

RISK ASSESSMENT STRATEGIES AGAINST MONEY LAUNDERING AND INTERNATIONAL TERRORISM FINANCING

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***Abstract:** In the context of geopolitical and socio-economic situation, organized crime, money laundering and international terrorism have taken on new meanings, extending their scope at an alarming level, designed to challenge the construction of the rule of law and democratic countries. Most professionals and researchers in criminology believe that the source of such facts lies in the perpetuation of deficitary structures in politics, economy and law, in the maintenance of increasing social and economic disparities among individuals, groups and communities and increasing social and ethnic conflicts and tensions.*

***Keywords:** money laundering, illegal financial system, tax evasion, organized crime, international terrorism, means of transnational terrorism infiltration in the economy.*

1. APPROACHES TO MONEY LAUNDERING AND TERRORISM FUNDING, IN THE CONTEXT OF FINANCIAL CRISIS AND ILLEGAL FINANCIAL FLOWS

Making recommendations on preventing and combating money laundering and terrorist financing must necessarily start from a deep analysis of factors generating the dynamics of this phenomenon, because the characteristics are specific to each country. The key feature of illicit financial flows and illicit capital flows is being hidden among the official records of the country of origin. Illegal capital gains obtained by placing such capital abroad usually do not return to their country of origin.

Illegal capital can be generated through series of means and operations which are not to be found in national accounts or payments balances. Some examples are illegal products trading, smuggling, corruption, currency movements, tax evasion, hawala transactions and more. It is obvious that most of the financial flows that are not captured by official records are unlawful and violate civil and criminal laws of states, fiscal and customs

regulations and banking regulations of the countries in which these capitals are produced. While the conceptual difference between licit and illicit financial flows is clear, the distinction between the two categories discussed in statistical terms is difficult. Not to mention that the available statistical data are often incomplete or inaccurate. In fact, there is no official statistics on the existence of illicit capital flows because they are not detected.

Empirical studies (UNDP, 2011:16-17) on illicit financial flows indicate the possibility to classify the generating factors into three broad categories (Figure 1): macroeconomic factors, factors dependent on the structural characteristics of the national economy, factors related to global governance.

Illicit capital holders, capital which is obtained as a result of committing crimes, are careful to hide these funds rather than to maximize the official rentability rate. Also, the holders of such funds are not interested in the evolution of the fiscal deficit, economic growth and external debt of the country of origin, which is increasing due to the economic activities in the field of underground economy.

Illicit financial flows are increased by structural factors such as rising income inequality, the rate of artificial and unsustainable economic growth, the increasing international trade without legal supervision etc.

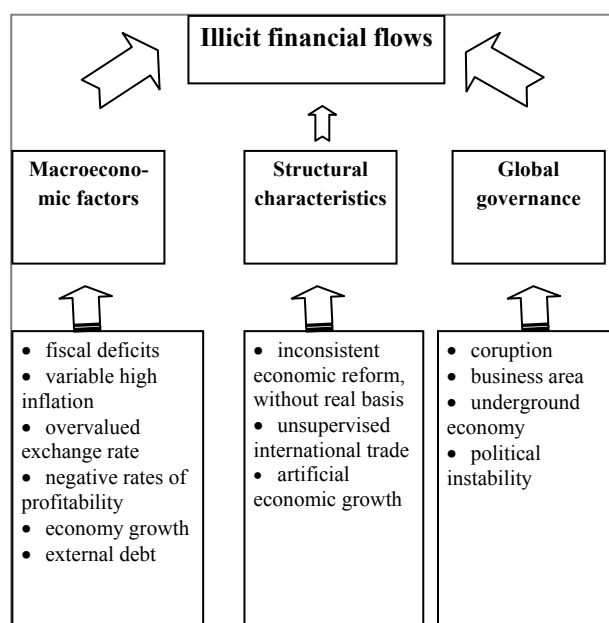


Figure 1. Generating factors of illicit financial flows. (Source: UNDP, 2011:17.)

It is obvious that there is a strong interaction between the three categories of factors. For example, overvalued exchange rates stimulate the development of a parallel foreign exchange market, with significant effects on the growth of the underground economy activities, including corruption and income distribution distortion in society.

There is also a strong interaction between macroeconomic context and the business climate. Promoting sustainable growth economic policies (sustainable fiscal deficits, low and stable inflation, attractive interest rates, etc.) may attract significant foreign direct investment, while an unstable economic policy, severe macroeconomic deficits discourage such investments. Moreover, corruption increases the cost of business development, reducing the country's ability to attract investors.

Money laundering and terrorism financing have some common aspects (Schneider, 2010:3): they use different types of transfers and electronic payments systems to move

money through several jurisdictions; the individuals involved engage in a variety of criminal activities either as traffickers or as members of criminal syndicates. In this regard, the line between money laundering and terrorism financing becomes thinner as terrorists often participate in the crime area and cooperate with criminals to get money and weapons.

Based on these features, a meaningful risk assessment strategy regarding money laundering and terrorism financing at state level should take into account the following three categories: geographic risk and country risk, business risk, production and trading risk.

Companies whose important customers are located in countries that have not implemented an adequate strategy to prevent and combat money laundering and terrorist financing will need to consider additional rules on customer knowledge and risk management procedures to monitor money laundering.

High risk countries are considered to be those that: use cash as the main exchange mean, have an unstable political regime characterized by high corruption both in the public and private sectors, are known as drug-producing or transit countries for drug trafficking, have been categorized as countries with major abnormalities in preventing and combating money laundering and terrorist financing.

Risk assessment on money laundering and terrorist financing classify countries worldwide as follows: countries with high risk, medium risk or low risk. These attributes are assigned based on publicly available information that can be found in the following documents:

- blacklisted countries at high risk of money laundering and terrorist financing, published periodically by the Financial Action Task Force (FATF) (includes recently removed countries);
- mutual evaluation reports of the FATF, the World Bank and IMF on money laundering and terrorist financing; the USA Patriot Act, Section 311 designates the most vulnerable countries to money laundering;
- OECD blacklist of countries that promote negative tax practices;

- USA list of drug producing countries and drug transition countries;
- U.S. list of terrorism sponsors;
- the annual reports of the State Department of the U.S. regarding the risk of money laundering and terrorism by countries, reports of the European Council, Transparency International and other similar bodies;
- management system and country rating of national banks.

There are different characteristics that make a business to be considered risky. For example, casinos and gambling are preferred targets for money laundering because in this activity field there is no developed culture on preventing and combating money laundering. Such activities, which convey significant cash amounts, should be carefully monitored.

Offshore banks provide a wide range of financial services under the protection of privacy and secrecy. Professionals facilitates the creation of genuine money laundering vehicles. When the illegally obtained amounts of money are used for the purchase of real estate, luxury cars and various items, it is likely that this action represents a net loss to the economy.

These principles do not apply in the context of illegal monies invested in legitimate, legal business. On the other hand, unfair competition generated by these amounts of money in that industry / branch induce potentially disastrous effects for honest operators in this area. Similarly, but in purely economic perspective, it may be considered that the entrance into the country of large amounts of money to be washed would generate an overwhelmingly positive effect. However, this kind of input creates unfair competition in the economy for legitimate operators and facilitates corruption proliferation.

Businesses that use cash funds allow masking money obtained from illegal activity into deposits containing money produced in legal activities. This is why the U.S. Bureau for exchange control published a list of high-risk businesses of money laundering.

Individual risk which an entity can expose itself to refers to the potential risk of facilitating a terrorist transaction by any

individual, organization or public person, by avoiding the mandatory inspections required by specific legislation in the area.

Products and services that involve high risk of money laundering are those in whose process of production and / or trading an intermediary element occurs, on an ongoing basis and without any constraints. In other words, selling / trading these products interposes an intermediary whose identity is usually unknown.

Movement of products / services ensures rapid movement of large volumes of funds or transactions, or both, hiding the real source of these funds. Such operations allow anonymity and cash converting into financial instruments. Individual and business accounts are likely to host such transactions.

Because the final goal is always obtaining profit and because the source of the funds and the financing is often "legitimate" the purpose of terrorism financing is different from money laundering, in each case, both criminals and terrorist organizations, transfer money from one country to another in order to conceal any traces.

Due to this fact and because some of the performed operations refer to people that are on the lists, the role of banks and other financial institutions - in particular, currency exchange houses, financial investment companies, insurance companies and quick money transfer operators - is essential in combating terrorist financing.

The instruments used in order to combat terrorism financing are similar to those used against money laundering: standard norms about the client, continuous monitoring of specific transactions (such as fast transfer of money and transfers via SWIFT) and norms about the accounts of customers who have as partners persons located or that come from countries with an increased risk of terrorism.

Banks and other financial intermediaries are required to focus in particular on non-profit and charitable organizations and on their activities or operations related to them by:

- the existence of non-profit organizations without being able to justify the connections between them (organizations that have the same address, same managers or staff, transfer

money towards each other or use the same intermediate in their dealings with the financial system) nonprofit organizations that operate across sectors or countries under different names;

- large amounts of money (especially cash) declared as being collected from various individuals or communities of a certain ethnicity or religion; amounts of money that do not seem to have any economic justification regarding the purpose and the activity of the declared non-profit organization or regarding the community from which the funds apparently came;

- sudden rise in the frequency of financial transactions and amounts of money credited to non-profit organization, or conversely, the non-profit organization has in the current account funds that have been kept for a long period of time;

- operations or transactions to or from countries of high risk; operations of the same type performed in their own name by the directors of non-profit organizations coming from such countries.

Identifying transactions with funds suspected to be linked to acts of terrorism involves transmitting a report to the appropriate competent authority. Other types of professions or activities which fall under the same incidence of combating money laundering should consider getting involved in activities intended to contribute to the development of laws, regulations and guidelines to combat money laundering and terrorist financing.

The financial crisis has revealed quite clearly the limits and sometimes the deficiencies of the surveillance system used in Europe. However, they could not identify excessive risks. The supervision and control did not intervene in time. Coordination among national authorities was far from optimal when transnational financial institutions were faced with problems, despite the fact that these institutions were becoming more numerous.

The Union's response to these serious problems was the introduction of completely new supervisory structures adapted to the transnational nature of financial transactions namely the European Banking Authority, the European Securities and Markets Authority

and the European Insurance and Occupational Pensions Supervisors (in operation since 1 January 2011). In addition, the European Commission proposed a series of measures that having as their object rating agencies, capital of the banks and audit reform.

European Systemic Risk Board monitors the entire financial sector in order to identify potential problems that could lead to a future crisis. It works in close collaboration with the new European Supervisory Authorities.

In addition to coordinating and monitoring national authorities these new bodies will work with other authorities around the world to ensure a better global supervision. In Romania, money laundering for financing international terrorism is regulated and sanctioned by law no. 230/2005, for preventing and combating money laundering and the establishment of measures for preventing and combating terrorist financing. In 2011, taking into account the recommendations included in the, MONEYVAL European Council report concerning the third round of the detailed assessment of Romania in the fight against money laundering and terrorist financing, the law was amended and supplemented by Law no. 23S/2011.

2. INSTITUTIONS INTERESTED IN COLLECTING AND PROVIDING DATA CONCERNING THE FREQUENCY OF OCCURRENCE OF MONEY LAUNDERING FOR THE FINANCING OF INTERNATIONAL TERRORISM

Until 1970 statistics of were widowed opportunity to examine crime patterns. Collection of data concerning crime was poor, without the possibility of electronic transmission and processing. In 1974 Professor Walker started the first research project on crime in Australia, his research was based on data collected from individual reports of the Metropolitan Police.

In Romania, terrorism is included in the category of threats to the national security by Law no. 51/1991 concerning Romania's national security. Subsequently, by Law no. 14/24.02.1992 regarding the organization and functioning of the Romanian Intelligence Service, preventing and combating terrorism is the express

responsibility of this service. Also, for combating terrorism, Romania has effectively committed to the International campaign against terrorism through military participation, being a major landmark of Romania's National Security Strategy. Romania has also acted and shall act within NATO, the European Union and other international organizations towards promoting and consolidating democracy, supporting governments and security and defense institutions in the fight against terrorism, participating in multinational operations, comprehensive assistance in the process of prevention, counteracting and post-conflict reconstruction (H.G. no.21/2001). The analysis of crime trends at a national and international level had started from the data provided by national police authorities on identified crime, but the processed information raised problems of reliability and international comparability, especially since national statistics were dependent on the availability of victims to report crimes. You might think that data regarding crime are collected and centralized by all interested institutions.

We refer in particular to the following categories of institutions / services / persons:

- police services that should be concerned by monitoring their own achievements recorded on line of identifying and bring to justice the perpetrators and publish such data as very important performance indicator;

- the prosecution and prosecutors should also monitor the achievements of convictions, so namely to make sure that offenders are appropriately punished, depending on the nature and seriousness of the offenses committed;

- criminology and forensics services whose mission is to prevent and counteract organized crime activities in the area and reduce their impact on society;

- Border Guard, Coast Guard and National Customs Authority, whose responsibility is to protect national borders and that represents the first and last redoubt of defense against transnational organized crime;

- National Agency for Fiscal Administration, whose job is to ensure that all incomes are taxed;

- attorney bars, associations and legal unions, accounters and appraisers, and other

similar bodies that protect the ethics and integrity of the profession;

- banking associations and other financial organizations whose concerns include ensuring the stability and credibility of the national financial system;

- national statistical institutes responsible for compiling statistics on important developments of society, including the economic ones.

Unfortunately, both at national and international level such bodies / institutions do not develop reliable and complete statistics concerning illicit financial flows and money laundering.

Most of them do not even centralize such data. The situation can be attributed to the fact that until recently it was not treated as money laundering phenomenon itself but was approached tangentially related to other crimes. As identifying and capturing an offender can be the first step towards dismantling a criminal networks, similar attempts to identify money laundering can lead to the discovery of drug offenses, for example, and vice versa.

By definition, the phenomenon of money laundering manifestation indicates a prior offense that is included and highlighted in the statistical processing and can be monitored in order to assess progress over time. Given the fact that the estimation of revenue generated by prior crimes is very difficult (for example, the crime of drug trafficking) is understandable why organizations like those listed above are reluctant to provide estimates of the share of illicit financial flows caused by such crime and involved in money laundering operations.

However, the existence of a problem of great importance, money laundering, is unanimously accepted. International organisms, governments, financial institutions etc. are willing to spend heavily in the implementation of strategies of preventing and combating the phenomenon, though they _ do not certainly know its extent. Furthermore, they are not able and do not have the capacity to check if the problem is extending and it takes the allocation of additional funds in order to fight the phenomenon, or if the size of was limited as a result of effective strategic measures. In the contemporary era it seems unreasonable to exert

so much effort in tackling money laundering without having to confirm their effectiveness.

To finish with explaining the reasons that caused us to state that official statistics are not useful in estimating illicit financial flows / money laundering we must underline that there are no such statistics actually.

There is published data concerning individual cases, that confirm the existence of the phenomenon, but not its magnitude. Furthermore, because in the investigation of money laundering are involved several institutions (police, forensics, criminal investigations, prosecution, etc..) and several procedural stages of legal research are held, published data are provided simultaneously by several institutions, sometimes overlapping which makes any form of analysis extremely difficult.

3. CONCLUSIONS

Analyzing the issue of money laundering and its impact on international terrorism financing one considers that at least the following conclusions can be drawn:

- money laundering or financial flows generated by organized crime are extremely difficult to quantify, certainty exists only with regard to the existence of the phenomenon that varies from one country to another;

- traditional methods, case studies, quantitative estimates econometric models for quantifying the size of the underground economy tend to underestimate or overestimate the contribution that money laundering has in exacerbating the phenomenon.

- the Walker pattern still seems to be the most reliable and robust method of estimating global financial flows generated by money laundering, although the microeconomic foundation is built on ad-hoc variables. Although plausible the variables of the model they are still arbitrary.

- estimating the size of funds of organized crime (money laundering volume) is an extremely difficult task mainly due to lack of adequate data, both at national and international level (one of the reasons for this is the lack of unity and transparency of states,

that have not established a system of integrated management of strategic information);

- effects generated by money laundering on the economy cannot be estimated accurately based on the information available (given that the estimation of prior revenues generated by crime is very difficult is explainable why concerned national and international bodies are reluctant to provide estimations of the proportion of illicit financial flows produced by the various operations involved in crime and money laundering and official statistics are virtually useless);

- quantifying the volume and dynamics of money laundering is a constant need for decision-makers involved in developing policies to prevent and combat the phenomenon, it is required a considerable improvement in the processes of collecting and providing adequate data on the effects of crime suspected and / or proven and the frequency of money laundering in different criminal environments.

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