

Written Statement of

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on

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and the Digitalization of Illicit Networks in the Americas”**

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¹ The views expressed in this testimony are that of the author and do not necessarily reflect the views of the William J. Perry Center for Hemispheric Defense Studies, National Defense University, or the Department of Defense. Testimony is drawn from the author’s publications, “Countering the Evolving Drug Trade in the Americas,” The Woodrow Wilson Center, January 2020, https://www.wilsoncenter.org/sites/default/files/countering_the_evolution_drug_trade_in_the_americas.pdf and “U.S.-Mexican Security Cooperation Faces the Future,” American Foreign Policy Council Defense Dossier, December 2021, <https://www.afpc.org/publications/e-journals/the-americas-influx>

Introduction

Thank you Chairman Whitehouse and Co-Chairman Grassley and members of the Senate Caucus on International Narcotics Control for the opportunity to testify on countering the evolving drug trade and the digitalization of illicit networks in the Americas. During the COVID-19 pandemic, transnational criminal organizations (TCOs), such as the Mexican cartels, have demonstrated their ability to quickly adapt to a changing environment and leverage emerging technologies to empower and enrich themselves. This testimony will examine the transforming drug market, the U.S. opioid epidemic, the role of the cyber domain as a force multiplier for drug trafficking and money laundering and recommend measures to counter the illicit economy.

The illicit drug trafficking business relies on the dynamic between supply and demand and is one of the most lucrative activities of transnational criminal organizations. These groups seek to maximize profits and sustain themselves through illicit financial flows. The illicit drug trade not only has detrimental health implications for consumers but fuels violence, insecurity, instability and corruption in nations along the production, transportation, distribution and consumption stages of this criminal enterprise. Drug trafficking is just one of the illicit activities TCOs engage in. They are also involved in human smuggling, arms trafficking, illegal mining, contraband, money laundering and public corruption. These crimes are accompanied by high levels of violence, and organized crime groups pose serious threats to citizen security and prosperity worldwide. Illicit financial flows serve as the lifeblood for all aspects of the criminal economy and curbing them is essential to impact global drug trafficking. Globalization has promoted movement of capital, financial innovations, and new technology such as mobile payments and digital currencies that have magnified the threat from illicit financial flows, the drug trade and transnational organized crime.

To combat drug trafficking, the U.S. and its partners must concentrate equally on supply and demand reduction with far-reaching strategies and policies that engage the public, private and civic sectors of society. The UNODC World Drug Report 2020 estimated that 269 million people abused drugs in 2018, that represented a 30% increase from 2009. Cannabis was consumed most widely in 2018, with an estimated 192 million users globally. Opioids, the deadliest of

misused drugs, recorded a 71% rise in deaths over the past decade, registering increases of 92% among women and 63% among men. Demand reduction is essential in combating drug trafficking with strategies that address prevention, treatment, recovery and international cooperation. Substance use disorder is a major public health threat, which unfortunately has intensified due to the COVID-19 pandemic since 2020. Drug use disorder is a preventable and treatable disease, and the drug trade threatens countries' political and social stability.²

Supply reduction is equally important in reducing drug trafficking. Restricting supply makes illicit drugs scarcer, more expensive and less socially tolerated. All phases of the drug trade that include cultivation, production, transportation, distribution, sales and income generation must be addressed. Efforts to reduce supply must be undertaken at the local, national and international levels. Nations should leverage diplomatic, military, intelligence and law enforcement capacity to interdict drug shipments, identify criminal networks and bring traffickers to justice.

The Evolving Drug Trade

The illicit drug trade in the Americas has been evolving from plant-based narcotics like cocaine, heroin and marijuana to potent synthetic substances like fentanyl and methamphetamine and has expanded due emerging technologies enabling marketing and trafficking. Since the 1980's, the U.S. war on drugs focused on countering cocaine trafficking that made the Colombian and Mexican cartels immensely wealthy and powerful. Over the past decade, U.S. drug consumption has shifted significantly from cocaine to opioids and methamphetamine, resulting in an unprecedented opioid epidemic in the U.S. with 104,288 people died of drug overdoses in the 12-month period ending September 2021, according to the Centers for Disease Control and Prevention.

Narcotics trafficking continues to be the most profitable illicit activity in the world but is adapting and leveraging cyberspace. As cocaine production in Colombia reaches its highest levels in history but consumption in the U.S. falls, cocaine traffickers

² U.S. Department of State, International Narcotics Control Strategy Report Volume 1, March 2021, <https://www.state.gov/wp-content/uploads/2021/02/International-Narcotics-Control-Strategy-Report-Volume-I-FINAL-1.pdf>

are seeking new markets as far as Asia and Europe where they can secure two to three times the proceeds more than in North America. Cocaine traffickers have gone global and are engaged in circumnavigating the world and stepping up their use of submarines. Meanwhile, heroin use in the U.S. has spread across suburban and rural communities and socioeconomic classes with over 90% of heroin in the U.S. originating from Mexico. Potent synthetic opioids like fentanyl have become more prevalent and popular in the U.S. that has resulted in the tragic opioid crisis.

Mexican cartels are increasingly trafficking opioids and synthetics responding to the changing U.S consumer market. Cartel Jalisco Nueva Generación, Sinaloa Cartel and the Gulf Cartel are the most powerful and dangerous transnational criminal organizations in Mexico. The atomization of large Mexican cartels and increased competition to dominate trafficking routes resulted in near record levels of violence in Mexico with 33,308 homicides registered in 2021. The cartels have remained active during the pandemic, trafficking dangerous drugs like fentanyl, heroin, meth and cocaine into the U.S. despite the COVID-19 lockdowns, closed borders and paralyzed international trade. Transnational criminal organizations have adapted quickly to the new pandemic environment. They are taking advantage of the fact that governments and security forces have been so focused on pandemic response rather than fighting crime. These groups are expanding their control of trafficking routes and markets and winning hearts and minds by providing COVID-related social services to marginalized communities in Mexico.

The DEA 2020 National Drug Threat Assessment published in March 2021 stated that Mexican drug trafficking organizations remain the greatest criminal drug threat to the United States. They are increasingly responsible for producing and supplying deadly fentanyl to the U.S. market. In Fiscal Year 2021, Customs and Border Patrol seized 624,500 pounds of drugs. Compared to last fiscal year, cocaine seizures increased 68%; methamphetamine seizures increased 7%; heroin seizures decreased 6%; and fentanyl seizures increased by a record 134%.³ With the pandemic lockdowns lifted and the U.S.-Mexican border reopened, drug trafficking destined for the U.S. is expected to surge as American demand for synthetic drugs like fentanyl and meth rises. The situation was

³ U.S. Customs and Border Patrol, Fiscal Year 2021 Statistics, <https://www.cbp.gov/newsroom/national-media-release/cbp-releases-operational-fiscal-year-2021-statistics>

exacerbated since substance abuse treatment centers were closed due to COVID-19, and emergency room visits for mental health conditions, domestic violence, child abuse, and suicide attempts increased.

The U.S. Opioid Epidemic

The U.S. is experiencing an ever increasing opioid epidemic. According to the Centers for Disease Control and Prevention (CDC), an average of 136 Americans die every day from an opioid overdose. The CDC reported that a record 104,288 people died of drug overdoses in the 12-month period ending September 2021 mainly due to opioids, and fentanyl has become the number one cause of death for adults 18-45 of age. Around 68% of the 70,237 drug overdose deaths recorded in 2017 involved an opioid. In 2017, the number of overdose deaths involving opioids (including prescription opioids and illegal opioids like heroin and illicitly manufactured fentanyl) was six times higher than in 1999.⁴

The first wave of overdoses began with increased prescribing of opioids in the 1990's with overdose deaths involving prescription opioids (natural and semi-synthetic opioids and methadone) increasing since at least 1999. Several U.S. pharmaceutical companies, including Johnson and Johnson and Perdue Pharma, are being blamed and sued for promoting prescription opioid use and contributing to the opioid epidemic. The second wave began in 2010, with rapid increases in overdose deaths involving heroin coming from Mexico. The third wave began in 2013, with significant increases in overdose deaths involving synthetic opioids, particularly those involving illicitly-manufactured fentanyl. The fentanyl market continues to grow and can be found in combination with heroin, counterfeit pills, and cocaine with most fentanyl coming from China and Mexico.⁵

Heroin: Heroin is an addictive opioid drug made from morphine, a natural substance taken from the seed pod of opium poppy plants. It can be a white or brown powder, or a

⁴ CDC/National Center for Health Statistics, National Vital Statistics System, Mortality. CDC WONDER, Atlanta, GA: U.S. Department of Health and Human Services, CDC; 2018. <https://wonder.cdc.gov>

⁵ *Ibid.*

black sticky substance known as black tar heroin that users inject, sniff, snort, or smoke. Since 2010, heroin availability in the United States has increased as Mexican transnational criminal organizations switched from trafficking marijuana and cocaine to the much more profitable heroin into the U.S. In 2015, 93 percent of the heroin analyzed entering the United States came from Mexico. Since poppy has such a short growing cycle of just four months, it is a very efficient crop in Mexico. Heroin laboratories located close to poppy fields are heavily dependent on precursor chemicals coming from China that transform the raw opium from poppy pods into the highly addictive narcotic.⁶

Heroin is readily available in the United States and is sold in various forms: fine powder, sticky tar, granular or chunky, gummy/pasty, pills, or a rock-like black substance that shatters like glass and is smoked, snorted, or injected. The CDC reported 21 percent increase in 2016 drug deaths involving heroin in 2016 at 15,469 over the 12,989 recorded in 2015.⁷ From January 2016 through December 2016, the price per pure gram (PPG) for heroin increased 5.5 percent, from \$855 to \$902 while the purity level averaged 33 percent, a slight dip from the prior years.⁸ Mexican traffickers are widening their profit margins and intensifying the “high” from low-quality heroin by mixing it with fentanyl that is much more powerful than heroin.

DEA Field Divisions seized 6,951 kilograms of heroin in 2019, a 30 percent increase from 2018, with the largest amounts of heroin seized in Texas, California, Arizona, and New York. California, Texas and Arizona are all major entry points for heroin sourced from Mexico and also serve as transshipment points for the onward movement of heroin to domestic markets throughout the United States. New York is regarded as the most significant heroin market.⁹ DEA Field Divisions reported heroin price increases as a result of the COVID-19 pandemic in 2020 in El Paso, Chicago, Denver, Houston, Louisville, New Orleans, New Jersey, New York, Philadelphia, and

⁶ U.S. Department of Justice DEA 2017 National Drug Threat Assessment, https://www.dea.gov/sites/default/files/docs/DIR-040-17_2017-NDTA.pdf

⁷ Department of Justice DEA 2018 National Drug Threat Assessment Report, October 2018, <https://www.dea.gov/sites/default/files/2018-11/DIR-032-18%202018%20NDTA%20final%20low%20resolution.pdf>

⁸ *Ibid.*

⁹ U.S. Department of Justice DEA 2020 National Drug Threat Assessment Report, March 2021, https://www.dea.gov/sites/default/files/2021-02/DIR-008-21%202020%20National%20Drug%20Threat%20Assessment_WEB.pdf

San Diego. It is possible that fentanyl availability experienced such little change during the pandemic due to the relatively smaller volumes of the drug needed to generate high amounts of revenue for drug traffickers, reflecting fentanyl's high potency, and the relatively small quantities needed for users to experience its effects. Pandemic-related challenges for drug trafficking organizations selling heroin, fentanyl, and other synthetic opioids have included supply uncertainty associated with fluctuating state lockdown orders throughout the United States and border restrictions issued by the United States and Mexico.¹⁰ More recently, the heroin trade has been overtaken by the more lucrative synthetic opioid market in illicit fentanyl.

Fentanyl: Fentanyl is a powerful synthetic opioid that produces effects such as relaxation, euphoria, and pain relief similar to morphine, oxycodone, methadone, and heroin but is some 50 times more potent. It can be used legally with a prescription, but illicit fentanyl is smuggled into the United States primarily in powder or counterfeit pill form that can be deadly in very small doses of as little as 0.25 milligrams.¹¹ China is the principal source country of illicit fentanyl and fentanyl-related compounds in the U.S., according to U.S. Customs and Border Protection. Fentanyl analogs and precursor chemicals used to make fentanyl are illicitly manufactured in Chinese labs and then sold on the Darknet and shipped in bulk to the U.S. and Mexico. Similarly, non-pharmaceutical fentanyl is increasingly being manufactured in Mexico and transported into the United States via well-established drug trafficking routes across the southwest border.

One kilogram of fentanyl costs about \$32,000, which can be used to make one million pills with a street value of more than \$20 million according to the DEA.

Fentanyl trafficking into the United States generally follows one of two pathways:

1. direct purchase of fentanyl from China by U.S. individuals for personal consumption or domestic distribution and

¹⁰ *Ibid.*

¹¹ American Addictions Center, "Fentanyl vs. Heroin: The Similarities and Differences Between Two Powerful Opioids," September 2019, <https://americanaddictioncenters.org/fentanyl-treatment/similarities>

2. cross-border trafficking of fentanyl from Mexico by transnational criminal organizations and smaller criminal networks.

How does the illicit fentanyl trade work? Orders and purchases from China are brokered over the internet. The predominant funding mechanisms associated with fentanyl trafficking patterns include:

1. purchases from a foreign source of supply made using money services businesses (MSBs), bank transfers, or online payment processors;
2. purchases from a foreign source of supply made using convertible virtual currency (CVC) such as bitcoin, bitcoin cash, ethereum, or monero;
3. purchases from a U.S. source of supply made using an MSB, online payment processor, CVC, or person-to-person sales; and
4. other, more general money laundering mechanisms like bulk cash smuggling associated with procurement and distribution.¹²

China has been accused of fueling the opioid crisis by exporting fentanyl and exploiting the U.S. Postal Service and international express mail carriers to ship fentanyl directly into the United States. According to a federal investigation, Chinese fentanyl dealers warned their U.S.-based customers via email that private delivery companies like FedEx electronically tracked packages, that would allow the easy identification of mail from suspect addresses and create a trail connecting sellers and buyers of illegal fentanyl, and they advised American fentanyl buyers they would send shipments by regular mail through the U.S. Postal Service to avoid detection.¹³

The U.S. Postal Service (USPS) has stepped up tracking, detection and interdiction efforts to curb the fentanyl trafficking into the U.S. through the mail. Congress has ordered the agency get advanced electronic data on 100% of inbound

¹² FinCEN Advisory to Financial Institutions on Illicit Financial Schemes and Methods Related to the Trafficking of Fentanyl and Other Synthetic Opioids, August 21, 2019, <https://www.fincen.gov/sites/default/files/advisory/2019-08-21/Fentanyl%20Advisory%20FINAL%20508.pdf>

¹³ Sari Horwitz and Scott Higham, "The flow of fentanyl: In the mail, over the border," *The Washington Post*, AUGUST 23, 2019, <https://www.washingtonpost.com/investigations/2019/08/23/fentanyl-flowed-through-us-postal-service-vehicles-crossing-southern-border/?arc404=true>

shipments by December 2020, with an urgent emphasis on parcels coming from China. By requiring data on the sender, recipient and the contents of an international parcel and incorporating new technology to scan packages, the postal service witnessed a 1,000% increase in the number of parcels seized containing synthetic opioids between 2016 and 2018. USPS saw the number of opioid parcel seizures increase by 750% domestically in the same timeframe.¹⁴ In September 2020, USPS issued their Strategy on Combating Illicit Drugs in the Mail.

Mexico has become a major transit and production point for fentanyl and its analogs. Mexico's two largest criminal organizations, the Sinaloa Cartel and the Jalisco Cartel New Generation (Cartel de Jalisco Nueva Generación – CJNG), are the most important Mexican purveyors of the drug and its precursors, although smaller criminal organizations and contractors may play significant roles in production and transport of the drug along the distribution chain. Both large and small transnational criminal organizations are capitalizing on the drug's popularity, and fentanyl is being laced into other substances such as cocaine, methamphetamine, and marijuana, without the end-user even knowing it. Rising seizures of counterfeit oxycodone pills laced with fentanyl illustrate that the market is evolving and adapting to consumer demand.¹⁵ The U.S. government has seized enough fentanyl this year (2021) to give every American a lethal dose, according to DEA Administrator Anne Milgram. With this shift from mail shipments of fentanyl from China to cross-border movement from Mexico, border security officials are enhancing measures to detect and interdict fentanyl trafficking into the U.S.

Methamphetamine's Comeback: While much of the focus in the U.S. has been on the opioid epidemic, the trafficking and consumption of methamphetamine (meth) has increased dramatically; meth is coming into the U.S. from Mexico at historical levels. Meth is a powerful, highly addictive stimulant, originally used in nasal decongestants and

¹⁴ Leandra Bernstein, Most fentanyl is now trafficked across US-Mexico border, not from China," WJLA News, July 16, 2019, <https://wjla.com/news/nation-world/most-fentanyl-is-now-trafficked-across-us-mexico-border-not-from-china>

¹⁵ Steven Dudley, Mexico's Role in the Deadly Rise of Fentanyl, Fentanyl: Summary and Major Findings, *InSight Crime*, February 19, 2019, <https://www.insightcrime.org/investigations/fentanyl-summary-major-findings/>

bronchial inhalers, that causes increased activity, talkativeness, and a pleasurable sense of well-being or euphoria. Lately, it has been marketed as a “safer” alternative to fentanyl because the chance of a deadly overdose from meth is not as great. Between 2017 and 2018, meth seizures in the U.S. increased by 142%, and overdose deaths from meth increased by 21% from 10,749 to 12,987 according to the CDC. DEA seized 53,079 kilograms of methamphetamine nationwide in 2019, an increase of 55 percent from 2018 (34,270 kilograms).¹⁶

According to the DEA, methamphetamine lab seizures have fallen across the United States to their lowest level in 15 years. However, the drug remains prevalent and widely available, with most of the methamphetamine in the U.S. produced in Mexico and smuggled across the southwest border. Meth seizures by U.S. Customs and Border Protection's Office of Field Operations have grown substantially, from 14,131 pounds in fiscal 2012 to 56,373 in fiscal 2018. Opioid-related deaths lead by far in the U.S., but when looking at the number of crimes committed by people under the influence of a particular drug, from stealing cars and burglarizing homes to rapes and shootings, meth is the No.1 common denominator.¹⁷

Mexican cartels are dominating the meth market as they can produce a more potent version of the drug, more economically. They have put domestic producers out of business in the U.S. According to Van Ingram, executive director of the Kentucky Office of Drug Control Policy, Mexican meth is so cheap you could not make it for cheaper than you could buy it. On June 6, 2019, three large meth labs were dismantled in Sinaloa, Mexico that were to produce 17 million doses of meth worth an estimated at \$160 million in the U.S. New technologies like drones that detect heatwaves of uninhabited areas are helping the Mexican military to detect meth labs. The Mexican authorities have dismantled 20 labs in Sinaloa so far in 2019.¹⁸ The cartels are bringing the meth into the U.S. at record levels, even using drones or aircraft and disguised it in different formats

¹⁶ DEA 2020 National Drug Threat Assessment, https://www.dea.gov/sites/default/files/2021-02/DIR-008-21%202020%20National%20Drug%20Threat%20Assessment_WEB.pdf

¹⁷ Katelyn Newman, “Breaking Back to Meth? As the opioid crisis snags headlines and attention, police in many parts of the country are grappling with a surge in meth from Mexico,” *U.S. News*, March 12, 2019, <https://www.usnews.com/news/healthiest-communities/articles/2019-03-12/meth-from-mexico-a-growing-problem-for-law-enforcement>

¹⁸ France 24, “Three large meth labs dismantled in Mexico,” June 5, 2019, <https://www.france24.com/en/20190605-three-large-meth-labs-dismantled-mexico>

such as cleaning fluids, in food items, and even in statues. On February 13, 2022, U.S. Customs and Border Protection officers seized nearly \$3 million worth of meth hidden in small packages within a shipment of onions at a commercial facility in San Diego from Mexico. The packages, detected by a canine unit, were mixed with the onion shipment in sacks; they were shaped into small globes with a white covering, designed to blend into the onions they were hidden with. This illustrates the ingenuity and the lengths drug trafficking organizations are willing to go to as they try to smuggle narcotics into the U.S.¹⁹ There is concern that increased meth consumption and supply could become the next drug crisis in the U.S.²⁰

The Digitalization of the Drug Trade in the Darknet

The marketplace for narcotics like cocaine, heroin, fentanyl, and methamphetamine has been supercharged by technology and the Internet, particularly by the Darknet. The deep web is the entire web that is not accessible by conventional search engines. Within the deep web, the Darknet is a network of websites with their IP address details intentionally hidden, often linked to criminal activity and illegal markets including drug trafficking. Narcotics transactions via the Darknet provide anonymity, choice, efficiency, ease of payment with cryptocurrencies like Bitcoin, and the convenience of having the narcotics delivered by mail to consumers.²¹ This online evolution, or digitalization, is disrupting and complementing the traditional marketing and distribution of narcotics.

Illicit online drug sales have grown in volume and complexity since the days of Silk Road, the original Darknet market that came online in 2011 and was taken down in 2013 by the FBI. The dealers who had been selling the drugs on that market migrated to competing sites set up with a similar infrastructure, using the Tor web browser, which

¹⁹ Emma Tucker, Authorities seize almost \$3 million worth of meth disguised as onions in California, CNN.com, February 26, 2022, <https://www.cnn.com/2022/02/26/us/border-patrol-meth-shipment/index.html>

²⁰ Charlie Lapastora, "Mexican drug cartels fueling meth comeback in US, with seizures at 'historically high levels,' Fox News, September 20, 2019, <https://www.foxnews.com/us/meth-border-mexican-drug-cartels>

²¹ Olga Khazan, "The Surprising Ease of Buying Fentanyl Online: To get extremely potent opioids, users turn to the dark web—and sometimes, Google," *The Atlantic*, January 2018, <https://www.theatlantic.com/health/archive/2018/01/the-surprising-ease-of-buying-fentanyl-online/551915/>

hides the location of the websites and their viewers, and Bitcoin, which allows for essentially anonymous payments. In 2017, when the police took down two of the biggest successors to Silk Road, AlphaBay and Hansa market, there was five times as much traffic happening on the Darknet as the Silk Road had at its peak, according to Chainalysis, a firm that analyzes Bitcoin traffic.

On Empire, one of the largest markets still online, people could choose from more than 26,000 drug and chemical listings, including over 2,000 opioids, shipped right to their mailbox. In June 2019, customers could still purchase five grams of heroin — “first hand quality no mix” — for 0.021 Bitcoin (roughly \$170), or a tenth of a gram of crack cocaine for 0.0017 Bitcoin (roughly \$14) on the dark market known as Berlusconi. Darknet markets are one of the vital sources of fentanyl and other synthetic opioids produced in and sent from China. Despite enforcement actions over the last six years that led to the shutdown of about half a dozen sites, including the takedowns of Wall Street Market and Valhalla, there are still close to 30 illegal online markets, according to DarknetLive, a news and information site for the Darknet. The desire to order drugs from the comfort of home and to maximize income from drug sales appears for many to be stronger than the fear of getting arrested.²²

Before and increasingly during the pandemic, the cartels have been capitalizing on cyberspace using online markets and cryptocurrencies to sell, finance and profit from the drug trade.²³ They are populating social media platforms like TikTok and Instagram to market narcotics, glorify the “narco” lifestyle and even recruit young people known as “ni-ni’s” (who neither study nor work) to their organizations. The Drug Enforcement Administration has warned of the alarming increase in the availability and lethality of fake prescription pills containing fentanyl and methamphetamine and their availability online. Teenagers on social media are two degrees of separation away from a drug dealer.

²² Nathaniel Popper, “Dark Web Drug Sellers Dodge Police Crackdowns, The notorious Silk Road site was shut down in 2013. Others have followed. But the online trafficking of illegal narcotics hasn’t abated,” *The New York Times*, June 11, 2019

<https://www.nytimes.com/2019/06/11/technology/online-dark-web-drug-markets.html>

²³ Steve Fisher and Kirk Semple, “Hit Hard by the Pandemic, Mexico’s Drug Cartels Tweaked Their Playbook,” *New York Times*, December 29, 2020,

<https://www.nytimes.com/2020/12/29/world/americas/mexico-pandemic-drug-trade.html>

The DEA has published a “reference guide” to alert the public that drug dealers and traffickers have been using emojis on social media to target children and teenagers, according to authorities. The guide was accompanied by a list of emojis that the DEA said represent certain narcotics, including Oxycodone, Xanax, cocaine, marijuana, and more. This was in response to drug traffickers increasingly using smart phones to distribute, sell and buy fake pills and using emojis to reach a younger market.

Meanwhile, in a disturbing development, already well-armed Mexican cartels are increasingly employing emerging technologies like drones used for surveillance, propaganda videos, night vision combat operations and kinetic attacks on adversaries. The incorporation of emerging technology and the exploitation of cyberspace and social media platforms are expanding and empowering narcotics trafficking and consumption.

Illicit Financial Flows and Adaptive Money Laundering Mechanisms

Financing serves as the oxygen for criminal networks whose main objective is income generation from illicit activities. They derive power from their wealth and use it to corrupt and co-opt rivals, facilitators, and/or government and security officials.²⁴ Financing is essential to support and sustain the command and control, personnel, arms, communications, logistics and operations of organized crime groups. For this reason, following the money trail and depriving criminals of illicit financial flows can disrupt and disable these networks.

Through money laundering, criminals try to disguise the proceeds, sources, or nature of their illicit activities. Terrorist financing refers to the processing of funds to sponsor or facilitate terrorist activity that could include clean and dirty funding. Methods of money laundering and terrorist financing include: the banking system, cash couriers, bulk cash smuggling, money services businesses, alternative remittance systems (hawalas), store of value, trade-based money laundering, mobile or internet payments, cryptocurrencies, non-profit organizations, real estate and

²⁴ Celina B. Realuyo, “The Future Evolution of Transnational Criminal Organizations and the Threat to U.S. National Security,” *The Shifting Human Environment: How Trends in Human Geography Will Shape Future Military Operations*, Paul T. Bartone & Mitchell Armbruster, Editors, Defense and Technology Paper 107, National Defense University Press, May 2015, <http://ctnsp.dodlive.mil/2015/05/06/dtp-107-shifting-human-environment-how-trends-in-human-geography-will-shape-future-military-operations/>

front companies. While terrorist financing and money laundering may have different objectives, they share similar tactics that abuse and undermine international financial systems.²⁵ Here are some ways transnational criminal organizations move, hide and store their income.

The Mexican cartels are among the richest and most powerful transnational criminal organizations in the world that engage in drug and human smuggling; they resort to various methods to move and launder their money. While they continue to practice cross-border bulk cash smuggling, the cartels have turned to shell companies to launder millions of dollars, through an intricate scheme that involves national and international money transactions. Criminals use straw men to create these companies, including real state companies, jewellery stores, and consulting services; all these companies made transactions that do not match their tax returns. Furthermore, the money laundering network employs housewives, students and bank tellers. In 2014, the Mexican Financial Intelligence Unit found four companies that sent and received resources to hide the origin and destiny of the resources. The four companies were created on the same day in 2012 and had the same address and the same legal representative, who turned out to be a straw man. After it launched an investigation into a more complex money laundering scheme, it found that four shell companies received and transferred MXN 3,523.2 million in less than two years. These companies were linked with another three companies that were being investigated for working for the Sinaloa Cartel.²⁶

Trade-based money launderers (TBML) continue to engage in a sort of parallel method of transferring money and value around the world. These methods often entail the alteration of shipping documents or invoices and are frequently undetected. The Black Market Peso Exchange (BMPE), one trade-based money laundering scheme, is often used by Mexico-based drug trafficking organizations to collect money from their drug sales in the U.S. without having to take the risk of

²⁵ Celina B. Realuyo, "Leveraging Financial Intelligence to Counter Transnational Threat Networks in the Americas," *U.S. Southern Command Dialogo Magazine*, March 2019 Special Edition, English: <https://dialogo-americas.com/articles/leveraging-financial-intelligence-to-counter-transnational-threat-networks-in-the-americas/>

²⁶ Zorayda Gallegos, "Mexican drug cartels used these shell companies to launder money," *El Universal*, June 6, 2020, <https://www.eluniversal.com.mx/english/mexican-drug-cartels-used-these-shell-companies-launder-money>

smuggling bulk amounts of U.S. currency across the Mexican border and without having to convert and wire the U.S. currency through established financial institutions, which not only carries transaction fees, but also a threat their illegal activity will be detected.

In a BMPE scheme, a peso broker works with an individual engaged in illegal activity, such as a drug trafficker, who has currency in the U.S. he needs to bring to a foreign country, such as Mexico, and convert into pesos. The peso broker finds business owners in the foreign country who buy goods from vendors in the U.S. and who need dollars to pay for those goods. The peso broker arranges for the illegally obtained dollars to be delivered to the United States-based vendors, such as the stores in the Fashion District, and these illegally obtained dollars are used to pay for the goods purchased by the foreign customers. Once the goods are shipped to the foreign country and sold by the foreign-based business owner in exchange for pesos, the pesos are turned over to the peso broker, who then pays the drug trafficker in the local currency of the foreign country, thus completing the laundering of the illegally obtained dollars.²⁷ The growing network of Trade Transparency Units (TTUs) is intended to combat this method of money laundering through the monitoring of import and export documentation. These units focus on detecting anomalies in trade data—such as deliberate over- and under-invoicing—that can be a powerful predictor of TBML.

Casinos and real estate are also money laundering mechanisms. One such method is known as the Vancouver Model. The process begins in China, where currency controls prevent citizens from taking more than \$50,000 out of the country. To avoid that rule, wealthy Chinese citizens enter into arrangements with domestic criminal syndicates with links to Vancouver, Canada. The citizens transfer money to criminal-controlled bank accounts in China before traveling to Vancouver where the criminals' associates provide them with their funds in

²⁷ U.S. Immigration and Customs Enforcement, Large-scale law enforcement effort targets downtown Los Angeles businesses linked to money laundering for drug cartels, September 14, 2014, <https://www.ice.gov/news/releases/large-scale-law-enforcement-effort-targets-downtown-los-angeles-businesses-linked>

Canadian dollars, which may be profits from pre-cursor chemicals or fentanyl sales. That money is then laundered through casino gambling. The Chinese citizens visit casinos in Vancouver, exchange their money for casino chips, and then make a series of low-value bets and then exchange back the chips to Canadian dollars, now clean of their illegitimate criminal origin. From there, financial proceeds from the Vancouver Model are either invested back into the acquisition of fentanyl supplies by the criminal gangs or invested into British Columbia real estate by the Chinese citizens themselves, who are able to avoid the scrutiny of Chinese regulators and Chinese taxes by doing so. The influx of foreign citizens buying property in Vancouver with their laundered money also impacted the city, causing the cost of living and housing prices to rise to levels unaffordable to most local residents. A 2016 report by Transparency International Canada suggested that almost 50% of the city's most expensive homes were bought using structured purchase methods that could conceal the identity of the owners.²⁸

Chinese money laundering rings have been increasingly moving the drug proceeds of the Mexican cartels earned in the U.S. The Department of Justice in April 2021 reported that three individuals pleaded guilty to their involvement in a conspiracy to launder at least \$30 million of drug proceeds combined throughout the U.S. on behalf of foreign drug trafficking organizations including the Sinaloa Cartel. These guilty pleas are the result of a nearly four-year investigation into the relationship between foreign drug trafficking organizations and Asian money laundering networks in the United States, China, Mexico, and elsewhere. The defendants converted drug proceeds into Chinese and Mexican currency through a variety of methods, including “mirror transfers” in which financial transactions in the U.S. are used to trigger the release of equivalent funds into bank accounts in

²⁸ Comply Advantage Knowledge Base, “Money Laundering: The Vancouver Model,” <https://complyadvantage.com/knowledgebase/vancouver-money-laundering-model/#:~:text=The%20Vancouver%20Model%20is%20a,regulatory%20approach%20to%20financial%20crime>, and Sam Cooper, “How Chinese gangs are laundering drug money through Vancouver real estate,” *Global News*, April 19, 2018, <https://globalnews.ca/news/4149818/vancouver-cautionary-tale-money-laundering-drugs/>

China, with those funds then being used to purchase Chinese goods that are subsequently sold by merchants in Latin American countries, including Mexico.²⁹

Among the defendants in this case, U.S.-based Chinese citizen, Gan Xianbing, was sentenced to 14 years in prison for running a scheme where money from Mexican criminal groups was picked up in Chicago, transferred to bank accounts in China and then ultimately sent back to Mexico. In 2018, Gan handled approximately \$534,206 in drug money before being arrested at Los Angeles Airport in November 2018, during a layover while flying from Hong Kong to Mexico. Gan has since become the most well-known, but far from the only, Chinese money launderer connected to some of Latin America's most dangerous criminal groups, including the Sinaloa Cartel.³⁰

Many of these Chinese brokers are also engaged in legitimate business and use that business as cover for and to further money laundering activity. Once the drug proceeds were in the hands of the launderers, they contacted one among a network of Chinese-owned businesses in the U.S. and Mexico and asked them to transfer a correspondent amount of money through Chinese banking apps. This happened entirely through the Asian country's domestic banking system and outside the purview of US authorities. This technique also allows the laundering process to avoid scrutiny in China. China's financial regulators limit private individuals from handling more than \$50,000 in foreign currency and any transfers surpassing this limit must be granted special dispensation. However, there is no such limit on domestic transfers. It is unclear to what extent the businesses and people used to move this money within China are even aware of the illegal nature of these transactions, making it all the more difficult to crack down on these schemes.³¹

Cyberspace and cryptocurrency are the new frontier for organized crime groups battling for control of vast criminal markets for drugs, arms, sex and people.

²⁹ U.S. Department of Justice, April 14, 2021 Press Release, Three Members of Transnational Money Laundering Network Pleaded Guilty to Aiding Foreign Drug Trafficking Organizations, <https://www.justice.gov/usao-edva/pr/three-members-transnational-money-laundering-network-pleaded-guilty-aiding-foreign-drug>

³⁰ Chris Dalby, How Chinese Criminals Secretly Move Millions for Mexico Cartels, InSight Crime, May 12, 2021, <https://insightcrime.org/news/chinese-money-launderers-mexico-cartels-move-millions-secret/>

³¹ *Ibid.*

To track the use of Bitcoin and other cryptocurrencies designed to anonymize users, the Mexican government instituted a new law in 2018 that requires all registered cryptocurrency trading platforms to report transfers above 56,000 pesos (\$2,830). Bitcoin's use to launder money is particularly increasing among drug gangs such as the Jalisco New Generation Cartel (CJNG) and the Sinaloa Cartel of captured kingpin Joaquin "El Chapo" Guzman, according to U.S. and Mexican authorities. Mexican cartels are believed to launder an estimated at \$25 billion a year in Mexico alone. Criminals typically split their illicit cash into small amounts and deposited them in various bank accounts, a technique known as "smurfing." The threshold for banking transactions that raise red flags is \$7,500. They then use those accounts to buy a series of small amounts of bitcoin online, he added, obscuring the origin of the money and allowing them to pay associates elsewhere in the world. According to the DEA, both Mexican and Colombian transnational criminal organizations are increasing their use of virtual currency because of the anonymity and speed of transactions, and the use of virtual currency will only expand in the future.³² The pandemic just accelerated the digitalization of illicit networks in their use of cryptocurrencies in drug trafficking and money laundering activities.

Measures to Counter the Evolving Drug Trade and Digitalization of Illicit Networks

The U.S. and partner nations must intensify their efforts in drug demand and supply reduction, narcotics detection and interdiction, and counter-money laundering and cyber measures to keep up with the rapid changes in the production, marketing, financing and delivery of drugs, particularly of synthetic drugs. The following measures can contribute to countering the evolving drug trade and digitalization of illicit networks:

1. Permanently place fentanyl-related substances (FRS) into Schedule I of the Controlled Substances Act (CSA) to empower law enforcement's ability to bring those involved in trafficking and producing of illicitly manufactured synthetic opioids to justice.

³² Diego Oré, "Latin American crime cartels turn to cryptocurrencies for money laundering," *Reuters*, December 8, 2020, <https://www.reuters.com/article/mexico-bitcoin-insight-idUSKBN28I1KD>

2. Actively educate Americans of all age groups on the opioid epidemic and deadly dangers from fentanyl-laced counterfeit drugs and opioids.
3. Identify, monitor and dismantle online illicit drug markets and the use of social media for the marketing, sale and promotion of drug consumption, especially to minors, and consider duty of care requirements to reduce the risk of harm to users.
4. Revitalize U.S.-Mexican cooperation to curb drug production, trafficking and the laundering of TCO proceeds under the auspices of the October 8, 2021 Bicentennial Framework for Security, Public Health, and Safe Communities.
5. Hold China accountable for the export of pre-cursor chemicals used for illicit narcotics and fentanyl that has become the number one cause of death of American men aged 18-45.
6. Detect, disrupt and prosecute Chinese money laundering networks associated with the drug trade.
7. Leverage digital and financial intelligence to detect and disrupt the use of cryptocurrencies in counternarcotics operations.
8. Establish specialized units or task forces at the national and international levels to share intelligence and investigate digital illicit financial flows, identify and seize assets and detect, dismantle and deter organized criminal networks engaging in drug trafficking and illicit financial flows.
9. Work with partner countries through the Financial Action Task Force (FATF) and the Egmont Group to share best practices regarding evolving money laundering schemes using cryptocurrencies.
10. Take steps to prevent the possible exploitation of newly emerging financial services and products, such as e-wallet services and cryptocurrencies, for drug trafficking and money laundering.