

# TYOLOGIES RESEARCH

OF THE STATE FINANTIAL  
MONITORING SERVISSE OF  
UKRAINE

for 2016, 2015, 2014 years



State Financial  
Monitoring Servise of  
Ukraine



State Financial Monitoring Service of Ukraine

State Training Institution of Postgraduate Education “Training  
Centre for Retraining and Professional Development of Experts on  
Financial Monitoring Issues in the Sphere of Combating Legalization  
(Laundering) of Criminal Proceeds, and Terrorist Financing”

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Kyiv 2017

Recommended by the Interbranch Research and Methodology Council of the State Training Institution of Postgraduate Education "Training Centre for Retraining and Professional Development of Experts on Financial Monitoring Issues in the Sphere of Combating Legalization (Laundering) of Criminal Proceeds, and Terrorist Financing"  
(Minutes of meeting as of January 30, 2017 № 1)



**Typologies Research of the State Financial Service of Ukraine for 2016, 2015, 2014 years – K., 2017. – 122 p.**

The edition covers more common in 2016, 2015 and 2014 trends and schemes of money laundering and financing of terrorism. In particular, the real case studies related to money laundering and financing of terrorism over the past three years which pertained to corruption, most actual schemes of money laundering and financing of terrorism were presented.

The information on the results of work of state bodies – participants of the national financial monitoring system were included to the typological researches.

The edition was designed for employees of reporting entities and state financial monitoring entities, law enforcement, intelligence and judicial authorities, as well as scientists and practitioners in financial monitoring sphere.



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# FOREWORD

Head of the State Financial Monitoring Service of Ukraine Mr. Igor Cherkaskyi



The State Financial Monitoring Service of Ukraine offers for consideration its typological researches of 2016, 2015, 2014, covering the results of FIU's work on exposure modern schemes and methods that are used by criminals for the legalization (laundering) of the proceeds from crime and terrorist financing.

Currently in Ukraine fundamental political, social and economic changes continue to occur as a result of the Revolution of Dignity, which took place on November 2013 – February 2014.

Ukraine stubbornly continues to take enhanced measures to develop and improve the national system of financial monitoring in accordance with international standards for three consecutive years despite the difficult political and economic conditions.

One of the most dangerous threats to the successful development of our country remains an escalation of such dangerous crimes to society as the legalization (laundering) of the proceeds from crime and terrorist financing.

In this regard, it is quite logically that the first SFMS's active work is carried out in relation to research and financial investigation cases of laundering proceeds from corruption activity, embezzlement and misappropriation of public funds and property by former President of Ukraine, his close persons, former Government officials and related persons.

In its turn, another of the priorities of the SFMS is an activity aimed at identifying individuals and their financial transactions that may be related to terrorist financing or conducted with the participation of persons who publicly call for violent change or overthrow of the constitutional order or change limits of territories or state border of Ukraine.

One of the effective forms of response to the challenges of criminal environment is research, detection and disclosure of schemes in which criminal proceeds are legalized and terrorism is financed.

The need for such SFMS's activity is directly provided for by law of Ukraine and FATF Recommendations.

Presented edition gathered typological researches of the SFMS for the last three years relating to:

- the legalization (laundering) of the proceeds from corruption activity (typology 2016);
- standart tools, methods and mechanisms of the legalization (laundering) of the proceeds from crime (typology 2015);

- actual methods, techniques and financial instruments of financing terrorism and separatism (typology 2014).

During all these years, we consciously focused on the analysis of the most fundamental risks that exist in the national system of financial monitoring. These are the fight against corruption, terrorist financing, actual money laundering schemes.

Today a whole community is looking after the issue of combating the legalization (laundering) of the proceeds from crime and terrorist financing, both at the international and national levels. Thus, the result of solving this problem depends on the combining efforts of all institutions and organizations active in AML/CFT area.

I am convinced that prepared by the SFMS compilation of typological researches will be useful to practitioners of public and private sector and to the public, dealing with the protection of the financial system from criminal encroachments



Igor Cherkaskyi



# LAUNDERING FROM CORRUPTION

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TYPLOGIES 2016

## Introduction

Corruption as a social phenomenon is the serious problem in any society. The most dangerous form of corruption is jointing of criminal elements with state structures resulting in the situation when an official operates for own beneficitation or trades with the official functions.

Corruption relations of the officials become a part of criminal business. Corruption penetrates into vital spheres of the society, allows controlling over financial and industrial groups and economic industries, certain large enterprises, promoting their interests in law-making authorities and state administration bodies and self-governing authorities.

The typological study on a topic “Money laundering from corruption” has been prepared by the State Financial Monitoring Service in cooperation with state regulators, regulating, law enforcement authorities of Ukraine and financial institutions.

It is the first unified study of the State Financial Monitoring Service of methods and schemes of money laundering. The results include best practice of all subjects of financial monitoring and are based upon proof that anti-corruption efforts are closely connected with the measures for anti-money laundering or countering the financing of terrorism and the financing of proliferation of weapons of mass destruction.

**The goal** of this study is focused on determination and summation of standard instruments, methods and mechanisms of money laundering.

The question of anti-corruption efforts is the up-to-date requirement and mostly vital for Ukraine. World experience shows that if the country is at the stage of reforming, the corruption level is always increasing. Thus, corruption in Ukraine and its volume, specific features and dynamics are resulted from common political, social and economic problems of our country and its reduction is vital and quite difficult matter in question. The unseen corruption level threatens the national security and constitution pattern of the country.

Corruption is a dangerous social phenomenon of any country. Money laundering has cross-border nature when a crime may be committed in one country and finally ended in another country. Thus, origin of corruption funds used for laundering may be both internal and external.

The most popular types of corruption are as follows: bribery, embezzlement of budget funds, and abuse of powers or official position.

The most vulnerable to corruption is the sphere of state procurement that is expressed in bribery taking for winning bidders, embezzlement of budget funds through signing of fictive contracts by the officials, provision of benefit to the affiliated persons through unjustified revoke of competitive bids for other potential vendors.

The most wide spread corruption phenomenon is so-called “trade” with the official powers, i. e. use by the officials of their official position for receiving economic benefits.



Those funds from implementation of the corruption schemes are further used for purchase of luxury real estate, VIP-class cars, yachtes, precious metals and stones, antiques, securities, luxury rest, investment in business and other personal needs.

At the moment, formation of the unified system of measures and efforts to be used by state authorities for anti-corruption efforts is the question of present interest for Ukraine and key for development of the effective state. International experience shows that anti-corruption efforts are effective only under conditions of complex settlement, definition of clear priorities when corruption penetrates into various spheres of state life, when anti-corruption efforts are taking on a regular basis and controlled both by government and society.

This report has been prepared in order to understand by the subjects of financial monitoring of the risk to be involved in the schemes of money laundering and taking of any effective measures to counter such involvement.

This typological study includes the examples of high-profile cases of corruption-related crimes. The given examples show the financial participation of public persons and officials of state authorities in criminal schemes causing damages to the state assets..

## 1. Common component of corruption level in Ukraine

The common level of corruption in Ukraine is quite high. In 2014, according to the international anti-corruption non-governmental organization Transparency International, Ukraine took 142<sup>nd</sup> place among 175 countries in terms of corruption level.

Over the past year Ukraine earned only one additional grade. Based on the result of the Corruption Perception Index, in 2015 Ukraine took 130<sup>th</sup> place in terms of corruption perception level among 168 countries.

Ukraine managed to show positive dynamics of index due to increase in counterspeech of corruptionists, formation of anti-corruption authorities and appropriate legislation.

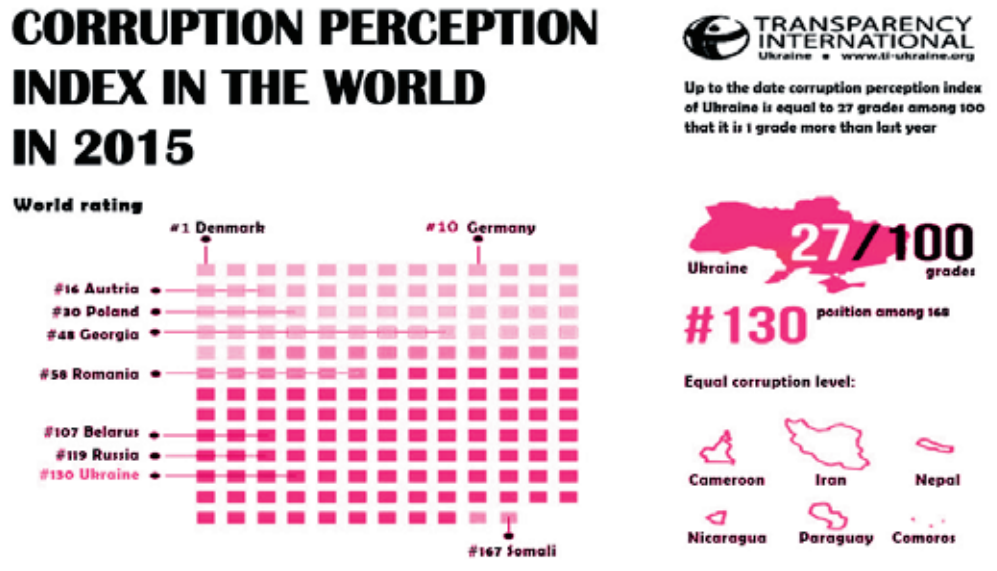


Figure 1. Corruption Perception Index in the world in 2015 (concerning Ukraine) 1.

For the last years Ukraine made a large number of anti-corruption efforts – adopted specific anti-corruption law and a range of other legislative actions for anti-corruption efforts, approved the Concept of anti-corruption efforts and special anti-corruption program, implemented systematic taking of measures at the highest level involving heads of law enforcement and other state authorities concerning anti-corruption efforts, etc.

1 Source: according to Transparency International.





Figure 2. Laws of Ukraine aimed at anti-corruption efforts

Effective anti-corruption efforts are possible only through concerted efforts of all law enforcement authorities, being an important element of crime prevention, in general, as it allows combining efforts of state authorities and coordinating between them for the most effective results.

The common number of the initiated pretrial investigations under file cases of the National Security Service of Ukraine concerning control of corruption in 2013 was equal to 1,027, 456 among them are concerning the persons suspected in commitment of corruption-related crimes (according to Article 368 "Bribery taking" of the Criminal Code of Ukraine – 247), 598 protocols on administrative corruption offences were recorded.

In 2014 the statistics was as follows: pretrial investigations – 954, 359 among them are concerning the persons suspected in commitment of corruption-related crimes (according to Article 368 "Bribery taking" of the Criminal Code of Ukraine – 233), 705 protocols on administrative corruption offences were recorded.

In 2015, according to the special forces units of the National Security Service of Ukraine, the persons were suspected in commitment of 544 corruption-related crimes, 414 among them are related to taking of offer, promise or undue benefit by the official (Article 368 of the Criminal Code of Ukraine), 476 protocols on administrative corruption offences were recorded.

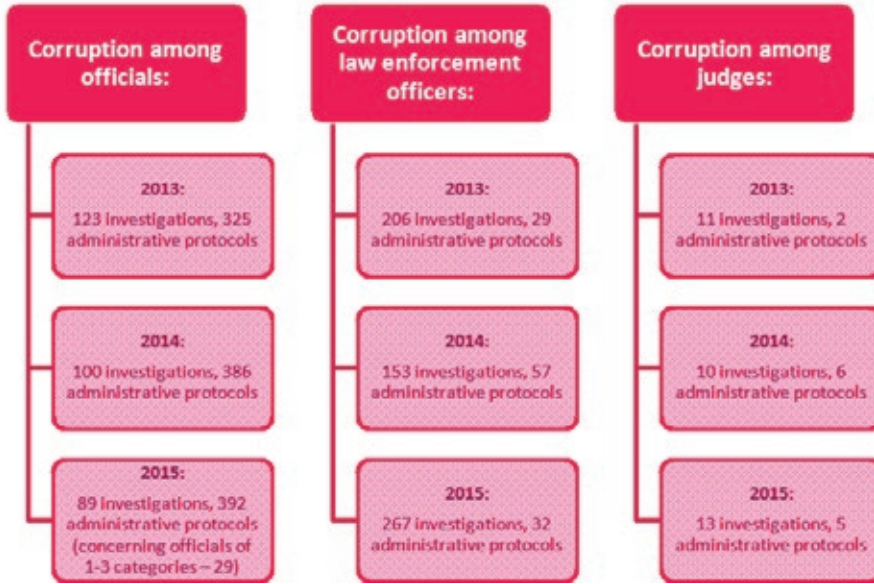


Figure 3. Anti-corruption policy of the National Security Service of Ukraine

The results of anti-corruption policy of the General Prosecutor’s Office of Ukraine are given in Figure 4.

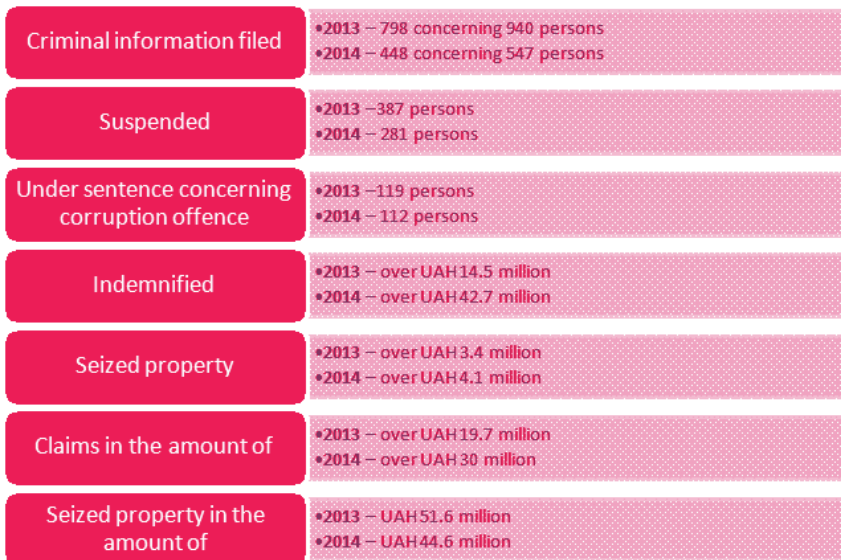


Figure 4. Anti-corruption policy of the General Prosecutor’s Office of Ukraine

During 2013 the authorities of the Ministry of Internal Affairs of Ukraine took to the court 668 protocols on corruption offences, in 2014-773, in 2015-2,147.

In 2013, 488 persons were brought to justice, 76 among them were subject to seizure, in 2014-553 persons, 28 among them were subject to seizure, and in 2015-1,720, 60 among them were subject to seizure.

The amount of losses in 2013 constituted over UAH 221.5 million and in 2014 – over UAH 67 million, the indemnified amount of losses in 2013-2014 constituted over UAH 11.5 million and UAH 34 million, accordingly.

During 2015, 125 criminal offences concerning 137 servicemen of the State Border Guard Service of Ukraine and 8 other persons were recorded in the unified state register of pretrial investigations.

63 facts of the commitment of corruption-related crimes by the officials of the State Border Guard Service of Ukraine were recorded in the unified state register of pretrial investigations.

For the commitment of crimes related to violation of anti-corruption legislation, 17 servicemen were convicted, 2 among them – for crimes committed in 2014.

As of the end of July of 2016, the National Anti-Corruption Bureau of Ukraine was considering 194 criminal investigations in process, 100 among them were registered upon the application of persons and entities, as well as own best practices of detectives and analytics of the bureau. 82 criminal investigations were accepted or registered upon the materials of other law enforcement authorities. The remainder was approved through a court proceeding and upon the application of the people's deputies of Ukraine.

The aggregate volume of the target of crime in criminal investigations to be conducted by detectives of the National Anti-Corruption Bureau of Ukraine exceeds UAH 23 billion.

Upon pretrial investigations, notice of suspicion was served to 87 involvents. Concerning 34 of them, criminal information was executed and taken to the court. As of 29.07.2016, detectives of the National Anti-Corruption Bureau of Ukraine finished the pretrial investigation and took to the court 24 trial contents.

Upon pretrial investigations, funds in the amount of UAH 411.07 million, US \$75.45 million and EUR 7.1 million was seized. Moreover, the National Anti-Corruption Bureau of Ukraine seized 2 integral property complexes of the enterprise, 94 land lots, 50 non-residential premises, 37 flats, 13 buildings, 35 vehicles, including 2 aircrafts, as well as 17 stocks of enterprises and securities in the amount of US \$75.5 million. Based on the results of the National Anti-Corruption Bureau of Ukraine, the amount of UAH 45 million was returned in favor of the affected parties.

It should be noted that coordination of actions of the State Financial Monitoring Service and law enforcement authorities plays the key role in concerted actions for prevention of corruption.

Common goals and tasks are focused on taking orchestrated and purposeful efforts, strengthening legitimacy and improving efficiency of enforcement of all members of the national anti-money laundering system.

## 2. International experience of money laundering

Money laundering is a complex process including a large number of transactions settled in various ways to be regularly improved.

The scientist Stephan Platt noted that bribery and corruption are one of the most spread forms of predicative crimes. Up to the date, Stephan Platt conducted the study of money laundering schemes, for example, bribery taking in the amount of US \$ 20 million paid by the company, being a large manufacturer of weapons, to the government executive of the Middle East country.

The given example shows the application of the sphere of financial services for payment of bribery and ways for money receiving and laundering by public persons.

Thus, the company-manufacturer of weapons has information on the demands of the Middle East jurisdiction in renewal of old military fighter aircrafts.

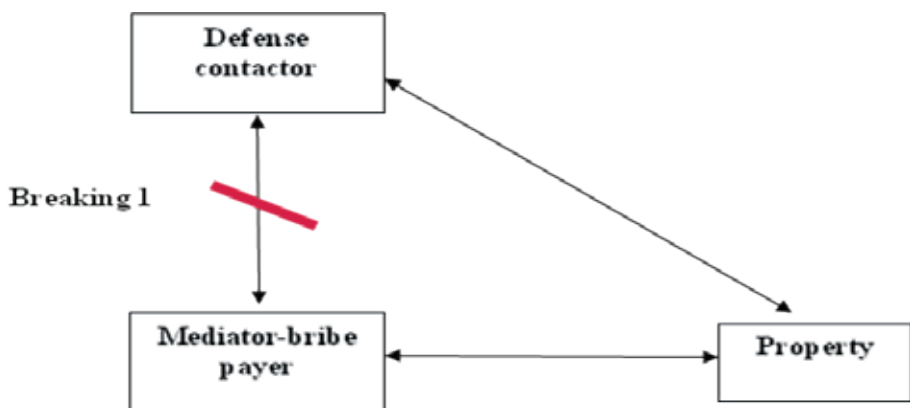
The contract is expected to provide the Company with hundreds of million USD and several thousands of workplaces. There are five nominees to be awarded by the given contract.

At this, such participation “costs” US \$ 20 million. The company-manufacturer of weapons considers the amount of US \$ 20 million as cheap economic offer for participation in tender. The company knows that this amount is bribery only.

The Ministry of Defense of the Middle East country is presented by the Company-mediator. The mediator requires for a “fee” in the amount of US \$ 2 million equal to 10% of the bribery amount.

Negotiations on the matter of participation of the company in tender and transfer of the amount of US \$ 22 million to the representative of the Ministry of Defense are being confidential.

For hiding of illegal source of funds origin, it is proposed to use the financial system. For the given scheme, it is required to break link between the Company-manufacturer of weapons and US \$ 22 million as follows:

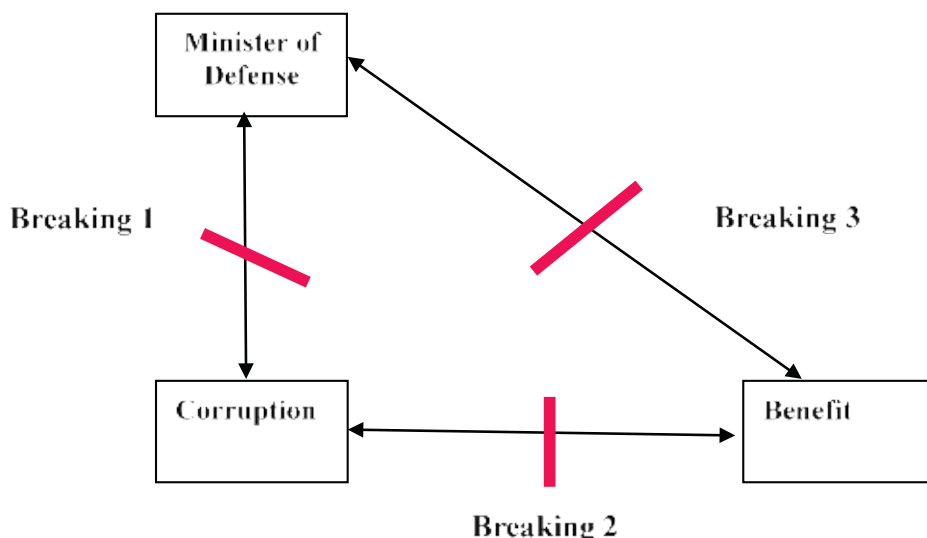




The company-manufacturer of weapons has controlled taxation free company for special purposes (Special Purpose Entity – SPV) in foreign jurisdiction. The controlled company was established by the company-manufacturer of weapons for performing overall activity with other manufacturer of weapons, not being sold. Funds from the accounts of the company-manufacturer of weapons in the amount of US \$ 30 million were previously withdrawn and holding on the accounts of the controlled company on the legal basis.

For hiding of bribery taking, the Minister of Defense intents to:

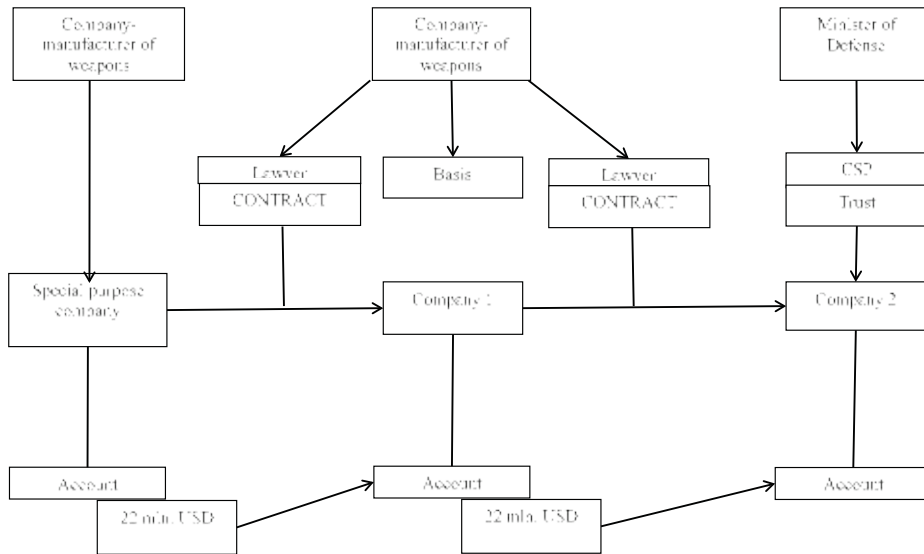
1. Receive funds from bribery taking, not being landed.
2. Disguise the bribery taking so that it cannot be tracked.
3. Disguise its participation in criminal property.



Breaking of chain for each goal may be made as follows.

Breaking 1 between the company-manufacturer of weapons and the Ministry of Defense is payment and taking of bribery, accordingly, in such form that the law enforcement authorities have no question to them. These two persons are related to participation of other person – representative of the Minister that controls the company-mediator and affiliated bank account. The company-mediator is represented by the Swiss law firm which partners seriously behave to the matters of confidentiality of their client.

The company-manufacturer of weapons, the Minister of Defense, Swiss law firm and the company-mediator negotiated on participation in the following scheme.



The main player is giving bribe to the Minister of the Defense through the mediator.

The Minister's representative firstly should give instructions to the Swiss law firm on conclusion of the master agreement on service provision. The Company-manufacturer of weapons should conclude the (fictive) agreement with the Company 1 on provision of services on search of potential contracts for weapons delivery in different regions of the world. In the Contract it is shown that the Company 1 will provide a series of services specified in the List 1 hereof, the common list of which may include up to 75 pages in some cases. Taking into consideration these services, the Special Purpose Company of the manufacturer of weapons shall pay to the Company 1 the amount of US \$ 1.22 million in equal instalments of US \$ 5.5 million during next four months.

At the same time, the Company 1 concludes with the Company 2 the sub-contract on services delivery under which the Company 2 undertakes to act on behalf of the Company 1 in a certain part of the world. The clauses hereof are similar to the clauses of the Master Agreement concluded between the Company 1 and the Company-manufacturer of weapons. Taking into consideration provision of these services, the Company 1 agrees to pay to the Company 2 the amount of US \$ 20 million (it means that the mediator will earn US \$ 2 million). The contracts are signed and funds are transferred through the bank accounts as specified herein. In cases if the bank employee has any question concerning funds transfer, the contract should be submitted for verification of such transfers. These two contracts should be seen as original as they will be certified by the Swiss law firm. The bank employee feels comfortable, taking into consideration stability of services delivery as specified in the Master Agreement and sub-contract on services delivery. Taking into consideration all these factors, the bank employee is sure that such funds transfer is direct and clear. Four months pass and as the last payment is credited to the account of the Minister of defense, he will earn revenue in the amount of US \$ 20 million.

Public bribe was disguised as a range of payments for provision of consulting services. The action of bribery taking of the Minister of Defense was disguised through the structure of ownership and bank accounts without which such bribe could not be paid. At this, the banking sector was used for corruption.

Activity on distribution and allocation is not given in such scheme. Funds allocation is not required as funds have been already credited to the account of the Special Purpose Entity (SPV) prior to bribery taking; there is no allocation as the activity will be performed later when funds will be credited to the accounts of the Minister of Defense as revenues received from fraudulent activities. Such scheme allows two persons, both the Company-manufacturer of weapons and the Minister of Defense, to move away from the structure of a crime.

Using this scheme, the Minister of Defense moved him away from bribery taking. However, he further decided to spend a half of the amount for purchase of hotel in Geneva. Revenue from hotel activity was distributed among the attorneys as dividends and the attorneys transferred funds for possession of the Minister. The Minister had never directly received revenues from the attorneys. In turn, they paid for education of the Minister's children in private schools, flight hours of charters, credit cards. The Minister's friends visited the hotel while making shopping tours in trading centers and watches in Geneva and visited their private bankers. Further, the hotel was used as security for credit for ski cottage in Verbier and 92-inches yacht at rest in Monaco.

The Minister, his family and friends visited the cottage in winter and yacht in summer at any time.

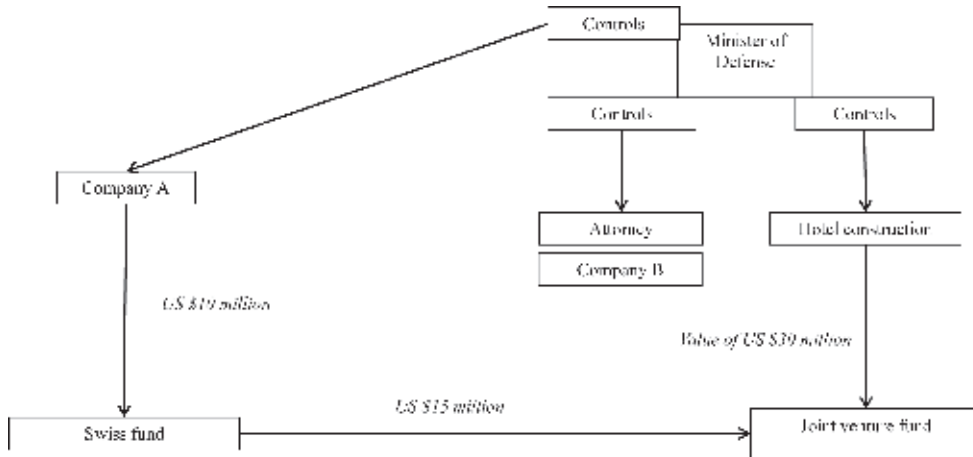
The Minister decided to invest other part of bribe into the hedge fund in Switzerland. Return on investments is amazing and proves the old saying "tis money that begets money", thus, the amount of US \$ 10 million was formed into the amount of US \$ 15 million in 3 years. The Minister of Defense instructed his counsellors that the manager of the Swiss fund should not pay US \$ 15 million to the structure of the original investment, but should pay to other company owned by the attorney acted on behalf of the Minister. Further, this amount of US \$ 15 million was invested by this company into joint venture fund that was awarded with the contract on construction of large hotel and trading complex in its hometown due to powers of the Minister. As a result, the Minister's investments into the project company were doubled and, thus, the situation is going on.

It lead to the following: while holding its position, the Minister transferred hundreds of millions to the bank accounts and other forms of assets owned by him through complex structures controlled by the professional mediators, private bankers, providers of corporate services.

Approach of all parties to collusion is characterized with self-abasement generated from fear of losing highly profitable business relationship with a person having important political and, accordingly, commercial influence.

The given example takes up the question whether involvement of banks in the commitment of a crime could be avoided or not. There are two conditions that banks should take into consideration. Firstly, the bank should know that the agreements on consulting services delivery to be provided by the company are characterized with high risk and, thus, the bank should verify legitimacy of any commercial justification. Secondly, combination of two agreements on non-material services

delivery (difficult to confirm) of the politically exposed person and the mediator should be a sign of a high risk. Upon the implementation of the risk-focused approach, these aspects would have been found and it would have finally prevented of the flow of illegally received funds.





### 3. Standard schemes of money laundering by types of activity

Corruption-related crimes have become especially urgent and are subject to constant attention from the side of governments and international organizations.

In turn, the State Financial Monitoring Service takes special attention to those financial investigations on money laundering.

To determine the level of custom risk concerning any potential involvement into the corruption actions, it should be considered for the sphere of activity where such party acts. Corruption may take place in any economic sector of any country. At the same time, certain economic sectors are sensitive to the corruption schemes.

According to the financial investigations conducted by the State Financial Monitoring Service, standard schemes of money laundering (unlawful enrichment, bribery taking or undue benefit) received in the most risk spheres of activity by the officials and affiliated persons or by the persons authorized to perform the functions of government or self-regulating authorities were summarized.

#### 3.1. Money laundering from the corruption actions in the defense-industrial sector

Realization of anti-terrorist operations in eastern Ukraine significantly increases the volume of costs for reforming and development of the defense-industrial sector of the country that, in turn, increases the risk of taking any corruption actions in this sector.

Thus, for example, the tendering process could be less transparent due to the fact that the subject of procurement/works is mostly confidential, as it concerns national security and its confidentiality is protected by the legislative and statutory requirements.

It should also be noted that state procurement in the defense-industrial sector is mainly not addressed to the providers or manufacturer of services, but conducted through a chain of mediators that, in turn, significantly increases the value of tender proposal as “the service value” for government relations of certain entities is influenced by profitability established by each party.

#### The example of embezzlement of budget resources for provision of fictive services on psychological adjustment of anti-terrorist operation members

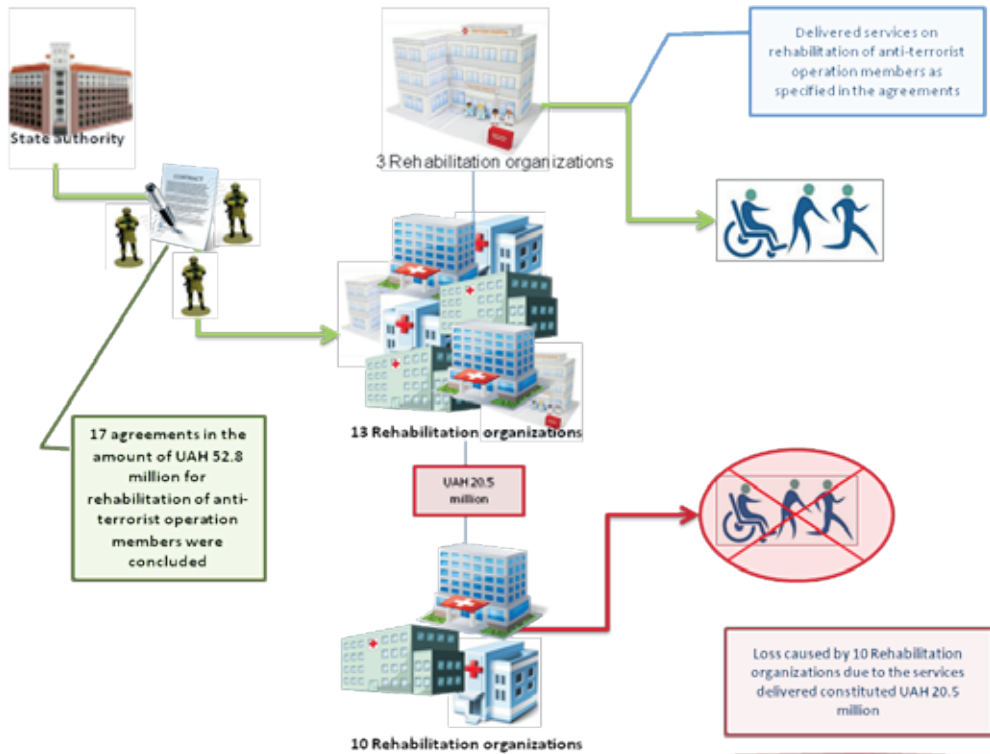
The state audit authority has found the scheme of embezzlement of budget resources for measures of psychological adjustment of anti-terrorist operation members with the potential enrichment of the officials of **the State Authority** resulted in loss of state budget in the amount of **UAH 20.5 million**.

Thus, **the State Authority** concluded 17 agreements with **13 Rehabilitation Organizations** in the total amount of **UAH 52.8 million**.

At this, only 3 from **13 Rehabilitation Organizations** provided services on psychological adjustment of anti-terrorist operation members as specified in the agreements. In turn, 10 remaining organizations had no relevant conditions and qualified personnel for provision of services specified in the agreements.

At the moment, all case files of the violations found and investigation outcomes concerning improper use of budget resources for psychological adjustment and sanatorium-resort therapy of anti-terrorist operation members are addressed to the law enforcement authorities.

The law enforcement authority carries out a criminal proceeding.



**The example of money laundering by the officials of the defense-industrial sector enterprises**

The law enforcement authority has found out the scheme of illegal enrichment of the officials of the defense-industrial sector.

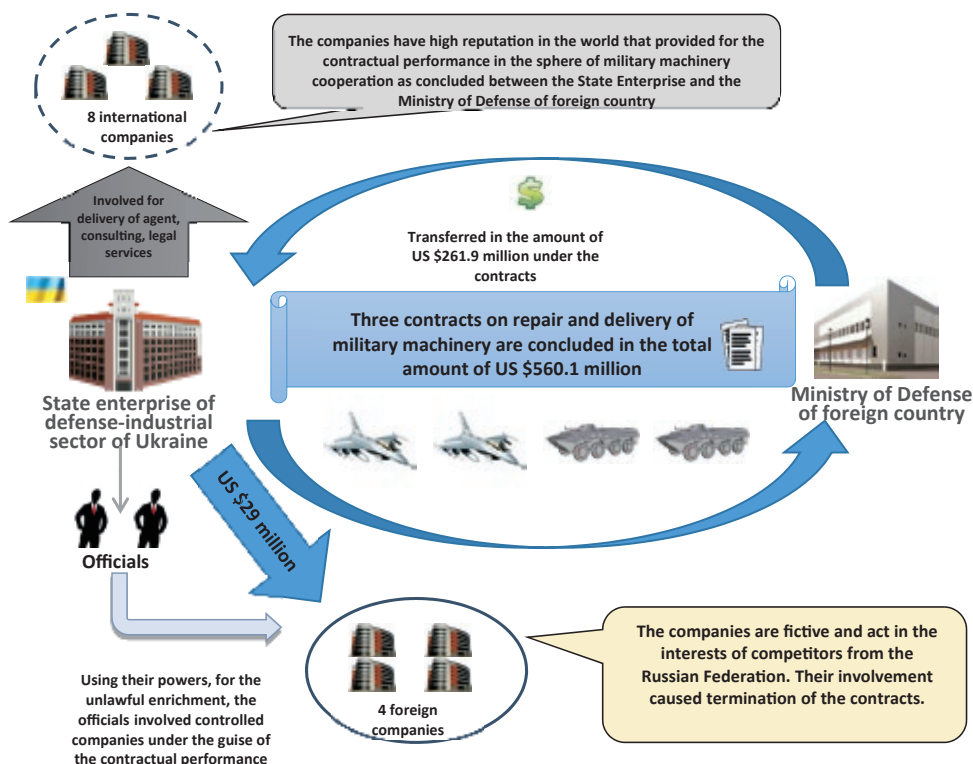
**The State Enterprise** operating in the military industry and **the Ministry of Defense of foreign country** concluded three contracts on repair and delivery of military machinery in the total amount of **US \$ 560.1 million**.

Under the given contracts, **the State Enterprise** received funds in the amount of **US \$ 261.9 million** and in pursuance of the contracts manufactured and partially delivered military machinery in favor of foreign country.

**The State Enterprise** involved international companies for provision of agent, consulting, legal and other services.

For embezzlement of funds under the guise of the contractual performance, the officials of **the State Enterprise** also involved four controlled foreign shell companies to the accounts of which **the State Enterprise** transferred **US \$ 29.0 million**. At this, the mentioned companies failed to deliver any services and acted in the interests of competitors of **the State Enterprise** from the Russian Federation. Their involvement caused termination of the contracts.

The law enforcement authority carries out a criminal proceeding.



### The example of embezzlement of funds of the state enterprise

The law enforcement authority has found the crime as specified by part 5 Article 191 "Appropriation, embezzlement of property or distress through abuse of official position" of the Criminal

Code of Ukraine concerning the official of **the State Enterprise "Z"** and the director of the commercial organization that appropriated budget funds in the amount of **UAH 23.1 million** through conclusion of fictive agreements; these funds were transferred in form of payment for undelivered accessories for military machinery.

### The example of money laundering involving the companies controlled by the official of state enterprise

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According to the financial investigation conducted by the State Financial Monitoring Service, there has been the scheme of money laundering by the official of state enterprise through the controlled companies.

**The State Enterprise** of the defense industry signed with the **Company-non-resident A** the contract on machinery delivery to the customs territory of Ukraine.

**The Company-non-resident A** is registered within the territory of the Republic of Cyprus at the address of mass registration, the final beneficiary of the company is the **Citizen A** receiving a salary at **the State Enterprise**.

**The Company-non-resident A** opened the account in banking institution of Estonia where **the State Enterprise** transferred funds in the total amount of **UAH 44.6 million** (US \$ 2.52 million and EUR 0.02 million).

The real supplier of vehicles to the customs territory of Ukraine on the total value of **US \$ 0.84 million** was **the Enterprise-Exporter** located within the territory of the Republic of Belarus that received from **the Company-non-resident A** only **US \$ 0.12 million** by invoice.

The large portion of funds received by **the Company-non-resident A** from **the State Enterprise** was further credited to the accounts of 10 legal entities and 2 natural persons.

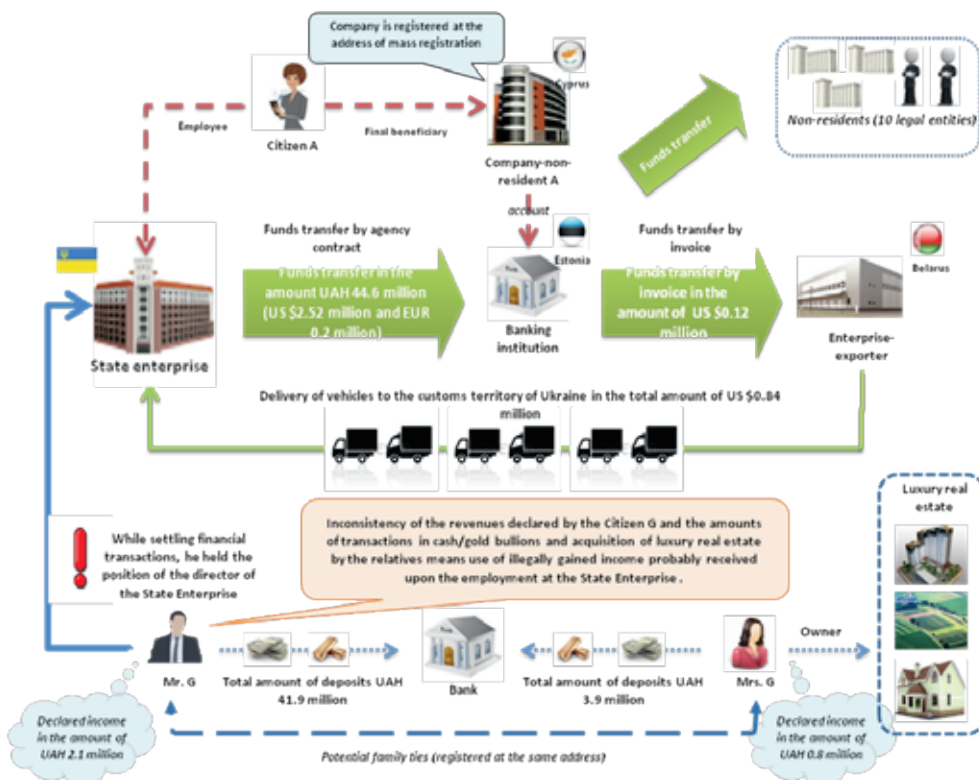
The implementation of the given scheme of settling financial transactions was made within the term when **Mr. G** was the director of **the State Enterprise**.

Concerning **Mr. G**, it is known that he declared revenues in the amount of **UAH 2.1 million**, at this, the total amount of funds credited to the bank accounts (in cash and bank metals/gold bullions) constituted **UAH 41.9 million**. It has been found that **Mr. G** was registered at the same address with **Mrs. G** (potential family ties) that declared revenues in the amount of **UAH 0.8 million**, at this, the total amount of funds credited to the bank accounts (in cash and bank metals/gold bullions) constituted **UAH 3.9 million**. In addition, **Mrs. G** is an owner of a large number of real estate in Kyiv.

Inconsistency of the revenues declared by **Mr. G** and the amounts of transactions on cash/gold and acquisition of luxury real estate by the relatives means use of illegally gained income probably received during the employment at **the State Enterprise**.

The law enforcement authority carries out a criminal proceeding.





### 3.2. Money laundering in the energy supply industry

The history of mass corruption in the Ukrainian energy supply industry numbers in decades. Absence of market competition, transparent regulation and dependency on the industrial magnates-monopolists make the energy supply industry very sensitive to the corruption actions.

Under the conditions of lack of reforms, a range of the officials in Ukraine received revenues over a number of years controlling the energy power special interests and, up to the date, they continue to control policy in the energy supply industry having representatives in the Verkhovna Rada. Sectors of gas and coal recovery, production and supply of energy, heating energy consumption show interests of corporations; activity of regulating authorities has no appropriate legislation for recognition of their dependency on influence of the political figures.

Besides, the corrupted Ukrainian energy supply state sector has been used by the Russian Federation for a number of years for blackmail and strengthen of own influence in Ukraine.

The most non-transparent spheres in the energy supply market in Ukraine to be used in the corruption schemes are state procurement and transfer pricing. Besides, the source of money laundering in the sphere of the Ukrainian energy supply industry is the world-wide schemes of commercial and non-commercial use of energy supplies between the price of import energy supplies and the discount prices for the population.

#### The example of money laundering of state enterprise embezzled by the companies controlled by the people's deputy of Ukraine

According to the financial investigation conducted, the State Financial Monitoring Service has found the facts of embezzlement of budget resources with the involvement of the company-non-resident controlled by the people's deputy of Ukraine.

Thus, **the State Enterprise** and **the Company-non-resident A** (Austria) concluded the contract and a range of additional agreements on sales of several thousands of tons of raw material to **the State Enterprise** for 4 years. In turn, **the Austrian Company-non-resident A** was controlled **by the people's deputy of Ukraine**. **The Company-non-resident A** was not a manufacturer of raw material and had no methods of transportation, i. e. it acted as the mediator only. For the contractual performance, **the State Enterprise** transferred **US \$ 75 million** in favor of **the Company-non-resident A**.

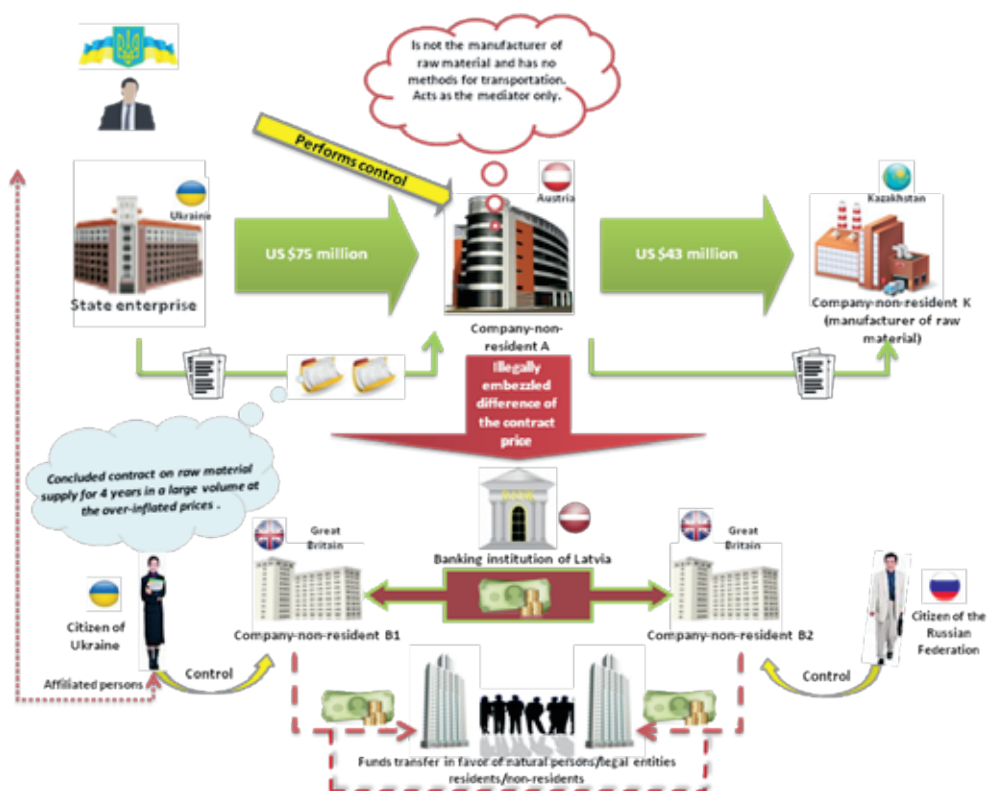
Further, **the Company-non-resident A** concluded the agreement with the existing manufacturer and supplier of raw material – **the Company-non-resident K** (Kazakhstan). However, the price of raw material hereunder was lower than in contracts and agreements between **the Company-non-resident A** and **the State Enterprise**, and the scope of raw material supply was much lower.

A portion of funds received from **the State Enterprise** in the amount of **US \$ 43 million** was transferred by the **Company-non-resident A** in favor of the **Kazakh Company-non-resident K**, other portion was transferred to the **Latvian accounts of two Companies-non-residents B1 and B2** (Great Britain) controlled by the citizens of the Russian Federation and Ukraine. Based on further investigations,

it has been found that **the Citizen of Ukraine** controlled by the **Company-non-resident B1** and the people's deputy of Ukraine were the **affiliated persons**. Thus, the **Company-non-resident A** embezzled funds due to difference of the contract price.

Further, funds were transferred from the Latvian accounts of the British **Companies-non-residents B1 and B2** in favor of a range of **natural persons** and **legal entities**, both **residents and non-residents** of Ukraine.

The law enforcement authority carries out a criminal proceeding.



### The example of money laundering by the national public figure of Ukraine as a bribe

According to the investigation conducted by the State Financial Monitoring Service together with the law enforcement authority, there has been the scheme of money laundering by the national public figure of Ukraine as a bribe.

Two **Companies-non-residents A** and **B** concluded the contract on cooperation under which **the Company-non-resident A** should be obliged to assist the **Company-non-resident B** in sales of equipment within the territory of Ukraine for a fee.

The beneficiary owner of **the Company-non-resident A** is **the Citizen A** at that moment holding the position of the people’s deputy of Ukraine.

The state enterprise of Ukraine in the energy supply industry purchased equipment from the **Company-non-resident** for budget resources.

**The Company-non-resident A** received funds in the amount of **EUR 2.8 million** transferred under the cooperation agreement on distribution of goods at the market of Ukraine. **The Company-non-resident A** transferred funds in the amount of **US \$ 0.8 million** in favor of the **Company-non-resident C**.

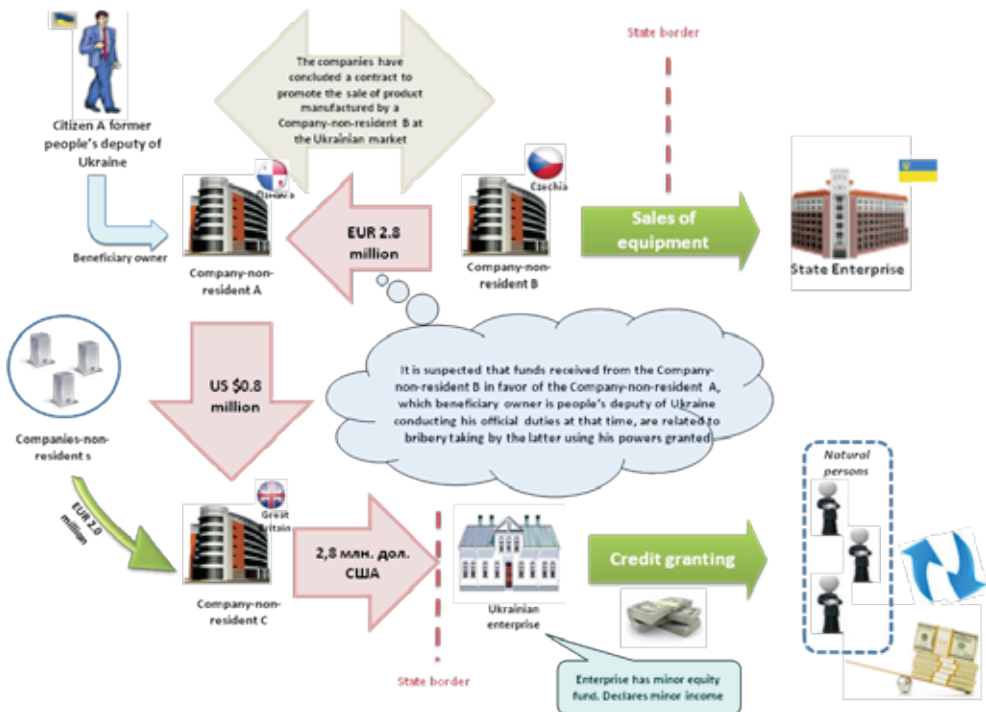
At the same date, **the Company-non-resident C** credited these funds in favor of **the Ukrainian enterprise**.

At this, the enterprise has minor equity capital, declares minor income.

Further, the mentioned funds were converted into cash through granting credits to the natural persons.

Thus, it is suspected that funds received from **the Company-non-resident B** in favor of **the Company-non-resident A**, which beneficiary owner is the people’s deputy of Ukraine, are related to bribery taking by the latter.

The law enforcement authority carries out a criminal proceeding.





### 3.3. Money laundering in the mining industry

In Ukraine there is a mass corruption in the industry of natural resources recovery and mining, such as coal, wood substances, amber, sand and black soil. This list is not comprehensive and depends on the certain region of the country, natural resources.

Extraction of mineral resources means use of various schemes allows embezzling of mineral resources, reducing liability for value added tax, income tax and payment for consumption.

Satisfaction of needs of Ukraine in mineral raw materials and energy supplies due to import and increase in prices for such products caused criminal activity at the market of mineral and energy resources.

Problem income received from sales of mineral resources often causes weakening of political responsibility, does not provide economic growth, human wellbeing necessary for the precedent conditions of responsible society and may give opportunities for the corruption growth.

Income level from sales of mineral resources many times exceeds revenues received in any other economic sector.

#### The example of money laundering by the officials holding chairs of state in form of the undue benefit

According to the investigation conducted by the State Financial Monitoring Service, there has been the scheme showing money laundering by the officials holding chairs of state in form of the undue benefit.

It has been found that the group of persons holding chairs of state established a criminal entity for their personal enrichment. Using powers imposed and official position, the mentioned persons sold natural gas produced by **the Controlled Enterprise** under the agreements on co-operation with **the Gas Producing Enterprise** state-owned at the prices much lower than those at the natural gas market.

Further, gas produced was sold by the enterprise of real economic sector at the market price. Revenues received as a difference of funds from gas purchase at a bargain price and further sales at the market price were transferred by **the Controlled Enterprises** as transit through a range of the accounts of **the second group of enterprises**, being fictive. Funds from the accounts of the last group were partially withdrawn in cash in the total amount of **UAH 229.2 million**.

The law enforcement authority carries out a criminal proceeding.



**The example of receiving surplus profit by the company controlled by the national public figure of Ukraine**

According to the investigation conducted by the State Financial Monitoring Service, there has been the scheme aimed at receiving surplus profit by the company controlled by the national public figure of Ukraine.

Funds from two **Companies-non-residents A** and **B** in the amount of **US \$ 42.0 million** and **US \$ 9.4 million**, accordingly, were credited to the account of **the State Enterprise**. The mentioned transfers were made according to the foreign economic agreements concerning purchase of products of **the State Enterprise**. At this, product value under the agreements is much lower than the market price.

In addition, according to the agreements, the offtakers of products are those enterprises located in different countries. Thus, **the Companies-non-residents A** and **B** act only as the mediators controlling financial flows.

It has been found that **the Citizen M**, being the people’s deputy of Ukraine, was related to the given scheme.

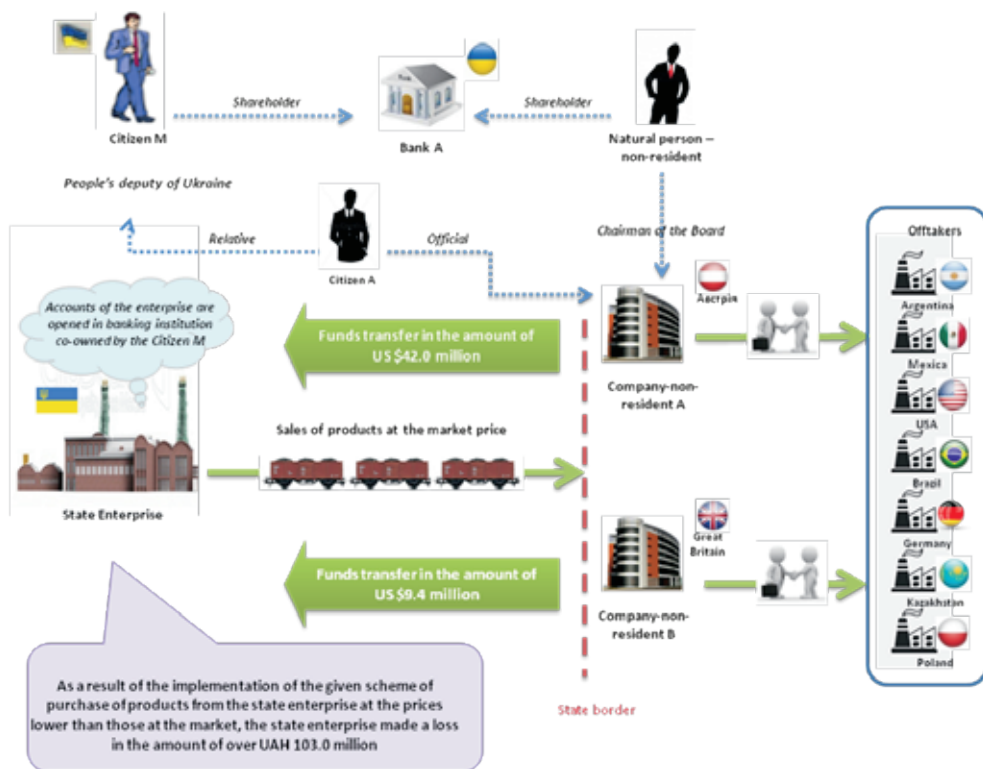
**The Citizen M** is affiliated to the **Company-non-resident A** through its relative– **the Citizen A**, being the official of **the Company-non-resident A**. The Chairman of the Board of the **Company-non-resident A** is **the natural person-non-resident**, being the shareholder of **the Bank A** together with **the Citizen M**.

It is known that the accounts of **the State Enterprise** were opened in **the Bank A**, co-owned by **the Citizen M** and **the natural person-non-resident**.

The above mentioned means the involvement of the national public figure into formation of the corruption scheme related to infliction of damages to the state enterprise due to delivery of products at the price lower than its market value to the controlled enterprise with its further sales at the market prices.

As a result of the implementation of the given scheme, the state enterprise made a loss in the amount of over **UAH 103.0 million**.

The law enforcement authority carries out a criminal proceeding.



### Example of money laundering as a result of bribery taking for execution of permits

The law enforcement authority carries out a proceeding when there has been corruption activity of the group of officials managed by the first deputy government executive that received funds in the amount of **US \$ 80,000** for assistance to the entity in execution of permits for mining.

Based on the inspections conducted, funds in the amount of **US \$ 315,000**, jewelry, icons, gold bullions, collectible coins, antiques, cold steel, military award pins of Hitlerite Germany of the Second World War, ancient books; firearms with ammunition; official documents on bank deposits in the amount of several millions UAH, and "black "accounts on disguised expenses were found and seized from these persons.

The law enforcement authority carries out a criminal proceeding.



### 3.4. Money laundering in the health protection industry

Corruption penetrates into all living environment of the society, including in the health protection industry.

Every year the country losses big money for maintenance of medical institutions, purchase of equipment and drug products that “force” unfair public officers and heads of state organizations to be involved in “allocation” of budget resources.

It is not uncommon when the winning bidder of the contract on reconstruction or major repair of the medical institution is the company not performing construction or repair works, having no production capacities and hired personnel. At the same time, budget sources are credited to the accounts of the mentioned company, a portion of them is to be embezzled, and the remaining amount is to be transferred to the existing companies under the sub-contract that directly execute construction or repair works. A portion of funds owned by the winning bidder is used as a “fee” by those persons “assisted” in receiving the budget proposal.

A significant amount of the corruption flows is accumulated in the pharmaceutical industry as various illegal expenses in this sphere are wide spread phenomena (fabrication, forgery of documents).

#### The example of money laundering by the officials in form of the undue benefit

According to the investigation conducted by the State Financial Monitoring Service, there has been the scheme of money laundering by the officials as the undue benefit.

According to the win in the competitive tendering of the Ministry of Health of Ukraine, the contract with **the Enterprise B** on delivery of drug products and medical products was signed and funds in the amount **UAH 291.5 million** were further transferred to the account of **the Enterprise B**.

At this, during the term specified in the contract, actual delivery of drug products was not performed.

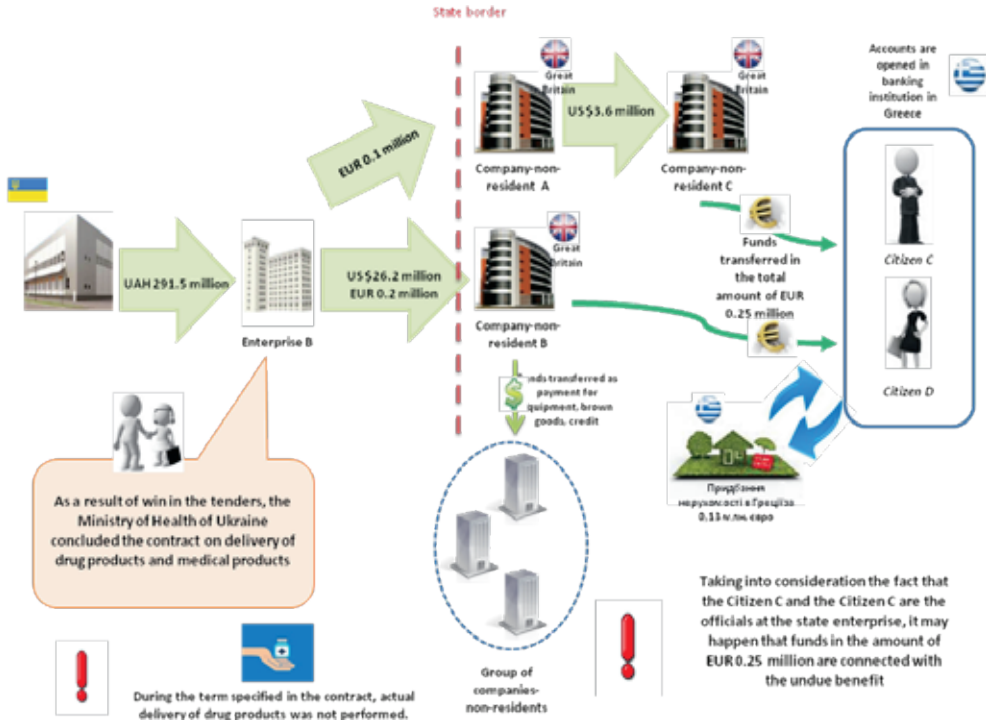
All funds received were converted and transferred in favor of **the Company-non-resident A** in the amount of **US \$ 26.2 million** and **EUR 0.24 million** and in favor of **the Company-non-resident B** in the amount of **EUR 0.1 million**.

Further, **the Company-non-resident A** transferred funds to the group of companies-non-residents as payment for building and electrical equipment, brown goods, credit, including to the account of **the Company-non-resident C** in the total amount of **US \$ 3.6 million**.

According to the financial intelligence unit of foreign country, **the Companies non-residents B** and **C** transferred funds in the total amount of **EUR 0.25 million** to the accounts of the citizens of Ukraine – **the Citizen C** and **the Citizen D** opened in banking institution in Greece. Further, a large portion of funds received in the amount of **EUR 0.13 million** was addressed to the mentioned persons for purchase of real estate within the territory of Greece.

Taking into consideration the fact that **the Citizen C** and **the Citizen D** are the officials of the state enterprise of Ukraine, it may happen that funds in the amount of **EUR 0.25 million** is connected with receiving of the undue benefit.

The law enforcement authority carries out a criminal proceeding.



### 3.5. Money laundering from the corruption actions in the sphere of development, construction and operation of the infrastructure projects

Significant state expenses on the infrastructure projects (development of railway, aircraft, maritime, motor and local transport, roadway construction) promote corruption in this sphere.

This sector of expenses has peculiarities including the scope of works, necessity of complex delivery schemes, involvement of a large number of legal entities, that, in general, additionally motivate corruption and allows disguising of the corruption flows in the large processes.

#### The example of embezzlement of budget resources granted as a credit against security of the Government of Ukraine and their laundering

According to the investigation conducted by the State Financial Monitoring Service, there has been the scheme of embezzlement of budget resources granted as a credit against security of the Government of Ukraine and their further laundering.

For execution of the works on construction of railway passenger service, **the State Enterprise** and **the Company-non-resident** concluded the agreement.

In pursuance of the credit agreement, the amount of **US \$ 14.89 million** (equal to **UAH 119.04 million**) was transferred to the account of **the State Enterprise**. Further, funds received were transferred by two installments to the multicurrency account of **the State Enterprise** opened in the **Banking institution M**.

Further, credit funds were used not as intended. A portion of funds was transferred through a period of time to the deposit account opened in the **Banking institution M**, with further return of funds transferred and interest to the current account opened in the **Banking institution M**. Other portion of credit funds was transferred to the current account in the **Banking institution M**.

Thus, after currency conversion, the amount of **UAH 165.78 million** was accumulated at the current account of **the State Enterprise** opened in the **Banking institution M**.

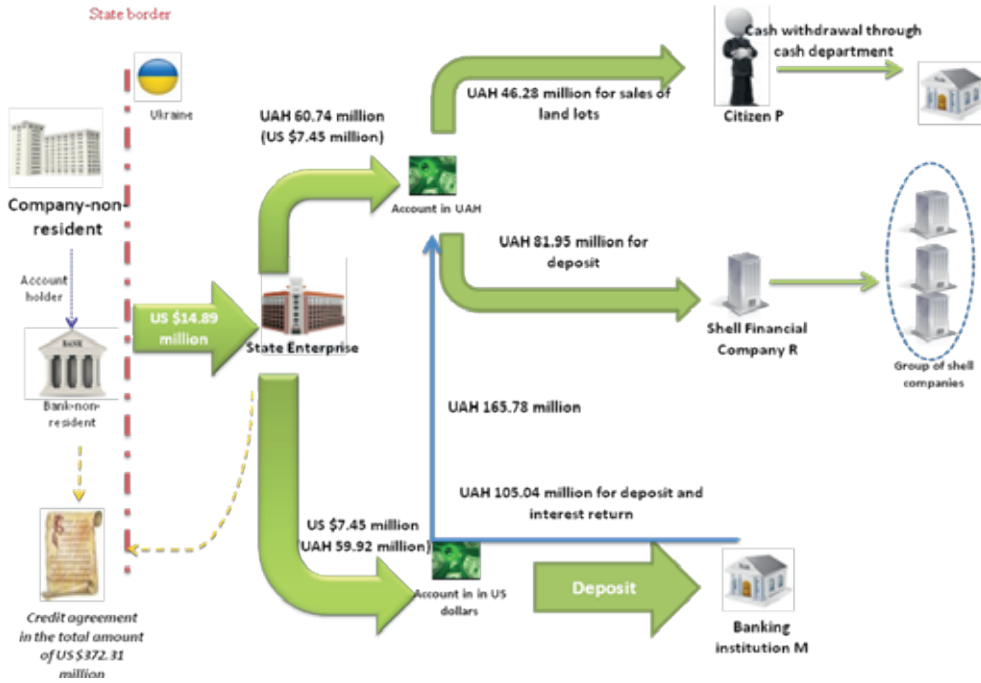
Upon investigation, it has been found that a portion of funds in the amount of **UAH 81.95 million** was credited to the deposit account of **the Financial Company R** that, in turn, transferred them in favor of a range of legal entities. The **Financial Company R** and legal entities in favor of which funds were further transferred appeared to be fictive.

A portion of funds in the amount of **UAH 46.28 million** was transferred to the account of the natural person **the Citizen P** as payment for acquisition of land lots intended for railway passenger service construction at the inflated price. Further, **the Citizen P** withdrew in cash all funds received.

Thus, taking into consideration the fact of non-performance of railway passenger service construction, the mentioned may mean formation of the corruption scheme connected with embezzlement of funds of **the State Enterprise** and their further laundering.

**The State Enterprise failed to return the credit amount to the Company-non-resident.**

The law enforcement authority carries out a criminal proceeding.



**The example of embezzlement of funds by state enterprises and further laundering**

According to the investigation conducted by the State Financial Monitoring Service, there has been the scheme under which funds as payment for the spare car parts were credited by 8 state enterprises to the account of **the Company T** opened in **the Bank Y**. The total amount of funds transferred constituted **UAH 3.8 million**. Based on the price analysis, the price of spare car parts was **inflated**.

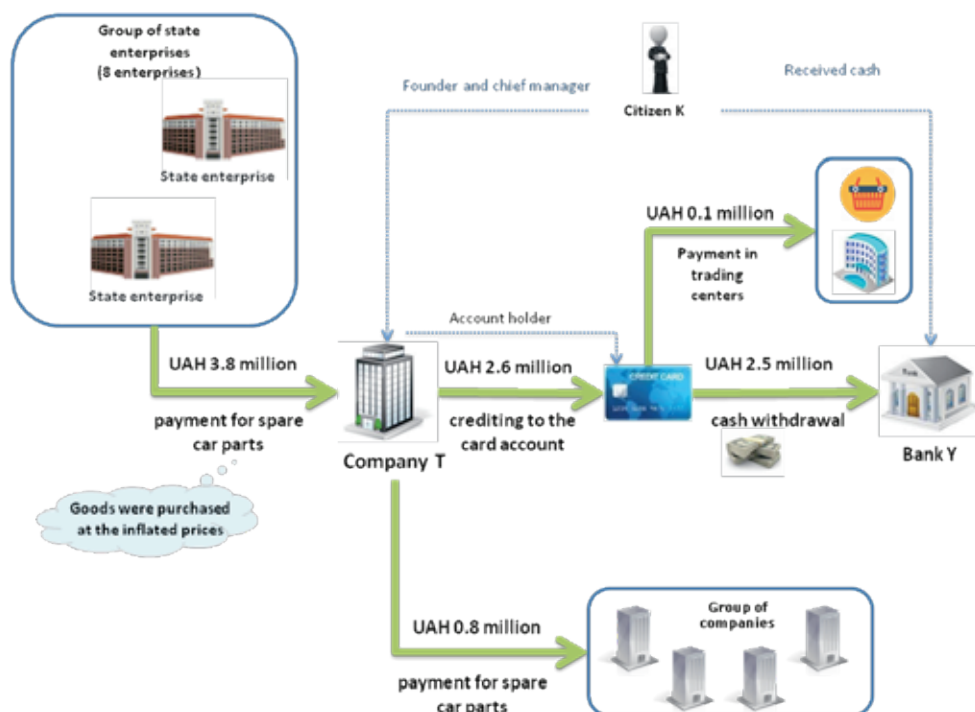
Funds of **the Company T** in the amount of **UAH 2.6 million** were transferred to the corporate card account. Further, the amount of **UAH 2.5 million** was withdrawn from the card account in cash by the founder and chief manager of **the Company T** – **the Citizen K**. Besides, a portion of funds in the amount of **UAH 0.1 million** was addressed for payment in trading centers and hotels.

At this, the suppliers transferred **UAH 0.8 million** only for purchase of spare car parts.

**The Company T** was registered within 20 days from the date of the note on tender of state procurement by state enterprises.

Based on these facts, the law enforcement authority carries out an investigation.





### The example of money laundering received from the state enterprise

According to the financial investigation conducted, the State Financial Monitoring Service has found the scheme of illegal embezzlement of funds of state enterprise through artificial rising of price levels by the supplier.

In collusion with the representatives of **the Company I**, the officials of the State Enterprise formed artificial conditions for win of the tender on procurement from **the Company I** controlled by **the Citizen Tz** at prices exceeding the market prices for the similar products. The expected price for procurement of the products by the state enterprise was defined in the amount of **UAH 39.5 million**.

Requests for products supply were submitted by three enterprises – **Private Enterprise A**, **Company B** and **Company I**. At this, only **Private Enterprise A** appeared to be the real market player and offered the lowest price – **UAH 47.4 million**.

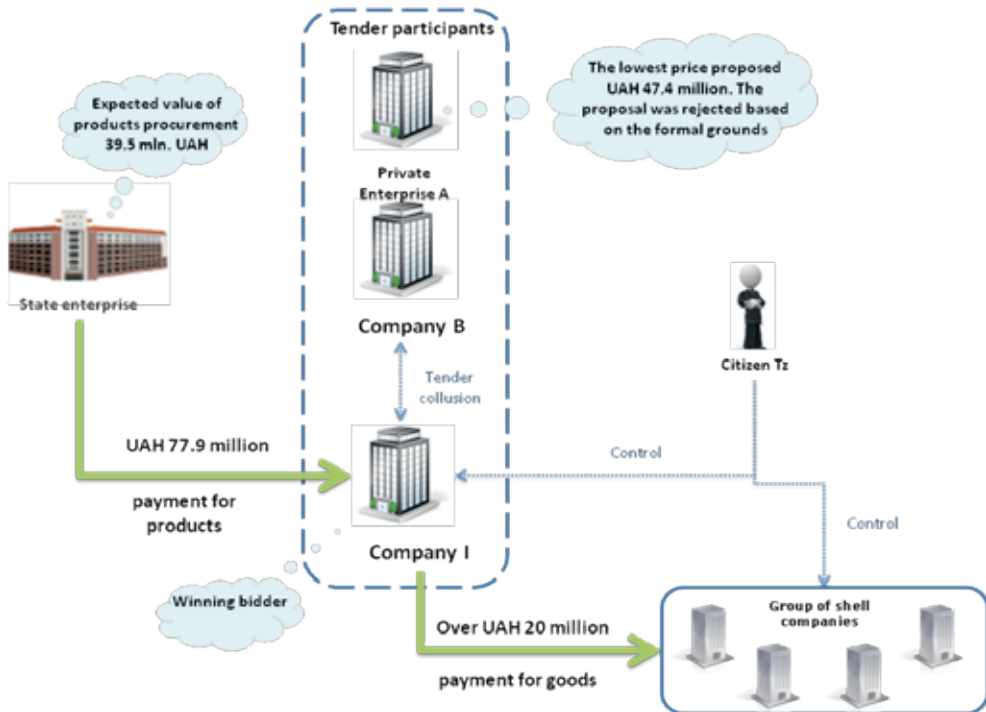
Thus, the proposal was rejected by the tender committee on the formal grounds.

Two other players (**Company I** and **Company B**), being in tender collusion, proposed the price for products supply in the amount of **UAH 77.9 million** and **UAH 82.5 million**, accordingly. As a result, the **Company I** won the tender of open procurement with the proposal of **UAH 77.9 million**.

Based on the inspections conducted, it has been found that the price for the products supplied by **the Company I** was inflated up to **UAH 20 million**.

Funds received were transferred by the director of **the Company I** in favor of the group of fictive enterprises affiliated to **the Citizen Tz**.

Based on these facts, the law enforcement authority carries out an investigation.



### 3.6. Money laundering from the corruption actions in the state management industry

Corruption in the sphere of state management with the conditions of appearance, growth and expansion threatens the efficiency of state management, in general, and, in the worst possible case, threatens the mechanisms of democratic management and the basic principles of state existence nowadays.

Corruption in the sphere of state management may be used and is actually used at the macro level for government relations of the oligarchic clans, crime syndicate as the tool for increasing assets or creating conditions for their reallocation.

Under condition of absence of transparency and accounting for population and society among the government authorities, it is easy to create conditions for expending corruption and, thus, supporting the corrupted officials and their affiliated business structures, other mediators, auditors, accountants, lawyers, skill journalists and unfair mass media.

The most spread phenomenon of corruption in the sphere of state management is protection – assignment of the employees based on family ties, citizenship, loyalty and intimate relations.

#### The example of allegation of using funds received from the corruption actions

According to the investigation conducted by the State Financial Monitoring Service, there have been found allegations concerning money laundering resulted from the corruption actions by the law enforcement officer.

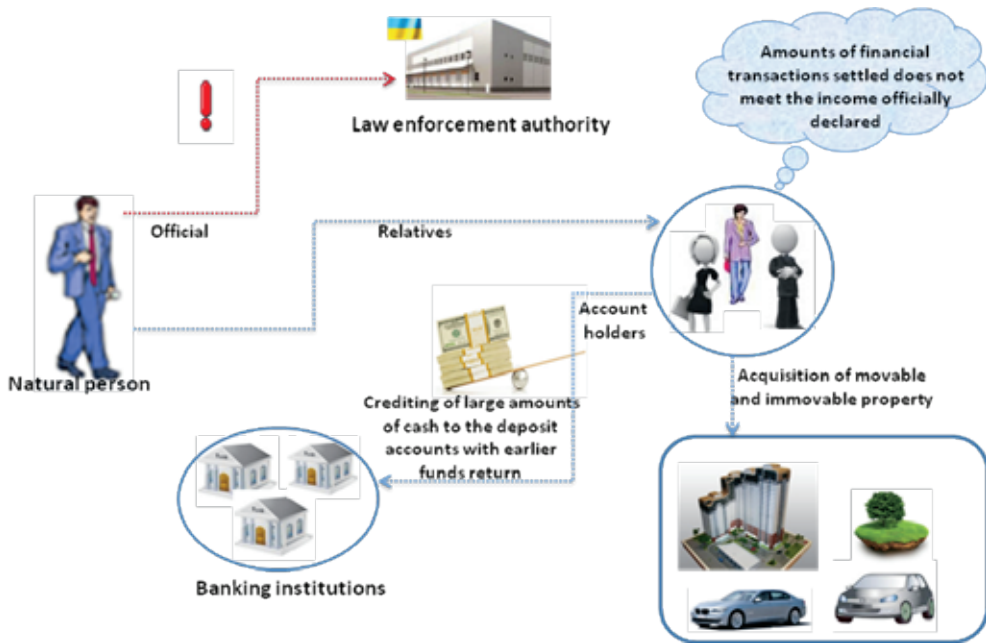
During 2003-2015 **the law enforcement officer** and his relatives received the minor amount of income. At the same time, the relatives of this official not once, but repeatedly credited the substantial amounts of funds to own deposit accounts for a short-term period with further withdrawal in cash.

His relatives also purchased cars, luxury apartments, non-residential premises and land lots.

The amount of financial transactions settled by the relatives fails to meet the income officially declared.

It is suspected that the financial transactions settled by the relatives may be related to use of illegally gained income by the law enforcement officer.

The law enforcement authority carries out a criminal proceeding.



### The example of money laundering by the national public figure

According to the investigation conducted by the State Financial Monitoring Service, there has been the scheme of money laundering by the national public figure.

**The Citizen K** invested into purchase of property in London (Great Britain) in the amount of **£825,000**. At this, the buyers used the uncommon commercial transaction and complex way of property acquisition that may potentially mean money laundering.

**The Citizen K**, being the people's deputy of Ukraine, received funds to its own account from two natural persons in the total amount of **UAH 2.6 million** as payment for corporate rights to the television and radio broadcasting company.

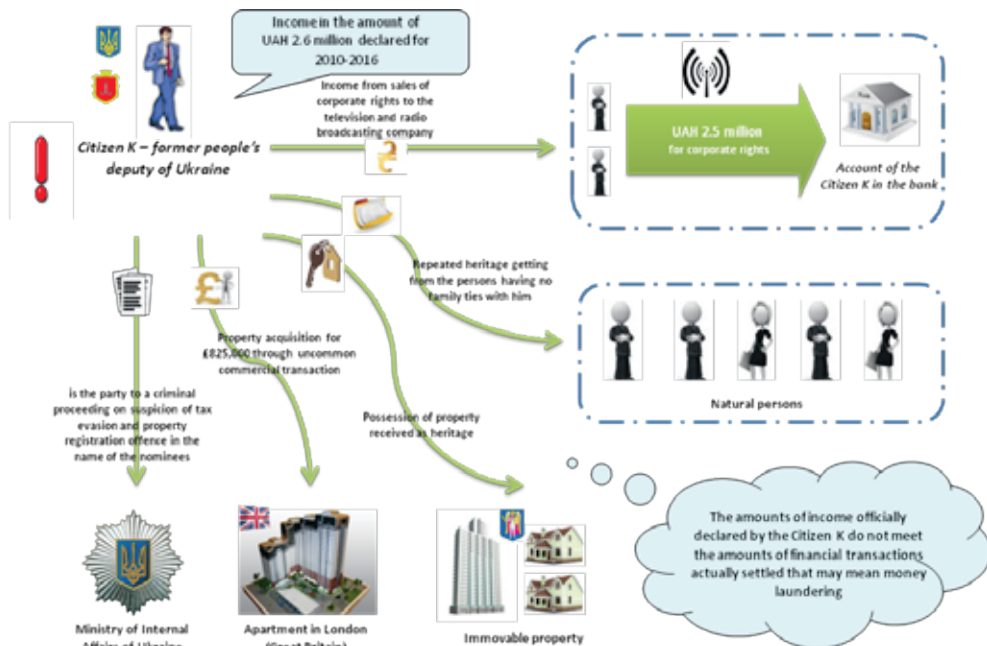
While holding official positions, **the Citizen K** repeatedly received heritage from the natural persons having no family ties with him and was the party to a criminal proceeding on suspicion of tax evasion and property registration offence in the name of the nominees.

For 2010-2016 **the Citizen K** declared income in the amount of **UAH 2.6 million**, at this, **UAH 2 million** – income received as heritage (gift) from the persons that are not family members of the first degree relationship.

The amounts of income officially declared by **the Citizen K** do not meet the amounts of financial transactions actually settled that may mean money laundering.



The law enforcement authority carries out a criminal proceeding.



### 3.7. Common factors of the corruption-related crimes. Instruments and ways of money laundering

In general, the corruptive flows penetrate all economic sectors of the country. Corruption causes significant losses for the country. Such losses may have financial, qualitative and political elements.

The common factors that increase interest to commitment of the corruption-related crimes are as follows:

- embezzlement of budget resources and bribery taking are mainly performed in those sectors of economic that are strategically important for the country (defense and energy industry, health protection, state management) as large cash flows are allocated there;
- large amount of funds for project implementation at the state and local levels at cost of state or local budgets;
- complex mechanism of defining the value of goods and services, regular changes in market conditions for definition of the actual price of goods purchased;
- sphere of state procurement is non-transparent and characterized with high competition that may lead to the conditions of the backstage collusion.

In the process of this typological study, there have been found the following common tools of money laundering:

- fictive services;
- involvement of the affiliated persons for fictive services delivery;
- prepayment for goods and services to the controlled persons with further non-delivery/ non-performance;
- underpricing for goods value by the state enterprise upon sales to the companies-mediators for income accumulation;
- conclusion of patently illegal agreements on purchase of goods at the prices established for social needs with further sales;
- involvement of fictive enterprises;
- "trade" with state services on issuance/execution of permits;
- use of bank accounts opened without the territory of Ukraine;
- rejection of competitive tender membership applications in favor of the controlled companies that propose higher prices.

The most spread ways of money laundering include the following:

- involvement of those persons that do not have any family ties with the "corruptionist", but are affiliated (extended family, drivers, assistants);
- bribery taking in cash with further conversion into non-cash funds;
- receipt of corruption-related revenue in Ukraine, its "whitening", legalization, certification abroad;
- repeated receipt of heritage from the persons not connected with family ties;
- acquisition of property abroad;
- purchase of corporate rights.

## Conclusion

The given typological study is based on practical facts of close cooperation of the process of money laundering due to the corruption element. This situation adversely influences the economic level of any country and, namely, Ukraine.

According to the international studies in the sphere of anti-corruption policy, negative affect from the corruption actions influences on all levels of economic of the country, thus, reducing the volume of private investments, distributively influencing on quantity and quality of state infrastructure, reducing taxable income and interrupting the formation of the efficient human resources.

The most sensitive economic factor of corruption is outflow of funds from state budget and redirection of such funds for payment of expenses with lower multiplies effect.

Thus, it is an urgent issue of reducing the level of corruption in Ukraine as corruption causes a chain of problems in the sphere of state management, thus, increasing tax load, reducing the volume of services for the persons concerned and leveling trust in public institutions.

Prevention of corruption is one of the vital social problems at the moment and its settlement is vital and complex for many countries. Thus, the task is focused on formation of the effective and efficient anti-corruption system consisting of preventions, determinations and relevant responses to corruption factors, disclosure of corrupt practices and implementation of the principles of unavailability of responsibility for commitment.

In recent years there has been a significant increase in high-profile cases related to money laundering with the involvement of persons authorized to perform functions of the country or self-governing authorities. At the same time, it is observed for the process of strengthening of corruption prevention at the international level – from the side of international institutions, at the regional level – from the side of law enforcement authorities, state bodies and taking of measures to determine such illegal actions by the financial mediators.

Conducting of the typological study upon analysis of financial transactions may allow determining and countering money laundering.

As a result, determination and suspension of the schemes of money laundering are two basic tasks for all members of the system of anti-money laundering, countering the financing of terrorism and the financing of proliferation of weapons of mass destruction.

It should be noted that the approval and determination of funds received from corruption are basic for the efficiency of successful anti-corruption policy that will allow renewing of confidence of the society to state institutions, improving investment environment, developing economic and becoming an important condition for effective country development. As anti-money laundering policy is an important part of combating economic crimes.

The results of the conducted typological study are formation of the analytical base for making further decisions in order to prevent money laundering by all members of national policy of anti-money laundering and countering the financing of terrorism.



# CURRENT INSTRUMENTS, METHODS AND MECHANISMS OF ILLEGAL FUNDS ALLOCATION AND LAUNDERING

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TYPOLOGIES 2015

## Introduction

The State Financial Monitoring Service in cooperation with state regulators, regulatory, law enforcement authorities of Ukraine and financial institutions annually conducts the study of methods and schemes of money laundering or the financing of terrorism and the financing of proliferation of weapons of mass destruction.

For efficient counteraction to money laundering and the financing of terrorism, there is a need to improve and take measures of organizational and legal, economic and political nature in the international and domestic sector. The above should be done by all parties to the process to prevent the use of the financial system of Ukraine's economy for money laundering and potential financing of terrorism (separatism) that could lead to poor economic condition of the country and violation of its territorial integrity.

The State Financial Monitoring Service and members of the national AML system, within their powers, take measures to create the effective AML system.

An important aspect for verification of the said results is a typological study in view of experience obtained by the participants.

**The aim** of the study was to identify and summarize current instruments, methods and mechanisms of the most common schemes of money laundering, terrorist financing and other crimes.

In this typological study the examples of any used schemes are summarized, the most popular economic areas of application are given.

## 1. Money laundering

The question of anti-money laundering is the up-to-date requirement and the most important for Ukraine.

Abusing its official powers, a natural person makes appropriate unlawful decisions aimed at obtaining benefits.

Any funds obtained from corruption schemes are subsequently used for purchase of luxury homes, VIP-class cars, precious metals and stones, antiques, securities, investment in business and other personal needs.

The identified schemes of money laundering are varied, from the most simple aimed at personal consumption, to more complex associated with investing in legitimate business activities.

The most popular ways of money laundering are as follows:

- crediting of funds in cash to the accounts of natural persons holding leadership positions in state enterprises, companies, organizations or connected natural persons or legal entities with further purchase of assets, services or investment into activity of legal entities being



under their control or with crediting of funds to the deposit accounts and further the above mentioned investment;

- repayment of credits to be used for purchase of luxury homes, VIP-class cars, precious metals and stones, other assets;
- provision of financial assistance or increase of equity capital of enterprises owned by the persons affiliated with the officials of state enterprises, companies, organizations;
- crediting of funds as royalty fee.

### Example

There is a scheme of money laundering by a person holding leadership position in state enterprise.

It has been found that the **natural person** being suspected in misuse of funds of state enterprise in a large amount settled transactions in a large amount, including in cash. He/she used own accounts opened in different bank institutions of Ukraine. He/she credited and withdrew funds, repaid credits, credited the funds to the deposit accounts both in national currency and in US dollars.



The total amount of funds credited by **the natural person** to the account during 2003-2014 constituted the amount equal to **UAH 138.5 milion** (including UAH 95.9 million – to the deposit accounts).

Thus, the official amount of income obtained by **the natural person** is lower than the amount of financial transactions settled, indicating the presence of disguised sources of income.

The amount of income received by **the natural person** during 2003-2014 constituted UAH 1.3 million that is 100 times less than the total amount of financial transactions settled.

It is also found that **the natural person** owns a number of luxury cars, two objects of expensive real estate.

The law enforcement authority carries out an investigation.

**Example**

It is found for the scheme potentially connected with receipt by the official of illegal benefit.



**The Company-non-resident** (Switzerland) credited funds to the account of the legal entity – **Company "D"** in the amount equal to **UAH 36.2 million (EUR 3.6 million)** with the purpose of payment "under the contract".

Further, **the Company "D"** transferred funds received to the card and current accounts of the natural person, being an executive official, in the amount of **UAH 12.9 million** and **UAH 12.2 million**, respectively, as royalty fees.

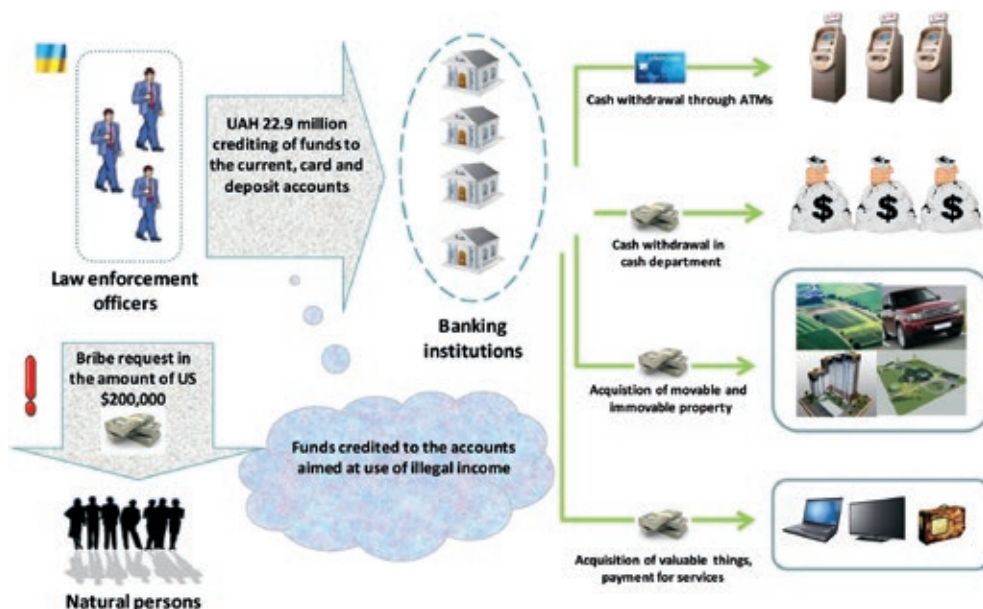
It should be noted that the Director of **the Company-non-resident** (Switzerland) is the official of the group of companies controlled by its close relative.



Upon receiving the undue benefits on a large amount, the law enforcement authority carries out an investigation.

### Example

There has been the scheme of potential money laundering as a result of soliciting and receiving the undue benefits.



It has been found that **the natural persons**, being law enforcement officers, during 2012-2015, credited a large amount of funds to their own accounts opened in various banking institutions of Ukraine, mostly in form of crediting cash, replenishment of deposit and card accounts. The total amount of funds credited to the above persons' accounts – **UAH 22.9 million** that does not meet the declared profits.

Further, funds at the accounts were used by **the natural persons** for purchase of real estate, cars, a variety of goods, payment for services. Also, funds were withdrawn in cash from ATMs and cash departments.

Each natural person opened from 5 to 40 accounts in more than 10 banking institutions.

**The natural persons** are law enforcement officers and involved in extortion in an especially large amount.

According to the facts, the law enforcement authority carries out an investigation.

**Example**

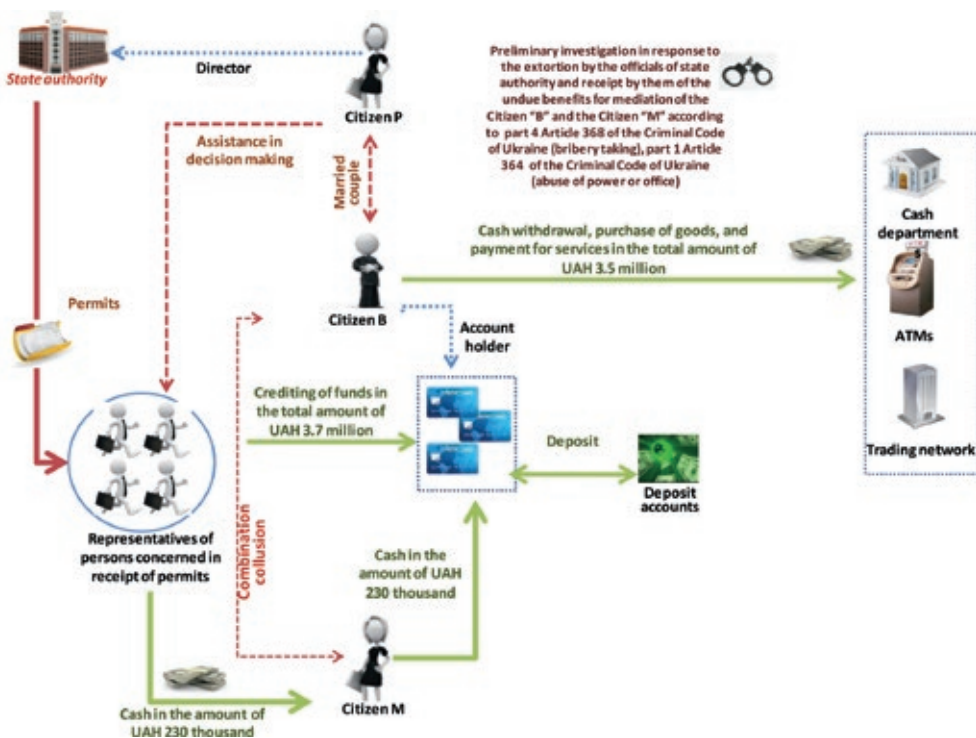
There has been the scheme of acquisition by the officials of the state authority of undue benefits for assistance in making the decisions on receipt of permits and money laundering.

**The Citizen P.**, holding a leadership position of **the state authority** and having the powers to issue permits, received the undue benefits for mediation of **the Citizen B** and **the Citizen M**.

To implement the given scheme, **the Citizen B** opened in banking institutions a number of accounts to which those persons concerned in the matter of receiving permits credited funds in the amount of **UAH 3.7 million**.

**The Citizen M** also credited funds in the amount of **UAH 230 thousand** to the accounts of **the Citizen B** that was probably received by her from the persons concerned in receiving permits.

Subsequently, funds were transferred to the accounts of **the Citizen B**, placed on the deposit accounts, then returned to the main accounts, together with accrued interest and withdrawn in cash, used for purchase of goods, payment for services in the total amount of **UAH 3.7 million** personally by **the Citizen B** and his wife **the Citizen P**.



Based on these facts, the law enforcement authority carries out an investigation.

## 2. Misuse of public funds and funds of public enterprises

The scope of government management is very attractive for embezzlement, taking into account a large amount of funds allocated for purchase of goods, works and services to meet the needs of enterprises, institutions and organizations of state property and enterprises with state shares.

In recent years, offences in public sector became actual and are the subject of constant attention from the side of international organizations and governments of countries.

The most sensitive areas of government management are funds of public entities. It is common for procurement of goods, works and services from companies with questionable or no business reputation, which have no production capacity, storage facilities or appropriate personnel. The presence of such intermediaries leads to overestimation of the cost for acquisition of goods, works and services at the expense of state-owned enterprises and enterprises with state shares.

For money laundering from state and local budgets, state enterprises, public entities with state shares in the authorized capital, standard instruments were used:

- involvement of nominees and shell corporations;
- conclusion of fictive trade agreements, cobber;
- use of "dirty" securities and non-repayable financial assistance;
- conversion into cash through the accounts of legal entities and natural persons.

The most used ways of embezzlement and money laundering of state enterprises are as follows:

- a state enterprise credits funds in favor of the enterprises (winning bidders) related to management of state enterprise. Further, funds are to be credited in favor of shell companies for conversion into cash;
- a newly established entity that has no employed workers and production capacity receives funds from a state enterprise, the portion of which is to be transferred in favor of mediators for implementation of bid, other portion is subject to conversion into cash or to be credited to the accounts of the officials of state enterprise and any affiliated persons or enterprises;
- any funds received from a state enterprise for goods, works, services shall be further divided and allocated among a large number of shell enterprises for the purpose of payment: financial assistance, securities, debt transfer with final conversion into cash;
- a state enterprise credits funds in favor of a public enterprise without actual supply of goods and provision of services.

### Example

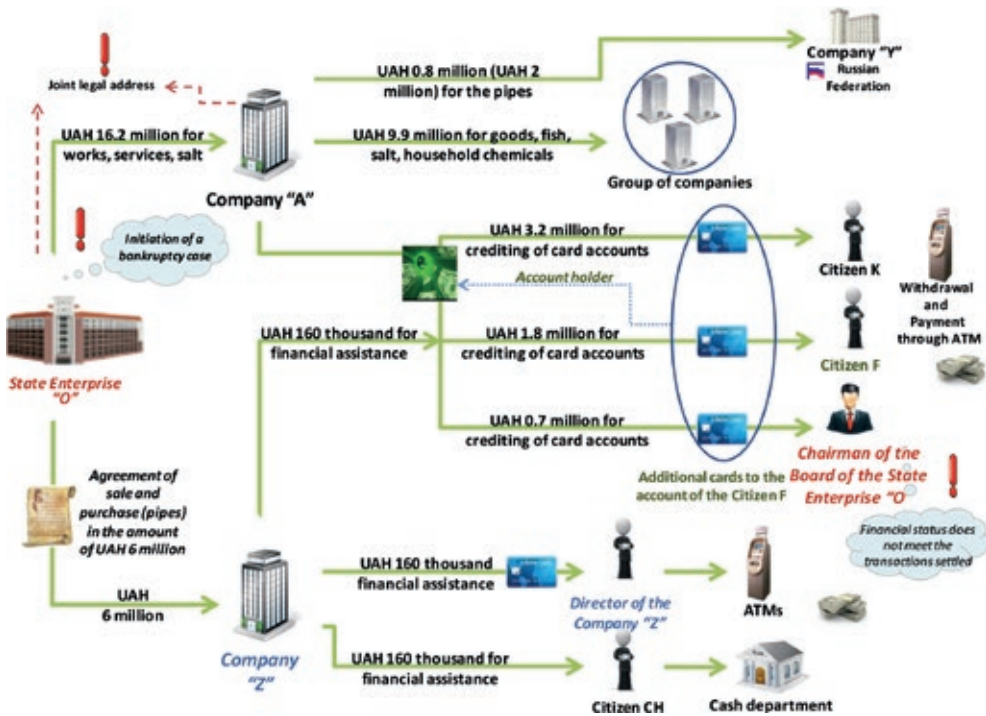
There has been the scheme of illegal embezzlement of public funds with the assistance of the official of state enterprise with further laundering through "conversion" into cash.

The banking institution, where the state enterprise has opened the account, informed the State Financial Monitoring Service on a number of withdrawals from the account and at the same time **the State Enterprise "O"** violated the proceedings in bankruptcy.

The State Enterprise “O”, with the assistance of the official, credited funds to the account of the Company “A” in the amount of UAH 16.2 million for works, services, salt and to the account of the Company “Z” in the amount of UAH 6 million for the pipes.

The Company “Z” transferred a large portion of funds received by three equal payments over UAH 160 thousand as financial assistance to the card accounts of natural persons, one of which was owned by the Chairman of the Board of the State Enterprise “O” that withdrew funds through ATMs and cash departments.

The Company “A” credited funds received in installments to the accounts of companies in the amount of UAH 9.9 million as payment for fish, salt, household chemicals and in favor of non-resident – Company “Y” (Russian Federation) in the amount equal to UAH 0.8 million as payment for the pipes.



Besides, the Company “A” credited funds in the amount of UAH 5.7 million to the account of the Citizen F (UAH 1.8 million) and additional payment cards to his account were opened in the name of the Citizen K (UAH 3.2 million) and the Chairman of the Board of the State Enterprise “O” (UAH 0.7 million).

Further, funds were withdrawn from the payment cards in cash through ATMs.

The State Enterprise “O” and the Company “A” have joint legal address.



The Company "A" and the Company "Z", being involved in the schemes of embezzlement of public funds with further conversion into cash, have signs of shell companies (sole founder, non-declared gross revenues, unpaid taxes, tax debt and minor equity capital).

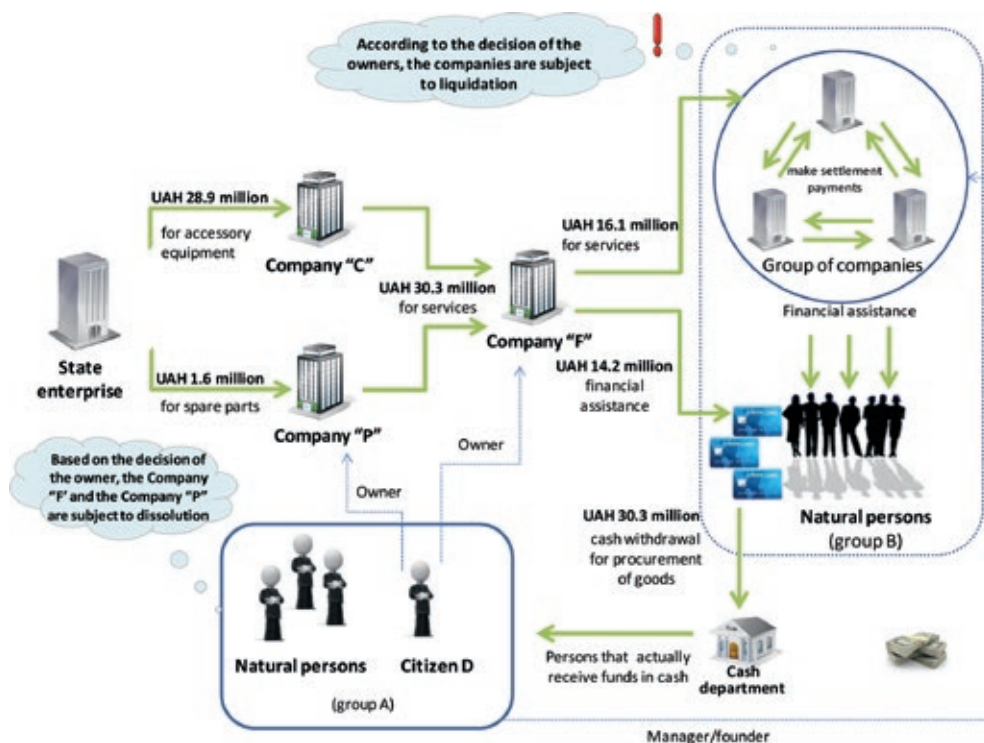
Based on these facts, the law enforcement authority carries out an investigation.

### Example

There has been the scheme of illegal embezzlement of public funds, with the assistance of the official of state enterprise, with further laundering through "conversion" into cash.

The state enterprise credited funds to the winning bidders in the total amount of UAH 30.3 million to the account opened in the Bank "Y", namely: in favor of the Company "C" – UAH 28.9 million as payment for accessory equipment and in favor of the Company "P" – UAH 1.6 million for spare parts.

Further, funds in the amount of UAH 30.3 million were transferred from the accounts of the Company "C" and the Company "P" to the account of the Company "F" opened in the Bank "Y" as payment for services.



In turn, public funds received from the account of the **Company "F"** (owner – **the Citizen D**) are partially aimed at settlement of payments with the group of legal entities in the amount of **UAH 16.1 million** and partially – in the amount of **UAH 14.2 million** – to the card accounts of natural persons (**group B**) as financial assistance with further conversion by them and their attorneys (**group A with the Citizen D**).

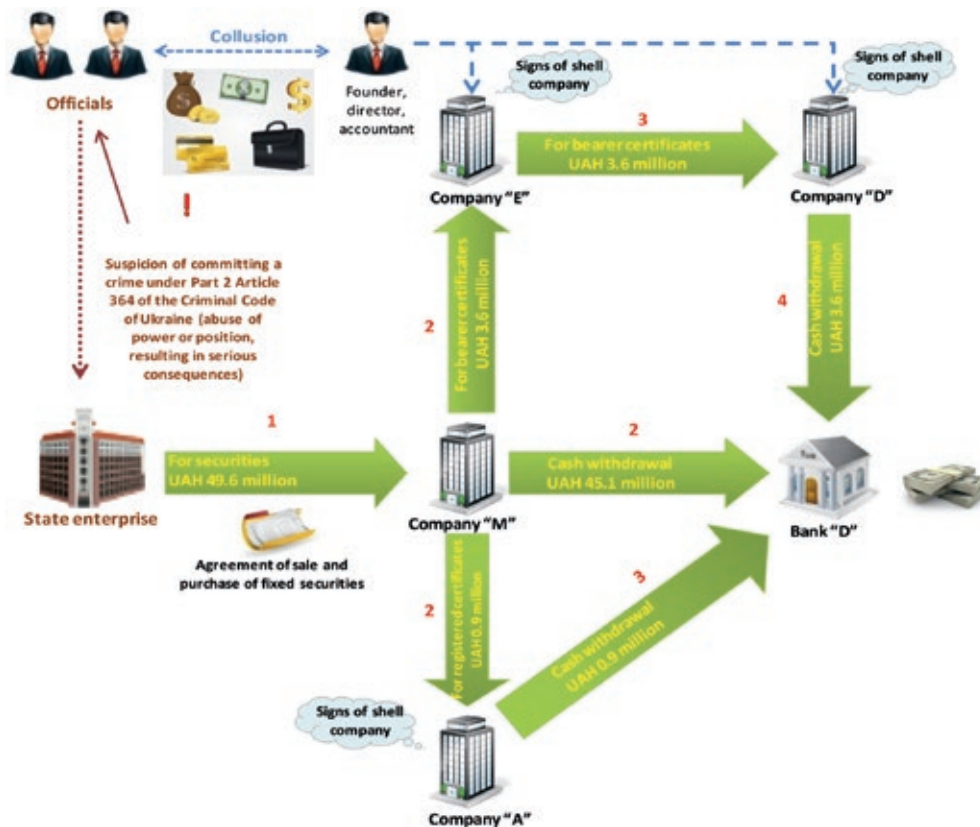
**The Citizen D** and natural persons of **the Group A** were the members of management/founder body of enterprises majority of which were shell companies and were attorneys of natural persons from **the Group B**.

Those enterprises and natural persons involved in the scheme used the accounts opened in **the Bank "Y"**.

Based on these facts, the law enforcement authority carries out an investigation.

### Example

There has been the scheme of capturing and/or embezzling funds of state enterprise as a result of conclusion of the agreements of sale and purchase of fixed securities with their further conversion into cash.



The state enterprise concluded the agreements of sale and purchase of securities issued by shell enterprises and credited to the account of the Company “M” (type of activity: securities exchange) in the total amount of UAH 49.6 million for investment certificates.

Further, the Company “M” withdrew the main portion of funds in the amount of UAH 45.1 million through the cash department.

The Company “M” transferred other portion of funds received from the state enterprise to the accounts of the Company “A” – UAH 0.9 million with the purpose of payment: “for registered certificates” and the Company “E” – UAH 3.6 million for the bearer certificates.

Further, the Company “A” withdrew funds in cash through the cash department of the same Bank “D”.

The Company “E” transferred funds received from the Company “M” to the account of the Company “D” as payment for “the bearer certificates” that further received funds in cash from the account through the cash department.

Those enterprise involved in the scheme appeared to be fictive.

Based on these facts, the law enforcement authority carries out an investigation.

### 3. Misuse of funds of banking institutions

Due to a great variety of financial services and instruments, customer database and accumulation of funds, the banking sector is attractive for the implementation of fraud schemes.

In many cases any criminal activity upon settlement of payment, deposit and credit transactions is performed with the involvement of bank officers, in particular, officials of banking institutions.

The main instruments to be used in the schemes of embezzlement and money laundering are as follows:

- “dirt” securities (shares, notes);
- debt obligations of shell enterprises;
- claim assignment;
- conversion into cash.

The most popular ways of embezzlement of funds of banking institutions are as follows:

- provision of credits by banking institutions to those borrowers affiliated with the owners of banking institutions;
- provision of credits by banking institutions to those shell enterprises;
- release of property through assignment of the right of ownership to the third parties;
- cash withdrawal through correspondent accounts in foreign banks.

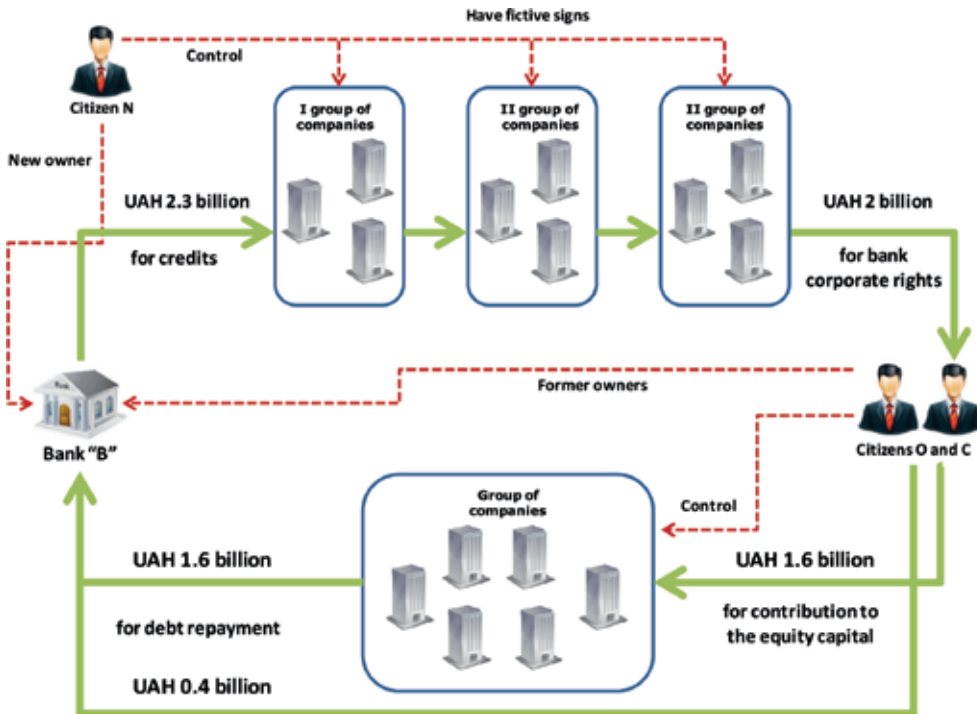
**Example**

Upon analysis of financial transactions, the State Financial Monitoring Service found the “round” scheme allowed making fictive sales of the control stock of the Bank “B” within one day involving shell enterprises.

It has been found that within one day the Bank “B” provided the I group of companies – newly established enterprises with credits secured on goods to be further purchased in the total amount of UAH 2.3 billion. At the same date, funds given were transferred to the accounts of the II group of companies that transferred such funds in favor of the III group of companies.

All the above mentioned groups were controlled by the Citizen K and were fictive.

At the same date, the III group of companies credited funds in favor of the Citizens O and C as payment for the control stock (80%) of shares of the Bank “B”.



The Citizen O and C used funds received in the amount of UAH 2 billion for repayment of own debt and debt of the controlled enterprises to the Bank “B” for previously granted credits.

It is resulted in actual debt assignment of the Citizen O and C and their controlled enterprises to the shell companies of the Citizen N.



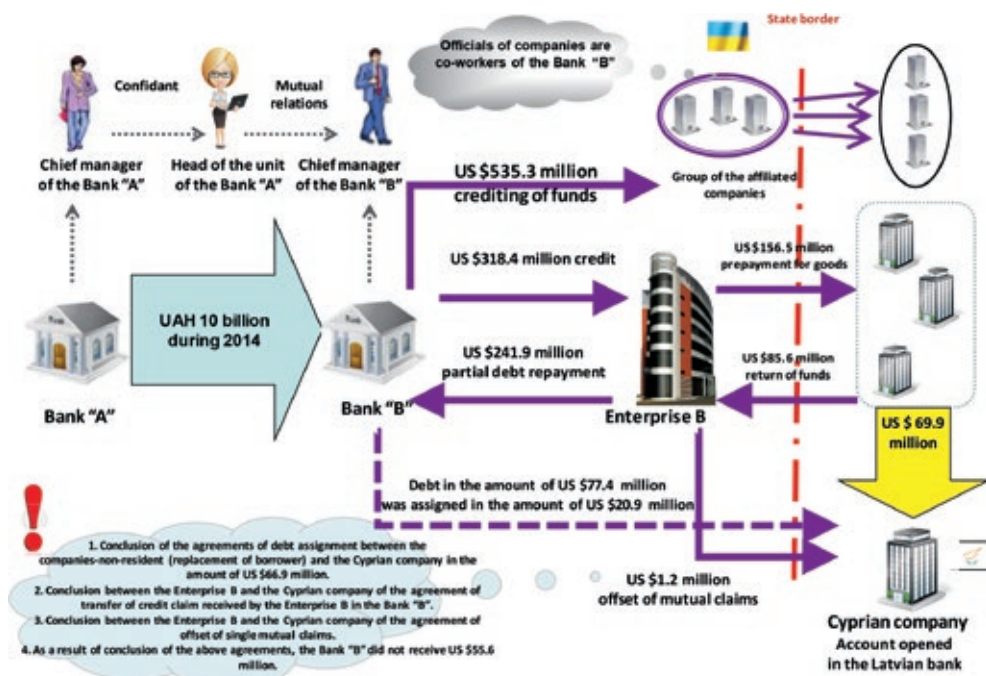
At the date, **the Bank "B"** forfeited the bank license and is in the process of liquidation.

Based on these facts, the law enforcement authority carries out an investigation.

### Example

There has been the scheme of embezzlement of banking funds and further laundering through credit and foreign economic transactions with the involvement of the officials of commercial bank resulted in the preconditions for bank bankruptcy (the bank is under temporary management).

It has been found that during 2014 **the Bank "B"** received from **the Bank "A"** funds in the amount of UAH 10 billion. The head of **the Bank "B"** had relations with the head of the unit of **the Bank "A"**, being, in turn, the attorney of the chief manager of **the Bank "A"**.



Further, **the Bank "B"** converted UAH 4.1 billion out of the given amount into US \$ 535.3 million and transferred the funds abroad in favor of 12 affiliated Ukrainian entities, partnerships which officials are employees of **the Bank "B"**.

Moreover, **the Bank "B"** granted the credit to **the Enterprise "B"** in the amount of US \$ 318.4 million, among them the amount of US \$ 241.9 million was returned as repayment of credit in this bank. Credit funds received were also partially transferred by **the Enterprise "B"** abroad in favor of three companies-non-residents as prepayment for goods in the total amount of US \$ 156.5 million. Further, the mentioned non-residents returned to **the Enterprise "B"** a portion of funds

in the amount of **US \$ 85.6 million**, due to inability to perform the conditions of the agreement on goods supply, and the remaining amount of debt **US \$ 69.9 million** was transferred by the non-residents in favor of other non-resident – **the Cyprian company**, according to the concluded agreements of debt assignment (replacement of borrower responsible).

The remaining outstanding debt under credit obligations of **the Enterprise “B” to the Bank “B”** in the amount of **US \$ 77.4 million** was assigned by **the Bank “B”** in favor of **the Cyprian company** for the amount of **US \$ 20.9 million**.

**The Enterprise “B” and the Cyprian company** concluded the agreement on offset of single counterclaims, as a result the amount of debt of **the Enterprise “B” to the Cyprian company** constituted **US \$ 7.9 million**, among them the amount of **US \$ 1.2 million** was actually paid.

Thus, upon conclusion by the officials of **the Bank “B”** of the unprofitable agreements on credit claim transfer to **the Cyprian company**, **the Bank “B”** did not receive the amount of **US \$ 55.6 million**, i. e. it made a loss.

Based on these facts, the law enforcement authority carries out an investigation.

#### 4. Money laundering in the insurance market

Possibilities of the insurance market are actively used for round transactions aimed at minimizing the taxation of entities, exaction of funds from turnover and transfer abroad or obtaining other economic benefits both by the insurers and third parties.

The priority functions of the country in the insurance market is to create optimal conditions for the insurance companies while minimizing the risks of the involvement of the insurance companies into money laundering and the financing of terrorism. The need for an effective anti-money laundering mechanism in the insurance market is determined by the fact that in recent years more than 70% of the reports on suspicious financial transactions from non-banking institutions were recorded by the insurance companies.

The main instruments in the insurance market in money laundering schemes are following:

- conclusion of insurance agreements with unlikely risks;
- fictive documents on insurance event;
- conclusion of agent agreements with increased fees;
- reinsurance in the company with insufficient financial status;
- “dirt” securities (shares, notes, investment certificates);
- conversion of funds into cash.

The most popular ways of money laundering through the insurance market:

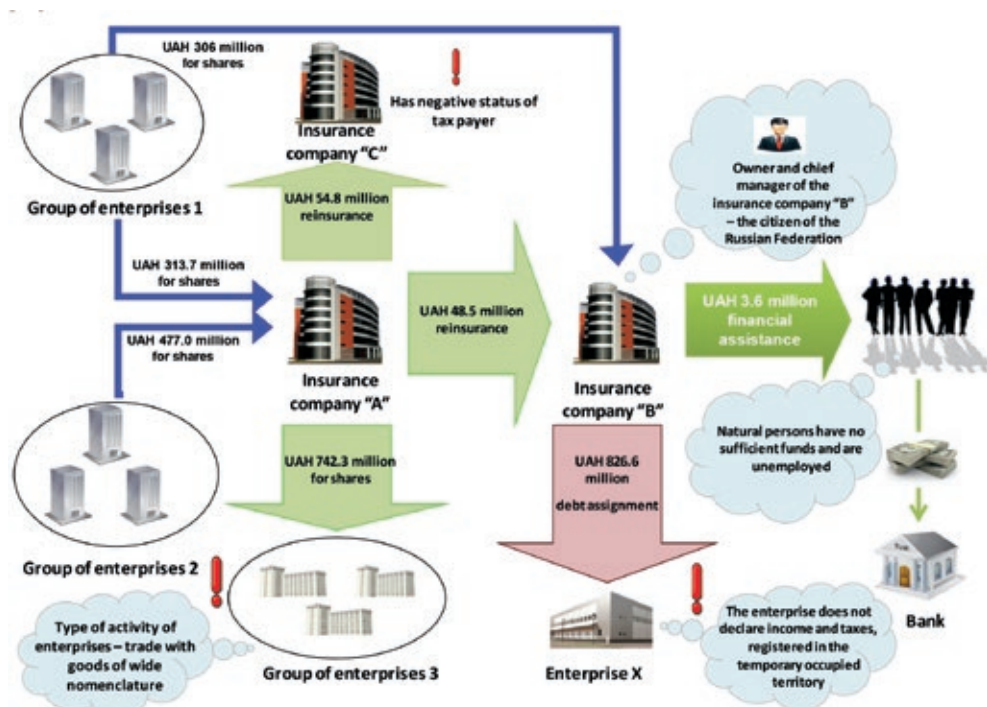
- receipt by the insurance company of funds under unlikely insurance risks with further transfer in favor of shell companies;
- settlement of a large number of financial transactions with reinsurance by insurance companies having insufficient financial status;

- crediting by the insurance company of a large amount of funds in favor of natural persons as payment under agent agreements;
- payment by the insurance company to a large number of natural persons of insurance premium during a short period of time.

### Example

There has been the illegal scheme of financing by the representatives of so-called “Donetsk People’s Republic” involving insurance companies.

It has been found that funds from a number of entities were credited to the accounts of two insurance companies: to the account of **the Insurance Company “A”** it was credited **UAH 477 million** as insurance payment and **UAH 313.7 million** as payment for shares. The amount of **UAH 306 million** was credited to the account of **the Insurance company “B”** – for shares, notes, payment as debt assignment, replenishment of own account, reinsurance of payments.



Further, funds accumulated by **the Insurance Company “A”** were transferred to the accounts of the group of enterprises, the main type of activity of which is retail and mediator trading activity, in the amount of **UAH 742.3 million** as payment for shares to the account of **the Insurance company “C”** (has negative status of tax payer) in the amount of **UAH 54.8 million** as reinsurance and to the account of **the Insurance company “B”** in the amount of **UAH 48.5 million** as insurance premium.

Moreover, **the Insurance Company "B"** owned and managed by the citizen of the Russian Federation transferred funds under the agreement on debt assignment to the account of **the Enterprise "X"** in the amount of **UAH 826.6 million**. **The Enterprise "X"** does not declare income and taxes and is registered in the temporary occupied territory.

Further, a portion of funds in the amount of **UAH 3.6 million** was transferred from the account of **the Insurance company "B"** to the account of three natural persons as financial assistance. Natural persons withdrew funds in cash in the cash department of one banking institution.

The mentioned natural persons are registered in the temporary occupied territory, have no sufficient funds and are temporary unemployed. Accounts of two natural persons were closed just upon settlement of financial transactions.

Based on these facts, the law enforcement authority carries out an investigation.



## 5. Money laundering in foreign economic activities

The sources of illegal capitals laundering through foreign economic activities may be revenues received from traditional forms of criminal activity (for example, drug traffic, human beings traffic), as well as revenues from financial crimes (embezzlement of funds and property).

Thus, the vast majority of transfers abroad is made in favor of non-residents registered in the countries with kindly taxation environment or simplified registration system, among them are following: Panama, Seychelles, Marshall and British Virgin Islands, Great Britain.

A portion of removed capital is further returned to the country in form of foreign investments, corporate rights, granted credits and loans to be addressed for business support and development and bring legal income. A portion of such transactions is settled with the assistance of shell companies.

The members of the schemes of withdrawing funds abroad are both national legal entities and companies-non-residents controlled by the citizens of Ukraine and foreign shell companies registered for fictive performance of operational activity.

At the same time, bank accounts of non-residents are opened in the following countries: Cyprus, Latvia, Lithuania, Austria and Switzerland.

The main instruments to be used in the schemes involving foreign economic transactions are as follows:

- fictive import agreements;
- "dirt" securities;
- shell companies – residents and non-residents;
- agreements on offset of single counterclaims;
- forgery of documents on performance of foreign economic activity;
- loans from non-residents, fictive investment, conversion into cash;
- involvement of nominees.

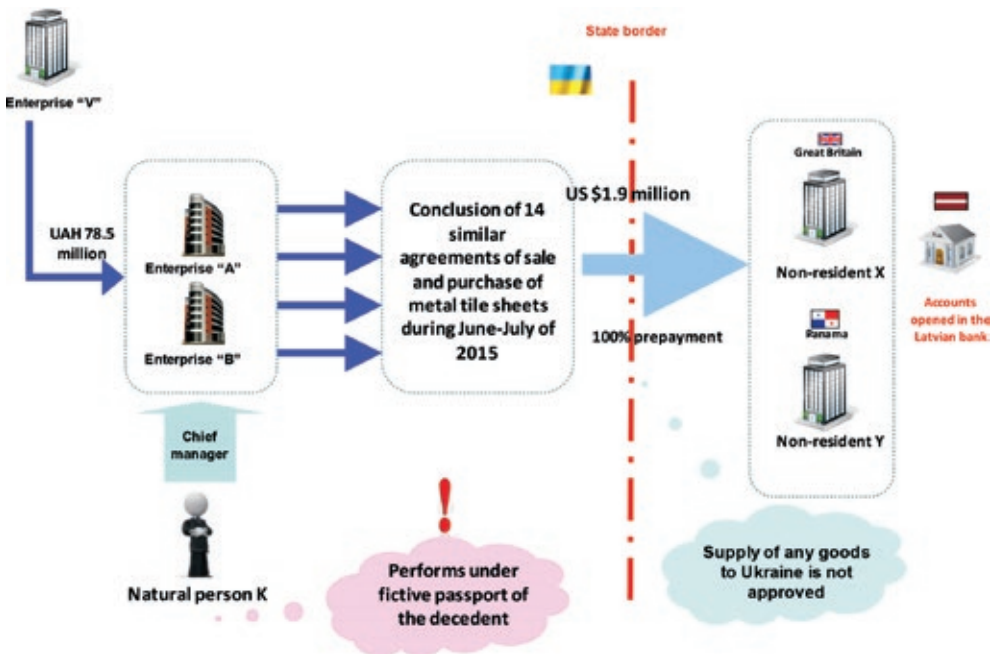
The most popular ways of money laundering using foreign economic financial transactions are as follows:

- funds from a large number of counteragents are accumulated at the account of the Ukrainian enterprise and further transferred abroad in favor of non-residents controlled by the citizens of Ukraine;
- settlement of transactions on fictive investment under which the company-non-resident purchases suspicious or fictive securities which it further sells to the affiliated companies at the price ten times higher than the purchase price with further withdrawal abroad in form of return of foreign investments and revenues from investment activity;
- settlement of financial transactions under fictive import agreements, transit funds transfer between non-residents without the territory of Ukraine and return of funds to the territory of Ukraine to the accounts of natural persons for conversion into cash.

**Example**

There has been the scheme of withdrawing funds abroad under the fictive agreements concluded between the Ukrainian fictive enterprises and the companies-non-residents.

Thus, **the Enterprise "A"** and **the Enterprise "B"** concluded **14** similar agreements of sale and purchase of metal tile sheets with **the companies-non-residents "X"** (Great Britain) and **"Y"** (Panama). In all cases the goods were 100% prepaid to the accounts of **the companies-non-residents "X"** and **"Y"** opened in the Latvian bank in the total amount of **US \$ 1.9 million**.



The source of funds at the accounts of **the Enterprise "A"** and **the Enterprise "B"** at cost of which currency was purchased was contributions from **the Enterprise "V"** in the total amount of **UAH 78.5 million**.

According to information received from the law enforcement authorities, the passport submitted to the banking institution by the chief manager of **the Enterprise "A"** and **the Enterprise "B"** is fictive as it is holding by the decedent. Besides, **the Enterprises "A", "B" and "V"** are "fictive", in particular: sole manager and founder, low level of equity capitals, lack of any declared gross revenue and payment of taxes.

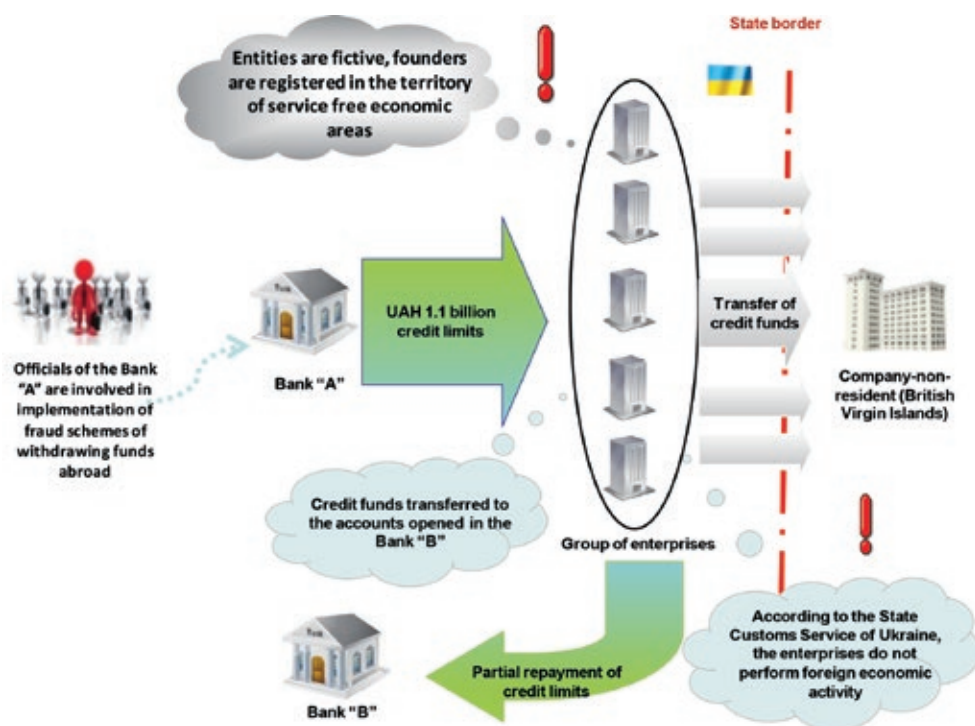
Supply of any goods to the customs territory of Ukraine in favor of **the Enterprise "A"** and **the Enterprise "B"** was not performed.

Based on these facts, the law enforcement authority carries out an investigation.

## Example

There has been the scheme of settlement of credit and foreign economic transactions having no economic sense and legal goal and aimed at embezzlement of the banking institution assets.

The "Bank "A" concluded with the fictive entities controlled by the chief management of the Bank "A" the credit contacts on granting of non-returnable credit limits with maximum credit risk. Further, credit funds received were partially transferred to the accounts of the mentioned enterprises opened in other banking institution and those credits previously granted were repaid.



A portion of credit funds received is addressed without the territory of Ukraine under fictive foreign economic contracts in favor of **the Company-non-resident** and over a period of time returned to the accounts of the mentioned Ukrainian enterprises.

At that, repayment of the principal amount received in **the Bank "A"** was mainly not performed. At the moment, the above mentioned entities have debt to **the Bank "A"** under the concluded credit agreements in the amount of **UAH 1.1 billion**. Thus, according to the State Customs Service of Ukraine, the mentioned enterprises do not perform foreign economic activity at all.

**The Bank "A"** had problems with liquidity and failed to perform its obligations to its depositors.

Based on these facts, the law enforcement authority carries out an investigation.

## 6. Money laundering in the securities market

Attractiveness of the securities market in the schemes of money laundering is due to a large number of professional players of stock exchange, among them there are those "technical" formed by a certain group of persons for certain financial transactions. Upon settlement of such transactions, newly established professional market players cancel their licenses or even disappear that is defined by the state regulator only upon conducting audit or receiving any claim from the investors on absence of the licensee at place of location.

Moreover, absence of the unified state register of notes adds complexity to proper control over their issuance and turnover and, accordingly, allows the note to take the first place among financial instruments to be used in the schemes of money laundering.

Typical example is the situation when the buyer makes a note with endorsement as payment for receipt of any goods or services from the seller. Upon settlement of any special transactions (including book-cooking and forgery of payment documents), such note is addressed to the natural person that submits it to the holder for payment, receives the funds and withdraws them from the account in cash.

Thus, the popular instrument for money laundering is saving (deposit) certificates that any natural person may buy from the legal entity deposited in the banking institution and, further, may receive the funds upon submission of such certificates to the banking institution.

Moreover, state securities are often used as a financial instrument – bonds of national credit. Thus, all securities purchased at the bargain price should be further sold at the market prices. Consequently, some players make a loss, while other players gain investment income.

Upon money laundering through the securities market, the following instruments are used:

- securities issued by fictive enterprises;
- off-market securities;
- notes with turnover more than 3 years or issued by the newly established enterprises;
- saving bearer certificates;
- bonds of national state loan purchased not at the market price;
- conversion of funds into cash.

The most popular ways for money laundering using securities are as follows:

- funds from the unknown sources are transferred as payment for "dirt" securities in favor of fictive enterprises;
- any note received upon sales of any goods or services is further received by the natural person through forgery of documents that presents it for payment to the holder and converts the funds received into cash;
- acquisition by the natural person of saving (deposit) certificates from the legal entity deposited the funds, for presentation of such certificates to the banking institution for receipt of interests with further sales of certificates;
- acquisition of bonds of national state loan credit at the bargain price and further sales at the market prices;

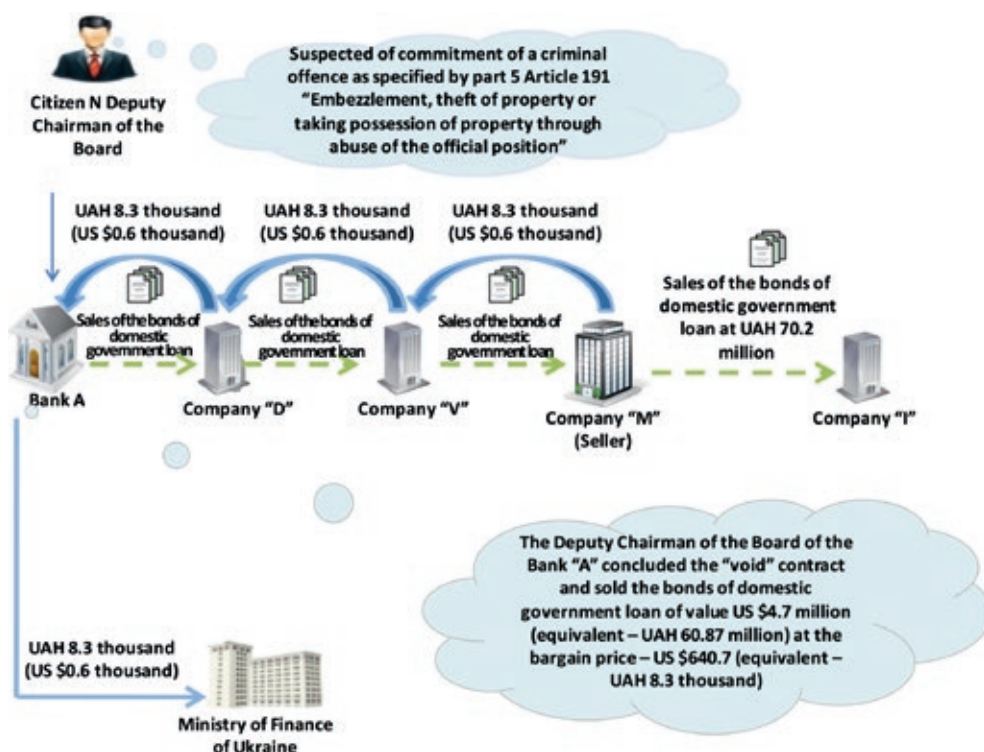


- involvement of the newly established professional securities market players for settling financial transactions;
- involvement of nominees and fictive enterprises.

### Example

There has been the scheme aimed at embezzlement of property through abuse of the official position.

Thus, the Bank "A" with the assistance of the Citizen N (Deputy Chairman of the Board of the banking institution "A") concluded with the Company "D" the agreement and sold bonds of national state loan with the total nominal value of US \$ 4.7 million (equal to UAH 60.8 million) for UAH 8.3 thousand.



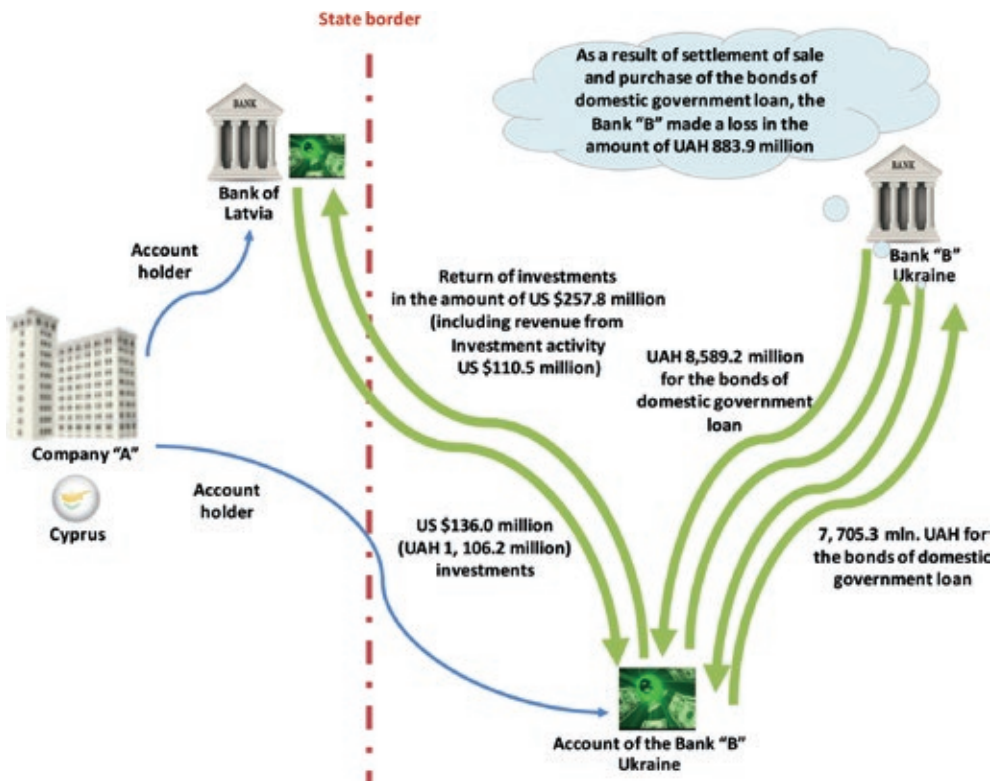
Further, the Company "D" sold the bonds of domestic government loan to other enterprise the Company "V" for UAH 8.3 thousand and then they were purchased by the seller of securities of the Company "M" from the Company "V" for UAH 8.3 thousand sold at the stock exchange at the market price of UAH 70.2 thousand in favor of the Company "I".

Thus, based on the order issued by the Deputy Chairman of the Board of the Bank "A", the bonds of domestic government loan were sold at the bargain price lower than the nominal value resulted in loss in the amount of UAH 60 million.

Based on these facts, the law enforcement authority carries out an investigation.

**Example**

There has been the scheme of embezzlement by the company-non-resident affiliated with the bank management of the funds of the banking institution resulted from settlement by the banking institution of unprofitable transactions on sale and purchase of the bonds of domestic government loan.



The Company "A" (Cyprus) transferred from the account opened in the Latvian bank the funds to the own account in the Bank "B" in the amount of US \$ 136 million as investment activity and, after conversion into national currency, the funds were credited to the own account in the same bank in the amount of UAH 1, 106.2 million.

Using the "round" scheme of sale and purchase and purchase and sale of the same bonds of domestic government loan, the Company "A" (Cyprus) transferred the above mentioned funds in favor of the Bank "B" as payment for the bonds of domestic government loan according to

the agreements on sale and purchase of the bonds of domestic government loan. At the date of receipt of the funds from **the Bank "B"** and execution of the transfer and delivery certificates of the bonds of domestic government loan, non-resident sold (returned) to the mentioned bank under other agreements of sale and purchase of the bonds of domestic government loan. The funds received from **the Bank "B"** from sales of the bonds of domestic government loan together with the remaining unused funds upon the first transfer were used by **the Company "A"** for purchase other stocks of the bonds of domestic government loan from **the Bank "B"**.

The funds were moved from **the Company "A"** to **the Bank "B"** and returned with revenue from investment activity.

As a result of round transactions, **the Company "A"** totally transferred the funds in favor of the **Bank "B"** as payment for the bonds of domestic government loan in the amount of **UAH 7, 705.3 million**, while it was received for the funds from **the Bank "B"** from sales of the same bonds of domestic government loan in favor of this banking institution in the amount of **UAH 8, 589.2 million**.

The amount of investment income of **the Company "A"** (Cyprus) and, accordingly, the amount of loss of **the Bank "B"** constituted **UAH 883. 9 million**.

The mentioned "investment" income in the amount of **UAH 883.9 million** as a part of the amount of **UAH 2, 298.0 million** was transferred for purchase of currency and, further, credited to the account in foreign currency in the amount of **US \$257.8 million** (together with revenue in the amount of **US \$ 110.5 million** from investment activity in Ukraine).

At the last stage, the mentioned funds were transferred abroad to the own account of **the Company "A"** in Latvian bank as income received from sale and purchase of the bonds of domestic government loan and return of the funds due to the suspension of investment activity.

Based on these facts, the law enforcement authority carries out an investigation.

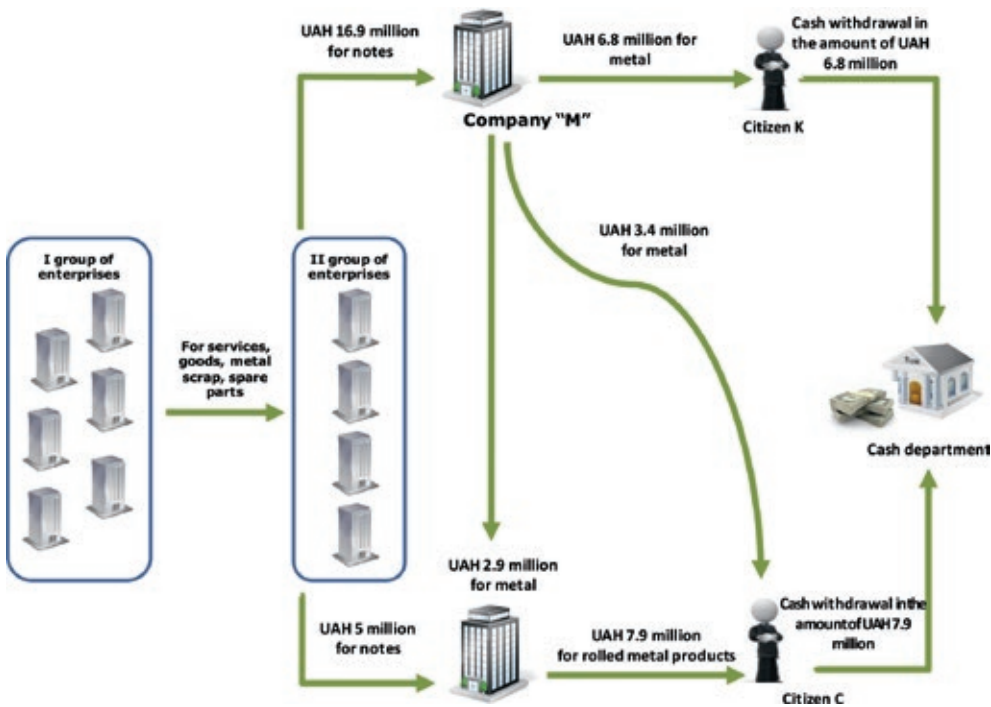
### Example

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There has been the scheme of movement of non-cash money with further "conversion" into cash.

Those funds received from the **I group** of enterprises in favor of the **II group** of enterprises as payment for services, goods, and metal scrap, spare parts were further transferred in favor of **the Company "M"** in the amount of **UAH 16.9 million** and **the Company "A"** in the amount of **UAH 5 million** for notes. In turn, **the Company "M"** transferred funds received in favor of **the Company "A"** in the amount of **UAH 2.9 million** with the purpose of payment – for metal.

Further, mentioned funds were transferred from the accounts of **the Company "M"** and **the Company "A"** to **the Citizen K** and **the Citizen C** as payment for metal and withdrawn in cash. The total amount of funds converted by **the Citizen K** and **the Citizen C** in cash constituted **UAH 18.1 million**.



Based on these facts, the law enforcement authority carries out an investigation.

### Example

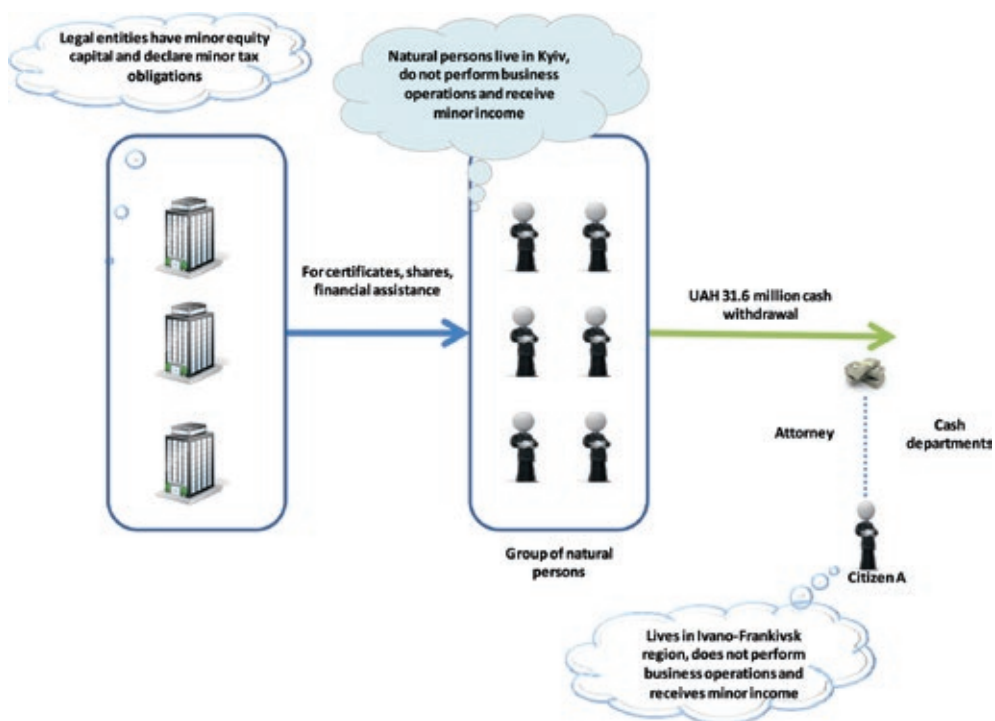
There has been the scheme of cash movement that allowed converting of non-cash funds into cash using the securities market.

Non-cash funds were transferred by **the group of enterprises** in favor of **a number of natural persons** as payment for certificates, shares, financial assistance.

Further, funds were withdrawn from the accounts of the group of natural persons by the same attorney-**citizen A** in cash departments of two banking institutions.

Those enterprises that transferred funds in favor of the group of natural persons are fictive: minor equity capital, minor tax obligations declared, sole manager and founder, accounts are opened prior to settlement of financial transactions, change in founders.





The group of natural persons, taking into consideration lack of income, has negative financial status, lives in Kyiv, while the **citizen A** lives in other region (Ivano-Frankivsk region).

The total amount of funds received by **the citizen A** in cash constituted **UAH 31.6 million**.

Based on these facts, the law enforcement authority carries out an investigation.

## 7. Money laundering through “convert” centers and fictive enterprises

Cash is one of the popular instruments in Ukraine to be used in the schemes of money laundering.

It should be noted that during 2014-2015 the National Bank of Ukraine adopted a range of statutory acts aimed at limitation of cash turnover in Ukraine.

Thus, from June 01 till September 01, 2014 according to the Decree of the National Bank of Ukraine dated 30.05.2014 No. 328 “On Regulation of the Activity of Financial Institutions and Settlement of Currency Transactions”, there have been established restrictions concerning issue of funds in national and foreign currency.

According to the Decrees of the Board of the National Bank of Ukraine dated 29.08.2014 No. 540, dated 01.12.2014 No. 758, dated 03.03.2015 No. 160, dated 03.06.2015 No. 354, dated 03.09.2015 No. 581 and dated 04.12.2015 No. 863, the term of restrictions was expended till December 02, 2014, March 03, 2015, June 03, 2015, September 03, 2015, December 04 and March 04, 2016.

Based on the above mentioned Decrees, the banks should restrict issuance of funds in national currency through cash departments and ATMs in the amount of up to UAH 150 thousand per day per one customer. From June 03, 2015 the daily limit per one customer was increased up to UAH 300 thousand.

In addition, according to the requirements of the Decree of the Board of the National Bank of Ukraine dated 04.12.2015 No. 863, the authorized banks are obliged to restrict issuance (receipt) of funds in foreign currency or bank metals from customs current and deposit accounts through cash departments and ATMs up to UAH 20 thousand per day per one customer in the equivalent at the official rate of the National Bank of Ukraine.

The mentioned requirement applies to issuance (receipt) of funds both within and without the territory of Ukraine regardless of the number of accounts in one bank.

The above restrictions significantly influenced on the mechanisms of operation of the “convert” centers. Recently, prior to application of the restrictions for issuance of funds, at the final stage of conversion of non-cash funds into cash, a few number of parties was involved (persons or entities).

Up to the date, taking into consideration the existing restrictions, the following mechanisms and methods are used for withdrawal of a large amount of funds:

- involvement of a large number of persons and entities (including those with fictive signs);
- opening of a large number of accounts by one entity or person in various banking institutions;
- involvement of socially disadvantaged population, persons with criminal history and persons using lost passports for settlement of financial transactions;
- combination of various forms connected with cash withdrawal abroad and trade with import goods for cash.

At this, funds are often withdrawn from the accounts of all scheme players by one attorney or the group of persons.

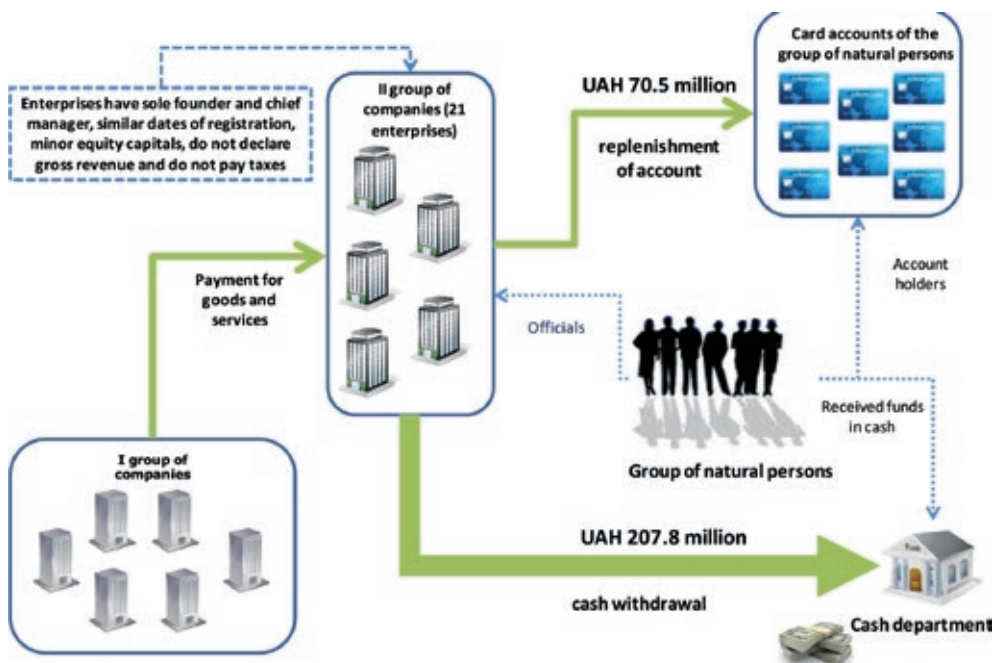
The most popular instruments to be used in the activity of “converti” centers are as follows:

- agreements on claims assignment;
- “fictive” securities (notes, shares, investment certificates);
- financial and charitable assistance, other types of loans.

### Example

There has been the scheme of funds movement on conversion of non-cash funds into cash.

Thus, funds credited from **the first group** of companies to the accounts of **the second group** of companies (**21 enterprises**) were further transferred to the card accounts of **20 natural persons** and withdrawn in cash.



The total amount of funds converted into cash and transferred to the card account constitutes **UAH 278.3 million**.

The vast majority of enterprises from which accounts funds were withdrawn are registered at the same period, have minor equity capitals (from 100 up to 3,000 UAH) and sole founder and chief manager. Information on the declared gross revenues and paid taxes is missed.

Natural persons-holders of card accounts are the founders of the mentioned enterprises. The mentioned persons do not have any appropriate income, taking into consideration lack of any revenues received and right of ownership on property.

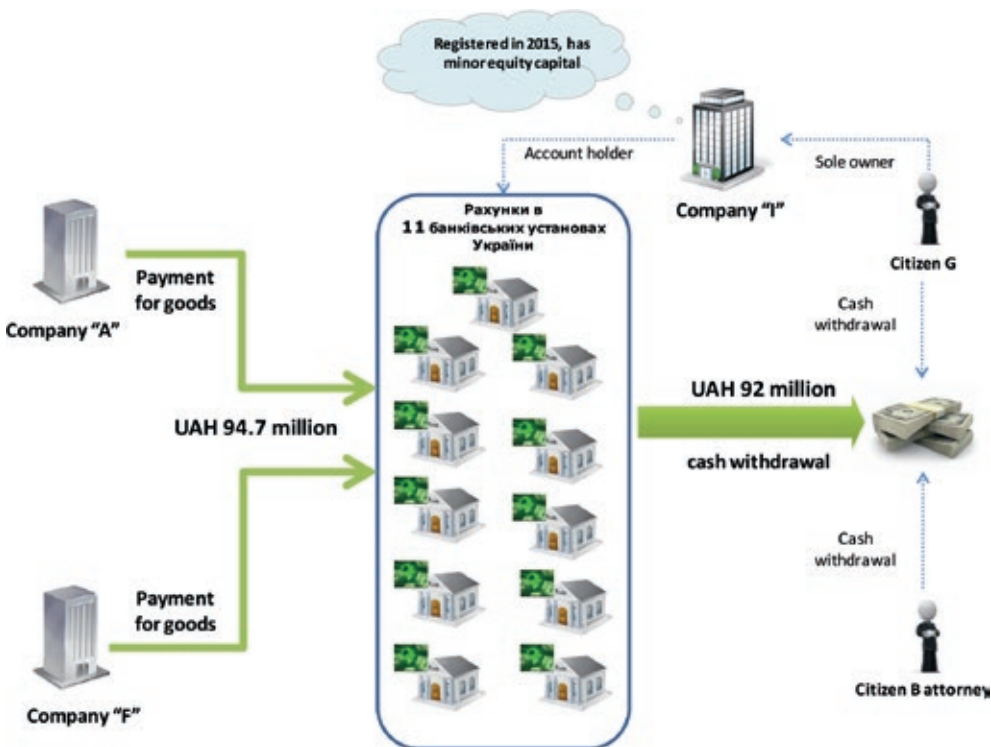
Based on the given facts, the law enforcement authority carries out an investigation.

**Example**

Upon analysis of financial transactions, there has been the scheme of funds movement that allowed converting of non-cash funds into cash.

Two companies transferred the amount of **UAH 94.7 million** to the accounts of the newly established enterprise **Company "I"** opened in 11 banking institution of Ukraine, as payment for goods.

Further, funds in the amount of **UAH 92.0 million** were withdrawn in cash from the above accounts by sole owner of the enterprise **the Citizen G** and by the attorney **the Citizen B**.



The enterprise, from the account of which funds were withdrawn, was registered in 2015, has minor equity capital (UAH 1,000) and sole founder and chief manager.

Based on the given facts, the law enforcement authority carries out an investigation.



## Example

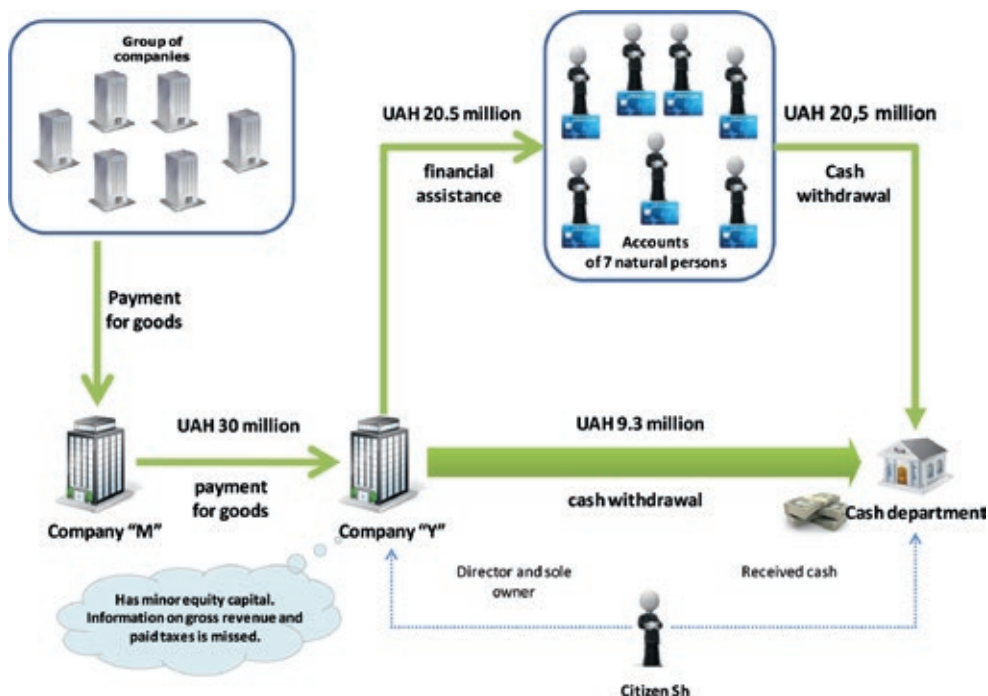
There has been the scheme of the activity of the “convert” center.

The group of companies transferred funds to be accumulated at the account of the **Company “M”** as payment for goods.

Further, non-cash funds in the total amount of **UAH 30 million** were transferred to the accounts of the **Company “Y”**.

Those funds received in the amount of **UAH 9.3 million** were partially withdrawn in cash by the director and the remaining amount of **UAH 20.5 million** was transferred as financial assistance to the accounts of **7 natural persons**.

The natural persons also withdrew mentioned funds in cash.



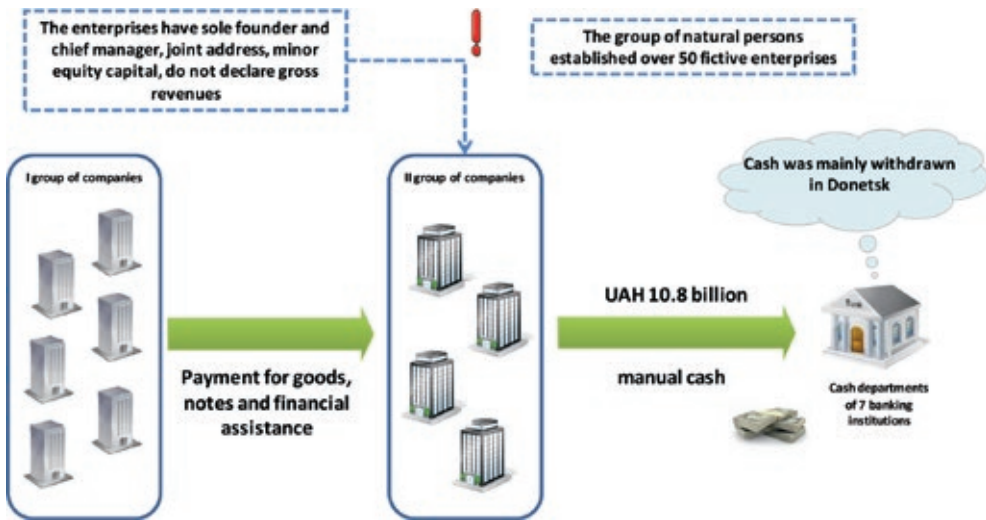
The **Company “M”** and the **Company “Y”** have minor equity capitals (UAH 1,000) and sole founder and chief manager, information on the declared gross revenues and paid taxes is missed. The accounts of the **Company “Y”** and natural persons are opened in the same banking institution.

Based on the given facts, the law enforcement authority carries out an investigation.

**Example**

There has been the scheme of operation of a large “convert” center in eastern Ukraine.

The group of natural persons established and purchased over **50 enterprises** used for accumulation of non-cash funds and further conversion into cash. Funds in the amount of **UAH 10.8 billion** were withdrawn in cash from the accounts of **7 enterprises**. Funds were withdrawn in cash departments of **7 banking institution** mainly located at the border of the temporary occupied territory. Previously non-cash funds were addressed from a large number of enterprises as payment for goods and notes, as well as financial assistance.



The enterprises have sole founder and chief manager, joint address, minor equity capital, do not declare gross revenues.

Based on the given facts, the law enforcement authority carries out an investigation.

## 8. Money laundering from cyberterrorism

Up to the date, cybercrimes are one of the most dynamic groups of socially-dangerous infringement. It is due to rapid growth of science and technologies in the sphere of computerization, as well as due to regular and rapid expansion of the sphere of computer techniques application.

The most sensitive for cybercrimes in the banking sector is online services or services of remove customer access to own accounts in banks, electronic wallets with the connected card accounts. Cases of thefts from the customer accounts of banking institutions are increasing.

The list of instruments to be used by cyber criminals for money laundering is quite wide, namely:

- use of the accounts opened under lost or fictive documents;
- opening of the account, including in the name of low-income citizens and fictive enterprises;
- use of international payment systems (e-payments);
- transfer of chain financial flows through several banking accounts with remote access;
- e-cash and cryptocurrency;
- involvement of nominees.
- The most popular ways of money laundering to be used by cyber criminals are as follows:
- funds transfer to the card and corporate accounts of natural persons with further cash withdrawal, including through ATMs;
- funds transfer through the accounts of persons and entities with further purchase of goods and services through Internet;
- conversion of funds into e-cash and further conversion into cash or purchase of goods;
- exchange/allocation of funds in electronic wallets.

### Example

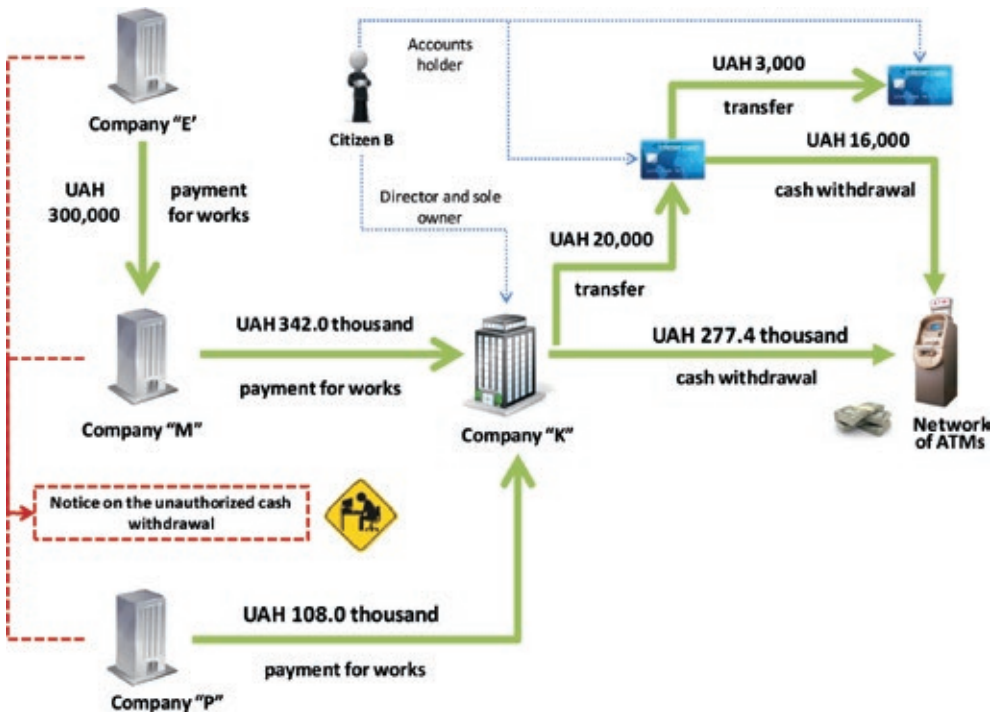
There have been found facts of unauthorized cash withdrawal from the accounts of a range of companies with their further conversion into cash.

During one day funds in the amount of **UAH 450,000** were withdrawn without authorization from the remote access accounts of three enterprises and credited to the account of **the Company "K"** with the purpose of payment "for works".

Further, a large portion of funds received in the amount of **UAH 277.4 thousand** was withdrawn in cash in ATMs. Other portion of funds in the amount of **UAH 20,000** was transferred to the card account of sole founder and chief manager of **the Company "K"** and further converted into cash.

**The Company "K"** has negative tax payer status (in the Unified State Register it is recorded on absence at the place of location), fails to declare gross revenues and pay taxes, being sole manager and founder.

Based on the given facts, the law enforcement authority carries out an investigation.



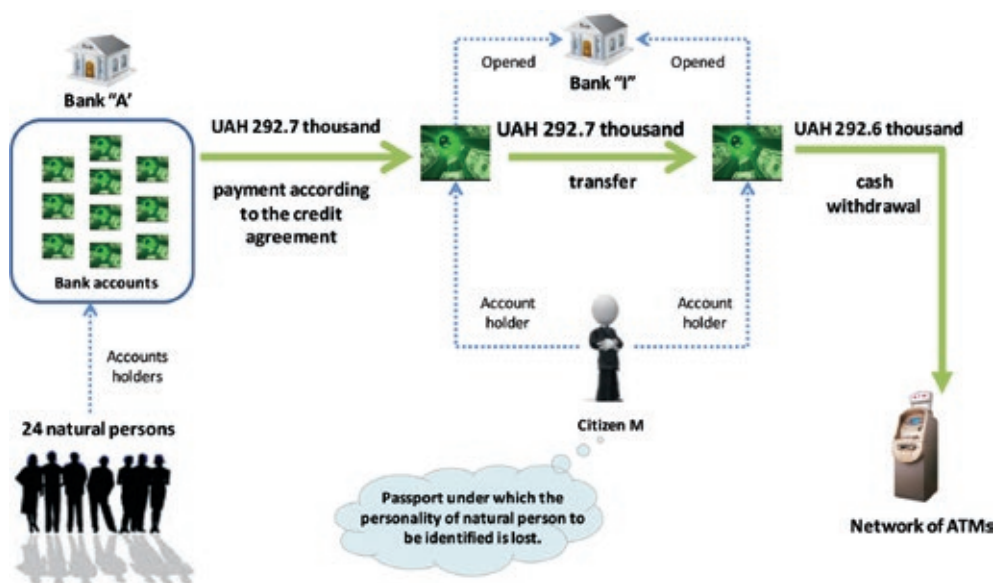
### Example

There has been the scheme of the fraudulent actions concerning unauthorized cash withdrawal from the accounts with remote access of the group of natural persons in the amount of **c 292.7 thousand**.

During a short period of time, funds were withdrawn from the accounts of **24** natural persons with authorization with the purpose of payment "payment under the credit agreement" to the account of one natural person.

Further, funds from the natural person's account were transferred to other account opened in the same bank and withdrawn in cash through ATMs.





The bank where the accounts of **24** natural persons were opened addressed to other bank-recipient with a notice concerning the fraudulent actions. The opened accounts have remote access.

Based on the given information, the passport of the citizen of Ukraine under which the personality of natural person to be identified is considered to be lost since 2011.

Cash withdrawal from the accounts of natural persons was made through the same IP-address.

Based on the given facts, the law enforcement authority carries out an investigation.

## 9. Legal investigations on terrorism (separatism) financing

Situation in the eastern regions of Ukraine requires for the strict measures to control over the financial flows. Determination and suspension of financial assistance for terrorist and separatist organizations should be one of the key trends of long-term strategy of the AML/CFT system. As the financing allows committing of terrorist attacks and appropriate training of terrorists (separatists).

The most spread instruments in the schemes of the financing of terrorism (separatism) are as follows:

- financial assistance;
- agreements on claims assignment;
- purchase of goods in the temporary occupied territory;
- involvement of charitable organizations;
- nominees.

Upon analysis, there have been found the following ways of the financing of terrorism (separatism):

- use of funds of natural persons for the financing of terrorism (separatism);
- funds transfer to the card accounts of those natural persons performing terrorist (separatist) activity;
- requirement of financial assistance from the entities by so-called officials of the "Donetsk People's Republic" and the "Luhansk People's Republic";
- involvement of "convert" centers;
- collection of funds in social networks as charity by the group of natural persons;
- funds transfer through electronic payment systems to the address of the nominees.

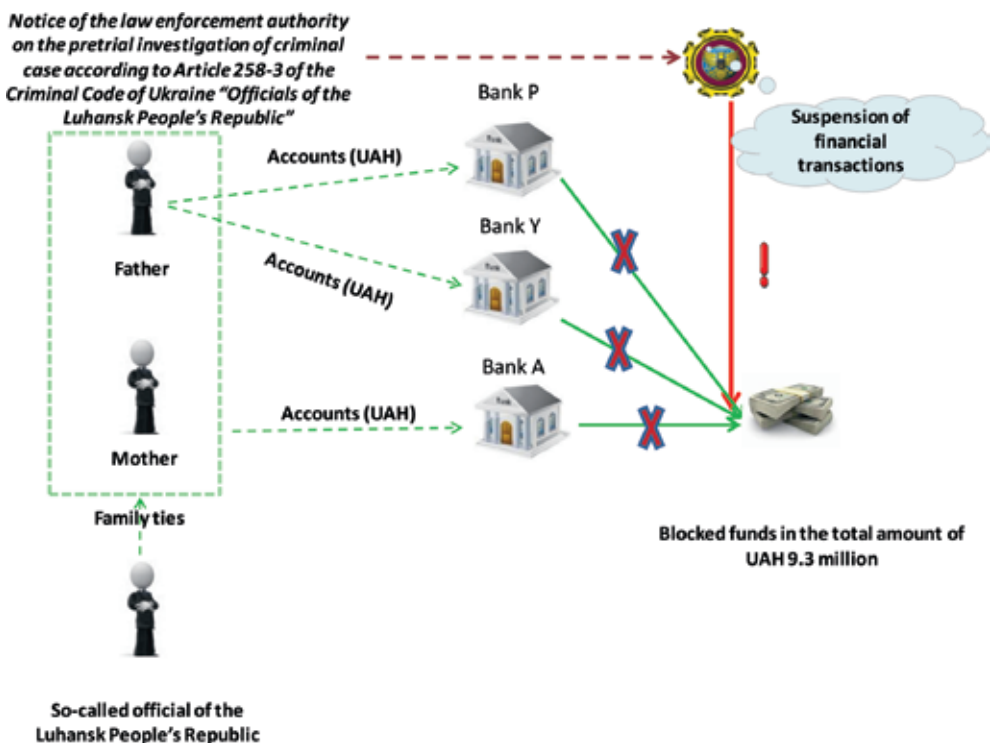
**Example**

According to the law enforcement authority, a number of natural persons settle financial transactions that may be connected with the financing of terrorist or separatist activity in the temporary occupied territories.

So-called official of the “Luhansk People’s Republic” transferred funds in large amounts to the accounts of close relatives (wife and father) in banking institutions. Funds were further withdrawn in cash and addressed for the financing of the “Luhansk People’s Republic”.

There have been found the financial flows under which the amount of settled financial transactions concerning so-called officials of the “Luhansk People’s Republic” significantly exceeded income received by him.

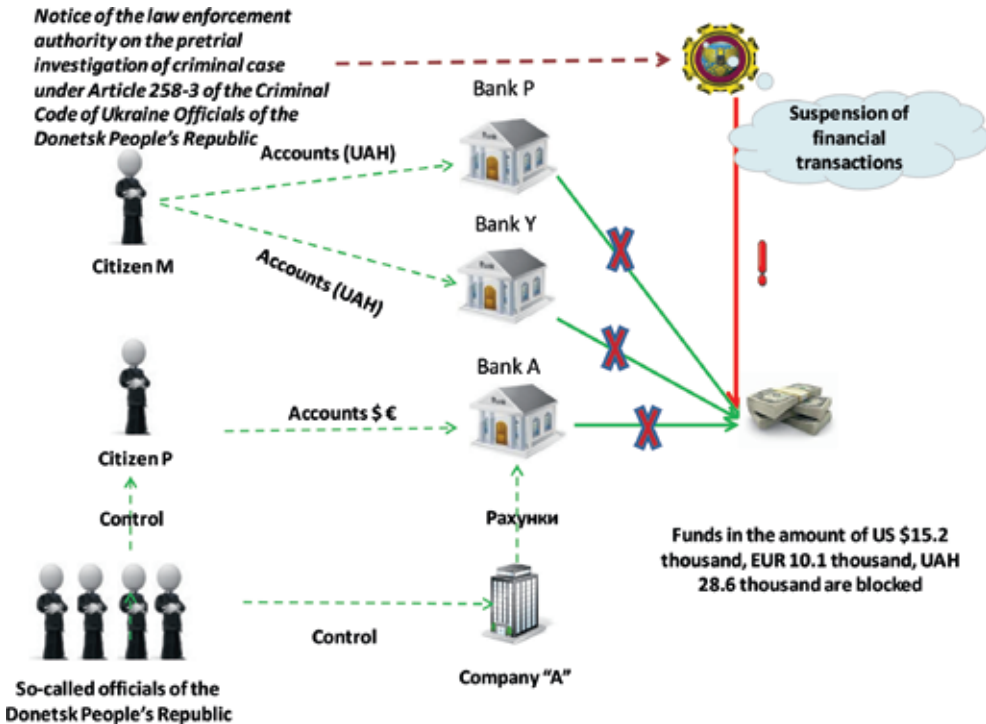
According to the analysis, there has been the balance at the accounts of the affiliated person; the amount of funds blocked constituted **UAH 9.3 million**.



Based on the given facts, the law enforcement authority carries out an investigation.

**Example**

According to the law enforcement authority, a number of persons affiliated with so-called officials of the "Donetsk People's Republic" settled financial transactions on the financing of separatist and terrorist activity in the temporary occupied territories.



The group of natural persons, so-called officials of the Donetsk People's Republic, transferred funds of the controlled enterprises to the own accounts in banking institutions or to the accounts of the affiliated natural persons. Funds were further withdrawn in cash and addressed for the financing of the Donetsk People's Republic.

Based on the analysis results, it has been found that the natural persons affiliated with so-called officials of the Donetsk People's Republic settled those financial transactions that failed to meet the declared income.

The remaining amount of funds constituted **UAH 28.6 thousand, US \$ 15.2 thousand and EUR 10.1 thousand**.

Based on these facts, the law enforcement authority carries out an investigation.



## Conclusion

Money laundering and the financing of terrorism are the essential component of the criminal world. Despite of the fact that a part of illegal income is used for illegal actions, a large part of income is invested into legal business.

The State Financial Monitoring Service, in close cooperation with the participants in the system of anti-money laundering, countering the financing of terrorism and the financing of proliferation of weapons of mass destruction, defines and suspends the scheme of money laundering and the financing of terrorism.

Rapid development of financial and information technologies, improvement and branching of relations both at the national and international levels facilitates and allows the criminals, organized groups and criminal groups to communicate, both within and without the territory of Ukraine.

New financial technologies influenced on the rate of cash turnover both in banking system and outside it, as well as a variety of forms of settlements between the participators, including those connected with the commitment of the financial crimes, such as money laundering.

The financial flows of money laundering as in previous years are aimed at their withholding or obfuscation of their further use through legal forms of the commercial activity.

In the process of the typological studies, it has been found that each year the schemes of money laundering become more complex and branched. A large number of participators and financial institutions from different regions of the country are involved in the schemes. The widespread phenomenon is participation of non-residents, both companies and banking institutions located without the territory of Ukraine.

It is not uncommon when one scheme of money laundering uses several financial instruments different by economic content and nature, for example: fixed and unfixed securities, credit and deposit contracts, debt obligations, "fictive" contracts.

Thus, determination and suspension of the schemes of money laundering and the financing of terrorism are the main tasks for all participators of the system of anti-money laundering, countering the financing of terrorism and the financing of proliferation of weapons of mass destruction.

Conducting of the typological study upon analysis of the financial flows allows defining of the entire situation and algorithm of money laundering or any other crime. To determine such schemes, it is required for an access to various information and definition of inconsistencies with the data known, as well as systematization of the analysis data.

As part of this study, instruments and ways of money laundering, the financing of terrorism (separatism) or other crime have been summarized.

In sum, it should be noted that the national AML system is operating, developing and improving.





**CURRENT TECHNIQUES,  
METHODS AND  
FINANCIAL INSTRUMENTS  
OF TERRORISM AND  
SEPARATISM FINANCING**

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**TYPOLOGIES 2014**

## Introduction

Up to the date, the problem of peace and international safety ensuring is vital for each country in the world. International terrorism violates the harmonious global development, as well as international peace and safety. Under such conditions, countering against terrorism is the matter of highest priority of the UN and other international organizations activity.

Expansion of terrorism and separatism in Ukraine formats the task of countering against financing and requires for strict measures to control over financial flows. Thus, activity on determination and efficient blocking of financial chains support of terrorist and separatist organizations should be one of the key focuses of long-term strategy of state authorities. As the financing provides an opportunity for making terrorist acts, provides relevant training of terrorists, their technical equipment and other required costs, and its suspension could be the best weapon in counterterrorism.

Expansion of financial control under conditions of counterterrorism and separatism defines the location of Ukraine and characteristics of activities of certain state authorities to address these problems. Methodologies for identifying the financing of terrorism and separatism, according to the national legislation, the development of international cooperation and information exchange are the essential conditions for detection and neutralization of the financial infrastructure that fuels activity of terrorist and separatist organizations.

Countering the financing of terrorism and separatism should include a set of measures of organizational, legal, economic and political nature in the international and domestic space to be made by all participants of this process in order to prevent terrorist acts and attacks on the territorial integrity of the state.

## Rationale

Rationale is conditioned by sharp increase in the financing of terrorist and separatism in Ukraine and the number of crimes under the International Convention for the Suppression of the Financing of Terrorism, 2000, the majority of which are to be committed by the citizens of Ukraine, Russian Federation and entities that are registered and/or staying on its territory. From March 2014, on the territory of Ukraine there are illegal terrorist organizations "Donetsk People's Republic" and "Luhansk People's Republic".

New challenges caused by the threat of the financing of terrorist and separatism in Ukraine require for the implementation of qualitatively new methods of detecting, preventing and countering such activities. Typological synthesis of schemes of the financing of terrorism and separatism will help the participants in the national AML/CFT system to reallocate the existing resources to effectively counter the identified threats and leveling the existing vulnerabilities.

Conducting this study will be the basis for implementation by Ukraine of the first FATF Recommendation concerning risks assessment and implementation of measures underlying its urgent character.



## Goal of study

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At the time of this study, the threat of terrorism and separatism in Ukraine grew into a direct military confrontation beyond this study.

Development of the events in regions have being suffered from the actions of terrorist groups showed the similarity of their scenarios. Previous dismantlement of situation often involves local population that through deception, threats and imposing fictive patriotic ideals were used in carrying out acts of civil disobedience and other actions aimed at violent change or overthrow of the constitutional order, seizure of state power, commitment of terrorist attacks, membership in illegal armed formations.

The organization of these actions, in particular, requires for financial support at places. These are the activities of foreign sabotage groups, local pro-Russian activists and movements, as well as measures to finance their activities.

If detection and prevention of activity of such persons and their communities are under the responsibility of the intelligence agencies, the task of identification and freezing the system of the financing of such activities is imposed on the system of financial monitoring.

The study is focused on establishment and generalization of typical methods, ways, financial instruments and schemes of the financing of terrorism and separatism at the existing risk level, determination of any possible ways for improving the system of countering the financing of terrorism to prevent implementation of these threats.

## Object and subject of study

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Current terrorist and separatist activity may be made by the following main methods:

- Through direct material and financial security, including by cash;
- Through financial support with involvement of intermediaries, including participants in the financial system.

The object of study – schemes of financial support of terrorist and separatist activities with the methods and participants in the financial system.

The subject of study – main threats and weaknesses spreading such crimes.

## Main tasks of study

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Such typological study is the element of the National risk assessment, mainly focused on determining threats and weaknesses, risk assessment and its neutralizing.

The main tasks to be achieved within this typological study are as follows:

- determination of weaknesses of the financial system that may be used for the financing of terrorism and separatism;
- assessment of probabilities of the threats of the financing of terrorist and separatist activities based on the existing weaknesses of the financial system;
- determination of any possible measures to minimize or eliminate the negative affect of the defined threats, to eliminate or reduce the weakness.

These issues are interdependent and could not be viewed separately. The answers to these questions combined in a single analytical conclusion will provide an opportunity to highlight the weaknesses, such as how and where the financial sector is subject to the risk of being used for the financing of terrorism and separatism both in separate organizations and at the sector level. It also will provide an opportunity to bring typological examples, identify the existing trends and identifying indicators (“red flags”).

Also, the goal of this typological study is focused on creation of the analytical framework for making further decisions about appropriate countermeasures at the national level and proposals for their support by the international community.

It also should be noted that this typological study shall not task concerning determination of reasons and conditions under which terrorist organizations and separatist movements perform their activities within the territory of Ukraine and, accordingly, use its financial system.

## Background

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The Financial Action Task Force on Money-laundering (FATF), as an intergovernmental authority established in 1989, also explores the issue of the financing of terrorism. FATF sets standards and promotes effective implementation of legal, regulatory and operational measures for anti-money laundering, countering the financing of terrorism and other threats to the integrity of the international financial system. In cooperation with other international partners, FATF identifies weaknesses at the national level to protect the international financial system from abuse.

Study of the question of the financing of terrorism was highlighted in the following international typological reports of FATF and its regional units:

- the risk of the financing of terrorism through non-profit organizations (2014);
- the financing of terrorism in West Africa (2013);
- typological studies of FATF on the financing of terrorism (2008).

On the side of the State Financial Monitoring Service, typological study will be based on information transferred as a part of general and additional general materials with possible signs of the financing of terrorism and separatism.

Also during this study, it was used for common national information from the Unified report on criminal offences and information of the law enforcement authorities concerning actual proceedings to be conducted by the law enforcement authorities within the current period. In addition, information received from the financial sector may also serve as one of the data sources that could

provide the possibility to define the main types of financial instruments to be used in the schemes of the financing of terrorism and separatism.

## Section 1. Risk of the financing of terrorism and separatism

### General description

The risk of the financing of terrorism and separatism should be defined as the derivative of the *threat* of terrorist activity or separatism and *weakness* of the financial system to be used for the financing of such activity.

According to the FATF Manual “National Money Laundering and Terrorist Financing Risk Assessment”, the threat is a person or a group of persons, object or activity that could potentially cause harm, such as to state, society, economy, etc. In the context of the financing of terrorism or separatism, this term includes criminals, terrorist groups and persons supporting them, their resources, and past, present and future activities of the financing of terrorism or separatism.

In that sense in which it is used under risk assessment the term “weakness” includes those areas where threat could be implemented, or anything that may support or contribute to its implementation.

The threat of terrorism or separatism, depending on the conditions of its origin, could be both internal and external. As already noted, Ukraine has not been suffered from such activities before; there has been found no presence of active forces of international terrorist groups in its territory. Furthermore, in the absence of radical sentiment in the society, the onset of the high risk of terrorism or separatism was hardly probable.

On the other side, the weakness of the financial system, including the possibility to be used for the financing of terrorism or separatism, exists regardless of the level of threat of such activity. It may include peculiarities of a certain region, sector, financial product or type of services that make them attractive for the financing of illegal activity.

### Backgrounds

According to the recent assessment of the mode of anti-money laundering and countering the financing of terrorism to be made by the experts of the Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism (MONEYVAL), Ukraine has not been suffered from internal terrorist accidents, although the law enforcement authorities sometimes defined some crimes as terrorist-related crimes.

Analysis of criminal cases to be conducted showed that there were not attributable to terrorist activity and there was not found for any sign of participation of any natural person or legal entity in Ukraine or abroad for the financing of terrorism.

*Thus, in particular, analysis of criminal cases to be conducted by the investigative authorities of the State Security Service of Ukraine connected with the commitment of any terrorist act gave the basis to note that the given crimes were committed mainly from molester motives or in order to redistribute property and were not connected with the organized terrorist activity. Besides, the units*



*of the State Security Service of Ukraine have not found any fact of participation of natural persons and legal entities of Ukraine within and without its territory for performing activity connected with the financing of terrorism.*

*Based on information received by the State Security Service of Ukraine, there were no structural units of international terrorist and religious extremist organizations within the territory of Ukraine, there were no members of such organizations. Ukraine has not been suffered from any terrorist attacks from their side and up to the date there were no backgrounds for terrorist attacks.*

However, the situation has dramatically changed in early 2014.

The nature of events, in particularly, at the first stages of escalation of terrorist threat and the threat of separatism in Ukraine, reflects the use of the financial system for integration and readdress of financial flows to be addressed for support of such criminal activity.

While high level of threat of terrorist and separatist activity in Ukraine is the actual factor, the general level of CFT system weakness should be defined for further development and implementation of countermeasures.

### **Threat level**

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As mentioned, up to the date, the high level of threat of terrorist and separatist activity (and also the financing of such activity) in Ukraine is the actual factor that has been transformed into the threat of direct military invasion. It is hardly to understand as Ukraine has not been suffered from internal terrorist accidents and analysis of criminal cases to be conducted by the law enforcement authorities showed that they were not connected with terrorist activity and there were no signs of participation of natural persons or legal entities in Ukraine or abroad for the financing of terrorism.

Also it was proved by the statistics based on the received general materials concerning the doubts on the financing of terrorism. Thus, in 2013 the State Financial Monitoring Service prepared and addressed for consideration to the law enforcement authorities 4 general case files of the above category.

The materials, being transferred to the law enforcement authorities, included information concerning notice on financial transactions connected with crediting of cash, cash transfer, granting of credit, payment of contribution to the funds of construction financing and payment for dual-use goods.

During 9 months in 2014 the State Financial Monitoring Service prepared and addressed for consideration to the law enforcement authorities 61 general and additional case files connected with the financing of terrorism and separatism. It is in 17 times more than for 2013. It also proves the growth of such threat level.

The transferred general materials were as follows:

- activity of charitable organizations for the financing of organizations connected with terrorism and separatism;

- public organizations and public Russian-minded persons;
- the financing of sports bases to be used for preparation of soldiers for their participation in riots by means of cash transfers through the Ukrainian international monetary system.

Growth of threat level of the financing of terrorism and separatism is also proved by the indicators from the unified report on criminal offences. Thus, during 2013 no offence on violation of foreign territorial supremacy and sanctity of Ukraine was recorded (Article 110 of the Criminal Code of Ukraine and only one accident of the financing of terrorism (Article 258-5 of the Criminal Code of Ukraine). At the same time, during 9 months in 2014 it was recorded for 258 offences on violation of foreign territorial supremacy and sanctity of Ukraine and 36 facts of the financing of terrorism.

### Threat sources

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The sources of terrorist threat and threat of separatism are based on economic, social and political, national and ethnic, religious and some other processes in Ukraine. Geopolitical factor is special, being the main catalytic element of the external threat.

In the current situation, the factor of external interference is significant. All internal stress points in the society were successfully used for escalation in the conflict.

However, analysis of the terrorist threat and the threat of separatism is not the objective of this study. Intending to highlight the matters of threat of the financing of terrorism and separatism, this study will consider the matters of sensitivity of the financial system that may be used by any terrorist and separatist organizations.

The greatest challenge of defining the source of the financing of terrorist and separatist activity and, accordingly, its prevention is focused on the fact that such financing may be made from legal sources, transfer amounts may be minor and financial transactions may not be different from other.

Investigation of terrorist attacks took place in the USA in September of 2001 showed that the CFT system was not appropriately developed rather than broken so that to define such "common" transactions.

The threat source includes regularity of financial transactions, lack of peculiarities of definition, branching of financial institutions, transfer mobility and deep level of penetration of financial services for all social groups (easiness of the financial service application).

Concerning the sources of the financing of terrorism and separatism, it should be noted that up to the date there is a lack of statistical data on the basis of which it may be concluded about all sources of their financing.

Also, as informed by banks, the large number of facts connected with the financing of terrorism and separatism appeared to be in south-eastern Ukraine. The detailed allocation of facts defined is given in Figure 1.

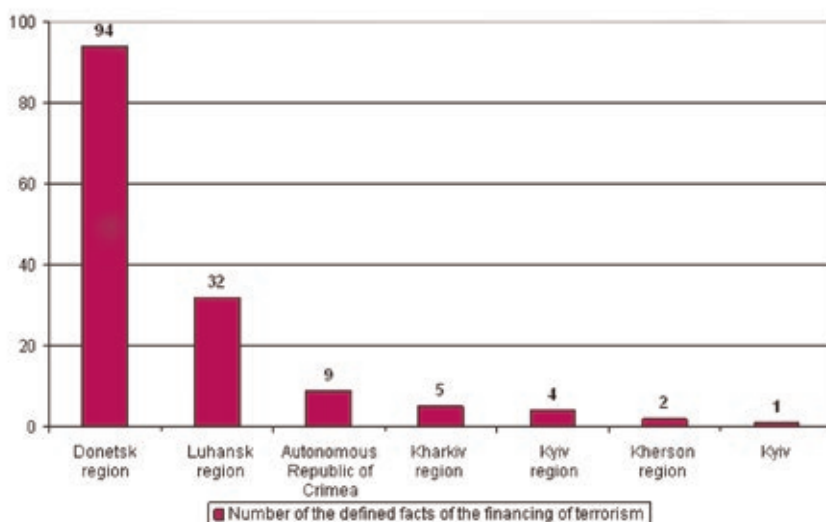


Figure 1. Number of facts defined by the banking institutions that may be connected with the financing of terrorism and separatism

### Weakness of the financial sector

The system of countering the financing of the terrorist and separatist activity in Ukraine is according to the international standards in this sphere (FATF) approved by the Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism (MONEYVAL).

Nevertheless, there is no financial system that may be protected from any potential use for the financing of the terrorist and separatist activity.

Among millions of financial transactions and thousands of financial instruments, those to be settled and used for the financing of the terrorist and separatist activity have corrupted nature and remain unchanged in form, peculiarities and features.

The point at issue is that, starting from any period of time, common, financial transactions may have disguised purpose, at this, any existing features remain unchanged, and thus, all mechanisms appear to be applicable.

It should be noted that it does not mean non-ideality of the countering mechanisms. There is a certain *objective level of sensitivity of any financial system*, firstly, due to the social factor.

Considering the financial system as a block of members and mutual relations between them, the system of countering the financing of terrorism and separatism, firstly, such mechanisms of countering as identification by the financial mediator of persons (customers) applied for financial services and

search of financial transactions to be settled by such persons for identification of those that may be affiliated to the financing of terrorism and separatism.

Financial transactions, being not subject to the requirement of identification of their initiator according to the legislation, may be used for the financing of terrorism and separatism. In Ukraine those financial transactions to be settled through payment systems, including with e-cash in the amount not exceeding UAH 10,000 or the amount in foreign currency that in the equivalent not exceeds UAH 10,000 are subject to the mentioned risk zone.

The up-to-date information technologies allow rapid settlement of the above mentioned financial transactions without direct contact of the initiator and the subject of financial monitoring. In principle, the cyber domain has no restrictions, thus, there is a possibility of formation of a great number of virtual members by criminals (e-wallets, virtual payment ways, etc.) for cash transfer. As a matter of fact, legislative restrictions do not permit to use this channel of cash transfer for large amounts of funds; however it may be successfully used for the targeted aid.

Thus, law enforcement authorities have found a lack of control over e-transfers through national and foreign payment systems as main sensitivity of the financial system that may be used for the financing of terrorism and separatism.

#### Example 1

In the process of conducting the monitoring of financial transactions of customers that made single cash transfers to the accounts of natural persons involved in the financing of separatism, one of the banks has found information included the fact that payment cards of this bank should not be used for assistance of "Donetsk People's Republic" and "Luhansk People's Republic", it was recommended to use such payment systems as Webmoney, Yandex money, Qiwi.

Moreover, even those financial transactions, including preventive measures from the side of financial mediators, as previously defined, may appear to be the disguised financing of terrorism and separatism, though being not characterized with the identifying features of detection.

#### Example 2

According to the monitoring of customer transactions of one of the banks, there have been found funds transfers from the current accounts using special payment methods (accounts were opened in Donetsk region) to the account of the counteragent – natural person in other bank. The amounts of payments were various (from 20 up to 250 UAH) and irregular (source of funds at the accounts of bank customers that initiated funds transfers – in general, targeted use: salary, pension benefits). Basic transfers were made with the purpose of "private transfer", but there have been found transactions on funds transfer with the purpose of "assistance", "for purchase of drug products". According to further analysis conducted, the person having received funds to its account appeared to be the member of "Donetsk People's Republic".



The schemes of the financing of terrorism and separatism may also be implemented through settlement of financial transactions through various banking institutions that makes it difficult to define.

Thus, the existing objective weaknesses of the financial system multiplied by the scope of use may present high risk of the financing of terrorism and separatism, but only under conditions when the threat from the side of terrorist and separatist organizations becomes accidental.

### **Difference of the financing of terrorism from money laundering**

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As previously noted, terrorists need funds to buy weapons, equipment, inventory and services. Funds may be transferred to them from the country (terrorism financing by the country) or from any private sources (from certain persons, companies, charitable and other non-government organizations) – often in form of minor, but numerous donations.

Funds to be transferred to terrorists may have legal or criminal source. According to the research organization **Council on Foreign Relations**, the main problem of defining the financing of terrorism is that 70% of all funds are to be received by terrorists from legal sources (though they use even illegal sources: illegal traffic, extortion racket, drugs traffic, arms traffic, etc.). Terrorists receive most of funds from business, charitable foundations and private sponsors that are often not aware of the purpose of funds use.

While laundering means funds management as a result of a predicative crime, the financing of terrorism, being a crime on its own, supports further commitment of a serious crime.

The objective of any investigation also differs, upon laundering it is focused on the open verdict and, accordingly, to be conducted by the law enforcement authorities against the cases of the financing of terrorism when the investigation is focused on prevention of a serious crime and to be conducted by the intelligence agencies.

Ways of criminal proceeding concerning money laundering and the financing of terrorism are similar under the fact that in both cases information on financial transactions should be collected. Such information may be included in financial reports from internal or international sources, as well as from witnesses.

However, there are differences. Upon investigation of any offences connected with money laundering, the law enforcement investigation considers that funds move from the offence to the lawbreaker and then, as a rule, to purchase of property (cars, jewelry, real estate, etc.). Upon the financing of terrorism, it should be tracked for cash flow from their source (income from criminal activity, donations) to terrorist organization and then to the certain terrorists or terrorist organizations that use them, act based on them, spend them for organization of terrorist attacks.

Differences between the financing of terrorism and money laundering also raise the problems to those financial mediators obliged to define these facts. The fact is that legally gained cash, minor transfer amounts and lack of visible symbols of suspicion (“red flags”) makes the financing of terrorism quite non-visual.

In the final count, the chief object of the countering the financing of terrorism is prevention of any terrorist threat of using the sensitivity of the financial system, i. e. risk control.

### **Direct support and use of the financial system**

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As previously noted, terrorist and separatist activity means the necessity of financial assistance. It is referred to the organization of actions and support of organizational form, the expenses on information campaigns, the involvement of new members.

Depending on the scope of activity, geographical location, desired goals and number of members involved, on the one hand, and available resources, their types, possibility of transfer and branching of representatives, on the other hand, the methods of financial assistance of terrorist and separatist activity vary.

It should be noted that the practice of countering the financing of terrorism by the world community proves the fact that terrorist organizations intend to use the simplest, the most available and understood methods of funds transfer.

Financial assistance of terrorist and separatist activity may be made both through the direct transfer of assets, funds and weapon and through remote control, i. e. use of the financial system services.

Those examples describing the cases of direct assistance subject to investigation are given below.

#### **Example 3**

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Early June 2014, the exact date and time are not given, staying in the territory of the town Yenakiyevo, Donetsk region, the Citizen X, date of birth 1951, willfully transferred to the representative of the terrorist organization "Donetsk People's Republic", nicknamed "Y", funds in the amount of UAH 200 and material valuables in the amount of UAH 20,000, i. e. committed an action of financial and material security in favor of the terrorist organization "Donetsk People's Republic".

#### **Example 4**

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The Citizen X, date of birth 1959, on 05.05.2014 in the town Druzhkivtzi, Donetsk region, for financial assistance of the terrorist organization, willfully transferred to the member of the terrorist organization "Donetsk People's Republic" funds in the amount of around UAH 17,000, thus, committed in its any the financing of terrorism.

### Example 5

The Citizen X, date of birth 1960, on 03.06.2014, transferred funds in the amount of UAH 3,000 in the name of the Citizen W. At this, the Citizen X understood that funds would be spent for financial security in order to promote the commitment of terrorist attack using the mentioned funds. Thus, intending to provide the involvement of the group of persons in the commitment of terrorist attacks against the members of anti-terrorist operations in the territory of Luhansk region, the Citizen X willfully transferred the mentioned amount of funds to the Citizen W for organization by the latter of the involvement of persons in armed conflicts on the side of "Luhansk People's Republic" against the members of anti-terrorist operations in the territory of Luhansk region, funds mentioned were used by the latter for transportation of persons to Luhansk and provision of their staying in the territory of the given town.

### Example 6

In May-July 2014, in Moscow, Russian Federation, being in collusion with the group of persons, the Citizen X and the Citizen W charged and accrued funds, ammunition, office automation equipment, drug products, food and further transfer and delivery to the member of terrorist organizations "Donetsk People's Republic" and "Luhansk People's Republic" in the territory of Luhansk and Donetsk regions of Ukraine.

Thus, the Citizen X and the Citizen W committed the financing of terrorism, i. e. those actions taken for financial and material security of terrorist organizations, organization and commitment of terrorist attacks, promote of the commitment of terrorist attacks.

It should be separately considered for the activity of cash couriers. On the one hand, cash couriers are involved for the provision of direct financial assistance and, accordingly, for avoiding financial monitoring in the financial system. On the other hand, FATF Recommendation 32 directly highlights the necessity of the implementation of countermeasures against such activity from the side of the AML/CFT system.

However, it is referred to cross-border funds and jewelry transfer through the organized checkpoints at the state border. Under conditions when Ukraine is unable to control over a part of its border due to the military acts, the countermeasures against transfer on these zones are impossible<sup>2</sup>.

According to the example above, cash couriers are involved between the territories of those regions of Ukraine suffered from terrorist attacks and separatist movements.

<sup>2</sup> It is referred to the countermeasures specified in FATF Recommendation 32.

### Example 7

In July of the current year, the citizens of Zaporizhzhya, being on duty at the checkpoints (route section Zaporizhzhya – Donetsk towards Donetsk), upon vehicle inspection driving towards Donetsk, found a large amount of funds. When the law enforcement officers found the conditions of funds transfer, they also found that such funds were intended to be transferred from the Autonomous Republic of Crimea to Donetsk through Zaporizhzhya region for further potential financial assistance of the members of “Donetsk People’s Republic” in eastern Ukraine, mainly, salary to the members of the terrorist organization “Donetsk People’s Republic”.

It should be noted that terrorist organizations and separatist movements may independently provide their life being at places of active performance at cost of the involvement of local population, building, processing and production funds in the region of performance.

The example of the mentioned self-support may be “The Islamic State of Iraq and the Levant” (ISIL) concerning to which the President of the USA announced on the intent to apply to the Congress of the USA for receiving the permit for taking military actions against it.

The ISIL established a control over the part of territory of its performance located within the territory of modern Iraq, Syria, Jordan and Levant. Due to control over the oil zone in southern Syria, the ISIL can earn from 1 up to 2 million USD per day.

We can draw a parallel between Ukraine when enterprises are captured and operated, mainly, those coal mining enterprises, in the temporary occupied territories. Other enterprises and population are forced to pay for so-called “taxes” to be charged by the representatives of occupiers, terrorist organizations and separatist movements.

### Example 8

Within the period from April of the current year, the officials of the Company “X” support illegal activity of terrorist organization (as defined in Article 1 paragraph 16 of the Law of Ukraine “On the Fight against Terrorism”) “Donetsk People’s Republic” through funds transfer at the address of the latter received by the Company “X” from sales of coal mining products to be recovered without any permits by the third parties without reporting on any financial transactions on financial accounting and reporting.



### Example 9

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The former head of the structural unit private of the Company "S" in the Autonomous Republic of Crimea, the Citizen X, date of birth 1971, and the former deputy head of the same structural unit, the Citizen W, date of birth 1959, acting in the collusion with other unidentified persons and performing control over the activity of the mentioned structural unit, within April-May 2014 in the territory of the Autonomous Republic of Crimea, effected the financing of terrorism, in particular: used property of the Private Company "S" transferred for their possession (corporate rights are state-owned) for the financing of the activity of illegally established armed organizations involved in terrorist activity in the territory of the Autonomous Republic of Crimea and continued to effect the financing of terrorist activity of such illegally established armed organizations in the territory of eastern Ukraine in order to destabilize the social and political situation.

### Example 10

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From June of the current year up to the date, the Citizen X, for effecting financial and material support of the terrorist organization "Luhansk People's Republic", regularly charges and receives from the enterprise heads located in the territory of the town Alchevsk, Luhansk region, funds in form of tax levies. The latter transfers the mentioned funds to the town Luhansk to the representatives of "Luhansk People's Republic" for the financing of its terrorist activity.

### Example 11

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In June of the current year, the Local Department of the Ministry of Internal Affairs of Ukraine in Luhansk region initiated an investigation on the fact that the director of market "S" located in the town X of Luhansk region, the Citizen X claimed funds for the financing of "Luhansk People's Republic".

## International studies

Meeting the up-to-date challenges, the world community gives full attention to the studies focused on the peculiarities of the activity of terrorist groups, including those fighting for recognition and receipt of independent status of separate territories, in the world and search of the countering measures.

Tragic events in 2000 in the United States of America (Terrorist attacks 9/11), Great Britain (2005) and other signaled on the fact that the external terrorist threat became internal. Globalization of international relations, reduction of the mechanisms of capital transfer and migration policy allowed terrorist movements to adapt to the modern conditions and deep penetrating into area of the world community.

Investigation of the high-profile terrorist attacks, in particular, described in *“Monograph on countering the financing of terrorism (9/11)”* (USA) and *“Official conclusions of the Committee concerning explosions in London in July 2005”* highlights the undisputed fact of using the international financial system by terrorist community for supporting activity of own representatives in the world.

Thus, for example, those persons involved in terrorist attacks 9/11 (USA) and in London on July 07, 2005, did not use any fictive documents, had opened bank accounts and made international transfers on their behalf.

Moreover, commitment of terrorist attacks does not require for large financial expenses. The cost of any terrorist attack committed by the organization “al-Qaeda” in 1998 (explosions of the Embassy of the USA in East Africa) is estimated in the amount of US \$ 10,000, in 2002 (explosions on the Bali Island) – US \$ 20,000, and the most scaling terrorist attack in the USA in 2001 is estimated in the amount of US \$ 400-500 thousand. It seems that great expenses in the financing of terrorist organizations include cost of living of such organization.

In response to new challenges and for countering the financing of terrorism at the beginning of the early two thousand years, the FATF reviewed the FATF Recommendations.

In 2008, for inspection of the efficiency of the measures to counter and summarize the common practices of determination, the FATF conducted the typological study “Terrorist Financing”. According to its results, there have been found the world trends of the financing of terrorism, in particular:

- terrorist organizations differ by size, level of centralization and ideological orientation;
- demands in the financing of terrorist organizations are different;
- commitment of a certain terrorist attack by one person or by a group of persons does not require for any large financial expenses;
- on the other hand, support of the network of representatives all over the world requires for a large amount of organizational expenses;
- the financing of terrorist activity may be made both at cost of funds received from legal sources and at cost of illegal business that terrorist organizations may perform;
- terrorist organizations use a wide range of methods and schemes of the financial resources transfer in the financial system, in particular – trade payments, cash couriers, charitable organizations, alternative payment systems, etc.

- It is interesting that those methods and schemes of money transfer by terrorist groups as identified upon the above mentioned study were approved in 2013 in the article of the professor Michael Freeman and Moyara Ruehsen "Overwiev of terrorism financing methods" (journal "Perspective on Terrorism" 2013, revision 4).

Thus, among the widespread schemes of money transfer by terrorist groups there are following: cash couriers, informal transfer systems (Hawala and other), services of cash transfer, use of banking system, fictive trading payments and trade with luxury goods.

Terrorist organizations are forced to use the schemes of cash transfer as the sources of funds and funds purpose may be located in various countries or even in the various continents.

Choosing the scheme of cash transfer, terrorist organizations take into consideration geographical location, primary type of assets, its amount, necessary transfer speed, transfer cost and potential risk level (theft, exposure by the law enforcement authorities, etc.).

In case of rapid transfer of a minor amount of funds, it is usually used for informal transfer systems (Hawala and other) and services of funds transfer (Western Union, MoneyGram, etc). For more detailed analysis of this type of transfers, it is recommended to overview the FATF study "Role of Hawala and Other Similar Service Providers in ML/TF" (2013).

Hawala (Hundi) in South Asia, Fei-Chien in China, Padala in the Philippines or Fei-Kwan in Thailand are the remittance systems established on the basis of clearing between their participants. Historically, these systems appeared prior to the establishment of banking institutions and, up to the date, they provide demands in offsets and transfers in trade and social spheres of life.

Existence of the mentioned remittance systems is due to the historical backgrounds, cultural peculiarities in the regions of activity, as well as insufficient level of penetration of services into the financial system among socially disadvantages persons and its costs. Lack of controlling procedures and KYC (know your customer) is also important.

In the classic sense, any informal transfer system looks as follows. Owners of services apply to the participants in the remittance system and give all funds necessary in cash. The participant in the system communicates with his colleague at the point of funds transfer and informs the transfer term. In turn, the owner receives password that the recipient of funds should use at the point of transfer purpose. In fact, funds transfer is not made, further, the founders in the system should make setoff or negotiate on transfer of claim difference.

It should be noted that, upon development of international economic relations, informal transfer systems gave the possibility of deep integration into global financial system. Thus, in order to make mutual setoff of the founders of payment systems, bank accounts of legal business (trade, production, services), prepaid (debit) cards, legal payment systems, cash couriers, private transfers of natural persons through banking institutions should be used.

It is impossible to define the amount of payments through informal transfer systems. In the above mentioned study it is noted that from 10 to 50% of all funds transfers are subject to such uncontrolled systems.

Thus, informal transfer systems carry serious threat of the financing of terrorism. In turn, the financial system has weaknesses that allow using of transfers in different ways.

In order to define any financial transactions that may be connected with the operation of informal transfer systems, it should be focused on the defined risk criteria:

- crediting to the bank accounts of natural persons of minor amounts or regular crediting of large amounts of cash to be further transferred to foreign accounts;
- regular transfers of funds to such international centers as Dubai (a majority of transactions of informal transfer systems is made through a certain international point, for example, Dubai);
- account to be used as a temporary repository;
- replenishment of the same bank account by different natural persons with further e-transfer abroad or cash withdrawal through ATMs;
- regular international e-transfers through bank accounts of the organizations not connected with the declared types of activity.

Moreover, in spite of the level of modern global and informational support that significantly facilitates the organization of informal transfer systems, standard cash transportation by cash couriers remains as simple and clear way of exchange (jewelry).

It should be noted that physical exchange has a range of weaknesses. The term of such transfers is longer and transfer is at risk of theft and exposure by the law enforcement authorities.

Moreover, transfer of large amounts is restricted by size and weight of cash. Thus, the amount of US \$ 1 million in US \$ 100 bills weighs 9 kg, and US \$ 20 bills – over 45 kg. At the same time, services of physical transportation remain popular.

As previously noted, choice of the scheme of funds transfer depends on a range of conditions. Choice of cash couriers may be based on the type of asset (gold, diamonds), geographical location (transfers of drug traffickers in Afghanistan, Pakistan) and other.

Thus, in the FATF study “Financial flows linked to the production and trafficking of Afghan opiates” (2014) it is specified that cash couriers are involved in activity in order to provide mutual payments for drugs within the territory of Afghanistan, Pakistan, Iran and Tadjikistan. The organized criminal groups of Turkey pay for deliveries from Iran in cash and gold involving cash couriers. According to the UN Sanctions Committee concerning al-Qaeda and Taliban, one third of budget of Taliban is granted through opiate traffic. Thus, the cash courier services remain those to be in demand from the side of terrorist movements.

Depending on geography of use, there have been found differences of activity of cash couriers. Thus, the FATF study “The financing of terrorism in east Africa” (2013), without limitation, describes “know-how” of terrorist organizations as involvement of women as cash couriers, as the majority of the customs service employees are men making a profession of faith in Islam which canons



prohibit men to touch women if they are not married. Inability of state authorities to perform proper control of the customs territories caused that cash couriers also transport weapons and explosive devices, besides cash funds.

It should also be noted that the involvement of cash couriers for the direct financing of the trigger-man has own peculiarities. The amount of such transfer will be rather minor, even for official border crossing. That person obliged to transfer cash should enjoy confidence of terrorist organization. Unfortunately, as specified in the article of the professor Michael Freeman and Moyara Ruehsen "Overwiev of terrorism financing methods" (journal "Perspectives on Terrorism" 2013, revision 4), even nowadays such cash transportations may not raise suspicion.

In cases when there is a demand in funds transfers to the western countries, terrorist organizations should find any ways for assets integration into the financial system. One of such ways may be use of the banking system, namely – accounts of actually existing enterprises for funds transfer not connected with production or trading activity.

The bright example of using legal business for disguise of activity of financial settlements center may be the example of the involvement of those companies performed honey export from the United States of America. Before terrorist attacks in 2001, founders of informal transfer systems, including those involved in terrorist organizations, used to engage companies performing export of hive products from the USA. As usual, the price of products was inflated and among the counteragents there were those staying in the countries calling for special attention from the side of the financial controlling (for example, Yemen). Thus, funds transfer required for the needs of payment system mediators was made due to transfer of the amounts exceeding the actual good value.

Among other examples of using legal business for the financing of terrorist organizations, it should be given for the example of import of the used cars from the USA to the countries of East Africa. According to the results of investigation conducted by the US competent authorities, the real goal of funds transfer was money laundering from the sales of drugs by the members of the terrorist group Hezbollah.

There are cases of organization of fictive payments between the natural persons, in most cases such transfers are to be declared as trading transactions, including with luxury goods or consumer goods.

In order to define those financial transactions potentially connected with legal business for the financing of terrorist organizations, the defined risk criteria should be taken into consideration:

- purchase, transfer and, finally, sales of material valuables for cash, especially in the regions of high level of activity of terrorist groups;
- transfer of large amounts to/from the accounts of natural persons or newly established enterprises that do not perform business activity;
- funds transfer from the countries with high level of activity of terrorist groups;
- transfers from the bank accounts of those organizations not performing the declared types of activity.

As previously noted, the ways of assets integration into the financial system by terrorist organizations differ depending on the type of primary assets, its volume, purpose and necessary transfer

speed, on the one hand, and level of the financial system potential to stand against the threat to be used for the financing of terrorism.

However, in any financial system there are institutions that differ from other by nature of their activity. It is referred to non-profit organizations.

Not intending to gain profit, these organizations have branched representative offices in various countries providing the basis for international transactions. Their human or social profile, suddenness of transfers, potential address and complex assistance and great experience of using cash contributions make them a proper mechanism for funds transfer to terrorist organizations.

Thus, in 1996 in its Resolution A/RES/51/210, the United Nations General Assembly drew attention of the world community at the problem of the financing of terrorism through the involvement of those organizations "intending to perform charitable activity, achieve social or cultural goals".

Trying to levelling the risk of the involvement of non-profit organizations for the financing of terrorism, the world community specified the methods of diligence to be used concerning their activity. Thus, in the FATF Recommendations, the eighth recommendation concerns the activity of non-profit organizations being especially "sensitive" in this sense.

Unfortunately, based on the results of the third FATF assessment of country compliance with 40 FATF Recommendations, 57% of the countries failed to comply or only partially complied with the eighth recommendation. Only 8% countries fully followed the requirements of the eighth recommendation.

Moreover, the recent study conducted by the Center of Global Counter-Terrorism Cooperation and the UN Counter-Terrorism Committee Executives "To Protect and Prevent" (2013) defined the global level of risk understanding in the sector of non-profit organizations as unequal. Up to the date, the world community understands the necessity of more detailed study of the threat to the sector of non-profit organizations from the terrorist groups for improving awareness and understanding of both threats and risks.

The most informative study on this topic is the FATF study "Risk of Terrorist Abuse in Non-Profit Organizations" (2014).

Technological advances allowed non-profit organizations to expend the borders of their activity, fundraising and promotional potentials. The process of globalization also drove up the demand in socially oriented services of non-profit organizations, especially in those regions suffered from natural or industrial cataclysms, but also in those regions suffered from poverty or being unstable due to political or military infighting. Terrorist organizations are interested in the same regions.

In spite of different goals set by non-profit and terrorist organizations, they perform in the similar global environment, often intending to involve the same population groups.

Legitimacy and scope of activity of non-profit organizations, together with the possibilities of operative decision making, may be attractive for those terrorists intending to promote advantages in the globalized world.

At the same time, when the threat of the involvement of non-profit organizations from the side of terrorist organizations is clear, weaknesses of the sector vary. Weaknesses of the sector are divided into organizational and sectoral.

Organizational weaknesses allow involving of legal non-profit organizations by certain persons (even by certain officials). Sectoral weaknesses mean potential performance at the market of fictive non-profit organizations.

It should be noted that prospects of the involvement of non-profit organizations by terrorist organizations are not restricted only by fundraising and accumulation, among them:

- mobility improving;
- interaction between independent structures;
- access to the regions of conflict or to the regions of low state control level;
- decentralizing of communications and control;
- advanced capabilities of public involvement.

Among basic methods of the involvement of non-profit organizations for the financing of terrorism, there are following:

*Redeployment of funds* – redeployment of the portions of funds by the non-profit organization or its official for the needs of terrorist organizations.

*Program operation*– misuse of funds for programs focused on achievement of legal human goals.

*Fictive non-profit organizations*– in the guise of charitable activity, an organization or private person performs fundraising for the financing of terrorism.

Thus, among the ways of assets integration into the financial system by terrorist organizations, non-profit organizations hold a specific place. Due to their all-purposeness and global activity, non-profit organizations appear to be the unique mechanism, it should be noted for the fact that, for example, the system of branching of non-profit organizations established by the terrorist organization “Tigers of rescue of Tamil-Eelam” (Sri Lanka) existed longer than warfare unit of this organization.

## Section 2. Methods of the financing of terrorism and separatism

### Standard schemes of the financing of terrorism and separatism

According to information recorded into the Unified state register of pretrial investigations, the following methods of the financing of terrorist and/or separatist activity should be divided as follows:

- freewill transfer of own funds by the natural persons to the representatives of terrorist and/or separatist organizations;
- cash transfer to the card accounts of the members of terrorist groups;
- unauthorized cash withdrawal from the accounts of natural persons;
- financial security of terrorist groups by those persons using their official position;
- requirement of financial assistance from the entities by those persons using their official position;
- use of fictive financial structures for funds obtaining;
- commitment of thefts, robberies, kidnapping for funds obtaining;
- fundraising in social networks in the guise of charitable assistance by the group of natural persons;
- transfer of funds through electronic payment systems to the address of nominees.

Certainly, the above mentioned division is conditional as the schemes of the financing of terrorism and separatism may combine various elements above mentioned. However, for the typological description, elements in the spread schemes of the financing of terrorism and separatism would be separated.

Terrorist organizations and separatist movements use various sources of income and methods of cash transfers. Depending on the source of income, type and volume of assets, urgency of transfer and number of recipients, there are various schemes of the financing of terrorism and separatism. The goal of any scheme of the financing of terrorism and separatism is stable financial security of the recipient with minimum drawing of attention of the financial mediator to any financial transaction.

As a rule, in case of legal source of funds, the reversal scheme of the financing would be characterized with use of simple, ordinary, rapid and convenience methods of transfer, financial instruments. As a rule, such financial transactions should not differ from many similar transactions settled by financial mediators. With minor amounts of transfer, criminals may even avoid the identification procedure. In order to avoid the procedures of obligatory financial monitoring, the schemes of the financing include the involvement of mediators, financial transactions are to be settled through different financial institutions or the amounts of the financial transactions are to be reduced.

In case of illegal source of funds, the schemes of the financing of terrorism and separatism are more complicated due to the elements aimed at levelling of risk to exposure link between funds and their source. In these schemes criminals take the methods of placement and layering of illegally gained funds. It is made by change in the form of assets, use of various financial instruments, nominees, etc. Such schemes have certain analogies with the schemes of money laundering, with the difference that it is to be implemented without the last phase – integration of funds into the



financial system, but with further funds transfer to the final recipient. In this case, the scheme of the financing of terrorism and separatism has the high risk of use by the subjects of financial monitoring.

We shall consider the basic defined schemes of the financing of terrorism and separatism. Some of them have similar features, as they are to be implemented through services of the same financial mediators, in particular, bankers.

## Phishing

As previously noted, the financing of terrorism may be conducted at cost of legally gained funds, although the facts prove the use by criminals of new information technologies as a direct instrument of a crime. The main attractiveness of this instrument is in absence of direct contact with a "victim".

The second advantage of this type of crimes is its availability, i. e. preparation and commitment of such crimes are to be performed at the workplace, as computer hardware becomes cheaper, crimes could be committed from any country in the world, in any town with the developed infrastructure, and the objects of criminal offenses may be staying thousand kilometers away from the criminal.

The basic types, method and ways of commitment of such crimes were described in the typological study of 2013 "Cyberterrorism and money laundering". However, the main objective of the unauthorized cash withdrawal for the financing of terrorism and separatism is funds obtaining, in particular, in cash to be further used for financial and material security of terrorist and separatist activity.

### Example 12

In 2014 the unidentified persons, without any cause, without consent and knowledge of its holder, being in collusion with a group of persons, illegally transferred funds in the amount of UAH 1.6 million from the current bank account of the legal entity staying in the region bordering with the zone of anti-terrorist operations, which account was opened four months prior to settlement of these unauthorized transactions, to the settlement accounts of two legal entities directly staying in the zone of anti-terrorist operations; these funds were further used by the latter for financial and material security of terrorist activity of separatists.

## Electronic payment systems and the financing of terrorism and separatism

State regulators and law enforcement authorities define electronic payment systems as one of the basic weaknesses of the financial system of Ukraine.

Within the territory of Ukraine there are 20 remittance systems established by residents, among them:

- 15 remittance systems established by banks;
- 5 – by banking institutions.

23 international remittance systems established by non-residents also perform their activity within the territory of Ukraine. Participants in this system are 150 banks of Ukraine, Private Company "Ukrainian Financial Group" and the national postal service provider "UkrPost".

In the first half of 2014, through internal national and international remittance systems established both by residents and non-residents, the following amounts were transferred:

	Amount of transfer	
	million UAH	million USD (in equivalent)
within the territory of Ukraine	23, 710.6	0.24
to Ukraine	-	2, 029.5
without the territory of Ukraine	-	323

The given data mean the high demand in services of the remittance system on funds transfer within the territory of Ukraine and to Ukraine from abroad.

It should be noted that funds transfer is obtained by the recipient in cash.

### Example 13

There have been found signs of the financing of terrorism by the citizen of Ukraine that regularly transferred funds to several persons through the Ukrainian international remittance system "Avers". At this, in order to avoid financial monitoring, the amounts of all financial transactions did not exceed UAH 150,000. Funds were withdrawn by the above mentioned persons for the financing of terrorist attacks in the territory of Donetsk and Luhansk regions.

### Examples 14

In July of 2014, the citizen X, a native of Donetsk region, transferred funds through the payment system "Zolota Korona" to the unidentified persons in the total amount of over US \$ 1,700. Funds transfer was made by several installments in the bank branch in Donetsk region. At this, in order to disguise the real goal of funds transfer, the citizen X made the above payment in the name of the nominee. The citizen X took the mentioned actions for the financing of the groups of persons for commitment of terrorist attacks against the members of the anti-terrorist operation in the territory of Donetsk region, for which reason he intentionally transferred funds to the citizen Y for organization by the latter of the involvement of persons in armed conflicts on the side of "Donetsk People's Republic", as well as material security of their family members.

Moreover, as of October 2014, 69.8 millions of payment cards issued by the banks were registered in Ukraine (33.2 millions among them are active), the amount of transactions with payment cards issued by the Ukrainian banks constituted as follows:

Period	Amount of transactions (million UAH)					
	Non-cash payments	%	Cash obtaining	%	Total	%
2002	1 163	6	18 885	94	20 048	100
2003	1 356	5	26 744	95	28 100	100
2004	3 418	5	60 341	95	63 759	100
2005	3 196	3	96 542	97	99 738	100
2006	5 049	3	147 597	97	152 646	100
2007	8 118	4	217 003	96	225 121	100
2008	16 980	5	355 438	95	372 418	100
2009	18 375	5	334 791	95	353 166	100
2010	29 463	7	421 189	93	450 652	100
2011	46 346	8	529 633	92	575 979	100
2012	91 561	12	649 859	88	741 480	100
2013	159 138	17	756 889	83	916 027	100
I-III quarters of 2014	179 292	24	557 523	76	736 815	100

Though opening of the card account requires for the identification procedure, and transactions on the card account may be subject to financial monitoring, according to the statistics, the majority of transactions with payment cards are to be settled with cash.

Cash use makes it impossible to control any financial mediator over the targeted use of funds, thus, reducing the possibility of identification of such transfers that may be connected with the financing of terrorism and separatism.

Moreover, there are prepaid (debit) specific payment instruments actually similar to payment cards (they even look like a payment plastic card), though with restricted functions concerning the number and amount of payments. However, these payment instruments are the bearer payment instruments, i. e. they may be freely purchased and transferred to other person. These payment cards may also be connected with virtual e-wallet that, in turn, may be replenished through international payment systems.

### Example 15

As a result of monitoring customer transactions of one of the banks, there have been found funds transfers from the current accounts through special payment instruments (accounts were opened in Donetsk region) to the account of the counteragent-natural person in other bank. The payment amounts were different (from 20 to 250 UAH) and not regular (source of funds at the customers' accounts that initiated funds transfer – mainly, targeted use: salary, pension benefit). Basic transfers were made with the purpose of "private transfer", but there have been found transactions with the purpose of "assistance", "for drug products". As a result of the analysis conducted, the person, to whom account funds were transferred, appeared to be the member of "Donetsk People's Republic". Information on fundraising for "Donetsk People's Republic" and "Luhansk People's Republic" through the person's account was posted in Internet (mainly, in social networks, such as "Vkontakte", "Odnoklassniki").

From the point of view of financial monitoring, the situation is complicated by advantages to be granted to any ordinary citizen as a result of the implementation of modern technologies, namely, – availability, mobility, efficiency and anonymity. It is referred to those financial mediators providing services on funds transfer without opening of bank accounts in payment systems available through Internet.

Those payment systems, based on public offer agreement, allows the user to register in the system anonymously, credit funds into the system (for example, through ATMs, deposit ATMs, payment terminals, cash-in ATMs, etc.), settle payments with counteragents, make fund transfers and withdrawal from the system.

Further, concerning settlement of those financial transactions through payment systems, including with e-cash, in the amount not exceeding UAH 10,000 or in the amount in foreign currency not exceeding UAH 10,000 in equivalent, there are no requirement of legislation in regard to identification of the remitter/recipient.

In pursuance of the Provision on the procedure for registration of payment systems, participants in payment systems and service providers of payment infrastructure approved by the Decree of the National Bank of Ukraine dated 04.02.2014 No. 43, the National Bank of Ukraine keeps the Register of payment systems, settlements systems, participants in these systems and service providers of payment infrastructure and, accordingly, establishes the rules of operation of payment systems.

Those payment systems established by non-residents also successfully perform activity within the territory of Ukraine.

According to legislation, payment systems management established by non-residents shall submit documents for registration by the National Bank of Ukraine in the Register of payment systems till January 01, 2015.

Thus, the comprehensive list of payment systems performing activity within the territory of Ukraine will be submitted by the state regulator only in 2015.



It should be noted that within the territory of Ukraine those payment systems established by non-residents perform activity de facto (for example, WebMoney) that, applying the provisions of the Civil Code of Ukraine, through civil and legal relations arising out of the right of sale and purchase of cash claim, provide those sellers of such cash claim (persons and entities) with the services on management of equivalent financial assistance through electronic wallet. Thus, the situation arises when the resident of Ukraine transfers tangible assets to the defined mediator and receives the right of cash claim to be managed through web-interface that actually operates in other country.

The given web-interface operates according to legislation of other country; web-interface provider is not registered within the territory of Ukraine and does not agree upon the rules of payment system operation with the regulator (National Bank of Ukraine).

Example 1 given above describes the situation proving the use of foreign payment systems established by non-residents for the financing of terrorism and separatism.

The basic principle of payment system operation focused on sale and purchase of cash claim allows any potential user to manage virtual currency (as equivalent of financial assistance) and avoid the requirements of the National Bank of Ukraine in regard to accounting, issuance and movement of electronic currency in Ukraine.

Thus, to the moment, similar payment system with fictive virtual currency is implemented by one of the mobile communication providers of Ukraine that provided its subscribers with the possibility to use the balance for payment through payment system to be served by the non-banking financial institution.

Though such co-constitution operates within the legal framework, but it sets a precedent when the issuer of electronic currency is not registered by the state regulator, thus, the latter is not able to evaluate system risks and define any weaknesses in the AML/CFT system.

### Fictive enterprise

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Shell companies are often used for conversion of large amounts into cash.

As a rule, a company is to be registered in the name of nominees (among socially disadvantaged population groups) intending to sign any required payment documents for a minor amount.

Essentially, “convert centers” serve as an instrument for cash obtaining to be further addressed for the financing and material security of terrorist groups and separatists.

Members of “convert centers” convert non-cash funds into cash, as well as to the current accounts of fictive enterprise hiding their illegal business in the guise of legal business.

Enterprise-customers of “convert centers” transfer non-cash funds to the accounts of fictive entities through “Customer-Bank” system upon account management, funds may be rapidly transferred to the accounts of natural persons, including for the alleged products delivery (services provided, works executed, etc.). Plastic payment cards are used for those transactions on cash obtaining (including – corporate).

As a rule, founders of “convert centers” are experts having corrupted relations with the officials of relevant banking institutions.

Practice of investigation by the law enforcement authorities proves that managers of convert centers agree in advance with bank officials upon any mutual actions in case of threat of funds blocking at the current accounts of fictive entities. For this purpose, the bank is given the application and appropriate order with the details of fictive enterprise without date and number on account closing by the customer itself, thus, allowing the bank employees to withdraw cash prior to blocking. Further actions concerning the purpose of funds that may be transferred to any previously given other account are to be agreed.

The peculiarity of the scheme is the fact that the firm, acting as the seller, is to be established for a short term. After a time upon settlement, the firm and its accounting disappear. As a rule, firms are to be established according to fictive or stolen passports or in the name of nominees.

#### Example 16

Within the period from April to July of 2014, the officials of the range of commercial structures of Luhansk region, for financial and material security of the terrorist group “Luhansk People’s Republic”, made illegal funds transfer to the accounts of controlled financial structures that were further withdrawn in cash and handed over to Luhansk by the unidentified persons for the financing of terrorist activity of the members of “Luhansk People’s Republic”.

#### Example 17

The law enforcement authority received information on illegal activity of the officials of the Company “X” in Kharkiv connected with financial security of activity of terrorist groups (organizations).

Thus, the officials of the Company “X” settled a range of fictitious operations with the fictive Company “F”, Company “A” and Company “O” abusing the official position. There has been found enterprise at the address of registration. The Company “O” also appeared to be fictive, the officials did not intend to perform statutory activity, and the enterprise was not at the address of registration. Besides, the Company “X” was included into “convert center” controlled by the citizen of Ukraine Z and provided services on tax mitigation, conversion of non-cash funds into cash with further money laundering. Funds received from performance of the above illegal activity were further used by the officials of the Company “X” and their crime partners for the financing of activity of certain persons and groups intending to organize, prepare or commit terrorist attack.

## Bank transfers and foreign remittance

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Taking into consideration the fact that legal funds may be the source of the financing of terrorism and separatism, bank transfers are the most convenient instrument of funds transfer for criminals.

Financial mediators and law enforcement authorities defined that in the schemes of the financing of terrorism and separatism those financial transactions *on transfer from the account to the account, international transfers and cash crediting and withdrawal* were mentioned.

At this, in order to disguise the financing of terrorism and separatism, criminals use combinations of financial transactions. The most popular financial transactions that may be used in order to disguise the financing of terrorism and separatism are crediting of funds to the accounts as financial assistance, donation with further cash withdrawal or transfer to the account in other bank.

### Example 18

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The legal entity granted financial assistance in the amount of UAH 20 million to the natural person, place of residence and registration – eastern region of Ukraine in the zone of anti-terrorist operations. At this, the named natural person is unemployed, has no sources of income and has no business relations with the mentioned legal entity.

### Example 19

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The law enforcement authority initiated a criminal proceeding on a crime as specified by Article 15 and Article 258 of the Criminal Code of Ukraine in response to the financing of terrorism and separatism by the citizen of Ukraine committed through bank transfer in the amount of UAH 3.93 million in the guise of non-repayable financial assistance to other natural person.

### Example 20

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Pursuing the aim of financial and material security of terrorist groups acting in the territory of southern and eastern Ukraine, being in collusion with the officials of the Company "X", a range of natural persons, using the personal data of the citizen Y, transferred funds in the amount of over UAH 5 million to the bank account of the given person. A portion of funds further should be transferred to the accounts of the above entity with conversion into cash for financial and material security of terrorist groups, organization and commitment of terrorist attacks within the territory of Ukraine.

Foreign remittance calls for special attention. All cases found by the entities and law enforcement authorities prove the undisputed fact of international transfers aimed at the financing of terrorist and separatist activity in Ukraine from the territory of the Russian Federation.

All given transfers are to be conducted both by persons and entities, private and even state structures.

### Example 21

The law enforcement authority initiated a criminal proceeding in regard to a crime as specified by Article 258 "Terrorist attack" of the Criminal Code of Ukraine in regard to commitment by the officials of the Open Joint Stock Company "X" (Autonomous Republic of Crimea) and the Company "U" (Donetsk) of actions aimed at laundering of 100 mln. Rubles received from the state body of the Russian Federation "B" in guise of payment for services for the financing of separatist groups in the territory of Donetsk region.

Thus, from its branch in Sevastopol the state body of the Russian Federation "B" tried to transfer through one bank the amount of 100 mln. Rubles to the account of the shell company in Donetsk. Payment was made as prepayment for construction works.

Instead, funds should be used for illegal activity of terrorist groups within the territory of Ukraine and commitment of explosions upon May 9 VE Day celebrations. According to the Law of Ukraine "On Prevention and Counteraction to Legalization (Laundering) of the Proceeds of Crime or Terrorist Financing", unlawful banking transactions were suspended, accounts of the fictive enterprise were blocked.

### Example 22

The law enforcement authorities of Ukraine initiated a criminal proceeding in regard to a crime as specified by Article 258 "Terrorist attack" of the Criminal Code of Ukraine in regard to commitment by the officials of the subsidiary banking institution of the Russian Federation during March-April 2014 of daily funds transfer to plastic cards of separatist group members in the amount of US \$ 200-500.

There have been found cases of conducting by the residents of the Russian Federation of international transfers with crediting of funds to the accounts of those non-profit organizations being registered and acting within the territory of Ukraine as assistance to be used for promulgation within the territory of Ukraine concerning discreditation of the ruling government, escalation of armed conflict between various social groups of Ukraine, stirring of ethnic hostility. The detailed overview of the mentioned examples is given in the section below.



## Non-profit organizations

According to given information, the main (prevailing) way of the illegal involvement of non-profit organizations was redirection of funds to terrorists from the side of non-profit organizations. In the sector of non-profit organizations there is a range of interconnected weaknesses and terrorist organizations try to use these weaknesses.

Peculiarities of non-profit organizations that may be also attractive for use in criminal schemes include, in particular, are as follows: possibility of piling up funds through member contributions, donations and so-called non-profit activity, and funds should be spent for the project implementation or purchase of required equipment.

It is quite difficult to track all frauds in this sector, prevent due to nature of these organizations (statutory functions) and loyal government control and monitoring system in different countries. Obtaining the status of charitable organization and being exempted from taxation, they could be involved in territorial funds transfer through branches and for material and technical support of terrorists and separatists (directly or as front of their actions).

Banking institutions involve charitable, public companies of other non-profit organizations for the financing of terrorism and separatism.

### Example 23

There has been initiated a criminal proceeding in regard to unlawful actions of the officials of the Ukrainian public organization that, acting in collusion with the unidentified persons among the citizens of the Russian Federation, concluded with the public company (RF) the agreement of granting funds in the amount of 8 mln. Rubles. These funds were credited to the account of the given Ukrainian public organization and should be used for promulgation within the territory of Ukraine concerning discreditation of the ruling directory, escalation of armed conflict between various social groups of Ukraine, stirring of ethnic hostility, information support for holding of so-called referendums concerning incorporating of administrative-territorial units of Ukraine to the Russian Federation in violation of the provisions of the Constitution of Ukraine.

### Example 24

The law enforcement authority initiated a criminal proceeding in regard to the citizen of the Russian Federation that organized transfer of funds to the controlled settlement accounts of charitable organization in the amount of UAH 23.9 million, further addressed for the financing of unlawful actions within the unlawfully annexed territory of the Autonomous Republic of Crimea.

For fundraising as charity support, information resources are to be formed in Internet with posted banking details for funds crediting.

### Example 25

Several persons posted in Internet informational resource to propose to the citizens of Kharkiv to credit funds for charity support of army of the self-proclaimed “Kharkiv People”s Republic” and further purchase of body armors, weapons and ammunition by the revolutionaries of “Kharkiv People”s Republic”. Thus, under the given conditions, the unidentified persons committed actions for financial and material security of the terrorist group, i. e. a crime as specified by part 1 Article 258-5 “The financing of terrorism” of the Criminal Code of Ukraine.

To prevent the involvement of non-profit organizations for illegal interests, the following is essential:

- control of funds transfer;
- clear requirements to registration of charitable and other non-commercial organizations, especially those foreign and/or established by non-residents, and state control over their activity.

## Section 3. Methods of determination and mechanisms of countering the financing of terrorism and separatism

### Criteria of determining the financial transactions on the financing of terrorism and separatism

Failure to define the common features of suspicions of the financing of terrorism and separatism is one of the difficulties of suspicions concerning such cases. It is referred to the fact that any schemes and methods, including the involvement of persons, may be used for the financing of terrorism and separatism.

Moreover, it is not possible to define purpose and further use of assets within one financial institution. In case of cash withdrawal, it is impossible to verify the targeted purpose. At this, there are no customer transactions, as a rule, having the direct purpose, peculiarities or details that could prove the financing of terrorism and separatism.

Nevertheless, according to the summarized information on the facts of the financing of terrorism and separatism, such criteria of determination of the above financial transactions could be defined:

- region of the most potential demonstration of the financing of terrorism and separatism;
- recipient and/or initiator of funds transfer is any public and/or charitable organization;
- crediting of funds in minor amounts from different persons within a short period of time in favor of one person with the purpose of "assistance", "for treatment", "charity support", "for humaneness";
- absence of confirmation of the targeted purpose of any incoming/outgoing payments settled many times (for example, funds credited as "charity support", "for treatment", etc. are to be used only for cash withdrawal, i. e. there is non-cash transfer that would allow defining of the targeted purpose of payment);
- financial transaction uncommon for the customer in the amount;
- counteragent uncommon for the customer;
- payment purpose unusual for the financial transaction;
- private transfer from the territory of the Russian Federation;
- payments to be made by those persons being not fully aware or not willing to inform the payment details (address/contact information, etc.);
- transaction on electronic transfer with missing information on the initiator or recipient;
- crediting of funds to the settlement/card account of the person or transfer in the name of natural person to be made without account opening, if the given information shows that the source of such crediting/transfer is funds to be transferred through payment systems providers of which are not registered within the territory of Ukraine, including with e-funds;
- involved nature of the financial transaction;
- lack of economic factor;
- settlement of financial transactions by the customer in large amounts without any direct (personal) contact with the subject of primary financial monitoring within three months.

It should be noted, that upon this study, the regions of Ukraine with the majority of facts of the financing of terrorism and separatism, according to information received from the law enforcement authorities, included the territory of Kyiv, Luhansk and Donetsk region.

According to the Decree of the Board of the National Bank of Ukraine dated 06.08.2014 No. 466 "On suspension of financial transactions", the banks of Ukraine should be obliged to suspend all types of financial transactions in town settlements not controlled by the Ukrainian Government, and non-banking institutions and postal service providers, being payment organizations of internal national/international payment systems and/or their participants, should be obliged to suspend transactions on crediting/payment of cash transfers from/in the territories not controlled by the Ukrainian Government.

Taking the foregoing into consideration, accumulation of financial flows related to the financing of terrorism and separatism *in the neighboring regions of performing the anti-terrorist operation* is possible.

Concerning funds transfer from the territory of the Russian Federation, it should be noted that such criterion should not intervene the exercise of rights of law-abiding citizens. This situation is complicated by a great number of employees settling financial transactions on funds transfer to Ukraine earned within the territory of the Russian Federation. However, it should be taken into consideration for importance of the given criterion, especially combining with other provided information.

It should also be noted on those transactions on cash withdrawal or crediting. Without other information, a certain financial transaction on cash withdrawal or crediting may not be deemed to be a sufficient ground for suspicion on its purpose for the financing of terrorism and separatism, but in the context of other information such sign should draw attention at the subject of primary financial monitoring.

## Preventive and countering measures

One of the efficient measures of countering the financing of terrorism and separatism is providing the financial market players with methodological, guidance and other assistance in the sphere of anti-money laundering or countering the financing of terrorism.

Such measures are not comprehensive and require for regular initiative from the side of state regulators.

In particular, the National Bank of Ukraine gave recommendations to the banks in regard to taking actions concerning:

- those persons involved in exacerbation of political and economic crisis of Ukraine and concerning whom international sanctions are applied;
- analysis of financial transactions aimed at determination of those cases proving use of bank services by the customers for the financing of any illegal business.



Concerning the subjects of primary financial monitoring, in particular, banks, they apply mechanisms of countering the financing of terrorism and separatism as specified by legislation in the sphere of anti-money laundering, internal documents on financial monitoring, with due account of recommendations of the State Financial Monitoring Service and the National Bank of Ukraine.

Some banks have own existing mechanisms for tracking of financial transactions of those natural persons, being directly or indirectly involved in the financing of separatism. For example, the bank makes and summarizes information on natural persons involved in the financing of terrorism based on information of the law enforcement authorities, received from the State Financial Monitoring Service, from open sources and due to the measures taken independently and defines a range of affiliated persons. In case any person involved in terrorism or separatism (or the affiliated person) tries to settle any financial transaction, information on such transaction shall be transferred to the bank unit performing financial monitoring of transactions, for further analysis of this transaction, decision making on registration in the register of financial transactions and notice for the State Financial Monitoring Service.

The example of the implementation of own bank mechanism of tracking financial transactions of natural persons, being directly or indirectly involved in the financing of separatism, may be used for information posted at the web-site of the Ministry of Internal Affairs, concerning those persons wanted, including according to Article 260 "Establishment of military or armed groups not permitted by law" of the Criminal Code of Ukraine.

Some banks use official mass media (Specially Designated Nationals and Blocked Persons List, journal of the European Union, etc.).

In order to execute own lists, some banks form own communication channel where citizens may inform on suspicions of utilization of bank accounts for the financing of terrorism or separatism.

The vital aspects complicated the measures of preventing and countering the financing of terrorism or separatism are volume and nature of funds attracted. Wherefore suspension of any financial flow of terrorists and separatists may appear to be complicated task. In this context, the best common decision may be full enforcement and absolute execution of the rules "know your customer". That bank, being aware of its customers, less likely could become an unforeseen channel for funds transfer from the side of terrorists and separatists.

Any preventive measures of the rules "know your customer" exceed the limits of standard account opening and recording, they require the banks to implement the policy of customer research and program of multilevel customer identification ensuring common and specially controlled verification of high risk accounts, as well as practical monitoring of any suspicious accounts.

Need for strict standards concerning customers should not be restricted by banking institutions. Similar rules shall be applied by any non-banking financial institutions, as well as professional mediators at the market of financial services.

In the context of the rules "know your customer", special attention should be drawn at search of additional information from open sources, in particular, in Internet and social networks where

many cases of publications on support (including financial) from the persons intending to prepare or commit any terrorist attack, involvement into commitment of any terrorist attack, public calls for commitment and direct commitment of any terrorist attack, overthrow of constitutional order in Ukraine and destabilization of social and political situation in eastern Ukraine have been recorded.

In the context of prevention and countering the financing of terrorism and separatism, those important measures required for special attention are increase in control of payment systems.

It should also be noted that fictive payment systems (issuers of own virtual currencies) based on relations of sale and purchase of the rights of cash claim (detailed description given in the section "Electronic payment systems and the financing of terrorism and separatism") take the risk to be neglected by state regulator, that may lead to system risks for the AML/CFT system.

The most progressive and efficient measures of countering the financing of terrorism and separatism may be strict limits of cash turnover, for example:

- establishment of strict limits of accounts for cash withdrawal;
- increase in limits of cash withdrawal only according to documents confirming sources of funds and targeted purpose.

However, establishment of mentioned limits may lead to dissatisfaction of all levels of population and become an impulsive cause of the shadow economy growth.

Information monitoring in Internet by the bank employees for search of those customers using their accounts for fundraising for charity support and security of terrorist and separatist groups, as well as imposition of limitations to the accounts of persons involved in the financing of separatism (limitation of funds transfer from the account or cash withdrawal) may be the most efficient measures of diligence of criteria of finding financial transactions in order to prevent use of bank services that could be used.

According to the found facts of the financing of terrorism and separatism by means of financial flows through the accounts of non-profit organizations, the important measures to prevent such cases in future should be strengthening of state control in the given sector. In particular, it is required for the implementation of clear control over declaration of programs by non-profit organizations and, accordingly, reporting on its performance. On the other hand, such information should be available for banks as subjects of primary financial monitoring that allows them to analyze financial transactions of non-profit organizations through data correlation. Such mechanisms allow finding of financial transactions if they do not comply with the registered programs.

## Interdepartmental cooperation

Expansion of terrorism and separatism in Ukraine in a new way sets the tasks of countering their signs and requires for taking strict measures to control over financial flows. Thus, measures to find and efficiency block any channels of financial security of terrorist and separatist organizations are the key trends of the long-term anti-terrorist strategy and may be conducted by efforts of all participants in the national AML or CFT system.

Under conditions of current countering the financing of terrorism and separatism, the expended sphere of financial control defines peculiarities of activity of certain state authorities concerning problem solving.

Basic principles of methodologies in regard to financial control, according to the national legislation, development of international relations and information exchange are the most vital conditions for definition and destruction of the financial structure fueling activity of terrorist organizations, mainly, focused on forcible change or overthrow of constitutional order or take-over, changes in borders of territory or state boundary of Ukraine.

On the other hand, active information exchange between private and state sector would contribute to efficient counterterrorism, in particular, in regard to the following:

- identification of persons involved in the financing of terrorism;
- receipt by the subjects of primary financial monitoring of feedback information concerning the results of financial transaction analysis according to banks to be addressed pursuant to Articles 15, 16 of the Law of Ukraine “On Prevention and Counteraction to Legalization (Laundering) of the Proceeds of Crime or Terrorist Financing”, on the facts of violation (termination) of criminal proceedings and adoption of court judgement on these cases.

## International cooperation

According to the Conception of counterterrorism, international cooperation of Ukraine concerning counterterrorism should be performed as follows:

- practice of accession, according to legislation of Ukraine, to international counterterrorism agreements concluded within the United Nations organization, other international organizations where Ukraine is a member;
- cooperation with the European Union in counterterrorism according to the rules of international law;
- coordination, improvement and extension of cooperation of subjects countering terrorism with law enforcement authorities and special services of foreign countries, anti-terrorist units of the United Nations organization, Organization for Security and Cooperation in Europe, North Atlantic Treaty Organization, European Union, other international organizations countering terrorism by virtue of international agreements;
- conclusion of international agreements on cooperation in the field of counterterrorism between the subjects of counterterrorism and relevant authorities of foreign countries;
- establishment of shared experiences with relevant authorities of foreign countries and international organizations countering terrorism, probation and training of national experts abroad by virtue of agreements on international cooperation.

The basic task of this stage of international cooperation in the field of countering terrorism and separatism should be making of strategic decisions. On the one hand, common actions of the European countries should improve the level of countering terrorism and separatism, namely, in the European region, and on the other hand – disadvantage the Continent of Europe.

International cooperation could be efficient under conditions of mutual confidence and similarity of executive functions based on similar standards, laws, procedures and – the most crucially – common values.

According to the EU approach, counterterrorism, in particular, on the one hand, requires for reducing obstructions, including those national and departmental, upon exchange of necessary information, in particular, intelligence information, and on the other hand, for establishing enforced multilevel systems of control over personal, financial and other data.

The problem of integration of Ukraine into the system of international security and cooperation with world and European integration structures in security sector is referred to setting of equal standards for different countries in regard to global counterterrorism that should include assessment and tracking of activity of terrorist organizations and groups under conditions of response coordination of the security system of Ukraine and foreign countries, in particular, NATO countries. In the context of ensuring own security, Ukraine should integrate into international anti-terrorist structures.

In this context, organizational and technical mechanisms of “rapid” information exchange between the Ukrainian authorized bodies and law enforcement authorities, armed power subdivisions, special services, financial monitoring institutions of NATO partner countries are vital.



## Public mechanisms

One of the basic information sources of finding financial transactions of those persons involved in the financing of terrorism and separatism is formation and execution of the list of persons by the example of the list of the State Financial Monitoring Service of persons related to terrorist activity or concerning whom international sanctions are applied.

Such mechanism provides for finding and suspension of financial transactions and would significantly improve finding of persons involved in the financing of terrorism and separatism. In particular, at the official web-site of the department, the Ministry of Internal Affairs posted the list of persons wanted on suspicion of the involvement in commitment of a crime pursuant to Article 260 "Establishment of military or armed groups not permitted by law" of the Criminal Code of Ukraine.

In turn, lack of any official list of separatists and persons suspected by the example of the list of persons related to terrorist activity or concerning whom international sanctions are applied to be noticed by the State Financial Monitoring Service is pointed by the National Bank of Ukraine as information not sufficient for verification by banking institutions in regard to financial transaction and involvement of its participants in the financing of terrorism and separatism.

## Conclusion

Risk of the financing of terrorism and separatism should be considered as derivatives from the threat of terrorist activity or separatism and weakness of the financial system to be used for the financing of this activity.

Till 2014 Ukraine has not been suffered from internal terrorist accidents, although the law enforcement authorities sometimes define crimes as terrorist actions (results of further analysis proved they have being committed from molester motives or in order to redistribute property).

The situation has dramatically changed in early 2014.

Up to the date, *high level of the threat* of terrorist and separatist activity (and the financing of this activity) in Ukraine is the actual factor.

This study intended to identify the methods of financing to be used by terrorists and separatists and defined differences of methods to be taken by other criminal groups and sources of funds, classified for the categories of relevant risks and proposed for the ways of risk mitigation.

There have been found differences between legal an illegal sources of funds and potential use of the existing anti-money laundering system for fining and proceedings concerning terrorists and separatists due to their financial activity.

Some groups of persons with common idea of forced changes or overthrow of constitutional order or changes of territory of state border of Ukraine may create funds, thus, fully controlling institutions within its partnership. Sources of any established funds may be various membership dues, publications, donations of rich partnership members, etc. Difference between legal and illegal ways of funds obtaining by terrorist organizations highlight the problem of taking any measures aimed at countering the financing of terrorism.

In opposition to money “laundering”, a terrorist does not intends to earn income resulted from application of any fund establishing mechanism, but obtaining resources necessary for commitment of any terrorist actions. Accordingly, the main problem of financial institutions is the fact that they should track not only sources of funds, but also purposes of use.

The control system is not properly established yet and does not allow completing of these tasks. The system mainly based on the ability of banks to analyze any given information is exposed to risk. On the other hand, too much complex procedures of inspection would create those conditions preventing the activity of law-abiding citizens, thus, they may be deemed to be those restricting legal rights and freedom.

As the zone of conflict is limited to south and east regions, any preventive measures concerning customers and their financial transactions based on the geographical location are justified mechanism of countering. At the same time, such approach may lead to charges of prejudgment in regard to citizens from the given regions. In addition, there is a problem with bank reporting as self-defensive instrument. Pursuing the policy of protection against any potential use by terrorists

of services of their institution, banks may inform on any suspicious transactions that, in turn, may create the situation when the regulating authorities would be engulfed by relevant reports.

The main obstacles preventing verification of financial information and their parties concerning the financing of terrorism were as follows:

- lack of any official public/confidential list of separatists and persons suspected;
- lack of any official list of countries supporting terrorism financing;
- lack of free electronic sources of information verification, especially lists of natural persons and free access to databases of lost passports (being declared as lost) and other;
- limitation of information on those persons settling financial transaction in the amount of less than UAH 150,000, without account opening, as well as in case of settlement of financial transactions with e-funds.

According to international studies, terrorist organizations apply a great number of methods and schemes of moving financial resource in the financial system, in particular – trade finance, cash couriers, charitable organizations, alternative payment systems, etc.

Choosing the scheme of financing, terrorist organization and separatist movements take into consideration geographical location, primary type of assets, amount, necessary transfer speed, cost of transfer and potential risk level (theft, exposure by the law enforcement authorities, etc.).

In Ukraine the main factor of choosing the scheme of the financing of terrorism and separatism is legal nature of income sources.

Under conditions of legal source of funds, the chosen financing scheme would be characterized with use of simple, standard, rapid and relevant methods of transfer, financial instruments. As a rule, such financial transactions would not differ from various similar transactions to be settled by financial mediators. With minor amounts of transfers, criminals may avoid identification procedure. In order to avoid procedure of obligatory financial monitoring, mediators are involved in the financing schemes, financial transactions are to be settled through various financial institutions or the amount of financial transaction is to be fractioned.

Failure to define similar signs for suspicions of the financing of terrorism and separatism is one of the basic problems in defining suspicions of such cases. At the same time, according to summarized information on the defined facts of the financing of terrorism and separatism, the following criteria of the above mentioned financial transactions may be defined:

- crediting of funds in minor amounts from different persons within a short period of time in favor of one person with the purpose of “support”, “for treatment”, “charity support”, “for humaneness”;
- recipient and/or initiator of funds transfer is a public and/or charitable organization;
- financial transaction uncommon for the customer in the amount;
- counteragent uncommon for the customer;
- payment purpose unusual for the financial transaction;
- private transfer from the territory of the Russian Federation;
- payments to be made by those persons being not fully aware or not willing to inform the payment details (address/contact information, etc.);

- transaction on electronic transfer with missing information on the initiator or recipient;
- crediting of funds to the settlement/card account of the person or transfer in the name of natural person to be made without account opening, if the given information shows that the source of such crediting/transfer is funds to be transferred through payment systems providers of which are not registered within the territory of Ukraine, including with e-funds;
- involved nature of the financial transaction;
- lack of economic factor.

In case of illegal source of funds, the schemes of the financing of terrorism and separatism are complicated by elements aimed at levelling of risk of defining the link between funds and their source. In such schemes criminals credit illegally gained funds and allocate them. It is made through change in assets form, use of various financial instruments, nominees, etc. These schemes are similar to the schemes of money laundering, with the difference that it should be implemented without the last phase – integration of funds into the financial system, but with further transfer of funds to the final recipient.

In this context, the best common decision should be enforceability and absolute execution of the rules “know your customer”. That bank, being aware of its customers, less likely could become an unforeseen channel of funds transfer from the side of terrorists and separatists.

Preventive measures of the rules “know your customer” exceed the limits of standard account opening and recording, they also require the banks to apply the policy of customer search and program of multilevel customer identification system ensuring common and specially controlled verification of high risk accounts, as well as preventive monitoring of suspicious accounts.

The schemes of the financing of terrorism and separatism concerning the following should be taken into consideration:

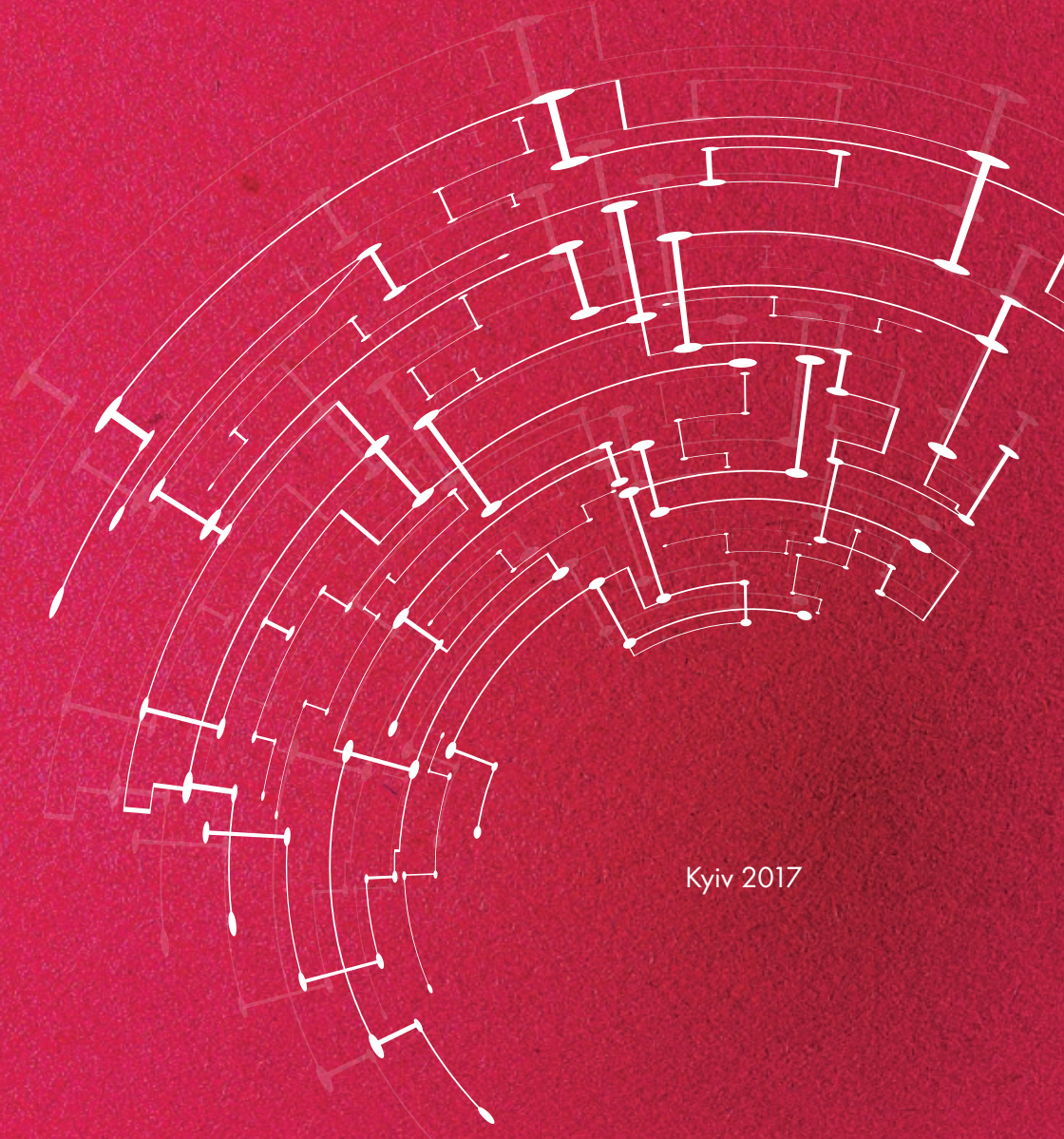
- activity of non-profit organizations
- fictive enterprise (conversion of non-cash funds into cash);
- operation of electronic payment systems.

Preventive and countering measures that may improve the level of efficiency of the AML/CFT system should be focused on the following:

- methodical and methodological assistance in the field of anti-money laundering or countering the financing of terrorism;
- measures taken by the subjects of primary financial monitoring aimed at the increased requirements to request for/investigation of information necessary for execution of rules “know your customer”, including with information from open sources, in particular, in Internet, social networks, etc.;
- increased control over payment systems and non-banking financial institutions in a part of extension of the requirements to the rules of internal financial monitoring;
- review of state standards that regulate settlements in cash downwards of aggregate settlement amounts;
- increase control over activity of non-profit organizations;
- increased interdepartmental cooperation between state regulators, subjects of primary financial monitoring, State Financial Monitoring Service and law enforcement authorities;
- increased international cooperation in the field of countering terrorist and separatist activity.







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