

# FINANCIAL SECURITY

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NO. 3 DECEMBER 2013

## V. ZUBKOV:

*"Qualitative leap in establishing the national AML/CFT regime was made possible thanks to the well-coordinated and hard work of the Russian financial intelligence staff, as well as the understanding of our partners".*





# FINANCIAL SECURITY

## CONTENTS

Welcome Speech of Yury A. Chikhanchin, Director of Rosfinmonitoring	5
Viktor Zubkov: "Human Resources Were Paramount"	6
Russian President V.V. Putin Held a Working Meeting With Director of Federal Service for Financial Monitoring Yu. A. Chikhanchin	10
Director of Rosfinmonitoring Attended a Meeting of the Presidential Council for Countering Corruption	12
New Law Sets Targets for Future	15
Assessment of Threats and Risks: on the Way Towards Finding Solutions to Strategic Objectives	20
Russia Presented 6 <sup>th</sup> Follow-up Report at the FATF Plenary Meeting	23
Russia – USA: Enhanced Cooperation	25
Drug Legalization as a Latent Threat to the Global AML/CFT System	26
New Counter Measures	29
Toward Creation of International Center for Risk Assessment in the CIS	33
Course Will Stay the Same	36
The National System of Financial Monitoring of the Republic of Kazakhstan	41
Financial Intelligence Officers of XXI Century	48
The IFES MEPhI as the Alma Mater for FIUs	51
Strengthening Cooperation of the EAG Member-States' FIUs During Anti-Drug Operation <i>Channel</i>	53
Network Approach to the Training of Financial Monitoring Specialists	55
Main Tasks: Upgrading Skills and International Cooperation	58
Virtual Currencies and Cryptocurrencies: New Possibilities or New Risks?	61
Discussion of E-Money, Cards and Payments 2013	65
Bitcoin – New Virtual Currency in Real Economy	68
Financial Monitoring in Banks	71
With an Aim to Strengthen Regional Stability and Security	72

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## DEAR READERS!

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This is the third and the last issue of Financial Security in the outgoing year 2013. Therefore, we would like to summarize the results of this challenging and yet eventful year.

2013 turned out to be very fruitful and successful not just for Rosfinmonitoring but for the entire Russian AML system. We jointly strived to accomplish the missions that had been assigned to us earlier and firmly defended the national financial system against criminal threats.

We achieved considerable success in the international fora. In summer 2013, Russia took the presidency of the Financial Action Task Force (FATF) and in October the follow-up report presented by our country was unanimously supported and adopted by all FATF members, which essentially meant recognition of the Russian AML/CFT system as one of the most mature in the world. We not just succeeded in becoming the member of the “exclusive club” but also took the leading position by adequately responding to the appeals announced at the G8 and G20 summits held in 2013 in Lough Erne and St. Petersburg, respectively.

Our victory was won, inter alia, through adoption of Federal Law No.134-FZ which was the outcome of the joint efforts and effective collaborative work.

This was the breakthrough event which essentially opened up new vistas for ensuring security of the national financial system by introducing progressive regulations for enhancing financial transparency and for optimizing the financial entities monitoring tools and mechanisms that meet the highest international standards.

But we should not rest on our laurels!

At present, we face the challenging task – to become the center for assessment of the national security risks and threats, accomplishment of which will require enormous efforts. We should keep on moving forward by achieving the desired goals and adequately responding to new and emerging challenges and threats.

The national risk assessment requires the cooperative efforts of all agencies concerned, which cannot be achieved without active involvement of all major AML stakeholders. Currently, it is important for us to integrate our intellectual potential and the capabilities of the government institutions and private sector. It is also important for us to keep in mind that the collaborative work is inefficient without common understanding of the assigned mission and methods of its accomplishment, since it is for the first time when Russia and other countries have to conduct comprehensive assessment of risks and threats. And time is running out for us – Russia faces the next round of the FATF mutual evaluations.

Happy New Year!

Wish you good luck and prosperity!

**Rosfinmonitoring Director**  
**Yury Chikhanchin**

THE MAGAZINE GUEST

## VIKTOR ZUBKOV: “HUMAN RESOURCES WERE PARAMOUNT”

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### *Background of Russian financial intelligence*

*Irina V. Ivanova,*  
*Editor in Chief*



*V. Zubkov*

**FS:** Viktor Alekseevich, you were the first head of the Federal Financial Monitoring Service of the Russian Federation. Could you tell us about the beginning of Russia's financial intelligence? What were the main reasons for its creation?

**V.Z.:** At the end of the XX century the impact of the global financial flows on the economic, social and political environment in a number of countries increased significantly. This dependence turned out to be especially great for the so-called countries-in-transition, and Russia was one of them.

Those were the years of primitive accumulation of capital where forms of ownership were shifting, legislation was rapidly evolving and the criminal world had a great influence over the overarching changes in our society. Illegal assets did not remain in the shadow, but were injected into *clean* industry, transferred abroad, and were used for achieving illicit political goals. It was the trend to use *dirty* money for expanding drug trafficking, smuggling, arms trafficking, and extremist activity

that raised the greatest concern of the international community.

In June 2000 the FATF published a list of countries and territories where anti-money laundering (AML) deficiencies hampered international cooperation. Russia was among those 15 jurisdictions.

This assessment of our AML efforts undermined the trust towards the authorities, blemished the country's international image, and led to actual financial losses.

It would be inaccurate to say that at the beginning of the new millennium Russia did not undertake any AML measures. As the cessionary of the USSR our country was party to a number of international treaties, participated in the MONEYVAL activities, and introduced an article to the Criminal Code that established responsibility for money laundering.

In 1999 the authorities created an Interdepartmental AML Center under the jurisdiction of the Russian Ministry of Internal Affairs. This was a notable step in the advancement of the international standards for AML and coordination between law enforcement and control authorities in Russia.

Nevertheless, the country lacked an AML system: first and foremost we did not have a basic law on combating money laundering.

The development of this regulation began in 1988, and it was not perfectly smooth. However, in the end, Federal Law № 115-FZ *On Countering the Legalization (Laundering) of Criminal Proceeds* was adopted by the State Duma on July 13, 2001, approved by the Federation Council on July 20, 2001, and signed by the President of the Russian Federation on August 7, 2001. It was in no small degree made possible due to an uneasy compromise of all the interested parties.

The adoption of this basic law led to a number of changes to a series of regulations, including the RF Criminal Code, the Federal Law *On Stock Market*, and the Federal Law *On Banks and Banking*.

Another important step towards an AML system was Decree of the President of Russia dated November 2001, № 1263 *On the Authorized Agency for Combating Money Laundering* that established the RF Financial Monitoring Committee (FMC of Russia). This document defined the status of the Committee and set its primary objectives.

The Russian Federation Government was tasked with approving the statute on the FMC of Russia, and securing its funding, extending to the creation of a unified information system and maintaining a federal AML database, as well as providing premises for the headquarters and regional offices.

The Bank of Russia was recommended to adopt regulations prescribing a procedure for complying with this Federal Law on the part of credit institutions, to coordinate a procedure for submitting information and documentation by the Bank of Russia to the Russian FMC, as well as assist the FMC in establishing a unified information system and maintaining a unified federal AML database.

**FS:** *How exactly was the agency formed? Could you recall how you selected the building, settled in the premises, purchased equipment?*

**V.Z.:** In November 2001 I was appointed acting head of the Financial Monitoring Committee in the rank of the First Deputy Minister of Finance. Within a short term (just over two months) we had to solve organizational and infrastructural issues: accommodation, equipment and most importantly staff recruitment.

While choosing the building for the Committee we had several criteria: convenient location, basic communications and employees' comfort. The group of buildings designed by architect Le Corbusier met all our requirements. In addition to accommodating the vanguard of financial intelligence and equipment, it allowed us to build up human and technical resources for years to come.

Timely funding allowed the Committee to purchase and configure the most up-to-date equipment and software in due time. In just couple of years' time we outmatched European FIUs in this respect, and approached the level of the US financial intelligence.

The most vital, especially at the very start, was of course the human resource issue. There were virtually no specialists in Russia with a record in financial intelligence, and our knowledge of foreign experience was insufficient. The FMC invited officers from law enforcement and supervision, special services, as well as lawyers, economists, foreign relations specialists, bankers and programmers. I should point out that quite a few of our first *crewmen* are still working in the Russian financial intelligence unit.

By February 1, 2002 we had built the entire legal and organizational framework required for the launch of the national AML regime. The country's government, the Bank of Russia and the Russian FMC provided for the adoption and implementation of a number of regulations, as well as formed the staff, ensured the accommodation and equipment for the primary departments of the Russian FMC and set up secure



networks of communications. In a nutshell, within the shortest time we provided for the compliance of the Russian AML system with the current international standards, alongside creating potential for further development.

Speedy and efficient achievement of the goals set by the Russian President was made possible thanks to a close cooperation between the FMC of Russia and the Central Bank. For example, due to the fact that the main informers of the FMC of Russia are credit institutions, they could use the secure network of the Bank of Russia to submit their reports to the FMC of Russia. This move allowed us to save up on time and money that would be required for setting up stand-alone channels. It is noteworthy that the coding system introduced by the FMC of Russia for reporting entities is a reliable barrier against third-party disclosure.

**FS: How the AML/CFT mechanism was created?**

**V.Z.:** By the beginning of 2002 Russia had built the main elements of the legal and institutional AML framework. However, they could be set in motion only as a system.

Combating legalization of illegal proceeds cannot be performed by a single agency, no matter how wide is its scope of authority. This work presumes highly coordinated efforts of the legislative, executive and judicial branches of power, alongside educational and research institutions, reporting entities and public associations.

The FMC of Russia (later Rosfinmonitoring) is the key element of our AML system by definition. However, a significant role in combating money laundering started playing interior affairs agencies, prosecution authorities, special services, credit and finance organizations, legal entities and individuals that were required by law to submit certain data.

In the first three years, AML/CFT coordination was performed mainly on a bilateral basis, until the creation of an Interagency AML/CFT Commission that embraced 14 ministries and agencies in October 2005. This Commission developed a plan of measures aimed at the implementation of the National AML/CFT Concept that was later presented to the Government of the Russian Federation and the head of state.

**FS: How did Russia manage to leave the FATF black list and become a member of this organization a year later?**

**V.Z.:** In September 2002 as part of the procedures aimed at reviewing the status of the *black* list countries Russia was visited by the FATF experts. It studied the Russian AML/CFT legislation as well as the practical work of the Russian FMC, the Ministry of Internal Affairs of Russia, the Bank of Russia and other law enforcement and supervisory authorities, alongside credit, insurance and other financial institutions responsible for its implementation. In addition to Moscow the FATF experts traveled through a number of Russian regions, including Saint-Petersburg and Tula, where they reviewed the work of regional offices of the federal law enforcement authorities and the Bank of Russia as well as the internal compliance routines in local financial institutions.

This mission led to the decision on the exclusion of Russia from the FATF *black* list adopted by the FATF Plenary Meeting in Paris (October 2002).

The FATF experts were impressed both by the actual progress in building the national AML regime achieved within limited time and the will to continue this work demonstrated by the authorities and businesses of all levels. The practically unanimous vote of the State Duma in favor of the two Federal Laws submitted by the President of the Russian President and aimed at the further enhancement of the legal foundation of this system, which was carried out on the last day of the FATF experts' visit to our country (27 September, 2002), may serve as an example of this readiness.

In February 2003 Russia took part in the Plenary Meeting of the FATF as an observer and at the Plenary Meeting in June 2003 in Berlin Russia became a full member of the FATF. This decision was preceded by another comprehensive assessment of our national AML/CFT system that was conducted by the FATF experts in April 2003. This assessment was based

on the new methodology and confirmed the overall compliance of the Russian AML/CFT regime with the FATF Recommendations.

I would like to emphasize that this qualitative leap in establishing the national AML/CFT regime was made possible thanks to the well-coordinated and hard work of the Russian financial intelligence staff as well as the understanding of our partners in particular in the legislative branch.

**FS:** *In the 2000's Rosfinmonitoring actively participated internationally. What were the key achievements in this sphere?*

**V.Z.:** In June 2002 the FMC of Russia passed the due procedure to become the official member of financial intelligence units — the Egmont Group. Joining the Egmont Group confirmed the compliance of the FMC with the generally accepted definition of FIU, including the powers required to receive, process and disseminate information, as well as full operative status, legal capacity and readiness for collaboration with other countries' FIUs.

While preserving its membership in the European FATF-Style Regional Body — the MONEYVAL Committee of the Council of Europe — following its accession to the FATF, Russia stepped forward with

the initiative to create an analogous structure in the Eurasian region, with the intention to spread the relevant international standards primarily in the Central Asian countries. At the initial foundation conference that took place in Moscow in October 2004 the declaration on the establishment of the Eurasian group on combating money laundering and financing of terrorism (EAG) was signed by Belarus, Kazakhstan, Kyrgyzstan, China, Russia, and Tajikistan. At the third Plenary Meeting of the EAG that was held in Moscow in December 2005 Uzbekistan joined this organization and became the member state of the Group.

The overall size of the EAG territory is the largest among the current FATF-Style Regional Bodies. With the assistance of international organization and observer states, including the FATF, IMF, World Bank, UNODC, Interpol, IPA CIS, EurAsEC, CSTO, alongside Germany, Italy, France, Japan, Ukraine, Moldova, Turkey, etc., the EAG undertakes intensive efforts to assist its member states to establish AML/CFT regimes in line with the FATF requirements. Even prior to the creation of the EAG Rosfinmonitoring supported the FIUs of the region in their preparation to joining the Egmont Group, acting as their sponsor in compliance with the mandate of this international group; in 2003–2004 Rosfinmonitoring helped the FIUs of Serbia, Georgia and Ukraine join the Egmont Group.

**INFORMATION ABOUT  
FEDERAL LEVEL EVENTS**

## ***RUSSIAN PRESIDENT V. V. PUTIN HELD A WORKING MEETING WITH DIRECTOR OF FEDERAL SERVICE FOR FINANCIAL MONITORING YU. A. CHIKHANCHIN***

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*The Director of Rosfinmonitoring briefed the President  
on the Service's current activities*

*V. PUTIN: Mr. Chikhanchin, since the mega-regulator was set up within the Central Bank system, the preliminary analysis of received information indicates that overall financial discipline is improving in the relevant organizations. How do you see the situation? You are in constant contact with the Central Bank and other financial institutions, so what is your view of things?*

*YU. CHIKHANCHIN: Mr. President, first of all I would like to say that with the enactment of the law on the mega-regulator and the law on combating illicit financial transactions the situation on the financial market has improved considerably. Acting in close cooperation with the other supervisory and law enforcement agencies we have of late succeeded in shutting down several shadow markets that were involved in money laundering and capital flight, including for dubious deals and transactions and we have also improved the state of affairs in the sense that we now have the chance to work as a mega-regulator not only with the banks but also with*

other sectors, such as the securities market and the insurance sector.

At the moment, we are working together to find solutions that will help us to identify risks in financial sectors and take preventive measures to make sure that these risks do not become reality. As an example of this work the Central Bank has revoked the licences of several banks that were violating the laws.

I can say that the demand for money is slightly lower at the moment. Most important is that this enables us to address the tasks that are put in your tasks. On the subject of your order concerning the Far East, in particular the issue of lowering the air fares, we have studied several airports' activity. These airports are in private hands, but we think there is insufficient control over spending there, with the result that the owners abuse the system by transferring part of the funds they receive as interest-free loans to their affiliated companies and transfer money to their companies' employees. This inevitably raises the cost of air tickets. Today we



are working with the law enforcement agencies by taking measures to improve this situation.

The mega-regulator's establishment and the law on combating illicit financial transactions are also very important in that they enable Russia to fulfil an important international obligation, namely, reporting to the FATF. We have essentially joined the elite club of countries that completely meet all international anti-money laundering standards. I think this is a big achievement. Above all, I would like to thank you, because you furthered this law. In fact we have launched two very good mechanisms now that we, the mega-regulator and all the financial institutions use. The first of these is to examine who is the ultimate beneficiary. This was an initiative that Russia had put forward at the G8 and G20 too. We think it will be an effective mechanism.

The second is that we have given financial organizations the chance to suspend dubious operations, not to conduct them and to reject them. This also helps to improve the system and gives

us the chance to maintain our platform, especially during the Russian Presidency [of the FATF].

Now we are working on resolving a number of other issues through this international platform. This year we are handing over the presidency of the Eurasian group, a FATF-style regional body. The Eurasian Group was established on our initiative and brings together the Central Asian countries: China and India. We have succeeded in establishing anti-money-laundering mechanisms in the Central Asian countries, set up Financial Intelligence Units and make sure that none of these countries ends up on the black lists. We consider it as a big step forward.

Also acting on the decision you took together with all of the CIS presidents, an agreement to establish the Council of Heads of Financial Intelligence was signed. One of the primary tasks will be to ensure financial institutions' transparency.

***kremlin.ru***

## ***DIRECTOR OF ROSFINMONITORING ATTENDED A MEETING OF THE PRESIDENTIAL COUNCIL FOR COUNTERING CORRUPTION***

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*The President of the Russian Federation Vladimir Putin chaired a meeting in the Kremlin dedicated to the implementation of the state anti-corruption policy and assessment of the impact of recently-adopted legislative and administrative measures. The meeting was attended by director of the Federal Financial Monitoring Service Yury A. Chikhanchin*

*Irina V. Ivanova,  
Editor in Chief*

*V. PUTIN: "The state's anti-corruption policy must be based on the principle of inevitability of punishment for offenses. Across the entire battlefield against corruption, authorities must act consistently and offensively."*

*The President stressed the paramount importance of the task of raising the level of citizens' legal awareness:*

*"Anti-corruption standards of behavior based on the knowledge of fundamental rights and obligations should become the norm for all. Society and the business community rightly expect a strict observance of these rules from authorities. However, it should be noted that they themselves sometimes play the role of bystanders, acting at times to encourage state corruption as a means of furthering their business interests."*

During his speech, the Rosfinmonitoring director expressed full support on behalf of the agency for both the assessment made of the current situation and proposals for improving anti-corruption mechanisms.

### **Abstract of the speech by Rosfinmonitoring director Yury A. Chikhanchin**

One of the most popular corruption mechanisms involves the use of financial institutions (banks, insurance companies, the securities market, etc.), some of which may either offer passive assistance to or, conversely, actively engage in their corruption schemes individuals prone to crimes, including corruption-related crimes.

The work of law enforcement and oversight agencies within the Interagency Working Group on Combating Illegal Financial Transactions, established by a decree of the President of the Russian Federation and whose meetings are held 3-4 times a month, has helped identify and suppress several illicit marketplaces, including in Dagestan, Samara and Moscow. These marketplaces specialize in cash-out transactions, funneling funds abroad - including for criminal purposes - and money laundering, with the total amount of funds channeled through them estimated at hundreds of billions of rubles. An analysis of the factors behind the current situation conducted by the IWG showed that the existence of this phenomenon is linked, among others, to illegal activities of persons charged with overseeing the activities of financial institutions.

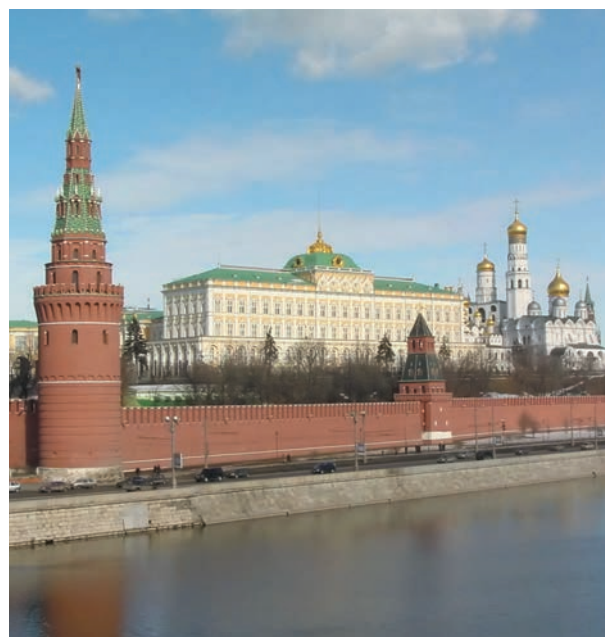
It should be noted that the initiation of criminal proceedings, revocation of several banks' licenses and dismissal of top managers in a number of credit institutions have all helped to somewhat improve the situation in this area across the country. Still, from Rosfinmonitoring's perspective we observe that the "grey" sector of the economy still survives and continues to look for new forms and methods of existence by exploiting loopholes in legislation.

For this reason, it makes sense to draft measures that will be aimed not only at the ongoing identification of illicit marketplaces, but also at the establishment of economic mechanisms that render such marketplaces ineffective for criminals.

One of such measure is that we can limit the number of cash transactions exceeding a predefined threshold amount (100,000 rubles), especially between legal entities and between legal entities and individuals.

A similar threshold can be applied to the cross-border movement of cash (not more than 15,000 Euros).

Another area of vulnerability that is often exploited by corrupt individuals is the insufficient level of control over budgetary funds. Work in this area is being carried out as part of measures aimed at fulfilling the orders of the president and the government of the Russian Federation. It is dedicated to analyzing the income declarations of employees of state-owned companies and contracts concluded by them with the goal of identifying possible conflicts of interest. The main reason for such conflicts is the conclusion by state-owned entities of contracts with companies founded by state officials or their family members. A total of 150 officials have so far been dismissed in



connection with this, while criminal proceedings have been initiated against many others.

In this regard, we consider it expedient to continue to work with the relevant ministries and agencies on the fulfillment of your decree regarding the monitoring of expenditures of companies with state participation.

Following a review of 2013 income declarations and contacts, it will be necessary to summarize its findings and draft proposals for changes to be made to the relevant regulations aimed at combating corruption in state-run companies and to the use of budgetary funds in general.

**It is the opinion of Rosfinmonitoring that this work should be continued and extended to cover all sectors of the economy prone to corruption and other risks, especially regarding the military-industrial complex, fuel and energy sector, timber processing industry and housing and public utilities sector, all of which share common illicit characteristics.**

1. Being customers of financial institutions that simultaneously act as illicit marketplaces.
2. Frequent use of shell companies in transactions. Just in the housing and public utilities sector alone, competent authorities identified in 2013 some 800 organizations that used about 1,000 fictitious contractors, transferring to themselves a total of approximately 12 billion rubles.

3. Transferring funds to companies affiliated with the organization's management. Only financial investigations conducted by housing sector authorities have revealed transactions of this type in the total amount of approximately 8.6 billion rubles.
4. Depositing funds, included budgetary funds, owed to suppliers in a bank for a long period to earn interest. In the fuel and energy sector, this amounted to over 200 billion rubles in the first half of this year.
5. Issuance of interest-free loans (about 2 billion rubles in the fuel and energy sector).

**Also, we believe it is necessary:**

- to clearly define the type of financial institutions high-risk industries should be allowed to work with. There are many trustworthy credit and non-credit institutions in the country to allow us to avoid infringing on anyone's interests;
- to take all necessary steps to ensure the enforcement of requirements of Federal Law № 134-FZ concerning the identification of partner and counterparty organizations' beneficiaries, as well as for banks to refuse to carry out suspicious transactions, which will make it possible to minimize the involvement of shell companies in transactions and address the problem of affiliation;

- to launch a mechanism prohibiting long-term deposits and issuance of interest-free loans.

I would like to mention one more problem. Both Rosfinmonitoring and law enforcement agencies have found ways to trace assets, including foreign-based assets, belonging to corrupt officials. The only problem is that there are no legal mechanisms for returning these funds to the rightful owners, including to the state budget. Once again we should try to go into this problem use the concept of forfeiture, as required by international standards and current situation.

In conclusion, I would like to inform you about the meetings that are held under the auspicious of presidential envoys in federal districts and dedicated to the implementation of Federal Law № 134 (on combating illegal financial transactions) by the relevant ministries and agencies and the private sector. During these discussions, the majority of participants and presidential envoys proposed to establish in the country's districts working groups similar to the IWG, which was set up in accordance with your instruction and is led by Yevgeny M. Shkolov.

These groups will be able to identify corruption risks related to the use of financial institutions and illicit schemes at an early stage and to take prompt action without having to wait to be summoned to the IWG meeting in Moscow.

The Central Bank's recently increased responsibilities as a Mega-Regulator will only contribute to this.

## NEW LAW SETS TARGETS FOR FUTURE

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*Meetings on implementation and enforcement of the provisions of Federal Law No.134-FZ on Amendments to Certain Legislative Acts of the Russian Federation Pertaining to Combating Illicit Financial Transactions were held in the Federal Districts*

*Irina V. Ivanova,*  
*Editor in Chief*

At the FATF (Financial Action Task Force) Plenary Meeting held in October, the Russian Federation successfully presented its next follow-up report on improvement of the national AML/CFT system which was unanimously adopted by all FATF members. Following the adoption of the report, our country was removed from the FATF regular follow-up process, which required submission of follow-up updates on annual basis and was placed in the reduced biennial follow-up. Thus, the Russian AML/CFT system was officially recognized as one of the most mature in the world.

Significant progress made by the Russian Federation in the international fora resulted from our collaborative efforts and effective work. Success

of the Russian Federation was, to a large extent, achieved due to adoption of Federal Law No.134-FZ. Practical implementation and enforcement of the new legislative provisions was discussed by the officials of the federal executive authorities with the representatives of the government authorities of the Federal Districts at the special meetings.

**Pavel Livadny, Rosfinmonitoring State Secretary and Deputy Director**, elaborated in his speech on the specificities of Federal Law No.134-FZ on Amendments to Certain Legislative Acts of the Russian Federation Pertaining to Combating Illicit Financial Transactions adopted on June 28, 2013.

**Pavel Livadny, Rosfinmonitoring State Secretary and Deputy Director:**

*Establishing the mechanisms for implementing and enforcing Federal Law No.134-FZ, which vested ample powers in each and all government authorities, including both supervisory and law enforcement agencies, involved in these efforts*

*is the issue of paramount importance which has to be addressed by us as quickly as possible. It should also be noted that the current remarkably favorable international environment gives us the opportunity to strike a telling blow against economic crime. Next year the Russian Federation will take the chairmanship in the G8. It is noteworthy that the most important and actively discussed issue in the current year agenda of the Group of Eight is the enhancement of transparency of the global economy.*

**Pavel Livadny** reminded that the Law was adopted as a result of the coordinated efforts undertaken by all government agencies and authorities under the auspices of the RF Presidential Executive Office. The Law can be implemented only through the streamlined efforts of all government authorities in charge of its enforcement in close

coordination with the activities of the private sector aimed at improvement of the Russian economy competitiveness.

**Galina Bobrysheva, Rosfinmonitoring Deputy Director**, reminded in her speech addressed to the representatives of the supervisory authorities about the main risks posed to the financial sector:

*This Law brings the Russian AML system at a new level. Primarily, it applies to compliance with the international standards. On the other hand, the Law identifies the specific mechanisms for mitigating the risks of illicit financial transactions in general and the ML/FT risks in particular. The outcome of the general assessment of the Russian anti-money laundering system and the risks of inclusion of our country in the so-called "black" and "grey" lists will depend on the effectiveness and efficiency of the efforts undertaken by the State in this area.*

### *Vladimir Bulavin, the Presidential Envoy in the Northwestern Federal District:*

"Laundering of illicit proceeds of organized crime, financing of terrorism, high level of corruption and general lack of transparency of the economy remain the major challenges of the national security of our country. In compliance with the RF legislation Rosfinmonitoring acts as the center for assessing the national security

threats related to money laundering and terrorist financing and for developing measures to counter these threats. President V.V. Putin has articulated the objectives targeted at combating illicit financial transactions. Adoption of the Federal Law No.134-FZ is the important milestone on this way."



### *Alexander Khloponin, Deputy Chairman of the RF Government, the Presidential Envoy in the North Caucasian Federal District:*

"In 2012, the FATF, being one of the organizations representing the global anti-money laundering community, adopted the fundamentally new standards intended for combating money laundering and terrorist financing. The essence of these changes was the development of new risk assessment standards and the formulation of the risk mitigation policy.

The banking sector, being the blood system of the Russian economy, is still exposed to the highest risk of illicit activities and large volume of shady transactions is still carried out through this sector. The adopted Law embodies all best initiatives, including international standards, international best practices as well as enforcement practices of Rosfinmonitoring and other agencies."

The attendees to the meetings repeatedly emphasized the need for joining the efforts in order to achieve the best possible results: the new Law significantly extended the powers granted to the government authorities and agencies engaged in combating illicit financial transactions. In this context, the interagency coordination and cooperation among the law enforcement agencies, the tax and supervisory authorities and Rosfinmonitoring are evermore crucial. For effective combating the economic crime the joint efforts should be aimed at and attention should be focused on confiscation of assets that are obtained in a criminal manner and "circulate" in the shadow economy. One of the examples of such cooperative arrangement is the working group established by the executive order of the RF President in last July. One of the results of the efforts undertaken by this working group chaired by Evgeny Shkolov, the Aide to the RF President, was adoption of Law No.134-FZ.

#### **Pavel Livadny, Rosfinmonitoring State Secretary and Deputy Director:**

*The information resources of various agencies should be integrated. Currently, they are disintegrated to such extent that when different agencies investigate the activities of the same person they are not aware of this and think that deal with different suspects. At present, I am not referring to establishing a common database or to the use of a common platform or operator. As the initial step, the public (unclassified) information resources of different agencies may be integrated and such work is already underway under the auspices of the working group chaired by Evgeny Shklovsky. For example, the process of integration*

*of information resources of some government agencies such as the Federal Tax Service, the Federal Migration Service, Rosfinmonitoring and the Interior Ministry is currently underway. In my opinion, if such mechanism is launched at the federal level it will be further adopted in the Federal Districts and constituent regions of the Russian Federation. At present, it is impossible to implement Federal Law No.134-FZ and ensure efficient law enforcement operations without integration of information resources.*

The final event was the meeting held in St. Petersburg. This meeting was chaired by Yury Chikhanchin, Rosfinmonitoring Director, who reminded that implementation and enforcement of the provisions of Federal Law No.134-FZ is personally monitored by the Russian Federation President.

#### **Yury Chikhanchin, Director of Rosfinmonitoring:**

*Adoption of Federal Law No.134-FZ is one of the outcomes of the comprehensive cooperative efforts undertaken by the interagency working group headed by Evgeny Shklovsky, the Aide to the RF President, and the interagency committee established under Rosfinmonitoring. This Law has actually opened a new page in ensuring security of the national financial system by introducing strict and progressive regulations for enhancing financial transparency and for optimizing the financial entities monitoring tools and mechanisms that meet the highest international standards. But we should not rest on our laurels! The work aimed at further enhancement of economic security should be focused on improvement of the AML system effectiveness and on increasing efficiency of all AML stakeholders, including Rosfinmonitoring, the Central Bank, law enforcement agencies, tax and*



*supervisory authorities, private sector, mass media and the public.*

The FIU Director highlighted the key objectives to be achieved by all national agencies engaged in the AML activities:

- Implementing and enforcing Federal Law No.134-FZ by adopting, as soon as possible, the relevant regulations.
- Establishing the comprehensive proactive multi-level system of monitoring the domestic AML/CFT risks for implementing preventive measures and ensuring recovery of the Russian economy.
- Establishing the inter-agency working groups in the Federal Districts for combating illicit financial transactions with the goal of further enhancement of interagency cooperation and improvement of efficiency of the AML/CFT efforts as

well as for detecting and deterring illicit financing transactions and solving the emerging problems in the Federal Districts in a prompt manner.

Following the meetings, it was decided to implement a number of joint initiatives involving arrangements for conducting assessments of the regional risks and the national security threats posed by money laundering, terrorism financing and illicit financial transactions in the Federal Districts.

In particular, these efforts will be targeted at ensuring compliance by the entities engaged in transactions with funds or other assets and by individual entrepreneurs with the requirements of the federal legislation pertaining to identification of beneficial owners and obtaining information on purposes and intended nature of business relationships with corporate customers. The regular outreach will be conducted for clarifying the provisions of the federal legislation to the institutions engaged in transactions with funds or other assets and to individual entrepreneurs.

*I.V. Yasinsky, Deputy Director of Financial Monitoring and Currency Control  
Department of the Bank of Russia:*

"Today we see that the entire system established since 2001 responds in a reactive manner to all cases of misuse of the financial system for money laundering and terrorist financing purposes. We know that financial institutions, primarily credit institutions, file large number of reports with the financial intelligence unit. Rosfinmonitoring, in its turn, disseminates the processed and analyzed materials to the law enforcement agencies. However, when the law enforcement agencies contact certain individuals who formally hold the senior management positions in the entities that have transferred funds abroad or withdrew cash, or in course of interrogation of the founders of such entities they found out that these individuals have actually nothing to do with the entities under consideration.

It happens, first of all, due to the fact that shady transactions are typically carried out by the so-called "shell" companies. In past, such companies were incorporated with the use of forged documents and lost passport forms. This did not allow us to identify the actual beneficiaries of these shady transactions. In recent years, the situation became even worse since such companies were established with the use of valid documents: for a small remuneration asocial individuals provide their passport details, sign many documents but in reality have nothing to do with the actual operations of particular legal entity.

As a result, we responded to such situations in a reactive manner: we detected offences but could not identify the persons who were actually guilty of perpetrating them. Therefore, the main objective faced by the financial intelligence

unit and the Bank of Russia was to increase efficiency of the anti-money laundering efforts. In such situation, financial institutions needed tools that would allow them to response to negative situations in a proactive and not reactive manner.

Currently, we firmly adhere to three fundamental principles:

1. We de facto recognize that a bank account agreement has lost its public status, although it is still formally considered the public agreement under the Civil Code. What does loss of public status mean? It means that a credit institution may refuse to establish business relationships with a customer if it just suspects that the customer will conduct transactions for money laundering, terrorist financing and/or tax evasion purposes.
2. The second fundamental standpoint concerns not just banks but all financial institutions covered by Federal Law No.115-FZ. Currently, if a financial institution just has suspicions it may refuse to perform a transaction if such transaction meets certain criteria.
3. Thirdly, it is the right to unilaterally terminate a bank account agreement without taking any legal action.

In the opinion of the supervisory authority, which is fully supported by Rosfinmonitoring, proper implementation of new powers will drastically improve the efficiency of the Russian AML/CFT system".

# ASSESSMENT OF THREATS AND RISKS: ON THE WAY TOWARDS FINDING SOLUTIONS TO STRATEGIC OBJECTIVES

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**Andrew N. Frolov,**

*Deputy chair of the macroanalysis*

*and typology department of Rosfinmonitoring*

In June 2012, in conformity with the Presidential Decree No. 808, the Rosfinmonitoring became directly subordinate to the President of the Russian Federation. Among the new functions delegated to the country's Financial Intelligence Agency as a result of subordination was that of the national center for the assessment of risks and threats to national security arising from money laundering, financing of terrorism and proliferation of weapons of mass destruction.

## Our strategic goals

- Improve the effectiveness of the Russian anti-money laundering and terrorist financing system.

The implementation of the strategic objective assigned to the Federal Financial Monitoring Service is designed to contribute to greater transparency, reliability and security of the country's financial system and its financial institutions.

- Build a comprehensive system of international counter-efforts.

The use by criminals of increasingly sophisticated methods and technologies calls for a continuous improvement of countermeasures against money laundering and terrorist financing.

One of the most important areas of international cooperation in this field involves the building of a comprehensive system of countermeasures against money laundering and terrorist financing based on common international standards.

In line with the FATF standards and commitments made at the G8 leaders summit, Russia is pursuing reforms aimed at ensuring transparency in the beneficial ownership of companies, other legal entities and arrangements and at preventing tax evasion, including through offshore jurisdictions. With the goal of preventing and detecting instances of illegal use of companies, other legal entities and arrangements, Russia has significantly tightened its national legislation by introducing additional oversight measures, including Federal Law No. 134-FZ «On amendments to certain legislative acts of the Russian Federation with regard to the fight against illegal financial transactions», which provides for the implementation of the following measures:

- Adoption of the Governmental Act that introduces additional requirements for VAT reporting.



- Adopt the Governmental Act that establishes the procedure for the formation and maintenance of a public registry of individuals barred from establishing and running legal entities for economic crimes they committed.
- Adopt the Governmental Act that raises the suitability and integrity criteria for financial institution employees.
- Enact a legal instrument that strengthens federal state control (supervision) over countering the legalization of proceeds from crime and terrorist financing.
- Draft the Governmental Acts that improve the measures for freezing the property of persons involved in terrorism.
- With the goal of identifying the ultimate beneficial owners, amend the Governmental Acts governing the requirements for the internal control rules drafted by financial institutions engaged in transactions with funds or other assets to ensure mandatory identification of the entire chain of beneficial owners of legal entities, as well as to strengthen customer due diligence measures.
- Raise the level of law enforcement by lawyers, notaries and persons engaged in business activities in the sphere of legal and accounting services.
- Improve cooperation between the FIU, government agencies and financial institutions in the sharing of information on beneficial ownership.

One of the important points of this plan was the commitment of the Russian Federation, made in 2014, to conduct a national assessment of the risks associated with money laundering, terrorist financing and proliferation of weapons of mass destruction and to publish its results.

In 2013 Rosfinmonitoring carried out a large volume of work aimed at the establishment of a national center for the assessment of risks and threats to national security (hereinafter the «Center») arising from money laundering, financing of terrorist and proliferation of weapons of mass destruction (ML/FT/FPWMD), and preparation of a report to the President of the Russian Federation.

The CRA was established to monitor the situation, ensure rapid respond to and localization of risks of money laundering and terrorist financing (risk management) and carry out an assessment of the measures taken. The Center's target audience comprises:

- President and the Government of the Russian Federation
- Interagency coordination bodies (National Security Council of the RF, IWG, etc.)
- Federal agencies of executive power and law enforcement



- Regional leaders and plenipotentiary representative of the President of RF in the federal districts
- Directorates of Rosfinmonitoring's central apparatus
- Rosfinmonitoring's territorial authorities

Pursuant to Rosfinmonitoring Decree No. 117 dated May 16, 2013, the Russian Financial Intelligence Agency has created a Working Group on National Threat Assessment, approved its staff composition and the regulation on the working group

as well as choosing the location for the future Center. The Agency has also conducted all necessary technical, information and engineering work needed for the proper functioning of the Centre.

Last October, the Federal Financial Monitoring Service launched the first stages of the Centre's operating cycle, including information and analytical resources of the tactical (operational) and strategic levels, and assessed the need for additional information resources, including external. The first results of the Centre's work in the form of analytic calculations are currently being used in the preparation of a report to the President of the Russian Federation.

**RUSSIA IN THE INTERNATIONAL  
AML/CFT SYSTEM**

## **RUSSIA PRESENTED 6<sup>th</sup> FOLLOW-UP REPORT AT THE FATF PLENARY MEETING**

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*On October 16, 2013 the Russian Federation succeeded in presenting its regular progress report on improving the national system of combating money laundering and terrorism financing at the FATF (Financial Action Task Force) Plenary Meeting with the unanimous support of all member states. The Russian interdepartmental delegation in Paris was headed by Yu. A. Chikhanchin, Rosfinmonitoring Director*

*Irina V. Ivanova,  
Editor in Chief*

The report allowed the Russian Federation to switch from the FATF standard monitoring process with annual reporting to a softer regime when progress reports are submitted every two years. Thus, the Russian AML/CFT system would be formally recognized as one of the most developed in the world while major FATF member states, including for instance the U.S. and Australia, have standard monitoring. As for Japan,

it has enhanced monitoring (which requires on-site control missions).

This report was of special significance. The successful presentation of this document means an automatic integration of the Russian Federation in the elite club of countries whose anti-money laundering systems comply with international standards to the maximum extent. As the FATF experts acknowledged, Russia has not only reached the top but also established itself as a leader. First of all, its success is due to the more efficient system

of detecting beneficiaries of legal entities. Secondly, the country has decent regulation with respect to the freezing of terrorist assets. So, Russia has implemented requirements announced at the summits of G8 in Lough Erne and G20 in Saint-Petersburg.

The report required 5-year work on the part of Rosfinmonitoring and experts of the Administration

of the President of the Russian Federation, Russian Government, Bank of Russia, Ministry of the Interior, Federal Security Service, Ministry of Justice, Federal Customs Service, Federal Tax Service, Federal Drug Control Service, Office of the Prosecutor General of the RF, Investigation Committee, as well as deputies of the RF State Duma.

### *P. V. Livadny, State Secretary, Deputy Director of Rosfinmonitoring:*



"Federal Law No 134-FZ dated June 28, 2013 "On Amending Certain Legal Acts of the Russian Federation in Part of Combating Illicit Financial Transactions" turned a new leaf in ensuring the safety of the domestic financial

system by establishing strict, modern regulations of transparency and optimization of controls of different entities in full compliance with international standards. The law defined a proper legal mechanism for combating unlawful financial acts. Our results (I would like to remind you that the FATF whose mandate is determined by the UN Security Council, G8 and G20, sets financial security trends) were

achieved by joint work of almost all government executive and legislative agencies and in fact of the whole Russian society: both financial experts and concerned citizens who discussed the draft which became law 134-FZ later on. The work of the Group of Countering Illicit Financial Operations created by the President of the Russian Federation and Rosfinmonitoring Interdepartmental Committee was of special importance.

Our next task is to ensure the law implementation. It is important for the good functioning of the Russian economic system as well as for its further monitoring by the FATF. This organization underscores the operational efficiency control of the laws adopted in each country because the lack of law enforcement practice discounts even the most advanced and sustainable regulation."

As A. G. Petrenko, a member of the Russian delegation (Rosfinmonitoring), stated that Russia showed high political will in upgrading the national anti-money laundering system. In his closing remarks he thanked the FATF members for their support:

*"We will continue to improve our system of combating money laundering and terrorist*

*financing, especially prior to the next round of mutual evaluations."*

The solution of such a challenging task in the year of the Russian Presidency in the Financial Action Task Force on Money Laundering (the Russian citizen V. P. Nechaev became the FATF President in June 2013) is indicative of the significant strengthening of Russian positions in the international stage.

## ***RUSSIA – USA: ENHANCED COOPERATION***

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*On November 12-14, 2013 Miami (U.S.) hosted the ninth session of the Drug Trafficking Working Group created within the Russia-US Bilateral Presidential Commission*

The co-chairmen of the Working group: from the Russian side — Viktor Ivanov, Chairman of the State Anti-Drug Committee, Director of the Federal Drug Control Service; from the American side — Gil Kerlikowske, Director of the White House Office of National Drug Control Policy. Rosfinmonitoring was represented by Yu. F. Korotkiy, First Deputy-Director.

The Working Group was created in July 2009. Its activity concerns a wide range of issues related to the fight against illicit drug trafficking, drug prevention, treatment and rehabilitation of drug users.

In the Plenary Meeting of the Drug Trafficking Working Group of the Russia-US bilateral Presidential commission participated representatives of the Russian Federal Drug Control Service, Ministry of Public Health of the Russian Federation, Ministry of Foreign Affairs of the Russian Federation, Rosfinmonitoring as well as White House Office of National Drug Control

Policy, U.S. National Security Council, U.S. Anti-Drug Agency, U.S. State Department, U.S. Department of Treasury, U.S. Health Department, U.S. Customs and Border Service, U.S. Immigration and Customs Enforcement.

The participants of the meeting discussed issues of countering global drug threat, drug demand reduction, anti-money laundering and anti-drug policy of both countries. They were also submitted reports on the Working Group main activities. The parties stressed the necessity to further enhance cooperation of two countries in their fight against illicit drug trafficking as well as in prevention and treatment of drug addiction.

The host party represented Russian colleagues the special equipment and weapon that are in service of national units to combat drug trafficking.

Moreover, the Russian delegation was shown the work of the rehabilitation center "The Village South", focusing on drug addiction and further rehabilitation of drug users.

## ***DRUG LEGALIZATION AS A LATENT THREAT TO THE GLOBAL AML/CFT SYSTEM***

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*Konstantin G. Sorokin,*  
columnist, PhD

Nowadays, the processes of globalization are casting doubts on seemingly unassailable facts. Herculean efforts exerted by the likes of Russia and several of its allies exemplify attempts by some countries to preserve the world envisaged by the founders of the United Nations: stable and secure, where the rights of man and citizen are guaranteed. One important instrument of stability and security in the world are the United Nations Conventions, implemented by countries with due account for the specifics of their domestic legal systems. These conventions declare the common principles of security and set standards for all countries in the world.

Prohibition of drugs (except for a limited number of cases where their use is related to medical conditions) was until recently regarded as one of the key pillars of global anti-drug policy. Among the most noticeable UN documents governing, among others, the global AML/CFT system is the UN Convention against Illicit Traffic in Narcotic

Drugs and Psychotropic Substances (Vienna Convention, 1988). In particular, the Convention states: "Eradication of illicit traffic is a collective responsibility of all countries... to that end, co-ordinated action within the framework of international co-operation is necessary..."

At the same time, there are countries which are trying to raise the issue of drug legalization and change the meaning of the term «illegal trafficking», with some going even further by suggesting that they themselves should be directly involved in the production and distribution (including export) of narcotic drugs and use the derived revenue to meet their own budgetary needs. In reality, what we are observing here is the beginning of a new trend which is yet to be fully understood by many governments.

Several Latin American nations that are currently battling one of the manifestations of the drug threat, represented by armed rebel and criminal armies funded through drug production, actively promote the idea of state-controlled cultivation and sale of narcotic drugs. The goal of such policy is two-pronged. First, it is to preserve the safety and statehood of such countries, and second, to redistribute the funds and deprive criminal groups of their funding sources. The global policy in favor of legalization is spearheaded by Uruguay, where in the summer of 2013, the lower house of



parliament passed a law allowing all adult residents of the country to legally purchase, sell and store marijuana and its derivatives<sup>1</sup>. The argument used by proponents of the law is that all traditional methods of fighting the spread of drugs have failed due to their ineffectiveness and that it is time now to try new approaches.

Similar problems, where in entire territories find themselves beyond government control and are de facto controlled by drug cartels, exist in Southeast Asia and Afghanistan. The inability of these countries' governments to restore control over these territories forces them to consider, among others, the possibility (currently still as a future option) of utilizing drug revenues for budgetary needs.

A typical scenario of legalization looks as follows. As part of the first phase, drugs are made available only to the local population. Then, legalized distribution is extended to cover foreign nationals in the country of manufacture (especially tourists). Finally, the government begins to offer cross-border deliveries and encourage large-scale export (drug intervention<sup>2</sup>) to neighboring countries, while working on expanding the supply logistics. Such deliveries may, among others, become a tool for addressing various differences that may exist between the countries.

This kind of situation will sooner or later lead to serious inconsistencies and attempts to disrupt the status quo, resulting in a situation where a number of countries will pull out of international treaties and agreements covering the illicit traffic in narcotic drugs due to the fact that they will legalize drugs in their borders and drug export will become an instrument of their fiscal policy. In such a scenario,

the financing of drug trafficking may no longer be considered as a crime, entailing a revision of the existing bases of the global AML/CFT system. Some experts leave open the possibility of establishment of cartels with government participation on the basis of sub-regional economic blocs like, for example, in Latin America. The outcome of this would be a possible revision of the format of participation of such countries in the global AML/CFT system and existing UN Conventions (including the Vienna Convention).

It is important here not to overlook another aspect. Unlike some Latin American countries where a trend towards legalization is seen as a means of improving government finances, in Europe the issue of legalization of soft drugs is more concerned with human rights issues rather than profit. It is for this reason that the international community should at the very least express its opinion on this trend now. And, above all, it should offer its assessment of the issue of transforming drug trafficking into an instrument of a state's fiscal policy.

Although this scenario may strike some people as being too futuristic, it is important to remember that even developed Western countries have no common view on this issue. For example, Mike Barton, police chief in the town of Durham, said that an outright ban on class A drugs (most dangerous) should be radically revised<sup>3</sup>. Barton suggests that the UK's National Health Service should supply drugs to addicts, breaking the monopoly and income stream of criminal gangs. Among those expressing their support for the initiative is the Transform Drugs Policy Foundation, which is also working to change existing legislation to allow for the legalization of

<sup>1</sup> <http://eterra.info/mosaic/ssha-kak-marihuana-v-remonte-pomogaet>.

<sup>2</sup> Drug Intervention means the trafficking of drugs by one country in the territory of another carried out either independently, e.g. with the involvement of its special task forces, or through non-interference with (or provision of support to) non-state organized criminal groups. In some cases, this may also be done for monetary gains, in addition to political and other goals.

<sup>3</sup> NewsRu.com, Moscow, September 30, 2013 14:38:00.

drugs. In January 2013, a similar initiative had already been presented by the House of Lords and involved an extended sale of the least dangerous drugs supplied with detailed labels through licensed stores.

Although these initiatives have not yet been supported at the government level (specifically, in December 2012 Prime Minister David Cameron rejected the proposal to set up a royal commission for the decriminalization and legalization of illicit drugs, as, in his opinion, the government's current anti-drug policy was sufficiently effective), the mere fact that this issue was raised sends a very alarming signal. Sooner or later the problem relating to the protection of human or minorities' rights (in this case of drug addicts') risks escalating into a completely different problem, namely the problem of finding additional revenues for the budget. Some manifestations of this problem are already beginning to become evident in another bastion of the global war on drugs – the U.S.

The U.S. is one of Russia's key partners in a war against the trafficking of drugs from Afghanistan. But even there, some rather disturbing symptoms are starting to be seen, albeit still at regional level. For example, on November 6, 2012 the state of Colorado held a referendum in which 53% of its inhabitants voted in favor of legalizing the storage, use and sale of marijuana. A similar outcome was reached in the ballot held in the state of Washington. This has created an unprecedented situation for the U.S.: the possession of soft drugs for personal use was legalized at the regional level with both states adopting the relevant laws in early December 2012. Additionally, about 65% of Colorado residents who took part in the referendum expressed their support for a measure aimed at monetizing the drug industry by introducing a 15% excise tax and a 10% sales tax on marijuana. According to experts, these fiscal measures will add up to \$70 million annually to Colorado's budget.<sup>4</sup>

By considering such situations and trends in the aggregate, one can come to a definite conclusion. The world has reached a threshold moment where every country must clearly define, confirm or change its position with respect to illegal drug trafficking. And the key definition here – in other words, the essence of the meaning – is what should be considered legal and illegal drug trafficking, and should a country be allowed to monetize drug trafficking (this is especially true for developing countries).

If, by acting within the framework and on the basis of international and domestic law, the Russian Federation and its partners from among the post-Soviet states continue to consistently advocate and implement a ban on the manufacture and sale of illegal drugs, our allies in the fight against drug trafficking – especially the U.S. and the E.U. – should clarify their position regarding this issue and declare their unshakable commitment to it. Otherwise, we will all end up in a situation where the desire on the part of some countries to solve their financial problems may in the future lead to widespread legalization of drugs, resulting in the repeat of the Opium Wars in China, only on a much larger scale, while the term «drug intervention» will make it into the daily vocabulary of contemporary politicians.

It is this trend that today represents a latent threat, including to the existing global AML/CFT system. While being aware to an obvious danger emanating from this trend, the international community should once again make an objective coordinated assessment of the issue of drug legalization in all its possible manifestations and pass an ethical judgment on all forms of drug trade monetization by states. Failure to do so may result in a situation where former allies in the fight against drug trafficking will find themselves on opposite sides, and where drug trafficking will be listed as a separate revenue item in the budgets of many countries.

<sup>4</sup> Information from <http://eterra.info/mosaic/ssha-kak-marihuana-v-remonte-pomogaet>.

## NEW COUNTER MEASURES

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*On November 10–11, the capital of Turkmenistan, Ashgabat, hosted the International Workshop on Assets Freezing in Accordance with the Requirements of UN Security Council Resolution 1373 (2001)*

**Konstantin V. Litvinov,**  
*Deputy Chief Editor*

The workshop was organized by the International Training and Methodology Center for Financial Monitoring of the Russian Federation through the UN Counter-Terrorism Committee Executive Directorate, the Eurasian Group on Combating Money Laundering and Financing of Terrorism and the Office of Financial Monitoring under the Ministry of Finance of Turkmenistan.

Over 110 representatives from 16 countries participated in the workshop including delegations from the EAG member-states and observers (Armenia, Belarus, India, Kazakhstan, China, Kyrgyzstan, the Russian Federation, the U.S., Tajikistan, Turkmenistan, Uzbekistan and Ukraine) as well as experts from the Great Britain and Belgium, the President of the Financial Action Task Force (FATF), representatives of the FATF and EAG Secretariat and following international organizations: the UN Counter-Terrorism

Committee Executive Directorate, the OSCE, the World Bank. Representatives of Financial Intelligence Units participated in the workshop together with law enforcement and supervision authorities of the Eurasian region states.

The workshop's topic selected is a hot one. UN Security Council Resolution 1373 (2001) adopted on September 28, 2001 is universal and stacked against terrorism financing as a whole. It should be underscored that the resolution sets terrorist assets freezing standards which were further developed and assigned in the FATF Recommendations, namely: blocking without delay, mandatory international cooperation in countering terrorism financing and terrorist assets freezing, response to relevant requests from foreign states. It contains the recommendation to make up national lists of terrorists while fully complying with UN sanctions lists as well as the detailed description of types of terrorist assets subject to freezing.

According to paragraph 6 of Resolution 1373 the UN Security Council Counter-Terrorism Committee

was established to supervise the proper compliance with the resolution, inter alia through in-country visits. The visit to Russia took place in 2012 and the assessments of the Russian freezing system were overall positive.

The Russian Federation is an active member of the Eurasian Group on Combating Money Laundering and

Financing of Terrorism (EAG) whose member-states all work to improve AML/CFT systems in general as well as terrorist assets freezing system in particular. For this purpose are used mechanisms of interaction and mutual assistance provided by the EAG experts who are result-oriented.

*Yury A. Chikhanchin, the EAG Chairman and the Director of the Federal Service for Financial Monitoring of the Russian Federation in his welcoming speech stressed:*

“Since June 2012 the Russian AML/CFT legislation has been greatly changed. As a result, Federal Law No 134-FZ was drafted and adopted in summer 2013 which should mainly improve the mechanism of freezing assets of individuals involved in terrorist activity. In this context the new article “Additional Measures of Countering Financing of Terrorism” added to the anti-money laundering law became the most significant counter-measure. It establishes the preventive administrative mechanism to freeze terrorist assets if there are “reasonable grounds” (i.e. sufficient to suppose or suspect that the given person finances terrorism), it also determines the procedure of responding to a third party requests

for freezing in compliance with the Standards. Furthermore, the clear mechanism was created to examine requests concerning delisting as well as the efficient and publicly known procedure to unfreeze funds of persons accidentally fallen under freezing.

Thus, Russia had showed high political will in upgrading of the domestic AML/CFT system. As a result of this work on October 16, 2013 all the participants of the FATF Plenary Meeting unanimously supported the decision to grant the Russian Federation with a milder monitoring regime when a progress report is submitted every two years instead of the standard monitoring procedure with annual reporting.”



The main objective of the workshop was to assist states to create an efficient mechanism of immediate freezing of funds and other assets of natural and legal persons involved in terrorist activity according to the requirements of UN Security Council Resolution 1373 (2001). Another important task of that event was to promote cooperation and coordination of relevant national and regional authorities necessary to ensure the operational response to external requests of freezing funds, assets and other economic resources.

The workshop participants discussed implemented measures, enforcement issues as well as national practices outside the region thus increasing the understanding of operational

measures and procedures which are to be taken for an efficient freezing regime in compliance with international requirements, including obligations on human rights.

They examined the positive experience of the states participating in the workshop; in particular Turkmenistan which had considerably intensified its efforts to develop the institutional framework of the national AML/CFT system as well as improve the legislation.

In the final part of the workshop the participants discussed eventual topics of next events in order to assist states-participants in strengthening national regimes to freeze terrorist assets according to UN Security Council Resolution 1373 (2001).

### *David Arthurs, Detective Inspector of the Great Britain (Counter Terrorism Command):*



"For me as a law enforcement officer, it is a very important event because from my experience of countering terrorism I know that it is impossible to support this phenomenon without accurate and concerted

efforts of the financial infrastructure. That is why if we manage to undermine the grounds of this system (this workshop is certainly promoting it), then the tasks to combat terrorism will be significantly simplified.

Yet the most important for such events is experts' round tables when they study the issue from different angles. It is essential to build a partnership which will facilitate our further concerted and successful work."

### *Jason Purcell, a Policy Advisor at the U.S. Department of the Treasury's Office of Terrorist Financing and Financial Crimes:*



"I believe that the event was successful first of all because countries which in great numbers had already frozen assets were given the opportunity to share their experience, what systems they had used for it. Me myself

learnt a lot related to freezing terrorist assets and systems built for this purpose.

The main outcome of this event is the possibility to work and think together and set aside the best practices from what we have learnt. Now we all have food for thought. The most important thing will probably happen when we return to our countries and continue thinking how to build our systems to combat terrorist assets in future."

*France S. Lemeunier, CT Intelligence Analyst for the Belgian Fusion Center (OCAM), Belgium:*



"Our unit connects all agencies concerned with terrorism financing and provides them with consolidated analytics. From my point of view, it is a very important workshop and it is not my first one as UN CTC executive directors have already invited me at the similar event in West Africa. Incidentally I can say that practice exchange is of great importance. As for me I learnt a lot during these two days.

Representatives of different countries gathered today in Ashgabat could see what a small country

can do. I am sitting next to the representative of the U.S., a big country with big economy. My country is small; therefore its economy is small too. I consider very useful the fact that the workshop's participants could learn what steps can undertake even such a small country as Belgium to counter terrorist assets. These two days were very good and efficient, maybe we were short of time because not all delegation representatives had a chance to get answers to their questions.

According to the information submitted by the countries I can say that all the states have implemented a mechanism to counter terrorism financing and it is rather solid. For that reason, we can speak to each other as equals when we share our best practices."

## ***TOWARD CREATION OF INTERNATIONAL CENTER FOR RISK ASSESSMENT IN THE CIS***

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*The 2<sup>nd</sup> meeting of the Council of Heads of Financial Intelligence Units of the CIS member-states was held in Ashgabat*

*Irina V. Ivanova,  
Editor in Chief*

On November 13, 2013 the 2<sup>nd</sup> meeting of the Council of Heads of Financial Intelligence Units of CIS member-states was held in Ashgabat, the capital of Turkmenistan. The Russian Federation was represented by Yu. A. Chikhanchin, Director of Rosfinmonitoring. In the Council meeting also participated A. I. Druzhinin, Director of the Department for Cooperation on Security and Countering New Threats and Challenges of the CIS Executive Committee and Turkmenistan delegation.

The Council found practical to amend the Agreement on the establishment of the Council of FIU Heads of CIS member-states in order that the Secretariat work on a regular basis (at present time Russia is an organizer of the Secretariat work).

The participants approved the Action Plan of the Council of FIU Heads of the CIS member-states

and the model Memorandum of Cooperation with Commonwealth bodies authorized to examine certain issues in the anti-money laundering and countering terrorism financing area.

The issue of the development of the Conception of Financial Intelligence Units Cooperation came up for an active discussion as it should determine the tasks and objectives of the CIS Council of FIU Heads at the first stage (2013 — 2014). Introducing the conception, a member of the Russian delegation P. V. Livadny (State Secretary and Rosfinmonitoring Deputy-Director) presented the rationale for the document:

*“The main strategic purpose of the Council that should be stipulated is to achieve specified practical results which should be reported to the chiefs of the Council of FIU Heads. First of all, these results should be in the following areas: mitigation of risks and threats to the national security, organization of efficient coordinated operational procedures in this field and as a result the coverage of the achieved results at the Council of CIS Heads of States.*

*We are expecting to work closely with the Eurasian Group in the first place which is the main AML/CFT policy-maker in the region within the FATF Standards and with the Interparliamentary Assembly of the CIS Member Nations which forms the model legislation."*

Yu. A. Chikhanchin, Director of Rosfinmonitoring, spoke about the issue of information exchange between Financial Intelligence Units of CIS member-states. He addressed the issue of principles and purposes of such exchange and suggested to create common standards in this sphere:

### *Yury A. Chikhanchin:*

"I suggest creating a working group of financial intelligence units' representatives in order to develop the information exchange system. I believe we should start with determining information interaction channels. So one of the forms to make this mechanism work is the exchange of public

lists of persons involved in terrorist and extremist activity. The work with information resources should be aimed at what can help us to create later on an international center for risk assessment in CIS countries in order to detect risk zones and prevent potential threats."



Another important agenda item was the creation of the AML Network Institute of the Commonwealth of Independent States which is going to be a community of higher education institutions, scientific and educational centers capable to become a personnel and science leader in the CIS.

The idea of the creation of the Institute was supported unanimously.

Next meeting of the Council of FIU Heads of CIS member-states will be held in June 2014 in Moscow.



### *V. V. Ovchinnikov, ITMCFM General Director:*

"The problem of staff training for the AML/CFT system is quite pressing today. Only in the Russian Federation around 200 thousand people are engaged in this area: from field investigators to bank employees. In fact it is a new economy sector which requires human resources."

### *Background Information:*

The Agreement on the establishment of the Council of FIU Heads of CIS member-states was signed on December 5, 2012 in Ashgabat. The document was signed by the presidents of the Russian Federation, Armenia, Belarus, Kazakhstan, the Kyrgyz Republic, Ukraine, and Tadzhikistan.

It was Belarus who in 2009 initiated the creation of a special body consisting of the heads of Financial Intelligence Units of CIS member-states in order to strengthen and enhance cooperation in the AML/CFT area. This proposition was supported by the majority of Commonwealth countries as well as by the Eurasian Group on Combating Money Laundering and Financing of Terrorism (EAG).

The draft of the Agreement passed all necessary expert studies and was approved by the Council of the Ministers of Foreign Affairs of the CIS in April 2012.

#### Main Tasks of the Council:

1. to determine priority areas of cooperation;
2. to facilitate the elaboration of common approaches to the harmonization of national legislations;
3. to develop proposals to improve the legal framework of cooperation;
4. to coordinate both the interaction of Financial Intelligence Units and other competent authorities.

The Council also promotes joint operations of Financial Intelligence Units, prompt information exchange and staff training.

## ***COURSE WILL STAY THE SAME***

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*The Russian Federation Transferred its Presidency  
in the Eurasian Group on Combating Money Laundering  
and Financing of Terrorism to India*

*Irina V. Ivanova,  
Editor in Chief*

*Konstantin V. Litvinov,  
Deputy Chief Editor*

During the 19<sup>th</sup> Plenary meeting of the Eurasian Group on Combating Money Laundering and Financing of Terrorism in Ashgabat on November 14, 2013, Yu. A. Chikhanchin, the

EAG Chairman, transferred his powers to Dr. K. P. Krishnan, the head of the Indian delegation in the FATF and the EAG.



In the meeting also participated V. P. Nechaev, the FATF President, P. V. Livadny, State Secretary and Rosfinmonitoring Deputy-Director, G. V. Bobrysheva, Rosfinmonitoring Deputy-

Director, V. V. Ovchinnikov, the ITMCFM Director, representatives of all EAG member-states as well as of several international organizations and observer states.

### *Dovletgeldi Sadykov, Turkmenistan Minister of Finance:*



"I would like to note that the EAG is taking on new significance today taking into account our close partnership relations within the international organization. We are aware of objective advantages of such

a partnership that is based upon well-established connections, experience and best practices in the international AML/CFT system. Turkmenistan is ready to make its contribution to the development of our region in this field. Our state is keeping a close eye on key issues in the AML/CFT area. We are actively studying new FATF Recommendations and working on their integration into the national AML/CFT system."

In his welcoming speech the FATF President V. P. Nechaev brought to recollection how the EAG had

been created with a direct involvement of V. A. Zubkov who had been the head of the Group from 2004 to 2007:

### *Vladimir P. Nechaev:*



"Ten years ago I was one of the first who worked on the initiative to create an FSRB – FATF-style regional body – in this region. I remember when Mr. Zubkov announced the establishment of our FSRB for the first time.

That is why October 6, 2004 became a very important date for us, that day the EAG was founded. Initially the Group united 6 countries. Now it is a full-fledged international organization

with 9 member-states, 14 observer states, and 18 international and regional organizations. In 2010 the EAG became an associate member of the FATF.

If before we paid attention more to the technical compliance and legislation compliance with the FATF requirements, now we turn it to the actual efficiency of these measures, to the necessity to ensure that all the components of the AML/CFT system interact and to how countries can deal with the issues that are the most important for them. Today the EAG member-states should show their intention to implement new FATF Recommendations."

V. P. Nechaev stressed the importance of the fact that since this October Russia has no longer been subject to the regular monitoring by the Financial Action Task Force. The FATF President especially emphasized that it is for the first time

that the EAG will participate in the FATF Plenary Meeting which will be held in Moscow in 2014. It will be an important step for further rapprochement of the FATF and FSRB.

Yu. A. Chikhanchin, Director of Rosfinmonitoring, underscored the significance of the FATF role in forming and improving the global anti-money laundering system and reminded the audience what significant progress had been achieved in

improving national AML/CFT systems of the EAG member-states: Turkmenistan was removed from the FATF "black" list, Kyrgyzstan and Tajikistan had greatly improved their domestic systems at all levels:

### Yury A. Chikhanchin:



"In the Eurasian region we are moving forward too. The main direction of our activity is to prepare for the next, the second, round of EAG evaluations, this work will be done with due consideration of the innovations introduced by the FATF.

The EAG member-states are improving their institutional and legislative framework to combat money laundering and terrorism financing, their Financial Intelligence

Units are operating in a comprehensive and efficient manner, they are working on interesting and promising initiatives some of which we are going to examine during this Plenary Meeting. This work is not easy, but very exciting. We hope that we will manage this task successfully despite existing and emerging challenges and threats.

I find symbolic that three EAG member-states and members of the FATF such as India, China and Russia were granted a milder monitoring regime. It offers proof that our efforts and interaction within the EAG have been de facto acknowledged. This work is continued in other states too."

On the first day of the meeting the participants summarized the Group's performance under the Russian Presidency. Yu. A. Chikhanchin, Director of Rosfinmonitoring, the EAG outgoing Chairman, reported the execution of plan for 2011-2013.

Some crucial achievements of the previous two years are as follows:

1. Strengthening of EAG member states positions within the global AML/CFT system as well as in the Eurasian region.
2. Increase of effectiveness and trustworthiness of expert missions, seminars, trainings, and workshops in order to ensure the implementation and efficiency improving of the AML/CFT system of the Eurasian region as well as domestic systems of the EAG member-states.
3. Intensification of countering drug trafficking, organized crime and terrorism within the EAG.
4. Preparation for next rounds of mutual evaluations within the FATF and the EAG, active

involvement in production of methodological materials, better training for the pool of expert assessors and upgrading of the EAG methodological support, use new technologies in assessments.

5. Cooperation with the EAG member-states and observers to improve their participation in the EAG activity and the provision of technical assistance.
6. Launch of new typologies researches within the EAG consistent with innovations determined in the new version of the FATF Recommendations and new AML/CFT risks.

New EAG Chairman was elected on the first day of the Plenary Meeting. Dr. Krishnan set out the priorities of his work the main of which is to ensure consistency of what Russia has done at this position. The new head of the Group is going to expand the EAG, to implement the new FATF Standards and the new Assessment Methodology in member-states, to create a pool of assessors in every state and to promote the level of technical assistance.

*Dr. K. P. Krishnan:*

"I am looking forward to the active cooperation with the Russian authorities which will play an important role in transferring the chairmanship in the intersessional period. To be elected the Chairman of the Eurasian Group which fulfils the significant role in spreading and entrenching the FATF Recommendations in the region is a great honour for my country and me personally. I would like to stress the great role of the Russian Federation in creating and strengthening our FSRB. Each EAG member state played an important role in establishing the EAG as one of the most efficient

FSRBs. We are the group of associates and friends who make decisions quickly. We always support each other within the FATF as well as in other organizations. So, we should continue our work in the same strain.

Accepting this very important and prestigious post of the EAG Chairman I realize that it is responsibility rather than power, it is the necessity to focus on the implementation of the new FATF Standards which set the high bar even for the oldest and the most active members of the FATF. Nevertheless, I think we should not be afraid of this challenge. As the FATF President and the Chairman have already said, the new Recommendations are focused on the efficiency of law enforcement in the AML/CFT area and on the ability of countries to detect new risks and threats and mitigate them efficiently."

The participants also supported the Indian suggestion that Russia as a country where the EAG Secretariat resides should render every possible help and support as well as technical assistance during the

transition period through the Protocol on Amendments to the Agreement on the EAG will come into force. P. V. Livadny, State Secretary and Rosfinmonitoring Deputy-Director, commented on this for the magazine.

*Pavel V. Livadny:*

"The Plenary Meeting charged the Russian Federation to facilitate the work of the Secretariat and the EAG as a whole in order to render technical assistance and solve operational issues. Furthermore, the decision was made concerning the necessity to codify the concept of dual co-chairmanship. The Secretariat was entrusted to develop the necessary changes to the current Agreement on the EAG as quickly as possible. The current version of the document supposes the single authority of the Chairman."

Moreover, according to the assignments of the 18<sup>th</sup> Plenary Meeting, Kazakhstan presented the intermediate data on improving the national AML/CFT system. The Plenary Meeting was concerned that the Republic of Kazakhstan had not adopted proposals for legislative acts indicated in the first progress report of Kazakhstan.

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On the closing day of the Plenary Meeting the participants listened to the reports of the Working Groups on Technical Assistance; on Typologies; on Combating the Financing of Drug Trafficking, Crime and Terrorism; on Supervision whose mandate delegations decided to extend in a new format.



V. V. Ovchinnikov, General Director of the International Training and Methodology Center for Financial Monitoring, did a presentation named "ITMCFM Projects and Technical Assistance within the EAG". The EAG Secretariat provided information on the joint EAG/APG workshop on typologies and capacity building held in September 2013 in Ulaanbaatar.

One of agenda items was to summarize the results of the Contest for the better interaction of authorities of EAG member-states in the AML/CFT area in which had participated the majority of countries members of the Eurasian Group. Three Contest best participants – Kazakhstan, China and Kyrgyzstan – presented their successful crime investigations and

after the counting of votes the Contest Committee named the winner – the delegation of the Kyrgyz Republic.

This Contest is the new EAG initiative. The 18<sup>th</sup> Plenary Meeting assigned the Secretariat to organize this event jointly with the Group member-states within the November Plenary week. The decision was made to organize such a contest annually during the autumn EAG Plenary Meeting

At the end of the 19<sup>th</sup> EAG Plenary Meeting the participants adopted the Public Statement, Working Plan and Event Schedule of the Eurasian Group for the first half of 2014. The delegations also approved the EAG Secretariat Progress Report for 10 months of 2013.

**FINANCIAL INTELLIGENCE UNITS  
OF THE EAG STATES**

# ***THE NATIONAL SYSTEM OF FINANCIAL MONITORING OF THE REPUBLIC OF KAZAKHSTAN***

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*Sophia S. Aisagalieva,*

*acting chair of the Financial Monitoring Committee*

*of the Ministry of Finance of the Republic of Kazakhstan*

The Financial Monitoring Committee (Committee) is a department of the Ministry of Finance of the Republic of Kazakhstan responsible, with respect to matters falling within its competence, for financial monitoring and implementation of other anti-money laundering and counter financing of terrorism (AML/CFT) measures in the Republic of Kazakhstan.



One of the most important aspects of the fight against money laundering and terrorist financing is the creation of adequate suppression mechanisms that will function both at the international and national levels. For Kazakhstan, with its special geopolitical position in the world, dynamically developing market economy and close proximity to the areas with busy drug trafficking routes and intensive terrorist activity, the issues related

to combating money laundering and terrorist financing are highly relevant.

The first major step taken by Kazakhstan in this area was the establishment in April 2008 within the structure of the Finance Ministry of the Financial Monitoring Committee (hereinafter the «Committee») responsible for gathering, processing and analysis of data on transactions with money and (or) other property subject to financial monitoring.

On March 9, 2010, Kazakhstan enacted the law «On combating money laundering and terrorist financing», signed on August 28, 2009 by the President of the Republic of Kazakhstan. Along with enactment of the above law, the country also amended 26 other existing laws.

In the period from October 2010 to June of 2011, Kazakhstan's financial monitoring system was successfully evaluated by the Eurasian Group on Combating Money Laundering and Financing of Terrorism (EAG) for compliance with international AML/CFT standards.

## *Committee's main areas of activity and functions*

### **Informational**

- Collection and processing data on transactions with money and (or) other property subject to financial monitoring;
- Establishment of the Unified Information and Analytical System;
- Establishment and maintenance of the National Database on combating money laundering and terrorist financing.

### **Analytical**

- Analysis of data submitted by the subjects of financial monitoring (SFMs) with the goal of identifying possible links to and involvement in money laundering and terrorist financing;
- Receipt from SFMs and government agencies of additional data on transactions subject to financial monitoring;
- Rendering decisions in favor or against suspending suspicious transactions with money and ( or) other property;
- Transfer of information to law enforcement authorities, as well as provision of information upon request of law enforcement authorities.

### **Combating terrorist financing**

- Forming a List of Organizations and Individuals associated with the financing of terrorism and extremism, and bringing it to the attention of SFMs through relevant governmental authorities;
- Analysis of data submitted by SFMs on organizations and individuals included in the List;
- Suspension of suspicious transactions carried out by organizations and individuals included in the List.

### **Cooperation**

- Coordination of government agencies' activities and cooperation with SFMs in combating money laundering and terrorist financing.

### **International**

- Collaboration with competent authorities of foreign countries in the field of AML/CFT and information sharing;
- Representation of the Republic of Kazakhstan in various international organizations and participation in their activities.

Kazakhstan has ratified all major international AML/CFT conventions and treaties.

Since its inception, the Committee maintains a constant dialogue with reporting entities, representing both financial and non-financial sectors, their public associations and government agencies that are members of the AML/CFT system on the issues of AML/CFT law enforcement, compliance with international standards and establishment of the financial monitoring state system. The Committee uses the newly created «Help to SFMs» section of its web site [www.kfm.gov.kz](http://www.kfm.gov.kz) to post instructions and

recommendations and update its replies to reporting entities' questions.

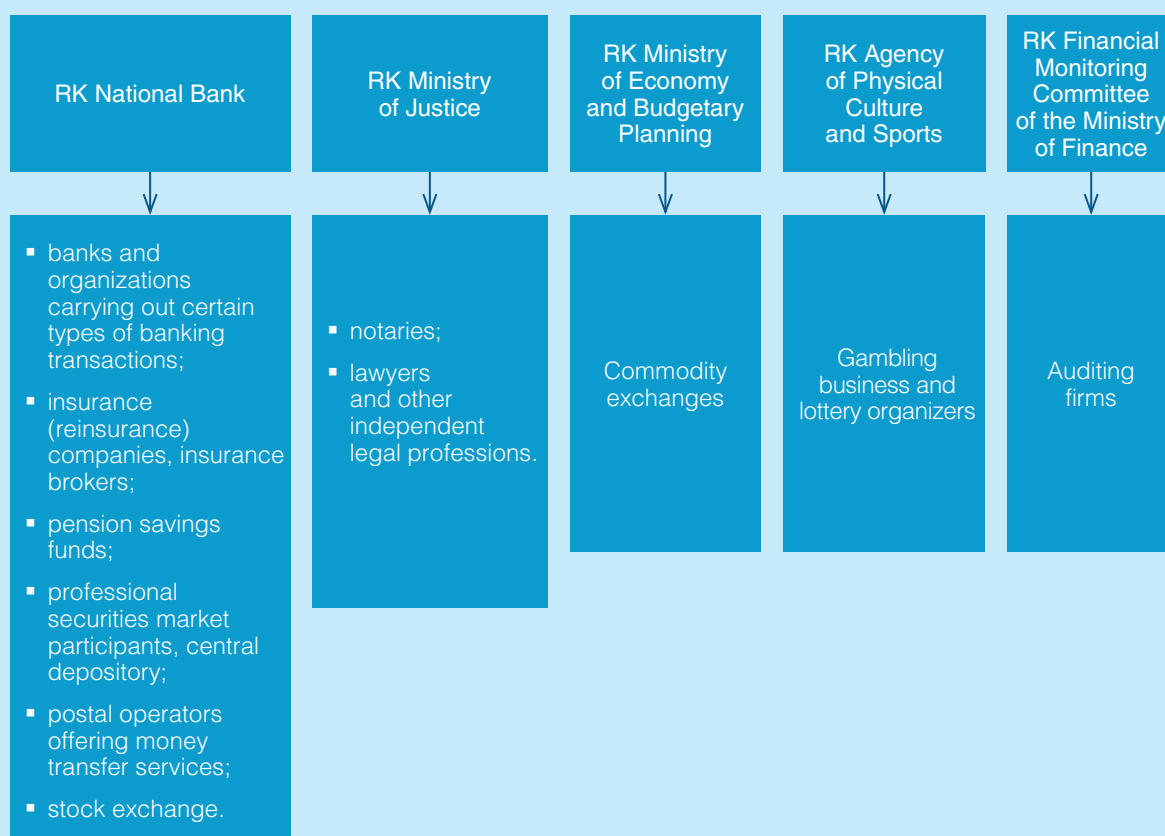
The Committee staff has organized more than 50 such events and workshops in Astana and Almaty, as well as in regions, addressing issues concerning not only AML/CFT legislation but also analytics and IT technologies. Some of these events were attended by international experts.

The Committee also focuses its efforts on coordinating the activities of government agencies in improving the system of AML/CFT-based control and supervision.

As a result of this work, government agencies have amended their regulations regarding mandatory departmental reporting forms, checklists, risk assessment criteria and annual audit plans.

A regulatory framework for monitoring compliance by the subjects of financial monitoring with the law on AML/CFT has been established.

*In accordance with the legislation, the responsibility for monitoring compliance by SFMs with the AML/CFT Law is assigned to the following government agencies (regulators):*



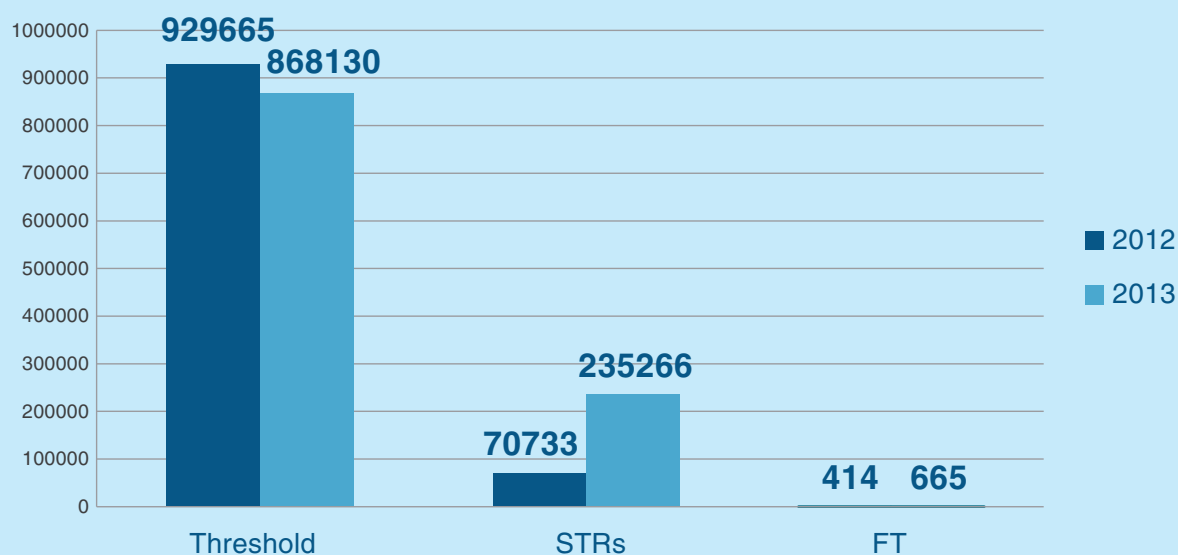
The Committee's key task is to gather and process data on transactions subject to financial monitoring, with the establishment of the Unified Information Analytical System (UIAS) and the work on maintaining and updating the National AML/CFT Database being part of its main areas of activity.

The messages on transactions subject to financial monitoring are provided FME by subsystem DCFO AWP-FME, WEB-FME and on paper.

Upon receipt of an electronic report, the UIAS decrypts it, conducts logical and format control of

the contained therein data and stores the retrieved data in a databank.

In order to enhance the effectiveness of interaction with the relevant governmental and law enforcement agencies of the Republic of Kazakhstan, joint orders for the exchange of information and transfer of materials related to money laundering and financing of terrorism (extremism) were signed in 2011 with the Prosecutor-General's Office of the Republic of Kazakhstan, the National Security Committee, the Ministry of Internal Affairs, and the Agency for Combating Economic Crimes and Corruption.

*Reports submitted by SFMs in 2012 and 10 months of 2013*

During 2012 and 10 months of 2013, the Committee referred to special state and law enforcement agencies of the Republic of Kazakhstan a total of 119 materials upon request and 293 materials at its own initiative.

The purpose of the Committee is to improve the effectiveness of mechanisms for combating threats to the national security of the Republic of Kazakhstan existing in its area of activity and to increase the importance of the results of work carried out within the international AML/CFT network.

Kazakhstan has been a member of the EAG since 2004. In 2011, the country signed the EAG Agreement, and in February 2012, the President of the Republic of Kazakhstan signed the Law on the Ratification of the EAG Agreement.

In December 2012, the President signed the Agreement on the Establishment of the Council of Heads of Financial Intelligence Units (FIUs) of the CIS Member States.

In July 2011, at the 19th Plenary meeting of the Egmont Group (Yerevan, Armenia) voted to offer its membership to the Committee.

Within the framework of bilateral cooperation with financial intelligence units of foreign states, the Committee has signed agreements with the FIUs

of the following countries: Ukraine, Moldova, the United Arab Emirates, Russia, Belarus, Kyrgyzstan, Tajikistan, Indonesia and China.

The Committee has established cooperation with more than 60 FIUs, with the most intensive information exchange being carried out with the FIUs of: Argentina, BVI, UK, Germany, Latvia, Lithuania, Luxembourg, UAE, Russia, Slovenia, USA, Turkey, Ukraine and Switzerland.

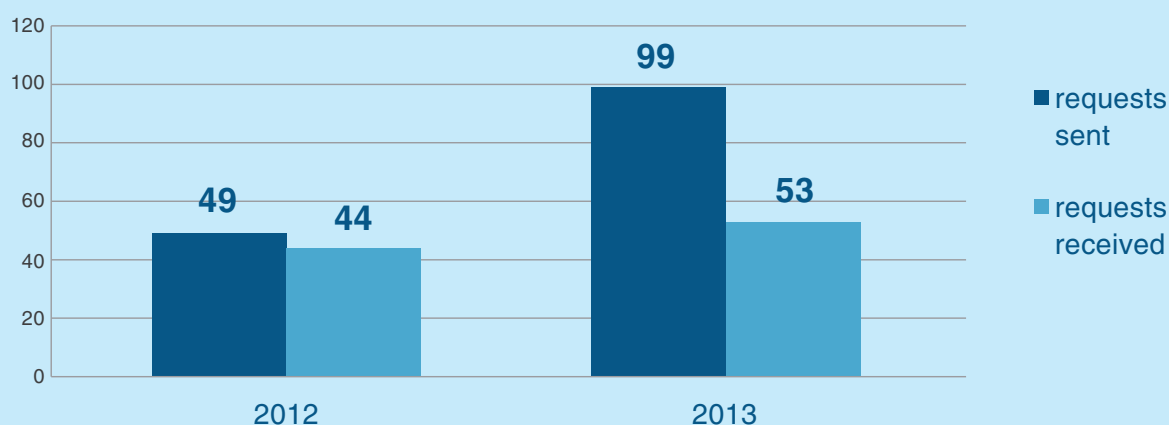
As part of the joint economic research program (JERP), the government of the Republic of Kazakhstan and the World Bank have been working since 2008 on the establishment and development of Kazakhstan's AML/CFT system.

### **Projects implemented in the period from 2008 to 2013:**

#### **1. Studies**

- A study of alternative remittance systems in Kazakhstan.
- National Risk Assessment (NRA) in the field of money laundering and terrorist financing.

### *Information sharing in the framework of the Egmont Group in 2012 and 10 months of 2013*



## 2. Trainings

- AML/CFT law enforcement practice;
- cooperation between state and private sectors;
- AML/CFT-related supervision;
- tactical and strategic analysis in the field of AML/CFT;
- cooperation and information sharing between financial intelligence units.

### **In 2014:**

#### **A study into the implementation of international standards on physical cross-border movement of cash and bearer instruments.**

Since its inception, the Committee has been devoting special attention to the issue of staff training. Given that AML/CFT is a new area of activity for Kazakhstan, during the Committee establishment all its employees studied the experience of foreign FIUs in the area related to the gathering of data subject to financial monitoring, its processing and analysis.

Assistance in the training of personnel for the Committee and other government agencies, members of the state AML/CFT system and SFMs was provided by international experts representing: the IMF, World Bank, U.S. Embassy in the Republic of Kazakhstan, OSCE, Egmont Group, JP Morgan Chase Bank, Citibank, International Training and Methodology Centre for Financial Monitoring (Russia) and the Training and Methodology Center of the State Financial Monitoring Service (Ukraine).

In 2009, the Financial Monitoring Committee of the Ministry of Finance of Kazakhstan, the Federal Financial Monitoring Service (Rosfinmonitoring) and the Autonomous Nonprofit Organization International Training and Methodology Center for Financial Monitoring concluded a tripartite Agreement on Cooperation in the Field of Training of Personnel for the National AML/CFT System of the Republic of Kazakhstan. Under this Agreement, 4 students from Kazakhstan were trained at the National Research Nuclear University (MEPhI) and, following their graduating in 2012, joined the Committee. At the present time two more Kazakh students are attending the course.

In keeping with the latest trends, the requirement for efficient use of time and resources is becoming one of the most important aspects of the Committee's work. In 2010, with the technical assistance from the ITMCFM, the Committee put into operation its own system of videoconferencing, allowing its users to

hold real-time forums, consultations, discussions and trainings. The Committee actively participates in all these events.

The Committee operates its own Situation Centre, a flexible and multifunctional management tool that acts as one of the most effective decision support systems.

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In November 2013, the Committee took part in the contest for the best cooperation of the state authorities in AML/CFT among the EAG member-states, held in the framework of the 19<sup>th</sup> EAG Plenary Meeting.

The contest's laureate was determined the Committee's case study on money laundering using offshore companies and cash conversion transactions.



*S. Aisagalieva*

The country's FIU received information about suspicious transactions conducted by five legal entities through second-tier banks. Suspicions were aroused by the crediting of large amounts of money to the accounts of five legal entities opened in second-tier banks. The money came from various companies located in different regions of Kazakhstan.

Among the payment purposes used for the transactions were:

- services related to the supply of goods;
- supply of agricultural products;
- marketing services;
- supply of commodities and materials;
- provision of construction services;
- contracting services;
- financial assistance.

A search through government agencies' databases revealed several inherent characteristics of a shell company:

- no tax deductions;
- no social security contributions;
- no payroll costs.

The undertaken reconciliation of transactions also revealed no traces of operating expenses, such as rent, utilities, etc., going through the accounts of the said five legal entities.

On the day of their receipt, some of the funds were converted into cash and withdrawn by private individuals B. Y. Yablonya and T. K. Topol.

The entire process of inputting money into the system and subsequently withdrawing it in cash took no more than one day.

In the final stage, the funds were transferred to the account of an offshore company.

In response to its information request, made via secure network Egmont Secure Web, the FIU of Kazakhstan was informed by a foreign FIU that Kazakh national B Y. Yablonya was the owner of foreign company N Ltd, (*registered in Belize*), which in turn was the founder of company Y Ltd (*registered in the Virgin Islands, UK*).

All materials relevant to this case were immediately referred to Kazakh law enforcement authorities.

Kazakh law enforcement authorities arrested Mr. T. K. Topol during the latter's attempt to withdraw cash in the amount exceeding \$70,000 from the account of company Z.

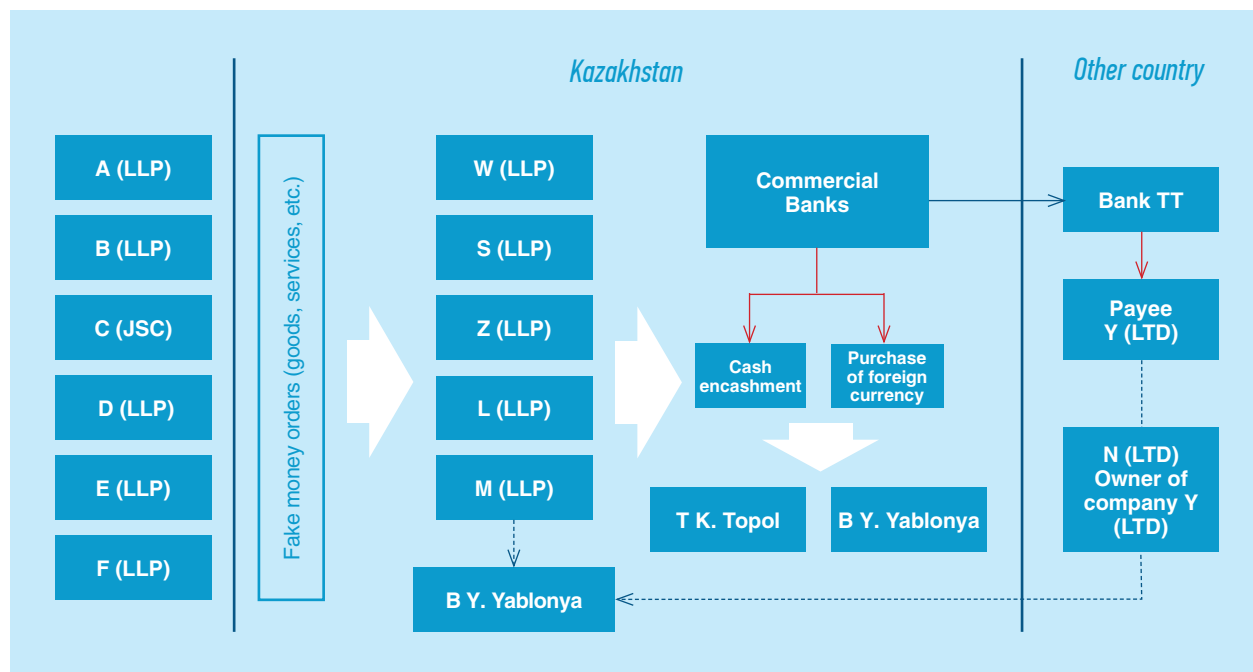
During a search of Mr. T K. Topol's personal belongings, investigators found a check for about \$360,000 issued by a Kazakh second-tier bank.

A subsequent search of company Z's offices led to the discovery of accounting documents and stamps belonging to 23 bogus companies.

The ensuing criminal investigation resulted in the seizure of the suspects' property and

freezing of their accounts and initiation of criminal proceedings under Article 193 of the Criminal Code of the Republic of Kazakhstan «Money Laundering».

The materials gathered by the FIU of Kazakhstan became the basis for initiating a number of other criminal proceedings linked to this case.



**EDUCATION AND SCIENCE  
IN THE AML/CFT AREA**

## FINANCIAL INTELLIGENCE OFFICERS OF XXI CENTURY

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*Igor N. Loskutov,  
Acting deputy chair of personal, logistics  
and inspection department of Rosfinmonitoring*



*Vladimir Ivanovich Glotov,  
Director of the MEPhI Institute for Financial and Economic  
Security, member of the Russian Academy of Natural Sciences,  
professor, Rosfinmonitoring Deputy-Director.*

**FB:** Vladimir Ivanovich, you became the Institute director not so long ago. What are your first impressions?



**V.G.:** I would like to highlight students' enthusiasm for studying. It could not have been otherwise as only the most qualified and motivated youngsters enter the IFES. To prove it I will cite the passing grades for different specialities:

- speciality 090305 "Information and Analytic Security System" — 290 points of 300;
- speciality 080101 "Economic Security" — 265 points of 300;
- speciality 090915 "Information Technology Security for Law Enforcement" — 280 points of 300.

Thus, IFES passing scores are the highest in MEPhI.

I should also say a few words about IFES teachers. Our lecturers, professors, doctors of

science possess colossal pedagogical potential, practical experience in the AML/CFT area. Many of our instructors worked in Rosfinmonitoring.

Studying in the IFES supposes work with big data sets some of which are related to financial transactions — all this requires ongoing improving and upgrading of the infrastructure, especially computer equipment.

The development of this area is one of our priorities in improving educational processes in the Institute.

**FB:** *There is no doubt that it is one of the topical issues for any modern higher education institution. Having in mind the IFES specific nature I would like to ask if there are any special requirements to prepare financial intelligence officers?*

**V.G.:** Besides profound knowledge of natural sciences students get strong interdisciplinary background. Issues of financial and economic security are not limited by the operation of the credit and financial system. The considerable part of

## Background Information

The Institute for Financial and Economic Security (IFES) of the National Research Nuclear University “MEPhI” was established in 2005 upon the initiative of the Federal Service For Financial Monitoring to prepare specialists in systems analysis and data protection in financial and economic areas as well as to solve the issues of combating money laundering and terrorism financing.

Training such specialists (we can call them financial intelligence officers) requires interdisciplinary knowledge and supposes enhanced professional training in creating and operating modern software and information systems, computer technologies in business as well as the appropriate background in economics, law and information security. This kind of professionals can only be prepared with fundamental science study as methodological grounds for analytical thinking necessary for a system approach.

The state standard for the specialty “Information Security of Automated Systems” is taken as the base, it was complemented by units of interdisciplinary education and special education in the financial and economic security. Thus, the unique field of study was created — “Financial and Economic Security”.

### **The curriculum includes not only Science disciplines proper for MEPhI but also:**

- enhanced training in computer and information technologies;
- business education: management and executive decision-making, investments and securities market, technologies of competitive intelligence;

- special linguistic training with learning English during 10 terms and the second foreign language (German, French or Spanish on student's preference) during 6 terms;
- economic education necessary to analyze the financial accounting of banks, enterprises and organizations;
- legal education in the area of financial and economic security as well as anti-money laundering and countering the financing of terrorism.

### **The relevant training in the IFES NRNU “MEPhI” prepares specialists for work in:**

- the Federal Service for Financial Monitoring and other government agencies monitoring and supervising financial and economic activity;
- internal control units of banks, leasing, real-estate companies, professional participants of securities market and other financial institutions dealing with funds or other assets;
- information and analytical departments of public and private companies ensuring the enterprise financial security, collecting and analyzing data on market conditions, production methods, etc.

The interdisciplinarity of education enables graduates of the IFES NRNU “MEPhI” to adjust easily to the modern labour market and business environment.

studying consists of acquiring knowledge and skills of designing, creating, operating and upgrading the modern IT infrastructure as it's a basic element of all modern global economy sectors.

Moreover, we pay a special attention to the social, political and patriotic education of our students who already in the Institute face the issues of the protection of national and public interests doing their research works in Rosfinmonitoring or other government agencies. Another important part of their education is linguistic skills: students are fluent in English and have sound knowledge of the second foreign language (they can choose German, French or Spanish).

**FB:** *With such knowledge and skills IFES graduates should be in high demand?*

**V.G.:** Certainly. To prove it I can say that by the 5<sup>th</sup> year of studies almost our students are employed thanks to the integration of the academic process into the activity of potential employers — students have practice in government agencies and leading financial companies where they prepare their scientific and research work as well as graduation paper.

I would like to underscore that upon request of the CIS governments the IFES prepares foreign students (their number reaches 10% of all students). Complementary to fundamental knowledge of finance and IT as well as extensive linguistic skills, students examine national legislation.

**FB:** *How does the Institute manage to attract dozens of foreign students annually?*

**V.G.:** The IFES attractiveness for both Russian and foreign students is in its unique educational environment, the history of MEPhI and of course in the quality of education.

We also do not forget about social conditions. In particular, students from other cities and countries are provided with rooms in a modern hostel and the Institute has all necessary infrastructure for physical and personal development.

However, the formula for success of our alumni is the constant and ongoing development of the IFES as the institutional basis of the integrated educational environment, the improving of forms and programmes of education and close interaction with employers.

Education in the IFES MEPhI is an important step towards success for smart, motivated and ambitious young people.

The IFES today it is 400 students including over 40 foreigners; in-demand specialties as follows "Information and Analytic Security System", "Information Technology Security for Law Enforcement" and "Economic Security", the enrolment competition is over 10 candidates per place.

# THE IFES MEPHI AS THE ALMA MATER FOR FIUs

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*Konstantin G. Sorokin,*  
columnist, PhD

*Alina V. Pascal,*  
Editor-columnist

Since 2009 the ITMCFM has been implementing a technical assistance project aimed at training specialists for the national AML/CFT systems of the EAG member-states and specifically highly qualified IT specialists focused on conducting financial investigations for the Financial Intelligence Units of their respective countries.

The project currently embraces 36 students from Armenia, Belarus, Kazakhstan, Kyrgyzstan, the People's Republic of China, Moldova, Tajikistan and Ukraine trained under the curricula of higher professional education. For the moment there are 13 graduates. The most talented alumni can continue their education in master's programmes and post-graduate studies; the admission is competitive.

A wide range of cutting-edge educational resources and technologies are used in training, including the system of videoconferencing among the EAG member-states.

The ITMCFM pays both for the education and hostel accommodation of students as envisaged by the trilateral agreement between Rosfinmonitoring, the ITMCFM and the Financial Intelligence Unit of the country sending its students to NRNU MEPhI.

The Financial Intelligence Unit as a programme participant traditionally submits at least two applicants per place.

Annually after the quota approval, the ITMCFM and IFES organize preliminary screening (interview) with applicants in profession-oriented subjects (physics, mathematics) using the EAG videoconferencing system. Applicants are admitted for the entrance exams only if they pass the interview with relevant teachers successfully.

On November 15 this year the International Training and Methodology Center for Financial Monitoring (ITMCFM) organized a meeting with the IFES NRNU MEPhI first year students enrolled in 2013. They were presented with ITMCFM projects, given a tour of the Center, told about the history, role and the place in the international AML/CFT system.

The students shared their impressions on studies, told about their own interest in the chosen profession underscoring the importance of linguistic training for their future job. They also noted several aspects to be addressed, notably the necessity for additional tutorials for some subjects. Although all students passed very serious admission tests, the level of the basic training varies in different countries. Understanding how important it is to prepare human recourse for national AML/CFT systems of the EAG member-states, NRNU MEPhI managers and teachers are ready to render students any necessary assistance and organize additional tutorials for difficult subjects.

It's important to emphasize high motivation and ambish of students. For instance, already now several students are concerned with the prospect to enter master's courses and post-graduate studies. The ITMCFM supervises this area too and coordinates the possibility of further education for the most talented students with national FIUs. The heads of national FIUs understand that this will

enable them to get a unique top-ranked specialists and support this initiative.

First year students were especially interested in guaranteed employment after they graduate from NRNU MEPhI. Following the agreements between the ITMCFM and national FIUs with Rosfinmonitoring participation, the FUI of the sending country acts as a guarantor of the IFES graduates' employment in the national AML/CFT systems as well as ensures interning.

At the end it should be mentioned the topicality of the idea to create the club of the IFES MEPhI alumni suggested by Rosfinmonitoring managers in summer 2013 during the presentation of graduation papers. If this initiative is implemented, the EAG videoconferencing can allow graduates to stay in touch (though FIUs where they will work are very far away from each other). The ITMCFM as the supervisor of the training project and a provider of the EAG videoconferencing system, is ready to render its support to the implementation of this idea.



## ROUND TABLE IN ITMCFM

# STRENGTHENING COOPERATION OF THE EAG MEMBER-STATES' FIUs DURING ANTI-DRUG OPERATION "CHANNEL"

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*Konstantin G. Sorokin,*  
columnist, PhD

Representatives of Financial Intelligence Units and concerned government agencies of Russia, Belarus, Kazakhstan and Tajikistan participated in the round table initiated and moderated by the Anti-Money Laundering Department of the Russian Federal Financial Monitoring Service. Konstantin Ivanovich Gobrusenko- Deputy Head of Anti-Money Laundering Department of Rosfinmonitoring was a round table moderator.

The parties discussed the practical aspects of the implementation of the "Channel" operation, inter alia the interaction of its active stages with respect to Financial Intelligence Units (FIUs).

Opening round table Russian representatives underscored the importance of detection the drug business financial infrastructure while law enforcement authorities are more focused on examining drugs as goods, thus, laying upon the financial intelligence the

enhanced responsibility for financial flows related to the drug business.

The parties noted that though several practical moments required the cooperation level strengthening between national law enforcement and FIU, current financial intelligence units had played an important role in the "Channel" operation which allowed to raise the question of further promotion of the development of the drug business financial infrastructure detection. To serve this goal they plan to explore the possibility of creating operations under the code name "Stream" where national FIUs would play the leading part.

Among the last joint achievements the parties mentioned the creation of drug business financial centers' map presented at the relevant working group at the 19<sup>th</sup> EAG Plenary Meeting in November this year as well as the development of criteria for suspicious transactions within the EAG.

The Belarusian delegation noted that the new means of payments are currently more topical than ever and many of them are actively being developed by criminal gangs to separate the physical transfer

of funds from the transfer of narcotic drugs and thus to make catching in flagrante more difficult. In particular, criminals worldwide frequently use prepaid cards, electronic systems of money transfers, and the financial infrastructure of mobile phone providers. In this case FIUs play a crucial role as they provide with invaluable help to law enforcement agencies by monitoring suspicious transactions.

Colleagues from Kazakhstan shared their experience how to deal with transactions without opening an account regularly used by some criminals when transporting narcotic drugs through the so-called "North Route" (from Afghanistan). They underscored the high level of cooperation between Kazakh and Russian officers of anti-drug agencies.

This May officers of the Belarus financial intelligence unit completed and sent to the law enforcement agencies the results of the conducted relevant typology research. The research results are expected to enable the law enforcement authorities to improve their efficiency.

Furthermore, the participants of the round table emphasized that during the "*Channel*" operation the parties detected very few financial transactions of the persons involved. This is due to both the use of new means of payments and the prevalence of cash in

drug trade. In other words, criminals are trying to keep away from the financial system. In such conditions the implementation of the FATF Recommendation 32 about cash couriers within the Customs Union becomes crucial.

In addition the parties studied the experience of foreign countries in respect to cooperation of Financial Intelligence Units with the law enforcement. For instance, the U.S. has the system of working groups consisted of representatives of the agencies concerned — FIU, anti-drug agencies, tax and customs authorities, etc.

The participants named the secure dedicated channels for the EAG member-states' communication one of the main aspects of the future work as it would allow to share information with the China FIU.

At the closing of the meeting the parties stressed the importance of joint training workshops including via videoconferencing for FIU officers and other law enforcement agencies. An educational workshop related to the illicit drug trafficking with a focus on the interagency cooperation of the law enforcement and FIU to detect the financial component of the drug business is expected to be held on the premises of the ITMCFM prior to the EAG meeting scheduled for June 2014.

## ***NETWORK APPROACH TO THE TRAINING OF FINANCIAL MONITORING SPECIALISTS***

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*On December 5, 2013, the Federal Financial Monitoring Service held a meeting dedicated to the establishment of a network Anti-Money Laundering and Counter Financing of Terrorism (AML/CFT) Institute*

*Inessa A. Lisina,  
redactor and correspondent*

*Konstantin V. Litvinov,  
Deputy Chief Editor*

The proposed network AML/CFT Institute will be the first in Russia. Originally enshrined in the Federal Law No. 273-FZ of December 29, 2012 «On education in the Russian Federation», this approach to education allows students to achieve better results in the learning of educational program materials through the use of resources of multiple organizations.

Mobile money transfers, virtual currencies, electronic money and financial schemes involving large numbers of companies from different countries are only some of the transaction tools

financial monitoring specialists have to deal with in their daily work. This segment of the economy is in need of highly qualified personnel capable of not only countering the existing threats associated with money laundering and the use of such tools for illegal purposes, but also of working proactively.

Among the issues discussed during the meeting, attended by director of the Federal Financial Monitoring Service Yury A. Chikhanchin, head of the Presidential Civil Service and Personnel Directorate Anton Y. Fedorov, head of the Federal Agency of Scientific Organizations Mikhail M. Kotyukov and deputy education minister Alexander A. Klimov, as well as by heads and representatives of the leading universities, research and educational centers and members of the network Institute from Russia,

Kyrgyzstan and Kazakhstan, was the training of specialists in the field of financial monitoring. The interest shown by educational institutions of the

CIS member-states in the project underscores the relevance of the issue of FM specialist training to many modern states:

*In his welcoming remarks, A. Y. Fedorov said:*

"The emerging modular or, more precisely, network system will assume the responsibility for the training of personnel for national anti-money laundering structures. This task becomes even more important as the need for building a talent pool of public service employees grows. I'm convinced that the focusing of efforts by concerned organizations on the network-based forms of education,

especially the leading regional universities, will generate positive results in the area of personnel training already in the foreseeable future... I'm glad, dear colleagues, that with this meeting attended by so many important people we are beginning a new chapter in the history of personnel training for national anti-money laundering systems."

Appreciation and support for the idea of creating a network Institute also came from the Ministry of Education of the Russian Federation. In his speech, deputy minister Alexander A. Klimov stressed that

the key near-term objective is to create conditions for the emergence of specialists integrated into the state anti-money laundering and terrorist financing system:

*Alexander A. Klimov:*

"I believe it is the task of the network Institute to accept the responsibility for addressing several very important issues designed to improve the effectiveness and quality of the training of specialists our financial monitoring systems need most. One of the most important tasks

is to establish the core departments directly in organizations. It's clear that without relevant practice academic training alone will not be enough to produce highly qualified specialists capable of addressing the challenges facing the financial monitoring service."



The main outcome of the meeting dedicated to the network Institute was the signing of the agreement on its establishment. Director of the Federal Financial Monitoring Service Yury Chikhanchin stressed that the ratification of the agreement was

only the beginning, and that much work still needed to be carried out in order to build a modern and efficient system of training, retraining and advanced training of personnel for the anti-money laundering and terrorist financing system.

### *Universities and scientific and educational centers that are members of the network Institute*

1. Financial University under the Government of the Russian Federation
2. Diplomatic Academy of the Ministry of Foreign Affairs of the Russian Federation
3. Russian Academy of Natural Sciences
4. International Training and Methodology Center for Financial Monitoring
5. National Research Nuclear University MEPhI
6. Institute of Legislation and Comparative Law under the Government of the Russian Federation
7. St. Petersburg State Polytechnic University
8. Lobachevsky State University of Nizhny Novgorod
9. Novosibirsk State University of Economics and Management
10. Pacific National University
11. Rostov State Economic University
12. Ural Federal University named after the first President of Russia B. N. Yeltsin
13. Institute of Further Education of State and Municipal Employees of the Academy of Public Administration under the President of the Kyrgyz Republic
14. Academician E. A. Buketov State University of Karaganda
15. Kyrgyz-Russian Slavic University named after the first President of Russia B. N. Yeltsin

## THE EXPERIENCE OF THE CIS STATES

# MAIN TASKS: UPGRADING SKILLS AND INTERNATIONAL COOPERATION

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*Next year the Training – Methodological Center for Retraining and Advanced Training of Financial Monitoring Specialists in Combating Money Laundering and Terrorist Financing (Kiev, Ukraine) will celebrate 10<sup>th</sup> anniversary. It's one of the first educational foundation within the CIS which is training financial monitoring specialists*

*Inessa A. Lisina,  
redactor and correspondent*

### The Center foundation

The Cabinet of Ministers of Ukraine issued a decree in 2004 for the establishment of Training and methodology center. The Center's main task is the retraining and advanced training of financial monitoring specialists (on a base of a license from Ukraine Ministry of Education, Science, Youth and Sports).

Today, the Center operates two regional branches, Western and Eastern, located in Lvov and Kharkov respectively, which allows to expand

the accessibility of training and has a workforce of 25 employees.

### The main areas of the Center's activities

The Center's activities are aimed at several major trainee groups.

The first group is comprised of employees of the state financial monitoring system, as well as

law enforcement and judicial authorities. This area of activity is particularly relevant to the country's national security, given that the representatives of this group are responsible for state anti-money laundering and counter-terrorism financing policies, and includes trainings for employees of the Ministry of Finance, Ministry of Justice, Ministry of Internal Affairs, the State Tax Service and a number of other government departments and ministries of Ukraine.

The second area of activity is the provision of retraining and advanced training to specialists in the field of primary financial monitoring, i.e. employees of pawnshops, commodity, stock and other exchanges, professional securities market participants, real estate agents, notaries, lawyers, accountants, and other entities carrying out financial transactions in accordance with applicable law. For each group of students, the Center has developed tailor-made courses that take into account students' professional line of activity, Ukraine's existing AML/CFT legislation, and international requirements.

Additionally, the Center actively develops international cooperation with representatives of foreign countries and organizations. Up till now, the Center has already been visited by FIU delegations from the United Republic of Tanzania, Azerbaijan, and several CIS countries with the goal of studying Ukraine's system for combating money laundering and terrorist financing. Jointly with the World Bank and the EAG the Center took part in national risk

evaluation events. Within International Technical assistance and Information Exchange Program (TIEX) were held training activities oriented to interagency sharing experiences and stiffening level of public authorities interaction. In cooperation with International Monetary Fund the Center hosts discussions about improving of national anticorruption and AML system. The Center has significant educational and technical resources. It's important for events management with representatives from international organizations and foreign countries.

Resource base includes:

- conference hall for 65 persons;
- classrooms with modern computer equipment and software;
- multimedia projectors for demonstration of educational presentations.

### The main results of education

During the period from 2006 to September 2013, the Center provided training to more than 5,000 individuals, the majority of which represent law enforcement and judicial authorities. The largest group of students, 1,151 individuals, was trained in 2011. The main reason for this was the adoption of



the Law of Ukraine No. 2258-VI of May 18, 2010 that amended Law No. 249-IV of November 28, 2002 «On combating money laundering».

### **The main directions of the Center's development strategy**

Now the Center is working on a distance-learning program, which is being developed in cooperation with the OSCE. It involves placement financial monitoring courses on the Center's website and is designed to simplify the process of training or retraining of specialists. Interactive training will allow students to study the available materials on a particular topic independently. After completing an online course a person can get a standard certificate.

The Center is planning to organize short-term trainings in the field of financial monitoring. This will allow us to familiarize financial monitoring experts with the latest changes affecting the sector and



update their existing knowledge in the shortest time possible.

The Center fundamental goal is raising the level of professional knowledge national AML/CFT system as it is the key to the effective functioning of the national anti-money laundering and terrorist financing system.

**PRIVATE SECTOR.  
THE ITEM – VIRTUAL CURRENCY**

## ***VIRTUAL CURRENCIES AND CRYPTOCURRENCIES: NEW POSSIBILITIES OR NEW RISKS?***

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*Victor L. Dostov,*  
*President of the Russian Electronic Money Association*

*Pavel M. Shust,*  
*analyst of the Russian Electronic Money Association*

The growth of the virtual currencies and cryptocurrencies market presents, perhaps, the most unusual tendency in the financial sphere in the last decade, confirming some of Friedrich Hayek's hypotheses on private monetary systems that he developed in the mid-1970s.

During the evolution of retail payment services, the main goal consisted of compensating for the shortage of cash which reduced the risks of moving large sums of money, provided the capability for long-distance finances, and protected consumers from possible fraud. This determined the pre-paid derivative nature of the majority of payment tools starting with checks and ending with electronic money, or e-money. Banks and other financial have never tried to produce their own money because regular money guaranteed by the state is already exist. As a result, the pre-paid nature of payment tools in some countries has been even fixed by law. This group of states includes Russia; by definition,

only transfers without opening a bank account are considered transfers of e-money in Russia.

Various types of virtual currencies and cryptocurrencies are built on different principles. Although no consensus has been formed among researchers regarding a single approach to classifying these new payment tools, we believe that they can be divided into at least 3 categories.

### **1. Virtual currencies with limited functionality.**

The most illustrative example of this category is currencies that are issued by online game operators to monetize their projects. Modern online games strive to create virtual worlds and the existence of their own currencies in these worlds is very logical: they give individuals the opportunity to purchase virtual resources or equipment. However, in contrast to e-money, the virtual currency can only be used to pay for goods and services provided by the issuer him or herself. Game operators tend to prohibit

removing funds since these operations are simply not profitable for them.

Some units (bonuses, points, and miles) offered to participants of consumer promotion programs can also be categorized as virtual currencies with limited functionality, but only if they are able to be purchased directly from the operator.

## 2. Centralized cryptocurrencies.

Centralized cryptocurrencies include the first e-money projects (e.g. Digicash) in which “virtual money” was issued. The bank issued money in exchange for the money presented, signed with an electronic signature, and transferred it to the client. Afterwards, these coins could be used to pay just like with cash (for example, by saving it to a disk) or deleting it (by transferring it on the internet). Such a system presented consumers with a certain level of anonymity because the bank did not know who had which coin. Nevertheless, clients did not appreciate this advantage because it reduced their rights to a minimum. Just as with normal cash, e-money is easy to lose and is not refundable. This is why all pilot programs for centralized cryptocurrencies were rolled back in the 1990s and were instead replaced by e-money systems that had a pre-paid nature and offered more of a financial service than a payment tool.

## 3. Decentralized cryptocurrencies.

Throughout the centuries'-old history of the development of payment technologies, a single issuer guaranteed the trust of all participants: in essence, consumers use payment tools only because they trust the state, bank, or payment operator. Until recently, no other means of providing trust existed. However, in 2008, a protocol for the decentralized currency known as Bitcoin allowed a single issuer to be excluded without damaging participants' trust was created.

Within the Bitcoin system's framework, separate computers receive access to complex mathematical problems whose solutions lies in a set of symbols, i.e. a digital coin. As soon as a computer is done generating another coin, it transfers information about this event to other users of the network who “register” the new Bitcoin and thus legitimize it. As a result, each participant knows which “coins” are valid and which aren't. When Bitcoins are transferred from payer to recipient, this

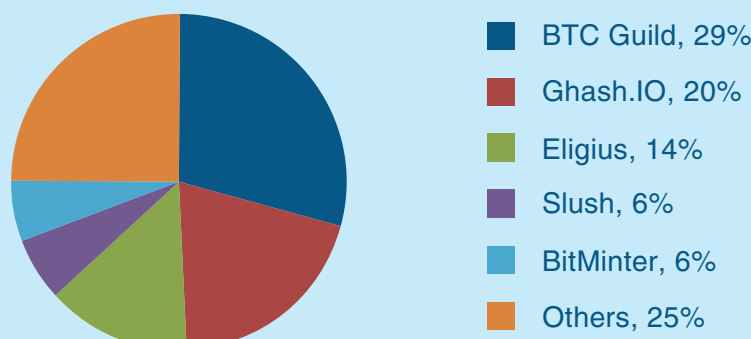
transaction is recorded in the system's “collective memory” and everyone knows from/to which address the transfer was made. The Bitcoin system's distributed nature makes it more easily scalable: accounts will be performed independent of how many computers are on the network—five, five hundred, or five thousand.

A stable rate of issuance is built in to Bitcoin's protocol which is why the mathematical problem becomes gradually more complex as the number of participants grows. Several years after the system's launch, the problem will become so complex that one computer will be insufficient to solve it and users will start to unite in groups (“pools”) to more effectively generating coins. Currently, the generation of 75% of Bitcoins is divided among 5 of the largest pools (*See Figure 1*).

Nevertheless, it would wrong to think that virtual or cryptocurrencies exist in an isolated realm. At its current level of development, the sphere of electronic payments is extremely integrated: no payment system exists in the world that could be completely isolated from other financial systems as a whole. In this regard, virtual and cryptocurrencies are not unique. To develop, they need connections with the formal, regulated financial sector. This is most evident for virtual currencies with limited functionality: consumers pay for their purchase through e-money systems, credit cards, or from a bank account. In such situations, they often use the term “exchange”, as though a fiat currency is being exchanged for a virtual, imagined one. However, a player in fact receives some service, pays for receiving advantages in the game process.

Intermediary services play no less of a role in cryptocurrencies. Since generating e-coins on individual computers is impractical, expanding the audience at the expense of “mining” participants is no longer possible. As a result, the demand for purchasing “coins” increases, a demand that exchange points are designed to satisfy by offering consumers the opportunity to obtain and sell a cryptocurrency using traditional financial tools. In order to effectively perform their activity, they should be registered as a legal entity, open accounts in a credit organization, and conclude contracts with payment systems.

In some countries, stock exchanges have become the main object of regulation by virtue of a special clause acting as a “bridge” between the real monetary system and the virtual one. For example, one of the largest MtGox exchange points was forced to submit to American financial regulators and receive a company license for transferring money. Before that, its business faced the threat of having accounts opened in US banks shut. Exchange points present the most obvious object

*Figure 1. Division of Bitcoin generation among organized user pools*

for regulation since mechanisms already developed for credit organizations can be used for oversight. At the same time, extending it to other participants of the cryptocurrency ecosystem (payers, receivers, and those who generate “coins”) presents a more significant task that states do not yet have experience resolving.

However, understanding how virtual and cryptocurrency systems work does not answer the question why consumers use these non-traditional means of payment. In the context of game currencies, the answer is more obvious: purchasing them is a natural means of receiving a specific service in the online game. However, it is more difficult to determine the motivation of consumers who select decentralized cryptocurrencies.

In our opinion, the specific advantages of cryptocurrencies lie in the social realm rather than an economic or technological one. Payments using this currency remain technically complex, take a relatively large amount of time (on average, 5-10 minutes), while the insignificant cost of transactions is compensated by the costs connected to exchanging a fiat current. The instable exchange rate of Bitcoins to fiat currencies requires a separate examination. It is important to understand whether it promotes the system’s popularity (by virtue of possible speculation characteristic for the Forex market, but much more volatile) or, on the contrary, inhibits it (from the point of view of “traditional” payments with a fixed included cost).

The popularity of decentralized cryptocurrencies is mostly due to the fact that it is possible to guarantee participants’ trust, bypassing states and central banks. While trust in national economies fell among individual social groups—in particular, among youth—this independent means of payment, for many people, filled the gap that arose. The value of cryptocurrencies,

just like the value of fiat currencies, is based on an economic expectation, not the presence of real assets (for instance, gold), but there is no institution that could single-handedly influence its main characteristics, i.e. rate of issuance and exchange rate. The number of generated digital coins is laid in the protocol itself and will be invariably independent of how many participants appear in the payment system. A computer program, as opposed to a national monetary system, cannot be exposed to corruption, irrational or poorly-verified solutions. Bitcoins are more difficult (or impossible) to confiscate from an individual. As a result, individual consumers have started to trust the cryptographic protocol more than they do the state. From this point of view, the growth of the cryptocurrencies market, as well as the natural result of increasing the regulatory burden on formal payment tools. If an outflow of the audience towards cash previously occurred in such cases, now part of clients are moving towards deregulated electronic cash.

Nevertheless, despite their technological originality, cryptocurrencies must submit to the logic of the global payment ecosystem’s development. No payment systems that could be isolated from others exist in the world. Moreover, their survival depends on their level of inclusion in world payment infrastructure. This also applies to cryptocurrencies that cannot exist without exchange points that act as channels between fiat and non-fiat currencies. In its turn, any contiguity of the virtual world with the real world sharply increases the ability trace operations as was demonstrated by the closing of the Silk Road’s trade floor for illegal products. Because it seems that it is not the isolation of cryptocurrencies, but, on the contrary, their integration with existing financial products could be a mean of decreasing risks of ML/FT. While the circulation of

*Figure 2. Bitcoin exchange rate relative to US dollar*

electronic coins in practice is as anonymous as cash, it is difficult for users to maintain complete confidentiality. When ordering goods to home addresses, using e-mail, indicating a cell phone number or withdrawing funds on payment cards, clients present to varying degrees information about themselves which allows them to be identified. In this regard, it is supposed that subdivision of financial intelligence agencies and regulators should, in time, pay more attention to information that is as yet considered minor. Such a tendency will be relevant for both private currencies and regulated retain financial tools.

Virtual and cryptocurrencies are unique in that they exist in a virtual realm that did not exist 30 years ago. Nevertheless, they have to develop according to the rules that have prevailed over the centuries'-old history of retail financial instruments. Regardless of which

economic or even political considerations lay at the basis of new payment technology projects, they have to interact with already-developed infrastructure. This makes technologically unique solutions relatively trivial from the AML/CFT's point of view: they always contain elements that can be embedded in the global anti-money laundering system. However, it is premature, in our opinion, to undertake any large-scale actions directed at strengthening their regulation. Throughout the workshop on virtual currencies conducted under the auspices of the Eurasian and Asia/Pacific groups on money laundering income and financing terrorism in Ulaanbaator, the participants have come to the opinion that developing profile typologies is, as yet, not relevant. We suppose that such position will become relevant in at least several years, when the virtual and cryptocurrency markets finally obtain clearer outlines.

## DISCUSSION OF E-MONEY, CARDS AND PAYMENTS 2013

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*Konstantin G. Sorokin,*  
columnist, PhD

The Forum «WE E-Money, Cards, and Payments 2013» was held in Hilton Moscow Leningradskaya Hotel on October 3-4, 2013. The topic of the first day was e-money and the second one was devoted to cards and payments.

Viktor Dostov, the President of the Electronic Money Association, hosted the first day of discussions and noted in his opening address that an electronic wallet which is now integrated with bank cards (linked to the wallet) changed its functionality and became an “interface”. He also noted that one of the predominant trends is that the existing “brands” are in fact dying out and that the customers focus mainly on functionality, not the “brand”.

Mr. Dostov named the “smart wallet” that chooses the best (the most advantageous) card out of linked cards and apps as the future of interfaces. The leading role will be given to more complex payment models like paying fines to the Department of Motor Vehicles and Traffic Control through mobile applications that receive information and make payments online in real time.

The problem of how to regulate e-money is vital in the private sector: how precisely should an electronic wallet be regulated—as an ATM card or as cash? And to which category do Bitcoin and other cryptocurrencies that do not have a common emission center, bank of circulation, or common “channel” to deal with regulators? The speaker noted Silk Road, a recently-closed online resource that

sold drugs in the USA for Bitcoin, as an example of what he was talking about. In conclusion, Viktor Dostov said that regulators tend to be slower than technology worldwide and assured that regulators will have to change their way of work to promptly respond to rapid changes in the payment ecosystem.

During the first day, presentations were mainly oriented towards promotion of speakers’ products and obviously had a commercial inclination.

The probable transition of responsibilities in terms of consumer protection from the Federal Service on Customers’ Rights Protection and Human Well-Being Surveillance to a mega-regulator (on the basis of the Central Bank of the Russian Federation) presents a certain interest to those dealing with the sphere of e-money and the banking community.

Tatyana Alekseeva, legal director of Yandex.Money, quoted statistics on noncredit banking services. There are 64 organizations of this type in Russia: 48 of them are settlement banks, 4 are banks of deposit and 11 are payment services. The peculiar features of payment services are lower minimal authorized capital (18 mln. rubles), no mandatory approval of the candidates to the Board of Directors by the Central Bank of the Russian Federation and simplified accounting. Payment services cannot exchange currency and can transfer money only without opening new accounts. According to the speaker, sublegislature is developing slowly and there are many questions with no answers in the law. For example,

there is no need to approve the candidates to the Board of Directors, but it is still necessary to approve acting directors while permanent members are away.

In the course of discussion, the topic was raised of the possibility of avoiding existing restrictions while making purchases (including plane tickets) that are higher than the set threshold amount, which is 15,000 rubles, from unidentified wallets. The details were given to self-study but the problem is how to make a payment in parts from different unidentified wallets. At the same time, it was said that it does not contradict the law directly. However, the need to regulate such cases by law in favor of non-cash methods of payment was vocalized. The arbitration favoring cash, for which no ID is necessary, is highly undesirable.

The presentation of Nadezhda Prasolova from the Federal Financial Monitoring Service caused heightened interest. The participants were especially curious about the freezing of assets and in particular about the formation of the Interagency Coordination Board (Ministry of Foreign Affairs, Federal Security Service, Federal Financial Monitoring Service) in charge of freezing. Nadezhda Prasolova said that due to various meanings of what a tax crime is in different countries, it will be hard to unify and, as a result, to implement coordinated international collaboration dealing with tax crimes. The participants wanted to know more about a recently passed Federal Law No 134 (including Article 200.1 of the Criminal Code, Article 15.27 of the Code of the Russian Federation on Administrative Violations and others). Nadezhda Prasolova was asked if the Federal Financial Monitoring Service was going to include data acquired from international information agencies and other organizations in the national list of terrorists and extremists. In this case, one should bear in mind that the "foreign" part of this list is composed in the Russian Federation based on the UN Security Council Resolution and, unfortunately, cannot include information provided by private organizations. It works the same way for most countries that have such lists. Together with that, as part of a risk-oriented approach, subjects of financial monitoring have the option to use various sources to detect fraud and to assign levels of risk to their clients.

Peter Drakhvelidze, a Webmoney representative, wondered about regulations in the sphere of mobile companies, especially in situations when stand-ins register SIM cards and subsequently use them to commit fraud. In the Russian Federation, one has to present a valid ID to purchase a SIM card which helps to identify clients. However, what a client will do with a SIM card is another story. Despite the fact that this problem is relevant, it has yet to be solved in many countries

where a SIM card can be obtained without documents. While the Federal Service for Supervision in the Sphere of Telecom, Information Technologies and Mass Communications is in charge of this matter at the current moment, the Federal Financial Monitoring Service will be involved in solving this problem in the future.

Armenian private sector representatives touched upon an interesting and burning issue regarding the possibility to have unidentified currency accounts in Russian e-money accounts. It is currently impossible (however, it is allowed to open unidentified ruble wallets and keep sums up to 15 thousand rubles, but identification is required to withdraw and cash this money). However, according to Russian representatives of e-money accounts, this might become possible in the future.

During the session about PayPal, it was discussed whether this system would appear on the Russian market and what prospects of development it has. In 2012, e-commerce equaled \$700 billion. In Russia, this amounted to \$12 billion in 2012 and the number is supposed to grow up to \$17 billion in the current year and 15% of these sums are paid off by credit cards and 5% by e-money and other similar forms of payment. The key competitive advantage of PayPal is its purchase protection service. In other words, customers have a money-back guarantee. Another advantage is safety (fraud protection in IT) as an electronic wallet can protect the credit card information. As regards the opinion that PayPal is strongly connected with the eBay electronic auction service, eBay consists of only 40% of the system's yearly turnout which totals \$145 billion (in Russia it is \$1 billion and eBay consists of about 50%).

According to the participants of this discussion, PayPal earned money with the approval of Visa and Mastercard, but now they are planning to limit this possibility and to start "wallets" that exclude PayPal. The participants also think that PayPal is not familiar with the peculiarities of the Russian market. At the same time everyone said that PayPal returns money to the card much faster than the fixed 30 days in Russia.

In the meantime, PayPal is negotiating with Russian banks to choose a partner. As of mid-September 2013, 13 of the largest trading systems in Russia work with PayPal. While participants agreed that rules and regulations in Russia are extremely strict, Russia is not favored by the Financial Action Task Force. Viktor Dostov, a leading expert on combating money laundering and terrorist financing in the private sector and participant of seminars for the private sector organized by the Financial Action Task Force (FATF), explained that as far as the FATF is concerned, the Russian Federation is rather strong and performs much better in certain

points than the USA, for example, which is proven by the recent transition to a 2-year (the easiest) monitoring period. As for identification, it was said that different variants of remote identification, including Skype, are being discussed. Everyone agreed that identification schemes by means of preauthorization of a bank card used by PayPal have certain imprudent risks and should be thought out together with the Central Bank of the Russian Federation. A representative of Armenia asked how PayPal will be developing in the CIS. The answer was that the company is working on it and expansion is planned, but no details were given.

The issue of how to reduce the amount of cash payments was also discussed. According to some participants' estimations, the commission for card payments taken by banks is higher than commission for collecting cash which slows down the development of non-cash payments. Viktor Dostov said that mobile companies spent about 1.2% on cash collection and the minimum commission of Visa and Mastercard is 1.6% and more.

The experts mentioned that in the past 2 months, Qiwi blocked a lot of suspicious wallets with the goal of identifying them (without linking them to threshold amounts) to prevent fraud.

The participants named consumer credits (put on an ATM card) as an option for noncash payments' further growth. The Central Bank of the Russian Federation managed to put cash credits in order, but there are still hidden payments for ATM cards, which makes cards more profitable for banks.

At the end of the first day, the question of cryptocurrencies, including Bitcoin, was discussed. Peter Drakhvelidze, Webmoney representative, emphasized that such currencies are in fact the enemy of every country since they are not linked to any jurisdiction and are completely anonymous. At the same time, he said that Webmoney allows their "identified wallets" to exchange such currency.

On the second day of the discussion, the conversation turned primarily to how much these or those payment tools are interesting to buyers. Topics related to expanding client bases and increasing client loyalty were raised and the issue of using mobile terminals and the prospects of introducing them universally were addressed.

In the context of the Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT), prepaid cards for a presenter (worth up to 15,000 rubles) were discussed. These cards can be used by minors or other groups of individuals who cannot receive a regular bank card for by some reasons or status. The representatives of VTB Bank opined that this niche is completely unpromising and does not current present the possibility of building a business on it. At the same time, participants noted that schemes that include applying these cards in drug trafficking (however, monetizing money from cards is only possible upon identification). The fact that Tinkoff bank was able to organize the logistics of delivering credit cards in Russia in under three days—its competitive advantage—was also emphasized.

Linking third-party banks' cards to a "home" bank's internet bank which will help users receive additional services could become a general trend in the long run. Also noted was the extreme relevance of users converting bonus miles from various rewards programs (primarily airlines).

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During the event, Baker and McKinsey presented a collection of English-language "Doing Business" articles by country (Russia, Ukraine, Kazakhstan, Uzbekistan) which contained research material on how to conduct business, including legislative control. This collection can be used as a reference by readers of different backgrounds, to conduct mutual assessments, to prepare for such assessments, to establish national risk weights, and for a wide range of readers.



## **BITCOIN – NEW VIRTUAL CURRENCY IN REAL ECONOMY**

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*E-money, online payments, cryptocurrency and other virtual financial tools have become a logical result of rapidly evolving and wide spreading of the modern information technology*

**Inessa A. Lisina,**  
*redactor and correspondent*

**Konstantin G. Sorokin,**  
*columnist, PhD*

Recently the idea of e-money was unknown to the most of people in the world. But the situation has changed. E-money has become an instrument for everyday payments in real-time. For less than 10 years e-money have found it's niche and became a common element of the financial system. That's why they are a subject of the regulation and supervision now.

Instant money transfers with using of digital tools are wide spread in the world economy. In modern Internet the main role play different cryptocurrencies, and particular significance is given to the bitcoin. This digital currency is rather young as its

implementation started in 2009. However, less than 4 years later, it appeared to be a widely known anonymous currency used for online-payments.

To buy or sell bitcoins, one should install an open-source client application. Numerous PCs running the applications comprise the P2P (peer-to-peer) network ("peer" is an equal right member of the network who provides his servers for using to other members and vise versa). The same principle applies to the torrent file system. Likewise, virtual currency is transferred among network nodes. There is no any central administrator or regulator, the currency is fully decentralized. Transaction details are stored encrypted on client computers that share equal responsibility and exchange services with other network users. It makes the bitcoin network 256 times more powerful than TOP50 supercomputers<sup>1</sup>.

<sup>1</sup> According to information at the <http://www.bitcoinwatch.com> to compare with the computers in TOP 500 overall power.

Each user can create an unlimited number of digital wallets to store bitcoins. Each bitcoin-wallet is associated with an unlimited number of independent addresses – different alpha-numeric combinations – for transferring virtual money. If you know an address it's possible to trace how much money was sent to or received from it, but cannot uncover the recipient and the purpose of payments. Developers recommend using a different wallet for every new transaction to ensure anonymity and prevent from hacker attacks.

Bitcoins can be sold for traditional currency at several virtual exchanges. The largest bitcoin trading exchange is BTC China, where bitcoins are traded for Yuan. The second and the third popular exchanges – Mt. Gox and BitStamp, respectively, trade bitcoins for dollars, BTC-e – for rubles. On the coinabul.com bitcoins are sold for gold coins. So, bitcoins can be transferred to precious metals and traditional currencies, which makes them a real instrument in the global financial environment.

Advantages of bitcoins for users are obvious. The official site of the most popular cryptocurrency says that a person can send a bitcoin-payment from Africa to Canada in 10 minutes. With that, no bank can slow down the process, charge enormous fees or freeze the assets<sup>2</sup>.

Another feature is pseudo-anonymity. It would be a mistake to assume that only criminals or buyers of illegal items are interested in concealing details of their Internet transactions. Some people are reluctant to disclose information on their credit cards being anxious of the information misuse, others try to prevent privacy invasion.

This currency is popular as an alternative saving funds method. More over it also might be used as a speculative financial tool, because of limited number of issued bitcoins. The difficulty of "mining" is constantly growing up. That's why this currency is a good investment sphere. A number of national governments can limit the foreign currency turnover. As a result they deprive residents of the opportunity to defend money from inflation and bitcoins help to avoid it. At the same time this tool is characterized by its high volatility and attractiveness for speculations.

Anyway, today's trend is evident. Anonymity and unaccountability to state agencies make virtual currencies particular attractive for black markets that use a huge set of tools to hide information. Governments are concerned about growing



popularity of such currency and practically untraceable anonymous transactions with significant amounts of it. This poses a serious threat to national AML/CFT systems across the world.

Online markets where bitcoins can be used for illegal sales (mainly, of drugs, weapons, forged documents) are yet another threat that comes to fore. It's much more difficult to track their activity as they are hosted on the so-called "deep web", where domains end with the .onion extension. These resources are accessible only by downloading a special Tor browser. Although access to the exchanges becomes more complicated, possible profit and unsupervised free appropriation are the reasons for high demand on the relevant software and technologies.

In October 2013 public attention was drawn to the problem of illegal financial bitcoin transactions, when Ulbricht Ross – alleged proprietor of the Silk Road site - was arrested. This site was created in 2011. It is estimated that Silk Road average revenue amounted to \$ 15 million a year. Approximately 900 thousand users and several thousand sellers sold there illicit drugs, agreed on illegal deals, for example contract killing, hacking, counterfeiting and fraud<sup>3</sup>.

Besides the notorious Silk Road, the "deep web" hosts a range of other shops engaged in illegal activities: Marketplace (forged documents, stolen credit cards), Drugs (different narcotic and psychotropic substances), Desert Eagle (weapons) and others. The specified sites also accept bitcoins.

<sup>2</sup> Russian version of the bitcoin official web-site <http://bitcoin.org/ru>.

<sup>3</sup> According to the Carnegie Mellon University report <http://www.andrew.cmu.edu/user/nicolasc/publications/TR-CMU-CyLab-12-018.pdf>.

This once again proves the fact that criminals tend to refuse from traditional currency in favor of anonymous virtual currency that is hard to trace and associate with a particular person.

Bitcoins and other virtual currencies become ever more popular not only for illegitimate activities. Today bitcoins are used to acquire companies. In July 2013 the gambling site SatoshiDice was sold to an unknown buyer for 126 315 bitcoins (\$ 11.5 million – according to bitcoin-info.net).

Bitcoins are widely used in everyday life. As a social experiment, a young couple from Utah, USA set off on a trip around the world. They were going to live several months strictly on bitcoins. Despite significant difficulties, after three months they announced the experiment a success. Car rent, fuel, restaurant bills, air tickets, hotel reservation and other goods and services were paid by bitcoins (the report about this travelling was published in the Wall Street Journal<sup>4</sup>).

The Federal Reserve Bank of Chicago confirms that the number of bitcoin transactions on the Internet is constantly increasing. It also reports that on average there are about 30 bitcoin transactions per minute. The average transaction size is about 16 bitcoins<sup>5</sup> (in the present moment it's about 16 000 \$). Certainly not all of these transactions relate to goods and services payment. The main part is speculative transactions that unfortunately couldn't be determined in exact number.

But in spite of its growing popularity, news of the Silk Road shutdown scaled down the value of bitcoins. But it lasted not for a long period. A month later – in November 5, 2013 – the second, more secure version of the site was launched and many users and sellers registered with their previous usernames. Meanwhile, on the exchanges the bitcoin value soared to a maximum of more than \$1000. This followed the US Senate hearing on bitcoins and other virtual currencies where the Chairman of the US Federal Reserve Mr. Bernanke called virtual currencies a promising payment method.

Such prospects will attract a big number of potential investors in the sphere of virtual currencies. However undetermined legal status is the reason why all predictions about the future of cryptocurrencies are conditional and fragile. In many points it's depend on the quick changing online payments nature. Anyway, bitcoins will be fully issued by the year 2140, while the current number of bitcoins is around 12 million (for the present moment it's nearly 12 billion dollars). Since bitcoins will be in circulation during a long period of time, governments and global financial regulators should elaborate a sound approach to digital currencies to make them relevant only for legitimate financial services and eliminate their usage in illicit activities, including ML/FT. More over virtual currency legal base and mechanisms of its functioning should be determined.



Also there is one more unregulated question – what will replace the cryptocurrencies in future, when they will become a subject of the national and supranational supervision. When the “newest” payment methods will appear and what technologies will be used? And the main question if the regulatory authority will be able to recognize new trends and to operate with them?

<sup>4</sup> <http://blogs.wsj.com/moneybeat/2013/11/14/life-on-bitcoin/?KEYWORDS=bitcoin>.

<sup>5</sup> <http://finance.rambler.ru/news/analytics/138457343.html>.

## NEWS BLOCK

## Financial Monitoring in Banks

*Inessa A. Lisina,*  
*redactor and correspondent*

On November 20, 2013, Kiev hosted the 2<sup>nd</sup> international conference titled Financial Monitoring in Banks. The conference was organized by company Business Format (Dnepropetrovsk, Ukraine), which specializes in the holding of international events attended by leading financial and banking sector experts.

Among the conference participants were delegations from Azerbaijan, Belarus, Georgia, Kazakhstan, Moldova, Russia and Ukraine, consisting mostly of



*I. Lisina*

employees of big banks responsible for primary financial monitoring and regulator-based interaction, including the Transnistrian Republican Bank, First Ukrainian International Bank, Citibank (Ukraine), Ukgazprombank, Cartu Bank (Georgia), Tsesnabank (Kazakhstan), etc. The conference was also attended by representatives of the two best-known global consulting firms: Ernst & Young CIS and KPMG Russia and CIS, specializing in financial advisory services. Among the institutions invited to participate was Russia's International Training Center for Financial Monitoring (ITMCFM).

The discussions focused on the issues of combating money laundering and terrorist financing, internal banking controls, the introduction of U.S. FATCA tax regime in the CIS countries, compliance monitoring (conformity of banking activities in the financial markets to the current legislation), the mechanisms for the implementation of «know your customer» guidelines in the banking and financial sectors, typologies and indicators of suspicious financial transactions, etc. The ITMCFM presented a concept of a network AML/CFT Institute. The relevance of this issue is highlighted by the need to ensure a steady supply of qualified personnel for the contemporary system of anti-money laundering.

The report provoked a series of discussions, with participants highlighting the key importance of this issue. This was due to the fact that the main task of the Institute graduates in their future professional activity will be maintaining interaction with representatives of the banking and financial sectors. Conference participants proposed involving banking experts in the training process in order to raise the level of students' awareness of contemporary practices and principals of working with reporting entities and to ensure a better mix of their academic and practical skills. This will form the basis for the successful functioning of the national AML/CFT system.

**Network AML/CFT Institute** is community of research and educational institutions working on a common task of training qualified personnel and providing methodological and research support for the AML/CFT system.

**Network AML/CFT Institute's objectives are:**

- to establish new forms of cooperation between scientific and educational centers comprising the network Institute with a focus on AML/CFT-related research and personnel training;
- to create conditions for the development of academic mobility among students and teachers;
- to achieve concentration of intellectual and other resources in the AML/CFT sector and recruitment of the most qualified teachers and most mobile and capable students;
- to follow the latest global trends in research and development, as well as FATF Recommendations and other international organizations' AML/CFT-related guidelines.

## ***With an Aim to Strengthen Regional Stability and Security***

Legal and institutional mechanisms designed to ensure security and to respond to new challenges and threats have been established within the framework of the Commonwealth.

This was the opening statement in a speech by Toktasyn Buzubayev, deputy chairman of the Executive Committee and deputy executive secretary of the Commonwealth of Independent States, to the participants of the international scientific and practical conference entitled "Improving Cooperation between the Competent Authorities and Special Services of the CIS Member-States in Response to Modern Challenges and Threats to Security", which began work on November 27, 2013, in Minsk.

He noted that the Commonwealth has conceptually defined the common principles, objectives, main areas, forms and systems of cooperation and collaboration in this field of joint activities.

For the purpose of their practical implementation, medium-term intergovernmental programs of joint measures for combating crime, terrorism and other violent manifestations of extremism, illicit trafficking of narcotic drugs, psychotropic substances and their precursors, illegal migration and human trafficking are being adopted. The work on the implementation of such programs for 2011-2013 is now in its final stages.

The organization is consistently working towards the goal of formalizing the participation of CIS member states in the international legal instruments governing cooperation in the fight against modern challenges and threats to security.



According to T. Buzubayev, the CIS is also continuing to further develop and improve the international legal framework for cooperation, with the number of international legal instruments adopted in this area currently standing at more than 60.

As part of its efforts aimed at the implementation in the CIS of the Long-Term Model Law Plan, the Interparliamentary Assembly of CIS member states has adopted the following model laws: «On combating terrorism», «On combating money laundering and terrorist financing», «On combating trafficking in human beings», «On combating corruption», «On transportation safety», «On border security» and «On the state border».

The CIS member-states' law enforcement agencies are continuing the practice of holding planned coordinated preventive measures and special operations, with 29 and 5 of such activities respectively held during 2011-2012, according to T. Buzubayev.

The organization continues to prepare a set of organizational and technical measures to create and effectively use modern and advanced



T. Buzubayev

telecommunications and information technologies needed for the exchange of information between law enforcement authorities of the CIS member-states.

The CIS countries actively collaborate with each other in the field of employee training and retraining.

A list of international organizations engaged in close cooperation with the CIS includes: UNSC Counter-Terrorism Committee, UN Office on Drugs and Crime, specialized bodies of the OSCE, SCO and CSTO. According to T. Buzubayev, this cooperation allows to coordinate efforts and together confront modern challenges and threats to security.

As a result of this work, the last few years have seen a steady decrease, averaging 5.25%, in the CIS crime rate with respect to some of the most important parameters.

Separately, T. Buzubayev touched on the outcomes of the CIS summit held on 25 October in Minsk. Specifically, he noted that the heads of states spoke highly of the CIS work and its development prospects, identified current issues and challenges facing the Commonwealth and outlined ways to solve them.

In order to promote cooperation between the CIS member-states in the fight against crime, terrorism, drug and human trafficking, the Council of Heads of State of the CIS has approved four programs:

- 2014-2018 Interstate Program of Joint Measures to Combat Crime;
- 2014-2016 Program for Cooperation between Members of the Commonwealth of Independent States in the Fight against Terrorism and Other Violent Manifestations of Extremism;
- 2014-2018 Program for Cooperation between Members of the Commonwealth of Independent States in the Fight against Illicit Trafficking in Narcotic Drugs, Psychotropic Substances and their Precursors and in Countering Drug Addiction;
- 2014-2018 Program for Cooperation between Members of the Commonwealth of Independent States in the Fight against Human Trafficking.

The heads of state have signed the Agreement on the Protection of Classified Information within the Commonwealth of Independent States and approved the Rules for the Treatment of Classified Information by the state bodies of the Commonwealth of Independent States. The main purpose of the aforementioned documents is to ensure full implementation on the part of CIS security agencies of the tasks assigned to them in the fight against international terrorism, drug trafficking and other forms of transnational crime.

Given the growing international relevance of crimes committed using information technology and the threat they pose to the national security of the CIS member-states, the Council of the CIS Heads of State has approved the Strategy for Cooperation between the CIS Member-States in the Fight against Crimes Committed Using Information Technology. The plan for the implementation of this Strategy calls for the development of a special program.

Attaching great importance to the development of cooperation in the fight against corruption, participants of the meeting of the Council of the CIS Heads of State signed the Agreement on the Establishment of the Interstate Anti-Corruption Council, which is to be tasked with coordinating the work of competent and other relevant agencies of the CIS and ensuring the implementation of the adopted documents on combating corruption.



The deputy chairman of the CIS Executive Committee separately mentioned the issue of external challenges to the organization's security, citing almost daily news about bloody armed conflicts, social, political and inter-religious upheavals, and terrorist acts. Another area of concern is the ongoing tensions around Syria and the high potential for conflict in Afghanistan. With regard to the latter, T. Buzubayev believes that the future prospects of this country following the impending withdrawal of coalition forces are extremely vague and uncertain.

A close study and an evaluation of the current geopolitical situation in the world points at the persistent challenges and threats posed to global stability by international terrorism, drug, arms and human trafficking, illegal migration, and other forms of transnational organized crime. The threat of use of chemical, biological (bacteriological) weapons and information technologies for terrorist purposes is also growing.

All these factors, according to T. Buzubayev, necessitate the need for further joint efforts to strengthen regional stability and security, including in

the framework of the Commonwealth of Independent States.

T. Buzubayev concluded his speech by expressing confidence that «today's Conference will become an important step in strengthening practical cooperation between the CIS member-states, and its results will contribute to greater security of our countries and effective countering of new challenges and threats.»

***Press service of the  
CIS Executive Committee***

### **Monograph annotation**

#### **"Topical matters of national anti-money laundering and terrorist financing systems development in EurAsEC member-states"**

K.G. Sorokin, B.E. Ponomarenko, S.E. Kovaleva, L.K. Karpov. Moscow, Yustitsinform, 2014. – 230 p. ISBN 978-5-7205-1215-6.

Monograph is devoted to analysis of modern condition and perspectives harmonization of national combating money laundering, terrorist financing and the financing of proliferation of weapons of mass destruction systems in the EurAsEs member-states. The problem under consideration emerges full blown because of financial integration activation within the EurAsEC. Another reason is the necessity of implementation of new international AML/CFT standards in national legislations of the Group

member-states before carrying out national risk assessment and mutual evaluations. They will be realized according to new FATF methodology. The special focus will be on the topical issues of establishing internal AML/CFT control system in the Russian bank system.

The research will be interesting to scientific community and practitioners in AML/CFT sphere as well as to students and candidates studying economics and jurisprudence.

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