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EUROPEAN COMMITTEE ON CRIME PROBLEMS
(CDPC)

Select Committee of Experts on the Evaluation
of Anti-Money Laundering Measures
(PC-R-EV)

FIRST MUTUAL EVALUATION REPORT ON UKRAINE

SUMMARY

1. A PC-R-EV team of examiners, accompanied by colleagues from the Financial Action Task Force (FATF), visited Ukraine between 22-25 May 2000.

2. Most criminal activity in Ukraine appears to have an economic purpose. While drug use is increasing, the Ukraine remains primarily a transit route in view of its geographical situation at the centre of Europe. Three primary areas of criminal activity are thought broadly to generate illegal proceeds: smuggling (of drugs, human beings and arms); fraud and tax evasion including the illegal manipulation of the privatisation process; and corruption. It is believed that most crime is conducted by groups, as opposed to individuals. Tackling organised crime is a major law enforcement priority.

3. The Ukraine is seriously vulnerable to money laundering. While some limited steps have been taken, there is still much work to be done to create an anti-money laundering system. There are currently significant deficiencies in all sectors. Paramount among these is the absence of a comprehensive anti-money laundering preventive law.

4. The economy is primarily cash-based, with limited use of non-cash financial instruments. This exposes Ukraine to money laundering at the placement stage. The commercial banks have therefore been the focus of Ukraine's first efforts at addressing money laundering through development of some rules on customer identification. There are also clear vulnerabilities at the placement stage in the exchange houses (of which the precise numbers are uncertain but which are estimated at about 5000) and in the casinos, which have money remitting services and currency exchange services attached to them. The number of casinos is not known. The casinos were not at the time of the on-site visit subject to any registration or licensing regime. The Ukrainian authorities reported that money laundering is often achieved through "payments" by front companies, under fictitious external contracts with fictitious companies overseas via offshore banks. Such money is often reinvested in Ukraine through the privatisation process. The purchase of real estate and luxury cars can also offer opportunities for money laundering at the integration stages.

5. It was generally accepted that some of the main outflows of money from Ukraine were unpaid taxes, facilitated by the use of front companies. It was, however, less clear to the examiners how far all the relevant authorities had fully analysed the extent and movement of proceeds, which are in fact produced by major non-revenue profit-generating offences. The examiners perceived that there is, at present, an incomplete understanding of the money laundering problem in the Ukraine by the Ukrainian authorities. Numerous agencies were seeking to craft responses to the money laundering threat without a real sense of the overall problem. The examiners strongly advise therefore that, as a first step, consideration is given to convening a seminar of all relevant ministries, regulators, bank representatives, prosecutors and investigators to develop a greater understanding of how criminals launder their money in Ukraine and how they move their funds into foreign accounts.

6. On the legal side, Ukraine has signed and ratified the 1988 United Nations Convention on Illicit Traffic in Narcotic Drugs and Psychotropic Substances (the Vienna Convention), which came into force in 1991 and the 1990 Council of Europe Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime (the Strasbourg Convention), which came into force on 01.05.98. The examiners were advised that both these Conventions were directly applicable in Ukrainian law. Nonetheless concerns were expressed that national legislation had not been brought into conformity with those Conventions at the same time, and work is ongoing to supplement the Conventions with further domestic legislation. As a result of the ratification of the Vienna Convention, Article 229 (12) of the Criminal Code was introduced in 1995, criminalising drug money laundering. Cases of drug money laundering

have been investigated, though there have been no convictions. A new article in the Draft Criminal Code is intended to widen the range of predicate offences the proceeds of which can be the subject of money laundering investigations and prosecutions. The examiners urge speedy introduction of such a provision, and it is important that it covers all the physical aspects of the offence, as envisaged in the existing international conventions. The mental element of the offence would benefit from revisiting in the light of experience with the provisions. In the passage of the new criminal offence it may be helpful to consider additionally a mental element based on reasonable suspicion with lesser penalties. Consideration should also be given to the introduction as envisaged in the Strasbourg Convention of the concept of negligent money laundering.

7. The examiners were advised that there have been some successful confiscations, but the basis of these orders and their extent were not clear. In the view of the examiners, the confiscation regime should be carefully reviewed by the Ukrainian authorities to satisfy themselves that it is capable of confiscating both proceeds (with the wide meaning that is attached to the term by the Strasbourg Convention) and instrumentalities. The regime should not be capable of frustration by transfer of proceeds to third parties. It should be ensured that value confiscation orders can be made.

8. The examiners were also advised that the Ukrainian authorities have had some success in obtaining provisional measures in criminal cases. It was noted, however, that no provisional measures had been taken in any of the 39 drug money laundering investigations that had been opened. The examiners consider that the provisional measures regime should also be revisited to ensure there is full legal provision to identify, trace and seize property and freeze accounts with a view to confiscation of proceeds, as widely defined in the Strasbourg Convention.

9. Criminalisation of failing to report and "tipping off" is urged when a preventive regime is in force. Careful consideration should also be given to the introduction of corporate criminal liability.

10. The number of international legal instruments signed in a relatively short period of time by the Ukrainian authorities and the growing number of bilateral agreements demonstrate the country's willingness to co-operate internationally. Presently, the range of mutual assistance in money laundering cases is limited only to drug money laundering cases, and early enactment of a broader based money laundering offence is urged in this context also. It would be helpful in particular to the international co-operation regime if the Ukrainian authorities inserted into their law the procedure for the enforcement of foreign confiscation orders in case problems arise in the implementation of the Strasbourg Convention.

11. The preventive side is a very long way from being in line with the 40 FATF Recommendations and the European Union Directive of 10 June 1991 on the Prevention of the Use of the Financial System for the Purpose of Money Laundering (91/308/EEC). It is critical that the Ukraine demonstrates its political will to fight money laundering by passing a comprehensive anti-money laundering law quickly, which meets FATF standards, and that a preventive system becomes fully operational rapidly. Currently the banks, and the other main actors in the financial system, are not required to detect and/or report suspicious transactions. Indeed, the detection of suspicious transactions appears at present not to be within the priorities of the banks.

12. The examiners have seen a draft of a preventive law but the timescale for its enactment was not clear. Similarly it was unclear whether the draft seen was the final one. In any event it would broadly apply to a range of natural and legal persons conducting "financial operations",

as defined. The examiners strongly recommend that a mandatory suspicious transaction reporting regime is incorporated into the law without any monetary threshold.

13. There is much work to be done in building the co-operation of the financial sector in order that the preventive law does not fail for lack of compliance, as was understood to be the case with a reporting system in respect of dubious cash movements set up under the 1993 Law on the Principles of Combating Organised Crime. The examiners consider the development of a partnership approach between the authorities and the financial sector will be critical to the success of the Ukraine's fight against money laundering. To support this, it is necessary to establish clear legal provisions protecting financial institutions and their staff from criminal and civil liability in respect of disclosures made in good faith and to design systems for appropriate feedback. A supervisory regime for anti-money laundering obligations needs to be introduced (where there are existing supervisory authorities) with supervisors who are sensitised to the money laundering threat. Active consideration needs to be given to the regulation and supervision of anti-money laundering obligations in the exchange houses and the casinos.

14. Some action has been taken to stop the opening of anonymous accounts by a Presidential Decree in 1998, which annulled an earlier decree which allowed anonymous accounts to be held by residents and non-residents. Coded accounts are permitted, though their extent is unknown. When the preventive law is passed, the Ukrainian authorities will need to have regard to the risk that comprehensive control procedures for identifying suspicious transactions can be greatly restricted by the handling of numbered accounts. Moreover, customer identification and record-keeping obligations for the opening of normal accounts currently apply only to banks and these need to be extended to all financial institutions. Clear provision should be made to ensure steps are taken to verify beneficial owners when an account is opened (or a transaction is conducted).

15. Stricter controls on the licensing of banks and exchange houses need to be put in place, and consideration is urged of a requirement whereby the source of original capital is checked as part of the licensing process. The National Bank of Ukraine should have powers to revoke licences if money laundering or criminal infiltration has been established. The Ukrainian authorities will also wish to satisfy themselves that they have a proper system in place to guard against criminal involvement in the ownership of casinos. Given the concerns expressed to the examiners about the use of "front" and "shell" companies as vehicles for money laundering, the company licensing regime should be urgently considered with a view to the development of strengthened powers on business licensing.

16. A range of law enforcement agencies are pursuing anti-money laundering matters. Some, such as the Tax Administration, are working hard, according to their own priorities and perspectives on money laundering, and are having some modest successes. However the current lack of convictions and restraint orders in drug money laundering cases indicates an ineffective response so far to the overall money laundering threat by law enforcement. The Ukraine urgently needs some successful money laundering prosecutions and confiscation orders arising from traditional criminal activities associated with organised crime. Proper priority should be given to investigations and prosecutions in serious profit-generating criminal activities. Any unnecessary obstacles in the investigative process caused by banking secrecy should be identified and removed. Prosecutors and investigators, as well as needing to develop a clearer understanding of the techniques involved in money laundering, need to agree a common approach to the minimum evidential requirements for launching money laundering prosecutions, and receive more training and support in the techniques of financial investigation.

17. In the absence of an FIU there is no one body at the centre of the national anti-money laundering effort. Consequently there was inadequate communication and co-ordination across the law enforcement agencies. The creation of an FIU will therefore be central to the success of the Ukraine's overall fight against money laundering. The FIU, when it is established, should meet the definition for Egmont Group Membership and in due course apply to join that group. Planning for the FIU needs to start immediately and consideration should be given to making it a multi-agency unit. Indeed, the process for implementing the law as a whole should begin in advance of its enactment and it is recommended, additionally, that a co-ordination body is set up at a suitably senior level, including all the main players in the anti-money laundering regime, to develop joint ownership of an action plan.

18. By pursuing these recommendations urgently, the Ukrainian authorities can make progress towards rectifying the current deficiencies and make progress towards meeting the international standards.

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