

Current dimensions of accounting affected by the introduction of black money

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Abstract: As far as money laundering is concerned through the company's accounting, a distinction should be made between the actual placement stage, as it is in the literature, and the stage (operation) where dirty money enters its accounts. The time of recording money in the accounting may coincide with the stage of placing the illicit funds or may be after it. To illustrate the above, we will analyze two distinct circuits generated by money from offenses, the form in which the money originally represents the cash held by the offender or another person considering recycling.

Key words: money, control, efficiency, cash

JEL Classification: M40, M42

Introduction

The accounting records underlying the insertion, transfer or exit of dirty funds are vulnerable to the risk of money laundering, providing criminals with justification of the origin of the funds. To this end, the surveillance of certain types of registrations is a form of money laundering prevention that is required to ensure the functioning of a healthy economic system.

Situation 1 - the placement stage is prior to the moment the money enters the company's accounting.

The amount gained from the offenses is deposited in a bank account of the offender or the money launderer, this being the placement stage. Any subsequent operation is layering until integration. After the money is deposited into the account, payment is made to the account of a company called "*crediting*", based on a contract concluded between the individual and the company. The moment of entering the dirty money in the company's accounting is represented by the cashing-in operation into the company's bank account and making the related accounting registration, but from the point of view of money laundering the amount was already "*placed*" in the banking financial system, the accounting operation 5121 – "*Accounts at the banks in lei*" = 462 - "*Various Creditors*" or 5121 "*Accounts at the banks in lei*" = 455 "*Amounts owed to associates / shareholders*" (depending on the relationship of the money launderer with the company concerned) being a segment of the layering stage.

Situation 2 - the placement stage coincides with the moment of money entry in the company's accounting

The amount gained from the offenses is deposited by the person concerned directly to the company's bank account or the company's cash desk with the same justification as "company crediting", but in this situation, the placement stage coincides with the input of dirty money into the company's accounting. The accounting operations related to the placement of black money are in this case 531 "House" = 462 "Various Creditors" (531 "House" = 455 "Amounts owed to associates / shareholders") or 5121 "Accounts at the banks in lei" = 462 "Various Creditors" (5121 "Accounts at the banks in lei" = 455 "Amounts owed to associates / shareholders").

A. Crediting of the company

Crediting of the company by associates is an attractive option for money launderers, regardless of whether they are made through the company's cash desk or bank account. In general, **cash crediting** is preferred by individual associates, as cash handling is not restricted by law. The crediting of the company by associates through cash deposits in cash desk is typical for tax evasion situations by not recording revenue. Thus, the amounts resulting from the sale of the goods traded by the company are deposited in the company's cash desk with title "crediting of the company" so as to create a right of claim on the company that justifies withdrawals of amounts from its accounts.

The crediting of the company is an extremely safe method for money launderers, especially when a small number of people (associates and administrators) are involved in the company's activity. This security is given by the "zero" exposure to entities in the banking financial system who may be aware of possible irregularities and who may find suspicions about the company's activity. After the money is collected, the money is immediately merged with the already existing amounts in the account 531 - "House", after which new cash payments can be made to the various suppliers. The balance may be deposited in the bank account, and there is no direct contact between the creditor of the company and the credit institution. However, the use of this money-laundering method also has a number of drawbacks, which is why it is used for smaller-scale criminal activities that do not require the transfer of large amounts of money (€ million!) and do not have a transnational character.

Crediting of the company on account 512 - "Current Accounts with Banks" = 455 - "Amounts owed to shareholders / associates" is one of the most widespread forms of infiltration of the profits from

offenses in the company's current activity and thus in the surface economy.

Unlike the direct infiltration of black money into the company's accounts (cash-deposited), crediting to the company using the bank accounts of the associates has no value limits, nor currency.

The crediting of the company by individual persons associates can be done both in lei and in foreign currency, from their accounts opened in Romania or abroad¹.

B. Crediting of the company by entities holding participation interests

Crediting of the company by entities holding participation interest in it is another method of recycling black money, usually on the territory of countries other than the one where the predicate offense (s) was committed.

Involvement of affiliated entities located in tax havens in money laundering schemes is a preferred method for transfers worth several hundred thousand or even millions euro (or equivalent in any currency) from one jurisdiction to another.

The method has a number of advantages for money laundering such as: the high amount of loans that can be granted in view of the association relationship between the parties, the favorable conditions for granting the justified loans in the same way, the performance of operations between firms controlled by the same individual person or group of individuals, which makes the risk of detection much diminished.

Thus, it can be found in the company's accounting:

- ✓ Settlements between two companies carrying out a joint-venture activity, materialized by bank transfers under the Association Agreement:

512 "Accounts at the banks" = 458 "Settlements from joint operations - liabilities"

- ✓ Loans granted by companies within the group with interests (expenditures with interests being deducted under certain tax conditions):

512 "Accounts at the banks" = 167 "Assimilated loans and debts"

666 "Expenditures regarding interests" = 168 "Interests on assimilated loans and debts"

- ✓ Transfers between affiliated companies and interest calculated for these transfers
512 "Accounts at the banks" = 4511 "Settlements between affiliated entities (A / P)" 666 "Expenditures regarding interests" = 4518 "Interests on settlements between affiliated entities (A/P)"

¹ Activity report ONPCSB, 2008, pages 71 and 78

C. Crediting of the company by various persons

Crediting of the company by other persons may be another form of introducing illicit funds into company accounts for recycling.

In this respect, the participation of the company by means of associates or administrators in the money laundering circuit can be voluntary or not, because offering cheap capital (Roudaut, 2010) is a temptation for any businessman, regardless of his position on the market or the size of the company.

In the situation where the entrepreneur is not in a criminal association with the person who offers the credit, it is desirable that he (the good faith investor) should take steps to ensure that the source of the funds is not likely to put him threatening reputation, moral integrity, or (even) ownership of the assets resulting from the use of dirty money².

Accounting records in accounts 455 - "*Amounts owed to associates / shareholders*", 1663 - "*Liabilities to entities to which the company is connected by participation interests*", 1661 - "*Liabilities to affiliated entities*" and 462 "*Different creditors*" are able to generate suspicions in certain situations.

D. Encashment from sale

Cash depositing in the company's cash desk or bank account with the title "*encashment from sale*" is a "classic"³ money-laundering method. It offers the advantage that it is part of the current characteristics of a retail activity and does not raise suspicions.

With regard to deposits in the cash desk, the participation of other entities in the transaction is excluded, which is likely to obliterate the origin of the money from any third party that might consider it as a suspect operation. Such situations may, however, be detected in the course of controls, for example by the Financial Guard Commissioners, who have the obligation to sanction the non-declaration to the authorities⁴ of cash operations in the cash desk of the company above the reporting limit⁵.

On the other hand, the major disadvantage of accounting records in relation to account 411 - "*Clients*" is that revenue is generated, with the obligation to pay the related taxes. Usually criminals do not assume this cost of recycling, and to avoid it, they generally appeal to parallel, fictitious records, representing payment obligations to "*phantom*" companies.

² Art. 32, Act no. 656/2002

³ It is Al Capone's famous method with his famous laundries

⁴ ONPCSB

⁵ Article 5, parag.(7) of the Act no. 656/2002

Another major drawback of this technique lies in its limited character in terms of volume and currency. Cash deposits with the "*encashment from sale*" justification can not exceed the modest values and can only be done in the national currency; often the amounts derived from organized crime exceed many millions of euros and are denominated in different currencies.

As strange as it may seem, there are situations where the money (found in the company's bank accounts) becomes dirty by handling operations on accounts 401 - "*Providers*" and 411 - "*Clients*". This is a special case, and it is about overlapping some tax evasion situations with money laundering operation. The special feature of such a technique is that the dirty money placement is completely missing, making the money *becoming dirty* directly in the financial-banking system by falsifying some accounting operations.

E. Participation in the share capital of companies.

Dirty money can be infiltrated into the company's accounting ever since it was set up, on the occasion of the increase of the share capital, or in any situation of changing the structure or composition of the shareholders.

In this situation, the following are recorded in the accounting:

- ✓ Decision of the Founding Companies' Associates or the Decree to increase the share capital for an existing company, as a commitment to deposit of the available:
456 "*Settlements with associates / shareholders regarding share capital*" = 1011 "*Subscribed and unpaid capital*";
- ✓ Submission of the share capital according to the commitment made by the Decision or the Decree:
512 "*Accounts at the banks*" = 456 "*Settlements with associates / shareholders regarding share capital*"
1011 "*Subscribed and unpaid capital*" = 1012 "*Subscribed and paid-up capital*".

Incorporation of companies by organized crime groups has at some point become a practice in the United States of America, which has generated a vigorous response from state authorities, especially with regard to those companies operating in risk-sensitive areas of money laundering, such as banks, insurance companies, brokerage firms, etc. It goes without saying that it is extremely easy to launder money when the offender is actually the bank's owner.

Money laundering schemes by combining illicit funds into the regular business of the company has the advantage of offering anonymity to operations as long as the company used was from the very beginning

constituted with suspicious funds and the offender holds control over it.

Given the obvious risks associated with the mix of illicit funds in the ordinary business of companies, the EGMONT⁶ Group has dedicated two chapters in the study of this phenomenon in "*100 Situations of Money Laundering*". Out of the 100 situations, the largest subsection shows black money blends in the business structure, due to attractiveness for launderers. One of the factors that led to the authorities' finding of these cases was the establishment of a new company, followed immediately by the sudden increase in the volume of transactions made by the company in the case, which could raise suspicions for the reporting entities⁷.

The infiltration of illicit capital into the share capital of companies raises a number of specific problems:

- The use of criminal capital, cheaper than illicit capital, offers a competitive advantage to companies controlled by organized crime groups, fundamentally disturbing the regulatory balance characteristic of market economy based on demand and supply;
- Control over corporations (which may become corporations) by criminals gives them an increasing power in the economy and society, with major risks that the status of investors, business people, also gives them political power, a state in which the very existence of the rule of law is threatened;
- Money laundering suspicions can be more difficult to be detected by external entities of the company (banks, accountants, auditors), as the whole activity of the company is directed to recycling operations. In other words, an abnormality can not be identified in a series of transactions that have (all) anomalies characteristics;
- A number of activities, such as nightclubs or restaurants, have more cash receipts, making it natural for large amounts of cash to be deposited in the company's cash desk or bank accounts. If the company was incorporated even for use in recycling black money, the situation becomes even more risky.

From the perspective of the offender, infiltration of black money into the company's share capital may be the stage of integrating the criminal profit, but from an accounting perspective it is the time of placing the illicit funds in the company's accounts. In the case of procedures for identifying the assets for seizure / confiscation, it should start from the accounting records and to follow the path, respectively the way of using the relative funds.

To better accurately reflect this integration stage, an example of such transaction (Bachmann, 1992) is the purchase of some businesses that have experienced considerable losses, and then, using the illicit financial

⁶ The EGMONT Group is an international body of Financial Intelligence Units around the world. The aim is to strengthen the analysis capacity of suspicious operations and promote the exchange of information between the FIU members. www.egmontgroup.org.

⁷ „100 cases from EGMONT GROUP” – page 10, www.egmontgroup.org

funds; the businesses are financially revived and resold at their real value.

Conclusion

The profit thus obtained appears to be a result of high-performance management and thus has a legal source, without any suspicion that commercial and financial transactions have been invested in financial funds, for instance, from drugs or arms trafficking.

Such a process is also used in the real estate market by purchasing a low-cost property, and then, using illegal funds, it is refurbished and resold at market value, resulting in an appreciable difference that is most often due to the improvement works with own forces and materials acquired in time (Bica, 2010).

After setting up the company and opening bank accounts, citizen M contacted the bank to discuss other investment projects he wanted to make. The analysis conducted by the Financial Intelligence Unit led to the police officers being informed and the citizen M was arrested on charges of money laundering. It seems that M's father had an impressive fortune in committing crimes, which he reinvested by setting up real estate agencies, or by financing companies incorporated in his name, on behalf of his son or on behalf of other family members.

Concluding, we can say that the use of commercial companies as levers for recycling of some origin funds, at least doubtful, was an attractive activity for criminal groups, because they managed to hide behind another legal entity that had a behavior in the market apparent to legality.

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