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Illicit Financial Flows in the Mekong

Kristina Amerhauser¹

1. Global Initiative Against Transnational Organized Crime
All correspondence to: kristina.amerhauser@globalinitiative.net

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About the author

Kristina Amerhauser is a programme manager at the Global Initiative Against Transnational Organized Crime (GI-TOC), where she conducts research and analysis with the Asia-Pacific Observatory. From 2018 until May 2022, Kristina worked with the GI-TOC's Observatory of Illicit Economies in South-Eastern Europe and focused on topics such as illicit financial flows, money laundering and how to strengthen civil society resilience against organised crime and corruption in the Western Balkans. Kristina holds a Master's degree in advanced international studies from the Vienna School of International Studies, a BSc in international business from the Vienna University of Business and Economics, and a BA in development studies from the University of Vienna.

About SOC ACE

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Acronyms and abbreviations

AML	Anti-money laundering
ASEAN	Association of Southeast Asian Nations
BRI	Belt and Road Initiative
CDC	Centers for Disease Control and Prevention
FATF	Financial Action Task Force
GDP	Gross domestic product
GFI	Global Financial Integrity
GI-TOC	Global Initiative Against Transnational Organized Crime
IFFs	Illicit Financial Flows
IMF	International Monetary Fund
IP	Intellectual property
IWT	Illegal wildlife trade
MERs	Mutual Evaluation Reports
NOB	National Office of Buddhism
OFDI	Outward foreign direct investment
SEZs	Special Economic Zones
TBML	Trade-based money laundering
TJN	Tax Justice Network
UNODC	United Nations Office on Drugs and Crime

Summary

Illicit financial flows (IFFs) are a serious concern in the Mekong region, which includes Cambodia, Lao People's Democratic Republic (PDR), Myanmar, Thailand and Vietnam. Facilitated by state-embedded actors, each year vast amounts of illicit proceeds are generated, moved and laundered across the region and beyond in offshore tax havens. This distorts the local economies; deprives the state of income needed for health, education and infrastructure; and deepens inequality.

This paper is part of a comparative research project that tests and applies the 'IFFs pyramid', a new framework of analysis of IFFs proposed by Reitano (2022), in the context of the Mekong region. Based on a review of secondary literature, it provides an overview of financial flows, trade flows and informality – the three main means by which IFFs are enabled, moved and held according to the 'IFFs pyramid' – and discusses how IFFs manifest across the Mekong.

It finds that:

- There is widespread evidence that each flow is significant in the Mekong and that flows converge and intersect. Nevertheless, current responses to IFFs almost entirely focus on the formal financial system.
- Porous borders and strong trade relationships, including with neighbouring China, offer abundant and diverse opportunities for trade-based money laundering (TBML). Lack of capacity to identify misclassified goods and low cross-border collaboration are key impediments to its response.
- There are a large number of special economic zones (SEZs), some of which are treated as 'lawless zones' where national governments have no authority. This creates widespread opportunities for value to be extracted, under-reported and comingled with legitimate flows. They have also been linked to other illicit markets, such as drug trafficking, the illegal wildlife trade (IWT), human trafficking and financial crimes, and provide the space to generate and launder illicit proceeds in a multitude of ways.
- The big informal economy, coupled with the large number of people who remain outside the formal financial system, limits the efficiency of regulatory and oversight instruments.
- Political will to tackle IFFs in the Mekong appears to be limited, in large part due to the involvement of Chinese actors. In fact, some actors in charge of the response to IFFs seem to have created loopholes to their own benefit. State-embedded actors are part of the problem, both as a source of IFFs as well as by further enabling them.

This research shows that the IFFs pyramid proposed by Reitano (2022) is a helpful tool for organising information related to IFFs in the Mekong and for improving understanding of the major negative impact and harms that IFFs exert on societies and economies of the region.

1. Introduction

Organised crime and illicit markets have a major negative impact on the Mekong region. Cambodia, Lao PDR, Myanmar, Thailand and Vietnam – five of the six countries that make up the Mekong region, excluding China – face a unique set of circumstances, exacerbated by the impact of the COVID-19 pandemic, the 2021 coup in Myanmar and a progression towards more authoritarian policies. Both the 2021 and 2023 iterations of the Global Organized Crime Index, developed by the Global Initiative Against Transnational Organized Crime (GI-TOC), which measures the prevalence and impact of criminal markets and actors, score all countries in the region as having high levels of criminality.¹

The Mekong is host to a plethora of criminal markets and a large number of criminal actors, both of which have a significant impact on evolving patterns of security, governance, climate change and development. Indeed, in many places afflicted by organised crime, local law enforcement agencies appear to be compromised and political actors corrupt, embedded in criminal markets and their activities.

The region is characterised by porous borders and strong trade relationships, including with neighbouring China.² However, while goods and people are reported to be well connected across the Mekong, there is less cooperation and coordination among official authorities to stop illicit movement. This facilitates trade misinvoicing and other forms of TBML, particularly through the region's SEZs.

Economies in the Mekong remain largely cash-based and informality continues to be widespread, with between 61% and 86% of people estimated to be working in the informal sector. However, while Myanmar has been designated as a high-risk jurisdiction by the Financial Action Task Force (FATF) (Strangio, 2022b), and transactions to and from the country are subject to additional international scrutiny, other countries such as Thailand have a diverse and sprawling financial sector. This is exploited by illicit actors, who also work through both corporate and non-profit guises, taking advantage of both formal and informal financial markets to launder their illicit proceeds.

1.1. Research aim

This paper is part of a comparative research project aimed at testing the applicability of the 'IFFs pyramid', a new framework of analysis of IFFs proposed by Reitano (2022) in

¹ See GI-TOC, Global Organized Crime Index 2023 and 2021b, <https://ocindex.net/>. The accompanying report includes explanation of the Index methodology and descriptions of categories and other key terms used; see GI-TOC (2021) and GI-TOC (2023).

² China is part of the Mekong region but not a focus country in this assessment. Given China's impactful role as a source, transit and destination country for organised crime and IFFs as well as the influence of China on the other Mekong countries, the decision was taken to examine IFFs from the other Mekong countries to/from China but not within China and from China to/from the rest of the world.

different geographical regions around the world.³ By looking at financial flows, trade flows and informality in Cambodia, Lao PDR, Myanmar, Thailand and Vietnam, this paper seeks to apply the framework proposed by Reitano and investigates if the ‘IFFs pyramid’ can be used as a tool for framing evidence and analysis and improving the understanding of IFFs in the region. It first analyses each flow separately before it provides observations on where the three flows converge and intersect.

The overarching conclusion of this research is that IFFs in the Mekong can only be understood comprehensively if the roles played by financial flows, trade flows and informality – the three main means by which IFFs are held, enabled and moved according to the IFFs pyramid – are analysed jointly. They often exist side by side as well as overlap and interconnect, causing substantive harm to local economies and societies. In this sense, the ‘pyramid framework’ is a helpful tool for understanding IFFs in the Mekong.

1.2. Research methodology

This paper is based on a review of literature on organised crime, corruption and IFFs in the Mekong region between December 2022 and January 2023. Tailored to the data available and accessible in the region, three stages of review and analysis were undertaken to develop the observations in the research report.

Firstly, the profiles for all Mekong countries in the GI-TOC Organized Crime Index 2021 and 2023 were comprehensively reviewed. Given the main interest of this research paper is IFFs, a focus was put on size and impact of the diverse illicit markets as well as the actors who benefit from and further IFFs.

Secondly, more than 40 research reports by international organisations (such as the United Nations Office on Drugs and Crime (UNODC)) and civil society (such as Global Financial Integrity (GFI) and the GI-TOC) were analysed. In particular, the review sought to gather information on how money related to organised crime is generated, moved and laundered into the legitimate economy. In addition, a review of more general political economy reports allowed for a wider contextual analysis of the economy of crime in the Mekong, its drivers and enablers and connection to IFFs.

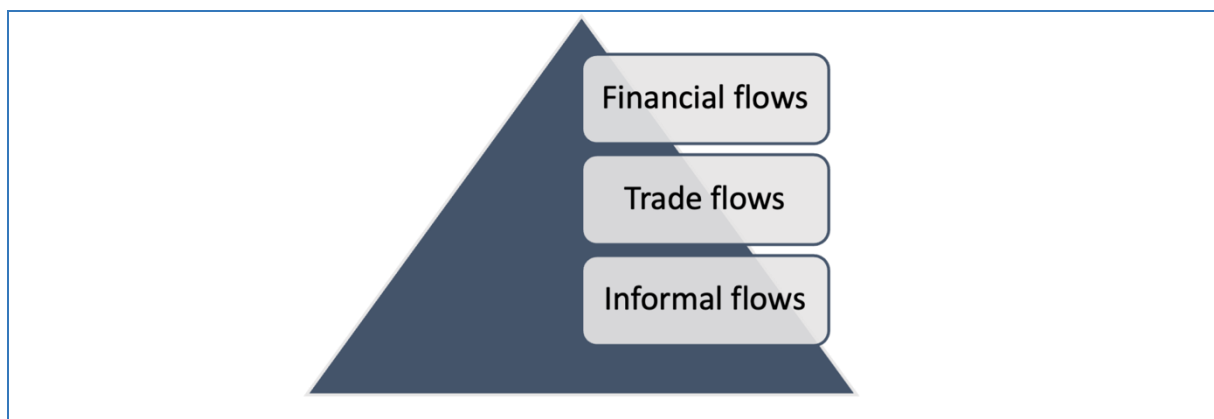
The third layer was to review available media reporting in English language, including national as well as international newspapers. This final stage allowed the author to capture recent developments and trends and provided significant evidence of the harms of organised crime and IFFs on the societies and economies of the Mekong.

³ Please see McLaggan, M. (2023). *Addressing Illicit Financial Flows in East and Southern Africa*. SOC ACE Research Paper No. 29 University of Birmingham, for an assessment of the ‘IFFs pyramid’ in East and southern Africa.

2. The illicit financial flows pyramid

In 'Political won't? Understanding the challenges of countering IFFs', Reitano (2022) proposed a new framework for analysis of IFFs. Intended to be used by researchers, analysts and policymakers, the so-called 'IFFs pyramid' (Figure 1) identifies three dominant means by which IFFs are enabled, moved and held: financial flows, trade flows and informality.

Figure 1: The IFF pyramid (according to Reitano (2022))



Financial flows, at the top of the pyramid, refer to a system of offshore jurisdictions with preferential tax regimes that has been created and allowed to grow with different countries competing to attract elites to shift their global wealth into these jurisdictions. Facilitated by a range of professional service providers, including bankers, lawyers and real estate agents, this system enables the bypassing of anti-money laundering regulations and undermines the rule of law.

Trade flows capture the over- and underpricing of the value of physical commodities across borders as a means to illicitly transfer money, evade taxes and customs duties as well as launder the proceeds of crime through the use of trade transactions. While the focus of trade flows is on the physical movement of goods, the purpose of misinvoicing is to register the financial value of the discrepancy in a new jurisdiction.

Informality, at the bottom of the pyramid, looks at transactions in the informal economy, such as earnings and transactions from remittances, cash, or other unregistered financial value services. By having no identifiable and traceable owner, these transactors go below the radar of the formal financial system.

Rather than describing the proportionality of each flow, the IFFs pyramid proposed by Reitano (2022) suggests that there is a wealthy cadre at the top that can access the mechanisms of global finance, while parts of society at the bottom of the pyramid are excluded from the formal financial system. In addition, Reitano argues that the pyramid is vertically integrated and shows that kleptocratic elites are able to extract money from

state budgets for private benefit while, at the same time, payments at the street level (such as bribes) can be linked to the highest level of the state. Similarly, systems of shadow banking, such as hawala, allow the offsetting of value against TBML systems, thereby reinforcing the movement of both goods and funds.

By looking at financial flows, trade flows and informality, the following sections test the applicability of the IFFs pyramid in the Mekong region.

2.1. Financial flows

Around the world, a system of offshore jurisdictions with preferential tax regimes has been created and allowed to grow, with different countries competing to attract the wealthy to shift their vast global wealth into these jurisdictions (Reitano, 2022). These jurisdictions also attract money from the rich and powerful in the Mekong, including money that stems from criminal markets and corruption.

2.1.1. Regional scandals involving financial flows

Corruption is reported to be widespread across the Mekong, extending from bribery to procurement fraud and grand corruption. All countries scored below the global average in Transparency International's Corruption Perceptions Index.⁴ Scandals regularly involve state-embedded actors as well as private sector actors. For example, in April 2022, the Lao PDR State Inspection Authority published a report estimating that the government had lost US\$767 million to corruption since 2016, particularly due to fraud involving government development and infrastructure projects (Radio Free Asia, 2022a).

In Cambodia, the military has reportedly been selling off the country's forests (GI-TOC, 2022b). According to a 2022 report by the GI-TOC, the country's political and military apparatus, in its current form, cannot survive without illicitly generated income and functions in a sophisticated system of political patronage. For example, it is reported that individuals at every level of the military apparatus first buy their position and then contribute funds to their superiors on a regular basis. In addition, to join the ranks of the business elite, citizens must purchase the honorific title of *oknha* for a donation of US\$500,000. This position comes with certain duties, including funding local public infrastructure projects. However, in return, the Cambodian People's Party also looks favourably at *oknhas'* business endeavours, and applications for licences and land purchases are easily granted by the government (GI-TOC, 2022b). Multiple investigations in Cambodia have uncovered cases of political elites and their families spending millions of dollars on properties in Australia and investments in Cyprus. Some of them are allegedly making multi-million-dollar citizenship investment payments by credit card, rather than bank transfer, to avoid scrutiny (Davies, 2021; Baldwin & Marshall, 2019; Adamovic Davies, 2022).

⁴ The Corruption Perceptions Index ranks 180 countries and territories around the world by their perceived levels of public sector corruption, scoring on a scale of 0 (highly corrupt) to 100 (very clean). The global average in 2022 was 43 out of 100; see <https://www.transparency.org/en/cpi/2022>.

In Thailand, the so-called ‘temple corruption scandal’ continues to erode public faith. It is reported that officials from the National Office of Buddhism (NOB) approached abbots in various provinces, promising to give them special budgets for temple projects on the condition that they must ‘return’ a certain amount of money called ‘the change’ from the approved budgets to the officials concerned. The fraud was first exposed in 2017, when an abbot petitioned the Thai Police Anti-Corruption Division and State Audit Office, as the NOB officials had demanded THB10 million (US\$300,000) of the budget, leaving the temple with THB1,000,000 (US\$30,000) for the construction of the temple’s ordination hall (Srisuwannaket, 2021).

Police corruption is a serious concern across the Mekong and reportedly facilitates a broad range of illicit activities. A prominent example is the case of ‘Joe Ferrari’, a policeman who was arrested in 2022 in Thailand after a video was leaked showing the brutal interrogation and subsequent death of an alleged drug trafficker. In the course of the investigation, authorities found that ‘Joe Ferrari’ lived in a luxury home in Bangkok, and estimated that he had amassed at least 42 cars. One of them was a rare Lamborghini priced in Thailand at THB47 million (US\$1.3 million) – worth more than a thousand times his monthly salary (BBC News, 2022). According to 2022 reports, Thai politicians and bureaucrats have also reportedly offered protection to transnational Chinese businesspersons involved in a range of illicit enterprises, including identity fraud and money laundering (Raymond, 2022).

The irregular awarding of state contracts is a common theme in places where state-embedded actors and weaker institutions exist. In 2022, the ‘Viet A scandal’ in Vietnam attracted significant attention. The Viet A health company is reported to have won a contract to sell COVID-19 test kits to hospitals at a 45% markup, after bribing officials. The defendants have been charged with violating regulations to win 16 bids to provide medical equipment to Dong Nai General Hospital at a profit of VND150 billion (US\$6.3 million) (Radio Free Asia, 2022b), allegedly paying a total of VND800 billion (US\$35 million) in kickbacks to secure contracts to supply test kits to local hospitals and Centers for Disease Control and Prevention (CDC). Along with Viet A principals, some government officials have also been prosecuted, including the head of Hai Duong CDC, who is reported to have accepted kickbacks of VND27 billion (US\$1.2 million) to approve the purchase of test kits worth VND151 billion (US\$6.6 million) from Viet A (Hiep, 2022). Experts have argued that it is not uncommon for suppliers to pay a markup of 30% or more for contracts in the healthcare sector (Nguyen, 2022; Hiep 2022).

However, the Viet A scandal is likely to be only the tip of the iceberg. Over 900 state officials and employees were investigated for alleged corruption and abuse of power in Vietnam in 2022. In addition, Vietnam’s president stepped down in early January 2023 after the ruling Communist Party found him responsible for violations and wrongdoing relating to numerous officials under him (Al Jazeera, 2023a; Al Jazeera, 2023b; Le, 2023).⁵ Fighting bribery and corruption was announced as a priority in Vietnam but motivations remain unclear, as its enforcement remains opaque and appears to be politically driven. Some have argued that the move is indicative of a power struggle at

⁵ It is likely that this move was connected to the departure of two deputy prime ministers also in January 2023.

the top of the party. As investigations increase, officials fear they could be caught if they inadvertently break rules, which are often badly written and difficult to interpret (Le, 2023).

2.1.2. Spoilers in the system

Singapore and Hong Kong special administrative region (SAR) have long been Asian offshore tax havens. They are ranked at the top of the Tax Justice Network's (TJN) Corporate Tax Haven Index⁶ (at ninth and seventh, respectively, in 2021) and TJN's Financial Secrecy Index⁷ (ranked third and fourth, respectively, in 2022). Tight bank secrecy laws and beneficial taxation rules have significantly contributed to the popularity of these key regional financial centres.

Criminal actors looking to move illicit money are often attracted by the same locations and circumstances that attract legitimate businesses (Kupatadze & Kumar, 2022). In Asia, it is therefore no surprise that Hong Kong SAR and Singapore are commonly linked with illicit proceeds from the Mekong. Two of the 14 offshore financial service providers named in the Pandora Papers are based in Singapore and Hong Kong SAR and have been used, for example, by family members of Myanmar's former agricultural minister who used shell companies to hold a property in Singapore and set up an investment firm (Alecci, 2021).

In Cambodia, the Minister of Justice was outed by the Panama Papers leak for having interests in offshore companies (Davies, 2016). In addition, the Pandora Papers revealed how NagaCorp, a Cambodian casino operator owned by Malaysian billionaire Chen Lip Keong, built its business partly through the CEO's use of offshore companies and a series of loans that lifted the casino company's value. While the use of these advantageous tax regimes is legal, and investigators could not find any evidence of wrongdoing in the NagaCorp case, these casinos often create permissive environments for illicit behaviour. NagaCorp is a Hong Kong-listed company and is the largest hotel, gaming and leisure operator in Cambodia. It also includes NagaWorld, the only integrated hotel-casino complex in Phnom Penh, Cambodia's capital. The Pandora Papers revealed advantages that offshore companies offered to Chen Lip Keong as he expanded his businesses across Cambodia (Alecci, 2021).⁸ NagaWorld has also been in the news for police violence after protests by workers who had been laid off during the COVID-19 pandemic (Keeton-Olsen, 2022).

Casinos in Cambodia and the Mekong region more broadly, including NagaWorld, are often connected to money laundering and various other types of organised crime (Dickison, 2019; UNODC, 2019; Farrelly, Dawkins & Deegan, 2022). The appeal of the Mekong physical and online casinos for criminal entrepreneurs derives both from the role of the casino itself as a money laundering vehicle – for example, through the

⁶ The Corporate Tax Haven Index is a ranking of jurisdictions most complicit in helping multinational corporations underpay corporate income tax. For more details and its 2021 results, see <https://cthi.taxjustice.net/en/>.

⁷ The Financial Secrecy Index is a ranking of jurisdictions most complicit in helping individuals to hide their finances from the rule of law. For more details and its 2022 results, see <https://fsi.taxjustice.net/>.

⁸ For the official website, visit NagaCorp LTD, NagaWorld, <https://www.nagaworld.com/nagacorp-ltd/>.

conversion of cash into chips, the use of foreign exchange services and security deposit boxes or the ability to utilise funds in another jurisdiction through foreign holding accounts. However, their appeal also comes from their locations within SEZs, where they can carry out illegal activities largely uninterrupted by law enforcement (Gore et al., 2022). Political permissiveness and corruption are reported to facilitate the operations of the casino industry, which is mostly targeted at Chinese gamblers. Numerous recent developments have raised concerns because of their potential to attract illicit activity, including three new megacities in Karen State, Myanmar, which are expected to attract investment as well as offer illegal gaming opportunities (Gore et al., 2022). Officials have previously estimated that around 90% of businesses in the Sihanoukville SEZ in Cambodia are Chinese-owned; including more than 80 casinos, only about half of which were legally registered (Goldberg, 2021). In addition, one of the leaders of the 14K triad, an organised crime syndicate, is reported to remain deeply involved in Cambodia's casino industry (Gore et al., 2022).

While the Mekong region featured in the Panama and Pandora papers, it appears that this only attracted limited attention from local authorities. In Thailand, more than 1,400 individuals were identified in the Panama papers but only 16 individuals were identified for follow-up by Thailand's Anti-Money Laundering Office (Kotani, 2016). Links were found to several current and former politicians and businesspeople, as well as several well-known companies and brands. For example, it was uncovered that the Yoovidhya family (Red Bull) had set up a network of offshore companies by Mossack Fonseca. They are reported to have used at least half-a-dozen offshore, anonymous companies in tax havens for more than two decades. While there are no indications that the Yoovidhya family's accounts violated any laws, the confidential deals could have been used to evade taxes or launder money (Mendoza, 2017). Similarly, family members connected to the Singha beer empire were identified as potential beneficiaries of a trust that owned luxury properties in the UK, although it remains unclear whether the transfer from the trust to the family was in fact finalised (Alecci, 2021).

According to the TJN, US\$21–32 trillion in financial assets is sitting in tax havens, and US\$483 billion in taxation is lost to these jurisdictions every year (TJN, 2021). In the Mekong, between 1.9% and 5% of tax revenue is lost every year to global tax abuse. In Cambodia, this represents more than 50% of the annual health budget.⁹ In 2015, in Thailand, as much as 25% of the country's total outward foreign direct investment (OFDI) stock is reported to have gone to three main tax haven destinations – the British Virgin Islands, the Cayman Islands and Mauritius. By comparison, 29% of Thai OFDI went to ASEAN neighbours, the country's main OFDI destination (Pananond, 2016). In addition, while it is widely recognised that Chinese firms set up offshore shell companies to seek foreign investment, the Belt and Road Initiative (BRI) as well as other campaigns have facilitated the investment of Chinese capital abroad using offshore companies (Asia Watch, 2021).

Sometimes it is not countries but provinces or cities that act as spoilers to the system. One of the most popular ones in the Mekong is the Golden Triangle – the border area between Thailand, Lao PDR and Myanmar – where the shadow economy is estimated to

⁹ See TJN country profiles at <https://taxjustice.net/country-profiles/>.

generate billions of US dollars annually (Lintner, 2022). While opium production is reported to have previously declined considerably in the area,¹⁰ criminal actors have instead turned to the production of methamphetamines and other synthetic drugs. The general lawlessness of the Myanmar sector of the Golden Triangle, in particular, has also made it a centre for other illegal activities, such as IWT, human trafficking and smuggling, and the illicit trade in rare earth minerals, arms and antiquities. At least 20 casinos have been built in northern Lao PDR and along Myanmar's borders with Thailand, many of which are based in SEZs (Lintner, 2022). For example, Bokeo in Lao PDR has been connected to TBML, IWT, drug trafficking and cyber slavery scams, among others.

2.2. Trade flows

Trade flows are financial losses resulting from the deliberate falsification of the value of goods on invoices submitted to customs officials when shipping or receiving physical commodities. Trade misinvoicing is done by either over- or underpricing the value of physical commodities as a means to illicitly transfer money across borders, evade taxes and customs duties or to launder the proceeds of crime through the use of trade transactions (Reitano, 2022). Trade in gems, timber, wildlife products and counterfeit goods – widespread across the Mekong – is a common vehicle for trade flows.

All Mekong countries are part of the BRI, and all countries with access to the sea have ports with considerable Chinese investment (Xie, 2021). Many BRI investments across the Mekong are transport infrastructure projects boosting connectivity between people and businesses. However, the increase in legal trade has also been linked to the proliferation of counterfeit goods and other illicit commodities, connecting criminal actors and making formerly isolated regions vulnerable to criminal exploitation (Kupatadze & Kumar, 2022). Some have also argued that the BRI creates rent-seeking opportunities among political elites and makes the environment more vulnerable to corrupt practices in customs and border agencies (Kupatadze & Kumar, 2022).

A significant portion of the Mekong's trade is facilitated through its 128 SEZs. SEZs are designed to stimulate trade, attract investment and create jobs by providing tax incentives, trade benefits, deregulation and other investment privileges. In addition, duty-free features along with reduced regulatory paperwork are intended to attract investors (Rowden, 2022). However, looking at the Mekong, it is becoming increasingly clear that SEZs also facilitate IFFs by offering the space to generate and launder illicit proceeds in a multitude of ways. In fact, it is the lax regulatory oversight within these zones that creates fertile ground for criminal activities such as smuggling, tax evasion and money laundering (Goldberg, 2021).

SEZs, particularly those linked to major infrastructure investments and the BRI, do not operate in isolation. Illicit trade and associated webs of corrupt and criminal networks can have serious ripple effects, leading to a bigger cross-border threat in terms of enabling criminal activity and other types of IFFs (Rowden, 2022). For example, it is

¹⁰ A 2023 UNODC report points to increased poppy cultivation in Myanmar (UNODC, 2023).

reported that in Sihanoukville, Cambodia, development was greatly undercut by increasing crime rates, rising rents, overwhelmed infrastructure and the suppression of local culture (Goldberg, 2021). Another example is the Golden Triangle SEZ in Lao PDR, where, despite its notoriety, expansion continues and a port is being developed. These developments are likely to further facilitate commerce of legal and illicit goods from China (Strangio, 2022a). Similarly, the Center for Advanced Defense Studies (C4ADS) uncovered allegations of corruption related to the permitting, construction and operation of regional economic development zones in all Mekong countries (Goldberg, 2021).

Key work on trade flows has previously been conducted by GFI by looking specifically at the value gaps of international trade data. Both their 2019 report (based on data until 2015) and 2021 report (based on data until 2018) highlight important value gaps for the countries of the Mekong (GFI, 2019). In addition, looking at the period from 2009 to 2018, China stands out as having by far the largest value gap for each year over the period under investigation; Thailand is also listed among the top countries (GFI, 2021).

For Myanmar, a discrepancy of US\$6.4 billion with China for 2018 data is indicative of possible under-invoicing of imports, of which US\$866 million relates to mobile phones and US\$216 million to motorcycles with small engines. This also supports claims previously made by Myanmar politicians that 80% of all motorbikes in Myanmar are illegally imported (Herbert, 2020). Herbert argues that lost revenue from the under-invoicing of Chinese imports in 2018 alone amounted to US\$306 million, an equivalent of 2.5% of total government revenue for the 2018-19 financial year (Herbert, 2020). However, this figure is likely to be an underestimation, given Myanmar's porous borders, challenging political situation and the fact it does not include the impact of smuggling, where goods are never registered with customs authorities. Myanmar also reported US\$713 million less tin ore exports to China than China reported receiving. Mines close to the border with China are alleged to be under the control of the Wa State Army, a key opposition group and on the US sanctions list for drug trafficking (Herbert, 2020).

2.2.1. Gems

Gems are considered a common vehicle for trade flows, and the practice is reported to overlap with general smuggling. In the Mekong, Thailand plays a particularly important role. Dubbed the 'ruby trading kingdom' or the 'ruby capital of the world', Thailand is a global hub for gem cutting and quality enhancement, and it is estimated that between 80% (Zheng, 2019) and 90% (Global Witness, 2015) of coloured gemstones worldwide pass through the country. More than 15,000 businesses are involved in the Thai gems and jewellery industry, employing 1.3 million people (Unninayar, 2016).

Recent research conducted by Vertriest and Saeseaaw (2019) highlights two key factors that facilitate the smuggling of gemstones through trade flows. First, the fact that once a stone is extracted, it is not possible to determine the mine of origin or sourcing date. Although the analysis of gemmological data usually provides a good indicator of the region of origin, it is not possible to establish whether an individual gem (a ruby, in this particular case study) was mined in a legal or illegal way. As such, illicitly mined stones can be easily mixed with legally sourced ones (Amerhauser & Cartwright, 2023).

Second, the value of each stone is subjective and highly sensitive to subtle changes in colour and quality. For example, rubies are reported to increase in value up to 25 million times between the mine and the sale (Amerhauser & Cartwright, 2023). Given that there is no ‘market value’ for rubies, but rather the value depends on the buyer’s willingness to pay for a specific stone, this offers significant potential for money laundering. Even at expert-run auctions, professionals have been willing to pay sums many hundred times higher than what their competitors were offering for the same stone, which makes gems a convenient vehicle for misinvoicing and evading taxes.

Some 70% to 90% of gems in the illicit market in Mozambique (which is worth between US\$80 million and US\$128 million annually), reportedly flow to Thailand. The stones are typically extracted in Montepuez, Mozambique, by unlicensed miners, who try to get access to concessions at night, often bribing police officers and security personnel to do so (Amerhauser & Cartwright, 2023). There is a substantial knowledge gap reported between the miner and the dealer, with most miners not being able to accurately estimate the value of a specific stone. As a result, most rubies that are extracted in Mozambique without a licence leave the country for a fraction of their value. Certificates of origin can be obtained in neighbouring countries (before export to Thailand) or in Thailand, facilitating the formalisation and laundering of stones into the local market. Rubies sourced in Mozambique are smuggled abroad by ship or plane, with the more valuable stones usually being transported by air (Amerhauser & Cartwright, 2023).

Neighbouring Myanmar is the world’s biggest source of jade, with the industry largely driven by demand from China. In 2014, Myanmar’s jade production was estimated to be around US\$31 billion (which is almost 50% of the country’s GDP), but China recorded only US\$12 billion of jade imports during the same period, thereby leaving a gap of US\$15.9 billion (Herbert, 2020). According to Global Witness, up to 90% of all jade mined in Hpakant in Kachin State, northern Myanmar, is smuggled to China without ever entering the formal system (Global Witness, 2021).

Jade prices in Myanmar are reported to have halved since before the 2021 coup and the COVID-19 pandemic, while prices in China have risen due to continued high demand and reduced supply (Bangkok Post, 2021a). Chinese investment in Myanmar jade mines is reported to be significant, with up to 70% of the financing for the major mining initiatives possibly coming from China (Herbert, 2020). In addition, several jade mines are reported to be under the control of Wei Hsueh Kang, a financier of the Wa State Army, who is allegedly using the gem to launder illicit proceeds from drug trafficking by bidding on his own jade at artificially inflated prices (Herbert, 2020). According to George Herbert (2020), Chinese online payment systems (such as Alipay and WeChat Pay) and e-commerce platforms (such as TaoBao) are used to transfer proceeds stemming from the illegal jade trade in Myanmar. In this context, it appears clear that little of the vast jade wealth benefits the local communities; instead, it contributes to financing both sides of the Myanmar conflict between ethnic groups and the military, as well as actors in China (Bangkok Post, 2021a).

2.2.2. Timber

Timber has also been identified as a common vehicle for trade flows and is widely used to funnel illicit proceeds in the Mekong. For example, according to a GI-TOC report, the

smuggling of timber from Myanmar to China was estimated to be worth between US\$112 and US\$133 million annually between 2015 and 2019 (Amerhauser & Cartwright, 2023). As well as the direct harm done by the illicit trade to the environment and local livelihoods, this also undermined the fiscal health of Myanmar with an estimated US\$30 million of unpaid taxes and tariffs as well as significant corrupt payments (Amerhauser & Cartwright, 2023). Anecdotal reporting since the 2021 coup suggest a continuation, if not a resurgence, in illicit logging and transportation.

Together with jade, teak is one of Myanmar's most valued export products. Despite the importance of timber for the local economy, the annual allowable cut was significantly reduced in 2015, and all exports of logs, except through the Port of Yangon, were banned. While officially all timber from Myanmar is to be auctioned by the state-owned Myanmar Timber Enterprise, it has been reported that illegal logging operations may even exceed their legal counterparts. Primarily facilitated by Chinese actors, timber is illegally logged by Chinese workers, operating out of Chinese companies set up to satisfy the demand in the Chinese domestic real estate market (Amerhauser & Cartwright, 2023).

Most of the profits are reported to be made by Chinese actors. The Environmental Investigations Agency (2015) reported that Myanmar export taxes are paid as trucks cross the Myanmar–China border, but these monies (US\$4,000 per truck in 2015; see also Amerhauser & Cartwright, 2023) are potentially partly corrupt payments, including to ethnic armed groups. On the Chinese side of the border, import taxes are reported to be paid in full, yet this money does not appear in the officially declared Chinese customs import taxes (Amerhauser & Cartwright, 2023).

Money related to the illegal timber trade is usually transferred in cash, with drivers also reportedly being paid directly in drugs. In addition, it is likely that the 'hundi system', an informal value transfer system comparable to hawala, is being used to pay loggers. Money made from illicit logging is laundered through construction, real estate and local businesses (Amerhauser & Cartwright, 2023).

Myanmar is not the only country in the Mekong from which timber is illegally transported to China. GI-TOC research has also documented the illegal timber trade in Cambodia, which has had one of the highest rates of deforestation (measured as a percentage of forest cover) of any country since the 1970s (GI-TOC, 2021a). There, logging is driven by large-scale conversion of forest for the production of commodities through government-sanctioned territorial concessions and illegal logging outside these land concessions, particularly of luxury timber and rare tree species. This illegal timber is often covertly transported back to sawmills within concessions and then sent for export. Illegally harvested luxury wood is either shipped under false customs declarations or sent across the border to Vietnam, which has been closed to timber exports since 2016 due to concerns surrounding the illegal timber trade (GI-TOC, 2021a).

2.2.3. Wildlife

The traditional medicine and food markets of East and Southeast Asia are key destinations for the global IWT. There is widespread reporting on multifaceted IWT

practices both online and offline, which supply the market with illicit goods from Africa and across the region. According to the UNODC's World WISE seizure data from 2015-19, most ivory tusk shipments were destined for Vietnam (42%), China (34%) and Cambodia (12%). Similarly, the primary destinations for rhino horn between 2002 and 2019 were Vietnam (41%), China (39%), Malaysia (5%) and Thailand (3%) (UNODC, 2020).

Massive poaching of abalone in South Africa is driven by demand from East Asia, where it is regarded as a delicacy (De Greef & Haysom, 2022). Evidence suggests that South African abalone (particularly in its dried form) is trafficked through the Democratic Republic of Congo, Lesotho, Namibia, Mozambique, Zambia and Zimbabwe in significant volumes to Hong Kong SAR, from where it is also re-exported to mainland China and Vietnam, among others (Amerhauser & Cartwright, 2023). In South Africa, between 1,000 and 2,000 people are reported to be involved in the business as divers, carriers and lookouts alone, before they sell the abalone to a network of buyers, dryers and exporters moving the product across borders (Amerhauser & Cartwright, 2023).

In addition, recent research by Nurbandi (2022) analysed the illegal trade in highly endangered parrots in Indonesia. They are reported to be routinely traded offline and online within Indonesia and the whole of Southeast Asia. Notably, online platforms have substantially removed barriers to entry into criminal markets and, as a consequence, the traders can easily expand their networks and reach a wider consumer audience.

These examples, similar to those involving timber and gems, underline the close interlinkages between smuggling and trade flows, as well as the role of China in driving demand. In fact, some of the IWT relates to smuggling proper, where animals are never registered by customs authorities and payments are made through WeChat or local forms of hawala systems. However, a substantial portion is reported to involve trade misinvoicing or scams in which wild animals are captured by poachers and either falsely registered or registered as having been bred in captivity (Herbert, 2020).

2.2.4. Counterfeits and illicit trade in excisable goods

The Mekong's proximity to China also makes the region a key destination market for counterfeit goods. Around 75% of global counterfeit goods are reported to come from China, with counterfeits estimated to make up approximately 12.5% of the country's total exports and over 1.5% of its GDP (Redfearn, 2022). Counterfeits are brought into the Mekong in large numbers and sold primarily on open markets. However, illicit sale on e-commerce sites, social media platforms and dark web markets has been also detected and reported, particularly since the beginning of the COVID-19 pandemic.

Counterfeit trade is facilitated by the large number of SEZs across the Mekong, as they facilitate the reprocessing of goods with unbranded packaging to be shipped and further rebranded and packaged for transit (Redfearn, 2022). A study conducted by the Organisation for Economic Cooperation and Development and the European Union Intellectual Property Office found that the existence, number and size of SEZs increase the value of counterfeit products exported by a given economy. The findings indicated that for every additional SEZ established, the percentage of counterfeited exports increases by an average of 5.9% (Rowden, 2022).

In Vietnam, the General Department of Market Surveillance uncovered about 4,500 intellectual property (IP) violations in 2020, resulting in monetary fines of a total of approximately US\$1.3 million. The value of counterfeit goods and goods without a certificate of origin, infringing IP rights, recorded in the first seven months of 2020 in Vietnam was approximately US\$1.74 million (European Commission, 2021). In Thailand, the number of seized items increased by 83.33% from January to May 2021 compared with the same period in 2020 (European Commission, 2021). This also includes part of the automotive industry, as a large number of counterfeit brake pads and airbags are reported to be produced in China and imported into Thailand (TRACIT, 2020). Many of these goods are imported at low prices, falsely declared at customs, or smuggled directly into the country.

The illicit trade in counterfeit medicines also plays a key role throughout the region. According to the UNODC, consumers across Southeast Asia spend between US\$520 million and US\$2.6 billion on falsified medicines each year. The report points out that some of these counterfeit medicines involve companies that cut corners by diluting products with substitute or cheaper chemicals, or altering expiration dates on packaging (European Commission, 2021). Counterfeit medicines are also widely produced across Southeast Asia, including in China, Malaysia, Myanmar and Cambodia (UNODC, 2019). Seizures included illicit anti-cancer medication in Myanmar in 2016 and 1.08 tonnes of erectile dysfunction pills in Vietnam in 2017. In January 2018, Thai authorities seized an illicit pharmaceutical factory producing falsified tramadol tablets, some of which appeared to have been trafficked to the United States and Europe (UNODC, 2019).

In addition, counterfeit cigarettes and alcohol are reported to commonly feature among flows for which trade misinvoicing is common. The Association of Southeast Asian Nations (ASEAN) was previously predicted to be the region with the highest consumption of unrecorded alcohol by 2025. According to the World Health Organization, 63% of annual per capita alcohol consumption in Vietnam was unrecorded in 2021; in Thailand, unrecorded alcohol consumption amounted to 20% of all consumption the same year (EU-ASEAN Business Council, 2022). This includes smuggled whiskey which is reported to cost half the price of legally sold bottles, resulting in a tax loss of US\$77.6 million annually (TRACIT, 2020). China is a leading supplier of counterfeit cigarettes, and around 62% of the illicit cigarette trade in Asia and the Pacific is reported to stem from China (Herbert, 2020). This results in an annual loss of US\$3.3 billion in ASEAN due to smuggled cigarettes, with the numbers being similarly high for Cambodia (US\$4.2 million), Lao PDR (US\$1.9 million), Thailand (US\$226.5 million) and Vietnam (US\$289.9 million) (TRACIT, 2020).

2.2.5. Drugs

Trade misinvoicing is also recorded in the context of the illicit narcotics trade, particularly in connection with payments for synthetic precursors manufactured in China that are under-invoiced or illegally smuggled to drug-producing developing countries in the Mekong region. For example, Myanmar is a key producer of synthetic drugs but does not actually produce any of the precursor chemicals; instead, these are transported into the country largely by organised criminal groups from China (Herbert, 2020).

2.3. Informal flows

All Mekong countries have sizeable informal sectors. For example, in 2018, the International Labour Organization estimated the share of informal employment as 77.5% in Cambodia, 86.7% in Lao PDR, 71.5% in Myanmar and 61% in Vietnam (ILO, 2018).¹¹ The volume of the informal economy and its continued growth have been described as major facilitators of IFFs, reducing the capacity of both national and international actors to respond (Reitano, 2022).

Financial inclusion is rising across the Mekong but it is estimated that more than 70% of the population in Southeast Asia do not have bank accounts and mainly rely on cash (Aravindan & Vu, 2018). However, an increased use of digital financial technologies and e-wallets (Frye, 2021) as well as mobile money is being reported. These technologies do not use traditional bank accounts but allow money to move directly from one party's account to another's in a secure manner, bypassing the regulation and enforcement of the formal financial system and making these transfers difficult to trace.

2.3.1. Sex industry

Despite being a billion-dollar industry, the sex trade remains an underground business in the Mekong, and sex work is illegal in all countries in the region (Global Network of Sex Work Projects, n. d.). It is estimated that around 250,000 people work in this cash-based industry in Thailand alone (Napatanapong & Saowakhon, 2022). They are not registered and do not have access to labour rights and social welfare benefits. Similarly, in Vietnam, there are more than 100,000 sex workers, particularly in bigger cities and tourist destinations (ILO, n. d.). The sex industry is also closely linked to other legal, cash-intensive businesses (such as bars, restaurants and the broader entertainment industry), but it is likely that a significant portion of payments in cash intensive businesses go unregistered. In addition, the sex industry is a source of illicit transactions, including payments related to corruption, the sexual exploitation of children and money laundering.

2.3.2. Remittances

Remittances are commonly used to send money to and within the Mekong and are a key source of funding for local populations as well as a vital source of income for the countries' economies. They become especially important when the formal financial system does not exist or cannot be accessed. According to the World Bank, which relies on International Monetary Fund (IMF) balance-of-payment data, Cambodia received approximately US\$1.15 billion in remittances in 2021, Lao PDR US\$232 million in 2020, Myanmar US\$2.25 billion in 2020, Thailand US\$9 billion in 2021, and Vietnam US\$17.2 billion in 2020.¹² However, these numbers are likely to be significant underestimations, as informal remittances remain strong. In 2015, the Ministry of Labour, Immigration and

¹¹ This study did not include any data on Thailand.

¹² World Bank Data, accessed 25 January 2023, https://data.worldbank.org/indicator/BX.TRF.PWKR.CD.DT?most_recent_value_desc=true.

Population in Myanmar estimated total remittances at around US\$8 billion (in contrast with the US\$3.5 billion estimated by the World Bank); additional estimates suggest that informal remittances in Vietnam could contribute a further US\$3 billion annually (Aneja, Gravesteijn & Hwang, 2017). These remittances remain unaccounted for and fall outside enforcement and regulation.

Various studies on remittances in Myanmar (2009-11) indicated that more than 90% of all remittances were sent informally, including through the hundi system (Akee & Kapur, 2017). Interestingly, the UN's Capital Development Fund reported that despite being informal, part of the remittance value chain is being formalised, as many informal agents have been using digital channels to remit money domestically (Aneja, Gravesteijn & Hwang, 2017). It is possible that formalisation of remittances in Myanmar had increased during the civilian-led government, but this trend is likely to have been reversed since the 2021 coup and the collapse of the country's banking system. The use of the hundi system is described to be culturally entrenched and, not least given the current situation in Myanmar, disrupting these remittance flows is likely to cause significant harm.

While the majority of people in Myanmar use informal channels for financial transactions, remittances in and to Cambodia, Lao PDR and Vietnam are reported to be more formalised, with most Cambodians having received money from formal remittance channels at least once (Aneja, Gravesteijn & Hwang, 2017). People in Cambodia were found to receive money mainly from non-bank institutions, including money transfer operators, post offices, microfinance institutions and formal digital finance channels (such as WING and e-money) (Aneja, Gravesteijn & Hwang, 2017).

In Vietnam, approximately 28% of remittances are transferred through remittance businesses, while 2% are by post (Tien, 2022). Mobile value remittances have also started to emerge, as users within the same provider network are able to transfer credit via phone. In addition, there are electronic kiosks where people can deposit money and input a mobile phone number to which the credit will be sent (Small, 2017). Digital remittance channels, such as mobile money, are reported to significantly lower the cost of transferring funds, but many of these transfers remain hidden from financial institutions. Despite being registered, they only allow limited checks on the provenance of transactions and are therefore vulnerable to abuse.

2.3.3. Migration

Remittances in the Mekong are closely linked to irregular migration and the smuggling of migrants. In particular the dynamism and relative prosperity of the Thai economy attracts thousands of migrants from across the region each year. In 2021 alone, more than 42,000 illegal migrants were arrested by Thai authorities for entering the country illegally (Bangkok Post, 2021b). The number of migrants in Thailand is reported to have increased in recent years, from 3.7 million to 4.9 million between 2014 and 2018, with 80% coming from Cambodia, Lao PDR, Myanmar and Vietnam (UNODC, 2019).

Despite high levels of demand for undocumented and cheap labour, especially in the tourism, agricultural and construction industries, Thailand's response to irregular migration has largely been to detain and return migrants to their countries of origin thereby pushing many underground and into the hands of smugglers (GI-TOC, 2022a).

UNODC has previously reported that around 80% of irregular migration is facilitated by smugglers (UNODC, 2019). Many migrants report high fees to brokers, recruitment agencies and others before and after they arrive in Thailand, and smuggling networks are often supported by complicit police, military and other local authorities (U.S. Department of State, 2022). Traffickers are reported to use debt-based coercion, deceptive recruitment practices, retention of identity documents, illegal wage deductions and violence to force irregular migrants to work and retain their jobs (U.S. Department of State, 2022). Irregular migrants are paid lower wages than the regular workforce, primarily in cash, and they often send money home via informal channels which are a substantial unregulated inflow into the country.

2.3.4. Cash

The majority of transactions in the informal economy take place using cash or through unregistered financial value services. In the Mekong, there have been significant incidents of bulk cash smuggling taking place between some countries, including Thailand, Cambodia, Lao PDR and Myanmar. In 2015, the US government launched 43 investigations tied to bulk cash smuggling in the Mekong, as a result of the seizures of over 140 currency or monetary instruments (UNODC, 2015). It is reported that money is moved by couriers in cash across borders, while informal remittance services, internet banking platforms and digital currencies are also being used (UNODC, 2019). All of the countries in the Mekong have porous borders, which further facilitates cash smuggling.

Cash also plays a key role in the laundering of illicit proceeds, through cash-intensive businesses or casinos. More than 350 casinos are recorded in the Mekong, many of which emerged after the crackdown on money laundering activities in Macau and China, raising concerns that a displacement of illicit activity took place (UNODC, 2019). Gambling is legal in all Mekong countries except Thailand. However, even in Thailand gambling is reported to take place on a large scale.

3. Assessing the pyramid and its applicability in the Mekong

The 'IFFs pyramid' proposes three dominant means by which IFFs are enabled, moved and held: financial flows, trade flows and informality. Most of the flows identified in the literature review fit into the framework of IFFs proposed by Reitano (2022).

This research has provided several examples of flows moving through the formal financial system; that is, flows of money stemming from corruption and organised crime that are leaving the Mekong countries and are moved abroad, including to offshore jurisdictions with preferential tax regimes. It has found many of them to be enabled by corruption and supported by state-embedded actors across the Mekong. Indeed, it appears that it is exactly those responsible for cracking down on IFFs who have able to legalise major points of vulnerability and are benefiting from the established system.

In addition, misinvoicing of timber, gems, wildlife, counterfeit goods and drugs – among others – was identified as a key concern in the Mekong. It was shown that across the region, an alarming number of SEZs enable illicit manufacturing and sourcing in under-regulated zones, which creates widespread opportunities for value to be extracted, under-reported and comingled with legitimate flows. The absence and purposeful manipulation of trade data in countries that are part of the BRI further increase the challenge of detecting TBML and illicit activity across supply chains (Herbert, 2020). Officials across the Mekong lack an understanding of the prices of goods and the capacity to identify poached IWT, logged timber or gemstones, enabling those who declare false prices and seek to launder money. In addition, it is likely that COVID-19 presented counterfeiters and smugglers with new opportunities to exploit inefficiencies in customs departments, especially as health goods needed to be moved quickly.

Finally, various examples were provided of how informal employment allows for labour payments to go unregistered, creating more opportunities for value discrepancy and for the transfer of value to occur without surveillance, as the economies in the Mekong remain largely cash-based. Large informal sectors, in which economic activity remains unregistered, facilitate that licit and illicit monies are comingled and become indistinguishable.

While financial flows, trade flows and informality are all significant and have major negative impacts on the Mekong region, it is also worth noting several examples in which the three flows overlap and intersect.

3.1. Special economic zones

Illicit activity connected to the high number of SEZs across the Mekong serves as a good case study of how illicit flows in the Mekong converge, as they offer opportunities to generate and launder illicit proceeds in a multitude of ways. Previous GI-TOC and UNODC reports, among others, have pointed to the roles that gambling centres in SEZs

in Lao PDR (such as Mong La and Boten) and Myanmar play as hubs for the trafficking of drugs, drug precursors and wildlife products. Moreover, casino complexes in Cambodia were found to be locations for flora and fauna crimes, cash smuggling and the laundering of illicit proceeds (UNODC, 2019; Gore et al., 2022). Government regulation and oversight of SEZs remains lax, enabling criminal networks to take advantage of weak inspection procedures, while large-scale real estate developments are facilitating capital flight and money laundering activities.

Since the beginning of the COVID-19 pandemic, SEZs and casinos located within them have attracted international attention for another reason: so-called cyber slavery operations, where many of those that are involved appear to have been kidnapped and trafficked and are forced to operate online scams (including ‘pig-butchers’¹³ and romance scams).

One well-known and controversial example is Sihanoukville in Cambodia, which has become a hotspot for these types of criminal activities. Between 50,000 and 100,000 people, many of them from Thailand, Vietnam,¹⁴ Lao PDR and other provinces of Cambodia, are reported to have been trafficked to work in scam operations in Sihanoukville (Kennedy & Southern, 2022; Clapp & Tower, 2022). Although there have been some official public crackdowns on these operations, it appears that victims are mostly being moved to other sites throughout Sihanoukville and border towns across Cambodia. Similar operations are also reported to be pervasive in casinos and SEZs across Lao PDR (for example, the Kings Romans casino), Myanmar (the number of people involved here is likely to be two or three times higher than in Cambodia; see Clapp & Tower, 2022), with victims originally from the Mekong, Southeast Asia and even Kenya, Uganda, Ethiopia and Brazil (Faulder, 2022; Gore et al., 2022; UNODC, 2019).¹⁵

The scam operations appear to be run by Chinese ‘investors’ with close links to criminal networks, and are enabled, or sometimes even protected, by a significant amount of political cover. For example, Kings Romans casino in Lao PDR is reported to be run by Zhao Wei, who was placed on the US sanctions list in 2018 for alleged activities of money laundering; storage and distribution of methamphetamine, heroin and other drugs; as well as the trafficking of wildlife, timber and people (Faulder, 2022). Similarly, in August 2022, Thai police arrested She Zhijiang, a businessman who is influential in the Shwe Kokko SEZ in Myanmar. She Zhijiang had been on the run from the Chinese authorities since 2012, and Thai police have charged him with running an illegal online casino. Nevertheless, little appears to have changed on the ground (Clapp & Tower, 2022). State-of-the-art telecommunications have sprung up in the Thai border area just across from known scamming operations in Lao PDR and Myanmar (Faulder, 2022).

¹³ This refers to a type of online fraud in which criminals build trust and lure their victims into relationships before convincing them to invest in online or cryptocurrency platforms.

¹⁴ Pacific Links Foundation, a GI-TOC contact, shared that the majority of victims whom they supported and who were referred to them, were mostly young boys from various regions of Vietnam, including ethnic groups and indigenous communities.

¹⁵ Recent developments in the cyber slavery operations were also shared and discussed at a regional conference organised by the Bali Process Regional Support Office (RSO) on 26 January 2023 in Bangkok, Thailand. See: Bali Process RSO (2023, April), https://s3.ap-southeast-2.amazonaws.com/assets.baliprocess.net/app/uploads/2023/04/07111922/TiPScams-Policy-Brief_RSO.pdf.

Illicit money linked to the scam operations is reported to be moved through various channels, including banks, the online trading of shares, anonymous payment systems, applications to buy lottery tickets or cryptocurrencies. This allows criminal actors to mix and legitimise money quickly (Zsombor, 2022). However, money is not only made from scamming: reselling victims to other scam compounds or extorting a fee for their release multiplies the profit.

As previously mentioned, the overwhelming majority of the businesses in SEZs across the Mekong are reported to be Chinese-owned. However, there is little information on the beneficial owners of companies, which makes it difficult to establish who ultimately owns the businesses and who owns the goods being stored there (Rowden, 2022; UNODC, 2019). This limits regulatory oversight and enables the use of shell companies to evade taxes, move money offshore and launder illicit proceeds. There appears to be little to no cooperation between the zone and customs and law enforcement authorities, and some SEZs are even located in areas where government authority and the rule of law are challenged by criminal influence (UNODC, 2019). Indeed, one key concern is the notion that SEZs constitute extraterritorial spaces or ‘lawless zones’ guarded by private security. For example, the national Royal Lao Police report that they were unable to gain access to the SEZ casino area of Kings Romans (Rowden, 2022).

3.2. Barter trade and hawala systems

To facilitate payment and avoid scrutiny from authorities, barter trade of illicit commodities is sometimes used. For example, truck drivers and loggers involved in illegal logging in Myanmar are reported to receive at least partial payments in drugs. It is assumed that this is mostly for personal use but these drugs might also be sold onwards and/or used to sustain other illicit activities (Amerhauser & Cartwright, 2023).

This is often also closely linked to hawala or other informal value transfer mechanisms (in Myanmar, the hundi system is common; in China, it is usually called *fei-chien* or ‘flying money’), which have been operating across the region for decades. They operate worldwide and involve the transfer of value from one jurisdiction to another without money actually being transferred, making them faster and more efficient than ordinary banks. It is a trust-based system, with potentially severe consequences for anyone who tries to run off with the money (Lintner, 2022, chapter 3). It is generally invisible, as goods are exchanged between countries, which are then converted into monetary value through domestic transactions and can therefore also be connected to misinvoicing and the illegal trade in goods (Herbert, 2020).

As reported by Herbert, China plays a significant role in these underground banking systems. In 2015, Chinese authorities seized approximately US\$130 billion from underground banks operating on the mainland, half through a single illegal operation. In addition, authorities seized another US\$148 billion in the first nine months of 2016 (Chen, 2017; Mavrellis & Cassara, 2022). Chinese underground banks are estimated to have over 10,000 clients and are believed to launder over US\$100 billion every year (Mavrellis & Cassara, 2022). There is a strong symbiotic relationship between TBML, informal currency exchange and illicit capital flight, as misinvoicing can serve as a method for Chinese citizens to convert yuan to a foreign currency and illicitly move it out of the country (Mavrellis & Cassara, 2022).

4. Observations

This paper has demonstrated that the ‘IFFs pyramid’, a framework for analysis of IFFs proposed by Reitano (2022), is a helpful tool for understanding IFFs in the Mekong region. The paper has shown that financial flows, trade flows and informal flows are all significant in the region and cause substantive harm to local economies and societies.

The Mekong region is host to a plethora of criminal markets, with a large number of criminal networks. In many of the places afflicted by organised crime, local law enforcement agencies appear to be compromised and political actors are corrupt, with ties to criminal groups and their activities. This was also confirmed by both the 2021 and 2023 Global Organized Crime Indexes, which showed that state-embedded actors play an important role in the Mekong region (GI-TOC, 2021b; GI-TOC, 2023). In such circumstances, it seems as if a lack of political will to address the issue is creating an open door for IFFs.

The role played by China is a clear golden thread running through the analysis of the drivers of IFFs in the Mekong, as illicit financial threats stemming from China pose a serious risk to the global financial system. The influence of Chinese interests and priorities has shaped economic and trade policies in the Mekong, to the detriment of meaningful control over illicit flows of any kind. The proliferation of SEZs, largely influenced by China – and amplified by the weaknesses created by tax havens, secrecy jurisdictions and failures in maintaining effective beneficial ownership – creates insurmountable vulnerabilities for regulators and enforcement.

One key area in which flows overlap (where trade flows mingle with informal flows and informality converges with financial flows) is in the numerous SEZs across the Mekong. Some have been morphed into ‘lawless areas’ where government agencies have little authority, further enabling and driving IFFs across the region.

Significant structural vulnerabilities that enable IFFs persist in all countries in the region, as the will to address them remains limited. Current responses to IFFs in the Mekong focus on the formal financial system, despite the importance of informal and trade-based flows. Indeed, despite the increased use of digital financial technologies, which provide some form of electronic trace, most trade and informal transactions remain hidden from financial institutions and fall outside government responses to IFFs. This significantly restricts the tools used by governments to respond. Additionally, also due to the widespread involvement of Chinese networks across multiple and diverse criminal markets, it seems that little is being done to change the status quo. On the contrary, in some cases, criminal actors are able to legalise the major points of vulnerability for the benefit of foreign actors and elites.

IFFs in the Mekong are transnational in nature, but cross-border cooperation and coordination among customs and police authorities, and also anti-money laundering (AML offices), remains limited. However, bank secrecy laws and beneficial taxation policies needs to be addressed jointly in order to decrease IFFs, so as to not displace these illicit flows. International organisations such as the FATF also have a crucial role to

play in countering IFFs in the Mekong. Although the FATF has no enforcement authority, its influence on the financial system and broader transactions should not be underestimated, as can be seen in the case of Myanmar. Through its Mutual Evaluation Report (MER) process, the FATF remains in dialogue with states and can push for reform, including on beneficial ownership. The latter can help uncover, for example, who is really behind casinos and other companies based in the Mekong's SEZs.

In conclusion, IFFs in the Mekong can only be understood comprehensively if the roles of financial flows, trade flows and informality – the three main means by which IFFs are held, enabled and moved according to the IFFs pyramid – are analysed jointly. They often exist side by side as well as overlap and interconnect, causing substantive harm to local economies and societies. Future research will need to map out the current responses to all three channels in order to be able to identify points of prevention and intervention.

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