

Methods and techniques of introducing black money into the financial accounting circuit

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Abstract: *Classical patrimonial crimes with operating modes that make them visible at the time of committing, such as robbery on a currency exchange office or a bank, traditional fraud, are no longer of interest to the new generation of white-collar offenders. They have found that they can earn much higher amounts of money with far lesser risks by using more sophisticated procedures, such as fraudulently obtaining subsidies or facilities, misappropriation, tax frauds or trade-related frauds via the Internet, illegal VAT reimbursements, smuggling or money laundering. The reason lies in the fact that the latter are more gently punished than the former, and the profits are much higher.*

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Introduction

Although it is clear to everyone that money laundering is a phenomenon with widespread negative implications for a well-functioning of a healthy economic system, accountants (and not just them) are asking a natural question: why is the state imposing on them obligations on prevention of an offense, as this is normally the duty of specialized, administrative and / or law enforcement bodies. The question is justified but it also has a very reasonable answer. [6]

Over the past decades, criminological science has found a shift in the profit oriented organized crime from violent crime to economic crime (fraud, VAT fraud, insurance fraud, cyber fraud, etc.).

In terms of profit rate, the illicit economy has no equivalent. Which product, which service can be sold in licit trade with a win that can reach up to hundreds of times the initial investment? Perhaps the trade of art objects can generate comparable margins (of profit). This financial force opens for the organized crime the road to the political, administrative and judicial power through a scientific dose of threat, blackmail and (especially) corruption. Anonymity is ensured through the creation of legal facades, by buying shares in companies or by buying trade funds. In turn, these activities produce benefits or facilitate the recycling of dirty money.

In this context, one can find that there are new types of criminal activities that appear and are being perfected on a daily basis, establishing that regardless of the economic or violent nature of the offense that generated the illicit financial funds, the money laundering activity becomes necessary and related, and the



"white collars" have no problem in providing assistance and counseling to persons showing obvious signs of behavioral violence.

In today's world, driven by globalization, by the falling obstacles to capital mobility, economic crime is characterized by a permanent relationship between legal and illegal activities, and this relationship is, in our opinion, ensured by the infiltration of dirty funds in the surface economy, i.e. money laundering, which is often performed involving the accounting of legally operating companies.

For law enforcement bodies, the presence of figures that do not fit into the typical criminal plot makes it even more difficult to identify the separation line between legal and illegal in economic and financial terms. In this criminal-commercial context where information plays a decisive role, and organized crime and financial crime have more and more common features and are beginning to overlap, the involvement of professionals in the efforts to fight this phenomenon has become mandatory .

2. Risks of money laundering in relation to company accounts

As we have shown, the company's accounting can and is being used in all phases of the money laundering process: placement, stratification and integration, with or without the involvement of institutions in the surface financial and banking system.

A particular benefit to the use of company accounts consists in the supporting documents accompanying the financial bleaching operations of illegally obtained funds. This advantage has been identified and used by money launderers from the time of the famous American gangsterism, and the operating principles are similar today, with the mention that the methods and tools are much more sophisticated and they include: company agreements to be credited by the associate or offshore incorporated companies, consultancy contracts with external partners, financial leasing contracts, debt assignment contracts, fictitious contracts with "ghost" companies, real estate transactions, capital market operations, etc.

Another "loophole" provided by the company's accounting for a potential money launderer is that at least a part of the recycling circuit can be carried out without the involvement of third parties, so that the degree of risk (for the offender) associated with committing the offense is extremely limited , which is extremely dangerous.

However, placement and even stratification of dirty money is perfectly possible through successive operations in the company's cash register, only the balance of the operations being (possibly) deposited in a financial institution, in the case of company financing or crediting, successive cash payments of invoices, respecting to the daily cash pay limit.

Taking into account the different positions of the accounting accounts in relation to the risks and phases of money laundering, we have carried out a detailed analysis of accounts 531 "Cash Register" and 512 "Current Accounts with Banks" in three phases of the circuit, namely placement, stratification and integration :

- ✓ **531 - "Cash Register", Placement.** Fraudulent money can be used to credit the company by the associate or by third parties with amounts being deposited directly into the company's cash register. This operation has the enormous advantage that no external entity is involved that could detect the (potentially) suspect nature of the operation and report it to the competent state institutions (the National



Office for Prevention and Control of Money Laundering). The justification document used is “the cash collection order”, a document that circulates only within the company and on which the collection of the funds is registered, with the mention that the law did not set a limit to cash payments coming from individuals.

There is, however, the requirement to report daily cash receipts higher than the equivalent in lei of 15,000 euros. The funded company is the one that decides whether to report or not. Law no. 656/2002 stipulates: "(6) The persons referred to in art. 8 or the persons designated according to the provisions of art. 14 par. (1) shall report to the Office, within 10 business days, about those cash transactions, in lei or foreign currency, the minimum amount of which represents the equivalent in lei of EUR 15,000, regardless of whether the transaction is carried out through one or several operations which seem to be connected.

Starting with 09.05.2015, Law 70/2015 has established limitations for cash collection and cash payments from and to individuals: “cash receipts from individuals up to a daily limit of 10,000 lei / person, representing the value of deliveries of goods or services, assignment of receivables, borrowings or other financing, and cash payments to individuals within a daily limit of RON 10,000 per person, in the case of transactions representing the value of acquisitions of goods or services, dividends, assignments of claims or other rights and repayments of loans or other financing.” The normative act was updated in 2016 and 2017.

- ✓ **531 - “Cash Register”, Stratification.** The money placed in the cash register of the company "mixes" with other amounts in this account. From this account, you can make cash payments to different suppliers, so practically suppliers will be paid in black money. Subsequently, (at the end of the day or the end of the week) the resulting balance, in which the black money can be found physically or not, can be deposited into the bank account.

It is worth mentioning that, starting from 10.02.1996, there is no cash register amount limitation, according to the provisions of GO no. 15/1996 amended by GO no. 94/2004. Under these circumstances, companies can keep any amount of cash, from which they can make cash payments within the next period, without being required to deposit it fully or partially into their bank account.

- ✓ **531 - “Cash Register”, Integration.** After a while, based on the loan agreements concluded to justify the depositing of cash into the company’s cash register or the crediting of its bank account, the person intending to recycle dirty money can withdraw this money in cash from the company’s cash register.*
- ✓ **512 - “Current Accounts with Banks”, Placement.** The 512 accounts represent the main "gateway" for capital of criminal origin into the accounting of companies. For these accounts to be used at the placement stage, the operation must be a cash deposit into the company's account. Banks monitor all transactions and have reporting obligations both to the National Office for Prevention and Control of Money Laundering (NOPCML) and to the National Agency for Fiscal Administration (NAFA), as regulated since 01.07.2015 (bank accounts, persons signing for bank accounts, transactions over the 5,000 euro limit, etc.).

*t is thus noticed that from the point of view of money laundering a "mirror" relationship between the placement and the integration of money is not important. In other words, if money is placed by depositing cash into the company’s cash register, it is irrelevant whether the integration is done through the reverse operation (cash withdrawal from the company’s cash register) or by any other operation through which integration can be achieved (for example, the acquisition a durable good).



- ✓ **512 - “Current Accounts with Banks”, Stratification.** If the dirty money has already been placed in the financial system in the accounts of another entity, person or company, the stratification stage can be carried out with great ease and in the most various of ways: from foreign exchange transactions to supplier payments, restitution of debts to associates or entities affiliated to the group, repayment of bank loans, financial investments, etc. The stratification stage can be performed through account 512, regardless of the meaning of the operation, whether it is crediting or debiting.
- ✓ **512- “Current Accounts with Banks”, Integration.** The company’s bank account can be used in the integration stage in two major ways: by withdrawing cash or by transferring the money to the accounts of other commercial companies or individuals as the final destination of the money. A form of integration specific to the accounting of an enterprise only is the acquisition of large goods or securities by correspondence with the asset accounts. This way, the dirty money’s ultimate destination is the surface economy and it is used to finance the company's current activities, the offenders benefiting from the company's assets and from the company’s results in the financial years to follow. Appearing as a phenomenon lacking in social danger (on the contrary, maybe), the integration of criminal funds into the company's current commercial activity may be a form of laundering with adverse and difficult to counteract consequences on both micro and macroeconomic levels.

3. Methods and techniques of introducing black money into the company's accounting

With regard to money laundering through company accounting, a distinction has to be made between the actual placement stage, as it is in the literature, and the stage (operation) through which the dirty money enters its accounting.

The moment where the money is recorded in the accounting may coincide with the stage of placement of the illicit funds or may be subsequent to it. To illustrate the above, we will analyse two distinct circuits generated by fraudulently obtained money, the money being originally presented in cash held by the offender or another person wanting to recycle it.

Situation 1 - the placement stage is prior to the moment the money enters the company's accounts. The amount illicitly obtained is deposited in a bank account of the offender or the launderer, this being the placement step. Any subsequent operation is stratification until integration

After the money is deposited into the account, a payment is made to the account of a company, justified as “loan”, based on a contract concluded between the individual and the company. The moment the dirty money enters the company’s accounting is represented by the cashing-in operation into the company’s bank account and the related accounting entry, but from the point of view of the money laundering the amount was already “placed” in the financial and banking system, the accounting operation 5121 - “Bank accounts in lei” = 462 - “Various Creditors” or 5121 “Bank accounts in lei” = 455 “Amounts due to associates/shareholders” (depending on the relationship of the launderer with the company concerned) being already a part of the stratification stage.

Situation 2 - the placement step coincides with the moment of entry of the money into the company's accounting. The fraudulently obtained amount of money is deposited by the person directly into the company's bank account or at the company's cash desk with the same justification of “company loan”, but in this situation, the placement stage coincides with the input of the dirty money into the firm's accounting. The accounting operations related to the placement of the black money are in this case 531 “Cash register” = 462 “Various



Creditors” (531 “Cash register” = 455 “Amounts due to associates/shareholders”) or 5121 “Bank accounts in lei” = 462 “Various Creditors” (5121 “Bank accounts in lei” = 455 “ Associates/shareholders loans”).

A special situation is that of Trade Based Laundering operations, in which the dirty money is presented in the form of an accounting record different from the actual commercial operation. Dirty money does not physically enter into the accounting circuit, but is “projected” into a debt or distorted claim, creating the premises for payments or collection of money for laundering purposes.

Without ignoring the relationship between the stages of money laundering (placement, stratification, integration), which has been dealt with in a previous subchapter, from this paper’s perspective, it is the moment the black money enters into the company’s accounting records that is essential. Depending on this moment, it is possible to establish the money trace, the way it has been stratified or integrated, as well as the amounts that have undergone the recycling process.

More importantly, in the case of the initiation of criminal proceedings, the analysis of accounting operations performed with the purpose of money laundering can lead to the identification of the location of money or assets that have been purchased with black money for seizure / confiscation.

3.1. Company loan

Lending money to the company by the associates is an attractive option for money launderers regardless of whether it is done through the company’s cash register or bank account.

Generally speaking, **cash lending** is preferred by individual associates, since cash handling is not limited by law in any way. The crediting of the company by its associates through cash deposits into the cash register is a typical operation for tax evasion situations in which revenues are not recorded. Thus, the amounts resulting from the sale of the goods traded by the company are entered into the company’s cash register with the explanation “company loan” so as to create a claim on the company which justifies withdrawals of amounts from its accounts.

Lending cash to the company is an extremely safe method of money laundering, especially when there is a small number of people (associates and administrators) involved in the company’s activity. This safety is given by the “zero” exposure to entities in the banking financial system, who may be aware of possible irregularities and who may detect suspicious elements in the activity of the company. After the money is cashed, it is immediately mixed with the amounts already in the account 531 - “Cash Register”, after which new cash payments can be made to various suppliers. The balance may be deposited into the bank account, and there is no direct contact in this situation between the creditor of the company and the credit institution.

However, the use of this money laundering method also has a number of disadvantages, which is why it is used for smaller scale criminal activities that do not require the transfer of large amounts of money (millions of euros!) and are non-transnational.

Lending money to the company through the account 512 - “Current Accounts with Banks” = 455 - “Shareholders/Associates Loans” is one of the most widespread forms of infiltration of fraudulent profits in the current activity of the company and thus in the surface economy .

Unlike the direct infiltration of black money into the company’s accounts (cash deposited in the cash



register), lending money to the company's through the bank's accounts has no value or currency limitations.

Crediting the company by the associates - individuals can be done both in lei and in foreign currency, from their accounts opened in Romania or abroad [5]

In this sense, a typology is hypothetically described as follows:

A company X SRL is owned by two individuals A and B, both foreign citizens. On October 12, 2012, the company registered a cash payment of EUR 600,000 into its bank account from Associate A by crediting the account 455 "Shareholders / associates loans" with the amount of RON 2,400,000. The next day, on October 13, 2012, the company was also credited through bank transfer, based on an interest-free contract, with the amount of EUR 500,000 by SC W LTD (incorporated in the jurisdiction of citizens A and B), a non-associated company which is also controlled by the individual A. The operation was recorded in the account 462 "Various Creditors" that was credited with RON 2,000,000.

As a result of these loans, the company acquired securities (508 "Other short-term investments and assimilated claims" = 5124 "Foreign currency-denominated accounts"), in this case mortgage loans (by creditor novation) from a foreign company M, incorporated in the same jurisdiction from where citizens A and B came from. For the payment of this purchase, the amount of EUR 1,100,000 was paid into an external account held by company M.

Shortly after the acquisition of the securities, SC X SRL sells the securities for the amount of EUR 1,200,000 to a company T registered in a tax haven, thus closing the account 508 "Other short-term investments and assimilated claims" and achieving revenues in the amount of EUR 100,000, with the rest of the amount repaying the loans received from associate A and from the non-resident company W LTD.

3.2. Company loans from entities holding participation interests

Company loans from entities holding participation interests is another method of recycling black money, usually on the territory of other states than the one where the offense(s) was (were) 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 of euros (or the equivalent in any currency) from one jurisdiction to another.

The method has a number of advantages for money launderers such as: the high value of loans that can be granted in view of the association relationship between the parties, the favorable conditions for granting the loans which are justified in the same way, performance of operations between companies controlled by the same individual or group of individuals, all of which account for a much more diminished risk of detection.

A hypothetical example could be the following:

Between SC F LTD (registered in the British Virgin Islands) as a lender and SC A SRL as the borrower, the following loan agreements were concluded:

- No. 1 /2011 for the amount of 400,000 EURO.



- No. 2 /2011 for the amount of 90,000 EURO.;
- No. 3 /2012 for the amount of 300,000 EURO;
- No. 4 /2012 for the amount of 500,000 EURO.

From the aforementioned agreements it results that the destination of the loans granted by SC F LTD is the construction of residences on the land located in the city of K, Q County.

According to the balance sheet, these amounts are recorded in SC A SRL's account 1663 – "*Debts to companies holding participation interests*", since SC F LTD is an associated company of SC A SRL.

The amounts collected are found in the accounts 231 - "*Tangible fixed assets in progress*", 232 - "*Advances granted*" and 5121 – "*Bank accounts in lei*". Part of the funds were used for expenditure on advertising services performed in 2008 and 2009.

Until 30th September 2012, SC A SRL has not refunded any amount of money from the above agreements. The repayment term is two years from the granting date of the loan.

In the above example, the money representing the criminal profits of an organized crime group was entered into the SC A SRL accounts that used it to set up assets (tangible assets). Upon expiration of the credit repayment term, the criminal group may opt to reimburse the money (now washed with the help of the Romanian company) or turn it into shares which will give it the right to dispose of company A and (possibly) of turning it into a recycling vehicle for subsequent operations.

4. Conclusions

The money laundering process takes place through institutions and legal procedures that have been set up to address market needs that are very different from those sought by those who recycle fraudulent money. Thus, a money laundering offender does not use ATMs to withdraw cash but to transfer money without the supervision of bank employees. Also, the confidentiality of bank transactions does not serve them to secure a citizen's right to privacy, but to escape the investigation of the suspicious funds they hold. The advantages of free international capital flow are not used to increase the promptness and effectiveness of fair trade operations but to transfer large amounts of money from states or areas with strict banking supervision provisions to places that are more permissive or less prepared to detect and counteract fraudulent activities.

Analysing the accounting operations meant to launder money can lead to the identification of the location of money or assets that have been purchased with black money for seizure / confiscation. This is because the accounting records and even the financial statements drawn up on a regular basis are capable of providing information based on which it can be deduced that there are some dubious transactions carried out or that have been carried out through the respective company.

To summarise the above, we can conclude that dirty money can be infiltrated into the company's accounting in three ways:

- **Directly**, by physically depositing the money into the cash register or into the company's bank



account (where placement overlaps with the entry of money into accounting);

- **Indirectly**, by recording financial flows through bank instruments doubled by accounting operations;
- **Through an accounting projection**, when a value is inserted or extracted from the company's patrimony, based on altered documents (the TBML situation).

When analysing money laundering related issues, the first correlation between the notion of risk and the accounting profession is how this is transferred from the accountant to the competent authorities when a suspicion occurs.

If there are abnormal elements in relation to a transaction or a client, there is inherently the risk of the accountant engaging in actions / operations that could involve money laundering or other criminal offenses. At that point, the accountant may transfer the risk by submitting a suspicious transaction report to the Financial Intelligence Unit (the National Office for Prevention and Control of Money Laundering) or simply assume it, either out of ignorance or by option.

This system involves the adoption of risk-based protection procedures by accountants, aiming at measures to prevent and minimize the phenomenon of money laundering / terrorist financing being taken on different levels and degrees depending on the vulnerable areas identified. The purpose of this approach is to allow resources to be allocated as efficiently as possible, according to the principle: the highest risk gets the most attention.

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