

## **BANK OBLIGATIONS REGARDING FIGHT AGAINST MONEY LAUNDRING**

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**Abstract:** *The development of the modern society, accompanied by the changes, which the industrial revolution with the new technologies, scientific discoveries and technical innovations brought with itself, the changes which globalization brings with it, has inevitably influenced on the shaping of a new banking organization which had to adjust to the modern social changes, not only in an organizational and functional sense, but in ethical as well. Expansion of international trade relations and the emergence of multinational (international) companies, which have expanded their business activities outside national economy borders, occurred in the second half of the 20<sup>th</sup> century. Forming such economic subjects which were, for the purpose of maximizing profits, oriented towards global international markets, since national markets became too small, had far-reaching consequences on the international economic flows, and thus onto the national banking systems. However, the expansion of international business relations and multinational companies brought with it the risk of conducting criminal activities which make exceptionally large sums of money, and which are illegitimately acquired possessions. Money laundering is carried out through banks, whereby legalizing illegitimately acquired money and in that way it is included into the legal financial flows. The fight against money laundering has always exclusively been in the jurisdiction of law enforcement. However, bank's business activities practice in the XXI century has shown that the bank is the major place where one gains information on money laundering as a criminal activity category. Banks should develop principles for meeting clients, and according to that they should develop and form their own special registration standards and admission of client accounts, taking into consideration the risky profile of each client.*

**Keywords:** *business ethics, money laundering, fight against money laundering, banks, bank internationalization, bank business dealings*

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## INTRODUCTION

Bank business ethics consists of moral rules of behaviour towards socio-cultural and business surroundings, towards other people with whom one comes into business contact and towards decision-making, duties, obligations, rights, responsibilities, in all aspects and spheres of business dealings. Those rules are of universal character (they refer to all business activities directed towards a successful and profitable business dealing) and form assumptions for developing new ethical consciousness of all business participants, which is very important for business dealings on a global market where differences in economical, political, cultural, informational, religious, ecological and ethical sense are distinct.

Money laundering represents an activity which belongs to organized crime, in which money was acquired by committing a felony, and later through various techniques, shown as earnings gained through legal business dealings. The money laundering phenomenon is a distinct social danger for any society, because it causes disturbance in the economic system.

Bank management in the era of globalization business dealings has the commitment of coming up with and applying internal controls, whose goals should be directed towards harmonizing the bank business dealings with the laws and regulations against money laundering. In the future, each bank clerk will have to be trained to recognize money laundering techniques and characteristics as a criminal activity, in accordance with the recommendations of the Financial Action Task Force on Money Laundering – *FATF*.

The aim of the paper is a scientific approach to the importance of bank responsibility regarding the fight against money laundering in a globalization era, which implies mutual connection and cooperation of all clerks who can detect the techniques of this criminal activity. Having in mind the importance of preventing money laundering as a form of organized criminal for the society as a whole, the subject of this paper's research is the obligation of the bank to fight against money laundering with all available means.

This paper consists of three parts, with an abstract, introduction, conclusion and used literature. The first part of the paper refers to the description of business ethics in bank business dealings as a necessary factor of bank clerks' adequate behavior in a modern world. The second part describes the term, phases and techniques of money laundering. The third part refers to the banks' commitment regarding the fight against money laundering.

### 1. BUSINESS ETHICS IN BANK BUSINESS DEALINGS

Business dealings of each bank are based on business ethics, or at least on its basic characteristics. Business ethics implies rights, obligations and responsibilities of the organization towards individuals, their mutual relations, towards all business relation participants, towards all other organizations with which they do business with, but towards the society as a whole as well. All the problems which arise in a bank refer to the morality dilemmas of sincerity, honesty, respecting others and fulfilling promises. In business practice, all employees, managers as well, can find themselves in front of numerous ethical dilemmas and doubts.<sup>1</sup>

Violating ethical principles causes increased expenses and decreases the competitive ability of the business system, because it disturbs the bank's reputation in the business sur-

1 Subotić, D. (2009), *Korporativna društvena odgovornost: vrednosti, principi, modeli*, Institut za političke studije, Beograd, p. 80

roundings. Each ignoring of ethics means abuse of ethics. „Overall corruption and unethical behavior are foremost explained as a consequence of the institution fragility and lack of democratic reputation, which today is a special characteristic of developing countries“.<sup>2</sup> In bank business dealings the main cause of ethical principles' erosion is criminalization of the bank business dealings, in order to get wealthy. All banks are obliged to manage who they do business with and to take all necessary measures in order to prevent such occurrences. Their duty is to comply with international laws and codexes.<sup>3</sup>

Different types of seminars and employee practice are important banker education instruments in the field of detecting criminal actions. In this way manager and employed staff's consciousness is increased on the importance of applying internal controls and procedures in banking. It is very important that above all the top management supports the introduction and implementation of this concept. Responsibility for bank activity realization regarding estimating a risky situation has to be assigned to all organization hierarchy levels, from managers to bank clerks.

## 2. MONEY LAUNDERING

Money laundering signifies various activities directed towards legalizing money which has been acquired by doing criminal activities. Money laundering is a procedure of „legalizing illegally acquired money with the aim of covering up its' true nature and source“.<sup>4</sup> Money laundering is in its nature an obvious criminal activity of concealing which does not recognize local, national and regional boundaries, and thus it is difficult to precisely determine its distribution in international financial flows. Even though numerous international organizations, institutions and states have given many definitions, for the purpose of this paper money laundering can be determined as a set of complex and mutually connected actions which cover up the source, illegitimate nature, existence, place, placing and movement of assets acquired by doing criminal activities, in order for that property, for the sake of future undisturbed use, to be given an illusion of legitimacy.

Money laundering is carried out in three phases with several different mechanisms.<sup>5</sup> The first phase represents the placement of money, when illegally acquired money is attempted to be put into the financial system, for example, with small sums, since they do not seem suspicious as payments of large sums do. When money has entered the system phase two occurs in which the origin of the money is concealed by a number of transactions (purchasing and selling of equities) or transfers (domestic or abroad). The third phase is the integration phase when persons who wish to cover up the money origin return the money into economic flows and most often invest it in immobilia and business ventures. The first and second phase are very critical from the banks' point of view. The bank becomes a part of

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2 Dajanu, D. (2002), Realnost zahteva preispitivanje poslovne etike i društvene odgovornosti, Southeast European Times, p. 23

3 Božović, J., Krstić, B. (2014), Bankarstvo, Ekonomski fakultet Univerziteta u Prištini, Kosovska Mitrovica, p. 530

4 Business dictionary, <http://www.businessdictionary.com/definition/money-laundering.html>, (accessed 14. November 2017)

5 Jerez, O. (2003), Le Blanchiment de l'argent, Revue Banque, Paris, p. 135-138

the criminal chain unless it has developed mechanisms for detecting money laundering and hindering it, or if it ignores the illegal nature of suspicious transfers.

### 3. BANK OBLIGATIONS REGARDING FIGHTING AGAINST MONEY LAUNDERING

The general globalization trend, fast growth of informational technologies and acceleration of money flow has undoubtedly made the financial system more susceptible to attempts to make it an integral part of profit legalization which comes from criminal activities and terrorism financing. Although the banking system is not the only sector where one must actively pay attention to the money laundering problem, the bank sector has a key position in the money laundering procedure, given that money is transferred through banks. Banks that do not pay attention to money laundering prevention standards and do not have firmly set ethical principles based upon which they do business, can become targets of malversation and part of criminal money transfer flows. It can negatively affect not only the future bank relations, but public trust in the banking system as well.

In brief, money laundering is a process of transferring assets originating from criminal activities with the aim to cover up their illegal origin.<sup>6</sup> In 1990 Financial Action Task Force on Money Laundering – FATF defined forty recommendations in order to help financial institutions, regulatory organizations and governments to persist the money laundering phenomena.<sup>7</sup> This list was updated in 2003, in order to enrichen it with recommendations on opposing terrorism financing. The recommendations of the Financial Action Task Force on Money Laundering – FATF today form one comprehensive and consistent framework of measures for fighting against money laundering and terrorism financing. The recommendations refer to client identification, monitoring accounts and transactions, keeping transaction records and reporting on suspicious transactions, internal controls and revision, integrity standards and mechanisms which alleviate cooperation between supervisors and other competent bodies.<sup>8</sup> The set of these recommendations forms the money laundering prevention strategy framework, and it is the most important thing for the banks to identify suspicious clients and transactions. Banks have to know who they are doing business with, and have to establish adequate internal controls and procedures, as well as the process of examining and meeting new and existing clients.

Money laundering is organized on a global level, even though the money is most usually paid relatively close to the place it comes from. In the middle of the three illegal money transaction phases, financial transactions often take place in *off-shore* financial centres since large sums of money are daily transacted there. Methods and techniques of money laundering change daily and become complex transactions. Due to that, it is necessary to continuously monitor new money laundering mechanisms and tendencies. States battle in different ways the money laundering phenomena, sanctioning money laundering and terrorism fi-

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6 Jerez, O. (2003), *Le Blanchiment de l'argent*, Revue Banque, Paris, p. 25

7 Financial Action Task Force on Money Laundering – FATE, <http://www.fatf-gafi.org>, (accessed 14. November 2017. )

8 Bennet, T. (2004), *A Practitioner's Guide to Money Laundering Compliance*, Lexis Nexis, London, p. 36

nancing as well as any assistance with these activities. It is necessary to legally introduce the obligation to control money laundering and anticipate hindering procedures which are in accordance with internationally accepted standards, as well as confiscating possessions and money made from illegal activities.

The Basel committee has issued a set of principles which the financial institutions and regulators should follow in order to strengthen the internal policy of knowing your customer („*Know Your Customer*“ *KYC Policy*).<sup>9</sup> In accordance with those principles, banks should develop and form their own standards for registration and client account acceptance, taking into account the risky profile of each client. The risky client profile is determined by different risk indicators such as land of origin, employment, business activities, connected accounts, etc. Depending on the risk level, with the meeting your client policy the banks organize the terms for opening accounts, whereas detail verification standards are applied with clients who use more sophisticated services. There are several indicators which point out to a higher risk level for participating in a money laundering chain. Those are the following clients: clients that when opening an account hide their identity behind various corporative forms and professional mediators; clients in personal transactions whose nature requires a high degree of confidentiality; clients who are political or public figures; a new founded subject whose capital and business policy is difficult to analyse due to insufficient evidence; clients who use bank services in a correspondent relation, especially in cases when a bank is from a country where there are no suitable standards for fighting against money laundering or where there are no adequate mechanisms for verifying clients.

Without an adequate procedure and continuous monitoring of client business dealings, banks would be hindered from honoring the commitment on reporting about suspicious transactions. Suspicious transactions are the ones that there is reasonable doubt that they are connected with money laundering or financing terrorist activities. Reasonable doubt depends foremost on what is considered to be normal clients' business activities and usual financial transactions. When grading the transaction suspiciousness one starts from a client's risky profile. It is very useful to, for example, determine limits for a certain group or category of accounts or analyse transactions which surpass those limits, as well as transactions that could not be deemed economically justifiable and normal in certain client's business dealings. However, this evaluation often demands complex technical and human resources and an established monitoring system. In evaluating suspicious transactions one takes care of the factors such as the amount and purpose of the transaction, frequency and bank account balance. Banks should intensify monitoring accounts to/from which payments are frequently made, and which often have a minimal balance, but also so called “dead accounts” (ones that do not have frequent transactions) which have large sums deposited.<sup>10</sup>

## CONCLUSION

Business ethics in banking implies rights, responsibilities, obligations and liability of banks towards individuals, their mutual relations, towards all participants in business rela-

9 Dedeić, P. (2006), *Subjeki bankarskog prava i proces upoznavanja*, Pravo i privreda, no. 5-8, Beograd, p. 800

10 Dedeić, P. (2006), *Subjeki bankarskog prava i proces upoznavanja*, Pravo i privreda, no. 5-8, Beograd, p. 809

tions, all other organizations they do business with, but towards society as a whole as well. Not abiding to ethical principles causes increased expenses and decreases competitive ability of the business system, since it distorts bank's reputation in the business surroundings.

Money laundering is a process of legalizing illegitimately acquired money with the aim of covering up its true nature and source. Money laundering is done in three phases with several different mechanisms. The first phase, money placement implies a process where the illegally acquired money is sought to be put into the financial system. Once the money enters the system phase two commences in which the money origin is tried to be covered up by a sequence of transactions (purchasing and selling equities) or transfers (domestic or abroad). The third phase represents the integration phase when persons who wish to cover up the money origin return the money into economic flows and most often invest it into immobilia and business ventures. The first and second phase are the most critical from the banks' point of view, where the bank becomes a part of the criminal chain unless it has developed mechanisms for detecting money laundering and hindering it, or if it ignores illegal nature of suspicious transfers.

Even though the banking system is not the only sector where one must actively pay attention to the money laundering problem, the bank sector has a key position in the money laundering procedure, given that money is transferred through banks. Banks that do not pay attention to money laundering prevention standards and do not have firmly set ethical principles based upon which they do business, can become targets of malverzation and part of criminal money transfer flows. Financial Action Task Force on Money Laundering – FATF defined forty recommendations in order to help financial institutions, regulatory organizations and governments to persist the money laundering phenomena. The set of these recommendations forms the money laundering prevention strategy framework, and it is the most important thing for the banks to identify suspicious clients and transactions. Banks have to know who they are doing business with, and have to establish adequate internal controls and procedures, as well as the process for examining and meeting new and existing clients. Without an adequate procedure and continuous monitoring of clients' businesses, banks would be hindered from honoring the commitment on reporting about suspicious transactions. However, such evaluation often demands complex technical and human resources and an established monitoring system. Due to that continuous training and development of all bank clerks is necessary.

## LITERATURE

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