What is an Informal Value Transfer System (IVTS)? This paper aims to provide a better understanding of the alternatives to conventional banking often used by criminal organizations to avoid detection of illegal activity. More importantly, this paper will identify and discuss how IVTS often interacts with conventional banking systems.

An Informal Value Transfer System refers to any system, mechanism, or network of people that receive transactions or money for the purpose of moving funds to a third party in another geographic location. The transfer of funds, whether in the same form or not, generally takes place outside of the conventional banking system through non-bank financial institutions or other business entities.[1]

Historical Perspective

The origins of IVTS are rather benign. The purpose served people well before the development of modern banking institutions. Historically, IVTS transactions were consensual, legitimate trades without promissory notes. The transactions were based solely on an honor system. Even as recent as 2003, FinCEN advised, “Despite such vulnerabilities, it should be stressed that IVTS operations, which are in compliance with the BSA regulations, can and do provide legitimate services to many customers who customarily prefer to use these types of financial service providers”. [2] It is important to note that IVTS can be utilized as a legitimate informal banking system in underdeveloped countries that do not have a stable financial system in place. However, often IVTS is used in larger metropolitan areas to evade western taxes and exchange rate fees.

IVTS not only pre-dates western banking systems, they existed as far back as 5800 BC.[3] Originating in Asia, IVTS is based on classic Islamic law. It was used as a means to settle accounts and trade within local villages. As people began to migrate to the four corners of the world, the IVTS infrastructure expanded. Global networks developed and today, IVTS operations are found in most countries around the globe.
Type of IVTS

Hawala, the most commonly discussed IVTS, is based in the Persian Gulf area, primarily in Islamic societies. It is used to finance or trade against produce or goods. It is believed to have started as a means to finance long distance trades around the emerging capital trade centers in the early medieval period. Hawala is available internationally and often is the only means of financial transactions in remote areas such as the mountainous regions of Afghanistan. Hawala is money transfer without money movement.

Hundi is an indigenous banking system of India. Traditionally, Hundi is an order in writing made by a person directing another person to pay a sum of money to a person named in the order. Because Hundis are an IVTS, they do not have legal status and are not covered under the Negotiable Instruments Act, 1881.[4]

Fei Ch’ien means flying money. This form of money remittance evolved during the latter half of the T’ang Dynasty in China. As a result of the growing commodity trading, tea commerce and the creation of imperial capital, there also grew a need for a convenient means of exchanging goods.[5]

Conducting risk assessments related to IVTS can be complex because of the geographical spread. Countries associated with IVTS include, but are not limited to:

While most IVTS are deeply rooted within specific cultures, others, such as Black Market Peso Exchange (BMPE) emerged as a means for Colombian drug lords to circumvent currency controls introduced by the U.S. Government. As the illegal drug trade intensified, BMPE became a means to widen the profit margin for the various drug cartels.

Transmission of Money via IVTS

Traditional Hawala Operations:

1. Originator gives currency to the Hawaladar in Country A.
2. The Hawaladar in Country A provides the Originator with a payment code.
3. The Hawaladar in Country A notifies his counterpart in Country B by phone, fax or email of the transaction amount to pay the beneficiary, as well as the payment code.
4. The Originator contacts the beneficiary (in Country B) and provides the payment code to him/her.
5. The beneficiary goes to the Hawaladar in Country B, gives the payment code and picks up the specified money sent.

Modern Hawala Operations:

Modern Hawala operations utilize U.S. financial institutions to move money from one country to another. As stated in the aforementioned traditional Hawala operation, the initial process (steps 1-5) is still followed. However, the settlement of the money transmission is different.

Today, if someone located in the U.S. wants to conduct a Hawala transaction, the Hawaladar is often a business owner of a cash intensive business (e.g., convenience store, travel agency, restaurant, etc.). The IVTS funds are co-mingled with funds generated from regular business transaction activity. Subsequently, the funds are deposited into the business owner’s bank account in the U.S.

After the IVTS funds are deposited into the U.S. bank account, the Hawaladar has various means to transmit the money to the beneficiary bank located in Country B. The money can be transferred via wire transfers, inter-bank transfers, intra-bank transfers, money orders or cashier’s checks. It is becoming more common that ATMs are being used for these transactions as well.

What is the Harm of IVTS

Under U.S. regulations that govern money remittance services, IVTS are considered illegal. However, because enforcement of the regulation is difficult, “hawaladars” advertise their services openly using ambiguous language.

It is common for people to use IVTS simply to follow cultural traditions. The service of IVTS is faster, less expensive and less bureaucratic. However, IVTS represents one of the more significant threats to the financial industry because at some point it moves outside of the conventional banking system. Additionally, financial institutions cannot readily identify IVTS transactions. The money movement is anonymous and leaves no written record.

In the aftermath of the September 11 attacks, IVTS have become the subject of heightened attention. The use of these unregulated systems by terrorist organizations and drug cartels present a serious concern worldwide. For those individuals and groups looking to hide dirty money, IVTS has historically proven to be one of the safest methods to transfer funds without a trace.
According to the 9/11 Commission Report, Al Qaeda used a dozen trusted Hawala couriers to fund the September 11 attacks on the United States. Hawala transactions were conducted through bank accounts titled to charitable non-government organizations (e.g., CAIR and Wafa Humanitarian).[6]

It is worth noting, charitable giving, known as zakat, is one of the five pillars of the Islamic faith. It is believed that some individual donors to the charities referenced above were aware of the ultimate destination of their donations.

The terrorist organization, Lashkar-e-Taiba, attacked Mumbai, India in November 2008. The group coordinated 12 attacks over a three-day period, resulting in 166 deaths and more than 300 injured. Hawala transactions helped fund the attack by facilitating training, purchasing equipment such as satellite phones, GPS devices, SIM cards, arms and munition.[7]

Faisal Shahzad, an American citizen, was arrested in 2010 for attempting to detonate a car bomb in Time Square. Information related to his financial support indicates funds moved through Hawala transactions. The militant extremist group Tehrik-e-Taliban used a Pakistani Hawaladar to send funds to a Hawaladar in Long Island.[8]

**IVTS Red Flags**

As with many AML red flags and scenarios, the monitoring in place will be contingent on the financial institution. AML policies and procedures should already address key AML scenarios such as structuring and thresholds around cash transactions. In conjunction with the risk associated with the aforementioned geographic regions, banks should be monitoring for accounts that generate multiple transactions from a single individual or to multiples individuals. These transactions will often be even dollar amounts, and usually less than $1,000.00.

**Conclusion**

Informal Value Transfer Systems are found in all three stages of money laundering:

1. **Placement**: IVTS funds are deposited into a traditional financial institution.
2. **Layering**: IVTS set up shell companies (i.e. convenience store)
3. **Integration**: The shell company uses funds to purchase merchandise for the convenience store or transfers money to accounts at other financial institutions or hides funds via invoicing.

It is vital that financial institutions maintain sounds policies and procedures that encompass more than regulatory recordkeeping minimums. Policies and procedures should consider potential scenarios for all three stages of money laundering when evaluating IVTS. Additionally, due diligence is a critical component in mitigating risk associated with IVTS. Whether manual or automated, monitoring should be sufficient to detect unusual trends and patterns associated with IVTS.

Sources:
[3] Informal Value Transfer Systems & Criminal Organizations; a study into underground banking networks
[7] Lashkar-e-Taiba