



IMPROVING THE SYSTEM FOR FIGHTING AGAINST THE LAUNDERING OF THE PROCEEDS OBTAINED FROM CRIMINAL ACTIVITIES IN BANKS

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Article history:		Abstract:
Received:	11 th January 2024	Every year, huge amounts of funds are obtained by illegal activities. These illegally obtained funds need a process, which is called laundering, in order to appear legitimately obtained and become usable. Although it is not possible to measure the exact volume of money laundering, the International Monetary Fund has stated that the aggregate amount of it in the world could be somewhere between two and five percent of the world's gross domestic product. The main vehicle for criminals to launder their illicit money is the financial system. Money laundering threatens the credibility of international financial institutions. It undermines the financial system and all of the countries integrated into the international financial system become exposed to the risk. The aim of this paper is to explain the relationship between the money laundering and financial system. It briefly examines money laundering from the perspective of financial system in the case of banks.
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INTRODUCTION

All operations in the economy of developing countries are carried out through banks, and of course risks arise in these operations. Risky operations carried out with the specific goal of achieving maximum profit in the activity of commercial banks will definitely lead to profit, and this is especially dependent on the decisions taken by the bank management. Cross-border financial crime is here to stay. While people everywhere enjoy the convenience of a globally connected financial system, criminals exploit this intricate network to move illicit funds across borders and evade capture. As these criminals protect their ill-gotten wealth derived from tax evasion, corruption, and drug trafficking, among others, financial crimes thrive. No financial institution or country is immune. Money laundering scandals caused bank collapses and shocked countries. Ultimately, society pays the cost through an erosion of trust in the integrity of the financial system, often leading taxpayers to subsidize failing banks and limiting customer access to credit.

Banks, as gatekeepers to the financial system, battle unceasingly against money laundering and terrorist financing. But national anti-money laundering efforts focus primarily on domestic risks, and as a result they often lag. Bank regulators also play a crucial role, but often don't make the best use of limited resources, and divergent approaches hamper effective global collaboration.

IMF staff partnered with eight Nordic and Baltic countries—Denmark, Estonia, Finland, Iceland, Latvia, Lithuania, Norway, and Sweden—in a first-of-its-kind anti-money laundering technical assistance project. Our findings reveal that combatting money laundering is beyond the capacity of any single nation—and that countries must innovate together to find a solution. IMF staff is constantly expanding the toolkit to help Fund members focus on cross-border illicit flows. Using machine learning technologies and data analysis, we scrutinize financial movements, gaining insights into the global landscape and identifying indicators of potential macro-critical money laundering scenarios. Our analysis features in the annual health checks of IMF member economies (e.g., Singapore 2022 Article IV consultation) and under the Financial Sector Assessment Program (e.g., UK 2022 FSAP). Collaborating with the Nordic-Baltic countries, we used these tools to improve countries' understanding of unusual financial flows warranting scrutiny. These tools enhance countries' ability to screen potential illicit financial flows and focus on emerging threats. Collaboration also allows countries to identify and connect seemingly disconnected cross-border money laundering and terrorism financing threats.

LITERATURE REVIEW

Taking a broader perspective, our study of the supervisory frameworks within the Nordic-Baltic region



led to recommendations at both country and regional levels.

As main gatekeepers of the financial system, banks must prevent and detect money laundering. Criminals find banks alluring due to their extensive cross-border networks, interbank ties, and products and services that open themselves up to the risk of money laundering. A parallel borderless trend is the rise of crypto assets, offering speedy global transfers attractive to criminals.

That is why it's imperative that national regulators who supervise banks' anti-money laundering efforts are able to look at the bigger picture when overseeing them. With a global supervisory mechanism lacking, supervisors need to broaden their perspective, scrutinizing non-resident risks and inter-border laundering countermeasures. This calls for stronger international collaboration, a point emphasized by IMF staff (e.g., Euro Area Article IV consultation).

Going forward, while good practices are emerging in cross-border transaction data collection and analysis, the integrated banking system calls for greater cross-border data collection to better understand and mitigate these risks. Technological solutions can aid in analyzing this information to create a regional picture for targeted supervisory efforts, including multi-country initiatives. Countries should also exchange data on money laundering incidents, while also delving deeper into the need for banks to bolster capital reserves against associated losses.

MATERIALS AND METHODS

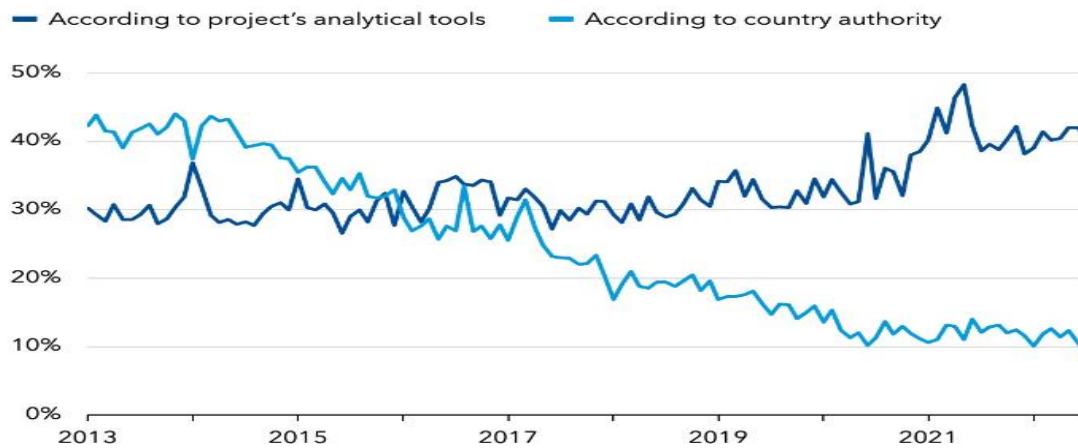
They may have negative consequences for a country's financial stability and macroeconomic performance, resulting in welfare losses, draining resources from more productive economic activities, and even having destabilizing spillover effects on the economies of other countries. In an increasingly interconnected world, the problems presented by these activities are global, as are the links between financial stability and financial integrity. Also the opinions of some other researchers and experts can be summarized as follows;

- One of the most serious microeconomic effects of money laundering is felt in the private sector. Money launderers often use front companies, which co-mingle the proceeds of illicit activity with legitimate funds, to hide the ill-gotten gains. In some cases, front companies are able to offer products at prices below what it costs the manufacturer to produce. Therefore, front companies have a competitive advantage over legitimate firms that draw capital funds from financial markets. This makes it difficult, if not impossible, for legitimate business to compete against front companies

with subsidised funding, a situation that can result in the crowding out of private sector business by criminal organisations. The management principles of these criminal enterprises are not consistent with traditional free market principles of legitimate business, which results in further negative macroeconomic effects (Mc.Dowell and Novis, 2008:7).

- Financial institutions that rely on the proceeds of crime have additional challenges in adequately managing their assets, liabilities and operations. For example, large sums of laundered money may arrive at a financial institution but then disappear suddenly, without notice, through wire transfers in response to non-market factors, such as law enforcement operations. This can result in liquidity problems and runs on banks. In some emerging market countries, illicit proceeds may dwarf government budgets, resulting in a loss of control of economic policy by governments. Indeed, in some cases, the sheer magnitude of the accumulated asset base of laundered proceeds can be used to corner markets or even small economies. Money laundering can also adversely affect currencies and interest rates as launderers reinvest funds where their schemes are less likely to be detected, rather than where rates of return are higher (Mc.Dowell and Novis, 2008:4-7).

- Money laundering can increase the threat of monetary instability due to the misallocation of resources from artificial distortions in asset and commodity prices. The unpredictable nature of money laundering, coupled with the attendant loss of policy control, may make sound economic policy difficult to achieve. It also diminishes government tax revenue and therefore, indirectly harms honest taxpayers. It also makes government tax collection more difficult. This loss of revenue generally means higher tax rates than would normally be the case if the untaxed proceeds of crime were legitimate. Countries cannot afford to have their reputations and financial institutions tarnished by an association with money laundering, especially in today's global economy. Confidence in markets and in the signalling role of profits is eroded by money laundering. The negative reputation that results from these activities diminishes legitimate global opportunities and sustainable growth while attracting international criminal organisations with undesirable reputations and short-term goals. This can result in diminished development and economic growth. Furthermore, once a country's financial reputation is damaged, reviving it is very difficult and requires significant government resources to rectify a problem that could be prevented with proper anti-moneylaundering controls (Mc.Dowell and Novis, 2001:8)



Source: IMF staff calculations.

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1-figure. Money Laundering and Abuse of the Financial System

As commercial banks use the main part of their funds as lending, it is necessary to determine in advance the issue of full recovery of the funds from the borrower, not just for income. Because the bank, as the owner of the investment, does not sell the investment, but the right to use the investment for a certain period of time based on certain conditions and premium interest. At the moment, the concept of "problem credit" is causing much more debates and discussions by theoretical and practical scientists in our country than before. This is certainly not in vain, because today the share of problem loans in the credit portfolio of commercial banks of our republic is quite high, despite the measures to reduce it. 1 On the strategy of reforming the banking system of the Republic of Uzbekistan for Today, due to the fact that many countries are facing the problem of increasing bad debts in the banking system, the urgency of improving the system of working with problematic loans of banks is still gaining importance. Therefore, there are unsolved problems related to credit repayment by clients as well as creditors.

RESULTS AND DISCUSSION

Financial abuse has the broadest meaning, encompassing not only illegal activities that may harm financial systems, but also other activities that exploit the tax and regulatory frameworks with undesirable results. When financial abuse involves financial institutions or financial markets, it is sometimes referred to as financial sector abuse. Financial crime, which is a subset of financial abuse, can refer to any non-violent

crime that generally results in a financial loss, including financial fraud. It also includes money laundering (Boorman and Ingves, 2001:3). Financial institutions such as banks insurance companies, securities firms and financial investment management firms are particularly vulnerable to the money laundering. Illegal money must be integrated into the legitimate financial system in order to be laundered. Money laundering can be done with or without the knowledge of the financial institution. Financial institutions may have three roles in money laundering; as a perpetrator, as a victim and knowing or unknowing instrumentality of crime. Money laundering affects financial institutions in a legal sense because of the obligations placed on them by legislation and financially because of the need for compliance. With the dismantling of exchange controls and the growing interpenetration of financial markets, access to one country's financial institution allows worldwide mobility of capital. Any country integrated into this global financial system is at risk of money laundering. Because of that, money laundering activities can occur in any country, but they may have a more significant impact on developing countries with relatively small or fragile financial systems or weak economies that are particularly susceptible to disruption as a result of illicit activities. They damage critical financial sector institutions and they may scare away foreign investors and reduce a country's access to both foreign investments and foreign markets (Humphrey, 2007:7). Money laundering is a complex economic crime which has many negative effects on the increasingly interconnected growing financial systems of the world.



It cannot be effectively controlled without the international cooperation of finance ministries, central banks, financial institutions, and financial regulators. But, the legal enforcement and punishment is the most effective measure against money laundering. In this respect, countries must criminalize all forms of money laundering, and establish efficient mechanisms and institutions capable of enforcing regulations. Second, in order to prevent them from being used by criminals for money laundering the financial institutions should; (i) know and record the true identity of their customers (know your customer), (ii) record the details of transactions (record keeping), (iii) report suspicious transactions and activities (reporting information), and (iv) respond to information requests from appropriate government authorities

CONCLUSION

The criminals need a process in order to use efficiently the money which is generated from their criminal activities. This process is called "money laundering" by which huge amounts of illegally obtained funds are given the appearance of having originated from a legitimate source. Money launderers, who are sometimes assisted by financial experts, can use highly sophisticated methods in order to introduce illegally generated money into legal economic flows. Money laundering threatens the credibility and effectiveness of financial systems and it has many negative effects on countries' economic structures. It may cause serious macroeconomic distortions and misallocation of resources and capital around the world, and hinder economic growth and reputation. The banking system is one of the most important vehicles for money laundering. There are certain banking instruments that appear potentially susceptible and exposed to various abuses related to money laundering such as electronic payment systems, wire transfer and electronic money transfer, branchless banking, private banking, correspondent banking and offshore banking. The complexity and international nature of the banking system allow money launderers to hide their illegal funds. The criminals use the banks to transfer the funds securely, quickly and with the appearance of legitimacy.

The laundering can happen in every country quickly, easily, with the ability to transferring money through several countries by these banking instruments. International cooperation is necessary to fight against money laundering which is also an international problem. It cannot be effectively controlled without the international cooperation of finance ministries, central banks, financial institutions, and financial regulators. The legal enforcement and punishment is the most effective measure against money laundering. In this respect, countries must criminalize all forms of money laundering, and establish efficient mechanisms and institutions capable of

enforcing regulations. In order to prevent them from being used by criminals for money laundering the financial institutions should; know and record the true identity of their customers, record the details of transactions, report suspicious transactions and activities and respond to information requests from appropriate government authorities. As a result, finance ministries, central banks, financial institutions, and financial regulators worldwide must continue to focus on money laundering and the efforts to combat financial abuse, including money laundering must be strengthened.

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