"Anyone who lives within their means suffers from a lack of imagination."
— Oscar Wilde

"*The Analysis of the Romanian National System of Prevention and Combating Money Laundering, Based On International Tools of Preventing and Combating Money Laundering*"

Abstract: *This paper provides an overview of the international instruments used to combat and prevent money laundering. There are presented the international and the national framework, FATF Recommendations, the Mutual Evaluation Reports, the Suspicious Transaction Report, the Cash Transaction Report, the Currency Transaction Report and an overview of the relationship between economic growth and shadow economy modeled by a least squares function. The paper presents the importance of the instruments in combating money laundering for the economy. The report analyzes statistically data collected from 27 EU countries, rendering a linear regression model. The study illustrates that the GDP has a very tiny correlation with the shadow economy volume. In my opinion, this paper will provide a view on the quantifiable tools used to prevent and combat money laundering.*

<u>The phenomenon of money laundering and its evolution</u>

The economic globalization has led to the globalization of criminal activity of organized crime groups, expanding criminal throughout several states.

Following the process of dirty money introduction in economy, it can be said that this activity is in the "benefit" of the state, in that money launderers pay taxes, for the introduction to the real economy of money derived from drug trafficking, human trafficking, and other crimes related.

Worldwide, the money is transferred, transformed, recycle faster and complex, by organized criminal groups. They use different financial instruments, in order to insert the money in the real economy Due to this fact, it is necessary to have a legislation constantly evolving in line with the crime it wants to fight.

In Romania, both financial strength available to organized criminal groups and the volume of laundered money market are seen as significant, developed on the basis of an effective management of criminal activities, rigorous specialization and sometimes superior to modern logistics available to law enforcement.

Global financial and economic crisis continues to influence economic, social and political, with inevitable implications on national mechanisms, and especialy on law enforcement. One factor of the economic crisis is the increasing need for cash in the market, thus easing application of countermeasures against people who are willing to provide fast, secure and impressive amount of money.

Since you can not identify the exact time of occurrence of the phenomenon of money laundering, it is rooted in elements related to it, such as the emergence of trade and banking.

According to Mr. Rodolfo Uribe's article[1], the term "*money laundering*" was first used in the early 20th Century, to define operations that are used introduced into the economy money from illegal activities, facilitating their entry into the cash flow of the economy.

In Romania the term *money laundering* is defined by Law no.656/2002 on the prevention and sanctioning of money laundering and on setting up of certain measures for the prevention and combating terrorism financing, republished:

"*Art. 29 - (1) The following deeds represent offence of* ***money laundering*** *and it is punished with prison from 3 to 12 years:*

a) the conversion or transfer of property, knowing that such property is derived from criminal activity, for the purpose of concealing or disguising the illicit origin of property or of assisting any person who is involved in the committing of such activity to evade the prosecution, trial and punishment execution;

b) the concealment or disguise of the true nature, source, location, disposition, movement, rights with respect to, or ownership of property, knowing that such property is derived from criminal activity;

c) the acquisition, possession or use of property, knowing, that such property is derived from any criminal activity;

[1] Dr. Rodolfo Uribe, *Changing Paradigms on Money Laundering*, Anti-Money Laundering Unit, CICAD/OAS, 2003

(2) The attempt is punished.

(3) If the deed was committed by a legal person, in addition to the fine penalty, the court shall apply, as appropriate, one or more of complementary penalties provided for in article 531, para (3) let. (a) –(c) of the Penal Code.

(4) Knowledge, intent or purpose required as an element of the activities mentioned in paragraphs (1) may be inferred from objective factual circumstances".

International regulations on preventing and combating money laundering

Given the magnitune of the phenomenon, the United Nations adopted the first international convention, on combating money laundering and presenting a series of predicate offenses for money laundering offense, thus: those related to the production, trafficking and consumption drugs, organized and economic crime.

The most important international regulations on money laundering are:

- ***United Nations Convention Against Illicit Traffic In Narcotic Drugs And Psychotropic Substances***, 1988 – it's aim was to combat drug trafficking and money laundering derived from these activities; it wasn't used the therm of "*money laundering*";
- ***The Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime,*** 1990, includes regulations that offenders will be deprived of the products of the offense; the offense of money laundering applies to goods and benefit deriving from any crime, not just those related to drugs;
- ***Council Directive 91/308/EEC of 10 June 1991 on prevention of the use of the financial system for the purpose of money laundering (The 3rd Money Laundering Directive)*** provides a defition of the concept of „money laundering", "political exposed person", "beneficial owner". This Directive proposes the development of strategies to combat activtities related to terrorist financing. It is the most important European law in the field.

I've presented the most important legislation and international and national autorities in the field of money laundering, in Chapter II.

In Romania, the most important regulations contained in the national legislation AML are related to:

- Defining concepts relating to the AML system, such as "*money laundering*", "*suspicious transaction*", "*external transfers to and from accounts*", "*credit institution*", "*financial institution*", "*business relationship*" "*politically exposed persons*", "*operations that appear to be related to each other*", "*shell bank*", "*beneficial owner*", etc.;
- Defining the entities obliged to report to ONPCSB any information or suspicious transactions of money laundering;
- Regulations concerning the duties and obligations of reporting entities in preventing and combating money laundering and terrorist financing;
- Defining measures of “know your customer”, the method of their application and the sanctions applied under non-compliance on the subject;
- Provisions to ensure competence to verify and control the application of national legislation to prevent and combat money laudnering and terrorist financing;

Money laundering methods

Crimes in the financial sector are defined - in a broad sense - as any non-aggressive offense involving a financial institution, leading to a financial loss due to a fraud or embezzlement. Financial institutions may be involved in committing such crimes as victims, perpetrators or tools.

Regarding the ways of becoming more innovative Dr. Dionysios Demetis, said: "*The variation of methods and techniques of money laundering is truly amazing,*". “*The strategies penetrate traditional financial institutions, the securities industry, insurance companies, casinos, real-estate and the gaming-sector. Each of those contains a number of typologies that can be re-synthesized with each other.”*[2]

To tackle a phenomenon, must be able to identify it and to create a plan through which you could diminish its negative effects. In this acceptance, I will present various ways that money can be introduced into the economic system.

[2] Smith,David, “Black Money: The Business of Money Laundering” Economy Watch, 07 iunie 2011

The most commonly used methods are made through *cash transactions, through bank accounts, internal and external bank transfers, throught the operations of the credit and investment transactions.*

In conclusion, in Romania, the clues that have raised suspicions of money laundering involving the following:

- organized criminal groups in collusion with bank officials, open bank accounts, attaching cards holders who are not aware of their existence; they use the accounts to transferre large sums of money, amounting to ATM group members;
- banking officials are using the accounts of customers to transfer and withdraw money from the illicit origin;
- withdrawal of cash from the banking system on the basis of fake documents;
- outsourcing operations funds based on justifications that they do not meet the financial profile and objects of authorizing, sometimes followed by reintegration companies by non-credit method;
- Romanian citizenship, unemployed and poor educated collecting large sums of money, with the justification compensation insurance or goods;

All these activities require good cooperation with traders, credit institutions, financial intelligence units in the country and abroad, law enforcement, supervisory and investigative bodies to mitigate the adverse effects on the economy caused by money launderers who have developed innovative and more complex ways to capitalize illegal funds.

International instruments on prevention and combating money laundering

The Financial Action Task Force (FATF - GAFI) is an inter-governmental body established in 1989 by the Heads of State of the G7 countries in order to protect the international financial system from money laundering risks.

In April 1990, FATF issued a series of 40 Recommendations, which were designed to provide a basic framework for action plans required to be taken at national level in order to protect the economic systems from the effects of money laundering activities.

In February 2012, the FATF standards were revised to strengthen the obligations in high-risk situations and to allow countries to identify, evaluate and understand the risk of money laundering and financing of terrorism and then take appropriate measures to mitigate the risks posed by them.

In the article[3] published in 2012, Louis de Koker conducted a study on the impact of new FATF standards on virtual money models of the developed countries. It highlights aspects of the new Recommendations that may facilitate the development of virtual money, but indicates some dilemmas and challenges arising simultaneously with the adoption of these Recommendations.

Empirical testing of the phenomenon of money laundering in ROMANIA

To understand the issue of money laundering worldwide, it is important to estimate the amounts of money laundered.

In this respect, in 1996, the International Monetary Fund (IMF) estimated that about 5% of the money in the world economy are money laundered. In this context, the Financial Action Task Force noted that "*in general, it is absolutely impossible to produce a viable estimatimation of the value of money laundered*."[4]

There have been several studies which attempted to quantify the laundered money worldwide, and John Walker (1999), Director General of Typologies of Money Laundering Directorate in Australia was the first who considered that have to give more accurate numbers. After conducting a study revealed that approximately $ 2850 billion from the worldwide GDP were washed, and the areas where this phenomenon is high were identified as North America and Europe.

"*The Walker Model*", examines two different aspects of the process of money laundering. First, considering the laundered money in each country, and then, considering the laundered money from one country to another, given that the money may be washed in the country in which they were generated, or can be "sent "in another country to be placed in the global economy. An important element of this model is that once the money has traveled at least once, they can be considered "laundered".

[3] Louis de Koker, *The 2012 Revised FATF Recommendations: Assessing and Mitigating Mobile Money Integrity Risks Within the New Standards Framework*, Washington Journal of Law, Technology & Arts, Volume X, 2012
[4] Smith,David, "*Black Money: The Business of Money Laundering*", Economy Watch, 2011

In Walker's Model, the U.S. is responsible for 46.30% of the laundered money ($ 1320 billion), and the following are the other two centers of well-known organized crime: Italy (5.30%, or $ 150 billion) and Russia (5.20%, or $ 147 billion). Next on the list are China (with a share of 4.6%, representing $ 130 billion, but its share is expected to have changed substantially from then to present), Germany, France, Romania, Canada, United Britain, Hong Kong.

As I previously presented, there were sevel attempts of the specialists in macroeconomics to measure the value of money in the underground economy, aimed at actually measuring laundered money, but the thing never realized. Various studies have been made, but unfortunately, to date, we can not discuss actual numbers illustrating the laundered money in a certain economy, or at least their percentage of GDP.

In this context, given that I wanted to use exact numbers from credible sources existing in the market, I decided to take in calculation the rate of the shadow economy in the GDP in order to demonstrate a direct correlation between it and the real GDP growth rate in 27 EU countries.

I used the model study by prof. Dr. Ion Stancu, prof. Dr. Daniel Rece Philip Iorgulescu, entitled "*The Relationship between Economic Growth and Money Laundering – a Linear Regression Model*", presented at the international conference "*Finance And Economic Stability In The Financial Crisis*", held from December, 2009.

Thus, in the following I wanted to study the relationship between economic growth and the shadow economy using econometric regression. The study is based on information obtained from the official website of the Statistical Office of the European Communities Eurostat on 27 European countries (28 member states after accession of Croatia in 2013, but it is not included in this study) and percentage of money in the underground economy in GDP, data used in the study by. Schneider, F., Size and Development of the Shadow Economy of 31 European and 5 other. OECD Countries from 2003 to 2012: some new facts., published in 2012.

Given that quantifiable tools to prevent and combat money laundering used by FIU Romania were exposed during 2008 -2012, presented in a previous chapter, the regression was performed on data for the same period.

Incoming data are presented in **Annex. 1**, and after application of the linear function y = a + b × X to 135 of observations, the results were as follows:

Regression Statistics	
Multiple R	0.030815753
R Square	0.000949611
Adjusted R Square	-0.00656205
Standard Error	4.11131432
Observations	135

Table no. 1. - Statistics regression equation for 135 observations

ANOVA

	df	*SS*	*MS*	*F*	*Significance F*
Regression	1	2.13683594	2.13683594	0.1264183	0.722738286
Residual	133	2248.08642	16.9029054		
Total	134	2250.22326			

Table no.2. - Analysis of variance of regression equation for the 135 observations

After analyzing the data and finding that the model is not valid and not as the hypothesis that there is a positive correlation between the share of money in the underground economy in GDP and its rate of growth.

I tried to remove outliers, extremes recorded, ordering data series based on the indicator of GDP growth rate, we decided to eliminate the 22, 22% of observations, respectively 15 and 15 negative values very highly positive values.

Generated results are found in Table. 3 and no. 4.

Regression Statistics	
Multiple R	0.015104836
R Square	0.000228156
Adjusted R Square	- 0.009478367
Standard Error	2.254353101
Observations	105

Table no. 3 - Statistics regression equation for 105 observations

ANOVA

	df	*SS*	*MS*	*F*	*Significance F*
Regression	1	0.119457178	0.119457178	0.023505439	0.878449966
Residual	103	523.4571143	5.082107905		
Total	104	523.5765714			

Table no. 4.- Analysis of variance of regression equation for the 105 observations

Provided that no such results are not much better than those obtained previously, I decided to extend the period for which I studied for 2003-2012. I thought that in this way will not be strong effects arising from the recession years of the study in Europe in the global crisis, a situation that has seriously affected the data.

Thus, I have shown in Annex. 6.2. - Data available on the Eurostat website and in the study by Mr. Schneider for the period 2003-2012.

After I applied the regression function on the 270 observations, the results generated were:

Regression Statistics	
Multiple R	0.192949672
R Square	0.037229576
Adjusted R Square	0.033637149
Standard Error	3.994302762
Observations	270

Table no. 5.- Statistics regression equation for 270 observations

ANOVA

	df	*SS*	*MS*	*F*	*Significance F*
Regression	1	165.3416	165.3416	10.36335	0.001444
Residual	268	4275.794	15.95445		
Total	269	4441.135			

Table no 6. - Analysis of variance of regression equation for the 270 observation

Although I tried to diminish the effect regression that registered a GDP indicator in economic states in the years that followed the crisis of 2008-2009, no such results were not consistent with those expected.

In this context, I ordered ascending indicator data by real GDP growth rate, and I decided to remove the 30 extreme values at negative and 30 positive values at the end.

The results obtained were as follows:

Table no. 7. - Statistics regression equation for 210 observations

Regression Statistics	
Multiple R	0.189925521
R Square	0.036071703
Adjusted R Square	0.031437433
Standard Error	2.045684473
Observations	210

ANOVA

	df	*SS*	*MS*	*F*	*Significance F*
Regression	1	32.57335968	32.57335968	7.78368509	0.005761928
Residual	208	870.4435927	4.184824965		
Total	209	903.0169524			

Table no 8. - Analysis of variance of regression equation for the 210 observation

Conclusion

Given that I removed 22, 22% of the extreme values for results that demonstrate the hypothesis, even this time I did not get a positive correlation between the level of money in the underground economy and the level of GDP growth in the context data of 27 countries in the European Union.

From Table..7. results a low intensity between variables, approximately 19%. Only 3.6% of the variation is explained by the variation economy growth rate of real GDP growth. GDP growth generates very little growth for shadow economy. It can be seen from the data presented that it is relatively constant, being greatly influenced by the change of state GDP. However, the increase in the shadow economy should generate a negative effect on the real economy of a state, in the context of law enforcement bodies and investigation would be effective and applicable tools to mitigate its effect on the economy.

However, higher values are found in the states economy in Southern Europe to North or West of it, which indicates a lower efficiency measures to combat crime in this states.

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