THE MONEY LAUNDERING PREVENTION SYSTEM

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Abstract

The paper presents the money laundering and terrorist financing prevention system in Croatia. The basic concepts are defined, the principles and fundamentals of international regulations analysed, and the regulatory system in Croatia covered by statute and money laundering prevention Regulations is presented, in conjunction with a description of the organisation, remit and international actions of the Money Laundering Prevention Office.

The infiltration of dirty money is a crucial problem from national economies. The purchase of shares, of real estate, the establishment of dirty investment funds and the use of the banking system for the embedding of such resources is a danger to the credibility of a whole country, and in particular to the security of the financial and banking system. Croatia has adopted statutory measures aimed at the effective detection and prevention of suspicious financial transactions, in other words the prevention of money laundering.

Launderers constantly find new ways, make use of new non-financial channels and expand their activities to real estate, artworks and insurance. Hence it is necessary to keep up with European approaches and recommendations, to strive for further improvement of the laws and the modernisation of the system, and to adopt new regulations harmonised with international standards, particularly with Directive 2005/60/EC.

Key words: money laundering, terrorist financing, prevention, harmonisation with international standards, due diligence, reporting suspicious transactions

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1 Introduction

Money laundering is a process the aim of which is to cover traces leading to the real source of illegally acquired money, in which, more and more often, the non-financial sector and the professions become involved. According to the definition of Directive 2005/60/EC this process includes covering up the real nature, the source of money, its transformation and transmission in order to conceal its illegal origin. This may involve purchasing, possessing or using property derived from illegal activities or participation in, connection with, abetting, stimulating and facilitating any of the aforementioned activities.

Dirty money is the money acquired through criminal activities and all property derived from such money. This means that money laundering cannot exist without predicate criminal activity.

The US Office for the Prevention of Money Laundering (FinCEN)[1] has described the money laundering process through three phases: placement, sublimation and integration.

In the phase of placement, proceeds generated from criminal activities are placed into the financial system, or invested into real estate and movables. The main goal is the lodgement of such proceeds into legal financial flows or their transfer outside the country. In this phase, the launderers must expose their earnings, which is crucial for the easier detection of dirty money (Maros, 1999:241).

This is the most dangerous phase for criminals regardless of whether their money appears in cash or not. Here there is a direct link between the money and the criminals.[2] After that moment, the money is not cash any more; it becomes a number on paper or on the computer display (Lilley, 2000:51-52).

The next phase in this process is most frequently called sublimation, but it can also be called swamping or mixing (Lilley, 2000:53). In the sublimation phase, launderers start to cover traces of the real source of money by a multitude of transactions. They transfer money to domestic and foreign accounts by using legal transactions and change the shape of money in order to make it harder to follow its flow.[3]

In this phase the omnipresent offshore companies can be used as suitable instruments.

The final goal of such money transfers is the dispersal of money and earnings and the laying of as many paper-trails as possible to confuse ongoing supervision or future investigations and finally, the making of an artificial origin or source of money. (Lilley, 2000:53).

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[1] The Financial Crimes Enforcement Network

[2] This is why Law and by-laws and the education of compliance officers and employees that work with clients directly should be based on due diligence measures and on the collection of data on the purpose and nature of the business relationship as well as on ongoing tracking of business relationships and transactions. Furthermore, identification of the beneficial owner and undertaking all necessary measures, dependent on the risk and type of client, business relationship, product or transaction, are extremely important.

[3] The nature of sublimation as such gives opportunities for the detection of certain features indicating possible money laundering: financial transactions without logical bases, the frequent buying and selling of goods that generate commission. Accounts made up of smaller, linked accounts, lack of interest in losses during investments, bank costs or adviser commissions. The money launderer is only interested in profit as a secondary goal and the concealment of the real source of money is the only motive.

And finally, *in the phase of integration,* money launderers integrate their proceeds into the economic and financial system and mix them with lawful proceeds in order to make detection of the real source of money harder (Maros, 1999:242).

The final phase of the money laundering process is actually the integration of the illegally acquired proceeds, which have become legal and successfully embedded in the financial system. This phase is sometimes called the drying or centrifuging phase (Blunden, 2001:24).

Money laundering is a complex system which is still developing; new techniques have been used and money launderers are becoming more and more sophisticated. Criminals hide themselves behind complex transactions, which include international transfers, dispersion into smaller amounts or transfers made to the accounts of different persons, changing the shape of money and advice received from banking experts, brokers, investment bankers, accountants, consultants, public notaries and lawyers.

The money laundering process never stops. Yet regardless how many phases dirty money passed through and how many forms it takes, such proceeds will never be legal in the sense of the law (Claessens, 2000:23).

1.1 What is money?

Money is a conception. The idea that a determined value can be ascribed to some object used for trading is very old and universal (Madinger and Zalopany, 1999:7).

Money is very old tool, but the view of it as a reliable artefact, something to be accepted unconditionally and without further verification, has appeared only sometimes in its long history. Actually, such a viewpoint was established only during the last century (Galbraith, 1986:18).

All people have their own views of money and it is natural that such meanings differ, especially in different cultures.

A clear understanding of the money laundering process requests an understanding of the nature and role of money itself. Money is most often considered as cash. How much is one kuna, dollar or euro really worth? Maybe a better definition would be "everything that is generally considered as cost-covering instrument" (Madinger and Zalopany, 1999:8).

Money appeared thousands of years before paper and coins, but it is impossible to know who had the idea of giving a determined worth to some object and thus giving it such an important place in the trading process (ibid, 1999:9).

So, money is the concept that a certain object could have a certain worth and could be accepted in a different kind of swap. As a concept, money can have a shape. In different times and different places, money can be everything we could imagine (ibid, 1999:9)

Why is all this so important for the prevention of money laundering? We have to be aware that, although most money laundering processes include particular types of money only, *everything* can be used in the money laundering process: diamonds, gold, credit cards, shares, guarantees, rare coins, insurance polices and many other types of repositories of value. The process is limited only by the imagination of the individual, not by the form in which money appears.

1.2 Definition of money laundering

It is not surprising that "the legislative premiere" took place in the USA in 1986 when Washington State adopted its Anti-Money Laundering Law. This Law strictly punished non-reporting in the case of cash transactions above 10,000 dollars. It is mentioned in the literature that the term "money laundering" was for the first time promoted by *The Guardian,* 30 years ago during Watergate. It was about the amount of 200,000 dollars used for the purpose of financing the Republican election campaign.

In the early 80s the term was included into the documents of the Council of Europe (Giunio, 1998:40).

Considering that money laundering is usually performed in three phases, crosses state borders and includes smaller or bigger groups of people established ad hoc or for permanent activities and that different predicate offences go before the laundering, one can see the complexity of the money laundering process itself. Therefore, there are different definitions of money laundering in the literature:

- Money laundering is every kind of technique directed to the transformation of unfairly and illegally acquired proceeds in order to make it appear legitimate (Heršak, 1992:741).
- Money laundering is an activity directed to the collecting of unfairly or illegally acquired proceeds through legal businesses (Vukelić, 1994:29).
- Money laundering could be in brief defined as the transformation of illegally acquired proceeds in such a way that they seem legitimate (Novoselec, 1996:41).
- Money laundering includes activities directed toward covering the value of proceeds acquired by criminal activities and the inclusion, lodgement and disposition of objects such as money, securities and jewels in order to make them appear legal (Giunio, 1998:40).
- Money laundering is a financial transaction made for the promotion of some illegal activities or for covering illegally acquired incomes (DeGabrielle, 2001:192).
- The term money laundering means changing the shape of illegally acquired money to impart to it the appearance of legality. This also includes covering the illegal source of money and its use (Claessens, 2000:22).
- Traditionally, money laundering is (among other things) the cleaning of dirty money derived from illegal activities, in the collective awareness most often related to drug trafficking (Lilley, 2000:1).

2 International acts

The international community adopted range of Conventions, Recommendations and Directives as a result of raised awareness about threats from organised crime, recognition of money laundering phenomena as a danger to economic stability, and also because it was considered that uncovering and preventing money laundering would be efficient instruments in combating organised crime. Among other instruments, the following deserve particular attention:

UN Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances (Vienna, 1988) that deals with this issue and determines the fight against drugs by the seizure of proceeds from the illegal production of or trafficking in drugs. The Convention also promotes international cooperation among signatories.

The Vienna Convention is particularly important because it was the first document that provided sanctions for money laundering, although punishment was related to a limited number of predicate offences only (drug trafficking) (Condemi & Pasquale, 2005:42).

Convention 141 of the Council of Europe on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime (Strasbourg, 1990.) which prescribes the obligation of seizing the profit derived from illegal activities. The main part of the Convention is an article related to international cooperation. Article 18 deals with the obligation of cooperation in the investigations, endorsement and application of provisional measures for seizure and confiscation related to procedural questions on requests which member states send to each other. This Article defines grounds for refusal as well (Condemi & Pasquale, 2005:44-45).

Convention on laundering, search, seizure and confiscation of the proceeds from crime and on the financing of terrorism (ETS 198) which, among other things define:

- the Financial Intelligence Unit (in the following text FIU), the obligation of establishing such a unit and ensuring that it has access to information equal to the FATF Recommendation 26[4],
- possibilities for postponement of suspicious domestic transactions and for international cooperation regarding the postponement (postponement could be requested by the FIU or other competent authorities if there is a suspicion of money laundering or terrorist financing. All of this is aimed at analysing transactions and confirming suspicions),
- cooperation between FIUs when they collect, analyse or investigate relevant information concerning any fact that could lead to money laundering or terrorist financing.[5] FIUs have to cooperate regardless of their internal status and type of structure,
- an FIU can refuse to supply data if such information could jeopardise a criminal investigation being conducted in the country which has received such a request, or when disclosure would be in disproportion with the legitimate interests of some physical or legal person or if it is not be in line with basic principles of domestic law in this country. Refusals must be justified.

40 + 9 Recommendations of the Financial Action Task Force (FATF), a body whose purpose is the development and promotion of policies to combat money laundering and

[4] Countries should establish FIUs as national centres for receiving (and, if allowed, requesting), analysing and forwarding of suspicious transactions reports and other data regarding potential money laundering or terrorist financing. An FIU should have access, directly or indirectly to the financial, administrative and security data of the law enforcement bodies for properly undertaking its functions including the analysis of STR.

[5] FIUs should exchange information either spontaneously or upon request related to money laundering and terrorist financing as well as data on physical or legal persons that might be important. Every request must have in an attachment a summary of the important facts. For supply of the data to third parties, the previous agreement given by the originating FIU is needed.

terrorist financing in developed world countries, have to be emphasised: enlargement of reporting institutions to non-financial institutions, identification of beneficial owners, undertaking due diligence measures, feedback information, reporting, supervision, regulation of suspicious transactions and international cooperation. The revised Recommendations got their final form at the 16th Plenary meeting (Berlin, 2003) where new standards for the prevention of and fight against money laundering and terrorist financing were adopted (Condemi and Pasquale, 2005:401).

EU Directive on Prevention of Use of Financial System for the Purpose of Money Laundering (1991/308/EEC, 2001/97/EC and 2005/60/EC) which prescribes client identification, client due diligence, verification and supervision of client-beneficial owner, cash limits, recognition of linked, illogical and suspicious transactions, reporting obligations, prohibition of announcing such information, maximal protection of employees in financial institutions in case of breach of any restriction on disclosure of information, training for staff, risk management, record and statistics keeping, supervision and sanctions.

Regulation 1781/2006 on information on the payer accompanying transfer of funds with the aim of preventing, investigating and detecting money laundering and terrorist financing.

For the implementation of FATF special recommendation No 7[6] which aims to improve the transparency of all kind of e-money transfers inside or outside a country, by making it easier to conduct legal measures in order to follow electronic money transfers made by criminals and terrorists. It entered into force on January 1, 2007.

According to the Directive, an institution which conducts transactions must have complete information on the payer, its name, address and account number when money is transferred electronically.

Furthermore, the Directive stipulates the obligation to verify all data gathered on the payer on the basis of documents, data and information available from reliable and independent sources.

In order to gather all data about the payer, the proceedings, risk management and obligation of reporting to the FIU on suspicious transactions have been stipulated for institutions which conduct transactions, intermediaries and recipients.

Finally, the obligation of data and information storage with respect to the payer has been stipulated, together with the obligation of cooperation with bodies involved in the fight against money laundering and terrorist financing, effective, proportionate and dissuasive sanctions as well as the conduct of efficient supervision.

Prevention of money laundering and terrorist financing including its legal, financial and supervision aspects has been stipulated by the international legal acts. International Conventions, Directives and Recommendations, led by the basic idea of the prohibition of

[6] FATF VII special recommendation on electronic (money) transfers. States have to undertake measures requiring that financial institutions including money remitters include valid data on: sender (name address, account number), money transfers and messages related to the transfers, which must connected with each other when passing through the payment chain. States have to undertake measures to ensure that financial institutions including money remitters conduct enhanced control and supervision of suspicious transfer activities that do not contain full data about the sender (name, address, account number).

money laundering and terrorist financing stipulate: seizing illegally derived profit, manner of implementing of the measures and activities in order to identify and report to the FIU, information exchange with other countries and international legal aid.

3 The law on the prevention of money laundering

The Croatian Law on the Prevention of Money Laundering[7] stipulates measures and actions in banking, money and other economic operations to be undertaken for the purpose of detecting and preventing money laundering and terrorist financing. Thus, the Law has a preventive character.

It is important to mention that all articles refer to the prevention of money laundering and terrorist financing, which is not stated directly, but derives from the regulations of the Article 1, Paragraph 1 of the Law.

The Law stipulates reporting entities measures and activities which must be performed according to the Law. The Law also stipulates the activities and operations of the Anti-money Laundering Directorate (in the following text, the Office) in detecting suspicious transactions that conceal illegally derived money and assets or rights that are suspected of having been illegally acquired within or outside country.

3.1 Reporting institutions

Article 2 Paragraph 1 of the Law stipulates that obliged legal entities and the responsible persons within those entities, as well as physical persons obliged to take measures and actions aimed at the detection and prevention of money laundering according to the Law are: banks and home loan savings banks, savings and loan cooperatives, investment funds and investment fund management companies, pension funds and pension fund management companies, the Financial Agency and the Croatian Post Office, the Croatian Privatization Fund, insurance companies, stock market and other legal persons authorised to perform financial transactions with securities, authorised exchange offices, pawnshops, organizers of lottery games, casino games, betting games and slot machine games.[8]

The obligation has been expanded to cover subsidiaries in foreign countries (for example of the banks, insurance companies) and obliged persons that have a majority ownership of financial institutions or control financial institutions in foreign countries that do not implement standards for the prevention of money laundering.

Reporting entities-Reporting Institutions are also deemed to be all other legal persons, traders and individuals, business persons and physical persons if carrying out an activity related to transactions referring to receipt of money deposits, selling and purchase of debits and credits, management of the property of a third party, issuance of credit and debit

[7] NN, 69/97, 106/97, 67/01, 114/01, 117/03 and 142/03.

[8] The Customs Administration has the status of special reporting entity obliged to inform the FIU, according to Article 9, Paragraph 1, of legal transfers or attempts at illegal transfer across state borders of cash or checks in domestic or foreign currency in the amount of 40,000 Kuna or more no later than three days upon receiving information concerning such a transfer. The report must contain data about the person, place and time of the border crossing and all other information about the money transfer.

cards, transactions with such cards, leasing, travel agencies, organizers of auctions, trade in real estate, art objects, antiques and other items of significant value as well as tasks of processing, and trading with precious metals and gems.

According to the most recent amendments to the Law (NN 117/03) reporting entities are also lawyers, law firms, public notaries, audit companies, certified auditors, legal and physical persons performing accountancy and tax advisory business. These amendments are aligned with Directive 2001/97/EC on the prevention of the use of the financial system for the purpose of money laundering.[9]

All reporting entities according to Article 15 of the Rules on implementation of the Law (in the following text: the Rules[10]), must appoint a natural person responsible for the implementation of the Law.[11]

This natural person will conduct its activities in cooperation with the "network" of responsible persons in the lower-level organizational units of the same reporting entity. This person is responsible for cooperating with the FIU and for undertaking all measures for detection and prevention of money laundering.

3.2 Client identification

Client identification at the time of the opening of an account or establishing other forms of permanent business cooperation is one of measures undertaken by a reporting entity aimed at the detection of money laundering:

- during each transaction made in cash, foreign currency, securities, precious metals and gems if the value of the transaction is 105,000 kuna or more,
- during linked transactions that together attain a value of 105,000 kuna or more,
- insurance companies verify client identity in the life insurance business if the annual premium exceeds 40,000 kuna,
- during all other cash or non-cash transactions if there is a suspicion of money laundering.[12]

[9] Taking into account the specific purpose of their operations and specific relations with the clients (for example lawyer-client confidentiality in judicial and administrative proceedings) and considering that they are not obliged to report on cash transactions related to the threshold except if there is a suspicion of money laundering or when they are being asked for advice connected to money laundering. These professions are separate from other obliged persons and constitute a special whole.

[10] NN 189/03 in the implementation from January 1, 2004.

[11] Reporting entities report to the FIU by their compliance officers concerning all cash or non cash transactions according to the Law. If they do not designate a compliance officer, then the responsible person within the legal person is also responsible for the mentioned area.

[12] Based upon Article 25 of the Rules, identification of the obliged persons acting as a clients is not necessary except if there is a suspicion of money laundering in following cases:
– when performing transactions between banks, saving banks, the Financial Agency, Croatian Post and insurance companies
– when performing transactions between banks and authorised exchange offices related to the purchase of foreign cash and cheques, or accepting foreign cheques in order to cash them
– when a bank transfers abroad foreign currency to its account in a foreign bank or transfers abroad foreign checks in order to cash them in foreign bank.

Furthermore, identification is not necessary if the client draws cash from its current account, drawing account or ordinary account for the purpose of purchasing or depositing foreign currency. The main condition for the exception is the simultaneity of such transactions.

By inclusion into international financial flows, Croatia is exposed not only to legal investments but also to transactions with unknown sources of money and identities of the person standing behind the transaction, as well as to investments the money for which came from offshore zones.

According to Directive 2005/60/EC (in the text below: Third Directive) and the FATF Recommendations, the Law stipulates that reporting institutions must ask the client for a statement concerning the beneficial owner of the legal person and the list of members of the Board during the opening of an account or during the establishment of a permanent business relationship.

The way in which the beneficial owner is to be identified is prescribed in detail by the Rules.[13]

3.3 Reporting to the anti-money laundering directorate

Article 8 of the Law stipulates the obligation of supplying data gathered by the reporting entity (about the client and transaction) to the FIU in the case of cash transactions, foreign currency transactions, transactions with securities, precious metals and gems and in case of linked transactions amounting to 200,000 kuna or more.

The identification threshold is 105,000 kuna, and for all transactions amounting to from 105,000 to 200,000, the reporting entity has to keep records.[14] For these transactions, the client is not obliged to report to the Office but the records have to be available to the Office at its request.

Reporting institutions have to report on transactions related to life insurance business if the annual sum of premiums exceeds 40,000 kuna. A reporting institution will also report on the amount related to the identification threshold in the manner prescribed by the Law.

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[13] Article 3 of the Rules clearly defines the way of identifying the beneficial owners. That is, the reporting institution is obliged, during the opening of an account or the establishment of any permanent business relationship, to ask the client for a statement on the beneficial owner and the list of the members of the Board.

If there is no possibility of verifying the beneficial owner's identity as a natural person, the reporting institution will accept a statement where a legal person is stated as the beneficial owner (name of the legal person, residence, country and register number must be stated). This legal person must be registered in countries which apply international standards in the area of the prevention of money laundering. However, for the clients registered in *off-shore* zones and non-cooperative countries, data on beneficial owner-physical person is necessary at the opening of an account or when establishing a business relationship.

If there is a doubt concerning change in the management/ownership structure, the reporting entity is obliged to ask the client for a new statement on the beneficial owner. The reporting institution will not be able to open an account or establish a permanent business relationship for a client that has not submitted a written statement on the beneficial owner, members of the Board or if the statement consist of uncompleted data, and there is no data on management-ownership structure. If the reporting entities ask the client for the new statement and the client does not forward the statement or submits an incomplete statement, the reporting institution is obliged to close the account or to break off the business relationship with the client

[14] Based upon the Article 21 of the Rules, reporting institution is obliged to maintain a list of conducted transactions amounting from 105,000 to 200,000 kuna for which there is only an obligation to identify, and another about transactions that exceed 200,000 kuna, which must be reported to the office. Data regarding identifying the client that performs the transaction, and regarding the transaction as a such, must be stored by a reporting institution in its records chronologically and in such a way as to enable efficient supervision by the authorized bodies. The reporting institution has to make possible fast and complete submitting of data related to the clients and transactions upon the request made by the Office.

Furthermore, the reporting entity will submit to the Office reports on all other cash and non-cash transactions if there is any suspicion of money laundering regardless of the amount and the type of transaction.[15]

Similarly, reporting institutions have to report to the Office on the transactions they refused to perform even if they have not identified the client or gathered all the data related to the transaction according to the Law.

In such cases, data and information gathered about such transactions have to be attached to the reports.[16]

3.4 Confidentiality of proceedings and data

According to Article 15 of the Law, all data gathered pursuant to this Law are confidential and can be used only for the detection and prevention of money laundering and crimes related to money laundering.[17]

Data gathered through international cooperation can also be used only for the detection and prevention of money laundering. For them to be used by the police and in court proceedings, agreement given by the foreign Office is needed.

Pursuant to Article 17 of the Law, the Office and the reporting institution must not notify the customer about information that has been gathered (and that pertain to such a person) or about procedures initiated according to this Law. Such data can be provided only upon a court order.

So, protection of the information and proceedings is one of the main features, since the reports received by the Office contain bank secrecy data and personal data related to suspicions of money laundering that may be unjustified.

The Office may provide information to the client to whom the information pertains, but only at the request of that client ten years after the information has been collected.

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[15] Taking into consideration that, the analytical work of the Office indicates that a certain transaction has no very great importance in the data analysing process. Article 24 of the Rules stipulates that reporting entities have no obligation to report to the Office on cash transactions intended for the deposit of the daily proceeds from selling goods or services unless if there is a suspicion of money laundering.

[16] If the conditions prescribed by the Law regarding the conducting of transactions are not fulfilled, the reporting institution will refuse to perform such a transaction. If there is no possibility of identifying the client during the conducting of any transaction prescribed by the Law, the transaction will not be conducted.

Furthermore, if the reporting institution cannot gather all the necessary data about the client (physical or legal person) and the transaction, the transaction will not be carried out. It is important to stress obligation of the reporting institution at the time of opening of account or establishing other forms of permanent business cooperation to ask the client for a statement concerning the beneficial owner of a legal entity and the list of members of the Board. If the client does not want to fulfill this obligation or sign such a statement, and reporting institution does not know the owner-management structure, the reporting institution will refuse to open an account or to establish business relationship with the client.

As a third case, reporting institution will refuse to conduct a transaction made by the client on behalf of a third party and when the client does not want to or cannot enclose written power of attorney that confirms what has previously been alleged.

[17] Predicate offences are in fact criminal offences from which illegal money is derived.

4 The harmonisation of domestic legislation with international standards

The fight against serious crime is becoming more and more an international issue, which requires the use of modern and efficient methods both nationally and internationally.

Amendments to current legislation or the adoption of a new Law on the prevention of Money Laundering and Rules for its Implementation are needed for the further harmonisation of the legislation of the Republic of Croatia with the international standards in the area of prevention of money laundering.

First of all, harmonisation with the Third Directive, 40+9 Revised FATF Recommendation, Warsaw convention and Regulation No 1889/2005 on the control of cash entering and leaving the Community is needed.

Alignment with the Third Directive and 40+9 FATF recommendations includes the area of client identification, beneficial owner identification and client due diligence (improved and simplified).[18]

Considering the importance of client identification in the process of the prevention of money laundering and terrorist financing, there is a need for further determination and verification of client identity, determination of the beneficial owner and the undertaking of adequate measures according to the risk and the type of client, business relationship, product or service, with the aim of a clear understanding of beneficial owner and of composing a mosaic of ownership structure as well as the control over the client.

Equal importance is given to the gathering of data about the purpose and nature of the business relationship as well as to permanent monitoring of the business relationship and transactions, aiming to ensure that operations are conducted according to knowledge about the client, its business and risk profile, including the source of money.[19]

In high-risk situations as regards money laundering and terrorist financing, it is necessary that financial institutions and the non-financial sector should undertake measures of client due diligence, especially when the client is not physically present, in the case of cross-border banking correspondent relationships and in transactions and business relationships with politically exposed persons.[20]

Furthermore, it is necessary to stipulate that reporting entities and all other bodies involved in the process should keep comprehensive records and statistics. This should contain statistics on suspicious transaction reports (STR) received and forwarded, activities which follow up on such reports and especially the number of investigations, prosecutions and convictions for incidences of money laundering or terrorist financing, data about frozen, seized and confiscated property and on mutual legal assistance or other international requests for the cooperation.[21]

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[18] According to Third Directive, due diligence measures are implemented when establishing business relationship, when performing transactions amounting 15,000 euros or more if there is a suspicion of money laundering or terrorist financing as well as in the case of suspicion of the accuracy and adequacy of previously gathered data regarding the client identity.

[19] Article 8, Third Directive and FATF Recommendation No 5.

[20] Article 13, Third Directive and FATF Recommendations No 6,7,8.

[21] Article 33, Third Directive and FATF Recommendation No 32.

The Office has to establish the main principles and measures that ensure annual feedback to the reporting entities on the effectiveness of forwarded STRs, and the activities undertaken after such reports. Feedback will help financial institutions and non-financial sectors and professions in the implementation and development of measures for the prevention of money laundering and terrorist financing as well as for the detection and reporting of suspicious transactions.[22]

Apart from this, primary and secondary legislation have to be amended in order to ensure that exchange offices, gambling houses, and money remitters are licensed, registered and supervised in order to prevent money laundering. Such measures would prevent criminals or their associates holding companies or becoming beneficial owners of a significant or controlling interest, holding management functions in, or being the operator of such institutions.[23]

Financial institutions and their directors and officials have to be protected by legal provisions from criminal and civil liability for breaches of any restriction on the disclosure of information imposed by contract or by any legislative, regulatory or administrative provision if they report their suspicions in good faith to the Office, even if they do not know precisely what the underlying criminal activity is and regardless of whether illegal activity has actually occurred. The Law must prohibit disclosure of the fact that a suspicious transaction or some related information was reported to the Office.[24]

In conclusion as regards new penalties in the law, it is necessary to ensure that effective, proportionate and dissuasive sanctions, whether criminal, civil or administrative, are available to deal with natural or legal persons covered by these Recommendations that fail to comply with anti-money laundering or terrorist financing requirements.[25]

Alignment of the Law with Regulation 1889/2005 on the control of cash entering and leaving the Community is related to the harmonisation of law and forms for transferring of cash or checks over the state borders in domestic or foreign currency amounting to 40,000 kuna or more. Such a form is used by the Customs Administration when reporting to the FIU in terms of reporting limits, the obligatory elements, the forwarding of data to foreign bodies and on record keeping and data analysis.

5 Anti-money laundering directorate (the office)

The Anti-Money Laundering Directorate (the Office) is an independent organisational unit established within the Ministry of Finance. Its internal structure is stipulated by the Regulation on the Internal Structure of the Ministry of Finance.

According to international standards, the Croatian Office is a financial intelligence unit and analytical service which operates on the basis of prevention in the area of money laundering and analyzes data gathered from reporting entities according to the Law; it

[22] Article 35, Third Directive and FATF Recommendation No 25.

[23] Article 36, Third Directive and FATF Recommendations No 23 and 24.

[24] Article 26 and 27, Third Directive and FATF Recommendation No 14.

[25] Article 39, Third Directive and FATF Recommendation No 17.

also delivers suspicious transaction reports (STR) to competent state bodies (State Attorney Office, USKOK, and/or Ministry of Interior) and foreign Offices.[26]

5.1 Scope of competences and internal structure of the office

According to the Regulation[27] the Office is an independent internal unit within the Ministry of Finance established on the basis of the Law on the Prevention of Money Laundering as an administrative type of financial intelligence unit that collects, analyses and stores data on transactions stipulated by the Law and gathered by the reporting entities with the aim of the prevention and detection of money laundering and terrorist financing. The Office:

- delivers suspicious transaction reports (STR) to competent state bodies for further action and together with the mentioned bodies undertakes measures for the prevention of money laundering and terrorist financing,
- performs administrative supervision of reporting entities with respect to enforcement of the law within its remit,
- exchanges information on suspicious transactions with counterpart bodies and services which prevent money laundering in particular countries, based on the existence of reciprocity,
- performs other matters important for preventive strategy development in the area of the prevention of money laundering.

The Office consists of the Prevention Department and the Analytic Department.

5.1.1 Prevention department

The Prevention Department conducts professional and administrative business together with the obliged persons determined by the Law and proposes and monitors the development of preventive strategy in this area.

One of the main duties of the Department is the development and monitoring of a list of indicators for the purpose of recognizing suspicious transactions and interpretations related to practical implementation of the Law and by-laws.

Employees of the Department, with the aim of alignment with international standards, write laws and by-laws and internal instructions from the area of the prevention of money laundering and the area of systematic protection of data and records made in the Office.

5.1.2 Analysis department

The main role of the Analysis Department is in the analysis of data received regarding cash and suspicious transactions based upon certain indicators, methodologies and specific expertise (so called group-intelligence analytics).

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[26] The Office mediates among, on the one hand, obliged persons from the financial and non-financial sector and, on the other hand, competent authorities which, after receiving suspicious transaction reports, determine the direction and dynamics of investigation into and the provision of proof concerning criminal activities.

[27] Rules on Internal Structure of the Ministry of Finance (NN 70/01).

The Head of Department, relying upon strategic analysis and investigation, proposes the analytical processing of new cases. Inspectors determine indications of money laundering and make links between a suspicion transaction and the particular criminal activity from which illegal money has been derived.

Through the exchange of information and data with international counterparts dealing with the prevention of money laundering and terrorist financing, the Department participates in international cooperation and analyses and follows trends in money laundering both domestically and internationally.

5.2 The secrecy of proceedings and data

Article 15 of the Law stipulates that all data gathered in accordance with this Law are considered confidential and secret and can be used only for the detection and prevention of money laundering or crimes related to money laundering.

Furthermore, Article 17 of the Law stipulates that the Office and reporting entities must not notify the customer about gathered records in procedures initiated in accordance with this Law. The Office can provide such information only upon a court order. The Office may give information to the client that the information pertains to, at the request of the client ten years after the data has been gathered. Protection of secrecy in the Office is stipulated by the Instructions for the Protection of Data Secrecy, proceedings with letters, protective measures for premises and documentation and observance of discipline in the Anti-Money Laundering Directorate.[28]

These Instructions first of all define the terms professional secrecy and secrecy of data, receiving and the protocol with post and the procedure with letters, supervision of entering and being in the Office as a measure for the protection of the working premises and the documentation.

Electronic data protection is regulated by the Guidelines Manual on Using and Obligatory Protective Measures for Intelligent IT system in the Anti-Money Laundering Directorate.[29] These Guidelines stipulate the system of certificated use of the system and protection of data gathered based upon the Law and Rules for the whole Intelligent Office IT system.[30]

Every Office employee has to sign a secrecy declaration. In this statement, persons commit themselves, under material and criminal liability, to keep data and information secrecy and secrecy of intelligence gathered through working in the Office. They also commit themselves not to inform, give or make such information available to third persons. The obligation to maintain data confidentiality pertains even after leaving the Office.

[28] Instructions came into force on December 18, 1998, in application from January 1, 1999.

[29] The Guidelines Manual entered into force on January 19, 2001, in application from February 5, 2001.

[30] Use of the Intelligent IT system includes strategic and operative analytic and visualisation with the final goal of detecting suspicious transactions by certain indicators and delivering STR to competent state bodies for further action. It includes connecting a suspicious transaction with the criminal activity of an individual, group or organisation including well-known typologies of money laundering.

5.3 International operations of the anti-money laundering directorate

As far as international cooperation in preventing money laundering and terrorist financing is concerned, in 1998 Croatia became a full member of the Egmont Group. Since international cooperation has great importance, the Office conducts it according to the Law and Memorandums of cooperation with foreign Offices.

5.3.1 Egmont group

The Egmont Group is an international network of national Financial Intelligence Units specialized in the combating of money laundering. The Egmont Group permanently promotes and supports mutual exchange of information and experience related to cases suspected of being money laundering operations (Condemi and Pasquale, 2005:161). In this group there are currently 101 national Financial Intelligence Units which deal with preventing and detecting money laundering.

One of the most important achievements of this group is the provision of secure Internet communication. Egmont's international secure Web system enables members to have mutual communication through protected e-mail, and this way makes practical and fast information exchange in the fight against money laundering easier. Although this way of communicating does not replace traditional channels used in getting court evidence, it can be of use for supervisory bodies in their investigations (DeGabrielle, 2001:202)

So, the main goal of the Egmont Group is the making of preconditions for the safe, fast and legal exchange of information in order to combat money laundering and to establish a central network for international cooperation among Offices. Aiming to provide a faster flow of information for the detection of money laundering, the Croatian Office has signed, memorandums of understanding with the Offices of Slovenia, Belgium, Italy, the Czech Republic, Panama, Lithuania, Macedonia, Lebanon, Israel, Bulgaria, Romania, Australia, Lichtenstein, Albania, Bosnia and Herzegovina, Montenegro, Poland, Serbia, Georgia and Ukraine.

Croatia is a full member of the Committee of Experts for the Evaluation of Anti-Money Laundering Measures (MONEYVAL).

5.3.2 Moneyval

Moneyval was established in 1997 as a PC-R-EV, as a Body for the evaluation of the measures conducted against money laundering within EU member states which are not FATF members. [31]

Moneyval's main purpose is to encourage countries to establish an efficient anti-money laundering and terrorist financing system as well as its alignment with adequate international standards.

These standards are part of the 40+9 FATF Recommendations, the UN Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances, Convention 141 of

[31] Moneyval members are: Albania, Andorra, Armenia, Azerbaijan, Bosnia and Herzegovina, Bulgaria, Croatia, Cyprus, Czech Republic, Estonia, France, Georgia, Hungary, Latvia, Lichtenstein, Lithuania, Malta, Moldavia, Monaco, Netherlands, Poland, Romania, Russia, San Marino, Serbia, Slovakia, Slovenia, Macedonia, and Ukraine.

the Council of Europe on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime as well as relevant EU Directives.

Moneyval experts delivered its Assessment Reports on the measures against money laundering related to particular Croatian institutions included in the fight against money laundering and terrorist financing together with the recommendations for improvement of the system and its alignment with relevant international standards.

The efficiency of the Croatian Office and other bodies involved in the prevention of money laundering was evaluated in 2000, 2003, and 2006. All moneyval reports are deemed confidential.

6 Concluding observations

Croatia has taken important steps in the fight against money laundering. It has ratified the Convention of the United Nations against Illicit Traffic in Narcotic Drugs and Psychotropic Substances (the Vienna Convention) from the year 1988 and Convention 141 of the Council of Europe on laundering, search, seizure and confiscation of the proceeds from crime from the year 1990. FATF Recommendations and EU Directives have been included into legislation.

Furthermore, in the year 1997, the Law on the prevention of Money Laundering and Rules for its implementation entered into force. The Law and the Rules keep up with trends in international legislation by the amendments that are made to them.

The international aspect of money laundering emphasises the importance of the Convention 141 of the Council of Europe on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime which stipulates general rules of international cooperation, as well as the Convention on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime and Terrorist Financing which discusses in more details and clearly defines rules of cooperation between the FIUs in terms of collecting, analysing and investigating all the relevant information on any fact that could suggest money laundering and terrorist financing.

For the purpose of alignment with international standards in the area of preventing money laundering and terrorist financing, there is a need to amend the current or to adopt a new Law on prevention of Money Laundering and Rules for its implementation.

The purpose of the aforementioned new Law would be first of all alignment with the Third Directive and 40+9 Revised FATF Recommendations in relation to client identification, identification of beneficial owner, client due diligence, keeping comprehensive records and statistics, feedback to reporting entities on the efficiency of reporting a suspicion of money laundering and protection of employees of financial and non-financial institutions when in a good faith they report to Financial Intelligence Unit.

The Croatian Office is an administrative type of Financial Intelligence Unit; it consists of a Prevention Department and an Analysis Department, which differ in their structures, but which are linked by their interconnected operations. Good prevention would ensure education of employees, resulting in turn in the better quality of reported transactions. *Off-site* supervision will *warn* reporting entities of business irregularities and

good IT support will make information available in the short term and make such analyses more clearly.

Quality of gathered data and quality of reports made by reporting entities based on risk assessment and related to money laundering and terrorist financing will result in better analytical work and in making better suspicious transaction reports which the Office delivers to competent authorities for further action.

And finally, it is important to stress that "smart obstacles" and cooperation of all bodies in the area of prevention and repression both nationally and internationally is crucial and one of the most efficient ways for the prevention of new opportunities for money laundering and terrorist financing created by the processes of globalisation.

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Convention 141 of the Council of Europe on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime.

FATF-a 40+9 Recommendations (40 recommendations related to money laundering and 9 special recommendations related to terrorist financing).

Instructions for protection of data secrecy, proceedings with letters, protective measures for the rooms and documentations and discipline keeping in the Anti-Money Laundering Directorate.

Regulation No 1889/2005 on controls of cash entering or leaving the Community.

Regulation on internal structure of the Ministry of Finance (NN 70/01).

The Guidelines Manual on using and mandatory protective measures for intelligent IT system in the Anti-Money Laundering Directorate.

The Guidelines of the European Parliament and Council (1991/308/EEC, 2001/97/EC i 2005/60/EC).

The Rules on the implementation of the Law on prevention of Money Laundering (Official Gazette No 189/03).

UN Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances.

Warsaw Convention (Convention of the Council of Europe on Laundering, Search, Seizure and Confiscation of the Proceeds from Crime and terrorist financing -ETS 198).

Zakon o sprječavanju pranja novca (NN 69/97, 106/97, 67/01, 114/01, 117/03, 142/03).