Chinese Money Laundering Organizations Enrich the Cartels

House Committee on Oversight and Accountability
Subcommittee on Health Care and Financial Services
April 26, 2023



Written testimony of
Channing Mavrellis
Illicit Trade Director
Global Financial Integrity



GLOBAL FINANCIAL INTEGRITY

April 26, 2023

Chairwoman McClain, Ranking Member Porter, and distinguished members of the Subcommittee on Health Care and Financial Services, it is an honor and privilege to testify before you today about Chinese money laundering organizations.

In the last few years, reporting has increased on the involvement of Chinese money laundering organizations (CMLOs) with the laundering of narcotics proceeds in the Western Hemisphere.

However, this is not a new phenomenon. The Treasury's *2020 National Strategy for Combating Terrorist and Other Illicit Financing* noted the *increase* in complex money laundering schemes involving Chinese citizens residing in the U.S. who, acting as money brokers, laundered drug-related cash proceeds via trade-related schemes in order to repatriate money to Mexico.¹ Additionally, Drug Enforcement Administration (DEA) annual *National Drug Threat Assessments* (NDTAs) have reported the involvement of CMLOs offering their services to Mexican, Colombian, and Dominican transnational criminal organizations (TCOs) since at least 2016.²

More importantly, the drivers behind the involvement of CMLOs in the laundering of narcotics proceeds in the Western Hemisphere are solidly linked to other countries' domestic policies, not U.S. immigration or border policies.

Specifically, China's economic policy in regards to foreign exchange controls prevents money from freely moving into or out of the country unless it abides by strict rules. For individuals, the Chinese State Administration of Foreign Exchange regulations set in 2017 cap foreign exchange transactions at roughly US\$50,000 per year. Those Chinese citizens seeking to exchange or transfer in excess of that amount frequently turn to informal means, which I'll discuss shortly.

Additionally, Mexico adopted a stricter anti-money laundering/countering the financing of terrorism (AML/CFT) policy in 2010 by placing stringent restrictions on the deposit of U.S. dollars into Mexican bank accounts, for example limiting individual account holders to no more than US\$4,000 in cash per month.³ This policy was intended to combat narcotics-related bulk cash, which it did. However, it also caused cartels looking to move and launder narcotics proceeds to search for new strategies, such as the use of CMLOs.

At the same time, Colombia has taken steps to develop "one of Latin America's most rigorous AML regimes," according to a recent U.S. *International Narcotics Control Strategy Report*.⁴ While the Colombian

¹ U.S. Department of the Treasury, *National Strategy for Combating Terrorist and Other Illicit Financing, 2020* (Washington, D.C.: U.S. Department of the Treasury, 2020), 24, <https://home.treasury.gov/system/files/136/National-Strategy-to-Counter-Illicit-Financev2.pdf>.

² Drug Enforcement Administration, *National Drug Threat Assessment 2016* (Washington, D.C.: Drug Enforcement Administration, 2016), https://www.dea.gov/sites/default/files/2018-07/DIR-001-17_2016_NDTA_Summary.pdf.

³ Regulations additionally limit Mexican citizens that are non-account holders to deposits of no more than US\$1,500 monthly, and businesses can deposit up to US\$14,000 cash, however exceptions are allowed if businesses meet stringent criteria. "Mexico - Foreign Exchange Controls," PrivacyShield, accessed April 24, 2023, <https://www.privacyshield.gov/article?id=Mexico-Foreign-Exchange-Controls>.

⁴ U.S. Department of State, *International Narcotics Control Strategy Report, Volume II: Money Laundering, 2020* (Washington, D.C.: Bureau of International Narcotics and Law Enforcement Affairs, U.S. Department of State, 2020), 82, <https://www.state.gov/wp-content/uploads/2020/03/Tab-2-INCSR-Vol-2-508.pdf>.

AML system is far from perfect, more stringent requirements have made some cartels look towards outsiders for help in laundering or moving narcotics proceeds. This is notable, as Colombian MLOs and brokers had previously played an important role in laundering narcotics proceeds. However, Colombian cartels are now reportedly seeking out CMLOs due to their success.⁵

Prior to professional money laundering, money laundering was done by TCOs “in house.” The outsourcing of money laundering to professionals means that the arrangement of the TCO has continued to expand horizontally, away from the traditional, clearly defined top-down model. This horizontal arrangement is more nebulous, with more moving parts and adaptability, and it makes it harder for law enforcement to investigate, build, and prosecute cases.

CMLOs and TCOs operating in the U.S. have a symbiotic relationship. TCOs face the age-old problem of laundering and repatriating the proceeds of crime from one jurisdiction to another without being detected as well as moving from one currency to another. This is particularly difficult with large volumes of cash proceeds, which is common for drug trafficking organizations (DTOs). On the other hand, CMLOs are looking to access large volumes of U.S. currency via informal means. They each have what the other wants.

CMLOs aren’t the first or only professional MLOs. However, they have a different focus than the rest. While other professional MLOs profit from the purchase of criminal proceeds, CMLOs’ primary objective is to gain access to U.S. dollars (or another desired currency) outside of formal channels in order to evade China’s currency controls. Therefore, while other professional MLOs and money brokers may charge 10 to 15 percent commission, CMLO brokers can undercut the competition by charging up to six percent, or nothing at all.⁶ They make their profit by reselling the U.S. currency to U.S.-based Chinese nationals.

The methods used by CMLOs reflect the impact of these policies and involve both “commonplace” money laundering techniques such as bulk cash smuggling as well as culturally-specific systems and mechanisms. It is important to note that the use of these systems and mechanisms by CMLOs extends to other criminal activities—including tax evasion, human trafficking, and wildlife trafficking—and are used around the world.

Once a commission is agreed upon and the cash collected in the U.S., Chinese MLO brokers are able to provide DTOs with near-instant access to a corresponding amount of funds; for example, Mexican pesos in Mexico.

CMLOs have several options on how to handle the U.S. currency. They can use cash intensive businesses, structured deposits, casinos or other common ML techniques to place the funds into the formal financial system in accounts they control.

Frequently, though, they use money laundering mechanisms that are unique to the Chinese context. They can make the funds available to Chinese citizens via an informal value transfer system, specifically through flying money also known as *fei ch’ien*, or through a mirror exchange via the Chinese underground banking system (CUBS).

⁵ Robert Zachariasiewicz, “Chinese Money Laundering Organizations and Narcotics Trafficking” (Report Launch - Made in China: China’s Role in Transnational Crime & Illicit Financial Flows, Washington, D.C., October 27, 2022), <https://gfiintegrity.org/event/made-in-china-chinas-role-in-transnational-crime-illicit-financial-flows/>.

⁶ Zachariasiewicz.

According to a former DEA Senior Supervisory Agent, the CMLO will typically use WeChat, a Chinese instant messaging system similar to WhatsApp, to offer the currency on message boards.⁷ He detailed that when a potential buyer responds (which will be a Chinese immigrant), a CMLO associate and the buyer will meet in person to exchange the cash, and then the buyer transfers an agreed-upon amount of renminbi from their Chinese bank account to the CMLO's Chinese bank account.⁸

The mechanisms have been in place for centuries, but have been largely contained within the Chinese community. For example, *fei ch'ien*, which is believed to have been started during the T'ang Dynasty, has traditionally been used by the Chinese diaspora to remit wages back to the mainland.⁹ Now though, as reported in the 2020 DEA NDTA, Asian MLOs "provide access to longstanding laundering networks for U.S.-based Mexican TCO members."¹⁰

Another "tried and true" method that has been frequently used by both CMLOs and narcotics traffickers in the Western Hemisphere is the black-market peso exchange (BMPE), a type of trade-based money laundering (TBML) scheme that is particularly difficult to detect since the value of the commodities, rather than the money itself, is shifted.

BMPE schemes have often been conducted as a two-country transaction involving the destination and source countries, for example the U.S. and Colombia. With the involvement of CMLOs, the schemes have now become three-country transactions. After accepting narcotics proceeds in the U.S., Chinese money brokers can then make an equivalent amount available in China that can be used to purchase Chinese goods, which are exported to the TCO's country of choice and then sold, with the profits going to the TCO.

CMLOs operate on a very large scale, often moving significant amounts of currency. In 2021, a Chinese ML network operating in Chicago and New York that laundered tens of millions of dollars in drug proceeds for Mexican cartels was dismantled.¹¹ One of this network's couriers, a Chinese national who was a legal permanent U.S. resident, reported that her average cash pickup was US\$500,000.¹² In another example, between 2008 and 2019, Xizhi Li, a Chinese businessman with U.S. citizenship, laundered nearly US\$30 million of drug proceeds for Mexican, Colombian, and Guatemalan DTOs via a casino in Guatemala, a U.S. seafood export company, and U.S. and Chinese bank accounts.¹³

⁷ Zachariasiewicz.

⁸ Zachariasiewicz.

⁹ John A. Cassara, *China-Specified Unlawful Activities: CCP, Inc., Transnational Crime and Money Laundering* (Washington, D.C.: John Cassara, 2023), 110–11.

¹⁰ Drug Enforcement Administration, *National Drug Threat Assessment 2020* (Washington, D.C.: Drug Enforcement Administration, 2021), 76, https://www.dea.gov/sites/default/files/2021-02/DIR-008-21%202020%20National%20Drug%20Threat%20Assessment_WEB.pdf.

¹¹ Frank Main and Jon Seidel, "Chinese Money-Laundering Rings in Chicago, New York Cleaning Mexican Drug Cartel Cash," *Chicago Sun-Times*, April 30, 2021, <https://chicago.suntimes.com/2021/4/30/22408448/chinese-money-laundering-mexican-drug-cartel-mirror-swap-trade-based-money-laundering-xianbing-gan>.

¹² Frank Main, "Chinese Immigrant in Money-Laundering Ring: Didn't Know \$24 Million I Picked up Was from Cartels," *Chicago Sun-Times*, June 11, 2021, <https://chicago.suntimes.com/2021/6/11/22529643/chinese-money-laundering-mexican-drug-cartels-sui-yuet-kong>.

¹³ Katie Jones, "Chinese Broker Laundered Latin American Drug Money Around the World," *InSight Crime* (blog), August 10, 2021, <https://insightcrime.org/news/chinese-money-laundering-networks-expand-profit-latin-america/>; Sebastian Rotella and Kirsten Berg, "How a Chinese American Gangster Transformed Money Laundering for Drug Cartels," *ProPublica*, October 11, 2022, <https://www.propublica.org/article/china-cartels-xizhi-li-money-laundering>.

As long as CMLOs can provide low commission rates, near real-time mirror exchanges, and handle large volumes of cash, they will remain a preferred money laundering service for DTOs.

Two of our principal vulnerabilities to Chinese ML organizations are that many of the mechanisms used, such as *fei ch'ien*, are neither well understood nor easy to detect. Much of global AML/CFT policy is focused towards the financial system, however many of the methodologies used by CMLOs involve trade-based schemes, underground banking, and informal value transfer systems which exist outside the formal financial system.

Money laundering expert John Zdanowicz succinctly sums up this issue. He stated: "The front door of money laundering is the banking system. The [U.S.] government has done a pretty good job of closing the front door, but the back door -- international trade -- is wide open."¹⁴ While this quote is nearly 15 years old, it still remains true.

Looking to the future, the drivers behind CMLOs' success are unlikely to abate. Nate Sibley of the Hudson Institute points out that the demand for U.S. dollars "stems from rising dissatisfaction with CCP policies such as Zero-COVID, the tech and business crackdowns, and strict capital controls that have made many elites desperate to escape Xi Jinping's increasingly autocratic rule."¹⁵ With the government's authoritarian nature a constant, and President Xi publicly vowing to "adjust excessive incomes" of China's super-rich, the demand for U.S. dollars will be sustained, if not grow.¹⁶

The U.S., as well as the international community, need to take the threat presented by CMLOs very seriously. China plays an outsized role in transnational crime and money laundering mirroring its growth as an international superpower. The country's rapid economic development has been a catalyst for advancements across a variety of industries as well as lifting 800 million people out of poverty over the last few decades. At the same time, however, the country has expanded its influence in a broad array of transnational crime areas including trafficking, narcotics and IP theft, as well as illicit financial flows.

My recommendations include the following:

- **Study the role of Chinese professional money laundering networks.** Conduct a study on the role of Chinese professional money laundering networks in laundering the proceeds of transnational crime and corruption.
- **Target the individuals, entities, and countries facilitating financial crimes and money laundering.** Apply economic and other targeted financial sanctions with respect to individuals and entities engaged in financial crimes and money laundering, particularly trade-based money laundering. In addition, explore policies to hold accountable countries that fail to sufficiently investigate financial crimes and money laundering and/or provide adequate responses to requests for financial investigations information.

¹⁴ "Trade-Based Money Laundering Flourishing," UPI, May 11, 2009, https://www.upi.com/Top_News/2009/05/11/Trade-based-money-laundering-flourishing/17331242061466/.

¹⁵ Nate Sibley, "Defunding the Deadly Fentanyl Trade," Hudson Institute, April 12, 2023, <https://www.hudson.org/drug-policy/defunding-deadly-fentanyl-trade>.

¹⁶ Phillip Inman, "Chinese President Vows to 'Adjust Excessive Incomes' of Super Rich," *The Guardian*, August 18, 2021, <https://www.theguardian.com/world/2021/aug/18/chinese-president-xi-jinping-vows-to-adjust-excessive-incomes-of-super-rich>.

- **Strengthen the U.S. response to other narcotics-related money laundering methods.** The involvement of CMLOs is certainly a serious threat, however, they are not the only or even the primary way that narcotics proceeds are laundered. Strategies to combat narcotics-related money laundering should combat CMLOs but should also consider other channels such as trade-based money laundering, real estate money laundering, the use of shell and front companies, and illicit gold, among others.
- **Continue to make combatting corruption a high priority in the U.S. national security strategy.** Corruption is a major facilitator of transnational crime and illicit financial flows, undermining national, economic, and environmental security in the U.S. and abroad. The U.S. Government must continue to curb corruption and its deleterious effects by modernizing, coordinating, and resourcing efforts to fight corruption; curbing illicit financing; and holding corrupt actors accountable, among others.
- **Address inefficiencies in mutual co-operation and data-sharing through the MLAT process.** Money laundering is very much a cross-border issue. To address the problems in the mutual legal assistance treaty (MLAT) process, it is recommended that the U.S. Government embed staff on a rotational/second basis within different government financial intelligence units to improve mutual cooperation and data exchange. Additionally, where appropriate, they should allow staff from other country governments to embed themselves with the Department of Justice Office of International Affairs to better understand the process and requirements of U.S. law needed to exchange information.
- **Improve the efficacy and efficiency of Trade Transparency Units (TTUs).** TTUs were established to exchange trade data between the U.S. and its trade partners (on a bilateral basis) as well as improve the understanding of trade-based money laundering (TBML). However, as noted in GFI's *Financial Crime in Latin America and the Caribbean*, one major weakness in the TTU model is that "data is not shared continuously, rather it is done on weekly, monthly, quarterly, biannual, or annual basis... [which] prevents potential real-time identification of TBML and fraud threats."¹⁷ The U.S. should explore more dynamic information sharing with its trade partners in order to move from a more reactive to proactive position. In addition, as noted by the U.S. Government Accountability Office, the Secretary of Homeland Security needs to both develop a programmatic strategy for the TTUs as well as a performance monitoring framework.¹⁸
- **Provide FinCEN resources to ensure that it can take on new and emerging challenges from financial crime risks:** To ensure that FinCEN is well equipped to provide assistance to foreign FIUs and address financial crime risks, it is recommended that additional funding and staffing should be authorized for FinCEN.

¹⁷ Julia Yansura et al., *Financial Crime in Latin America and the Caribbean: Understanding Country Challenges and Designing Effective Technical Responses* (Washington, D.C.: Global Financial Integrity, 2021), 169–70, <https://gfiintegrity.org/report/financial-crime-in-latin-america-and-the-caribbean/>.

¹⁸ U.S. Government Accountability Office, *Trade-Based Money Laundering: U.S. Government Has Worked with Partners to Combat the Threat, but Could Strengthen Its Efforts* (Washington, D.C.: U.S. Government Accountability Office, 2020), 44–45, <https://www.gao.gov/assets/gao-20-333.pdf>.