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EUROPEAN COMMITTEE ON CRIME PROBLEMS
(CDPC)

SELECT COMMITTEE OF EXPERTS ON THE EVALUATION OF ANTI-MONEY LAUNDERING MEASURES
(MONEYVAL)

Second round mutual evaluation report on Ukraine

SUMMARY

1. A MONEYVAL team of examiners, accompanied by one colleague from the Financial Action Task Force (FATF), visited Ukraine between 16 – 20 September 2003, in the context of MONEYVAL's second round of evaluations.

2. The purpose of the MONEYVAL report is twofold: to follow up the recommendations made to the jurisdiction in the first round; and, secondly, to examine more closely the effectiveness of the anti-money laundering regime at the time of the on-site visit.

3. This evaluation team found significant improvements in the anti-money laundering system in Ukraine since the first evaluation report was adopted in January 2001. The main achievements are the legislative base to fight money laundering with the passage of the law on "Prevention and Counter-action to the legalisation (laundering) of the Proceeds from Crime" ("the Preventive Law") and the associated Resolutions under it, and the setting up of the state system to combat money laundering with the SDFM, as the country's FIU, at the centre of the system with access to a broad and comprehensive range of additional information. The preventive law provides a basically sound, if complex, legal basis for an unusual and suspicious financial transaction reporting regime which has the capacity to perform effectively. The political commitment to improving the anti-money laundering regime is also evidenced by the allocation of significant human resources and an impressive IT infrastructure to the FIU.

4. By way of background, organised crime groups are known to be involved in money laundering operations and are responsible for certain categories of predicate offences, including human, drugs and arms trafficking. In the first six months of 2003, law enforcement had detected 19 laundering offences committed by organised criminal groups.

5. Illegal income is said to be mainly generated by the following: economic crimes (usually in the form of illegal production, storage or sale of excise goods and breaches of the procedures for economic activities); corruption; tax evasion and fraud (including manipulation of the privatisation process) as well as smuggling and crimes against property. Drugs offences are also thought to be a continuing generator of criminal proceeds.

6. There have also been significant changes so far as money laundering criminalisation is concerned since the first round. At the time of the first on-site visit, only drug money laundering was criminalised. This remains a separate offence in A. 306 of the Criminal Code. The physical and mental elements of the A. 306 offence, if it is to be retained, need to be brought in line with the Strasbourg Convention.

7. A. 209 was introduced by the new Criminal Code of 1 September 2001, which was amended by the law of 16 January 2003. The new article extended the laundering offence to "socially dangerous illegal actions". This term defines the predicate criminality as any offence that is punishable by 3 or more years' imprisonment (with the exception of offences covered by A. 207 and 212 – ie capital flight and tax evasion). It covers (as does A. 306) "own proceeds" laundering. The coverage of the physical elements of the money laundering activity is comprehensive and consistent with the international reference instruments. Nonetheless, it was regretted by the examiners that the "all-crimes" approach to predicate offences had not been adopted.

It is understood that there are plans to reduce the threshold of domestic predicate offences from three years to two, but the examiners consider this should be further reviewed. There is, in any event, an inconsistency between foreign predicates and domestic ones. Unlike domestic cases, where the three-year threshold applies, money laundering can also be charged in respect of foreign predicate offences on the basis of dual criminality, without reference to a 3-year restriction. The examiners cannot see the logical distinction and urge that the 3-year threshold is also abandoned in respect of domestic predicates. The mental element, which currently requires wilfulness, implies real knowledge of the specific predicate offence. It appeared that the jurisprudence generally precludes "knowledge" being capable of being deduced by a court from objective factual circumstances, and there were doubts as to whether wilful blindness would be covered. The examiners urge that the Ukrainian authorities ensure that the provisions of A. 6(2) (c) of the Strasbourg Convention, which permit knowledge, intent or purpose to be inferred from objective factual circumstances can be applied in money laundering cases and ensure that wilful blindness can satisfy the mental element. The examiners also advise that consideration should be given to the introduction of negligent money laundering. Equally consideration could usefully be given to a lesser mental element, namely (subjective) suspicion with appropriately lower penalties.

8. There is no concept of corporate liability in Ukraine, although some administrative laws do provide for some punitive measures against legal entities. The examiners recommend that a review is undertaken to determine the extent to which civil or administrative liability applies to legal persons in a money laundering context, and whether sufficiently effective, proportionate and dissuasive sanctions are in place.

9. The various confiscation provisions present a rather unclear picture. There are two basic grounds for confiscation: confiscation as material evidence, and confiscation of property as a form of punishment, which is a very focused and incisive measure and applies to a series of very lucrative crimes, such as money laundering, drug trafficking and smuggling.

10. The examiners consider that the existing confiscation provisions should be generally reviewed. The examiners (sharing the views of the first round evaluators) consider that the current provisions should be replaced by a coherent modern confiscation regime which clearly focuses on the confiscation of both instrumentalities and criminally acquired proceeds (as widely defined in the Strasbourg Convention) or property of equivalent value (where the proceeds have been dissipated) in a broader range of serious proceeds-generating offences. Such a regime should also provide for the confiscation of such proceeds from convicted persons and from third parties, while protecting the rights of the *bona fide* purchaser for value. Consideration should also be given to applying a confiscation regime in appropriate circumstances where a verdict cannot be reached because e.g. the defendant has died, absconded or for any other reason is unable to stand trial. In the course of reviewing the confiscation regime, the Ukrainian authorities might also wish to consider the issue of how prosecutors identify to the courts which assets are capable of being confiscated. For some particular offences, elements of practice which have proved of value elsewhere might usefully be considered, such as the reversal of the burden of proof post-conviction as to whether assets in the possession of the offender were criminally acquired, or proof in similar circumstances on the balance of probabilities. To support such an approach to the confiscation issue, the examiners consider that more resources need to be invested in modern financial investigation in all major proceeds-generating offences.

11. The preventive law was enacted on 28 November 2002 and came into effect on 12 June 2003, having been amended twice before implementation. It provides for a system of 'financial monitoring'. Entities which are involved in financial transactions (i.e. obliged institutions) are subject of 'initial financial monitoring'. They include: banks, insurance companies and other financial institutions; payment organisations; stock exchanges; professional participants in the Securities Market; gambling institutions; companies and organisations which manage investment funds; money remitters and other legal entities that engage in financial transactions. The list should be extended to fully reflect the 2nd EC Directive (2001/97/EC). The entities of initial financial monitoring are required to: identify persons engaged in financial transactions or who open accounts; detect and register financial transactions subject to financial monitoring; report to the SDFM financial transactions subject to "compulsory" and "internal financial monitoring" within 3 working days from their registration; maintain customer identification and maintain transaction data for 5 years; appoint compliance officers; and train employees in detecting transactions subject to initial financial monitoring. The unusual transaction reporting system is based on a threshold limit and other objective criteria set out in the law. The suspicious transaction reporting regime applies *inter alia* the 'internal monitoring regime' to any other financial transaction (regardless of a threshold), *if there are grounds to believe* that (it) is conducted with the aim of legalisation.

12. Thus, the system is now operating with large numbers of disclosures to the SDFM, though mainly (at the time of the on-site visit) from the banks. More disclosures need to be received from the non-bank financial institutions and from the securities market. It was understandable that a preventive system, in such a big transitional economy, has largely turned in its initial stages on automatic disclosures, based on objective criteria set out in the law. 70% of disclosures are based on such objective criteria. As the system develops, more emphasis needs to be placed on the subjective assessments of reporting entities as to what are suspicious transactions for transmission to the FIU. Equally, the suspicious transaction reporting regime should be broadened beyond the transaction base to cover disclosures of any fact indicative of money laundering (in line with the 2nd EC Directive). More guidance and training on these aspects of the reporting system should be provided. The FIU passed 11 suspected money laundering cases to law enforcement at the time of the visit, which was an acceptable output after 4 months of functioning.

13. As well as the introduction of clearer regulation of the customer identification process in the Preventive Law, in parallel, the examiners welcomed the amendment to A. 64 of the Law on Banks and Banking to prohibit the opening and use of anonymous (and coded) accounts and to prohibit the entry into contractual relations with clients (legal entities or natural persons) in the case of doubts as to whether the legal entity or natural person acts in their own name. Moreover, as of 11 July 2003, the banks of Ukraine closed all anonymous and coded accounts under a Resolution of the National Bank of Ukraine. That said, Ukrainian banks were allowed, at the time of the on-site visit, to issue, as a means of attracting funds, certificates of deposits to bearer, whereby the purchaser or the person who surrenders the Certificate of Deposit is identified and registered only if the amount of the deposit exceeds UAH 50,000. The examiners recommend that the NBU should examine the whole issue (of certificates of deposits to bearer) to determine whether such instruments can be misused for money laundering purposes and that it should consider prohibiting them.

14. The Law on Banks and Banking Activities and the Law on Financial Services and State Regulation of Markets of Financial Services now require full disclosure of beneficial ownership information at opening of accounts for physical and legal

persons. Banks and financial institutions are obliged to refuse to open accounts and carry out transactions if this information is not provided.

15. Given the brief time between the introduction of the preventive law (and amendments to the Law on Banks and Banking Activity) and the on-site visit, it would have been premature, at the time of the on-site visit, to draw any firm conclusions on the effectiveness of the preventive system as real implementation had just commenced. It is clear that, in general, the legal framework gives greater emphasis to the identification of clients, including beneficial ownership, and it is now up to the supervisory authorities to see that this is being carried out in practice through meaningful compliance checks. The evaluators considered that the Prudential Supervision Department of the National Bank of Ukraine (regulators for the banks and exchange houses) needs to be strengthened to meet their obligations, which should include appropriate guidance to and supervision of the banks (and any licensed non-banking institutions) offering money remittance services. The Securities and Stock Market Commission needs to intensify its supervisory work and raise money laundering awareness among stock market participants. The State Commission for Regulation of the Financial Services Market, created in December 2002, was initially tasked with creating a register of all pre-existing financial institutions. According to the law, financial institutions were allowed one year from their registration to comply with legal obligations. It appeared therefore to the examiners that, at the time of the on-site visit, some financial services entities (including pawn shops and trusts) were formally outside the scope of the preventive law at that time. The examiners consider that monitoring and supervision of the non-banking financial institutions should be intensified, and that the Commission's resources should also be strengthened beyond the increases planned at the time of the on-site visit.

16. The Ukrainian authorities should ensure that full information is available on the ownership of banks, and on exchange houses and casinos, and that checks on sources of capital are in place for banks and non-bank financial institutions.

17. The FIU is authorised under the anti-money laundering law to exchange information directly with its counterparts and to co-operate with international money laundering bodies. It applied for Egmont Group membership, and has entered into co-operative relations with other FIUs1. No major problems were raised in respect of international co-operation at law enforcement and judicial level, and Ukraine conscientiously applies the 1990 Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime (the Strasbourg Convention), to which it is a party.

18. The system would domestically benefit from the SDFM having power to suspend transactions in appropriate cases of suspected money laundering. The SDFM itself is playing the major leadership role in the co-ordination of the system, particularly at an operational, and strategic level through the Inter-Departmental Working Group. At the strategic level, they need to develop key performance indicators for the system as a whole and monitor progress in all sectors on the basis of reliable statistical information. This includes monitoring the progress of the prosecutorial/judicial side in achieving convictions and significant confiscations in money laundering cases, which are not simply based on "own proceeds" laundering, but which also target laundering on behalf of 3rd parties, particularly those who launder on behalf of organised crime, in serious proceeds-generating cases (beyond the fraud and fiscal predicates). A more proactive emphasis is therefore urged on asset tracing and money laundering investigation and prosecution in non-fraud and non-fiscal offences. The law enforcement statistics provided to the examiners do show 91 convictions in total

[1] The SDFM was accepted as a member of the Egmont Group in June 2004.

for offences under A. 209 and A.306 in 2002, and 49 in total for both offences in the first 9 months of 2003. However, it was noted that all A 209 and A 306 convictions are achieved simultaneously with the predicate offence, or are directly linked to a conviction for the predicate offence. 94% of cases represented "own proceeds" laundering. It was noted also that there are no "stand alone" convictions for money laundering. This may be the result of the present jurisprudence, which takes a very rigid and demanding stance towards the proof of the predicate offence: a previous or simultaneous conviction is a prerequisite before a money laundering conviction can be secured. The examiners strongly advise that this approach is re-visited to ensure that autonomous prosecutions for money laundering can be brought successfully against third parties who launder on behalf of others, (particularly where the proceeds-generating criminality is foreign). It is advised that the Ukranian authorities ensure, if necessary by legislative provision, that a money laundering prosecution can be brought in the absence of a judicial finding of guilt for the underlying predicate offence.

19. All in all, in a very short period, Ukraine has made rapid progress to build a firm legislative base and put in place an anti-money laundering infrastructure. The challenge now for the SDFM, the regulatory authorities, police, prosecution, and judiciary is to make the preventive system operationally effective, and to develop an effective repressive money laundering system which is producing results in all areas of predicate crime. Many of the building blocks are now in place.

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