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**Five insights into the art
market and money laundering**
Focus on five

Connoisseurs and collectors may not view rare artwork as commodities. But frequently that's how cultural objects are perceived in the marketplace, where legitimate investors and businesses see both aesthetic and financial value in paintings, antiquities, and other art forms. Illegitimate investors and businesses see additional value in these objects: the means to mask, move, and leverage ill-gotten proceeds.

Money launderers aim to integrate illegally obtained proceeds into the financial system without getting caught. These funds can then be used for personal enrichment, to mask crimes, or to advance terrorist causes.

Launderers traditionally "washed" illegal proceeds through the banking system. But as the global financial system improves detection and mitigation of money laundering, criminals are increasingly turning to trade-based money laundering—that is, trading commodities in deals that may look unremarkable on the surface, but actually, are undertaken to disguise and leverage illicit money. Like other commodities, artwork can be used to launder the proceeds of narcotics trafficking, embezzlement, insider trading, illegal gambling, and other crimes.

It's hard to quantify the size of the problem, but an estimated \$4 billion to \$6 billion in art is stolen annually, which de facto must move undetected, and which likely represents only a fraction of efforts to exploit artwork to launder money.

Institutions, collectors, and governmental authorities are working to stem the use of art for money laundering. These five insights aim to inform their efforts:

Insight #1:

The art market is especially vulnerable to trade-based money laundering

The art market is appealing to criminals for several reasons. First, the art market is huge and growing, fueled by the increasing ranks of ultra-high-net-worth individuals (UHNWIs), technological advances, and globalization. Art and collectible wealth held by UHNWIs alone is predicted to grow from an estimated US\$1.62 trillion in 2016 to US\$2.7 trillion in 2026.

While scholarship, connoisseurship, and forensic testing can reduce risks related to the authenticity and provenance of pieces, the art trade appears to lag in the identification and management of financial crime risks across counterparties and transactional operations. Parties to transactions can sidestep the banking system through activities such as bartering and payment in cash. The pricing of art is more subjective than valuation of many other commodities. The process of passing a stolen piece through layers of people, institutions, and places can scrub away origins and ownership until it's safe to integrate the work into the flow of legitimate commerce and extract its value as clean money.

Furthermore, unlike in the European Union, the US art industry is not subject to anti-money laundering (AML) regulations in the manner of financial institutions—a factor that cannot escape the attention of money launderers who are adept at exploiting legal and regulatory regimes. Yet, absent a statutory requirement for know-your-buyer and know-your-seller safeguards, money laundering is still a crime. Thus, large auction houses and dealers have been and are currently adopting more robust safeguards to prevent laundering, for good reasons. They could face prosecution if the US Department of Justice, a state or local prosecutor, or another country's prosecutors believe they are either complicit in or willfully blind to wrongdoing.

Together these factors highlight the inadequacy of the longstanding “handshake” approach to the art business that prizes confidentiality regarding participants, pieces, and prices.

Insight #2:

Terrorists exploit commodities, including those traded on the art market, to raise hard currency

Statues, antiquities, and other cultural objects are desired by collectors in major art business hubs around the world. ISIS (The Islamic State of Iraq and Syria) has used the sale of plundered artifacts, also described as “blood antiquities,” to finance its activities for years in a manner similar to al Qaeda and the Taliban before it.

In early 2018, police in Barcelona arrested two men for allegedly smuggling art pieces looted from sites in Libya by ISIS-affiliate groups. According to a police statement, the suspects, two Spanish art dealers, were part of a Catalonia-based group selling artworks from territories controlled by ISIS-affiliated groups. Authorities recovered stolen works including sculptures, mosaics and sarcophagi. Charges against the men included financing terrorism and trading in stolen goods.

The question is no longer whether terrorists are selling cultural property, but rather how can the international community slow or halt the flow and keep illegal objects off the market? The stakes are

high: reducing violent terrorist operations and protecting the cultural heritage of the community of the world. Since 1970, the UNESCO Convention on the Means of Prohibiting and Preventing the Illicit Import, Export, and Transfer of Ownership of Cultural Property has helped guide participating countries in addressing the problem.

The legal jeopardy and reputational challenges that the art trade faces today are akin to those that the diamond market has faced and tried to resolve. While consumers once focused predominantly on the quality of stones, many now reserve their business for vendors who participate in the Kimberley Process, a system designed to remove conflict “blood diamonds” from the global supply chain. Today, the Kimberly Process claims to actively prevent 99.8 percent of such trade worldwide.

As evidenced by the Spanish police operation described above, authorities also continue to focus on the trade in ‘blood antiquities.’

Insight #3:

New and pending legislation targets art-related financial crime

Art is increasingly treated as an alternative financial asset yet remains largely unregulated. Legislative initiatives in the United States and abroad could help address art-related financial crime.

In early 2018, the Council of the European Union adopted the Fifth Money Laundering Directive (MLD5). Among the directive's provisions is a requirement to report transactions above \$10,000 and the prohibition of cash transactions that exceed that amount. The latter provision could have outsized impact on art deals, which frequently exceed the \$10,000 threshold and often involve cash. MLD5 also broadens access to information on beneficial ownership, dissolves the anonymity of using electronic money products such as prepaid cards, and addresses risks linked to virtual currencies.

Shortly after MLD5 adoption, legislation was introduced in the US Congress to add art and antique dealers to the list of businesses subject to strict AML and other financial compliance rules. The proposed expansion of the Bank Secrecy

Act would require dealers and sellers of art and antiques to establish compliance programs and customer due diligence and monitoring systems. This goes well beyond screening potential clients against the US Treasury's Office of Foreign Assets Control (OFAC) sanctions lists—which prohibit US persons from trading with specific entities (unless granted a formal exemption by OFAC or via statute).

The Art Dealers Association of America (ADAA) opposes such legislation and the burden it could place on art galleries across the country. Yet while many are small businesses and might initially struggle with the compliance and reporting requirements of the bill, other small businesses subject to similar requirements have developed manageable risk-based processes in order to comply.

Insight #4

Most stakeholders prefer self-regulation to address art market money laundering risk

Industries generally prefer to use voluntary guidance to create standards. The US Department of Justice typically views compliance programs created to meet such standards as a mitigating factor in prosecutions and punishments.

The Jewelers Vigilance Committee is one example of this approach. The committee provides guidance to jewelry dealers in AML risk assessment and establishment of compliance programs.

The American Bar Association has stated its support for “reasonable and necessary domestic and international measures designed to combat

money laundering and terrorist financing,” and the association has published voluntary guidelines. At the same time, the ABA opposes “legislation and regulations that would impose burdensome and intrusive gatekeeper requirements on lawyers.”

One way the art world could seize the initiative in self-regulation would be establishment of a consortium to create unique identifiers for each piece of art. Such an initiative would have to address the high thresholds of anonymity and privacy protection demanded by art dealers and owners.

Insight #5:

New technologies, effectively deployed, can help identify and mitigate art market risk

Advanced analytics, blockchain, and other emerging technologies can help reimagine the traditionally opaque art market. Analytics can help illuminate disparate pieces and sources of information to identify patterns that might indicate either legitimate or questionable activity. For example, a new software tool and methodology from Deloitte, Art-360, is designed to help identify and triage to what extent a potential art transaction or holding exposes an entity to fraud, non-payment, legal jeopardy, and other risks. The tool identifies, correlates, and scores a catalog of more than 85 object, counterparty, and transactional potential risk indicators, which can be edited or augmented to fit each user's need. Combining Art-360 with contextual assessments made by subject matter specialists can enhance human decision making to understand how risky a potential transaction or holding may be.

Blockchain too presents a potential opportunity to help the art industry deal with opacity. By using cryptography to record and connect pieces of digital information—a series of numbers—tagged to a specific artwork, blockchain can help maintain privacy while resolving questions around an artwork's provenance, copyright, ownership and movement. However, blockchain may also be exploited in the art market if money launderers use cryptocurrency for payments.

Our take

The artworld is under growing scrutiny as a potential vehicle for financial crime, as evidenced by recent legal investigations, court cases, legislative initiatives, and media reports. Recognizing this, some of the most reputable art businesses in the world are developing and implementing risk-based anti-money laundering and anti-corruption programs. Leaders in the art industry increasingly understand the potential perils of turning a blind eye to illicit activities and are taking these actions that demonstrate good corporate citizenship and good faith to governments, as well as appealing to consumers.

Art auction houses, dealers, financiers, and insurers can follow suit by first performing a money-laundering risk assessment to uncover and understand exposures, some of which are unique to the art trade. Based on the risk assessment, they can implement financial and operational safeguards—internal controls—that mitigate exposure to financial crimes. These actions can also help businesses gain insights that might lead to cost reductions and operational improvements.

Finally, the growing threat of art-related financial crimes highlights the need for greater marketplace cooperation to combat money laundering. Working together won't dampen competition or erode bottom lines. Instead, it can help make the art business overall more resilient and profitable.

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End notes:

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