

**RISK MONITORING OF BANKS' PARTICIPATION
IN THE PROCESS OF MONEY LAUNDERING**

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Actuality of this article is argued with the fact that together with the dynamic development of the economic situation and creation of new financial products, a series of illicit activities of money legalization and laundering have been triggered. The assessment of money laundering process has become a problem of the international community, which currently imposes stringent development of prevention and compensation methods of its negative manifestations. Thus, we aim to analyze this negative phenomenon and determine the measures of suppression and minimization of processes of legalization of income from illegal activities. The following research methods have been used during the process of writing this article: logical method of systemic analysis and synthesis, comparative method, classification method, method of deduction, etc. Referring to the results and conclusions, we can emphasize that the banking sector's activity on combating money laundering is constantly jeopardized by certain vulnerable situations, thus being required a constant monitoring for decision making of minimizing and suppression of risks timely. The external environment of the banking sector was always favorable for forming new risks involving banks in illegal money laundering schemes. In this context, the identification of these risks is possible through implementation of new technologies in the banking system, tools and techniques for financial and banking monitoring, along with the application of good management of staff in the banking practice.

Keywords: globalization, financial-banking sector, bank, risk, monitoring, money laundering.

Actualitatea prezentului articol este argumentată de faptul că, odată cu dezvoltarea dinamică a stării economice și crearea noilor produse financiare, au fost declanșate un șir de activități ilicite de spălare și legalizare a banilor. Evaluarea procesului de spălare a banilor a devenit o problemă a comunității internaționale, care, actualmente, impune cu stringență elaborarea măsurilor de prevenire și compensare a manifestărilor sale negative. Scopul studiu constă în analiza acestui fenomen negativ și determinarea măsurilor de suprimare și minimizare a proceselor de legalizare a veniturilor provenite din activități ilicite. În procesul de scriere a prezentului articol științific au fost utilizate următoarele metode de cercetare: metoda logică de analiză și sinteză sistemică, metoda comparativă, metoda clasificării, metoda deducției etc. Cu referire la rezultate și concluzii putem sublinia faptul că activitatea sectorului bancar cu privire la combaterea spălării banilor a fost periclitată în permanență de anumite situații vulnerabile, ceea ce necesită o monitorizare permanentă la luarea deciziilor de minimizare și suprimare a riscurilor în timp util. Mediul extern al sectorului bancar întotdeauna a fost favorabil pentru formarea unor noi riscuri ce implică băncile în scheme ilegale de spălare a banilor. În acest context, identificarea acestor riscuri este posibilă prin implementarea în activitatea bancară a noilor tehnologii, instrumente și tehnici de monitorizare financiar-bancară, de rând cu aplicarea în practica bancară a unui management performant al personalului.

Cuvinte-cheie: globalizare, sector financiar-bancar, bancă, risc, monitorizare, spălarea banilor.

Актуальность данной статьи утверждается тем что параллельно с динамичным развитием экономической ситуации и созданием новых финансовых продуктов, был вызван ряд незаконных действий по отмыванию и легализацию денег. Оценка процесса отмывания денег стала проблемой международного сообщества и в настоящее время строго налагает разработку мер профилактики и компенсирования своих негативных проявлений. Целью данного исследования является анализ этого негативного явления и определение мер пресечения и минимизации процессов легализации доходов, полученных преступным путем. В процессе

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написания этой научной статьи в качестве методов исследования были использованы: логический метод системного анализа и синтеза, сравнительный метод, метод классификации и дедукции и т.д. Результаты и выводы. Банковская деятельность по борьбе с отмыванием денег постоянно находится под угрозой некоторых уязвимых ситуаций, что требует постоянного мониторинга для принятия решений по своевременной минимизации и подавления рисков. Внешняя среда банковского сектора всегда была благоприятной для формирования новых рисков, вызывающих банков в незаконной схеме отмывания денег. В связи с этим определение этих рисков возможно путем внедрения новых технологий в банковской деятельности, инструментов и методов для финансового и банковского мониторинга наряду с применением в банковской практике эффективного управления персоналом.

Ключевые слова: глобализация, финансовый банковский сектор, банк, риск, мониторинг, отмывание денег.

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Introduction. Currently, the state of the global economy is under a considerable pressure of the movement of financial resources flows, which has a visible impact on the socio-political status from worldwide. According to international practices, during the globalization process, fluctuations in the volume of inflows or outflows are considered, on the one hand, as catalysts for development, and on the other hand – a real threat to socio-economic tasks.

The dynamic development of the economy and creation of new financial products triggered an active request from criminal groups of new opportunities for expansion of investment fields through the mechanism of money laundering and legalization.

In this regard, identification of processes of legalization of income is essential for maintaining the stability of the financial-banking system. Or, evaluation of the process of money laundering has become a problem for the international community, whose aim is to study this phenomenon, which would allow the development of preventive and compensation measures of its negative manifestations. Thus, understanding the consequences of development of this negative phenomenon has forced the international community to focus its efforts on the development of suppression and minimization measures of the processes of legalization of income from criminal activities.

A leader in this field now is the International Financial Action Task Force (FATF). The International Financial Action Task Force was established by the G7 Summit in Paris in 1989, being an inter-governmental body that sets international standards, develops and promotes policies to combat money laundering and terrorist financing. FATF monitors the progress of its members in the implementation of the necessary measures, review of terrorism financing techniques and counter-measures, as well as promotes the adoption and implementation of appropriate measures globally. Currently, FATF includes 34 members, respectively 32 countries and governments and two international organizations, and more than 20 observers from which the five regional bodies of the FATF type and over 15 other international organizations or bodies. FATF has developed 40 +9 recommendations forming the international framework of fight against money laundering and terrorism financing. Recommendations are updated periodically in view of developments and trends of the two global phenomena. This international organization aims to develop and implement international standards in the field of combating laundering and legalization of income from crime and terrorism financing [10].

In February 2012, the FATF adopted new standards, which set a precedent regarding the need for a national assessment of the risks of income from criminal activity laundering. FATF recommendations urge member states to implement an approach based on risks evaluation, directed towards the detection, analysis and elimination of these threats.

Also, there was imposed the need to develop an effective risk minimization system and mitigation of possible consequences through rational management of financial resources. According to this approval, states should create a toolkit that will be able, in each concrete case to identify and establish the key criteria to determine and assess an existing or potential risk of legalization of income from crime. As a result, bank institutions that hold a key role in combating legalization of income from illegal activities become subject to an increased surveillance from the state and correspondent banks.

Functional analysis of the risk event of bank's participation in schemes of legalization of dirty money. Given the above mentioned, the prerequisites for economic and institutional environment modernization have gained a great social significance. Criminal groups in order to gain control over the economic activity in the area, invest in companies and then acquire control over them. On the other hand, banks, in order to obtain loans repayments, begin to use the help of these "investors". In turn, the last ones, obtaining these powers and using illegal methods, force bank customers to honor their debts. Thus, the financial-banking system becomes vulnerable vis-a-vis the laundering of income derived from illicit activities by certain criminal structures. The emergence of these vulnerabilities creates premises that the bank will later become a complicit in the process of legalization of illegal income. To minimize this fact, there is necessary to intensify the financial monitoring mechanism of the banking institution directed towards countering the money laundering.

One of the key principles of risk occurrence that involves participation of the banking sector in the process of money laundering is corporate governance. This principle is very important, because in the process of application of financial monitoring tools, the qualified personnel takes into account only personal responsibility, which is considered a key factor in accumulating the necessary information.

Thus, the consequences of including the financial-banking institution in the illegal schemes of income laundering, lead to the appearance of other risks in the activity of the mentioned institution, such as the risk of reputation loss, which ultimately will lead to loss of trust of partners, including the foreign ones, as well as to the diminish of the capitalization level, lowering of the price of own shares, etc.

After defining the concept of participation risk of the bank in the process of legalization of income obtained from illicit activities and for the development of measures on the establishment of an effective model for monitoring this risk from the bank's side, it is appropriate to classify this risk according to certain features and criteria.

For a better study of the essence of the risk event of the bank's participation in fraudulent schemes of legalization of income obtained illegally, we illustrate its functions as follows (see figure 1):

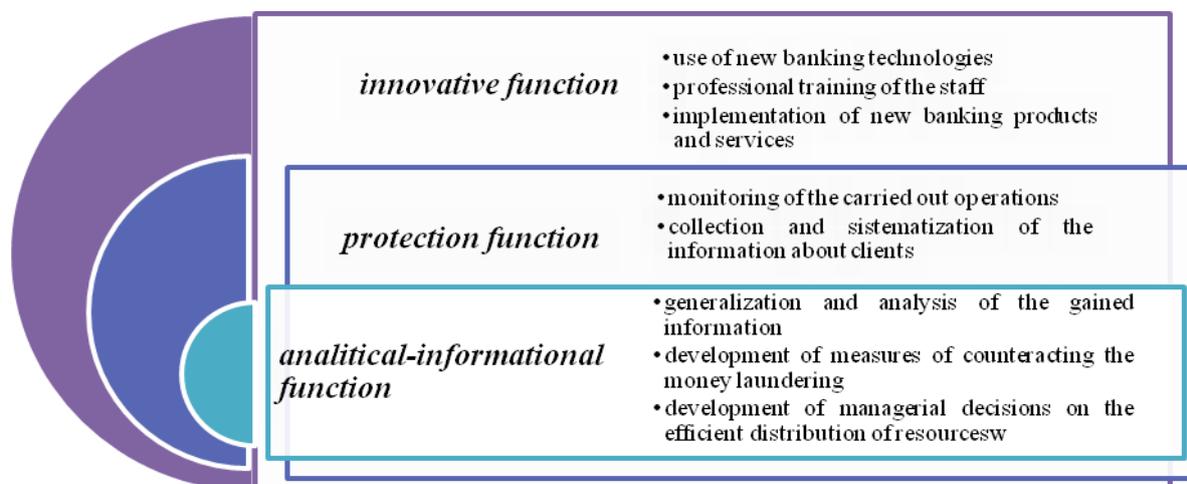


Figure 1. Functions of the risk of bank participation in the money laundering process

Source: Developed by the author.

Given the specificity of money funds laundering, the banking sector currently faces with achieving of the innovative function of the studied risk. This function is manifested by the continuing need to improve the level of knowledge of bank employees, with the aim of qualified and qualitative assessment of possible threats and their elimination in the short term through the bank's internal control mechanisms.

The innovative function allows the bank to implement financial mechanisms to reduce this risk in the safest way, based on a skilled and motivated assessment of the external and internal environment, thus ensuring a progressive and stable development of the banking activity.

Money laundering is regarded by the financial-banking institution as an opportunity that contributes to the establishment of the management strategy of banking operations by implementing the regulatory functions of the investigated phenomenon. Thus, it is required the awareness of the fact that obtaining illicit income can significantly increase the liquidity of the banking institution. Namely

the possibility of getting extra profit is often the reason why top managers of the bank participate in illegal money laundering schemes.

Bearing in mind that banking sector activity depends on external factors, as well as on internal ones, there always remain a high probability for it to be involved in illegal schemes to legalize monetary funds. Therefore, at this stage, the protection function of the studied risk is done by enhancing the internal control over operations conducted by the bank, and by taking immediate decisions of detection and minimization of the risk.

Thus, the efficiency of application of the protection function depends on the internal control structures, which will focus on activities to counter legalization of income from illegal activities.

In the process of monitoring the risk of participation of the banks in money laundering, a particular importance is given to informational support that is supported by analytical-information function. This function of the risk of bank participation in fraudulent schemes of legalization of illegal income is manifested by the need to collect and process information on possible threats and vulnerabilities in order to carry out a normal activity of banking institution.

Based on this analysis, we find that banks often classify risks for the participation of the bank in fraudulent schemes to legalize the money according to certain specific criteria, valid namely for the bank. These criteria are used to implement the policy of suppressing these risks. In addition, risk monitoring mechanism for the participation of banks in the money laundering aims at preventing, detecting and minimizing the risks. The analytic-information risk function is the most important in the monitoring process, as its qualitative implementation ensures the performance of subsequent measures in the process of suppression of money laundering activities. At the same time, by accumulating information resources, the analytic-informational function has the ability to create new risk management technologies and techniques. Also, this function creates possibilities for evaluating the potential risk events in the distribution of financial resources and requires an effective tactic in making management decisions.

It should be noted that the risk of involvement of the bank in the process of legalization of funds derived from illegal activities affects different components of the banking activity. Competent assessment of this risk helps to form an effective internal control model that includes monitoring tools of the risk of participation of banks in the process of money laundering, aimed at prevention, detection and suppression of vulnerabilities of the researched phenomenon.

Vulnerabilities characteristic for the Republic of Moldova's banking sector. Referring to the Republic of Moldova, in the context of the carried out investigations, we find that currently the banking sector represents the core of the financial market of the Republic of Moldova, while the other elements are underdeveloped (capital market), have a small share (microfinance and non-bank lending institutions, leasing), or are virtually non-existent (investment funds and venture capital) [3, p. 220].

The banking system is one of the most deeply embedded sectors in the national economy due to its lending activity, as well as collection and aggregation of savings of the population and companies. Therefore, it is the most sensitive to changes in the macroeconomic situation and expectations, showing a pro-cyclical behavior.

The crisis from the banking system underpins all the economic problems that the Republic of Moldova is facing at present, these being the biggest challenges to economic security of the country since 1991. The current conjuncture is caused by weak and easily influenced by obscure interests state institutions that allowed the spread of the deep crisis from the banking system and the economic downturn in the region. So, during 2014 and early 2015, the Moldovan banking system was disrupted by a series of bank frauds of historic proportions, which risks to undermine not only economic perspectives, but also those of European integration of the country [3, p. 248].

The main vulnerabilities that characterize the Moldovan banking sector in 2015 (in relation to the three financial institutions – C.B. „Unibank” J.S.C., C.B. „Banca Sociala” J.S.C., C.B. „Banca de Economii” J.S.C., being since 2014 under special administration) are:

- the high level of bad loans in a negative dynamic conditions of crediting of the real sector;
- liquidity and solvency were not placed in the appropriate levels;
- negative implications for the quality of the loan portfolio of domestic banks caused by increased depreciation pressures on the national currency [6, p. 51].

The fact that for about 1.5 years, three systemically important banks have committed a fraud of about 13.3 billion MDL or 950 million USD (12% of GDP) is a real failure in the regulatory activity of the

NBM [5, pp. 11]. Although the crisis of the 3 banks did not have systemic repercussions or origins, however, this has caused a considerable and sudden increase of inflation.

In the context of these events that were a direct threat to the economic and social security of the state, it is important to understand what the risks, legislative gaps and institutional vulnerabilities were that allowed decapitalisation of the respective banks and what will be done to transform the banking system from threat to opportunity of economic security and development.

The critical situation of the three banks was caused by a series of frauds aimed at de-capitalization of banks through offering credits in large proportions, with the involvement of offshore companies, local companies, foreign banks and perhaps, with the assistance of officials from state institutions. BEM, BS and UB were brought to bankruptcy by the artificial rise of liquidity indexes through interbank deposits and masking the bad loans, by assigning them to offshore companies. The ultimate goal was to artificially increase the lending capacity of the 3 banks and emits huge volumes of loans to a group of affiliated companies [9].

However, in 2015, despite the increase in non-performing loans and exchange market volatility, high levels of bank profitability were registered. In June 2015, banks' profit in the entire system amounted to 605.4 mil. MDL, up to 23.2% compared to the same period of 2014. This increase is due to the main component of the operational activity – interest income with 22.3% compared to the end of June 2014 had shown a positive dynamic. However, two commercial banks under special administration have recorded losses amounting to 302.4 mil. MDL: Banca de Economii – 166.8 mil. MDL and Banca Sociala – 135.6 mil. MDL. It should be noted that the population in the republic prefers loans with maturity of 2 to 5 years [8].

According to reports published by the NBM, the total volume of lending by commercial banks amounted to 2272.76 mil. MDL in June 2015, with 29.3% less than in June 2014. Loans in the national currency with the term 2 years to 5 years are granted at an average interest rate of 13.35%, and respectively, in foreign currency – at an average interest rate of 6.97% [6]. For comparison, in Romania, credits in national currency with maturity up to 5 years are granted at an average interest rate of up to 10% and in foreign currency – at an average interest rate of 5% [1].

Based on the carried out research, we support to the experts in the field opinion that state that the embezzlement of funds from BEM, BS and UB was based on fundamental factors such as:

1. The financial position of BEM has been undermined by acquiring the assets and payment liabilities of Investprivatbank (bank that went bankrupt in 2009) and the intensification of imprudent lending since 2013. In spring 2015, a significant package of shares became in the property of some companies from offshore zones which afterwards, have been transferred to companies from the Russian Federation. Subsequently, the critical situation of the BEM served as the main reason for transfer of the state a majority stake to Russian investors, with a doubtful reputation. Soon, some shareholders of BEM used shares in the bank to guarantee loans obtained by other companies from BS [2, p. 239].

2. Violation of the basic principles of corporate governance at BEM, BS and UB. Apparently, the new shareholders acted in concert, determining the management of banks to extend credit volumes for a number of companies affiliated to shareholders, violating all possible prudential rules [7].

3. Delayed and inadequate reaction from BNM and other relevant institutions. The fact that three banks of systemic importance during about 1.5 years defrauded the banking system with about 13.3 billion MDL, without essential constraints, denotes the failure of NBM in terms of regulation and supervision of the banking system [2, p. 240].

In other way, due to reduced transparency of the Moldovan banking capital, it is quite difficult to assess the actual situation on foreign investment chapter. Except for major „real” foreign investors' (Group Societe Generale in Mobiasbanca, Gruppo Veneto Banca in Eximbank, ProCredit Holding in ProCredit Bank, Erste Bank/BCR in BCR Chisinau), the other „foreign investors” are off-shore companies. Thus, four licensed banks have fully foreign capital – C.B. „EXIMBANK – Gruppo Veneto Banca” J.S.C.; C.B. „ProCredit Bank” J.S.C.; BCR Chisinau J.S.C.; C.B. „COMERTBANK” J.S.C., followed by C.B. „Mobiasbanca – Groupe Societe Generale” J.S.C. that holds 96.69% and B.C. „EuroCreditBank” J.S.C. - 98.84% [6].

According to the latest analyzes of NBM and NIER foreign direct investment remain weak for the national economy, while their need is felt more and more. Or, in the context when a set of reforms and public projects are awaiting external financing and business environment requires major investments to increase competitiveness, other domestic financing sources are compromised. In the pre-crisis period,

financial results of enterprises progressively worsen; access to credit becomes more difficult under the progressive tightening of monetary policy in this year; budgetary constraints are high and availability of businesses support is very small. All these create prerequisites for worsening of the existing economic situation, delaying the implementation of initiated reforms, mainly the Association Agreement with the EU, which without persistent and continuous efforts may result in a major failure.

Estimation of the macroeconomic risks of participation of banks in the process of money laundering. Thus, given that about 12% of GDP disappear from the banking system, and 3 banks whose assets are totaling about 35% of the assets of the entire banking system, the risks for the macroeconomic situation and the state of the entire country are obvious [5]:

1. *Country risk.* In the situation when the 3 banks will not be able to return the money (the probability is quite high because of the deplorable financial situation), the guarantees will be transformed into state debt. According to IMF forecasts, this will lead to a substantial increase in the level of indebtedness of the government: the share of public debt in GDP could increase from 32% in 2014 to 48% in 2015 and 51% in 2016. Against the backdrop of budget deficit and the risks for the national currency, the increase of debt is fueling the country risk [5].

2. *The risk of national currency depreciation and inflationary effects.* The period after the special administration within BEM, BS has coincided with the rapid depreciation of the national currency: from November 2014 to May 2015, the Moldovan leu has lost around 17% of its value [4, pp. 149-152].

Thus, the carried out analysis indicates that the critical condition of the local banking system is still actively influenced by the risk of participation of certain banks in illegal schemes of laundering of funds.

The lack of transparency of financial flows in the banking sector leads to emergence of risks of participation of the bank in money laundering. This also indicates on the occurrence of certain opportunities in the monitoring stage of the risk of participation of banks in the money laundering and obtaining reliable information about the client in order to identify potential threats and suppression of probability of their appearance.

Results and conclusions. Activity of the banking sector on combating money laundering is constantly jeopardized by certain vulnerable situations, which requires a constant monitoring for decision making of risk minimizing and suppression timely. The external environment of the banking sector was always favorable for the formation of new risks that involve banks in illegal money laundering schemes. In this context, identification of these risks is possible through implementation of new monitoring financial and banking technologies, tools and techniques in the banking activity.

The intense occurring of frauds in the Moldovan banking system during 2012-2015 was appropriate for appearance of the risk of participation of banks in such illegal schemes that ultimately led to inflation increase and jeopardize of the economic growth. In such cases it is very important the qualitative accounting which will enable the development of effective measures to combat money laundering in the banking activity.

Thus, the national economic experts recommend NBM to identify policies aimed at resolving the crisis in the banking system and eliminate regulatory gaps, as well as institutional vulnerabilities that allowed the deterioration of situation at BEM, BS, and UB in order to prevent future occurrences of similar practices. There is required the recovery of all deposits of individuals and legal entities, the responsibility of persons and institutions involved directly or indirectly in the frauds and reform of banking supervision and regulation system. We emphasize that the main challenges to financial stability for the next period are: resumption of lending in sustainable conditions, proper management of the quality of bank asset, including by providing a functional balance between the costs and benefits of various solutions for managing non-performing exposures, etc.

Elimination of institutional vulnerabilities that allowed the embezzlements from BEM, BS and UB must be an immediate priority for the authorities. In particular, it is necessary to increase the level of professional independence and personal protection of the NBM officials, who are directly responsible for the regulatory act. At the same time, NBM's independence has to be substantially strengthened to eliminate any excuses of regulatory failures. In this regard, it is necessary to remove the possibility to suspend the NBM decisions related to the regulation of the banking sector by any court.

In addition, the Administration Board of the NBM must be filtered from any political interference, and its members must not have direct or indirect political affiliations. Strengthening the independence of the NBM should take place in parallel with increasing its responsibility. In particular, it is necessary to

establish a mechanism to evaluate the performance of NBM by a foreign counterparty. This will ensure responsibility and allow an independent assessment of the institution, especially in crises conditions similar to the ones at BEM, BS and UB. It is important to ensure the independence of the NBM, while the financial sector should play an important role in the economic growth.

Finally, we emphasize that the attenuation of the state control along with tightening of contradictions between the social-economic and outdated regulatory framework became a good catalyst for corruption, which led to the development of illegal financial activities and widespread use in practice of various economic schemes of money laundering. Thus, there is required the total civic intolerance towards participation of the banking system in the legalization of income obtained illegally schemes.

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