

About the need of  
Forensic and  
Anti-Money Laundering  
services for art market  
professionals



Over the past months, the international press has featured numerous articles about suspected cases of money laundering. From the 'Gurlitt case' in Germany, to the suspected large money laundering schemes involving a famous New York art gallery or a Long Island art dealer, the media have reported a great variety and an acceleration of money laundering schemes and techniques.

Understanding the global art market and its needs against financial crime has become a hot topic of discussion. "Money laundering in the art world should be considered a big problem," says Judge Fausto Martin De Sanctis, a Brazilian judge from Sao Paulo's Tribunal Regional Federal, who released a book on this topic in June 2013.

### **Forensic and anti-money laundering procedures are increasingly becoming an essential component of art market business activities.**

The French National Union of Antique dealers held the "TRACFIN<sup>1</sup> and antique dealing - the legal risks of operating on the antique market: laundering operations and similar situations" conference in February 2012. During this conference, the discussion shifted to the art world, showing a real concern that the art market could be a significant target for financial crime.

Artworks are often highly valued, appreciating assets, which can be readily transported, and are traded in an exchange defined by discretion, where protecting their clients' privacy is paramount. For these reasons, both fraudulent and money laundering activity can threaten the art world.

For instance, a recent case at a major auction house in Paris over the sale of a painting without establishing identity of the vendor, has exposed the firm to money-laundering risk, resulting in a temporary suspension of its auction activities. This scandal has brought to light the pertinent need to perform regular due diligence on your client, as a

necessary safeguarding measure against financial crime.

### **What has money laundering to do with Art?**

The art market can be appealing for money laundering due to a number of distinctive features:

- The confidentiality of the buyer and seller
- Industry categorisation by private transactions
- Discretion is one of the golden rules of the art market - making the obligation to report any suspicions a heavy one for art market professionals
- The common use of intermediaries/proxies for transactions (e.g. telephone or online auctions)
- The common use of foreign/offshore accounts
- International market and networks
- High value goods with semi-independent valuation
- The cash incentive for some markets
- Authenticity, as major risk not currently addressed
- Unregulated by financial authorities
- Limited controls on transactions (e.g. client confidentiality)
- Purchasing an artefact, antiquity or piece of artwork legitimises cash and converts it into an asset that gains value and can be sold at a later date
- Fraudulent activity is pervasive in the art world, due to the high value and limited supply of works by any given artist

Money Laundering could both cause and impact at least two of the current trends observed in the art market: high volumes of transactions and an activity boom in Asia and the MINT<sup>2</sup> economies.

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<sup>1</sup> TRACFIN (*Traitement du Renseignement et Action contre les Circuits Financiers clandestins*) is an French governmental entity part of the Finance and Economy Ministry in charge of the fight against money laundering. Tracfin is the French Financial Intelligence Unit ("FIU").

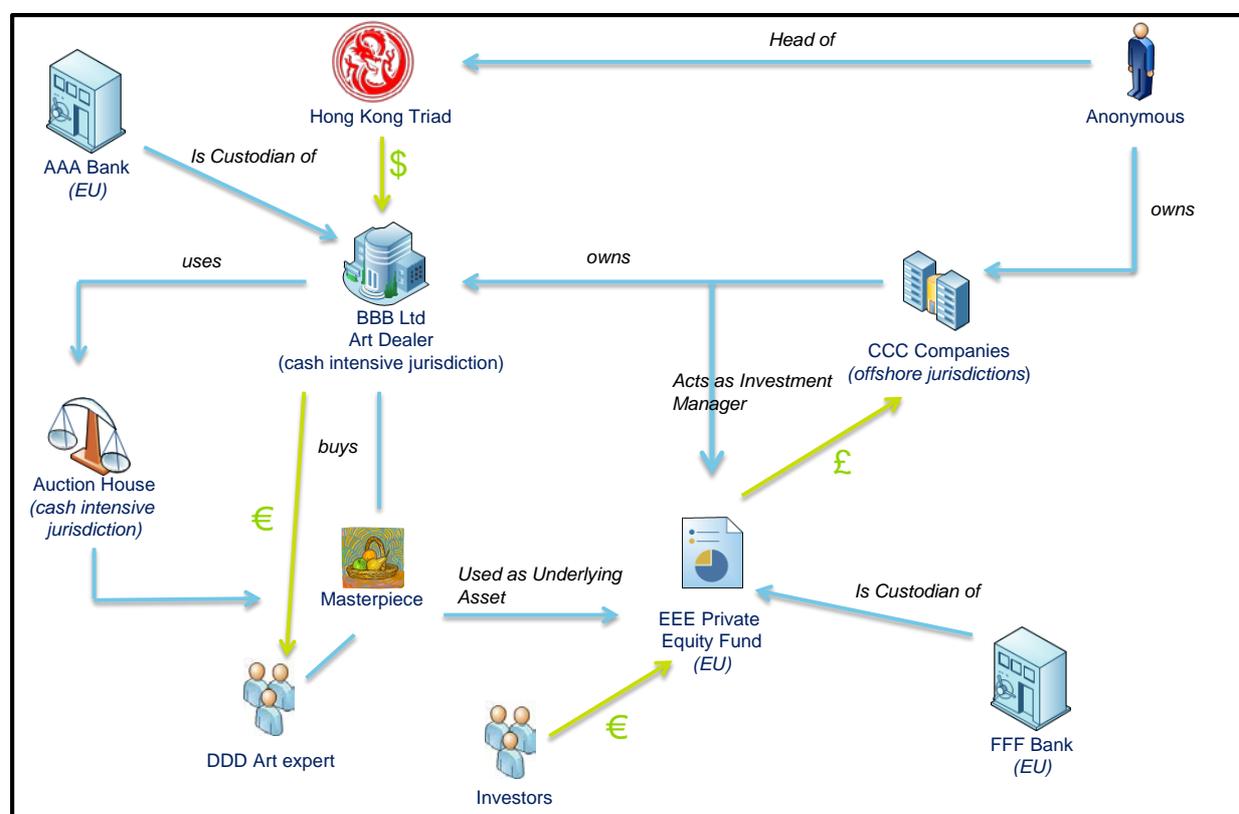
<sup>2</sup> MINT commonly refers to a group of 4 countries (Mexico, Indonesia, Nigeria, Turkey) considered as new booming economies due to very favourable economic and demographic prospects expected for the next 20 years. The MINT countries have superseded the BRIC nations as the latest group of emerging economies.

Money launderers may push the prices up as they do not have the same economic rationale for transactions. The main objective of a money launderer is to convert illicit funds into 'clean' assets. The acquisition price is not an issue but an advantage, as the criminal can funnel a larger amount of funds to be cleaned.

Indeed, money launderers favour high value pieces because they allow greater volumes of money from their illicit activities to be injected. For the sake of efficiency, a few master pieces are easier to acquire and sell than thousands of medium or low price items.

Booming economies might not yet be fully aware of money laundering risks or equipped to identify money laundering schemes. The financial markets in booming economies face so many simultaneous challenges that the legal and regulatory framework can still be weak on this topic, or its implementation is only beginning. The art market can be the victim of criminal organisations that abuse such situations to blend the proceeds of their illegal activities with the surrounding abundance of wealth and euphoric market conditions. In addition, some economies are still very cash-based, even for large amounts. Finally there is a high demand for art from a new wealthy class that is not always aware or concerned about the origin of the artwork it wants to purchase, or the funds with which it was acquired.

### An illustration of money laundering case using art market professionals



Source: Deloitte Tax & Consulting © 2014

In this illustration, a criminal organisation advises an alternative investment fund to acquire a master piece for its art portfolio, and is funding the purchase of the said piece via an art dealer located in a location where cash settlement of auction sale is legal and common. The financial professionals have a legal responsibility to identify and verify the identity of their clients, and to obtain the source of funds at the opening of the relationship. They are also required to

perform on-going name screening and transaction monitoring.

Art professionals should be inspired by these obligations to perform due diligence and verification on their clients, service providers, and related parties to avoid being used in a money laundering scheme and thus exposed to reputational risk and legal/financial sanctions.

## Why art market professionals need Forensic & Anti-Money Laundering services?

Art market professionals have a legal obligation, depending on the legal jurisdiction, as retailers of high value goods to undertake protective measures against money laundering and terrorist financing.

EEC and US resident art market professionals have a professional responsibility as retailers of high value goods to undertake preventive measures against money laundering and terrorist financing, according to the recommendations of the FATF<sup>3</sup> and similar bodies,.

At the European level, the draft of the 4th European directive (EC) 2013/025 shows a similar trend to broaden the scope of regulated entities and require tougher controls. The main new features include reducing thresholds for traders in high value goods from €15,000 to €7,500 for cash transactions.

The British Art Market Federation (BAMF) members have agreed to make themselves aware of relevant anti-money laundering laws and regulations to demonstrate goodwill in the context of increasing regulatory pressure.

The Brussels developments<sup>4</sup> from June 2012 proposed changes to money laundering legislation. This means more galleries will need to register as 'high-value dealers' (i.e. a dealer who accepts payments in cash for €15,000 or above for a single transaction) and comply with stricter guidelines when accepting cash from buyers.

When supported by clear and transparent procedures, art market professionals can systematically and discretely monitor activities related to accounts and lower the risk of financial crime. For this reason, forensic expert services (i.e. Know Your Customer (KYC), forensic and business intelligence services) are ideally positioned to initiate discussion and propose solutions for the art market.

## The increasing need for transparency in art market forces Anti-Money Laundering and

## Know Your Customer preventative measures to be undertaken

The industry background and current trends point towards a prudent approach by art professionals in preparation for future regulation changes.

The scope of art professionals concerned with this issue is broadening; including auction houses, foundations/trusts, financial service providers, Port-Franc (freeports), galleries, art dealers, legal advisors, insurance companies, funds (private equity), art fair organisers, and also online ventures such as online auction houses, art fairs, and galleries.

The client base of the global art market has proved to be the greatest area of UHNWI<sup>5</sup> growth<sup>6</sup> in the world's emerging economies - MINTs. These new customers are not well known yet, and professionals might not have sufficient background information and history to appreciate fully the range of money laundering risks.

All this shows the growing need for customer due diligence measures to be undertaken by art professionals.

## The typical range of forensic and consulting services pertaining to the art world that prudent players should consider include:

### Anti-Money Laundering services

- Anti-money laundering training (basic to advanced level)
- Customer due diligence assistance
- Name screening on persons: checking client/prospects database against blacklists and sanction lists.
- Business Intelligence Services for background searches on buyers and sellers (with a focus on the individuals, not the artwork).
- Selection and implementation of anti-money laundering systems
- Anti-money laundering compliance reviews
- Remediation projects in order to update 'Know Your Customer' documentation

<sup>3</sup> The Financial Action Task Force (FATF) is an inter-governmental body established in 1989 by the Ministers of its Member jurisdictions. The objectives of the FATF are to set standards and promote effective implementation of legal, regulatory and operational measures for combating money laundering, terrorist financing and other related threats to the integrity of the international financial system. The FATF is a 'policy-making body' which works to generate the necessary political will to bring about national legislative and regulatory reforms in these areas.

<sup>4</sup> "Submission to the consultation on the review of the Anti-Money Laundering Directive" dated 13 June 2012

<sup>5</sup> The definition Ultra High Net Worth Individuals varies, but usually refers to individuals with assets between \$5 million and \$50 million and/or investable finance in excess of \$1 million.

<sup>6</sup> Sources: <http://www.wealthinsight.com/pressrelease/the-2014-millionaire-explosio-4161554> and <http://www.livemint.com/Companies/0prRXgELhxYfgl5Lz8kBX/BNP-Paribas-says-to-focus-on-6-Asia-wealth-markets.html>

- Compliance guidance for private equity art funds
- Forensic due diligence of intermediaries such as fund distributors
- Forensic due diligence of client portfolios
- Investigations of unusual/suspicious transactions

#### **Business Intelligence Services**

- Standard or advanced background searches on physical or legal persons
- Use of multiple keywords (e.g. fraud, scandal, theft, embezzlement, etc.) in several languages (English, French, Spanish, German, Farsi, Russian, etc.) to refine the searches targeting negative news on physical or legal persons
- Search of transaction history and ongoing monitoring for business relationships

#### **Fraud forensic services**

- Awareness of common schemes, training, procedures, and controls design/review
- Business Intelligence Services for background searches on third parties (e.g. service providers, business partners, etc.)

- Fraud prevention and detection procedures
- Forensic technology (computer investigations)
- Fraud investigation
- Asset tracing and recovery

#### **Why should art professionals consider this seriously?**

As early movers, the benefits for art professionals will be to establish a diagnosis of their exposure to risk, a mapping of these anti-money laundering and fraud risks and the ability to prepare procedures and controls to mitigate them. Legislators are also applying punitive sanctions to natural persons. Imprudent art professionals could be pushed out of business by such sanction. Anticipating the trend for stricter and broader regulation on the fight against financial crime worldwide, art market professionals (both legal and natural persons) will benefit from early reflection and preparation beforehand.

The initial movers can also consider using this as a PR and marketing strength, showing their quality and their assistance in managing the reputational risk of their partners and clients.

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