

**MONEY LAUNDERING TYPOLOGIES
IN THE REPUBLIC OF SERBIA**



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MONEY LAUNDERING TYPOLOGIES IN THE REPUBLIC OF SERBIA

There are many definitions of money laundering, but regardless of the differences between these definitions, whether they are simple as: legalization of the illegal capital, or complex, such as the one stipulated by the Warsaw Convention¹ and which was implemented in the Criminal Procedure Code of the Republic of Serbia, the entire professional and practical community agrees that:

Money laundering is the process of disguising of an illegal origin of money or property acquired by criminal acts.

In case the property is obtained by committing a crime, the perpetrator tries to find the way to use the money without attracting the attention of relevant authorities. Therefore, he performs a series of transactions in order to show that the money was legally earned. Money laundering consists of three basic phases:

1. The first phase: the phase of “placement” is an interruption of the direct link between the money and illegal activity used to acquire that money. Money is placed on the bank accounts, usually in form of some legal activity where the payment is done in cash. One of the approaches is a foundation of a fictitious company which does not have business activities, but is used for placement of “dirty” money or dividing of the large sums of money and their placement on the accounts in the amounts which are not suspicious or do not have to be reported to the relevant authorities.

2. The second phase: the phase of “layering” or “disguising”. After the money enters the legal financial system, it is transferred from the account where it was placed, to the other accounts of the companies, in order to show some fictitious business activity or to perform some legal business (trade or service) with a company which operates legally. The main goal of these transactions is to disassociate the money from the crime it originates from.

3. The third phase: the phase of “integration”, where the “dirty” money is assimilated as the money which originates from the permitted activities. Frequent method for integration of the “dirty” money, in the legal financial system, is purchase of real-estate or purchase of control packages of shares of joint-stock companies, which is an example of the concentration of “dirty” capital in the great amounts, and that is the goal of the money “launderers”. The integration concentrates on market values i.e. whatever can be purchased and sold. Giving real-estate under lease is legal, and income from the rent is not suspicious. Money is often invested in companies experiencing difficulties, which, afterwards continue to work successfully, and the results of these activities are considered as legal revenue. Once the money enters this phase, it is difficult to discover its illegal origin.

Illegal gain of assets is main, if not the only, motive for committing a crime. In order to enjoy the gain from a crime, this property needs to be falsely presented as being legal.

¹ Conversion or transfer of assets, knowing that those assets are gained from a crime, for the purpose of hiding or disguising of the illegal origin of the assets or assisting a persons involved in crime to avoid legal consequences of his actions; hiding or disguising the real nature, source, location, disposal, movement, property rights or other ownership rights over property, knowing that those assets are acquired through crime.



The consequences of money laundering are: undermining of the stability, transparency and efficiency of the financial system of a country, financial disorders and instability, threatening the reform programs, reduced investment, deterioration of country's reputation and jeopardizing of the national security.

Money laundering is a global phenomenon, and very often, money laundering crosses the borders of one country. Money laundering has become a worldwide problem. Namely, there is a data showing that approximately 1000 billion dollars are laundered every year, and only 1 per cent of the total amount is seized.

Administration for the Prevention of Money Laundering (hereinafter referred to as the: "Administration") is a financial intelligence unit of the Republic of Serbia, and the central body for the prevention of money laundering and financing of terrorism. Pursuant to the Law on the Prevention of Money Laundering and Financing of Terrorism, the obligors submit the reports to the Administration on all suspicious transactions and entities, and the Administration then analyses them, gathers additional information, and in case there is a reasonable doubt that someone is engaged in money laundering in a specific case, such information is forwarded to the relevant institutions, primarily, competent prosecutor's office and the police. The Administration may, without previous report of suspicious transaction, notice that there is a doubt that a certain person or organized group are engaged in money laundering, and request information from the obligors and other state institutions. Furthermore, the Administration may also establish a "suspicious case" based on the initiative of another state institution, such as: courts, prosecution, Security-Information Agency, Privatization Agency, Securities Commission etc.

Although the Administration for the Prevention of Money Laundering is the only institution with the words "prevention of money laundering" in its name, it is not the only institution engaged in the fight against money laundering. Apart from the Administration for the Prevention of Money Laundering, the entire system for prevention of money laundering consists of:

- Obligors, i.e. all those representatives of the financial and non-financial sector obliged to apply the regulations for the prevention of money laundering. Their goal is to, through application of legally prescribed actions and measures create unfavorable climate for money laundering in one country. Pursuant to Article 4 of the Law on the Prevention of Money Laundering and Financing of Terrorism the obligors are:

- 1) Banks;
- 2) Licensed exchanges offices;
- 3) Investment fund management companies;
- 4) Voluntary pension fund management companies;
- 5) Financial leasing providers;
- 6) Insurance companies, insurance brokerage companies, insurance agency companies and insurance agents with a license to perform life insurance business;
- 7) Persons dealing with postal communications;
- 8) Broker-dealer companies;
- 9) Organizers of special games of chance in casinos;
- 10) Organizers of games of chance operated on the Internet, by telephone, or in any other manner using telecommunication networks;
- 11) Auditing companies;



12) Licensed auditors.

The obligors shall include both the entrepreneurs and legal entities exercising the following professional activities: intermediation in real-estate transactions; provision of accounting services; tax advising; intermediation in credit transactions and provision of loans; factoring and forfeiting; provision of guarantees; provision of money transfer services.

Despite the fact that they are not named as obligors, the attorneys shall also be obliged to apply the actions and measures prescribed by the Law on the Prevention of Money Laundering and Financing of Terrorism.

- Bodies competent for supervision, which supervise the application of the provisions on the prevention of money laundering and financing of terrorism by the obligors, thus ensuring proper application of the regulations and functioning of this part of the system. Bodies competent for supervision are: National Bank of Serbia, Securities Commission, Foreign Currency Inspectorate, Administration for the Prevention of Money Laundering, Ministry of Trade and Service, etc.

- Police, prosecution and courts, are repressive bodies in the system for the prevention of money laundering, since they prosecute the perpetrators of the criminal act of money laundering. Proper functioning of this part of the system is of crucial importance: prosecution of money “launderers”, their severe punishment and seizure of the property influence a general prevention, i.e. the message is sent to the society that money laundering does not pay off in Serbia, and possible money “launderers” are deterred from committing such actions.

In the past, there were frequent cases of so called “self-laundering“, i.e. when a certain person performs an illegal activity, e.g. tax embezzlement, and tries to hide the tracks of such money and falsely represents it as legally obtained.

The situation has slightly changed recently both in Serbia and in the world. There is a tendency for the criminal organizations to “hire” a professional money “launderer”, usually an attorney or an accountant, or both, to design a number of complex activities in order to disguise illegal origin of money. The available data shows that some of the most talented financial experts are recruited for that (especially young ones with the ambition to get rich quickly) by the organized crime, in order to “cover the tracks” of the cash flow and origin. There is a tendency of association, with national and regional groups which “professionally” perform money laundering, thus, money laundering has become an international business. Also, money laundering is much more sophisticated and more difficult to detect and prove.

It can be expected that abuse of off-shore destinations will continue. The reasons are already well known: simple procedure for the foundation of companies, without the obligation to determine the founder, placement of money without the obligation to determine its origin are definitely the advantages which will be used by the “launderers” in the future.

There are some predictions that the insurance industry, which was not especially interesting for the “launderers”, will now become important, due to the new products which are about to be placed. Beside above stated, the risk of money laundering is caused by disputable identification, payment of premiums of third entities etc.



The process of privatization in Serbia is coming to an end. For this reason, in the future, the privatization will not be primary channel for the “dirty” money. However, we should not forget the fact that these are the enormous amounts of money of undetermined origin.

The main goal of these typologies is educational: they should demonstrate to the obligors, starting from the banks, exchange offices, and other representatives of the financial sector, and the intermediaries in real-estate transactions, accountants, auditors and attorneys, what the possibilities for money laundering in different sectors are, what the weak points of each sector are and to which type of legal operations they should specifically pay attention.

MONEY LAUNDERING TYPOLOGIES IN THE BANKING SECTOR

During the last ten years, the banking sector in the Republic of Serbia has undergone significant changes. Four big state banks have been shut down, and the Service of Social Accounting was closed due to comprehensive transformation of the financial and commercial system. When the Administration started working, there were many financial institutions. At a time, there were over sixty banks operating, and they significantly differed from one another not only in size, but based on their founders and clients.

From the moment the Administration started working until now, the number of banks has halved. Some of the banks went to bankruptcy and some of them were purchased by the foreign banks. Coming to our market, the foreign banks have introduced their procedures related to the prevention of money laundering and financing of terrorism, thus, until 2009, when the Law on the Prevention of Money Laundering and Financing of Terrorism was adopted, it used to happen that the banks with majority foreign capital applied the rules and procedures of their group, which were less lenient than what current Law stipulates. Supervision of the banks by the NBS has led to creation of an organized sector which we have today, when it comes to the prevention of money laundering and financing of terrorism.

Due to the fact that the banks are an important factor of the economic and financial stability of each country, it is important for them to prevent the inflow of “dirty” capital which could jeopardize their reputation. During last few years, the banking sector has been experiencing major turbulences. In order to overcome the financial crisis, banks offer many new products and services, which could potentially be used to place illegally gained money in the financial flows. The criminals have tendencies to attempt and invest illegally gained assets in the banking sector by purchasing the shares of the banks, and, thus directly or indirectly, take part in the management of a bank and design of its business policy. Such activities should be prevented by strict application of the legal solutions related with the ownership of the banks and participation in the management structure.

Money laundering always means that, in one of the phases, the assets must go through a bank account. Therefore, increased offer of banking services and different payment instruments provides many different options for their abuse.

So far, based on the experiences of the Administration, the most frequent ways to use legally defined banking services and codes based on which transfers are performed, in order to integrate “dirty” money in the banking system are:

- Loans with 100 per cent deposit as security or prepayment of loans,
- High cash payments without real grounds or payments which are unusual for the client (very often, “other transactions” is stated as the basis for the payment, or different transactions for “placement” of illegally gained money),
- Payments based on the turnover of goods, especially services with the off-shore companies (frequent successive payments based on providing of services of market research, consulting, marketing, attorney’s fees or accounting fees, purchase of real-estate etc.),
- Payment based on services to newly founded domestic companies,
- Cash payments as a loan of the founder for solvency of a company (the founders of legal entities abuse this legally allowed basis for payment for integration of “dirty” money, since the origin of the assets is not questioned, there are no limits in regards to the amounts of cash payments and these amounts are not a subject to tax payment).

TYPOLOGIES

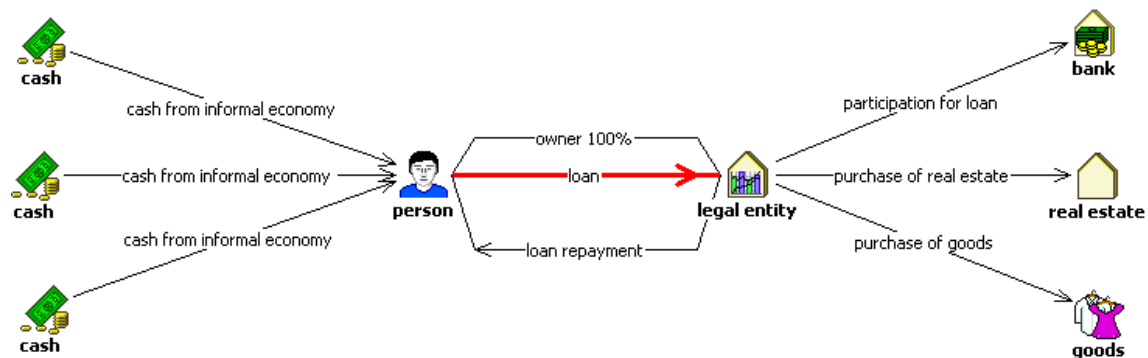
When it comes to money laundering typologies, here are some of the most significant risk factors:

- Risk of the transactions (fictitious, withdrawal of money on different grounds, deposits, loans, mortgage transactions, different placements, service transactions, liens etc.)
- Risk of the offered bank products (cards, mortgages, loans for different purposes, certificates of deposit, custody services, safe deposit boxes ...),
- Risk of the clients (relations, knowing, identification, discovery of real owner)
- Risk of the bank as a financial institution (persons who could influence the bank policy related with the application of legal standards on the prevention of money laundering and financing of terrorism are included in the ownership structure of the bank, through off-shore companies, custody accounts or investment funds).

Considering above stated aspects and the experience so far, these are some of the most important typologies:

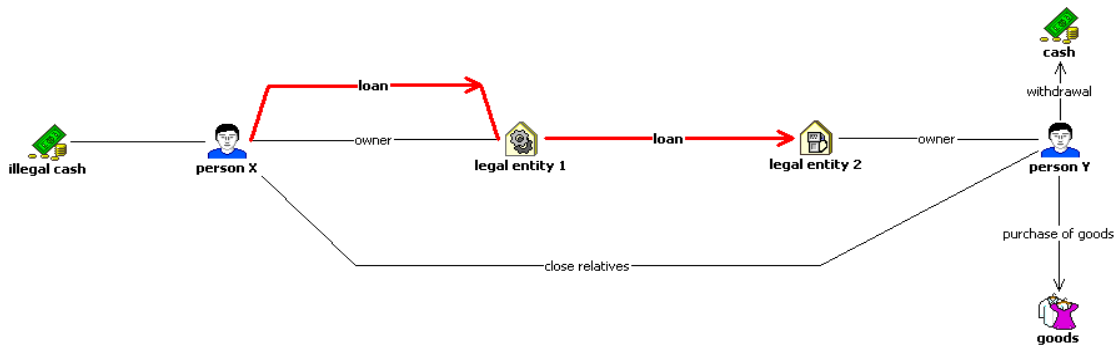
- **Cash payments of an illegal origin as a loan of the founder for liquidity for the expansion of business activities.**

Natural persons place higher amounts of cash, as a loan of the founder in favor of a legal entity. Money which is thus invested in a legal business, and is exempt from tax, may be from selling of goods and services for which this legal entity is registered but on the black market. The amount of the loan may be returned to a bank account of a natural person or may be permanently invested in business as a security deposit for obtaining loans, repayment of loans, purchase of goods, real-estate, securities etc.



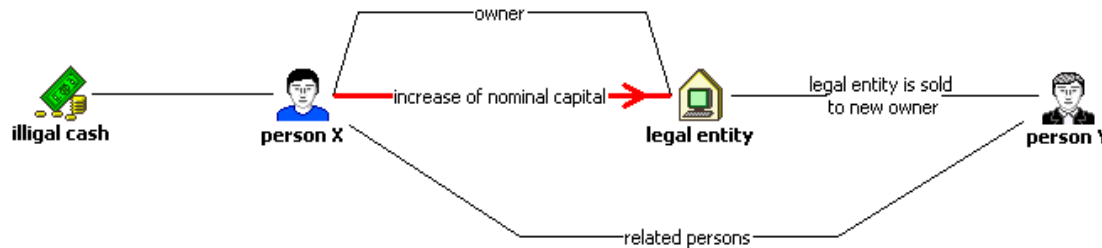
- **Cash payments of an illegal origin as a loan of the founder for liquidity are transferred to other legal entities.**

Natural persons successively place cash of illegal origin in smaller amounts, as a loan of the founder, in favor of a legal entity, which then transfers the total amount also as a loan to the account of another close relative. The assets can be withdrawn in cash or can be invested in goods.



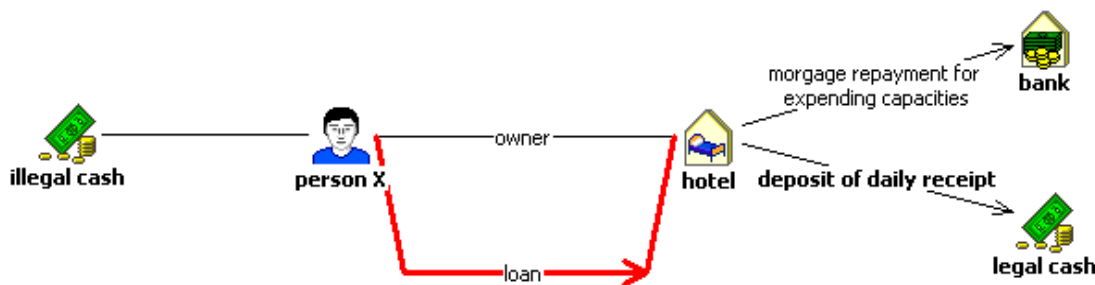
- **Cash payments for the purpose of increase of nominal capital before selling of the legal entity**

Natural persons place illegal cash in smaller amounts, as an increase of nominal capital, in favor of the legal entity which is later sold to the known owner.



- **Cash payments of an illegal origin as a loan of the founder for liquidity for payment of mortgage loans.**

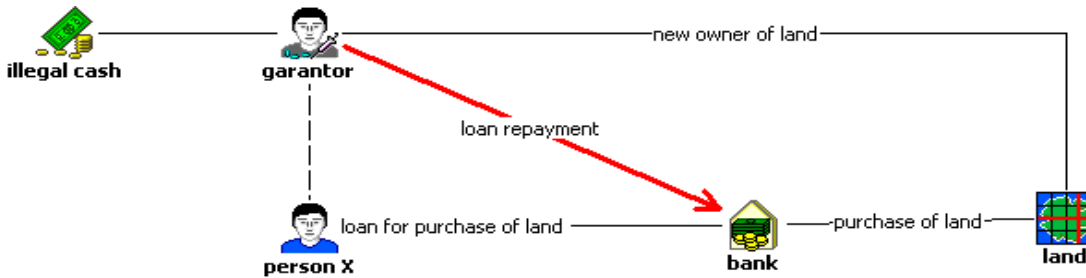
Persons involved in organized crime who own a hotel-hospitality facility make cash loan payments to the account of their own company. The funds from the account are used for mortgage repayment, which is used for expansion of the capacities and purchase of the new facilities. By showing the greater extent of hotel or hospitality related activities, it is possible to introduce illegal cash in legal operations of a legal entity.



- **Loan repayment by the guarantor using the illegal cash payments**

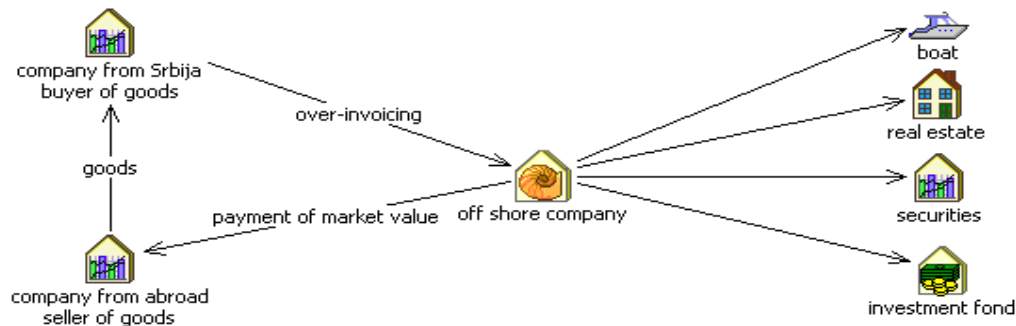
A person involved in organized crime, is designated as a guarantor by the loan agreement. In case a loan beneficiary does not fulfill the obligations stipulated by the agreement, the repayment of the loan shall be a responsibility of the guarantor, who shall make cash payments of due installments. The loan was used for the purchase of land, therefore, the

loan beneficiary, based on the debt, shall transfer the ownership of the land to the person who repays the loan.



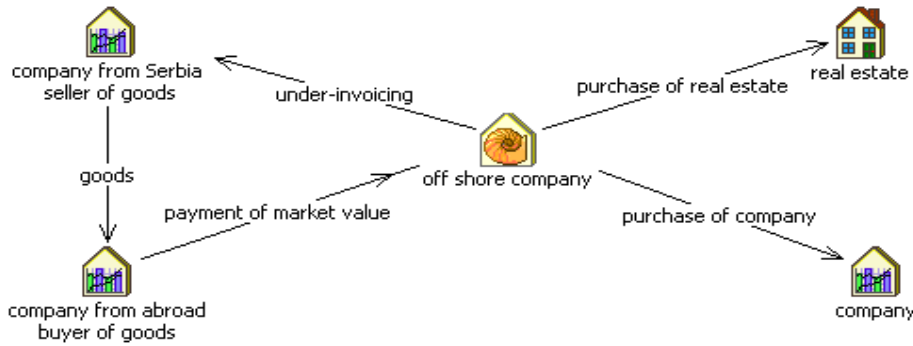
- **Transferring of the assets in favor of the off-shore companies based on over-invoicing**

In order to avoid payment of the value added tax, legal entities from the Republic of Serbia issue orders to transfer the assets for the increased invoices, either in quantity or value of the imported goods, in favor of the off-shore companies of the same real owners, which then sell the goods for market prices to the real seller. Afterwards the off-shore companies dispose of the acquired difference in prices, from the non-resident accounts opened in neighboring countries, by investing the money in real-estate, securities, investment funds, antiques, yachts and goods.



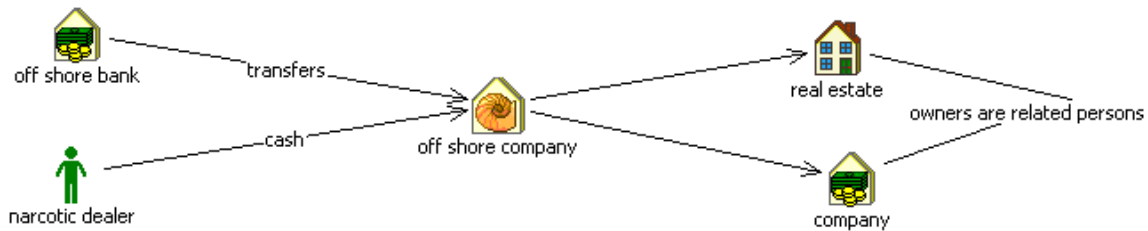
- **Transferring of the assets based on the order of the off-shore companies based on under-invoicing**

The off-shore companies, which originate from Serbia, charge foreign buyers with real market prices, transfer the assets in favor of Serbian export companies based on under-invoicing. The same real owner of the legal entity in Serbia and the off-shore company uses the difference in price from the off-shore company's account, which is not a subject to tax payment, for the purchase of the production facilities and real-estate in Serbia and abroad.



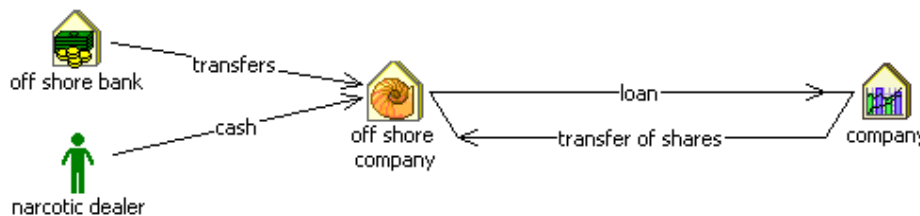
- **Transfers ordered by the off-shore companies for the purchase of companies and real-estate**

Persons involved in **organized crime own several off-shore** companies whose accounts are used to transfer illegally obtained assets **based on the purchase of** newly founded companies and real-estate in Serbia which are, partially, owned by the members of the family or business associates.



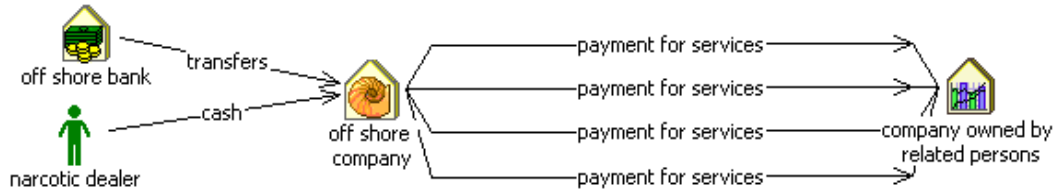
- **Transfers ordered by the off-shore companies in favor of the legal entities based on the loans**

An off-shore company owned by a person involved in organized crime transfers illegal cash based on the loan from its account in favor of a legal entity in Serbia, and the contract regulates that the security will be a pledge on shares of the loan beneficiary. The loan is not paid and an off-shore company takes the majority ownership over the company in Serbia.



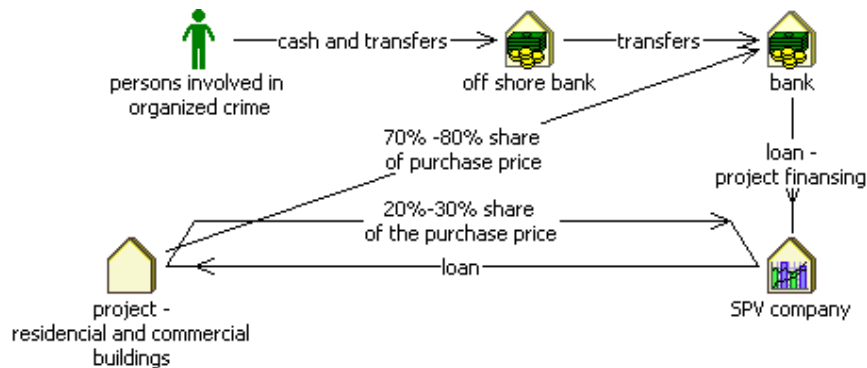
- **Transfers ordered by the off-shore companies in favor of the legal entities based on the services**

The off-shore companies whose real owners are involved in organized crime, **transfer small amounts of illegal cash from their accounts**, based on providing services of market research, consulting, marketing, attorneys' and accounting fees, in favor of the companies in Serbia owned by the business associates or relatives.



- **Investments of the off-shore companies through loans of foreign banks granted to the legal entities in Serbia.**

An off-shore company owned by a person involved in organized crime owns an investment account with a foreign bank, where the assets gained by selling of the narcotics are placed or transferred. The bank uses such assets to establish funds for the investments of higher risk to purchase state securities, shares of other banks, legal entities or for placing of the loans such as project financing. Project financing is granted to newly founded companies (SPV - Special Purpose Vehicle) for building of the residential and commercial buildings, and as a security for repayment of the loans, mortgage on the building and pledge on the shares of the company are envisaged. In case the loan is not repaid, the bank activates the mortgage and becomes the owner of the bigger part of the building, and by selling this building, the high profit is gained by the loan beneficiary (SPV), bank, and all the owners of investment accounts in proportion to their participation in the financing.



- **Cash transactions of the natural persons in higher amounts**

The natural persons, who acquired financial gain by abuse of their professional position or based on corruption, are placing or paying higher amounts of effective money, which

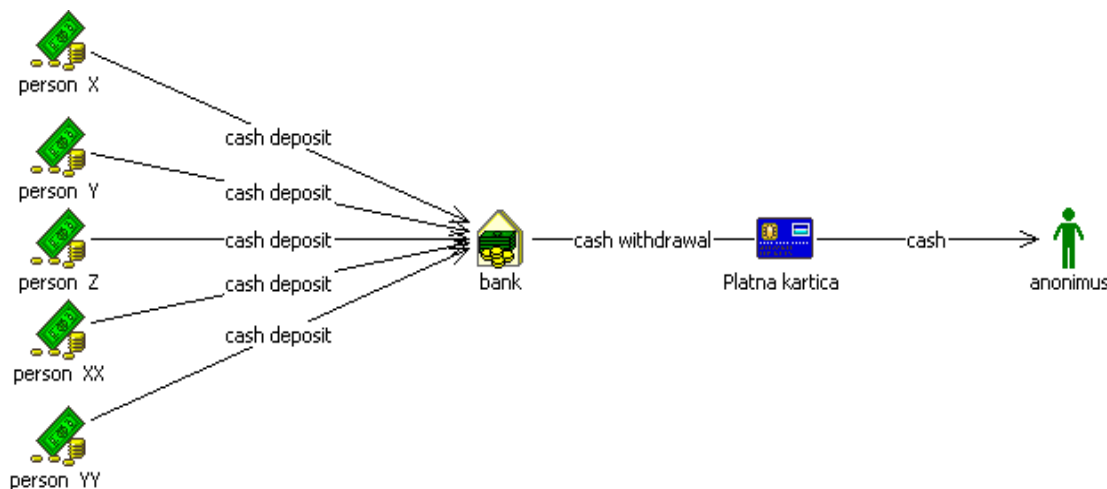
significantly differs from the usual transactions of that client and are not in accordance with the revenue and status of the client.

- **Transfers from abroad in favor of the natural persons, without clear grounds**

The natural person, who acquired financial gain by abuse of their professional position or based on corruption, receive payments from abroad from natural persons or legal entities with which they do not have business relation.

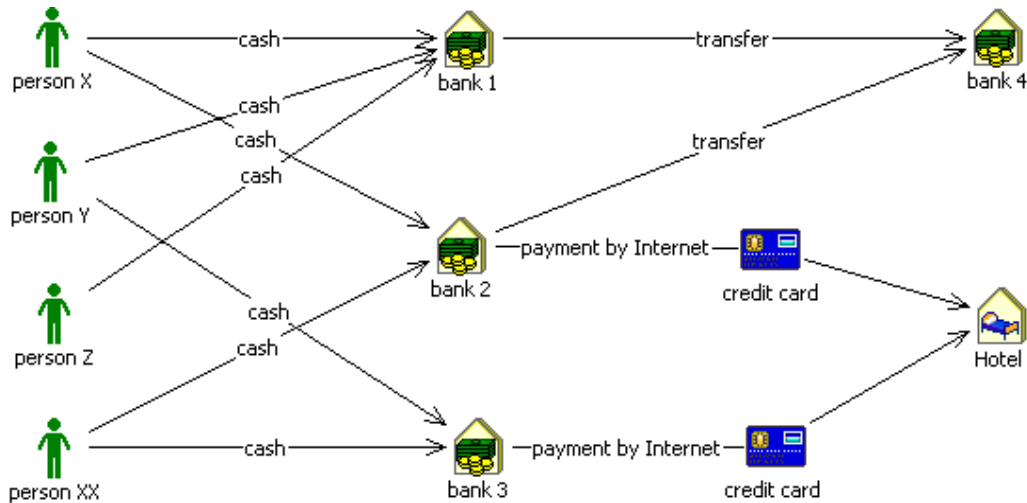
- **Numerous cash deposits by several natural persons on the account of one natural person**

Numerous cash deposits within a short period of time, done in accordance with an order of several persons, below the legal minimum for reporting, on the account of one natural person, from which the cash is withdrawn within a short period of time and transferred abroad based on the cash withdrawal from ATM machines aboard.



- **One person is authorized to dispose of the assets on the accounts of several persons with frequent cash deposits**

Numerous cash deposits within a short period of time, done in accordance with an order of several persons, below the legal minimum for reporting, on the accounts of several persons where the same persons is authorized to dispose of the assets on these accounts, and the assets are directed or transferred abroad based on the card spending for the purchase of goods and services via Internet.



- **Owning more accounts in different banks**

A natural person opens more dinar or foreign currency accounts, special purpose accounts and savings accounts in different banks and makes frequent transfers from one account to another.

EXAMPLE

Person X was depositing his illegally acquired assets on the account of his off-shore companies in the British Virgin Islands and the Seychelles, which founded the business in Liechtenstein. All three companies opened investment accounts with the Foreign Bank Y.

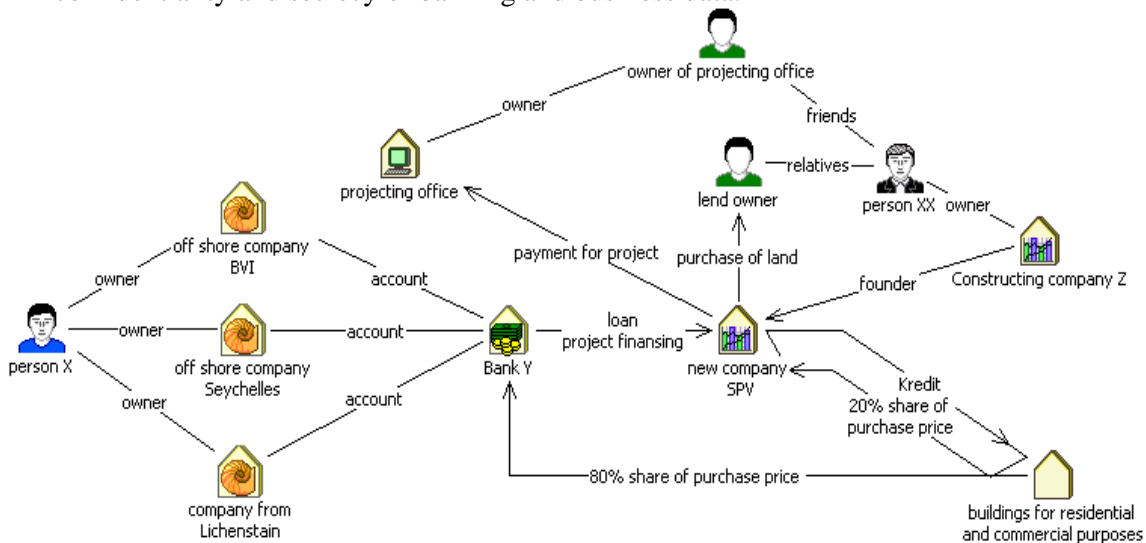
The funds from the clients' investment accounts were used by the Foreign Bank Y, in accordance with the cost-effectiveness assessment, for project financing of commercial and residential building in Novi Sad. The contract anticipated mortgage on an object under construction as a loan guarantee. The loan beneficiary -investor is the Construction Company Z owned by Person XX who, in order to get the loan, founded a new company – SPV, whose sole commercial activity was the construction of a specific object, with an obligation to participate with a minimum of 20 per cent in the entire investment.

For the purpose of founding and operating, Construction Company Z transferred to the new Company SPV funds from cash deposits on the basis of loan from the founder, which originate from the apartment sales in the black market. The new Company SPV, which was obliged to secure property ownership of the building site, the project documents and the construction permit, purchased the land from Person XX's relative and paid close business associates for drafting the project, by over-invoicing, which calculates in the obligatory participation of 20 per cent in the investment. The loan was used for the purchase of the required building material and paying for the services of multiple sub-contractors, also owned by relatives and friends.

The loan beneficiary was not paying the installments, so the Bank activated the mortgage and became the owner of a larger part of the residential and commercial building, while the funds remaining from the sale were divided according to participation in financing, between the loan beneficiary and Bank Y, which includes owners of the investment accounts abroad.

Indicators by which transactions may be characterized as suspicious:

- Client performs cash deposits on the account of his own company with purpose of payment designated as “loan from founder”, and the assets are then transferred to a newly founded company.
- Significant increase in the amounts of deposits into the account of a company whose main activity is providing of architectural and engineering services.
- Client withdraws large sums of money from an account into which significant amounts have been transferred on the basis of a loan approved abroad.
- Transactions which include multiple intermediaries or a larger number of accounts, particularly if the participants of such complex transactions are from the countries where standards in the field of the prevention of money laundering and financing of terrorism are not applied, or from the countries with strict regulations in force regarding confidentiality and secrecy of banking and business data.



TRENDS

An increasing offer of services and products provided by the banks will change in the future. The development of infrastructure and technology will result in priority of the e-banking over conventional modes of banking. E-banking is a package of modern services which enables simple use of banking services by the clients, using the most common channels of communication – Internet, mobile phone, land phone. Major advantages of these services are their lower cost, significant saving of time and the possibility of performing transactions at any time of day or night, but it is these very characteristics, where the client is spatially remote from the bank, thus hindering the identification procedure, that offer new possibilities for money laundering, which should be timely foreseen, prevented or recognized.



With the M-commerce service, the client will be able, at any time, using his mobile phone, to give an order to his bank to transfer funds in a small amount, from his account to a different one, from which the funds can be further transferred or withdrawn in cash or with a bank card.

The question is how banks will fight against alternative modes of payment via Internet, which already exist, such as “cyber cash”. A card with a chip contains cash which can be withdrawn by phone or from the ATMs, and the cash can also be transferred from one card to another. There is no way to track down these card transactions, because there is no registry of transactions, as it exists with Visa or MasterCard credit cards. There are two key reasons why banks are interested in Internet banking:

1. Internet users are mostly young people with higher degree of education and higher income than an average client.
2. Internet is a very efficient and cheap distribution channel.



Fighting for the clients, the banks will expand their services and offer the products which rely more on Internet, therefore, the increased offer of services over so-called virtual counters is expected, as they are used today when applying for an online loan.

The PayPal payment system already exists in the region, and is also soon expected to be present in Serbia. The PayPal system enables transactions, via Internet or by using bank cards, directly from a PayPal account, which is not subject to strict procedures for client identification and for determining the origin of funds, as well as sending money to anyone with an e-mail address.

It is anticipated that the financial institutions in Serbia will, by expanding their offer, take over the existing trends in economically developed countries in regards to the investment of assets through investment funds and trading new financial products, making it harder to determine the ownership and legality of the origin of assets of the final investor.

It should also be mentioned that the global economic crisis, which brought to the dramatic drop in value of shares worldwide, led to the increased demand for gold and other precious metals, which are currently very interesting for investments and trade.

There is also an opinion, advocated by the large banks, that the future belongs to huge financial institutions which will provide investors with various services ranging from the insurance, car loans, to airplane tickets. On the other hand, those advocates, led by the software companies, believe that the future belongs to the companies that will, with the development and application of new technologies, offer investors the maximum control over their finances, through sophisticated products that balance risk and profit. The idea behind the revolution in technology of banking is that technology and finances have become one and that the difference between the software and the money is disappearing.

The Administration for the Prevention of Money Laundering, as part of supervising the application of regulations in force regarding domestic banks, and related to the prevention of money laundering, particularly insists on the importance of constant improvement and specialization of employees and structural and technological equipment, which certainly affects the quality of analytics and recognizing potential risks. This secures handling quality and precise information about suspicious transactions, which is one of the preconditions for the establishing of a comprehensive system which would efficiently deal with the prevention of money laundering and financing of terrorism.

The Administration will continue to actively follow new trends in bank offers, as well as misuse of financial instruments of the banks worldwide and in Serbia, and will continue to exchange experiences with other financial and intelligence services at international seminars and conferences.



MONEY LAUNDERING TYPOLOGIES THROUGH THE EXCHANGE TRANSACTIONS

One of the ways to place “dirty” money into legal financial flows is through the exchange transactions.

However, money is not laundered directly through the exchange offices, instead they are used for disseminating of the “dirty” money, which is only part of the road to its legalization and entry into a country’s financial system. This “dirty” money may originate from corruption, narcotics trade, prostitution, human trafficking, arms trade, sale of goods in the black market, and many other criminal acts.

Black market existed in Serbia in the 90s, as very fertile grounds for all kinds of illegal activities. At that time, the exchange transactions were conducted by the street dealers who had large amounts of cash, without any proof of its origin. Namely, in that period, the foreign currency exchange rates on the streets were different than those in the banks, and the dealers made large profits based on the difference between those two rates.

The first years of the 21st century started with the introduction of the regulations for this part of the financial market, by adopting large number of regulations and laws. Exchange transactions can be performed by banks and licensed exchange offices, and the license for performing these operations in the Republic of Serbia are issued by the National Bank of Serbia. Until the adoption of the new Law on Foreign Currency Transactions, the National Bank of Serbia performed supervision over the work of the exchange offices.

In accordance with the existing legal regulations in Serbia, the exchange offices may only do business with the natural persons, in cash exclusively. Also, the exchange offices may perform payment transactions, domestic as well as foreign. For these reasons the risk of money laundering by means of the exchange offices is smaller than with other financial institutions, which does not mean that an exchange office cannot be used for the purpose of money laundering.

According to data from the National Bank of Serbia, there are 3,017 licensed exchange offices registered in Serbia today. A large majority of them are former street dealers who have legalized their business. It is not rare that the exchange offices are opened in order to facilitate the covering of the real origin of “dirty” money. Namely, an exchange transaction begins by depositing cash into the register of an exchange post, which is done exclusively by withdrawing cash from a current account of a licensed exchange office with a commercial bank. Depositing effective foreign currency into the cash register can be done solely by buying that money from a commercial bank. At the end of the working day, the money bought from the natural persons has to be returned to the exchange office’s current account with the bank. If there is a disproportion in the amount of money withdrawn at the beginning of day and deposited at the end of day, it is one of the signals that may indicate that the exchange office is doing illegal activities.

TYOLOGIES

Based on the experience of the Administration, several typologies of dissemination of “dirty” money through the exchange offices can be identified:

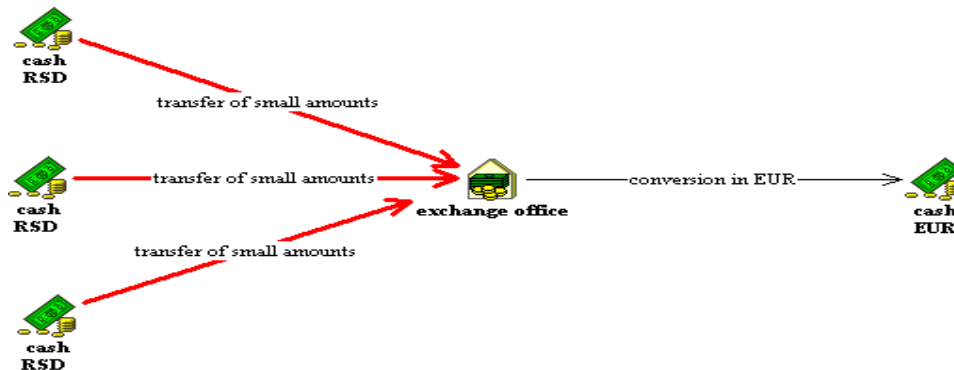
- **Conversion of large amounts of money**

There is a possibility that the money being converted originates from the organized crime. Namely, a natural person having a large amount of cash, originating from a certain criminal activity, will not go to a bank to deposit it, instead, the simplest way is to take the money into an exchange office and convert it into another currency. It is common that a person working in an exchange office does not even identify such clients.



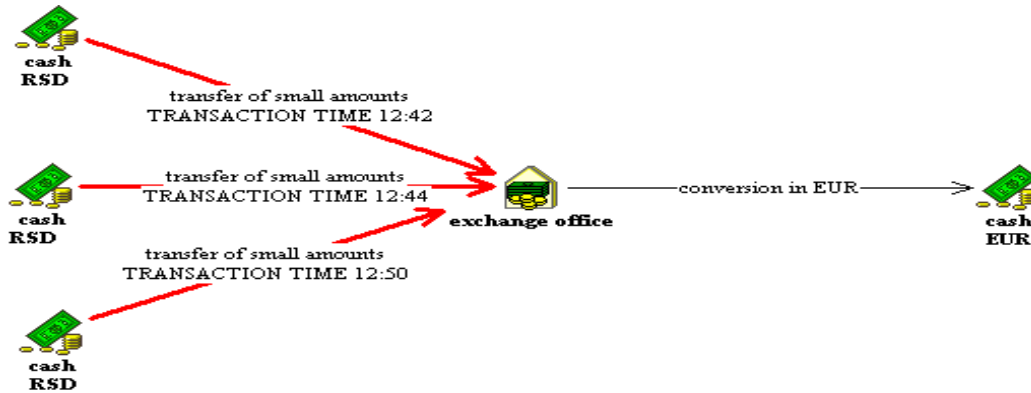
- **Conversion through several small cash transactions**

It has been noted that the exchange transactions of large amounts usually take place through several small transactions. The purpose of these transactions is to avoid reporting to the Administration for the Prevention of Money Laundering, and that is why the participants in these activities are careful not to pass the amount of **EUR 5,000.00** per transaction, the amount being the limit for reporting. A large number of individuals are often hired to perform transactions like these, accepting minimum provision from a person possessing money with suspicious origin. This process is known as “smurfing”.



- **Several transactions within a very short time period**

Some exchange offices will present having performed a large number of transactions in a very short time period, even if known that it is technically impossible. The purpose is to cover up the conversion of a large amount, showing it through a larger number of small transactions, however, the exact time presented for each transaction makes separate transactions impossible to have been performed.



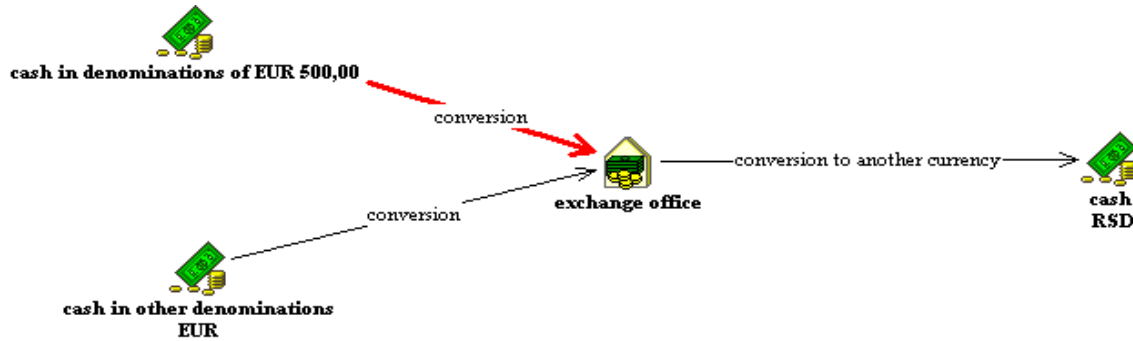
- **Conversion of funds from one foreign currency into another**

In order to perform this transaction in Serbia, the assets are first converted into dinars, and these dinars are then converted into a different foreign currency. These transactions are not economically justifiable, as the owner of the assets most often loses a certain amount, but for money launderers that is not of importance as their only goal is to hide the real origin of the assets by any means possible.



- **Conversion of money denominations linked with criminal acts**

Some states recommend to the exchange offices not to sell bank notes of EUR 500.00, as their usage is helpful for the organized crime. This bank note is favorite among the criminals, because large sums of money can be easily laundered through relatively small transactions, and large denominations make large sums of money convenient and simpler for transport, unlike small bank notes.



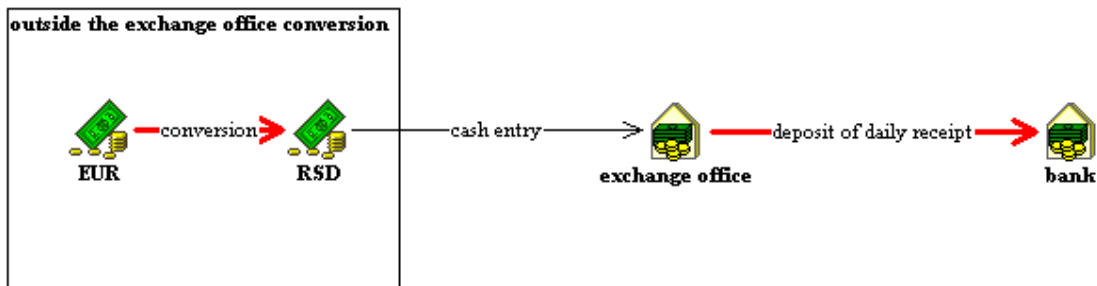
- **Conversion of marked bank notes**

When handling foreign bank notes, special attention should be given to marked bank notes, which may indicate a connection to persons involved in money laundering and financing of terrorism. These markings may not be always seen with the naked eye, as they are often inscribed using substances visible only under ultraviolet light.



- **Performing the exchange transactions outside the exchange office**

Some exchange office owners, or their employees, work in the field, i.e. outside their office, and these assets are later turned over to the bank as legally converted assets from the exchange office.



- **Conversion of damaged bank notes**

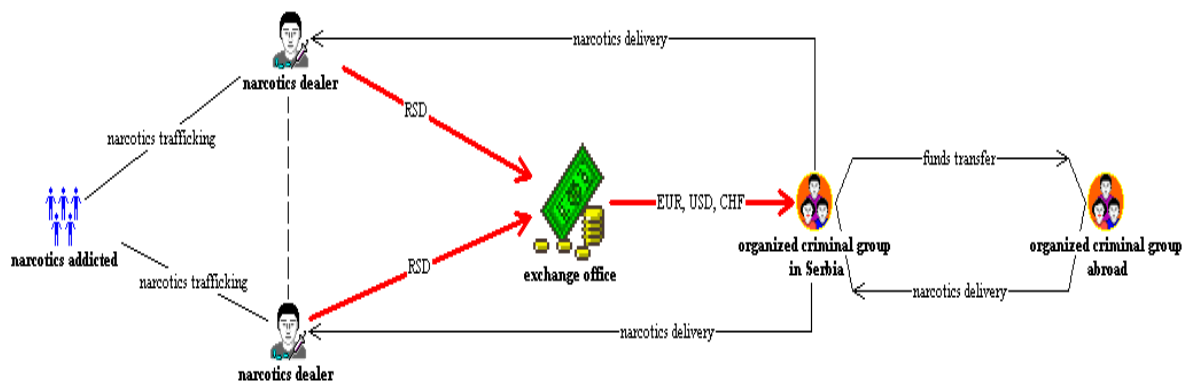
When being converted, the type and means of damage to bank notes must be watched out for, as they may come from a criminal activity. It may be that the bank notes have been deliberately damaged. Although these bank notes are exchanged by paying large commissions, the important thing is to hide their true origin.



EXAMPLE

An organized criminal group in Serbia deals with narcotics trade. Through several dealers, they sell narcotics to the natural persons throughout the country. The amount of money received from each individual sale of narcotics is not large, but it is frequent. In order to avoid rigorous control in the banks, the alternative ways are sought to convert money into a different currency and deliver it to its final destination, i.e. narcotics producers. Funds received from narcotics sale are taken to an exchange office and converted into foreign currency (EUR, USD, and CHF). Money is then transferred through different channels into another country, where narcotics are bought for further distribution in Serbia.

Note: As can be seen from the said example, an exchange transaction, i.e. conversion of funds from one currency to another, can play only one small part in the process of integration of illegally acquired money into legal flows of money. In this case, an exchange operation only makes it possible to hide the true origin of money through several small transactions, being one of the main **indicators** for recognizing the suspicious transactions in the exchange activities.



TRENDS

We may expect in the future that certain owners of exchange offices, which serve for the conversion of “dirty” money, will open several branches, in order to achieve greater layering of transactions of such cash.

Money launderers will tend to distant themselves from the banks, as these became the most organized sector when it comes to the prevention of money laundering and financing of terrorism, and turn towards the non-bank financial institutions such as the exchange offices and the companies for electronic money transfers.

Having in mind that this sector of the financial market is more and more legally regulated and given more and more attention through rigorous controls of the exchange posts, as well as through education of the employees, it should be expected that the suspicious transactions connected with money laundering and financing of terrorism will be recognized to the most possible extent, leading to the prevention of laundering of certain portions of “dirty” money,



which circulates in large amounts in every country and presents a serious threat to any national economy.

The trend of money laundering, which comes from organized crime, through the exchange offices, will continue. In what scope it will affect the exchange rates and demand for the most popular foreign currencies in Serbia (EUR, USD, and CHF) will depend on the monetary policy of the National Bank of Serbia, but also on the global economic crisis, which has influence on the economic and financial situation in the country.

MONEY LAUNDERING TYPOLOGIES BY THE ATTORNEYS OR LAW FIRMS

An attorney, as a person who knows the law well, should have the ability to solve problems or improve the interests of the person he represents, but that attorney must be socially responsible and his actions should prevent committing of the criminal offences. Some attorneys, in addition to knowing the laws, use all the ‘gaps’ in the laws so that, when doing business with the criminals, all these activities seem legal. It is also difficult to detect money laundering, due to the fact that the ‘launderers’ often use the people who have no criminal history, such as the attorneys.

More and more frequently, we can read the following news in the media: by the order of the Prosecutor’s Office for organized crime, several people have been arrested under suspicion that they were directly connected with the drug dealers. Among those who were arrested was an attorney, suspected to be a member of the organized crime group, whose task was to invest the money obtained from the criminal activities, by purchasing the companies in the process of privatization. Not a single member of the organized crime group has a real-estate or a company in their own name, the real-estate and the companies are owned by their relatives and attorneys.

How can the attorneys jeopardize the system for the prevention of money laundering and financing of terrorism? Is the code of ethics sufficient to prevent some attorneys from assisting the criminals in “laundering” of millions of dinars, dollars, and euro obtained from drug trafficking, arms trade or human trafficking? Each country must develop its own mechanism in order to disable the abuse of the attorneys and other tax payers for ‘laundering’ of illegally acquired assets.

In Serbia, as well as in the rest of the world, the attorneys and the law firms provide complete documentation necessary for a foundation up and registration of the companies, transfer of ownership title, opening of resident and non-resident accounts with the commercial banks and they are also authorized to dispose of the assets on these accounts. The attorneys appear as the participants in the transactions: as persons authorized to dispose of the assets on the accounts of the persons with criminal background or who are associated with drug trafficking or as persons who give orders to the banks to transfer the assets abroad, usually to pay the off-shore companies, and the payments are generally done based on fictitious documentation. The attorneys develop the payment scheme for the purpose of foundation of several off-shore companies, usually in the countries with strict banking secrecy policies, whereby the attorneys and the law firms provide the complete documentation on foundation of the companies, as well as the contracts based on which the payments are made. In the privatization process, the attorneys were involved in the acquisition of the companies, thus hiding the real owners of the capital. Despite the decision of the NBS (National Bank of Serbia) on the conditions and methods for the residents to hold foreign currency account in a bank abroad, according to which, they are not allowed to open personal accounts abroad, the large amounts are transferred from the attorneys’ overseas accounts to their local accounts from which they withdraw cash.

The development of the information technology has enabled foundation of the companies and control of the business from a “virtual office” via Internet, or foundation of the companies around the world, which has been especially simplified for the off-shore regions, dozens of

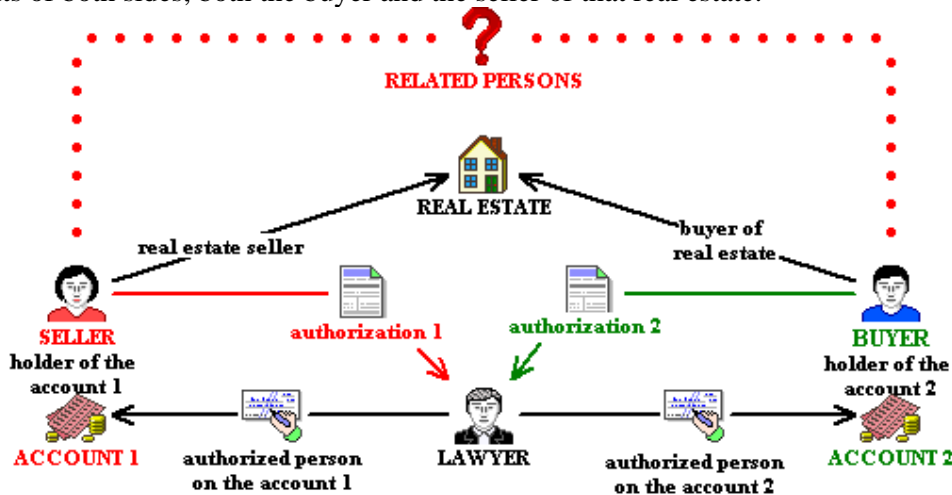
them around the world. There is a saying that every money “launderer’s” dream is to pay taxes, but the journey from “dirty money” to paying taxes is not easy or cheap. It is also a widespread belief that money cannot be “laundered” without an advice from the attorneys and accountants. There is a danger that a legal advisor, or an attorney participates in the activities of money laundering or financing of terrorism, in the instances where the advice is given to assist money laundering or financing of terrorism, undermines the very foundations of our society. On the other hand, if an attorney is aware that a client is seeking a legal advice for the purpose of money laundering or financing of terrorism and that the flow of “dirty money” would endanger the stability and the reputation of the financial sector and threaten the single market, the application of the Criminal Code is one of the efforts to protect the financial system. If the attorneys provide timely warning of their clients’ irregular or suspicious transactions and activities to the Administration for the Prevention of money laundering, that is the first step in the process of the prevention of money laundering activities, without the actual money but with the documentation (e.g., authorization given to an attorney to dispose of the assets on an account; contracts for purchase of real-estate or companies; Contract on foundation of a company in an off-shore destination; Contract on transfer of shares etc.), based on which certain financial transactions should be made.

Prevention of money laundering is not just about fighting the crime, but it is also an effort to preserve the integrity of the financial institutions and the financial system in general. The application of procedures, training of the attorneys and adequate supervision of the attorneys by the Bar Association can improve the system that is aimed to prevent money laundering and financing of terrorism.

TYPOLOGIES

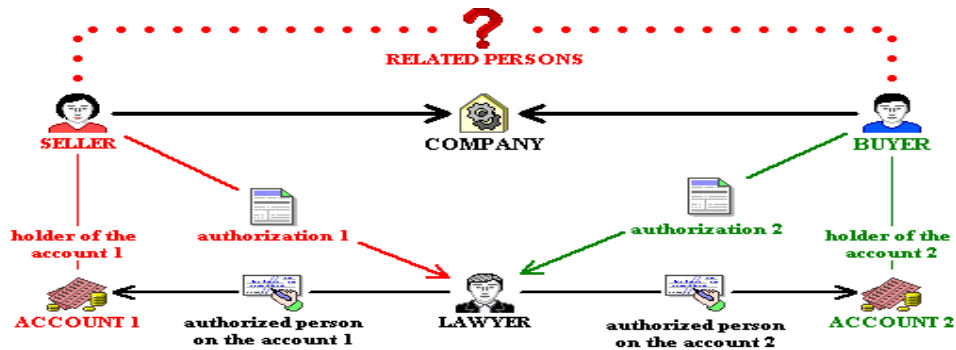
- **Purchase or sale of a real-estate**

An attorney assists his client in the matter of purchasing or selling of a real-estate – the same attorney acts as a representative and a person authorized to dispose of the assets on the accounts of both sides, both the buyer and the seller of that real estate.



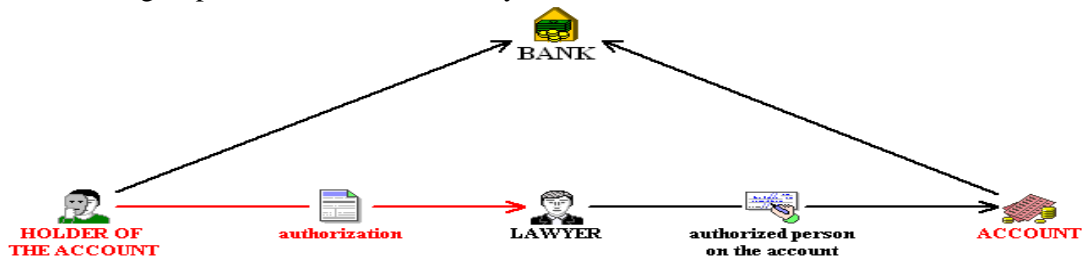
- **Sale or purchase of a company**

An attorney assists his client in the matter of purchasing or selling of a company – the same attorney acts as a representative and a person authorized to dispose of the assets on the accounts of both sides, both the buyer and the seller of that company.



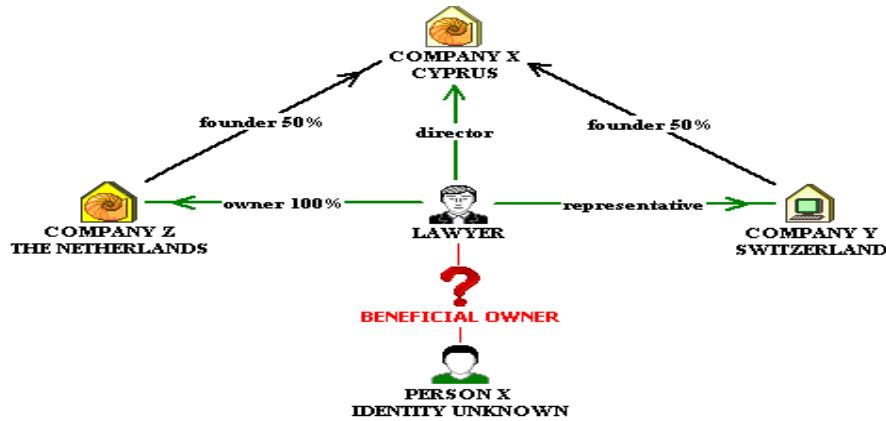
- **Planning and execution of the transactions by an attorney**

An attorney assists a client in planning and executing of the transactions regarding the opening or disposing of a bank account (bank account, savings deposit or account for operations with the securities) – the attorney appears as an authorized person for the account of a criminal group member and the attorney makes all the transactions on his behalf.



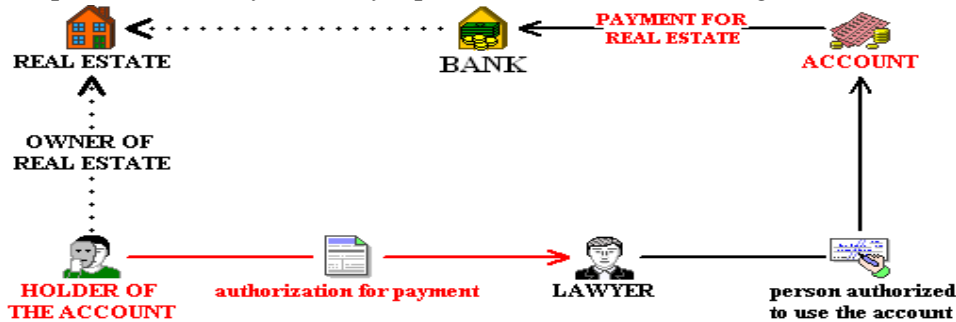
- **Assisting in business or management**

An attorney assists in business and management of a foreign company – the same attorney appears on different positions in different companies established worldwide (owner, agent or director).



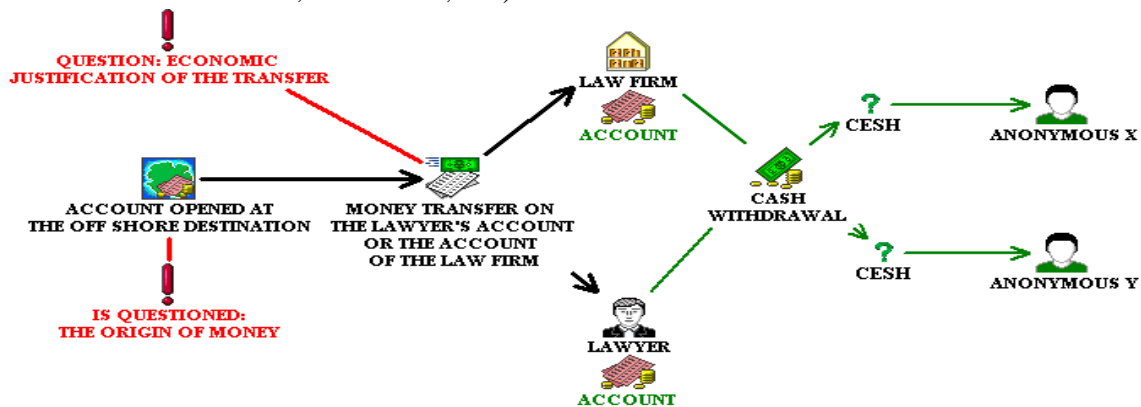
• **Performing financial transactions**

On behalf of a client, an attorney makes financial transactions related to the real-estate – based on a power of attorney issued by a person associated with an organized criminal group.



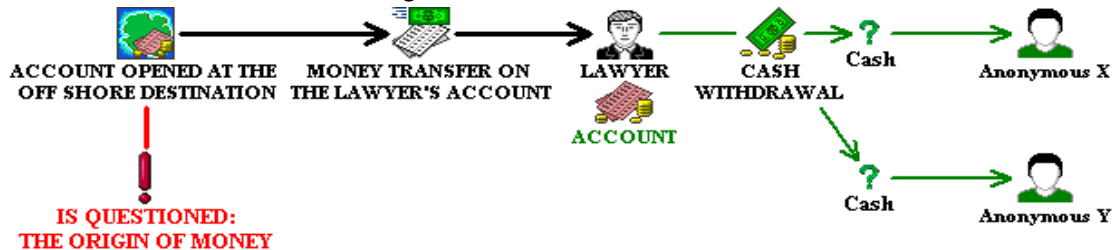
• **Using of attorney’s account or his firm’s account**

Using of attorney’s account or his firm’s account to transfer the assets without a clear economic basis – money transfer made to the attorney’s or firm’s accounts are suspected to come from the organized crime groups, without a clear economic basis (based on marketing or architectural services, inheritance, etc.)



- **Use of attorney’s personal accounts opened abroad**

Use of attorney’s personal accounts, opened in resident country and abroad, for money transfers which do not have a clear economic logic – transfer of funds goes from the personal accounts of the attorneys, opened in off-shore destinations, or in the countries with strict bank secrecy policy, to a personal account opened in a bank in Serbia. An attorney withdraws the assets in cash and hands it to its rightful owners.



EXAMPLE

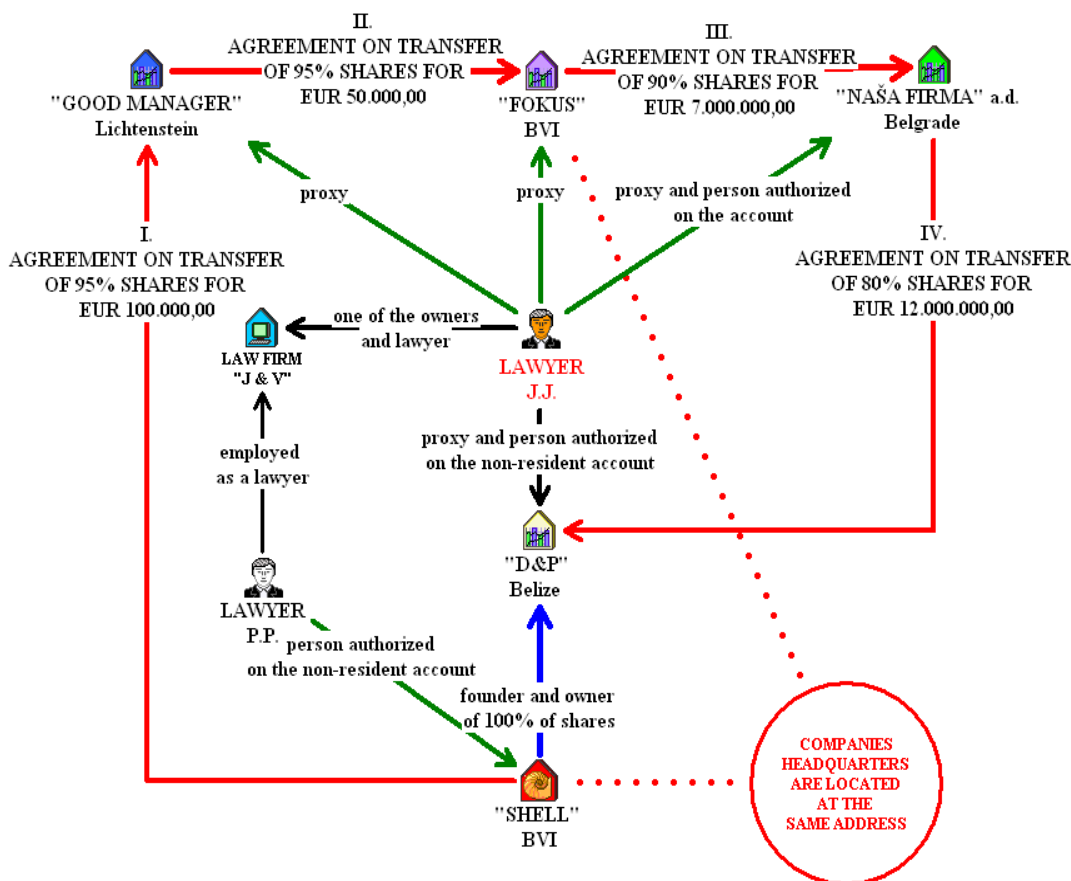
The off-shore companies are established, in order to transfer illegally acquired assets to Serbia, and they serve to disguise and integrate these resources into the payment system of the country. Within a short period of time of only few months, a fictitious sale of the company is done to associated entities at prices which have no economic logic. Persons who appear as the representatives of all the participants in transfer of shares in the companies, are also associated because they are employed by the same law firm.

Off-shore Company “Shell” BVI purchases 95 per cent stake in company “Good Manager” from Liechtenstein for 100.000,00 EUR. Few days later, company “Shell” BVI transfers its 95 per cent stake in company “Good Manager” from Liechtenstein to company “Fokus” BVI for the amount of 50.000,00 EUR, which after some time sells 90 per cent stake in company “Good Manager” for 7,000.000 EUR to a domestic company “Nasa firma”. Domestic company “Nasa firma” transfers 85 per cent stake to company “D&P” from Belize for 12,000.000.00 EUR. This way we can see that the increase in share value, which increased several times in a short period of time, was not conditioned by the market and it was not economically realistic. In fact, it is illegally acquired money inserted through off-shore companies into the payment system of the foreign countries, and then finally embedded in the payment system of our country.

The founder of off-shore company “D&P” from Belize is an off-shore company “Shell”, BVI with 100 per cent stake. In all of these transactions, the transfer of shares is done by local attorneys J.J. and P.P. who appear as the representatives, agents and persons authorized to dispose of the assets on the non-resident accounts. Attorney J.J. is one of the owners of a local law firm “J&V”. Companies “Focus” BVI and “Shell” BVI are seated at the same address. Obviously, these companies are associated by the ownership structure, as well as by the individuals or attorneys who are authorized to dispose of the assets on the accounts of the companies incorporated at an off-shore destination, which also applies to company “Nasa firma” a.d.

Indicators which raise suspicion of money laundering:

- A client signs or verifies contracts which are unusual or economical and business background does not justify this kind of contracting.
- A client makes real-estate transactions for natural persons and legal entities, residents and/or non-residents from the off-shore destinations or on behalf of the off-shore companies.
- Selling price of a real-estate set by a client is not in accordance with the market prices.
- Business relation is not in compliance with client's financial situation, i.e. his regular business operations.





TRENDS

The trend of purchasing of the companies, real-estate and land by the attorneys, law firms and persons without criminal records, with real owners of the assets hiding behind them, will continue. In these transactions, some attorneys will endeavor to introduce as many entities, natural persons or legal entities, which are usually established in off-shore destinations, with accounts opened in countries with strict bank policy of secrecy, and certain law firms which operate in few countries will act as the intermediaries. These attorneys will also be involved in the implementation of activities related to the purchase of property of bankrupt companies.

If we do not do something on a global level, which certainly cannot be expected in a near future, then the trend of founding of the companies in tax havens, opening non-resident accounts in the region and "managing dirty" funds from certain law firms, will be continued, which, due to new technological developments, will spend more time designing the entire money laundering scheme, than applying it through the transfers of newly established companies.

The loans will become more expensive but, nevertheless, it is likely that the trend of taking the loans with 100 per cent deposit and their early prepayment for purchase of a real-estate or companies will continue. The attorneys will continue to appear as the persons who participate in such transactions.

Transfers of the assets to the personal accounts of the attorneys or law firms, for various reasons, will continue in the future. This way, after cash withdrawal from the account, an attorney gives the money to the rightful owners, thus hiding the identity of the owner of the capital.

Completion of the privatization process will contribute to the reduction of criminal offences of money laundering, due to the reduction of the opportunities to invest "dirty" money in purchasing of the companies which are privatized. And there will still be a tendency of investing the "dirty" money in the purchase of agricultural land.

Liberalization of foreign trade and foreign exchange operations will also increase the risk of money laundering. As it becomes more difficult to integrate the assets acquired by criminal activities in regular financial flows, the attorneys will have to come up with a complete documentation covering the most complex transactions, which will include the companies founded in so-called "tax heavens", local companies, money transfer in or from the countries with strict bank secrecy policy, natural persons and transfers on various grounds (loans that companies take from companies abroad, marketing services, advance payment for goods and services, etc.).

MONEY LAUNDERING TYPOLOGIES IN THE ACCOUNTING SECTOR

All legal entities and entrepreneurs must keep accounting books, evaluate the value of the assets, revenues, expenditures, and prepare financial statements in accordance with legal regulations and international accounting standards. The financial statements imply the principles of completeness, including all accounting categories (assets, liabilities, own sources of revenue and expenditures).

The management and the accountants are responsible for preparation of the financial statements. Accountants employed in legal entities for which they prepare financial statements, are not the obligors pursuant to the Law on the Prevention of Money Laundering and Financing of Terrorism.

In case the legal entities or entrepreneurs hire other legal entities and entrepreneurs registered for the provision of accounting services and bookkeeping, they become obligors and are obliged to take measures and actions in accordance with the Law.

The accounting sector is very unique because it is present in all areas and sectors of the economy. All changes related to the company's business are recorded through its accounting. The task of accounting sector is to record these changes on the basis of accounting documents such as contracts, decisions, invoices. That is why the accounting sector is highly sensitive, because any manipulation and any attempt to conceal or distort the items in the accounts can result in serious consequences for the operations of that legal entity. All forms of commercial crime, including money laundering, corruption, tax evasion, investment fraud, etc., contain counterfeit documentation and fabrications of false financial statements. It is very difficult for an accountant to assess whether all the business documentation, which was submitted for entry, is false or regular, whether all the documents are submitted for entry, which is a basic requirement of international accounting standards. This includes general and integrated involvement of all elements of accounting categories in accounting management in order to prevent various abuses.

Engaging of the accounting sector is very attractive for potential money "launderers" because each accounting document that is given for entry, if formally valid, will be cleared regardless whether the transaction took place or not.

The abuses in accounting actually present a risk for objective financial reporting. Entry of false documents can be made through accounting (fraudulent income, false expenses, covering liabilities and expenses) which will lead to false financial statements. All of these crimes may precede money laundering, which can have consequences for the overall socio-economic system of a country.

The experiences of the Administration in dealing with cases of other governmental authorities (prosecutors and inspection bodies) show that the accounting sector was one of the key levers of criminal structures in some cases of money laundering, because after committing a fraud, it was necessary to make the accounting semblance of legality for the particular transaction.

TYPOLOGIES

- **Fictitious revenues**

Fictitious revenues imply lack of actual customers. Fictitious accounts are created for trade of goods and services, making their entry without inflow of assets on the account of that client. This way, the revenues are increased, which then results in an increase in profit not covered in the cash flows. The financial statements show the claims known to be uncollectible and that will be written-off in the future.

- **Selling of the products and services to affiliate entities at prices significantly higher than the market prices and calculation of unrealistically high interest**

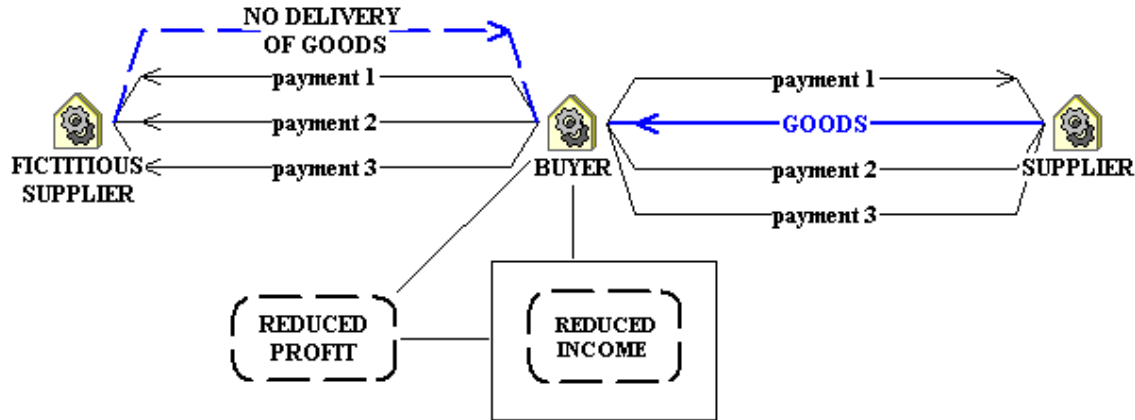
Invoices are issued to affiliate entities for the products and services at unrealistically high prices, which are significantly higher than the market prices, thus creating a false image of success of business entities. Increased revenues and profits are reported for all affiliates, which creates a false image of business success in the financial statements, and opens a possibility for participation in tenders for certain jobs or taking loans from commercial banks. This typology is most often used for the loans from the Development Fund, because it has the most favorable credit terms. As a rule, these firms, after taking the loan from the account in cash, quickly disappear or move to other legal jurisdictions (mostly in Kosovo) and the loans are never repaid.

- **Overestimation or decrease of net assets**

Depending on the needs and interests, it is often the case that companies overestimate or underestimate the net assets and operating results. In fact, they show false revenues, expenses, claims, and assets.

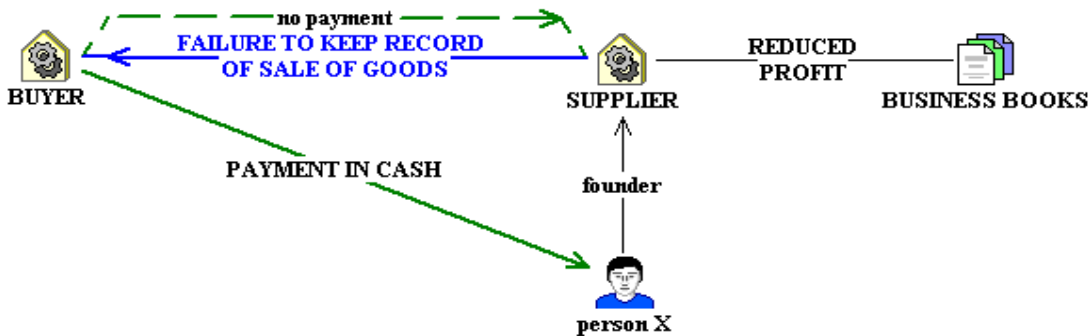
- **Multiple payments for the same product or service**

Payments are made several times for the same purchased product or performed service to the same or different vendor. In this case, cash flows do not coincide with the movement of goods and services, there is only a fictitious documentation.



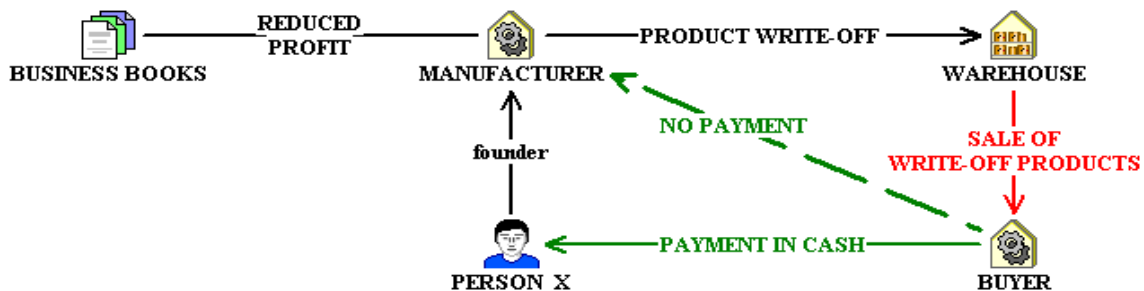
- Failure to log the business transactions

In such cases, there is a trade of goods and services, but these transactions are not logged in the books and there is no cash flows that accompany the transaction. This is how the cash is received, which is used for various illegal purposes.



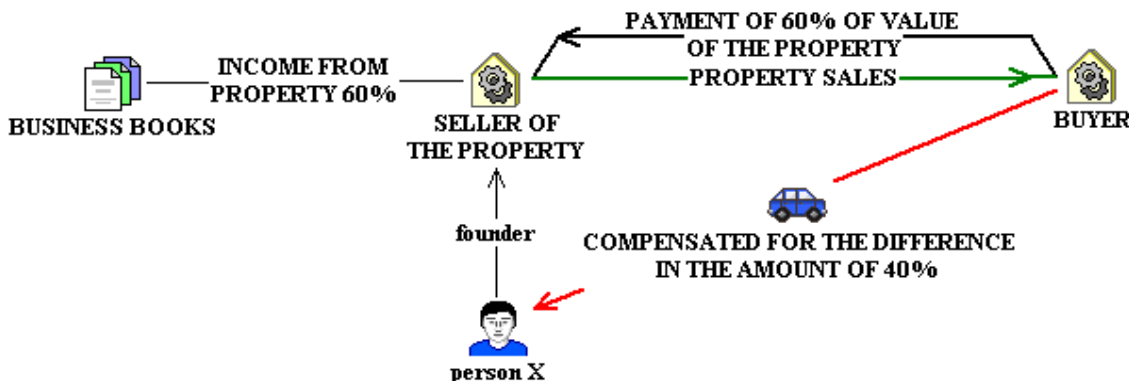
- Write-off of products

Due to a fictitious increase in expenditures by write-off of products as a result of various factors such as: force majeure, shortages which are the result of stealing, deterioration of products due to weather conditions, failure due to inadequate storage, breaking, causes an increase of expenditures, and reduction of revenue and profits. Goods that are written-off goods are sold for cash.



- **Sale of assets at prices substantially lower compared to the market prices**

In these cases, the difference is paid in cash or compensated by certain material goods such as consumable goods, artwork, jewelry, etc..



- **Increased invoices in foreign trade**

- **Import:** The goods from the foreign producers come directly to the customer in the country, but the invoice is issued by another firm, often from the off-shore destinations, increased for a certain amount. Usually an off-shore company is owned by local companies that are importers or the founders of both companies. Later on, the off-shore company appears as an investor in our country, investing the money paid based on over-invoicing, using the benefits offered by the State to foreign investors.

- **Exports:** The invoices with increased prices are issued for the goods exported to foreign countries, with an intention to insert illegally obtained assets into the payment system of the country. Illegal assets are legalized by mixing them with legal assets.

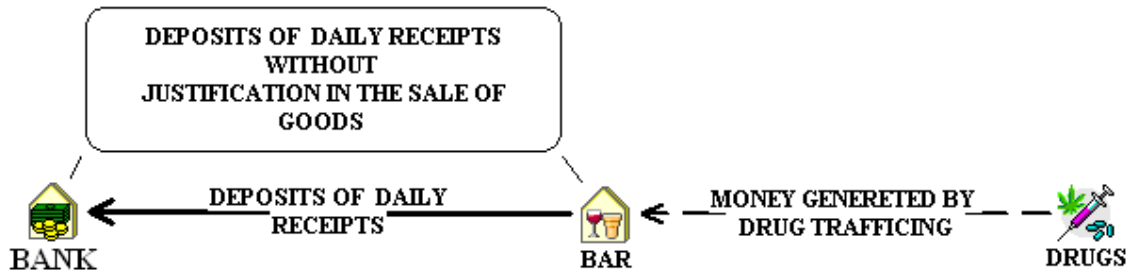
- **Services:** The services which were not performed are paid in accordance with the invoices, usually issued by the off-shore companies, to the non-resident accounts of those companies opened in neighboring countries. The cash is withdrawn, in the amount that is reduced for the commission it is returned to the owners of local companies, which paid this amount based on unperformed services.

- **Investing cash through the purchase of raw materials**

The cash coming from some illegal activity is not entered as cash input, but it is mixed with the legal capital in order to purchase the raw materials used for production. This method of mixing capital is particularly frequent in the construction industry, where the certain services are paid by illegally obtained cash.

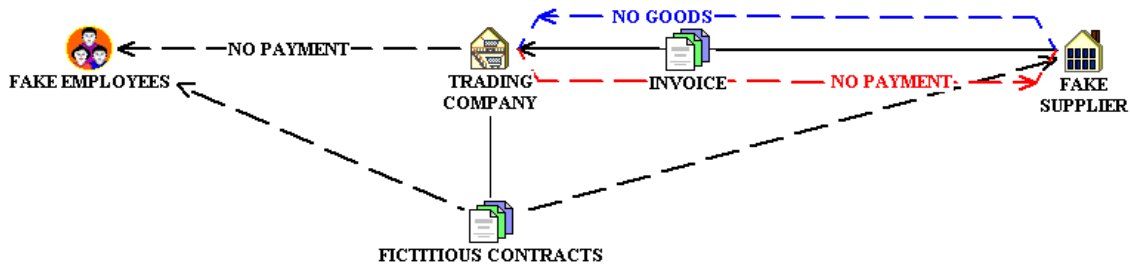
- **Recording cash payments which are not covered by the goods sold and services performed**

Illegal cash is paid through the retail market, restaurants, organizers of games of chance, casinos, businesses that pay flat taxes, without having the goods or services sold.



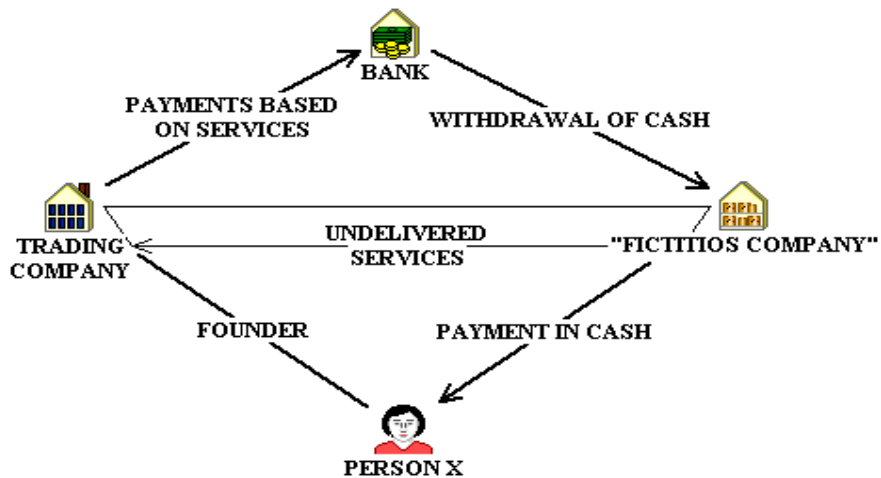
- **Creating false liabilities**

False liabilities are created by fraudulent procurement of goods, services and fictitious hiring of employees, which are not followed by cash payments, but they are just reported as false financial results through financial statements. This is how the expenditures and operating costs are increased, and the profit and liabilities towards the State are decreased.



- **Cash withdrawals from companies' accounts for fraudulent purchase of agricultural products and raw materials**

Some legal entities make payments based on invoiced services, which were never performed, on the accounts of the companies which were founded in order to operate for a short period of time. The money from these companies' accounts is withdrawn for the purchase of agricultural products and recyclable materials. False purchasing blocks are then established as a proof that the purchase was made. The cash, withdrawn for the purpose of repurchase is returned to business owners who made payments for the services, reduced for the amount of commission.



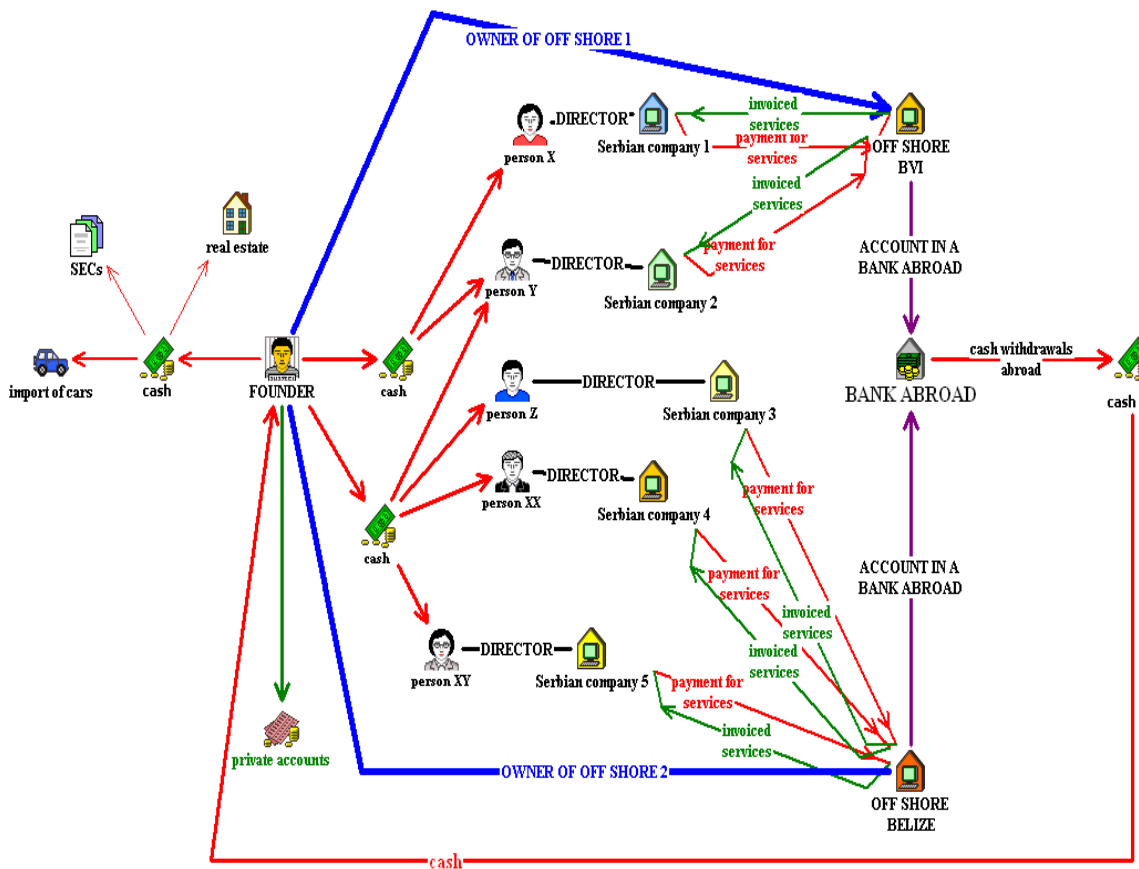
EXAMPLE

A founder of the off-shore companies contacts the owners and directors of certain legal entities, which are in need of cash for private purposes (purchase of real-estate, cars, securities, etc.). They agree that, based on the invoices which will be issued by the off-shore

companies, the payments will be made on their accounts for the services which will never be performed. The money from the companies' off-shore accounts is withdrawn in cash, in the amount reduced for the amount of commission, and it is paid to the companies' owners and managers.

Indicators leading to the suspicion:

- Procurement of services that have never been a part of company's business activities, without clear economic justification;
- Invoiced services, without a proof of execution.





TRENDS

The experience from the previous period shows that many of the “phantom” and regular companies were creating false documentation in a wide range of operations, with the help of some accountants, from mowing grass to the development of software and chips used in the airplane industry. This is why the accountants’ expertise and knowledge will be used by a potential “launderer” for the fabrication of false documentation, which is recorded in the transactions and creates a false image about performance of that legal entity, expressed through the financial statements.

Due to the real possibilities to use the accounting sector in order to cover the traces of the “dirty” money, this sector will continue to be attractive to potential money “launderers”. Some accountants will continue to perform the most useful tasks on behalf of their clients “launderers”, such as potential investment of illegally gained money or sheltering those assets out of reach to avoid future liabilities, financial transactions on behalf of a client in the field of payment transactions in the country and abroad, they will perform a currency conversion and conversion of property, purchase or sell the shares, advise the clients to avoid tax liabilities, and how to create fake revenues and expenditures.

Some accountants will be key designers for covering the traces of “dirty” money, which was obtained illegally, by multiple transfers of the money from one account to another, in order to detach it from its sources and at the end, to get an apparent legality.

One of the ways to create favorable ethical and professional climate within a legal entity is the adoption and controlled application of the ethical code of conduct and licensing of the accountants. Licensing of the accountants is a necessity, since only a licensed accountant can be liable for false entries which are not logical.

The increase in the number of abuses within the accounting sector is caused by a small number of detected criminal acts, mild punishment policy and unclear legislation, which is subject to a frequent change. Thus, in the period from 2001 to 2009, the Excise Tax Act was amended thirty-nine times. Only certain criminal acts are being prosecuted, and even when cases reach the court, the proceedings take a long time and, for a considerable number of criminal cases, a statute of limitation applies.

MONEY LAUNDERING TYPOLOGY IN THE AUDITING SECTOR

Legal entities that have the status of medium size and large enterprises are under obligation to have their financial statements audited at least once a year, in order to provide objective evidence that the financial statements impartially represent the results of legal entity's operations in all significant aspects.

Financial statements are prepared by the client, and not the auditor, who, on behalf of a client, gives an opinion, therefore, the financial statements are the responsibility of the management, not the auditors. The auditor should show special attention, which is expected from him as a professional person, and he bears a legal responsibility for his auditing and opinion.

Since the audit is expected to become an instrument for increasing the security of information used by decision makers, the audit becomes one of the indispensable tools to detect and prevent errors and frauds.

Modern financial flows are characterized by a large number of transactions, rapidly performed using computer technology and the reduced use of cash and paper documents. Criminal offence in the financial statements are the constant companions of the auditing practice in terms of responsibilities of auditors to detect those offences. Given that the independent auditing is done based on a sample, one cannot expect auditors to detect all cases of non-compliance. His professionalism, knowledge, experience and awareness of client's business can provide a good basis for identifying specific actions and activities that are inconsistent with the Law.

The auditor has a legal responsibility for the detection of non-compliance of legal entities and accountants in preparing of the financial statements and accountability for incorrect opinions expressed in the financial statements.

Money laundering typologies associated with auditing and accounting are exactly the same (see accountants), with the difference that the accounting sector is used to cover up criminal activities and attempt to validate those actions through financial statements, and the task of auditing is to detect the cases of manipulation of accounts in order to show better or worse business results, which are the result of criminal activity.

A criminal offence is rarely immediately and fully disclosed as a single unit composed of connected transactions, supported by the documentation. It is hidden and its detection and understanding, in most cases is hard. It can be compared with a mosaic or a puzzle of certain images.

The role of the auditing process to detect the abuse in the economy is diminished because of the possibility to cancel the audit, and hire a different independent auditing firm, paid by the client. Since the client pays the auditor, and conducting of an audit of financial statements requires close cooperation with the management, it is clear that complete independence of the auditors is not feasible. The connection between an auditor and a client is therefore sensitive

and complicated, so unlike the audit, other service industries are almost exclusively in obligation only toward the clients. The situation of auditing is further complicated by the existence of three opposing parties as follows: auditors (auditing firm), managers and owners of capital as the users of auditors' opinions.

In the practice of auditing, certain influences are possible, so it is possible to doubt the objectivity of the auditor's opinion.

These influences may include:

- **Pressures**

The pressures that may affect auditor's independent position come from various activities, relationships and circumstances that may affect the impartiality of the audit.

- **Qualifications of the auditors**

Incompetent or less competent auditor is willing to accept others' opinions.

- **Conflict of interest**

The auditor may be in a position to review the financial statements of a client, which he also assists in managing of financial activities.

- **Non-audit revenues**

Recently, there has been an increase of participation of not-audit revenues from non-audit services in the revenue structure of auditing firms. It cannot be expected from an auditor to disclose the errors and irregularities, which have occurred during the performance of his non-audit services.

- **The existence of close relationships from the previous period**

Auditor's transition to a position in the company he was performing audit for may have a negative impact on independence of the future audits.

- **Family and personal relations**

When a close relative, spouse, children, parents work in the accounting and financial sectors, it can be expected that the auditor's report and opinion will not be impartial.

- **Client has a significant share in the revenue structure of an auditing firm**

If the auditor has its share in the revenues structure of an audit firm, direct or indirect blackmails could be expected that might compromise the independence of the audit.

- **Auditor has a financial interest in the company where he performs an audit**

The auditor who owns shares (joint stock company), has no interest in expressing an objective view of the financial position of the company.

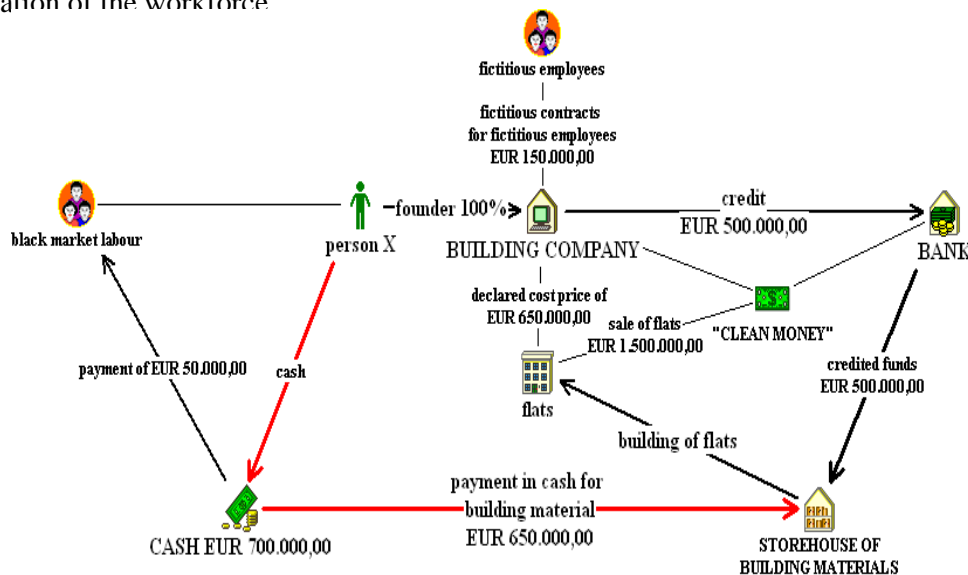
- **Intimidation**

Threats made by the management and the employees of the client of an audit, may affect the auditor's report and opinion.

EXAMPLE

Owner of a construction company has a certain amount of illegally obtained cash. In order to, at least ostensibly, legalize that money, he is procuring building materials, paying one part in cash from illegally acquired assets, and the other part he pays with the money from the loan, which he took from a commercial bank. The loan was secured with a 100% deposit, also by illegally acquired assets. In the bookkeeping reports, the owner of the company justifies his obligations to fictitious employees based on the employees' salaries, taxes and contributions. Essentially, salaries are paid from illegally acquired cash, without taxes and contributions. He registers the cost of procurement of construction materials in the accounting books only in part of non-cash transactions, which were paid from the loan proceeds. Built residential units are sold at market prices, and thus, the illegal assets are legalized.

- Indicators leading to a suspicion:
- Entry of changes on the basis of non-credible documentation
- Confirmations of receipt of raw materials are kept separate and are not connected with incoming invoices
- Great fluctuation of the workforce



MONEY LAUNDERING TYPOLOGIES ON THE CAPITAL MARKET

The capital market in the Republic of Serbia is “relatively young”, since serious trade, based on recognized standards for securities trading, started in 2001, with introduction of new legal provisions, which included development of new rules which did not apply before that time. Thus, the intermediaries (broker- dealer companies) got a new and more important role in the securities trading on the stock market and on over the counter market.

The main characteristic of the Serbian capital market is that the securities’ trading is performed in the conditions of shallow and undeveloped market, asymmetry of information and low level of corporate culture. Another proof of this is the fact that there are only few companies listed on Belgrade stock-exchange, and many companies are listed “by the force of law”, and those are mostly the companies which were privatized in the recent period.

The success achieved by the capital market, and primarily continuous increase of turnover at Belgrade Stock Exchange and rapid increase of the value of shares until mid 2007 is behind us, due to global financial crisis which started in the second half of the same year. The crisis cause rapid and significant decrease of the scope of trading on the Stock Exchange, which caused the decrease of the value of shares index.

Objectively speaking, the capital market has been decreasing in the last four years and there are no signs of fast recovery. The market is not solvent and there is no significant interest in securities trading by domestic and foreign investors.

Although it is undeveloped and “inactive”, the capital market has not been immune to money laundering and attempts of money laundering, and the Administration recorded certain examples of cash flow on the capital market, which point out to money laundering or at least the attempts of money laundering.

- **Sensitivity and vulnerability of the capital market to the threats of money laundering**

Before we describe the experiences in fight against money laundering and the trends which were noticeable on the capital market, we can give a brief explanation as to why the capital market in Serbia was a channel and provided great potentials for the attempts of money laundering.

These are some of the main reasons of the “vulnerability” of the capital market:

- A new developing sector for investing of free capital has been provided, and it has been eagerly accepted by the owners of illegally acquired capital who use it to place it in the legal flows;
- Money “launderers” like complex techniques and numerous opportunities for placement of the capital, and investment in the securities has provided layered hiding and more difficult identification of the cash flow;
- The development of the capital market was, and still is accompanied by the fact that broad public is mainly uneducated in relation to the participation in the ownership of companies as shareholders. The development of culture and rising



of the awareness are ongoing, and the first signs of progress are noticeable. Such environment and atmosphere are suitable for the criminals, since they provide them with wider space for the maneuver, because a limited number of people understands “what they do” and “how they launder the money“;

- If we observe the history of the development of the capital market in the Republic of Serbia, we can conclude that our “shareholding” was voluntary and unplanned (distribution of free shares to the employees starting from 2001). Later on, in most cases, those same small “insolvent shareholders” were “recruited” and manipulated to sell their shares for, almost always, cash reimbursements. Very quickly, the “dirty” capital recognized its target group.
- The level of knowledge of investigative bodies that fight against organized crime on the capital market is not sufficient. There is still an issue of the quality of their education, as well as their capabilities to fight quickly and efficiently against the criminal and money “launderers”, and the criminals are aware of it, and that has encouraged them to use the capital market as one of the sectors in their money laundering strategy.
- It is also important to say the Securities Commission, as a regulatory body for the capital market, has not had required legal independence, and efficient monitoring (control) which would give it an automatic right of efficient action in prevention of irregular and unpermitted actions.
- Criminals (money “launderers“) have recognized the capital market as an excellent and complex channel to efficiently integrate “dirty” money and thus legalize their activities by purchasing and obtaining solvent and healthy market joint stock companies, as one of the most significant motives for the placement of illegal cash. The legal provisions directed them to the capital market (Law on Takeover of Joint Stock Companies).

The experiences of the Administration in the period from 2002 to 2010, in relation to the attempts of money laundering can be grouped as the following suspicious activities on the capital market:

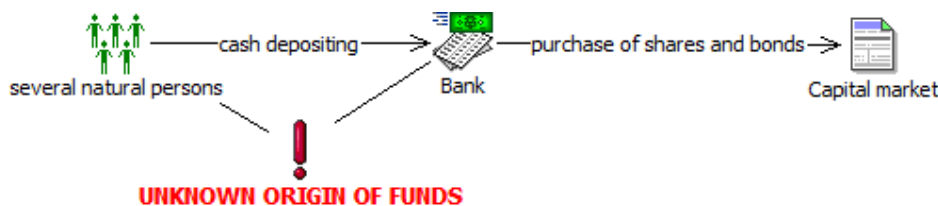
- Dematerialization of bonds on behalf of the bearers (bonds for the development of the Republic of Serbia – initial owners of the bonds were paid in cash by the following bearers and future owners of electronic bonds);
- Purchase of the old foreign currency savings bonds for cash placed on special purpose accounts in the banks. Apart from the revenue, another advantage of this purchase was the possibility to take part in the auctions for the purchase of the companies pursuant to the Law on Privatization;
- Over the counter trade (purchase) of the old foreign currency savings for cash payments to the clients by the investors;
- Purchase of the securities for cash placed on the current accounts and savings accounts without interest, opened in the banks (layering on the special purpose accounts);
- Purchase of the shares by authorized persons (attorneys) by small shareholders for cash and processing of the shares through the stock market in favor of the issuers of authorizations (real investors) – transfer of securities;

- Issuing the shares as lien for short-term borrowing paid in cash, and then “sliding” it through the Stock Exchange and purchase of the same shares in Block trade (transfer in favor of the issuers of the borrowing);
- Disposal of the shares of small shareholders by giving shares as a present to the directors “saviors” of the companies without any type of official reimbursement, although in reality the money is given directly to small shareholders;
- Purchase and selling of the shares high on the list by very young investors within a short period of time, but in high amounts;
- Purchase and selling of the shares high on the list by natural persons who frequently and quickly change the banks for opening of special purpose accounts, where they place the cash for purchase of the securities, and afterwards they withdraw quickly from the market;
- Investors – off-shore companies with unknown ownership structure and capital who take part in takeover of Serbian companies by purchasing of control packages of shares;
- “cover persons“ – purchase of control package of shares by insolvent investor in favor of other natural persons – real investors with criminal records. (so called “selling of the biography for financial percentage “)²
- Purchase of the securities and portfolio formation by the persons who are prosecuted for different crimes in the field of commercial and organized crime;
- Offers for takeover of the companies (control package of shares) by newly founded (just registered companies) or natural persons who are not solvent for such undertakings (cover persons for the real investors)
- Specific trading – FOP transactions (transfer of securities), money “launderers” are particularly drawn to the gifts in form of securities, lien and share in joint stock companies for the foundation of new limited liability companies (LTD) in order to, subsequently, sell the same shares (stake in LTD) without firm business reasons.

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- **Unknown origin of money on special purpose accounts.**

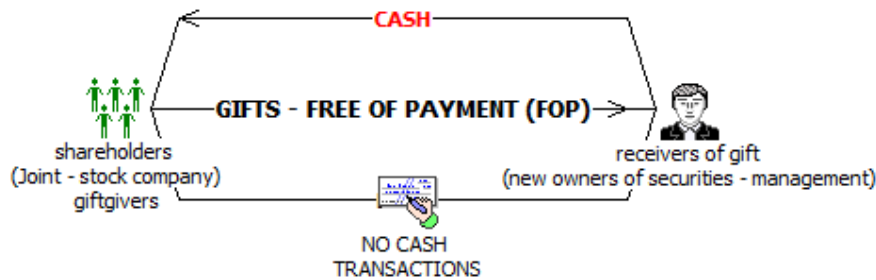
Depositing money of unknown origin to special purpose (financial) accounts for the purchase of securities;



² Young investor with university degree, respected and without criminal background, acts on behalf of the persons involved in criminal activities when trading procedure requires fulfillment of certain legal prerequisites (e.g. when one of the prerequisites is that the participant has not been registered in the criminal records of the relevant institutions within previous six months). The investor accepts this type of substitute for certain financial reimbursement or commission. This case is known in practice as “selling of biography“

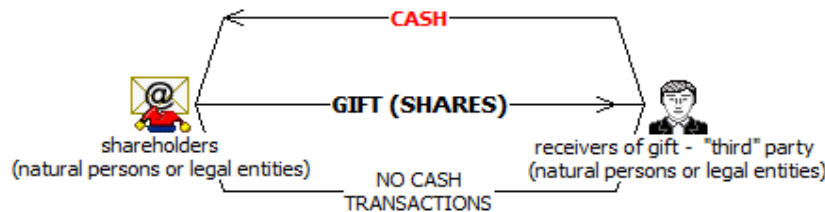
- **Transfer of securities to the benefit of managers**

Gifts in securities from small shareholders to the benefit of their managers, with suspicion that they are being paid in cash (transfer of securities);



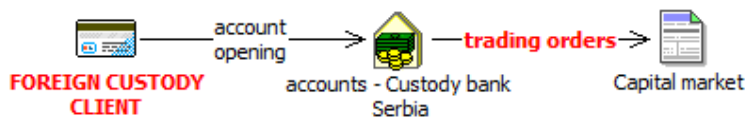
- **Transfer of securities to the benefit of third parties**

Transfer of securities in the form of gifts, where securities are given to third parties or legal entities;



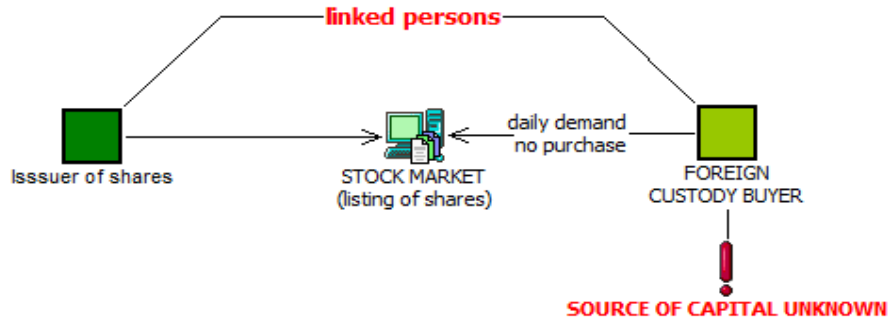
- **Custody accounts**

Trading securities through custody accounts for which it is hard to determine and identify the actual client, especially relating to clients “hiding” behind foreign custody banks and accounts;



- **Raising the indicative price**

Simulated (i.e. through linked persons) and frequent (everyday) raising of the indicative price of shares (fictitious demand) by the custody buyers, which takes place without trade (purchase), with the intention to “enormously” increase the share price, in order to introduce the capital with suspicious origin;



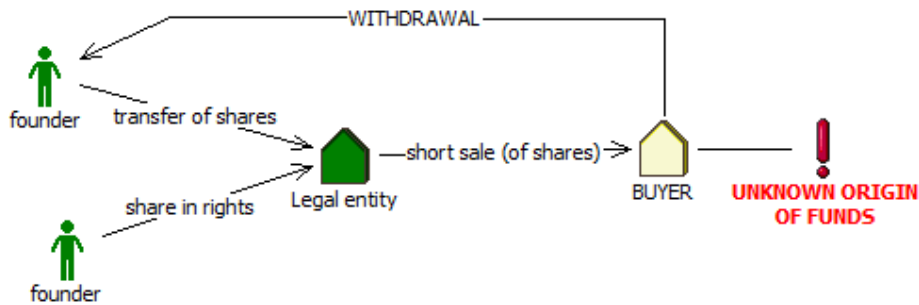
• **Taking over companies**

Taking over companies (joint stock companies) – bids for buying shares submitted by recently registered companies or companies that do not have financial capacity (solvency);



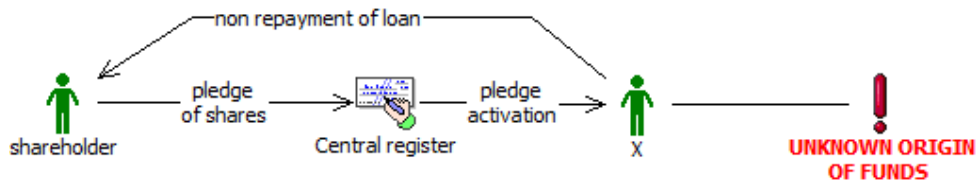
• **Founding capital in form of shares**

Introduction of shares as founding capital in rights in a newly registered legal entity, followed by swift sale of shares (stock) to legal entities and natural persons, suspected to be performing illegal business activities.



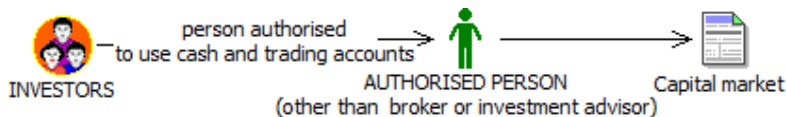
• **Pledged shares**

Transfer of shares that were pledged as security on the basis of approved short-term cash loans, for which it is hard to determine the origin of money.



• **Trade by unknown investors through authorized persons**

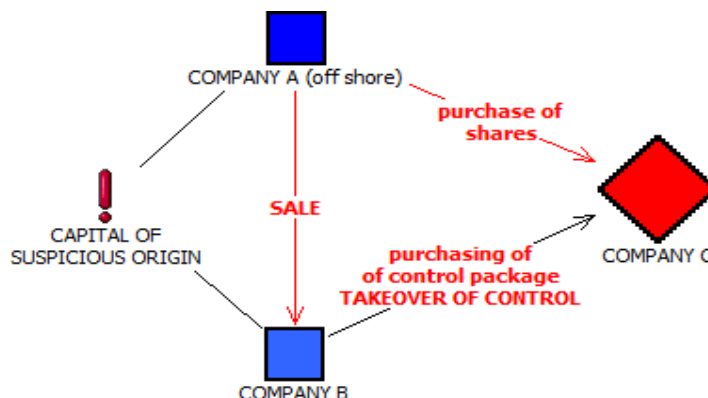
Unknown investors trading securities through authorized persons (usually not qualified brokers or investment advisors), who are given broad powers in managing of the portfolio and trusted funds, and whose origin is difficult to identify.



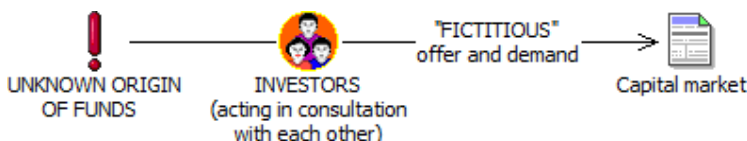
• **Manipulations in the capital market**

Attempts by the investors, whose money is suspected to be coming from illegal activities, to place, layer and integrate “dirty” money through different illicit activities – **manipulations** – in the capital market, where special attention should be turned to the following occurrences:

- simulated and connected activity of multiple investors with disputable personal and business reputations (connected persons, where it is hard to identify the real owners of legal entities) in forming an unrealistic market price of a share of the targeted joint stock company, with the obvious intention to later take over that targeted joint stock company;



- occurrences in the form of “deceiving” the capital market – transactions or trading orders using fictitious procedures, as well as any other forms of deceit or fraud where a person, or more persons acting together, maintain the price of securities on an unrealistic or artificial level, especially relating to the persons reputed as suspicious investors or suspicion in the origin of the investment capital.



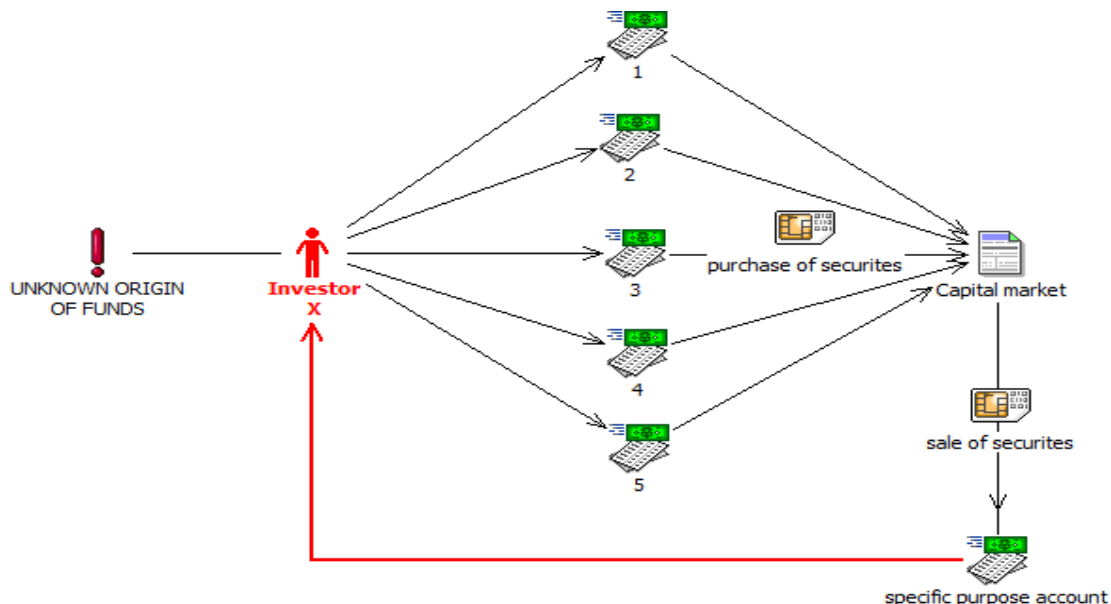
EXAMPLE

Case description: Natural Person X deposits assets on special purpose accounts for purchase of securities with five different banks in a short period of time. Investor X is relatively young, age 28, without permanent employment and regular income. He deposits money on special purpose accounts in a calculated manner, below the legal minimum for reporting, in the amounts ranging from EUR 10,000 to EUR 14,000. Within one month the Investor has made a total of 32 cash deposits. Immediately after these deposits, through an agent – a broker-dealer company – Investor X purchases very liquid shares (shares subject to constant offer and demand), day after day. Very shortly after the purchase, the Investor sells the portfolio of these shares, although their price keeps growing day by day, on the capital market, making a significant profit. The profit from selling shares is then transferred by X to his newly opened special purpose account, from which he then successively withdraws the assets.

The Administration has taken the actions and measures according to its competence and, after gathering additional documentation, forwarded the case to the relevant authorities. It was established that the person was associated with criminal groups.

Numerous **indicators** of suspected money laundering can be recognized in this case:

- relatively young investor without permanent employment and regular income (cover person),
- quick sale of shares immediately after purchase, although the share value keeps rising,
- transactions that are interconnected (32 transactions in the period of one month),
- successive cash deposits on the accounts below the legal maximum,
- each special purpose account opened with a different bank.



TRENDS

Based on the present analysis of the capital market, we cannot foresee an increased offer of additional emissions of shares or creation of joint stock companies through public emission of shares.

What can be expected in the following period is the dominance of foreign investors. They have already dominated in the domestic capital market in the past period, and have had a significant influence on the index value of the Belgrade Stock Exchange. From the money laundering aspect, various investment funds seated in off-shore destinations will be of particular significance, and their activities will be regularly followed.

In case of an attempt of reviving the market through the emission of corporate (company) bonds and local administration bonds, as well as emission of securities issued by the state, we may expect increased investor activity, together with the introduction of suspicious capital.

In the context of fight against money laundering, as a new feature, it is important to stress that, in accordance with the new Law on Capital Market, obligors – broker-dealer companies may handle their clients' money on their accounts with a credit institution (bank). This will additionally oblige them to get to know and follow their clients and their sources of assets better.

It remains to be seen in the following period whether new financial instruments (financial derivatives – futures, options) will make their way into the Serbian capital market. They will surely lead to the increased interest of money launderers to enter new markets. Even more so if those markets are poorly regulated. Regulatory authorities, as well as good preventive actions, can contribute to averting the introduction of “dirty” capital, and their role will increase.

According to the previous experience on one hand and the global trends on the other, the increase of the following activities may be expected in the future:

- introduction of shares as a stake for foundation of new companies, and sale of this stake (shares) to persons whose capital has suspicious origin;
Takeover of the joint stock companies and introduction of shares for the purpose of foundation of new companies (foundation stake in limited liability companies) which are later sold, mostly at much higher prices, to the buyers with the capital of suspicious origin. This way, transparency of the market is skillfully avoided, more precisely, regularity of shares trading on an organized market (on and off the stock exchange) is avoided.
- massive gifts in shares of the employees of the mother company to their managers or third persons, for compensation in cash;
The existing trend – transfer of securities as gifts from small shareholders to their managers, for compensation in cash, should decrease, as this form of transfer of shares has mostly been completed, but it will surely not be eradicated completely.



- high-value shares as gifts to third persons
On the other hand, gifts in shares between unrelated persons, where there are no payment transactions still leave a space for doubt (debt settlement, transfer on the basis of bank guarantees, fictitious transfers for the purpose of money laundering through cash payments to the benefit of former owners of securities), and are expected to increase in the future.
- Investors on the capital market whose coverage of the assets on the accounts originates from cash (cash deposits)
What has always been and will remain a trend is the problem with investors in securities – natural persons, with suspicion in the origin of their money that has been deposited in cash to their accounts.
- off-shore investors (off-shore funds, in particular), whose ultimate owner is difficult to identify;
Doubts will remain in the following period regarding investors from the off-shore zones, because of impeded and, in certain cases, impossible identification of the real owners and the origin of money. Special threat is posed by the investors coming from the areas with data protection (banking secrecy and tax deductions)
- investors hiding behind custody accounts, whose identity is unknown;
One form of skilled and hidden money laundering which will remain is the case of active trade in securities through custody accounts, with a special emphasis on the group of clients standing behind accounts with foreign custody banks that strictly apply the principle of professional secrecy.

Various techniques of manipulating the capital market can still be expected, with the goal to activate “dirty” capital, like, for example, connected activities of multiple investors in order to acquire or transfer certain target shares, or counterfeit fictitious trade in shares for the purpose of “playing the market”.³

In case of the innovations on the capital market, in form of new financial instruments, introduction of “dirty” capital may also be expected, as it creates a new opportunity for money launderers to transfer their illegally acquired money. For these reasons it is important to uphold the regulations in the sense of protection of the capital market and the investors.

³ In situations when the recorded volume of trade in securities on the market is not large, without big changes and oscillations, as is the case in Serbia, for the purpose of facilitating the placement of dirty money, multiple connected investors give day-by-day orders for trading of shares, thus creating fictitious demand and an appearance of activity on the market. This situation is known in practice as “playing the market”.

TYPOLOGIES OF MONEY LAUNDERING IN THE INSURANCE SECTOR

Generally speaking, the insurance market in the Republic of Serbia is not “hit” by money laundering, i.e. placing illegally acquired money for the purchase of life insurance policies.

The insurance industry is a branch of the financial industry, which has been increasingly developing in Serbia, and will probably attract more and more new clients in the future with the development of new products and diverse offer of services.

It should be noted, that we are primarily concerned with business activities related to life insurance, because this form of insurance is under constant eye of the Administration for the Prevention of Money Laundering in the fight against money laundering.

During the 1990s, insurance as a commercial activity and life insurance in particular almost completely faded. Only in 2004, with the adoption of the new law, with its subsequent amendments in the following year, this area was regulated in accordance with the developed and organized countries of the Western Europe. Accordingly, foreign insurance companies recognized their opportunity in the new market and have, along with few domestic companies, significantly induced the development of life insurance.

It has to be stressed that foreign insurers significantly dominate the market in Serbia. Also, the state strongly supports this branch of the financial industry, not surprisingly, since it deals with collection of important free assets of citizens and securing of their future.

By comparing the participation of life insurance in the country’s GDP, Serbia with 0.3 per cent is significantly behind the developed countries (with participation of up to 10 per cent). According to the capital value, the total insurance premium for the year 2010 equaled 536 million EUR, putting insurance by capital value of its portfolio behind leasing, banks and the capital market. Out of 536 million EUR only 16.5 per cent related to life insurance premiums, being completely different from developed countries where the life insurance premium participates with over 50 per cent in comparison to non-life premiums.

When discussing past experience in the work of the Administration relating to life insurance business activities, it has been noticed that life insurance policies are mostly sold for a longer time period and with an average yearly premium below 1,000.00 EUR. The presence of one-piece premium deposits is not significant.

With such structure of issued policies, it may be concluded that money launderers do not have big interest in depositing money by purchasing policies and “disseminating” that money for years.

However, that does not exclude the possibility for the industry to become an attractive sector for “dirty” money and money laundering channels.

The insurance sector is traditionally viewed as a low-sensitivity industry with regards to money laundering, compared to the banking sector which was and remained the primary path for money laundering and legalization of illegally acquired money.



It must be particularly pointed out that life insurance is not the primary channel for money laundering, but reports and statements from insurance companies (as obligors) are very important, because they have directly led to the persons connected with criminal offences and pointed out, through further analysis, to a criminal offence of money laundering.

The analyses and performed surveys of the Administration show far larger danger of money being laundered through the sector of non-life insurance, as the risks the insurers are exposed to when it comes to fraud are larger, and there is a big probability of “dirty” money being behind it (fictitious insurance and deliberate arson, fake car crashes etc.) The value of deposited premiums in non-life insurance by far surpasses the value of deposited premiums in life insurance.

There are certain characteristics of the insurance industry making it attractive to criminals, and those are:

- lack of what is usually called “good or particular attention” of representatives and agents, not recognizing which insurance products are especially interesting for money laundering, as well as failing to identify transactions that lead to money laundering, are all result of poor knowledge of obligors about money laundering through insurance;
- prevalent focus of insurance companies on fraud and compensation paid on the basis of acts of fraud (arson, theft...);
- possibility of investments and savings (many products with elements of both investments and savings – policies with depository possibilities (collateral) – are used as guarantees for obtaining loans and purchasing of real -estate);
- cash deposits that are especially encouraged in situations when the premiums are used as savings or pension stimulus;
- role of intermediaries (brokers, agents, representatives).

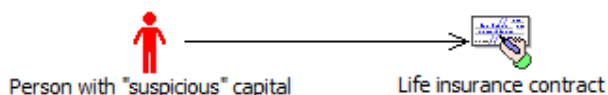
Taking into account the experience in the work of the Administration in the period from 2002-2011, and subliming the situation in the life insurance market along with the business policies of insurance companies designed to attract clients, the following activities may be distinguished as particularly significant:

- depositing large premiums of life insurance, at once or in installments, by natural persons for whom it is hard to determine professional occupation. It is noted that these persons do not have permanent employment, and are suspected to be performing illegal activities;
- policy buyer – an insured person lists a third person as beneficiary (a common case is that these are non-related natural persons);
- payment of policy (compensation, damages...) is referred to a third person;
- purchasing life insurance policies with securities (old savings bonds), for which it is hard to determine the mode of acquisition of the bonds.

TYOLOGIES

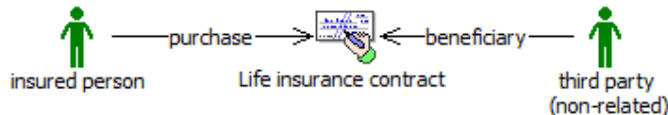
- **Large insurance premiums**

Depositing large insurance premiums, at once or in installments, by natural persons without permanent occupation, who are suspected to be performing illegal business activities;



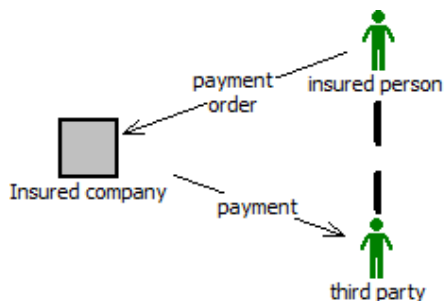
- **Policy beneficiary – non-related natural person**

Policy buyer – an insured person lists a non-related natural person as beneficiary in the policy;



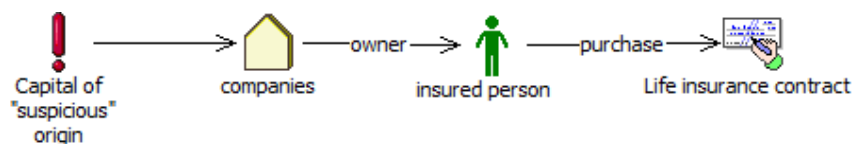
- **Payment of policy to the benefit of a third party**

Payment of policy (compensation, damages, and expiry) is referred to a third party (natural person or legal entity);



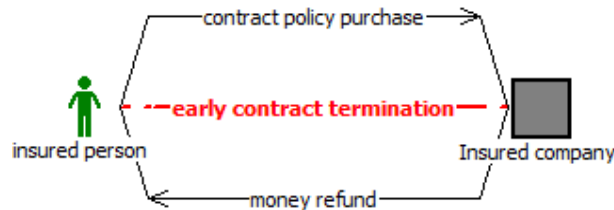
- **Capital of suspicious origin**

Purchase of a life insurance policy for the purpose of layering and integrating money of suspicious origin;



- **Short termination period**

Purchase of policies with one-time premium deposit, to a larger amount, with a short termination period



EXAMPLE

Description of the situation: A natural person – insured persons bought several life insurance policies from an insurance company for unusually high amount of money (it is well known that average payments of policies by the insured individuals in the Republic of Serbia are low). Some of the policies have short termination notice, and payments of the insurance premiums were made in cash successively and regularly. In the same period, except for the purchase of the policies, “the insured person” paid significant amounts of money to personal accounts.

The origin of the financial assets of the insured persons is unknown.

The Administration gathered all additional information for the insured person and discovered, by analyzing numerous unusual transactions with company “A”, that there was a link between above mentioned company and the insured person. Namely, in only three months, a great number of transfers of substantial amounts were performed on behalf of company A on the account of the “insured person“. The trade of goods and services was stated as the basis for transfer. Right after the completion of payments by company “A“, the insured person would withdraw the money from his personal account.

Based on the further analyses, it was determined that the real owners of company “A” were persons involved in organized crime.

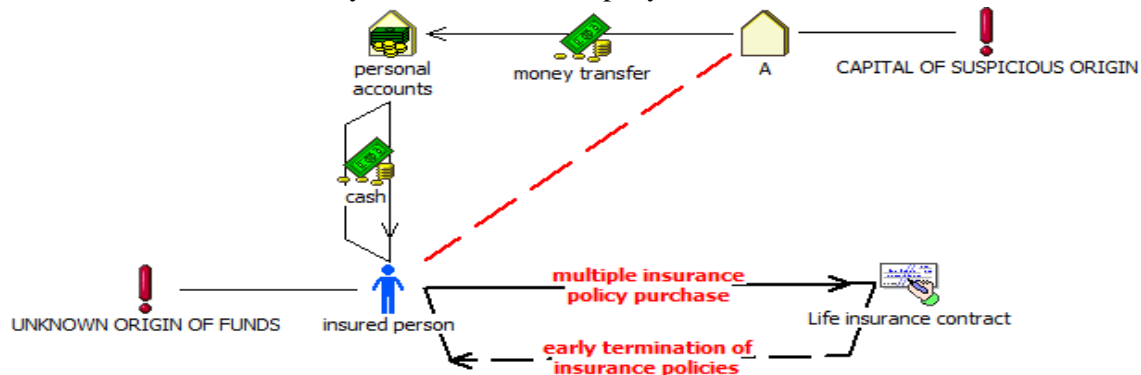
Based on the report of a suspicion transaction by the insurance company, tracking the cash flow, it was discovered that the origin of the cash which was used for purchase of life insurance policies was irregular and illegal. The insured person attempted to integrate part of that “dirty” money in legal flows, through purchase of life insurance policies, with an intention to buy the policies within a relatively short period of time.

This case was directed to competent institutions.

There are numerous **indicators** which led to a suspicion that there was money laundering in above described case:

- Unusual and high payment of life insurance policies (if it is known that average payments of policies per insured person are approximately EUR 1.000,00),
- Some of the policies had short termination notice,
- There were numerous high cash placements to personal accounts of the insured person,

- It is difficult to identify real owners of company A.



TRENDVI

The assumption is that, when it comes to insurance, the doubt will be related to the “disputable identifications” of the clients (unemployed persons, suspicious activities, concealed sources of cash for high premium payments), policies in the names of different insured persons and payments of the premiums by third persons in favor of the insured persons.

Special attention should be paid to the development of new investment products which become very interesting to money “launderers”. This primarily refers to the fact that life insurance policies could be used as stimulative savings or collateral for getting the loan.

The development of the life insurance industry in Serbia depends on the introduction of new products, purchase of life insurance policies which offer investment possibilities – investment policies (mortgage and other loans) and purchase of the policies which have elements of savings (offer profit which is higher than average for the other policies).

In case this increasing trend of the insurance industry continues, we could expect that the following characteristics will be a new motive for introduction of “dirty” capital:

- Purchase of life insurance policies and investment products (what does life insurance with investment risk refer to– indirect investment in investment funds and entrance to the capital market with the goal of achieving higher value of the policy etc.)
- Purchase of life insurance policies with deposits-savings characteristics or purchase of different types of life insurance – so called “grouping of policies“(life insurance, rent insurance, additional insurance, voluntary pension insurance, risk life insurance). The characteristics of this type of insurance stimulate the placement of “dirty’ money;
- Committing fraudulent actions in insurance supported by money laundering such as: insurance of risky population who frequently change addresses or conceals real identity and place of residence, close relations between the representatives and insured persons, or management and the insured persons, and all with the goal to aggravate the identification of “dirty” money which is placed for purchase of the policies.



We would like to emphasize once again that insurance is not the primary channel for money laundering, but some experiences of other countries show that that “money launderers” especially focus on insurance companies who offer products of investment character, such as savings or investments in capital market which enables money launderers to use numerous legal and new products in order to legalize illegally obtained cash, in much faster and efficient way and with higher amounts of placed capital unlike in case of purchase of regular life insurance policies.

MONEY LAUNDERING TYPOLOGIES IN THE REAL-ESTATE SECTOR

Both in the Republic of Serbia and the world, the real-estate sector is largely used in order to integrate the “dirty” money. The facts that support this claim show that the extent of laundering in the world is so high, that it was discovered that the entire complexes worth hundreds of millions of dollars are built using this “dirty” capital. The experiences show that Serbia has not been spared from money laundering on the real-estate market.

“Dirty“ money obtained in the nineties, when the commercial crime was strengthened, was massively used at the beginning of the twenty first century, due to the economic recovery of Serbia and sudden increase of demand for the apartments.

In the period after 2000, there was a trend of rapid growth of residential construction. Each individual could obtain land, building permit and build business or residential facilities. On the other hand, it was obvious that high amounts of money in the real-estate sector had suspicious origin. Investment in building of the real-estate and later disposal of the real-estate was very interesting for the individuals involved in organized crime, as well as to organized criminal groups. The link between crime and political structures is very important for this process. In order to obtain the permits for attractive locations, “dirty” money i.e. those who had it, used extremely corruptive methods.

Each person for whose needs a facility is built and in whose name the construction permit is issued can be an investor in Serbia. That practically means that each natural person can very easily be in construction business.

In the previous periods, the Administration intensively worked on its own, as well as in coordination with other state institutions on the cases where there was a suspicion of money laundering. In the real-estate sector, transactions of high amounts were especially interesting, and they were used for purchase of the land (location for construction) or construction material. It is not rare that the “launderers” used several related transactions in order to conceal the real origin of money.

The aggravating circumstances which make the real-estate sector vulnerable for money laundering are obvious connections between the organized crime and the politics, especially in relation to the purchase of attractive locations for construction of buildings, and in the segment of issuing of construction permits. All this makes the fight against organized crime and money laundering, as its integral part, more difficult.

It is safe to say that money laundering through real estate is significant. Money, i.e. assets are often laundered through purchase of real-estate. The fact which contributes to this situation is, as it was previously stated, the real-estate market which is not regulated.

The experiences so far show us that:

- “Dirty“ money is integrated in the real-estate sector through purchase of land, building of apartments, houses and business premises;
- Numerous construction companies are founded by the criminals;



- High amounts of cash are placed through banks and other financial institutions (postal services) for purchase of real-estate and construction materials;
- In order to conceal “dirty“ money, it is layered through several companies in order to conceal criminal origin of that money;
- Also, high amounts of cash are paid on the accounts of the institutions that deal with construction land;

The experience tells us that some very powerful and suspicious investors have appeared, which could be categorized as follows:

- Off-shore companies which provide money for construction of real-estate, and their real origin, or real owners cannot be determined;
- Individuals (natural persons) with criminal records;
- “Start up“ – newly formed “target” companies with primary goal of placement of “dirty money“ in real-estate and construction sector;
- Cover persons – i.e. persons with “clean” past, who work in the name and on behalf of criminal investors.

TYOLOGIES

Based on all above stated, the following typologies of money laundering through real-estate sector can be recognized:

- **Investor – natural person**

Placement of high amounts of cash of unknown origin to the personal bank accounts of the investors (natural persons) for the purchase of real-estate – cash which is suspected to be illegal is placed on the account of the investor – seller of the real-estate, and thus, his “dirty” money is “turned into” the property –house or apartment. The real-estate can further be sold and the money received from selling is invested in the securities, or it is simply used to purchase a new real-estate. The goal of this series of transactions is concealing of illegal origin of money;

- **High amounts of cash**

Payments of high amounts of cash of unknown origin by foreign investors (natural persons) to the institutions authorized to sell the locations and land;

- **Investor pays with cash**

A natural person appears as an investor, who uses the cash of unknown origin to pay for the construction works, sells newly built apartments and thus obtains clean money;

- **Third entities**

Payments through “third“ entities – an authorized person with no criminal background, respected citizen, with low income or without regular income purchases a real-estate on behalf of a money “launderer”;

- **Cashless transactions**

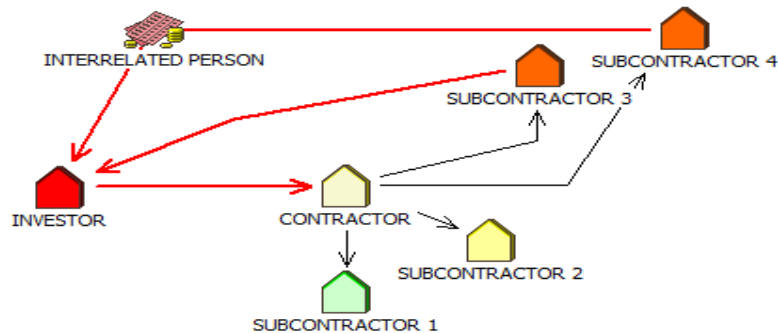
Cashless transaction through legal entities for which there is a doubt that the money originates from illegally obtained assets or it is difficult to identify a real owner;

- **Off-shore investment assets**

Purchase by investment assets from the off-shore destination, but their origin is unknown;

- **Subcontractors**

An investor uses “dirty” money to pay the contractor for the services in the amounts which are higher than the real ones, and then the contractor layers the money once again based on the service to several legal entities (subcontractors), which are then issued fictitious invoices, and that is how he receives laundered money.

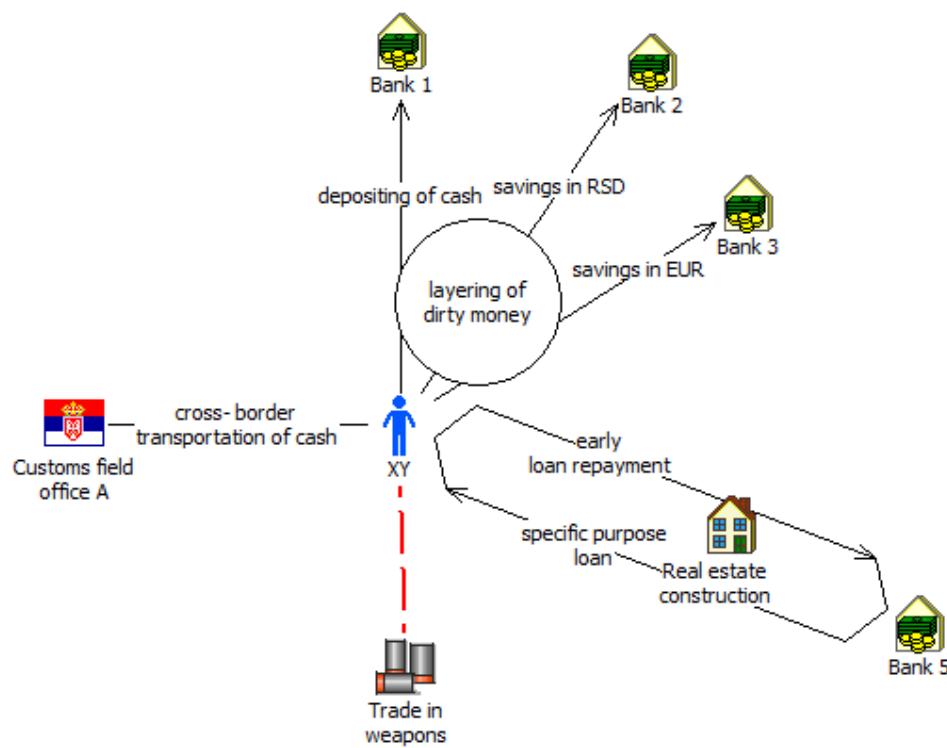


EXAMPLE

Based on the information received from the Customs Administration, the Administration discovered that, within a short period of time during a few months, natural person X brought cash in the amount of EUR 1.400.000 to the Republic of Serbia. The origin of the money is unknown, but it is suspected that it was received from illegal arms trade. Natural person X is a non-resident, working in construction and selling of the houses, he is not the owner of the company, nor is he registered as an entrepreneur. Cash brought in the Republic of Serbia was then placed on several accounts opened in different banks. The bases for the placements were different: sale and purchase agreement, placement of the account, term deposits of RSD amounts, foreign currency savings etc. An agreement was concluded with a bank on special purpose loan without deposit in the amount of almost 1.000.000 EUR. The purpose of the loan was completion of the construction works on a real-estate on an attractive location. A mortgage on another real-estate was registered as a security of the loan. The loan was repaid immediately after it was granted, and a lot before the expiration of the deadline for repayment.

The **indicators** which bring to the conclusion that this was a case of money laundering:

- Placement of the high amount of cash as a deposit for receiving a loan, and then, unexpected request of the client to repay the loan before deadline;
- Frequent transfers of high and rounded amounts by the client.





TRENDS

In the last few years, due to the influence of the world economic crisis on the economy in Serbia, construction business has been slowing down.

In the upcoming period, it is expected that that the trend of money laundering through real-estate will decrease, due to the world financial crisis, on one side, and more attentive “public eye” focused on the current events, on the other side. The criminals tend to find more sophisticated methods for money laundering, such as securities trading, insurance, which require better knowledge and skills, but also provide better guarantee that “dirty” origin of money will not be discovered.

However, regardless of all that, if the real-estate market recovers, the flow of "dirty" money will start again, because this sector is always very attractive, and especially when it comes to integration, the third phase of money laundering, when illegally obtained money is presented as legal, and it is the most difficult to prove its origin. The inflow of foreign capital is expected, which originates from the off-shore zones, and it will be very difficult to determine who the real owner is. It is expected that the attractive locations will be the target for this capital. Furthermore, elements of corruption are expected to remain as before.

On the other hand, implementation of the Law on Confiscation of Property Gained by Crime, will contribute to the decrease, and during a year and a half since its implementation started (in force since March 2009) it has given good results.

GLOSSARY

- **CyberCash** is a payment system which provides secure flow of information on transactions over Internet by payment cards but it does not include processing of the payment cards.
- **Dematerialization of securities** – conversion of the securities from material form (paper) into electronic records kept with the “Central registry, depository and clearing of securities“
- **E-Banking** is a service offered by the banks, which provides online disposal of assets from all the accounts. In Serbia, by using E-banking, natural persons may dispose of their assets only from their RSD accounts, and legal entities both from RSD and foreign currency accounts.
- **Futures** – Futures is a financial derivate presenting an obligation to purchase or sell certain goods or financial assets such as for example wheat, gold of securities on a certain day, based on previously agreed price.
- **Grouping of policies** – The insured persons purchase different insurance policies, such as long term life insurance with termination, life insurance with short termination notices, policies for insurance of third persons for higher amounts with termination clause, investment policies, pension and health insurance policies, etc. This practically means that an insured person makes a portfolio of policies.
- **Indicative price of shares** – Price of securities for real trading.
- **Investment policies** – Policies which enable the owner of the policy to select an investment fund where the insurance company will invest his money. For this reason these insurance policies have investment character.
- **Custody account** – Securities account opened and kept with custody banks with the Central Securities Registry, and may be individual or group.
- **Conversion of property** – Conversion of one type of property into another one.
- **Listed companies** – Companies which fulfilled the condition and criteria for their securities to be listed on the Stock Exchange.
- **Mobile Commerce** – Means each transaction of money realized through mobile telecommunication network.
- **Non-auditing services** – Non-auditing services includes all the services except for the auditing services.
- **Non-resident account** – Account opened in the country whose owner is a natural persons or legal entity who is non-resident of that country.
- **Off -shore legal entity** – Means legal entity which does not or may not have production or trade activities in the country where it is registered.
- **Option** – Option is a financial derivate which includes a right, but not the obligation, to purchase or sell certain assets, on a certain day, based on previously agreed price.
- **Cover person** – Person without criminal file who acts in the name and on behalf of another person – a criminal.
- **PayPal** is a company which provides intermediation services for payments, thus the money transfers are completely done via Internet, i.e. everyone who has an e-mail address can send money to another person who has an e-mail address. This process includes opening of the user’s account to which the assets from the current account are transferred or via payment card.



- **Payment cards** are the instruments of non-cash payments which enable the users to pay the goods or withdraw the cash without going to the bank.
- **Insurance policy** – Basic written document which accompanies insurance activity, which defines the duties and obligations of the parties. In certain cases the policy is a form of insurance agreement.
- **Tax haven** – Countries where financial investment is made easier, lower taxes and strict rules on banking secrecy..
- **Transfer of shares** – shares are transferred without compensation, based on a contract of gift.
- **Transfer of shares based on contract of gift** – Transfer of the ownership of shares from one person (initial owner) to another person (new owner) without financial compensation (financial transaction). This type of transactions is also defined as FOP transaction (engl. *free of payment*).
- **Insurance premium** – Cash amount the user of the insurance, i.e. insured person is obliged to pay as a compensation for securing insurance.
- **Dirty money** – Money obtained by committing crimes.
- **Selling of biography** – Natural persons without criminal history, who represent business interests of the persons involved in criminal activities in the situations when it is required to fulfill certain legal requirements. A natural person accepts this type of substitute for a certain financial compensation or commission.
- **Project financing** is a type of loan which is, under certain circumstances, granted to newly founded companies for construction of residential and business premises, and mortgage on the facility being built is seen as security for repayment of the loan, as well as lien on company shares.
- **Accounting documents** – All the documents which prove business activities.
- **Accounting statement**– means written presentation on financial conditions in certain legal entity. The basic financial reports comprise of balance sheet, income statement, statement of cash flow, statement of changes in equity and notes to financial statements.
- **Warming up the market** – An attempt to activate the market i.e. to use “artificial approach” to create offer and demand for certain securities.
- **Legal gap** is a gap which occurs when certain social relation is not regulated by legal norms.
- **SPV - Special Purpose Vehicle** means newly founded companies which are granted project financing.
- **Medium size companies** – medium size companies include those legal entities which on the day financial statements are made fulfill at least two of the following criteria:
 - annual revenue of 2.500.000 EUR to 10.000.000 EUR in RSD;
 - that an average number of employees in a year for which the statement is made is from 50 to 250;
 - that an average value of the business property (at the beginning and end of a business year) is from 1.000.000 EUR to 5.000.000 EUR in RSD.
- **Smurfing** – conversion of a great amount of financial assets through numerous transactions of smaller amounts, and all in order to avoid reporting to the Administration for the Prevention of Money Laundering.



- **Currency conversion** – conversion of one currency to another one.
- **Big companies** – big companies include legal entities which have the amounts higher than the highest ones in the indicators of medium size companies for at least two of the listed criteria.
- **SWIFT is the system for communication between financial institutions for exchange of the following data:**

103 MT 103 Single Customer Credit Transfer

Correspondent Input Reference

Sender : bank of the order issuer or correspondent bank

Receiver : bank of the beneficiary or correspondent bank Date:

STP

:20: Sender's Reference:

:23B: Bank Operation Code:

CRED

:32A: Value Date/Currency/Interbank Settled Amount ...

Date: | Currency: | Amount:

:50K: Ordering Customer:

Order issuer

:52A: Ordering Institution:

Bank of the order issuer

:53A: Sender's Correspondent:

Correspondent bank, bank of the order issuer

:57A: Account with institution

Bank of the payment beneficiary

:59: Beneficiary Customer:

Payment beneficiary

:70: Remittance Information:

Based on which the transaction was done

:71A: Details of Charges:

Who bears the costs