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Money Laundering risk in criminal connected firms: the Emilia-Romagna, Liguria and Piemonte cases

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Firma dello studente

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A coloro che sempre mi hanno sostenuto,
la mia famiglia

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Introduction

Money laundering is one of the most critical things that worry governments, both those who are rich and those who are poorer; in particular, this phenomenon has always been a big problem for Italian economy. In Italy the dangers of laundering are considerable because of the diffusion and pervasiveness of organized crime, the corruption and tax evasion. It is not only a problem in terms of crime, but it is a characteristic that weakens the economy and prevents social development, discouraging investment[1]; for example, it should be noted how organized crime reduce total population's income, because of the so called "*pizzo*". Extortion, as well as directly subtract resources to entrepreneurs subject to racketeering, disincentives any investment in local economy. An economy that is mafia infiltrated is distorted by many ways: a merchant victim of the racket may consider "*pizzo*" as a compensation for a protection against competitors; moreover, laundering of criminal proceeds into legal economy imposes a competitive disadvantage to companies that do not benefit from this source of cheap money; finally, the links between criminal groups and corrupt public administration affect the provision of goods and services.

The impact on economic growth of the perception of corruption and the lack of confidence that goes with it can be even more serious than those resulting from the corruption itself. As it is reported in the National Risk Assessment, according to a recent analysis conducted by World Bank, every point down in the ranking of Transparency International corruption perception causes the loss of 16% of foreign investments. Moreover, a study of Unimpresa[2] shows that the phenomenon of corruption in Italy decreases foreign investment by 16% and increases of 20% the sum of contract costs.

The set of laws introduced by each country involve both the aspect of persecution, with a gradual expansion underlying offences[3]'s list, both the strengthening of a prevention

[1] It's very hard to estimate the real effect of organized crime, as it's said on the document of Unioncamere, *La misurazione dell'economia illegale*, page 2*;* more important, it's difficult to individuate any possible infiltration in legal economy, especially in the Nord of Italy.

[2] "*Expo. Unimpresa, con corruzione in 10 anni -100 miliardi di Pil in Italia*", 12 maggio 2014

[3] There isn't a legal definition of underlying offence, but traditionally is defined as a crime but at the same time represents a constituent element of other criminal offence.

system, based on cooperation between public authorities and private operators. The aim of this partnership is to identify each possible suspected transaction of the proceeds of crime in the legal economy.

Money laundering prevention consists, for example, on rules that limit the use of cash, or on the rules that impose to banks and professional obligations to cooperate with authorities and on seizure and confiscation measures, as required by Decree 159/2011; prevention phase is fundamental because it allows to intercept crimes when there is its cash flow effect. With regard to the repression phase, the main rules that talk about it are the Penal Code, on article 648 bis and the Decree 231/2007, which provides for administrative sanctions.

Preventive action should be carried out in close connection with the prevention of criminal activities, because money laundering often is strictly connected with organized crime: laundering is the perfect solution of illegal activities of organized crime; an example is given by profits from drug trade, they cannot be totally used in such illicit behaviour, but they must be used in legal market.

Money laundering methods are diverse and are constantly evolving: they range from trade-related operations to on-line banking. Money launderers may also operate outside financial systems, for example, through alternative remittance systems. This paper focuses on the relation between money laundering and criminal connected companies, i.e. business enterprises that appear legitimate and engage in legitimate business but are actually controlled by criminals.

This thesis follows a branch of money laundering research in criminal companies; after creating a criminal company's database region from the north and centre of Italy, the aim of this paper is to prove whether there is a relationship between criminal enterprises and participations thereof.

In the First Chapter, after a general description of money laundering and its legislation, there will be a more deepener illustration of the use of dirty money in companies that appear legal, but in reality they are used to clean dirty money, to mask illegal activities or to hide a criminal or the real owner. At the end of the chapter it will describes the reasons that can bring a criminal to decide to invest his money in companies, rather than keep it in a bank or reinvest it in other criminal activities.

The Second Chapter is dedicated to a fundamental element in combating money laundering: co-operation with other institutions, including banks, other financial intermediaries and professionals. They are obliged by law to report to appropriate authorities any suspicious transaction; moreover, they are the main recipients of this research, because the results will add this information up to other crucial factors that identify criminals companies.

Finally, the Third Chapter is committed to a statistical analysis of criminal companies and their shareholdings; in order to be able to perform this analysis, criminal companies will be compared, using Stata, with a sample of not criminal companies. It will compare:

- The existence or not of participations;
- The total number of portfolio companies;
- The participation fee.

It is taken into consideration Emilia-Romagna, Liguria and Piemonte regions.

First Chapter

Money laundering: definition and its development through companies

In order to make a complete and thorough analysis it is necessary to understand the structure of money laundering. This Chapter has the aim to define the perimeter in which to move; it will describe also the legislation that has dealt with this issue, both at national and European level. Later it will discuss the tasks of the two most important bodies that deal with the prevention of money laundering, Financial Intelligence Unit and Financial Action Task Force: both publish annual reports that are very useful because they allow to have an up-to-date knowledge, especially against the new methods used by criminals to launder money. It was decided to introduce as of now these institution since their role is very important in the fight against money laundering, because this matter is very intricate and evolving very quickly and not always law is able to keep with.

At the end, it will be analysed in more detail money laundering in criminal connected companies: here describes the methods used and the reasons why launders adopt this method, including the acquisition of minority interest.

1.1 Definition of money laundering and its legislation

Money laundering can be defined as "*a process that employs financial, accounting, legal and other instruments in conjunction with an object that has either been used in, or derived from, unlawful activity. The primary process is to create a veil of legal cleanliness around the object. This veil not only prevents the object's association with unlawful activity from being accurately traced and identified, but also enables the object to be used in the legal economy with anonymity and without fear of criminal, civil or equitable sanction*"[4].

Indeed, once cleaned, money cannot be easily traced from the criminal origins of the funds: money laundering allows criminal to make the reinvestment, which permits to

[4] K. Hinterseer (2002), *Criminal Finance: The Political Economy of Money Laundering in a Comparative Legal Context* , UK: Kluwer law International, page 11.

increase their capital and it can be in turn reinvested in criminal activities, generating a kind of vicious circle[5].

Money laundering is the process that encourages and promotes the development of illegal activity; in this way, criminals attempt to hide the true origins and sometimes the ownership of the proceeds of criminal activities[6]. It is important that governments and authorities from all over the world try to prevent from legitimising the proceeds of criminal activities by converting 'dirty' funds to 'clean' funds, paying particular attention to financial system: the increased integration of the world's financial systems, and the removal of barriers to the free movement of capital have enhanced the ease with which criminal money can be laundered and it is complicated to keeping trace process. Indeed criminals are able to exploit all the opportunities offered by globalized economy: laundering tends to take place in an international context, focusing on countries that have less stringent regulation concerning client identification.

From a national perspective, one of the main consequences of money laundering is that it has a negative effect on the transparency, good governance and the accountability of public and private institutions. Money laundering activity also causes damage to a country's national security and reputation and has both direct and indirect impact on a nation's economy.

Typically[7], money is laundered through a three stages process:

- Placement, consist on investing illegal profits in the financial circuit, for example a business or a bank and it is characterized by the separation of those profits from the person who produced them. During this stage the proceeds are only physically deposited in the financial system, there isn't the real laundering. Money laundering techniques during this phase can be: smurfing and structuring and currency smuggling. With smurfing it is possible to make repeated payments or exchange transactions below the fixed threshold for supervision concerning money that has the same origin: the aim of this technique is to avoid any banking operations' monitoring. Another frequent technique during

[5] This definition is explained in G. Rodano (2001), *Denaro sporco: politiche criminali, politiche di contrasto e ruolo dell'informazione*, Donzelli , pag. 125.

[6] G. Rodano (2001), *Denaro sporco: politiche criminali, politiche di contrasto e ruolo dell'informazione*, Donzelli, page 124.

[7] Michael Zeldin, (1998),"*Money Laundering*", Journal of Money Laundering Control, Vol. 1 Iss 4 pp. 295 – 302 and others.

placement phase is currency smuggling, the physical transfer of money from one country to another[8], and it can return later to its country of origin;

- Layering is given by a set of financial and commercial operations design to losing track of the illegal origin. Once the cash is converted in a more manageable form, it is important to create distance between criminals and the illicit process.

  During this phase the main tasks identified by Financial Guard are the transfer of funds, the use of offshore companies, which are discussed later and wire transfer. In particular, wire transfer allows the transfer of large sums quickly between countries that are free of control.
- Integration, is the final stage, where founds are completely cleaned and are assimilated into the legal economy. Now money can be used in commercial activities, such as a restaurant, or it could be invested in capital markets or it can be used in the purchase of gold or diamonds, thanks to their high convertibility into money.

One of the main purposes of money laundering process is to "*disguise their illegal origin*"[9]: this activity help preventing actions taken by law enforcement and financial supervisors. In particular the Layering phase may involve disguising dirty money through the use of different methods[10], that are used simultaneously or sequentially, or they are alternated; the continuously shifting of money launderers makes it difficult to find the financial crime. Specifically, the use of non-financial business is increasing, considering even illegitimate institution, for example shell companies, but even legitimate companies[11]. Integration of the cleaned money into the economy is the final stage of the process, and is accomplished by the launderer that making appear that money has been legally earned. Here it is extremely difficult to discern between legal and illegal wealth.

Moreover, it should be noted how the last two phases of laundering, layering and integration, are more dangerous, because, even if they are different operations, at the same time they can be merger in one phase, because criminals try to superimpose them.

[8] Typically the final destination is a tax haven.
[9] This is the definition given by FATF.
[10] The number and variety of transaction used to launder money has become increasingly complex, involving financial institutions and using non-bank financial institutions.
[11] International Monetary Fund (2001)"*Financial System Abuse, Financial Crime and Money Laundering—Background Paper"* page 7.

The best condition for launders is the one where it is possible to coincide the two moments, so that dirty money, which can more easily conduct to its criminal origin, does not remain in the circle for a long time.

1.1.1 Anti-money laundering laws

Art. 41 of Italian Constitution guarantees freedom of economic initiative, but it underlines that *"non può svolgersi in contrasto con l'utilità sociale o in modo da recare danno alla sicurezza, alla libertà, alla dignità umana";* here we find the basis of all anti money laundering legislation and it is also possible to note how the problem of money laundering and in general organized crime's infiltration in Italy had always felt as a big damage for economy and society.

The nature of money laundering makes it very dangerous because it causes negative effects both economically and socially, and, thanks to the various techniques used, it is always more difficult to be identified. An effective anti-money laundering regime will have in place measures aimed at identifying any laundering activity and at using the evidence obtained in bringing the person or persons concerned to justice.
This set of laws will also have in place measures aimed at preventing the loss of the proceeds of crime and at confiscating them.
Anti-money laundering can therefore make a significant contribution to the fight against corruption in at least two main ways:

- It could help uncover evidence of criminal activity through identification of suspicious movements of financial assets, thus increasing the chances of a successful prosecution of the perpetrator of the crime;
- It also enables the tracing of criminal proceeds to facilitate their preservation, recovery and ultimate return to their rightful owner.

As said above, anti-money laundering system has the aim to prevent the entrance of illegal origin resources into legal business, in order to preserve stability and integrity of economic and social context; moreover, thanks to its ability to identify criminal behaviour, it is also used to combat financing terrorism.

The Italian legal system has developed in line with international standards and EU directives.

In Italy the violation of money laundering has been incorporated for the first time in Penal Code in 1978 with art. 648 bis; originally they were identified four types of offences, which are needed to accumulate dirty money. Those offences are: aggravated robbery, extortion, kidnapping and drug trade. The purpose of this article was to identify limited set offences for money laundering, in order to create a general better defined guideline with the requirements to reporting any possible suspicious transactions operations.

In 1991 the legislature has decided to limit the use of cash in transactions over twenty million lire: this is because the main method used to launder money was through the use of financial intermediaries. The law[12] also establishes certain requirements for financial intermediaries such as the identification clients' data, the recording of transactions relating to movements exceeding the threshold, the duty to report suspicious transactions to authority and the creation of a data base with all suspicious transactions.

This legislation was altered in 1993 with laws n. 328 with the intent to increase the list of predicated offences. With the aim to carrying out Directive 2001/07/EC in 2004 it was issued d. lgs. n. 56, which extend the obligation to report suspicious transactions to other actors, besides the financial intermediaries, such as professionals like accountants, auditors, lawyers and notaries. This was necessary because launders make use of non-financial entities for their illicit operations, and for this reason it was introduced new subjects to obligations. In this way Italian law also respected FATF recommendations, which were increased to extend their range of action.

Significant changes have been introduced due to the Directive 2005/60/EC (the Third Money Laundering Directive); in Italy, it was adopted with D. lgs. 21 November 2007, n. 231. In particular, it focuses on a clear definition of the recipients of the obligation and on their analysis and identification of the beneficiary owner; moreover, a very important point of the law is the obligation of customer due diligence, which must be run according to of risk-based approach system.

On 20th May 2015 the European Parliament approved the Fourth European Directive on Money Laundering which is compliant with anti-money laundering international standards developed by the Financial Action Task Force.

[12] Law 197/1991.

This came into effect by 27th June 2015. The most significant Fourth Directive's news concerns[13]:

- The establishment of central registers in every European country containing accurate and current information on beneficial ownership of companies, legal entities or trusts; these records will be of public domain and can be consulted freely and without any restrictions by the competent authorities, as well as by journalists and by any person or organization that can demonstrate a legitimate interest;

- News about customer due diligence by banks, accountants, lawyers, notaries, real estate agents and casinos with the exception of the professional relationship when representing a client in legal proceedings;

- New rules to make it easier to trace the transfer of funds.

Finally, one of the most important Fourth European Directive's aims is to provide much greater transparency in the shadowy business structures that are at the heart of money laundering schemes, as well as schemes used by businesses to avoid their tax responsibilities. It will be required that the ultimate owners of companies (the "beneficial owners") are listed in central registers in EU countries, accessible to people with a legitimate interest. In this way financial institutions will have to improve their reporting obligations in the sense of guaranteeing more accountability and transparency.

Moreover, in 2014 there was the strengthening of tax compliance, that introduce a series of initiatives, that have transformed anti money laundering function of banks and other financial intermediaries into a super "compliance entity" which have to deal with legal, risk, operational and tax matters: a strong worldwide anti money laundering processes should be implemented in banks.

The l. 186/2014 introduces, in line with European legislation, the activities of self-laundering: it is the set of transactions carried out by those who have committed the

[13] http://uif.bancaditalia.it/sistema-antiriciclaggio/ordinamento-italiano/index.html 3 September 2015

crime that cause dirty money[14]. Self-laundering is included among crimes which may give rise to administrative responsibility pursuant to Legislative Decree no. 231/2001. Furthermore, l. 186/2014 introduced voluntary disclosure, with the aim to oppose tax evasion: this operation is possible thanks to the new context of international cooperation, which has changed a lot and is based on principles of transparency and exchange of information[15].

The system of preventing money laundering is based on a series of collaboration between operators and administrative authorities. Operators are required to fulfil specific obligations and to comply with special rules:

- The customer due diligence and record of relationships and transactions in Computer Archive;
- The identification and reporting of suspicious transactions, integrating the "active cooperation";
- The adoption of organizational measures and principals dedicated training, which forms the substrate of those obligations.

In order to reduce the circulation of dirty money it were introduced restriction on cash transactions[16].

1.1.2 The rule of Financial Intelligence Unit and its "active cooperation"

Italian Financial Intelligence Unit was established at the Bank of Italy, with Decree 231/2007, in accordance with international rules, which provide for the presence in each country of a FIU with full operational autonomy and management and it is provided of functions that combat money laundering and terrorist financing. The decision to contrive Financial Intelligence Unit within the Bank of Italy was taken to use, for countering money laundering, the assets of the Bank information and integrate it with

[14] In the Penal Code we have art. 648 ter.1, which punishes anyone who: *"chiunque, avendo commesso o concorso a commettere un delitto non colposo, impiega, sostituisce, trasferisce in attività economiche, finanziarie, imprenditoriali o speculative, il denaro, i beni o le altre utilità provenienti dalla commissione di tale delitto, in modo da ostacolare concretamente l'identificazione della loro provenienza delittuosa"*.

[15] UIF (2015) "*Rapporto annuale dell'Unità di Informazione Finanziaria*", page 15.

[16] D. L. December 6, 2011, n. 201 ("decreto Salva Italia") with effect from 6 December 2011 reduced, from € 2,500 to € 1,000 the threshold of cash payments.

the information obtained by FIU; in this way it is possible to take advantage of its extensive financial expertise and to be able to maximize synergies.

FIU is responsible for gathering information on money laundering cases, primarily through suspicious transaction reports submitted by financial intermediaries and other professionals; with that information it develops a financial analysis[17], using all the sources at its disposal, and evaluates their relevance for the transmission to the investigative bodies and to judicial authorities, for an eventual progression of the repression action.

After receiving the advisory, this is associated to other information included in the FIU's database and there is a first analysis designed to identify the priority of the warning; this operation is done by following the risk based approach principles. Reports that are easy or those that can be attributed to the facts already known are forwarded to Financial Police and the Anti-Mafia Investigation Department; those that appear to be unfounded are dismissed, even if law enforcement agencies are informed of these advisories. Reports that appear most relevant are subjected to in depth-analysis with the aim to identify the origin and the destination of the funds.

The legislation establishes disclosure requirements for supervisors and professional associations. The Unit works with law enforcement agencies for the identification and analysis of abnormal financial transactions; it participates in the worldwide network of FIUs[18] to exchange information essential to face the transnational dimension of money laundering and terrorist financing.

For its purpose FIU has a series of model, practices and behaviour patterns: in particular, it uses its information database to develop, starting from the financial analysis of individual reports, a strategic value with the aim to highlight trends and operational models that are risky in relation to money laundering[19].

FIU focuses particularly on surveillance on possible types of corporate structure and other instruments that are suitable for shield the property, such as trusts and fiduciary,

[17] With financial analysis FIU there are a series of activities that enhance the information arrived: this help in widening the original context reported and to identifying criminals .

[18] According to FIU 2014's report, in 2014 there were 660 applications was made to foreign FIU.

[19] UIF publishes "*Casistiche di riciclaggio*": this work collects a series of cases with difference in terms of complexity and economic importance. This paper provide an information tool that can help everyone in the detection of other cases due to money laundering.

or legal entities which are a kind of articulated corporate structure that collaborate with foreign entities, especially those located in in countries at risk or uncooperative[20].
At the end of the research and analysis there is a technical report prepared for the investigative agencies and it also discusses possible ideas for the investigative activity; FIU is the heart of money laundering system, because it connects different part of prevention money laundering system, the public with the private side, the national with international side.
Beyond of operational analysis, which analysed every case of suspected money laundering, Financial Intelligence Unit plays a strategic analysis, aimed at identifying the weaknesses of the system. The strategic analysis using all available information, and enrich these information with input from public or private external sources. It is based on two pillars: the survey of patterns of financial behaviours and observations of money laundering financial flows. Another objective of strategic analysis is the evaluation of risk levels related to the system as a whole or considering a specific geographic area, means of payment or economic sectors.

Among intermediaries and professionals that collaborate with FIU, it is worth to notice the importance of banks and their role in surveillance companies; they have personal incentive[21] in combat money laundering because the infiltration of illegal activities in banking and financial system is a threat for their stability and for the proper conduct of their economic function. The legal and reputational risk that banks can face, resulting from an involvement, even unconsciously, in crime acts, can generate economic losses and it is potentially able to affect profitability and, ultimately, financial stability of intermediaries. In the Second Chapter it will be analysed in detail the role played by banks and other professionals, and it will be proved as they contribute in the fight against money laundering.

1.1.3 Financial Action Task Force (FATF) on money laundering

The FATF is an intergovernmental body and it was established in 1989 with the aim to find and examine measures to combat money laundering: it is the principal anti money laundering multilateral organization.

[20]UIF, "*Rapporto annuale dell'Unità di Informazione Finanziaria*", May 2015, page 55.
[21] This theory is sustained by that fact that most of advisories in 2014 (83,2%) came from banks and Poste.

FAFT is a voluntary task force: since its creation, it has been at the forefront of measures designed to counter criminal attempts to use the financial system for criminal purposes.

Most notably, in 1990 the FATF established a series of money laundering recommendations. They established a series of special recommendations on the prominent threat of terrorist financing, whose aim was to unite anti-money laundering and terrorist financing efforts into one universal instrument. The Financial Action Task Force came out with a revised set of 40 principles for AML; this was also incorporated with work done by the Basel Committee on customer due diligence standards. The FATF had earlier in October 2001 issued 8 Special Recommendations on Combating the Financing of Terrorism followed by a 9th recommendation on cash couriers in October 2004. Those Recommendations has a generic character: each country will have to adapt to the Recommendations and this would be realized in different ways, since that there are different legal system. Because money launderers change techniques over time, the FATF has to update its recommendations every couple of years: moreover, annually, the FATF presented a report on specific issues regarding money laundering.

FATF, in close collaboration with its members, conducts regular typology exercises to uncover new money laundering techniques and to develop strategies for countering them: it examines techniques and counter-measures and reviews whether existing national and international policies are sufficient to combat the developing threat[22].

The Forty Recommendations can be grouped as follows[23]:

a) Legal recommendation:
   - Field of application of money laundering crime (rec. 1 and 2);
   - Provisional measures and confiscation (rec. 3);
   - Customer due diligence and operation's registration (rec. from 4 to 12);
   - Reporting of suspicious transactions (rec. from 13 to 16);
   - Other measures to deter money laundering and terrorism financing (rec. from 16 to 20);

[22] Moreover, member countries complete annual self-assessment style questionnaire and the FATF regularly conducts a Mutual Evaluation Report examinations on individual jurisdictions, assessing the effectiveness of their national policies in dealing with money laundering and terrorist financing.

[23] International monetary fund (2001)"*Financial System Abuse, Financial Crime and Money Laundering—Background Paper"* page 29.

- Measures to be taken against countries that do not respect or insufficiently respect the FATF recommendations (rec. 21 and 22);
- Regulation and supervision (rec. from 23 to 25);

b) Recommendations for financial and non-financial institutions (Gatekeepers):

- The competent authorities, their expertise and resources (rec. from 26 to 32);
- Legal persons' transparency (rec. 33 and 34);
- Legal assistance (rec. from 35 to 39);
- Forms of cooperation (rec. 40).

1.2 Use of companies

Both the FATF's Recommendations and FIU's behaviour pattern are of fundamental importance in the prevention of money laundering, particularly in the event that commercial companies are used to clean the money resulting from illegal activities.

One of the most attractive methods to clean dirty money is the use of companies that operate in legal economy; a business has several advantages over on individual or a nominee. First, a business is expected to generate revenue, so that illegally acquired money blends with clean money. Second, the principal can establish the business in such a way that he controls it. Third, assets can be held in the business name, not the principal's, so a cursory asset check would not disclose the principal's interest. Finally, the business may also be used as a place where illegal activities can be conducted as well.

Companies can be used both in the placement phase, in which dirty money is used within the company, for example to own assets, or it is used in the layering and integration phases. In this way it is more difficult to identify dirty money and it is possible to have only one phase of laundering, where the moments of placement, layering and integration phases are combined in a single moment.

Obviously, money laundering cannot be done in the 'open air' and it requires sophisticated means to disguise the origin of the assets. In particular, this phenomenon is contemporary in Italy; on one hand organized crime has deep roots and it is well distributed throughout the Country, on the other side economic crisis hit very hard the Italian economy: today companies are struggling to obtain loans from banks and they

not easily receive payments of their performance. In fact, the study conducted by Transcrime[24] showed that the availability of obtaining resources from illicit markets allows criminal businesses to finance itself without having to resort to bank credit.

Criminal infiltration in businesses appears to be a significant component in the national economy: criminals prefer limited liability company in which they can hide their presence, for example, through the use of nominees[25].

In the European Journal on Criminal Policy and Research[26] it is highlights that there are five reasons for which Mafia making investments in business:

- Concealment of criminal activities: criminals may infiltrate legitimate businesses in order to hide the origin of illicit funds. When the purpose is money laundering, they may decide to infiltrate sectors with a weak or changing regulation and territories with high levels of tax evasion;
- Profit maximization: include reasons related to the minimization of costs, or to the maximization of profit and return on investment;
- Social consensus, by which it means criminal corporate social responsibility;
- Control of the territory: control of the territory is a distinctive feature of mafia-type organisations and has both a physical and a strategic component, in particular it refers to reasons related to the maximization of the main centres of power, including public administrations;
- Cultural or personal reasons: reasons both personal, as in investment in family business, and cultural, in order to have more social prestige.

In the document presented by Sos Impresa Confesercenti (2012)[27] there is an analysis of economic sectors where proceeds of crime are invested; obviously, this is correlated with criminals' interests. At the top there is construction industry and all its phases, followed by commercial activities and food service, road haulage and entertainment industry. All those economic activities are business that enable a strong flow of money and require capital injections but poor managerial know-how.

[24] Transcrime (2013), P*rogetto PON sicurezza 2007-2013, Gli investimenti delle mafie,sintesi*, page 150.
[25] Transcrime (2013), P*rogetto PON sicurezza 2007-2013, Gli investimenti delle mafie,sintesi*, page 8.
[26] Levi, Michael, *European Journal on Criminal Policy and Research*. June 2015, Vol. 21 Issue 2, page 275.
[27] Sos Impresa Confesercenti (2012), *Le mani della criminalità sulle imprese*, page 101. This study was made taking in consideration 100 confiscated companies.

Other studies suggest that Mafia groups "*seem to prefer those markets that allow them to maximise their territorial control, to benefit from and expand their political relationships, to distribute jobs and sub-contracts and that are close to their personal and cultural background*"[28]. This is because organized crime in Italy, especially in the south, is present in people's daily lives, both for historical and economic reasons.
All those peculiarities perfectly fit with the aim of money laundering activities, that are to profit, because "*Profit is fundamental to the goals of most crime and therefore criminals make great efforts to move illegally obtained money and other assets in order to convert, conceal or disguise the true nature and source of these funds*"[29]. More deeper, traditional typologies of legitimate businesses' involvement in money laundering are cash intensive small businesses, such as restaurants or car washes, in which funds from illegal activities can easily be commingled with deposits of legitimate business receipts. Usually criminals use small businesses, that allow to bypass audit requirements, hence appearing 'low risk' to authorities.

This is also highlighted in Business Customers and Money Laundering Risk document[30] where it is explained that, thanks to global economy, not only large corporations are involved in international trade, but also small and medium-sized business. Import and export are critical issues of a company's risk assessment, because they facilitate flows of dirty money across country, but even it's easier to sell illegal products, such as trading in drugs or weapons; this because legal business creates a shield of protection against this type of goods.

Limited liabilities company are particularly simple to establish and most state laws require only minimal disclosures of ownership during the corporate formation process, furthering concealment of this information from financial institutions and regulatory agencies. For these reasons a limited liabilities corporation can be established as a shell company, which has no physical presence and generates little or no economic value.

[28] *European Journal on Criminal Policy and Research*. June 2015, Vol. 21 Issue 2, p275, 23 p Levi, Michael, page 291; this analysis was of about 2000 companies confiscated in Italy since 1983 to 2012.
[29] FATF Guidance (2013), *National Money Laundering and Terrorist Financing Risk Assessment*, page 26.
[30] Advancing Financial Crime Professional Worldwide (2013), *Customers and Money Laundering Risk*, page 7.

Since that there are legitimate business reasons for establishing a shell company, this entity type has become a pervasive tool for money laundering, not only in Italy.
Holding companies and joint venture both have fundamental structures with the potential to obscure the entity's true beneficial owners and ultimately the actual purpose and activities in which the entity is involved: significant higher risk is present when the ownership structure includes multiple, complex subsidiaries (holding companies) or limited partners (joint ventures) that have no apparent commercial purpose.

In the following paragraphs it will explained which are the main activities that drive criminals to launder money within companies; of course, the list is not exhaustive because launders are able to find new methods to clean money in a company, in order to make more difficult to discover the crime.

The most popular money laundering schemes using companies are:

1.2.1 Shell companies

Shell companies are designed to perform some functions, but they don't conduct the normal business of a corporation. Some shell companies may be set up for a single purpose or hold just one asset; others may be set up for a variety of purposes or manage multiple assets, which facilitate the co-mingling of legal and illicit assets.
Moreover, shell companies may be set up in many jurisdictions, including in certain offshore financial centres and tax havens. In addition, their ownership structures may occur in a variety of forms. Shares may be held by a natural person or legal entity, and they may be in nominative or bearer form. They may be used to hide the identity of the natural persons who are the true owners or who control the company[31] Shell companies can be pyramided, that create a confusing path to follow, especially if it is organized in countries where there is a flexible jurisdiction[32]; in this way, finding the identity of the true owner become impossible. This is the reason for which shell companies are effective as layering devices.

[31] Commonly referred to as the *beneficial owner*.
[32] That is, jurisdictions where law permits secrecy in business relationship.

As placement mechanisms, shell corporations have the appearance of legitimate business, and their bank account can be used to receive cash deposits or to transfer money.

1.2.2 Offshore shell corporations

The offshore companies are companies registered under the laws of a foreign state, usually in one of the 'tax havens', but conduct their business out of this state. Tax havens usually offer weak controls and tax regimes in favour of foreign investors. Confidentiality is a cornerstone of those countries: they do not provide information on companies based on their territory.

For this reasons offshore companies are used to make reckless speculation, to make illegal operations or to hide budget losses.

Moreover, the aspect of these companies, particularly useful for launders, is the lack of a requirement that shareholders be identified: for example, it is impossible to know who is the beneficiary of the company's current account. In this way off shore companies can be used like shell companies.

It's not expensive or difficult to establish an off shore company; internet is making the creation of this kind of company easier than ever.

1.2.3 Trust

This institution has Anglo-Saxon origin, this is why it is not expressly regulated by Italian law. However, trusts that are established in a country where is its own regulation are recognized in Italy, as a result of the Aja Convention of July,1st 1985, regulated by law n.364/1989.

Trust is defined as a technique that allows the owner of certain assets, defined as the settlor or garantor, to deprive the assets and confer them to another person or entity, the trustee. In this way it is created legal barrier, thanks to the trustee, that protects the grantor and the beneficiaries. If the trustee is bound by a confidentiality agreement, the true beneficial owner may be unidentifiable. Also, the asset protection attributes of trusts are often leveraged for illegal purposes, including money laundering and tax evasion.

1.2.4 Banking/Business combination

Another money laundering schemes is banking/business combination[33]; in this case, the launderer is trying to take advantage of the use of a simple business and after move money into a bank. By doing this, the money launderer gives up all the flexibility that goes with dealing only in cash: now he's submitted to rigid rules, since that every transaction is recorded, every asset is accounted. In this case, it is up to the banking authorities to become aware the danger and they must conduct of their own risk assessments. Cash intensive business can be considered a more simple variation of banking/business combination: the cash intensive business is defined as a company whose business is mainly due to high number of cash transactions, such as restaurants and casinos. Because their sales are primarily in cash, funds from illegal activities can easily be commingled with deposits of legitimate business receipts.

1.2.5 Real estate sector

The use of real estate is an established method of money laundering: criminals buy high-value goods such as real estate as a way of laundering illicit funds. The reasons behind this technique is that criminals use dirty cash money to buy real estate, they can disguise the ultimate beneficial ownership of real estate and they can increase the value of the real estate, through renovation. Moreover, due to the international nature of the real-estate market, it is often extremely difficult to identify real estate transactions associated with money laundering or terrorist financing. Compared to other methods, money laundering through real estate can be relatively uncomplicated, requiring little planning or expertise. Large sums of illicit funds can be concealed and integrated into the legitimate economy through real estate.

Financial Action Task Force[34] gathers the most common methods to launder money in real estate sector in eight typologies, which are:

- use of complex loans or credit finance,
- use of non-financial professionals,

[33] As it is rightly noted by J. Madinger (1999) *Money laundering : a guide for criminal investigators*, page 333.
[34] FATF, *Money laundering & terrorist financing through the real estate sector*, 29 June 2007, page 7

- use of corporate vehicles, manipulation of the appraisal or valuation of a property,
- use of monetary instruments,
- use of mortgage schemes,
- use of investment schemes and financial institutions,
- Use of properties to conceal money generated by illegal activities.

Furthermore, criminals often use artificial transactions of properties: this method assumes the sale of a property at a higher price than its market value. For example, a launder has a million euros to clean in the legal market; he decides to buy a property at its market value, that is lower than one million, and then resells it to a compliant client for a million euro, the same amount that must be recycled. At the end, the compliant client receive what he paid for the purchase; this payment is made in cash, because cash payment are not traceable.

1.2.6 Invoice scams

Invoice is a bill for goods delivered or services rendered: there are purchase invoices and sales invoices.

In the case that a company decide to deal with counterparties without commercial letters of credits[35] can face the risk of incur in a trade base money laundering: this is a means of fraudulently transferring value. A classical method of achieving this value transfer is through over-invoicing and under-invoicing of goods and services. Using an invoice the amount shown can be whatever the two parties agree upon: if a money launderer controlled both ends of a transaction, great quantities of dirty money could be integrated into the economy, probably without anybody notices that.

This kind of laundering schemes is particularly used for cross border operations. The misrepresentation of the price effectively transfers additional value between the

[35] LoC are used to mitigate the risk involved in dealing with overseas counterparties; LoC is irrevocable undertaking by which a financial institution promises to pay a specific sum of money to a beneficiary, provided stipulated documents are presented and all the terms and condition of the LoC are in compliance.

importer and the exporter. This method is very successful in money laundering processes, because there is minimal involvement of customs agencies and information sharing between countries[36]. Other techniques used to hide illegal movement of funds in trade finance is doing short/over shipping to misrepresent the quantity or quality of the goods, and the 'phantom shipping', where all documentation is completely falsified and there is no shipment of goods[37].

In wider terms, it is possible to say that one of the primary characteristic of a criminal connected company is when it inflates sales reports or write cheques to accomplices for bogus service; in this way, a well-run front company can launder thousands of euros a day with little risk of detection. In general, any business that accepts cash and refunds the same with a cheque is primed for abuse of launders.

1.2.7 Loan back schemes

The purpose of the loan is to give the source of the money an appearance of legitimacy and to hide the true identity of the parties in the transaction or the real nature of the financial transactions associated with it: this scheme is used during the integration phase.

For example, there are 1000 euros to integrate[38]: this could report in the financial statement as an ordinary income or it is possible to report it as a loan from offshore business. The criminal deposits, through a special purpose vehicle, this sum of dirty money in an off shore bank. At the same time criminal is the owner of another company, via another person, and this company operates in the legal system.

If criminal wants to make an investment in the legal business, ha can use dirty money in the off shore bank as a collateral for a loan in another bank. Thus, the amount originally deposited at of the country offshores' bank will be used as the balance of the loan contract and the investment has been made thanks to dirty money, which has been cleaned.

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[36] This process is described on Advancing Financial Crime Professional Worldwide (2013), *Customers and Money Laundering Risk,* page 7

[37] Financial Conduct Authority (2013), *Bank's control risk in trade finance,* page 12.

[38] John Madinger, Sydney A. Zalopany (1999), *Money laundering : a guide for criminal investigators*

1.2.8 Acquisition of subsidiaries

As it has already been mentioned in the introduction, this thesis will analyse if a relationship exists between the laundering of money within the company and the existence of subsidiaries and affiliated companies, with the aim to identify the specific characteristics that may more easily discover criminal firm from non-criminal. In fact, it is reasonable to think that, thanks to the huge flow of money from illegal activities, it is easier to buy shareholding in other companies.

A company is always looking for its best operating condition: that is why it buys stakes in other companies: the union of two or more entities has the stated aim to reduce competition and strengthen economic efficiency, pursuing the object of improving the functional capacity of companies grouped.

In general, business combination have two objectives, one external and one internal: the first is to control a piece of market, the second refers to rationalize the business management, in order to increase productivity. As regards to criminal companies, they may have other reasons, in addition to those just mentioned, for deciding to buy shares in other companies, for example, to make more difficult to find detention of dirty money, or to have offices in other areas that can also be useful for illegal activities.

In some cases, targeting businesses with economic difficulties facilitated the infiltration process, since the owners of the companies were eager to sell their shares before leading their business to bankruptcy; in these cases, criminals simply acquired the shares of the targeted business, and the acquisition process did not involve any illegal activity.

This method used to launder money will be the subject of the Third Chapter, which has the aim to ensure, through the analysis of a sample for criminal and non-criminal enterprises the existence of a relationship between criminal factor and equity investments.

1.2.9 Corporate liability

Decree N.231/2007 introduced companies' responsibilities for violations resulting from the commission of a crime[39]: the purpose of the decree is to protect financial system from being used for money laundering or terrorist financing.

[39] Specifically, decree indicates that "*i destinatari sono gli enti forniti di personalità giuridica, le società fornite di personalità giuridica e le società e le associazioni anche prive di personalità giuridica*" (art. 1, co. 2).

In particular, art.52 of Decree 231/2007 forces management audit entities, such as the board of statutory auditors and supervisory board, to monitor and report violations of law[40]. The information's duties regardless possible violations relating to the registration, reporting and limits the use of payment instruments and deposit, for example cash or savings accounts and anonymous or fake registrations. The combination of controls to prevent money laundering' crimes concerns on one hand activities with third parties, from other intra-group activities, carried out as part of the relationship between companies within the same group.

1.3 The reasons behind the choice of using criminal connected companies

In order to understand the reasons that lead the use of criminal companies to launder money in respect of the choice to keep the money in liquid form, it is useful to note how organized crime, since the 70s, used dirty money: in fact, during this years criminals have made significant capital investments in their areas of origin, acquiring farms, tourist complexes or small banks. But most of the dirty money remained liquid and it was sent to the Swiss banks or to other tax havens. During 80s there was an expansion of criminal economy, thanks to the expansion of internal market and the growth in demand for hard drugs; on the other side, the increased ability to identify real estate owned by criminals led to raising the threshold of the risk of expropriation. As a result, a larger share of criminal surplus remained in liquid form and it has taken the path of the banks and financial institutions in the northern and international banks. This is the reason why traditionally cash is considered to be the preferred means of payment for transactions related to illegal economy because it guarantees non-traceability and anonymity of trade.

Looking at a study conducted by European Central Bank[41], the use of cash in Italy is particularly high: the volume of transactions settled in cash is equal to 85% of the total, against an EU average of 60%. This element from one side can be seen as a different degree of development of financial system, as far as concern possible alternative payments instruments, such as electronic payments; form the other side this may reflect

[40] Confindustria, *Linee guida per la costruzione dei modelli di organizzazione, gestione e controllo ai sensi del decreto legislativo 8 giugno 2001, n.* 231 Approvate il 7 marzo 2002 (aggiornate al marzo 2014), page 145. The fulfilment of information's duties should be appropriate to the specific supervisory powers.

[41] Source: Ministero dell'Economia e delle Finanze, Comitato di Sicurezza Finanziaria "*Analisi nazionale dei rischi di riciclaggio e finanziamento del terrorismo 2014*", page 8.

the heterogeneity in the size of the underground economy. In recent years the use of cash has suffered a steady decline due to the increasing use of alternative instruments, and the effect of fiscal tightening on the circulation of cash: this may be due to the introduction, with *Decreto Salva Italia,* of a maximum threshold of 1000 euros, even if the Government has increased the threshold to 3000 euro[42], for cash transfers between individuals, for bank deposit or postal bearer or other bearer securities. Those restrictions have two purposes: to trace financial movements to contrast money laundering and to combat tax evasion and tax avoidance. Indeed, for transactions worth more than 3,000 euro it must necessarily resort to banks, to Italian post office, to electronic money institutions and to payment institutions: these institutions are forced to issue checks, for amounts exceeding € 3,000, which indicates the exact information about the name (business name) of the beneficiary and the 'not transferable' clause[43].

The decision to raise the limit to 3000 euro was taken as a 'liberal measure'[44]: if on one side this can be seen as a step backwards in the fight against money laundering, it should be noted that in Italy, although there is the lower cash limit in Europe, tax evasion does not seem to have suffered. A study conducted by CGIA shows that there is very little correlation between the threshold limit of the use of cash money and tax evasion. Instead, a study conducted by Italian FIU[45] shows that the greater the number of crimes per capita, the higher the incidence of cash payments observed in individual municipalities.

Definitely, the introduction of this threshold is a reason why dirty money is redeployed in companies: moreover, since that dirty money is less liquid[46], it's easier to re-use it only in the same illegal circuit, for example in drugs traffic: laundering has the aim to separate money from its illicit origin and this is made even more efficient if it is cleaned in companies because it is more difficult to distinguish it from legal money. Major distortions of laundering is that there are financial capital at no cost and theoretically unlimited; dirty money is used by acquisition of direct or indirect control over a company or through managing of economic activities. This cause: alteration of the

[42] Source http://www.repubblica.it/ ; this new roof has been introduced with *Legge di Stabilità 2016* and it became law on 1st anuary 2016.

[43] Only the recipient can collect it.

[44] These are the words of Interior Minister Alfano in a Rai interview (http://www.rainews.it/dl/rainews/articoli/ContentItem-630f2db2-ad45-4d61-a295-9f785cea8d5a.html?refresh_ce, 26 October).

[45] Annual report page 68.

[46] Scuola superiore dell'economia e delle finanze(2011), *La prevenzione del riciclaggio nel settore finanziario, Testimonianza del Vice Direttore Generale della Banca d'Italia,* page 4.

conditions of fair competition between businesses and infringement of the principle of freedom of the market.

Bank of Italy's Deputy Manager[47] define laundering as a bridge between organized crime and civil society that gives criminals the tools to be integrated into the system, coming to sit on the boards of directs and contribute to economic, social and political decisions. As it was previously highlighted, the authorities should pay particular attention to this kind of laundering technique because it offers the possibility, for example to companies in trouble, to obtain large sums of money without having to resort to loans or mortgages with banks.

[47] Scuola superiore dell'economia e delle finanze(2011), *La prevenzione del riciclaggio nel settore finanziario, Testimonianza del Vice Direttore Generale della Banca d'Italia,* page 4.

Second Chapter

The importance of active collaboration

In the previous Chapter, after defining the general concept of money laundering and after describing its set of laws, it has been described how criminals can clean dirty money by using companies that operate in legal businesses, including the use of subsidiaries. Before starting to statistically analyse if there exist a relation between criminal companies and equity participation in other firms, it has been decided to describe in detail one of the focal points of the fights against money laundering: the obligation to report suspicious transactions.

Customers Due Diligence are at the core of effective anti-money laundering risk management: a good due diligence is the key to a wider anti money laundering environment, as it is a prerequisite for effective risk assessment, transaction monitoring and suspicious reporting.

The choice of introducing obligations for banks and other intermediaries was taken because, over time, the evidence had shown that it was necessary to introduce deeper controls in entities where money has to pass; those entities are essential in being able to support any operation that is necessary to wash funds with illicit origin.

In order to define a prevention system "effective", it must be observed how participants create an inhospitable environment against money laundering; an active cooperation can make a substantial contribution in achieving this result: this is evidenced by the fact that criminals are constantly trying new laundering's techniques and tools to avoid being discovered.

At the end of this chapter it will show the result of FIU 2014 Annual report, with the aim to see if active cooperation is truly useful in the fight against money laundering.

Although the effectiveness of prevention system cannot be assessed only by looking at the change in the reports received, the results of those reports are an important indicator of the parties responsible to recognize behaviours that are effectively criminal. As it was said in the previous Chapter, laundering requires the existence of other crimes and is therefore normal that on these crime offenses have been individuated the investigation

start. Even in such cases, they provide a significant added value in terms of demonstration of crime and at the same time in terms of enrichment of the evidence and for the identification of criminal relations' networks.

2.1 Money laundering risks

As it was highlighted in the First Chapter, money laundering is a serious threat to legal economy, because it has the power to change the "rules of the game" in certain sector and, in the long run, it corrupt society as a whole. More in detail, the main reasons that lead to combat money laundering are[48]:

- The social importance, because money laundering causes damage to society as a whole, especially within developed countries[49];
- The economic importance: fighting money laundering means also fighting tax evasion; moreover, money laundering has a direct negative effect on economic growth by diverting resources to less productive activities. Rather than being placed in productive channels for further investment, laundered funds are often placed into "sterile" investments to preserve their value or make them more easily transferable. Such investments include real estate, art, jewellery, antiques or high-value consumption assets such as luxury automobiles. Such investments do not generate additional productivity for the broader economy.
- The legal importance, because there is a relationship between the level of anti money legislation and the prevalence of criminal activities, like organized crime and terrorist financing.

Since new money laundering methods continuously emerge and present special characteristic, criminals can take advantage of different financial and legal systems of different countries[50]. Moreover, it is difficult to find a definition for money laundering

[48] The matter of money laundering is not just a problem about few states, because laundering is just the tip of the iceberg of criminal activities: behind it, there are other activities, such as human trafficking and drog truffiking. Even OECD in his document "Money laundering awareness" (2009) has highlighted this aspect, in order to raise awareness on money laundering.

[49] This was demonstrated by a Bank of Italy' s study conducted in 2009, in which it was analysed what is the impact of crime on bank loan. In general, in countries where crime rate is higher, entrepreneurs face more costs for security and protection and may be discouraged to invest.

[50] This could depend also on criminal's personal preferences and behaviour.

risk that is appropriate for all countries, because nations have different definition of this kind of crime[51]. These are the reasons why governments cannot fight alone and led him to introduce laws aimed to put forward countermeasures in order to combat money laundering more efficiently and more effectively. Anti-money legislation is relevant for two objectives: first, it reduces the possibility to use a company for purposes connected with financial crime[52]; second, it protects market confidence and reputation.

Financial services institutions such as banks, non-banking financing companies, insurers, and capital market firms are generally the most favoured channels through which illicit money is laundered across the globe. Many financial services institutions may be associated with money launderers unknowingly, which is a primary reason that financial firms are subjected to stringent anti-money laundering regulations to track the trail of illegally-sourced earnings.

In order to get benefit for the analysis that will be made in Third Chapter, it was decided to analyse which is the role that professionals, auditors and above all banks play in combatting money laundering, because they have more contact with commercial companies and thus can identify more easily the use of legal business to launder money or to hide illegal activities. Furthermore, the results of these analyses could be used together with other data to identify criminal companies from non-criminal.

One of the sectors that is more vulnerable by laundering and crimes is the banking sector, in particular bank's credit market: these risks will experience loss as a result of fraud from direct criminal activity, lax internal controls, or violations of laws and regulations. Looking at KPMG's Global Anti Money Annual Survey (2014)[53], most of the respondents said that money laundering is considered a high risk area within their business risk assessment, given the impact that anti money laundering compliance can have on the reputation, share price, and economic viability.

This is also highlighted in Italian FIU's 2014 Annual report, which states that banks are highly exposed to the risk of being used to launder money, because of their interconnection system with foreign financial entities, their use of cash and their broad

[51] This is the reason why many international bodies, like FATF with its Recommendations, try to have a global definition of money laundering.

[52] As it was illustrated in the First Chapter, launders use companies to clean money or to hide their illegal activities.

[53] This survey was made based on 317 respondents participated across the financial services industry representing 48 countries,.

spectrum of activities. In short, their biggest risk is to lose the reputation and trust with other customers[54].

On the other hand, banks have interest to verify with which type of customers they are dealing with. For example, if a bank receives a loan application from a company, it wants to make sure that this company is not engaged in illegal activity, this is because it could risk losing his money, and because it may be denounced by the authorities for cooperation with criminals. For these reasons, banks have personal interests to intervene actively in the fight against money laundering: public confidence in financial institutions, and hence their stability is enhanced by sound banking practices that reduce financial risks to their operations.

Customer identification and due diligence procedures, also known as "know your customer" (Kyc) rules, are part of an effective anti-money laundering and countering terrorist financing (Aml/Cft) regime. These rules enhance the safe's operation of banks and other types of financial institutions and are an effective risk management tool.

2.2 Regulatory landscape of active collaboration

An effective Aml/Cft regime reduces the potential that the institution could experience losses from fraud. Proper customer identification procedures and determination of beneficial ownership provide specific due diligence for higher risk accounts and permit monitoring for suspicious activities. It is essential to raise awareness about the negative impacts of money laundering and inform about various resources that can be available to counter money laundering activities.

As stated above, from the beginning of the fight against money laundering it was acknowledged the need to collaborate with non-authorities organizations, such as banks: the Basel Committee[55] was among the first authorities to highlight the importance of cooperation with banks and other professionals to combat money laundering. The Declaration of Principles of the "Basel Committee" of 12 December 1988 argued that the approach against money laundering should necessarily involve the banking and

[54] The reputational risk is the risk on which Bank of Italy posesita attention on its "Decalogo", an anty money document in which it lists the instruction to be observed for the identification of suspicious transactions.

[55] The Basel Committee was established in 1974 within the Group of Ten55, following the banking crisis in the domestic and international markets; its aim was to promoting the exchange of information between member countries and develop cooperation between supervisors to set up early warning systems in case of banking crises with international repercussions. The Committee members are representatives of the central banks or institutions responsible for banking supervision of each member country.

financial system and those banks, having direct contact with the customer, could be a source to obtaining information about economic transactions that they perform. The Basel Committee introduced the concept of "due diligence" that was defined as the investigative process that is put in place to analyse a person or company to obtain economic and financial information or other information included on the balance sheet. The Basel Committee is acknowledged of having introduced the principles for the prevention of money laundering and banking regulations supervisory practices, even if these documents represent only 'best practices' approach to money laundering. In the document of 1988 are explained the motives that led to the decision to deal with the activities that banks and brokers can make and it is explained that the need to identify these principles arose from the fact that banks have an institution often used by criminals, for "*make payments and transfers of funds from one account to another";* for *"hide the source and beneficial ownership of money; and to provide storage for bank-notes through a safe-deposit facility*"[56]. The Basel Committee has developed other general principles of banking supervision, which contain instructions for the prevention of laundering and, in particular, to the awareness of the customer knowledge: "*Core principles for effective banking supervision*", which talk about knowledge of customers as the basis of prevention of the use of the banking system for money laundering.

In 2003 the Committee, together with the International Association of Insurance Supervisors (IAIS) and the International Organization of Securities Commissions (IOSCO) published a joint paper on the standards anti-money laundering and anti-terrorism applicable to the three regulated sectors (banks, insurance companies, investment companies).

On January 2014 Basel has published new guidelines on the prevention and combating money laundering and terrorist financing; these guidelines conform to the 2012 standards International Standards on Combating Money Laundering and the Financing of Terrorism and Proliferation processed by the FATF and will complement the aims and objectives. They refer to the FATF standards to assist banks in fulfilling national requirements based on those standards.

In fact, as explained in the First Chapter, even FATF has shown interest in regulating active collaboration. Notably, FATF introduces Core Principles for effective banking

[56] P*revention of criminal use of the banking system for the purpose of money-laundering* (December 1988) page 1.

supervision: for example, Core Principle 15, states that: *"Banking supervisors must determine that banks have adequate policies, practices and procedures in place, including strict "know-your-customer" rules, that promote high ethical and professional standards in the financial sector and prevent the bank being used, intentionally or unintentionally, by criminal elements."*.

The recommendations also call for 'special attention' to be paid to all complex and unusually large transactions and to those transactions involving new or developing technologies. This is extremely important as the more intensive the controls placed on transactions taking place through banks and financial institutions the more likely is that criminals will resort to other methods to disguise the source of their wealth.

At European level, the European legislator has introduced the duty of active participation with the Directive 91/308 / EEC of 10 June 1991; over time European Union has expanded the audience and it have been specified what actions they need to take in cooperation with the authorities, until the Third Directive. As said in previous chapter, the fourth Directive, which is not yet recognized in Italy, has introduced significantly changes, even with regard of active collaboration[57]: tax offenses were included in the list of crimes that define criminal activity[58], in this way they constitute a predicate offence of laundering. This means that, if there is the suspect that the origin of the funds can be derived from illegal tax, it will generate an obligation to make a suspicious transaction report. Finally, the sanctions of inappropriate measurement, the reporting of suspicious transactions and record keeping and internal controls are worsened.

With regard to Italy, the first law that introduced obligations for intermediaries was law n. 197/1991: this law introduced the principle of active collaboration for which the intermediaries, previously only committed to facilitate access of information by authorities, they are obliged now to directly participate in the fight against money laundering. This law provided both obligations' identification, transactions' detection and recording, both to report suspicious transaction, independently of its amount.

[57] http://www.dt.tesoro.it/it/news/accordo_riciclaggio.html, 9 December 2015

[58] Art. 3, co. 4: *" 'criminal activity' means any kind of criminal involvement in the commission of the following serious crimes: (f) all offences, including tax crimes relating to direct taxes and indirect taxes and as defined in the national law of the Member States".*

Later, other rules have been introduced, with the aim of improving money laundering regulation. As it has been said in the First Chapter, today in Italy the law which regulates this crime is Decree 231/2007.
Decree 231/2007 states on articles 12, 13, 14 who is compelled to observe the provision of this Decree; those subjects are[59]:

- Financial intermediaries and other entities operating in financial sector, like banks, Poste Italiane, electronic money institutions and asset management companies;
- Professional, like accountants, lawyers and notary;
- Auditors;
- Other entities, like activities that deal with transporting cash and activities engaged in managing casinos.

In the following pages it will described what kind of controls these authorities must make; in this way it is reconstructed and defined the process that these institutions must execute against natural persons and legal entities, and that may be supplemented by the analysis that will be performed in the Third Chapter.
Decree 231/2007 imposes obligations on recipients of this rule, which are: customer due diligence obligation (arts. 15 et seq); abstention' obligation from completing the transaction (Art. 23); registration obligation (arts. 36 et seq); mandatory reporting of suspicious transactions (Art. 41).

Increasingly, legitimate businesses in industries traditionally perceived as low risk are acting as intermediaries in the three phases of money laundering for transnational organized crime and other illegal activity. Financial institutions should therefore modify and expand their customer due diligence beyond traditional high risk business customer profiles for money laundering – such as money transmitters or third party payment processors – and begin evaluating all business customers from a new perspective.

2.3 The importance of risk assessment

In the previous paragraph it was described how authorities, both at national and international level, have proceeded to outline the ways in which external authorities are

[59] For a more completed list, see articles 12, 13, 14 D.Lgs. 231/2007.

involved in fighting money laundering. The importance of risk assessment is highlighted by FATF, which states in Recommendation 1 that "*Countries should identify, assess, and understand the money laundering and terrorist financing risks for the country, and should take action, including designating an authority or mechanism to coordinate actions to assess risks, and apply resources, aimed at ensuring the risks are mitigated effectively.":* through risk assessment countries mitigate their money laundering risk, because it is necessary that Public Authority monitors the risks of money laundering. This is the reason why it was published National Money Laundering on Terrorist Financial Risk Assessment, prepared as part of art. 5 Decree 231/2007. In this case the contribution of private sector is crucial in order to build a complete picture of national money laundering risks and to create a deepened risk assessment. Before starting to see what are the activities they are obliged to do, it is useful to understand what is risk assessment, that serves to highlight key risk areas; it describes how well those risk are managed and it test the controls that a firm has in place to mitigate these risks. Intermediaries and other professionals must be able to recognize a possible danger, especially when they have contacts with companies because, as it was said in the First Chapter, companies hide more easily dirty money, moreover they are able to mask illegal activities, such as drug trafficking.

Financial firms must put in place systems and controls to identify, assess, monitor and manage money laundering risk; these systems and controls must be proportionate to the nature, scale and complexity of a firm's activities. In its *Financial crime: a guide for firms*, Financial Conduct Authority[60] indicate what are possible examples of poor practice that a firm must to consider when evaluating its risk assessment. Financial firms must pay attention on their risk classification system, means that they should be able to classify low, medium or high risk and the reasons behind this choice; moreover, they should pay particular attention on new relationship, looking at their potential profitability and their danger.

In the document "*Frequently Asked Questions on Risk Assessments for Money Laundering, Sanctions and Bribery & Corruption"* of Wolfsberg Group[61] it is possible

[60] The Financial Conduct Authority (FCA) is a financial regulatory body in the United Kingdom, but operates independently of the UK government; even this is not an Italian or European body, it is useful for the purposes of understanding and managing risk assessment.

[61] Wolfsberg Group (2015),"*Frequently Asked Questions on Risk Assessments for Money Laundering, Sanctions and Bribery & Corruption"* , page 3. The Wolfsberg Group is an association of thirteen global banks which aims to develop frameworks and guidance for the

to see a standard methodology to conduct risk assessment, that is, determine the residual risk in every Financial Institution. The residual risk rating is used to assess whether the money laundering risks within the Financial Institution are being adequately managed. This involves three steps:

- Determine the Inherent Risk[62]: this can be made considering five risk categories of its own Clients, Products and Services, Channels, Geographies and Other Qualitative Risk Factors. The Association recommends risk based approach's use, in order to assign a score for each risk factor which reflects the level of risk associated with that risk factor. It is advisable to create subcategories for each risk factor depending on the risk score.
- Assess the Internal Control Environment: once the inherent risk have been identified and assessed, internal controls must be evaluated for their effectiveness in mitigating the inherent money laundering risk.

  In this phase there are all controls categories that will be illustrated later, such as Client Due Diligence, Enhanced Due Diligence, Record Keeping, Monitoring and Controls and others.
- Derive the Residual Risk: once both the inherent risk and the effectiveness of the internal control environment have been considered, it is possible to determine the residual risk. In order to be clear and correct, the Association suggest creating a 3 tier rating scale, with High, Moderate and Low level of residual risk.

2.4 Identification of the risk based approach

Risk assessment is based on the risk based approach that is an essential foundation in allocating anti money laundering resources efficiently: this principle is included both in the FATF Recommendations[63], both in European and Italian Decree.

The first generation of anti money laundering solutions operated on a rule based approach, where the regulator determines the controls that the regulated must apply, but, as the sophistication of money laundering evolved over the years, it was necessary to

management of financial crime risks, particularly with respect to Know Your Customer, Anti-Money Laundering and Counter Terrorist Financing policies.

[62] Inherent Risk in this case represents the exposure to money laundering risk in the absence of any control.

[63] The risk-based approach is central to the effective implementation of the FATF Recommendations adopted in 2012. Between 2007 and 2009, in order to assist both public authorities and the private sector in applying a risk-based approach, the FATF has adopted a series of guidance in co-operation with relevant sectors.

introduce an intelligence and more flexible approach to anti money laundering by way of customers risks profiling, suspicious activity reporting and monitoring. As it's noticed by Louis de Koker[64] *"Risk is not unimportant because a reasonable regulator will determine the relevant controls based on its assessment of the risks. The main difference between the two approaches is the the allocation of responsibility for determining the risk as well as the appropriate risk management actions: the regulator (rule-based) and the regulates (risk-based)."* The reason behind this choice is the fact that money laundering risks are not the same for every country: a country that is a large financial centre faces significantly different risks than a country that does not have an important role in the international financial market. The risk based approach enables countries to use this resources more wisely by devoting them the areas where the risks are the highest; the same holds for banks and other institutions, because the revised Recommendations allow countries to permit individual institutions to design elements of their anti money laundering control measures on a risk sensitive basis. In this way it is possible to hold intermediaries responsible in the application of the right level of control and at the same time give them freedom to make decision: what is important is to make a proper control[65].

The most recent update of the FATF Recommendations, in 2012, emphasises the risk based approach even more than previous version of the standards: the objective of the risk based approach is to ensure that anti money laundering measures are commensurate with the risk identified, as well as to enable decision making on effective resource allocation.

With regard to Italian Regulation, art. 20 of Decree 231/2007 says that the burden of proof that the entity has select which is the customer profile to be monitored. The reporting of suspicious transactions is entrusted to the weightings of information obtained, also based on customer history: to do this, it is useful read a Bank of Italy's provision[66], which explain how to interpret article 20 of the Decree. Particularly, considering legal entities, banks should verify if in the past the customer or, in the case of a legal entity, its related person, have received sanctions for violation of anti money laundering rule. It is very important to understand what are the aims of the company and

[64] Louis de Koker, (2009),"Identifying and managing low money laundering risk", Journal of Financial Crime, Vol. 16 Iss 4 pp. 334 – 352, page 336.

[65] Art. 16 D.lgs: 231/2007.

[66] This document is "*Provvedimento recante disposizioni attuative in materia di adeguata verifica della clientela, ai sensi dell'art. 7, comma 2, del Decreto Legislativo 21 novembre 2007, n. 231.",* 2013, page 10 and subsequents.

how it tries to achieve them: that information can be known not only by reading its Status but also watching what kind of operations it performs to see if its activities correspond to its purposes and its intended nature.

It is also important to pay attention on the legal form choose: as an example, in the First Chapter it was highlighted that criminals often use for the creation of a company the Limited legal form, because with this type of structure it is possible to hinder the identification of the beneficial owner.

Banks must scrutinize customers' activity; this imply to look if the companies has business or financial connections or it has shareholdings with foreign entities, particularly if it is a state that present a deficient money laundering legislation or that belongs to the Non-Cooperative Countries[67].

Then, there are other factors that may alarm banks: for example, if a company is in financial difficulties, it may be more exposed to the risk of criminal infiltration. There are also activities, which by their nature, are more exposed to the risk of money laundering and that for this reason they must be analysed in a more specific way: the cash-intensive business, thanks to their high use of cash, can be used by criminals to clean money.

The last customer's feature that must be analysed is its geographical interest area: if a company is based in an area that is economically weak and has a high degree of infiltration of crime has greater risk[68], especially if this area is abroad. The same applies if a company holds interests in other companies that are based in areas at risk, as it will see in Third Chapter. The same holds for geographical location of the transaction requested by the customer.

On article 20, co. 1, letter b) the Legislator has introduced criteria for evaluating the risk of laundering connected with the type of operation; it is observed type of operation, the implementation procedures, the destination's country or countries of the product and its total amount[69]. This is because institutions subject to Decree 231/2007 must be able to prove to authorities that their measures taken are appropriate to the level of risk of

[67] In those countries, that are also called 'tax haven' countries, anti money laundering rules are minumun; they are gather together in a Black List, that is periodically updated. According to Law May 22, 2010, n. 73 all Italian entities who conduct business operation with them have the obligation to report to Italian Tax Office all those transactions, but only if the total amount of such transactions exceed the threshold of € 10,000.

[68] One way to determine the level of risk in money laundering is to look at the use of cash, as it is not traceable; in Italy, National Risk Assessment has produced a ranking of the provinces where there is an excessive use of cash andare therefore more exposed to the risk of money laundering.

[69] Art. 20, co. 1, D. lgs. 231/2007.

money laundering or terrorist financing. For the money laundering risk's evaluation financial institution must refer to instruction issued by Bank of Italy, which is called Bank of Italy Handbook.

2.4.1Bank of Italy Handbook

This handbook was issued in 2001, and its goal was to help all financial intermediaries[70] in the identification of money laundering's potentially suspicious transactions: in a later moment, in 2010[71], Bank of Italy has published new *"indicatori di anomalia"* for intermediaries: here, twenty-one cases of anomalies are indicated, which in turns are disaggregated into various "sub-indices". In this list it is possible to find both indicators that are updated, and others that are completely new; this is because Financial Intelligence Unit analysed the evolution of the most commonly behaviours discovered in their reports. Those indicators are then issued by different authorities, depending on the subject: Bank of Italy issues provisions for financial intermediaries and other entities operating in the financial sector; the Justice Ministry, in consultation with the professional orders, is responsible for professionals; the Interior Ministry is responsible for the remaining non-financial and public administrations.

This document demonstrate the importance of active collaboration and the need of these institutions get going to know their costumers and be able to assess whether the transactions they carry out are related to their activities or result from illegal activities.

This Handbook is divided into two parties: the first one regulates rules that intermediaries must meet to properly carry out their monitoring role; the second one provides a list of the main abnormality indicator of operations that should be controlled

[70] Specifically, as it is sayed on article 2, the beneficiaries of this provision are: "*banche, Poste italiane S.p.A., istituti di moneta elettronica, istituti di pagamento, società di intermediazione mobiliare (SIM), società di gestione del risparmio (SGR), società di investimento a capitale variabile (SICAV), imprese di assicurazione che operano in Italia nei rami di cui all'articolo 2, comma 1, del CAP, agenti di cambio, società che svolgono il servizio di riscossione dei tributi, intermediari finanziari iscritti nell'elenco speciale previsto dall'articolo 107 del TUB, intermediari finanziari iscritti nell'elenco generale previsto dall'articolo 106 del TUB, succursali insediate in Italia dei soggetti indicati alle lettere precedenti aventi sede legale in uno Stato estero, Cassa depositi e prestiti S.p.A., società fiduciarie di cui alla legge 23 novembre 1939, n. 1966, soggetti operanti nel settore finanziario iscritti nelle sezioni dell'elenco generale previste dall'articolo 155, comma 4, del TUB, soggetti operanti nel settore finanziario iscritti nelle sezioni dell'elenco generale previste dall'articolo 155, comma 5, del TUB, altri soggetti esercenti attività finanziaria".*

[71] Resolution 616 of August 24; source Ranieri Razzante, http://www.ilsole24ore.com/art/norme-e-tributi/2010-08-28/antiriciclaggio-nuovi-indicispia-080020.shtml?uuid=AYMhzWKC.

in a deeper way[72]. With this list financial institutions are able to reduce uncertainty margins related to the fact that this kind of evaluation has a 'subjective' base and it is strenuous to identify all possible existing type of offences. Moreover, they must consider case by case: as an example, an operation cannot be justified for a company, but it may be economically justifiable if requested by another client.
Thank to Bank of Italy Handbook is it possible to reduce the costs necessary to make this analysis and it is possible to properly conduct the burden of reporting suspicious transactions.

Specifically, in the first part Bank of Italy clarifies that the suspicious transaction report must be made even if the underlying offense has already been reported to authorities. About this, Razzante in his article explain this with an example: if the bank becomes aware that his client has committed a fraud on checks, the bank will report the customer, but it must remember to warn of potential suspicious transaction, if there are the conditions of that. This is possible because there exist a deep knowledge of the customer, through the Know Your Customers principle, in which Legislator requires to identify and record in Centralized Computer Archive both the data of owner's operation both the data of beneficial owner. It is clear that the principle is particularly important with regard to the case of a company, given the fact that often it is used to hide the beneficial owner, which could be a person linked to crime. Moreover, in addition to Know Your Customers rules, there exists a more objective analysis, an informatics support called GIANOS[73]: with this system it is possible to identify anomalies from customer's normal activity.
Combining subjective and objective elements it is possible to have a complete knowledge of the customer and it make possible to find more easily suspicious transactions because, based on the economic and financial profile of the customer, intermediaries can decide how to carry out the economic analysis. As an example, considering a company, before starting to see anomalies found by GIANOS, intermediaries should analyse the company, such as knowing its field, its economic context and the existence of holdings in other companies.
There are other factors that make authorities suspicious, for example when there are outliers in certain balance sheet items: in particular in the Third Chapter it will try to

[72] It should be noticed that this list is not exhaustive, they are only examples.
[73] GIANOS is "*Generatore di Indici di Anomalia per le operazioni sospette*".

understand if there exist a relationship between criminals companies and the presence of equity participation.

With regard to the second part, the indicators have the aim to reduce the margins of uncertainty associated with subjective or discretionary behaviour; moreover, they contribute to the proper and uniform commitment to report suspicious transactions. It is worth to notice that this does not mean that the presence of one of those indicators it is not need to immediately send a report to the FIU, but supervisors have to pay attention to the customer.

In his document *"Provvedimento recante gli indicatori di anomalia per gli intermediari"* Bank of Italy make a list of indicator of possible suspicious transaction: particularly, there are six macro areas[74]:

- Anomaly indicators related to customers: the list starts with customers because there is the need to highlight the importance to the identification of beneficial owner and truthfulness of information given by customers. This, in particular, is important considering companies because, as it was said in previous Chapter, firms permit to hide more easily the beneficial owner and the origin of money ;
- Anomaly indicators related to operations: here financial intermediaries must pay attention on the primary activity that the company should carry and what it really does. It is also important the kind of operations companies carry out: as it was said in the First Chapter, launders often use companies to hide dirty money and to pass this money into other hands using false invoices which take only the passage of money but not the goods. Moreover, financial intermediaries should pay attention operations that appear disadvantageous for the firm: if, for example, a company makes transactions involving sales or purchases at a price that is significantly disproportionate to current market value, this may hide a suspicious transaction[75];
- Anomaly indicators related to means of payments: this kind of indicators are related to the abuse of use of cash, because, as explained above, dirty money often remains in cash;

[74] For coherence, it was decided to report what are possible suspicious behaviour related to legal subjects.

[75] In general, intermediaries must pay attention on those transactions in which there is transfer of large sum of money, but they are not justified considering the activity performed by the company, especially if the move is made with foreign companies and the relations between the parties can not be justified.

- Anomaly indicators related to financials tool operations: in this case intermediaries must pay attention on the activities the company seek on purchasing and selling of financial instruments, looking at whether these operations are consistent with its economic and financial profile;
- Anomaly indicators related to financing terrorism: since the system for money laundering controls is used also to counter terrorism, financial intermediaries must ensure that the transactions of their clients are not related to terrorism financing phenomena. The international system for preventing and combating the financing of terrorism is based on the application of restrictive measures to "freeze" the funds held by "designated" individuals and legal entities identified by the United Nations and the European Union: those measures have a legal basis on Leg. 109/2007[76].

As highlighted by Pietro Cenci[77] it is important to remember that, if a financial intermediaries finds one of those indicators, it must not immediately report it to the FIU, but it involves a deepening of the suspected operation; moreover, it is very important to make a careful assessment of the operations on which money is transferred often for large sums, this is because often this tool hides significant conduct regarding money laundering.

2.5 How to protect from money laundering risk

The importance of risk assessment is highlighted in many Documents, because it helps all financial institution to have adequate policies and processes to prevent the bank from being used, intentionally or unintentionally, for all kind of criminal activities, including money laundering. Thanks to risk management process it is possible to create an up-to-date customer profile and it helps both the intermediary and the financial system as a whole: particularly, the risk management process is necessary to pay more attention on

[76] In particular, Leg. 109/2007 for the identification of freezing procedures, as regard to freezing of founds says that there is "*divieto di movimentazione, trasferimento, modifica, utilizzo o gestione o di accesso ad essi, così da modificarne il volume, l'importo, la collocazione, la proprietà, il possesso, la natura, la destinazione o qualsiasi altro cambiamento che consente l'uso degli stessi, compresa la gestione di portafoglio"* (art. 1, comma 1, lett. e). With regard to freezing of economic resources thare is "*divieto di trasferimento, disposizione o utilizzo, compresi, a titolo esemplificativo, la vendita, la locazione, l'affitto o la costituzione di diritti reali di garanzia*" (art. 1, comma 1, lett. f).

[77] P.Cenci(2010), "*La nuova normative antiriciclaggio, Direttive Comunitarie e normativa nazionale*", page 107.

categories that are more involved in the system of laundering: the FIU annual reports show that there are few advisories of sophisticated mechanisms, such as the use of corporate mechanisms[78].

Paragraph 2.3 has been shown the three steps to conduct an adequate risk assessment: as it was said in this paragraph, a bank should develop a thorough understanding of the inherent money laundering risks, and those procedures must be designed and implemented to adequately control the identified risks, as it was said by Basel Committee:*"the policies and procedures for CDD, customer acceptance, customer identification and monitoring of the business relationship and operations (product and services offered) will then have to take into account the risk assessment and the bank's resulting risk profile"*[79] .Of course, as it was explained in paragraph 2.4, this is based on operational data and other internal information collected by the bank as well as external sources of information

For risk management it is essential to create an adequate control system: the Basel Committee pinpoint "*three lines of defence*"[80] that a bank should have to control the risk of its business. A strong oversight of anti money laundering risk management and the adoption of a robust ethical stance by senior management are fundamental to the operation of effective AML systems and controls.

- The first line of defence is the bank's business units, like its front office or its customer-facing activity. They are the first that come into contact with customers and consequence, they are the first who can become aware of anomalies: this is the reason why it is fundamental to provide them guidance on how to keep and detect suspicious transactions.
- The second line of defence includes the chief officer in charge of anti money laundering, who is responsible for monitoring of the fulfilment of all anti money laundering duties by the bank; in order to fulfil his duties, he should make sample testing of compliance and review of exception reports to alert the board of director. Moreover, the chief officer should be in contact with all anti money laundering issues for internal and external authorities, including Financial Intelligence Unit. To do this the chief AML officer should be provided with

[78] This issue is highlighted in the speech of Dott. Luigi Mariani, during the 10th Compliance Meeting, June 2014, page 11.

[79]The Basel Commettee (2014), *"Sound management of risks related to money laundering and financing of terrorism",* page 4.

[80] The Basel Commettee (2014), *"Sound management of risks related to money laundering and financing of terrorism",* page 5.

sufficient resources to execute all responsibilities effectively and above all play a central role in the bank's anti money laundering regime.

The AML office should be independent and robust and it should have a direct reporting line with executive management; it is responsible to the creation of an adequate anti money laundering solutions landscape, through which it is possible to understand and prevent money laundering issues. First of all, it should focus on formulating a compliance policy, assess the risks of money laundering and create a strategy, evaluate and select anti money laundering tools and assess technology. Secondly, it is responsible of the creation of a robust data exploration and visualization system and this is given also by the modification of rules to reduce false negatives or positives

- The third line of defence is internal audit; in particular, a bank should establish policies for conducting audits of the adequacy of the bank's AML policies identified risks, the effectiveness of bank staff in implementing the bank's procedures, the effectiveness of compliance oversight including parameters of criteria of automatic alerts and the effectiveness of the bank's training of relevant personnel.[81]

Of course it is essential to create collaboration between these three steps and this can be achieved through the use of reports, such as suspicious activity reports and customized reports for internal and external purposes. In this way it is possible to report solution, perform multidimensional analysis and create a business intelligence dashboard. It is essential that senior management take responsibility for the firm's AML measures; this includes knowing about the money laundering risks to which the institution is exposed and ensuring that steps are taken to mitigate those risks effectively: for this purpose, they must be informed about decisions of entering or maintaining a business relationship and they must be provided of an accurate picture of the risk to which the firm would be exposed if the business relationship were established or maintained.

Financial institution should have procedures in place to ensure that there is a clear allocation of responsibilities and an appropriate approval of client relationships, in

[81] Moreover, external auditors have an important role: in cases where a bank uses external auditors to evaluate the effectiveness of AML policies and procedures, it should ensure that the scope of the audit is adequate to address the bank's risks and the auditors assigned have the requisite expertise and experience.

particular for those accounts which were assessed as high risk from a money laundering perspective.

2.6 Customer identification and Due Diligence[82]

As stated above, the private sector is a potential key user of any ML risk assessments, because the bank should have a thorough understanding of all the risks associated with its customers: in particular, financial institution may have valuable information on the structure, organisation and size of sectors to help with determining the level of risk presented and to assist in identifying vulnerabilities[83].

The anti money laundering Directive allows banks to determine the extent of customer due diligence measures on a risk based approach and for this reason it is possible to "tailor" the controls.

Customer Due Diligence consists on measures taken to all entities obliged by law to identify their customers and to verify the customer's identity by using documents or reliable independent sources; it also includes obtaining information about the purpose and reasons for opening an account, anticipated account activity, clients' business and business structures. In his way it is possible to define the money laundering and financing terrorism risk profile attributable to each customer.

All banks and other financial institutions should have policies and procedures in place to conduct due diligence on its customers sufficient to develop customer risk profiles either for particular customers. In this way the risk profile facilitate the identification of any account activity that deviates from behaviour that would be considered "normal" for the customer. Even the Basel Committee[84] considers that the adoption of an effective due diligence an essential part of bank's risk management practices, as banks with inadequate due diligence programmes may be subject to significant risk, especially legal and reputational risk.

Customer due diligence is one of the focal point of D. 231/2007: the first Chapter of the second Title of the law is dedicated to it; from 1st January 2014 new obligations have

[82] A synonym of Customer Due Diligence is Know Your Customer (KYC); this term can also refer to suitability checks related to the regulated sales of financial products.

[83] Customer segmentation founds on drive and processing of data and information. The data' gathering may be done through questionnaires. The development of the risk profile can also be done using procedures that assign automatically the risk class.

84 Basel Committee (2004).

been changed on the basis of Bank of Italy Instructions, published on April 2013[85]. The previous law, Law n. 197/1991, for Customer Due Diligence considered only the collection of customer' data and information, such as his name, surname, date of birth, but it was clear that those kind of controls were not sufficient: specifically, the law of 1991 did not consider constant and continuous monitoring, that is essential to detect potential problems and anomalies associated with the operations made by the customer.
It should be notice that the Decree provides standards both in case of new customers' identification both in case of existing customers' due diligence; in this way it is possible to identify money laundering risk and it is possible to properly evaluate whether to proceed or not with their relation.
Customer due diligence consists on four tasks:

- Customer's identification; this must be proved on the basis of documents, data or information obtained from a reliable and independent source. In particular, if the customer is a legal entity, the identification must be made against the customer, but even against the performer of the operation, looking at his identification information and about his power of attorney;
- Identification of an eventual beneficial owner: where the client is a company, it is important to be able to follow the chain of title to know who is the beneficial owner and conduct due diligence on the principal beneficial owners. It occurs both thanks to information provided by the customer, who is obliged[86] to provide all information necessary to enable the entity to fulfil its obligations, either by using public documents;
- To obtain information on the purpose of the account and, if applicable, the occasional transaction;
- Constant control over the business relationship.

Article 15 considers cases where financial intermediaries are obliged to do customers due diligence: when they establish a continuing relationship[87]; when they carry out occasional transactions, which involve the handling of money for an amount not less

[85] For auditors these new obligations are based on the "CONSOB Regulation" published December 2013.
[86] Decree 231/2007, art. 21 provide that *"I clienti forniscono, sotto la propria responsabilità, tutte le informazioni necessarie e aggiornate per consentire ai soggetti destinatari del presente decreto di adempiere agli obblighi di adeguata verifica della clientela".*
[87] Bank of Italy defines continuing relationship as a contractual relationship that gives rise to more than one operations.

than 15,000 euro, regardless of whether they are carried out with a single operation or in several operations that appear connected; when there is suspicion of money laundering or terrorist financing; when there are doubts about the veracity or adequacy of information previously obtained.

On the other hands, professional and auditors must follow article 16, in which there is the duty to check if customers professional performance has for object goods or means of payment that are equal to or greater than 15,000 Euros, this is also true in the case of operations split; when the operation has indeterminate value; when there is suspicion of money laundering or terrorist financing; when there are doubts about the veracity or adequacy of information previously obtained.

One of the main challenging tasks is to confirm information obtained on customer and beneficial owner: as stated above, customer data should be compared with other sources "reliable and independent"[88]; according to the risk-based approach, these checks must be made in an appropriate manner, in the light of the risk profile of the customer. In all these cases the addressee of the rule evaluates whether to perform further evidence, and it may resort to entities that provide economic or commercial information or to more independent sources.

Control that runs on existing customers must be constant, in this way the client profile is updated and it is possible to identify elements of inconsistency, which might be related abnormalities; to do this they analyse customers' operations and after they compare them with other information. This operation is called ongoing monitoring and it is an essential aspect of effective ML risk management, because in this way they are consistent with what the entity knows about the customer.

The update frequency is determined by each institution on the basis of their specific risk. The results of these audits may lead to the update of their own information and their risk profile, or it can lead them to make other checks; in the extreme cases, it can lead to reporting of suspicious transactions, freezing of funds, to abstain from performing the transaction or the termination of the relationship.

[88] Bank of Italy mentions some of these sources, such as public records, private authenticated documents, documents of the chamber of commerce or other register, deed of incorporation,balance sheets, statutes; information from public authorities, including Public Administration, even from foreign states.

Those involved in the customers due diligence are required to keep obtained documents[89], in order to demonstrate to the supervisory authorities that the followed procedures were correct to fulfil their legal obligations and to allow their use in the context of investigations of money-laundering operations, financing of terrorism or other crimes. Moreover, these documents can be useful for FIU during his in-depth analysis. It is considered that the documents will be kept for ten years from the start of occasioning operation or from the date of closing of the continuing relation.
Financial Services Report[90] for customers' verification suggest including inspection, made by managers of the institution, at their homes or business, both at the start of a relationship and also on an ongoing basis: this may allow substantiating clients' personal and business circumstances and cross referring these to patterns of activity on clients' accounts.

Article 23 of the Decree provides that, in case the entities which must follow those roles are not able to respect them, they cannot establish the relationship with the customer. The abstention duty is, as it has been defined by Pietro Cenci[91], is the obvious corollary of the due diligence, because, if the subject of the Decree cannot verify their customers, it's impossible to create any relationship between them. In the case that the obligation to report suspicious transactions to Financial Intelligence Unit, these are triggered by a decision of the entity, but only in the case of money laundering and terrorist financing suspect it is compulsory.
Finally, there are cases where this prohibition does not apply: when the abstention is not possible on the basis of legal obligations, where the execution transaction by its nature cannot be postponed and when abstaining may impede investigations[92].

2.6.1 The treatment of high and low money laundering risks

Risk based approach entails that compliance must be adapted according to the money laundering risk associated with the profile of the client concerned. This is the reason

[89] Bank of Italy (2013), *Provvedimento recante disposizioni attuative in materia di adeguata verifica della clientela, ai sensi dell'art. 7, comma 2, del decreto legislativo 21 novembre 2007, n. 231*, page 19.
[90] Financial Conduct Authority, *Bank's control risk in trade finance,* July 2013, page 15.
[91] P.Cenci(2010), "*La nuova normative antiriciclaggio, Direttive Comunitarie e normativa nazionale*", page 45.
[92] However, article 41 provides that the report of suspicious transaction is made.

why the Decree 231/2007 has introduced "enhanced requirements due diligence" and, in other cases, where the risk is lowest, the "simplified due diligence obligations". These two extreme cases are interesting to observe because, if on one hand the enhanced due diligence has an object that must be handled with care, on the other obligations simplified are often overlooked because the risk based approach focuses attention on high-risk matters. At the same time, simplified controls are easier and cheaper to implement and maintain and, if correctly implemented, they free up resources that can be focused on higher risk cases.

With regard to simplified customer due diligence, it is regulated by articles 25, 26 and 27 of the Decree 231/2007; these simplified procedures for customer due diligence apply when the customer falls into the following categories: *"a uno dei soggetti indicati all'articolo 11, commi 1 e 2 , lettere b) e c); un ente creditizio o finanziario comunitario soggetto alla direttiva; un ente creditizio o finanziario situato in uno Stato extracomunitario, che imponga obblighi equivalenti a quelli previsti dalla direttiva e preveda il controllo del rispetto di tali obblighi; una società o un altro organismo quotato i cui strumenti finanziari sono ammessi alla negoziazione su un mercato regolamentato ai sensi della direttiva 2004/39/CE in uno o più Stati membri*[93]*, ovvero una società o un altro organismo quotato di Stato estero soggetto ad obblighi di comunicazione conformi alla normativa comunitaria".*

Therefore, a simplified due diligence is chosen if the customer is a bank: this rule applies because it assumes the absence of risk of money laundering, since both parties are financial intermediaries. It is important for our analysis to observe that article 25 does not apply to trusts, as they are always required to provide, upon request, the information about the settlor to the one who has to carry out an operation from among those listed in the decree; for the simplified due diligence, these kind of data are not provided. Of course, there could be situation in which it is not possible to conduct a simplified due diligence; Bank of Italy lists these cases[94]: *"vi siano dubbi sull'idoneità o la veridicità delle informazioni acquisite ai fini della riconduzione del cliente alle categorie sopra indicate; non vi siano più le condizioni per la configurazione di un basso rischio di riciclaggio e di finanziamento del terrorismo – che consente l'applicazione della procedura semplificata – in base al giudizio dei destinatari, che si*

[93] The Economy Ministry of identifies non-EU states whose regime is deemed to be equivalent.
[94] Bank of Italy (2013), *Provvedimento recante disposizioni attuative in materia di adeguata verifica della clientela, ai sensi dell'art. 7, comma 2, del decreto legislativo 21 novembre 2007, n. 231,* page 22.

avvalgono, a tal fine, degli elementi di valutazione indicati nella Parte Prima, Sezione II; vi sia comunque il sospetto di riciclaggio o di finanziamento del terrorismo; la Commissione europea adotti, con riferimento ad un Paese terzo, una decisione di accertamento a norma dell'articolo 40, paragrafo 4, della terza direttiva antiriciclaggio; in tal caso, i destinatari delle presenti istruzioni non possono applicare misure semplificate di adeguata verifica della clientela agli enti creditizi e finanziari o società quotate del Paese terzo in questione o ad altri soggetti in base a situazioni che rispettano i criteri tecnici stabiliti dalla Commissione europea a norma dell'articolo 40, paragrafo 1, lettera b), della terza direttiva antiriciclaggio."

One of the most interesting features of simplified due diligence is that the beneficiaries of the Decree are exempt from registration in Centralized Computer Archive, although it must demonstrate that they gathered enough information to determine whether it is possible to apply the simplified procedure. For example, the beneficiary must verify the identity of the client, acquiring data about his name, legal status, registered office, and tax code; moreover, they are obliged to verify the persistence of the conditions for the application of the simplified procedure and its frequency is determined in accordance with the risk-based approach.

Finally, in paragraph 6 of Article 25[95] there are cases in which recipients are not required to carry out the obligations of customer due diligence; in any case, if there are

[95] The article says*:" a) contratti di assicurazione-vita, il cui premio annuale non ecceda i 1.000 euro o il cui premio unico sia di importo non superiore a 2.500 euro; b) forme pensionistiche complementari disciplinate dal decreto legislativo 5 dicembre 2005, n. 252, a condizione che esse non prevedano clausole di riscatto diverse da quelle di cui all'articolo 14 del medesimo decreto e che non possano servire da garanzia per un prestito al di fuori delle ipotesi previste dalla normativa vigente; c) regimi di pensione obbligatoria e complementare o sistemi simili che versino prestazioni di pensione, per i quali i contributi siano versati tramite deduzione dal reddito e le cui regole non permettano ai beneficiari, se non dopo il decesso del titolare, di trasferire i propri diritti; d) moneta elettronica quale definita nell'articolo 1, comma 2, lettera h-ter), del TUB, nel caso in cui, se il dispositivo non è ricaricabile, l'importo massimo memorizzato sul dispositivo non ecceda 250 euro oppure nel caso in cui, se il dispositivo è ricaricabile, sia imposto un limite di 2.500 euro sull'importo totale trattato in un anno civile, fatta eccezione per i casi in cui un importo pari o superiore a 1.000 euro sia rimborsato al detentore nello stesso anno civile ai sensi dell'articolo 11 della direttiva 2009/110/CE ovvero sia effettuata una transazione superiore a 1.000 euro, ai sensi dell'articolo 3, paragrafo 3, del regolamento (CE) n. 1781/2006. Per quanto concerne le operazioni di pagamento nazionali, il limite di 250 euro di cui alla presente lettera è aumentato a 500 euro; e) qualunque altro prodotto o transazione caratterizzato da un basso rischio di riciclaggio e/o di finanziamento del terrorismo che soddisfi i criteri tecnici stabiliti dalla Commissione europea a norma dell'articolo 40,*

doubts about the information obtained, it is necessary to apply the ordinary due diligence.

For the purpose of this paper it is more interesting to look at the enhanced due diligence. The enhanced due diligence consists on the adoption of more detailed and frequent measures, that must be made in different areas for an adequate control. For example, it requires the acquisition of more information about the identification data of the customer or the beneficial owner; moreover, it is required to increase the frequency of monitoring continous controls and, with regard to occasional operations, it is required to carried out further investigation on the nature and purpose of the transaction.
Article 28 of the Decree provides this throught controls when:

- The customer is not physically present, or, in case of a legal entity, its legal representative; to compensate this risk there are specific measures to be taken, which are listed on Article 28. These measures are: the assessment of the customer through documents and additional measures, in order to verify the veracity of what has been provided, if a payment has already been made it must verify that this operation has been carried out through an account opened in customer' name; in this way it is possible to verify the existence of the client.

  There are some cases in which the physical presence of the customer is not necessary, for example when the identification and verification have already been carried out; if the recipient of the decree collaborates with third parties for the due diligence and those carried out checks, as required by article 29 of the Decree; if the recipient acquires public documents, private documents authenticated.

  In the event that the customer is not physically present and there is also the absence of direct contact with the third party, which could be internet banking and phone banking it is essential to pay more attention, because greater is the risk of fraud related to electronic identity theft and can seriously affect the reliability of the data collected.

  Obviously, in extreme cases where it is not possible to obtain data and information needed or is not possible to verify its reliability, otherwise there is no confirmation about the coincidence of the customer with the entity or person

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paragrafo 1, lettera b), della terza direttiva antiriciclaggio,se autorizzato dal Ministro dell'economia e delle finanze con proprio decreto."

to whom the data are related, or, after the check inconsistencies have emerged, the supervisor cannot begin or continue the relationship with the customer and it must assess whether to send a suspicious transaction report or not.

- In the case of Politically Exposed Person and residents in the country who are or have been entrusted with public prominent; PEPs are defined by Third Money Laundering Directive as "natural persons who are or have been entrusted with prominent public functions and immediate family members, or person known to be close associates, of such persons". This definition only applies to those who reside out of state. Because of their position PEP status may lead to a client being considered high risk, and thus it is necessary an enhanced due diligence. The supervisors must, on a risk sensitive basis, to have appropriate risk based procedures to determine whether a customer is a PEP; to do this, in addition to obtaining the relevant information from the customer, they must use additional sources, such as commercial databases of the countries of origin. Moreover, they should take reasonable measures to establish the source of wealth and source of funds of such customers; if the supervisor is unable to verify the reliability of the PEP, it cannot continue the relationship.
- In the case of correspondent accounts with non-EU entities; in this case they gather information about its activities and on the supervision to which it is subject;

Moreover, Bank of Italy[96] identifies other situation in which the supervisors should adopt enhanced due diligence:

- In the case of transactions of cash payment from other countries: if the value of the transaction is equal to or greater than 10,000 euros the recipient is required to obtain a copy of the cash transfers statement, as considered by Article 3 of the legislative decree n. 195/2008; if it cannot get this statement, it gives up the operation and evaluates whether to send a suspicious transaction report to FIU.
- If there is suspicion of high risk of money laundering it has already been sent to FIU the suspicious transaction report;
- If the customer uses products, operations, technologies that can increase the risk of money laundering. To this end, supervisors must remain informed of new

[96] Bank of Italy (2013), *Provvedimento recante disposizioni attuative in materia di adeguata verifica della clientela, ai sensi dell'art. 7, comma 2, del decreto legislativo 21 novembre 2007, n. 231,* page 24.

types of laundering, both nationally and internationally; they can use also the indicators identified by the Bank of Italy's Handbook.

Finally, as it was highlighted in the First Chapter, launders often hold dirty money in cash: the use of large bills, like 500 euro and 200 euro, presents a greater money laundering risk, since it facilitates the transfer of large amounts of cash, favouring untraceable financial transactions; however, at the same time, this method is risky and often is preferable to use checks, bank or credit cards which are more secure. Therefore, in the presence of withdrawal and payment with use of large bills for amounts exceeding € 2,500, recipients must carry out specific investigations, also together with the customer, in order to verify the reasons behind this operation, allowing for the exclusion of any connection with money laundering. Such considerations are even more important in the case of customers who have a significant financial handling both considering the frequency of operations and their amount, such as the case of a business.

2.7 Reporting of suspicious transactions

In the previous pages it has been described what are the warning signs that may lead the suspicion of money laundering: as we have seen, this happens during the due diligence, which, thanks to the problem indicators' identification, identifies risky situations. The next step is the reporting to the authorities responsible for the suspicious transaction.
Ongoing monitoring and review of accounts and transactions will enable banks to identify suspicious activity, eliminate false positive and report correct suspicious transactions. This requirement was introduced so that the signals sent to UIF can bring out operations for the completion of which are used money or securities of dubious origin to be reinvested into the legal economy. According to art. 41 of Decree 231/2007, the recipients of this law must "*inviano all'UIF, una segnalazione di operazione sospetta quando sanno, sospettano o hanno motivi ragionevoli per sospettare che siano in corso o che siano state compiute o tentate operazioni di riciclaggio o di finanziamento del terrorismo. Il sospetto è desunto dalle caratteristiche, entità, natura dell''operazione o da qualsivoglia altra circostanza conosciuta in ragione delle funzioni esercitate, tenuto conto anche della capacità economica e dell''attività svolta dal soggetto cui è riferita, in base agli elementi a disposizione dei segnalanti, acquisiti nell' ambito dell''attività svolta ovvero a seguito del conferimento di un incarico. E' un*

elemento di sospetto il ricorso frequente o ingiustificato a operazioni in contante, anche se non in violazione dei limiti di cui all'art. 49, e, in particolare, il prelievo o il versamento in contante con intermediari finanziari di importo pari o superiore a 15000 euro".

This Decree introduced active cooperation obligation: in the precedence role of law legislator had imposed the reporting requirement for each operation *"che induca a ritenere che il denaro, i beni o le utilità oggetto delle operazioni possano provenire dai delitti previsti dagli articoli 648 bis e 648 ter del codice penale"*[97]. With Article 41 it is made a step forward in the fight against money laundering , because now it is sufficient the suspect that there are transactions of money laundering[98] to make report to FIU. This was necessary to resolve the operational and normative uncertainty, because it is not possible to list all circumstances that could lead to an advisory.

It is clear that cooperation envisaged in the Decree 231/2007 requires greater attention and a careful screening activities, why was expanded sphere of hypotheses to be reported, since the indicators that can lead to an alert were expanded.

As it has previously been said, the report is the result of a comprehensive review of all available information; when FIU receives it, through a financial analysis, it performs further investigations. In the case where there are elements that have mafia origin, the alert will be sent to Direzione Investigativa Antimafia, DIA; otherwise, it will be sent to Nucleo Speciale Polizia Valutaria, NSPV.

2.8 Registration obligation

The last duty for the recipients of Decree 231/2007 is registration requirement in Centralized Computer Archive, provided by article 36: according to this article supervisors must keep documents and record the information acquired; this ensures traceability and the ability to trace over time the customers' cash flows.

The Centralized Computer Archive, enabling the traceability of financial flows within the system, is a fundamental aid in the prevention and combating money laundering and terrorist financing and is the main computer tool to identify suspicious transactions.

Furthermore, in order to fulfill the obligations of customer due diligence, supervisors must keep documents and record the information acquired in order to be used by FIU or

[97] Art. 3, law 197/1991.

[98] P.Cenci(2010), "*La nuova normative antiriciclaggio, Direttive Comunitarie e normativa nazionale*", page 74.

other competent authorities in their investigations: in fact, they must keep both the documents required during the due diligence and the other writings and records of transactions for ten years.
Between the information that must be kept on the Archive, beyond the generality of the delegates and the beneficial owner, there is the obligation to record transactions involving the movement of money for a total greater than or equal to 15.000, because this amount represents an element of suspect, even if connected or split. This amount must consider portioned transaction and connected operations: more in detail, for partitioned transaction the Legislator refers to a set of operations performed at different times, but which, from an economic point of view, is considerable as a unique operation; with regard to connected operation, these are those who are not the execution of the same contract but are mutually connected to the person who performs them.

When talking about the obligation related to Decree 231/2007 it is important to remember that there exists a traceability principle: all the steps made by the supervisor must be reconstructed from the documents in its possession, so that if another person carries out the checks, he should be able to verify each step performed. The correct application of this standard enables the correct delineation of the responsibilities of those involved in the evaluation process.

2.9 An overview of active collaboration in Italy

The last part of Second Chapter allows obtaining an overview of the role that banks and other entities have in combating the laundering of dirty money: this analysis will be made by looking at the FIU's annual report and at the National Risk Assessment[99].
An effective implementation of money laundering legislation requires the full knowledge of the purposes and principles that sustain the system and National Risk Assessment (NRA), in accordance with FATF Recommendations, helps to identify, analyse and assess the threats of money laundering and terrorist financing, identifying what are the methods to carry out these activities and identify which are the vulnerability of the prevention system.

[99] The document is "Analisi nazionale dei rischi di riciclaggio e finanziamento del terrorismo". This was developed by Financial Security Committee and it was carried out under the first Financial Action Task Force Recommendation, with the aim to identify, analyze and assess the threats of money laundering and terrorist financing, identifying also what are the methods used of conducting such criminal activities and the vulnerability of national prevention system.

As explained in the previous Chapter, Italy, for various reasons, both economically and socially, has a high risk of money laundering, especially because much of dirty money is introduced into the legal economy. This is also shown on NRA, in which Italy has identified a high 'significant risk' of money laundering. This phenomenon has increased because of the economic crisis, which has offered for launders new opportunity to growth, such as in companies with liquidity crisis, because they need money but their economic situation does not allow him to borrow it 'legally'.

On the other side, NRA clarifies that the Italian preventing and combating system appears adequate; this is proved also by the positive trend of the reports received. Table 1[100] shows this: from 2010 to 2014 there is an increase of 14% of reports received. In the first half of 2015 there is also a growth, compared with the first half of 2014.

	2010	**2011**	**2012**	**2013**	**2014**		**2015**
	total	**total**	**total**	**total**	**1st seme**	**total**	**1st seme**
received	37.321	49.075	67.047	64.601	37.575	71.758	39.021
ml	37.047	48.836	66.855	64.415	37.543	71.661	38.883
analyzed	26.963	30.596	60.078	92.415	39.731	75.857	40.372
% variat	43,1%	13,5%	96,4%	53,8%	-	-17,9%	-

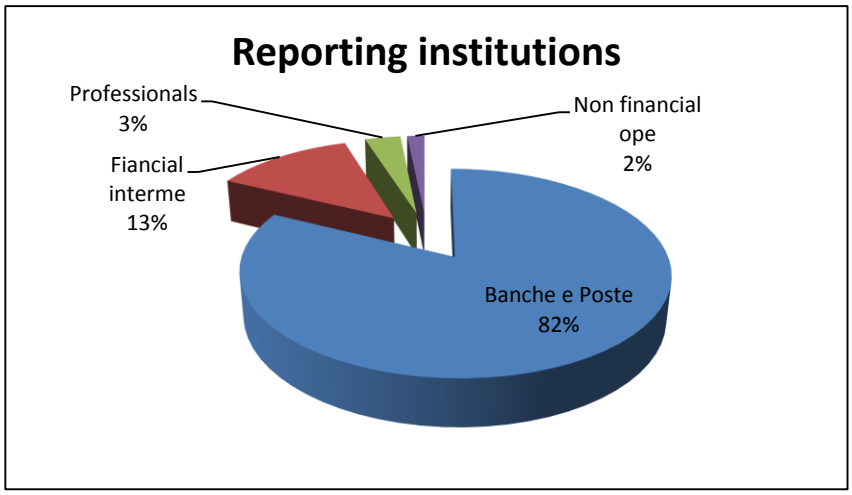
Table 1 Source: FIU 2014 Annual report and Quaderni dell'antiriciclaggio2015

The second row of the Table shows how many reports descend from suspicion of money laundering, that is the large majority of total sum: this clarifies why the use of active collaboration is so important in the fight against money laundering.
The last two rows refer to the total number of reports that have been analysed: as explained above, FIU performs financial analysis, which consists of a series of activities aimed at expanding the original context advised by banks or other institutions. As an example, FIU identifies subjects of reporting and the ties that thay have undertaken, reconstruct the cash flows underlying the operations described and identify the transactions related to money laundering purposes. Finally, the information obtained by

[100] Source https://uif.bancaditalia.it/pubblicazioni/quaderni/2015/quaderni-1-2015/index.html and Rapporto Annuale dell'Unita di Informazione Finanziaria (2015).

FIU allow to classify suspicious transactions and identify and define the types and patterns of irregular behavior that broadcast to supervisors.
The last row represents the variation percentage of analysed reports from previous year: these results were achieved thanks to the continuous improvement of work processes that can benefit from increased availability of information sources and thanks to a better resources' organization.

The NRA also shows that the obligations of Decree 231/2007 are not applied uniformly[101]: Graph 1 shows this assertion. It is clear that most of suspicion activity reporing comes from Bank and Poste; this trend is growing, year by year.



Graph 1 Source: FIU 2014 Annual report

These data may be explained by the fact that, as it has already been explained above, banks have personal interests, such as reputation, to intervene strongly against money launderes. On the other side, professionals have not yet a key role in the sending of suspected warning: this is due to inability to manage the monitoring requirements, caused by inadequate training and for fear of revenge, although this figure has grown by 20% compared to 2013. The largest contribution comes from the notaries, with 91.5% of reports sended, in line with the previous year. Specifically, the role of notaries is very important considering the signing of real estate transactions and the creation of corporate acts.

[101] This work considered banks (about 700), financial intermediaries generally (about 700 and 150 investment companies), professionals (more than 4,600 notaries, 230,600 lawyers, 115,000 accountants), and other parties obliged by Decree 231/2007, including game operators.

With regard to the first, the previous chapter explained that real estate is one of the most used to clean dirty money; in this case the anomalies detected are usually suspected based on the origin of the funds used and on atypical payment.
Considering use of legitimate business for money laundering purposes, the main suspects came from the acquisition or sale of companies, in particular companies that were in financial difficulties; from interposition of nominees or from the inclusion in society of persons involved in investigations.
With regard to non financial operators there is an increase, from 851 suspected warning of 2013 to 1148 of 2014; more than 90% of these were submitted by games and betting management. This sector is very exposed to money laundering risk; money launderers use this sector both using dirty money to play or bets, or invest it by opening, for example, a casino. In particular, the NRA states that *"Il comparto del gioco, sia illegale sia legale, risulta di altissimo interesse per la criminalità organizzata, per la quale ha storicamente costituito una importante forma di sovvenzione. Attualmente la criminalità mafiosa investe nel settore dei giochi acquisendo e intestando a prestanome sale da gioco, sia per percepire rapidamente guadagni consistenti (soprattutto se le regole vengono alterate per azzerare le possibilità di vincita dei giocatori o per abbattere l'ammontare dei prelievi erariali), sia per riciclare capitali illecitamente acquisiti"*[102] .

A further analysis is to see the final rating that was attributed Fui and compare it with the risk level assigned by the sender of the report, becuause appropopriate risk reporting evaluation is useful not only for FIU itself but also for investigative bodies that can take into account the two assessments. Table 2 reports a FUI Reports' evaluation[103]: this comparison shows a convergence between the ratings for more than 70% of reports analyzed in 2014 compared to those of 2013. This convergence is greatly increased, and this factor implies that the analysis carried out by banks or professionals have improved; the remaining differences between the two types of signaling may be due to characteristics of the obliged entity, for example because of their size or the quality of their control systems.

[102] Comitato sicurezza finanziaria "*Analisi nazionale dei rischi di riciclaggio e finanziamento del terrorismo 2014",* page 13.
[103] Rapporto Annuale dell'Unita di Informazione Finanziaria (2015), page 43.

Confronto per ciascuna segnalazione analizzata tra rischio indicato dal segnalante e *rating finale* della UIF *(composizione percentuale)*				
		Rischio indicato dal segnalante		
		Basso e medio-basso	Medio, medio-alto e alto	Totale
Rating UIF	Basso e medio-basso	20,0 (25,1)	12,7 (25,5)	32,7
	Medio, medio-alto e alto	15,9 (10,3)	51,4 (39,1)	67,3
	Totale	35,9	64,1	100,0

Table 2 Source: FIU 2014 Annual report

Finally, considering the topic that will be discussed in the next Chapter, it is useful to know how many suspected signals come from regions that will be analysed, Emilia-Romagna, Liguria and Piemonte. Even if, as it has been explained at the beginning of the Chapter, it is not true that the regions where it come more alerts are the most dangerous, it is possible to use this data to compare with the other regions.

Figure 1 shows the distribution of the reports received: Lombardia, as in previous years, is the region that has sent more warning, with 13.021 reports, about 18% of the total. The others regions in red, Campania and Lazio, have sent respectively 8786 (12,2%) and 8948 (12,5%) reports.

With regard to the regions under consideration, Emilia-Romagna sent more reports in 2014, 4760, approximately 6.6% of the total; Piemonte has sent 4667 (6.5%) reports, with an increase of 30.5%[104] compared to 2013 and Liguria has sent 2,195 (3.1%) reports, with an increase of 24.6% compared to 2013. All three regions are located in the first half of the list, they are then regions that send a large number of reports.

[104] This was one of the largest increases compared with 2013.

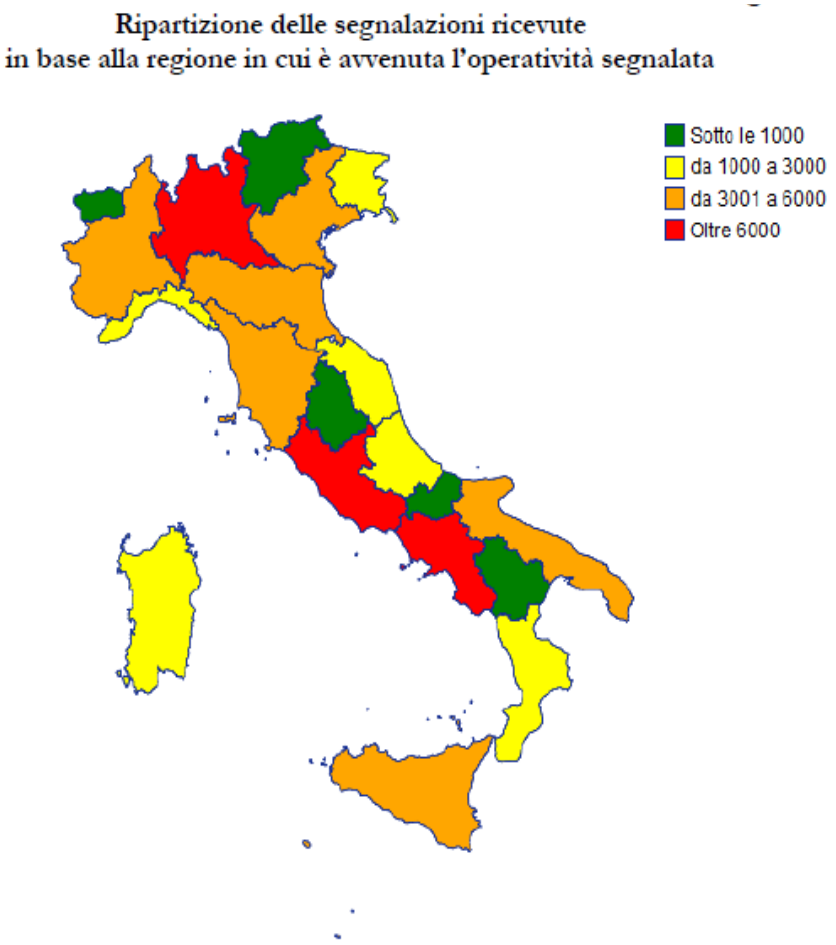


Figure 1 Source: FIU 2014 Annual report

Another method used to see what is the danger that the proceeds of illegal activities can be reintegrated into the formal economy is to analyze the use of cash. In the First Chapter it has seen that often dirty money is held in cash, because in this way it is not traceable. NRA about this information analyzed the abnormal or excessive payments in cash and divided the provinces a four categories based on their risk, high, medium-high, medium, medium-low and low. Taking into account the provinces where there are criminal organizations analyzed in the next Chapter, considering 17 provinces in which these criminal companies are established their headquarters, 8 are in the medium-high level risk (Torino, Savona, Imperia, Rimini, Novara, Alessandria, Verbano-Cusio), 6 in the medium-low risk (Ferrara, Forlì-Cesena, Genova, Piacenza, Vercelli, Cuneo) and only 3 in the low risk (Reggio Emilia, Parma, Modena). This information shows that more than half of pronvince are considered at risk of money laundering; the result is supported by the data presented in the FIU annual report where the three regions are considered at risk of money laundering.

In conclusion, it can be said that an effective collaboration requires not only active timeliness of communication, but also requires the quality and completeness of the information. This is also created with a complex prevention system of money laundering, that, considering in particular Italy, as has already been explained, suffers a very significant money laundering risk.
In its document, NRA to strengthen both the analytical work of the persons obliged by the Decree and, above all, to improve the communication with FIU: about this, to encourage active cooperation, FIU has introduced, in collaboration with the in charge ministries, the definition of specific indicators of anomalies. Moreover, from 2012 UIF started meetings program with leading entities reporting, focusing on behaviors that are difficult to detect.

The importance of the principle of active collaboration was highlighted by Tarantola[105], who in 2011 argued that: "*È dunque cruciale l'impegno sostanziale degli operatori e il coinvolgimento effettivo del vertice aziendale che deve assumersi la responsabilità di adottare modelli organizzativi e gestionali efficaci e promuovere la più ampia diffusione della cultura antiriciclaggio, attivando le opportune leve gestionali e di incentivazione del personale*".

Conclusively, it can be said that the activities of prevention and combating money laundering has recorded significant progress in recent years, also baceause there is awareness of the serious threat that laundering has for economic development and financial stability. It is not only a national problem: in a globalized world, the only effective response to the proliferation of economic crime goes through the achievement of a greater convergence of standards and in strengthening cooperation between countries and international investigative authorities; this is also demonstrated by the Fourth Directive, which has the purpose of further harmonize anti money laundering measures.
These initiatives are even more important in the current economic environment, that was affected by the recent financial crisis.

[105] Anna Maria Tarantola "*Prevenzione e contrasto del riciclaggio: l'azione della Banca d'Italia*" , page 10.

As we have seen above, this need for coordination is felt at national level; Decree 231 is based on cooperation and coordination between obliged authorities, FIU and the other entities. This is demonstrated by the positive results achieved by Financial Intelligence Unit.

To effectively combat criminal infiltration in the economy is essential the contribution of all the beneficiaries of the Anti money laundering requirements: the focus on prevention of money laundering must become a constant practice operational, based on risk based approach; it must overcome the formal approach of the past.

Third Chapter

Check of the relationship between criminal companies and equity investment: an analysis of Emilia-Romagna, Liguria and Piemonte firms

The previous Chapters had the purposes both to show how companies can be used to launder money and why criminals choose this way in respect of holding dirty money in cash; the other purpose was to analyse the role that banks and other intermediaries have in the fight against money laundering. These entities use anomaly indicators that reduce the margins of uncertainty and allow to properly fulfilling their obligations. The role of these entities, as demonstrated by the reports of the Financial Intelligence Unit, is critical because it allows to detect an increasing number of suspicious transactions.

The objective of those involved in criminal activities is to disguise the source of money and to convert the dirty money and wash it so it will be difficult to retrace its origins: one way to do this is placing dirty money in legal businesses.

The aim of this Chapter is to understand if criminal companies hold more equity participation in respect to non-criminal companies; moreover, the next step will be to understand why criminals choose to acquire shares; these hypotheses will be formulated starting from the information obtained from the data analysis and from information given by the First and Second Chapters.

This study follows other research which had the aim of identifying features of criminals companies in northern Italy; the analyses were performed comparing financial index and balance sheet items of criminal companies with a sample of non-criminal companies. Now, after finding the equity participation of each criminal company from Emilia-Romagna, Liguria and Piemonte, it is found a sample of non-criminal companies that have similar characteristics to those criminal, such as production sector or headquarters' province.

All the analysis in this Chapter are made with Stata program.

3.1 Riskiness in Emilia-Romagna, Liguria and Piemonte

Given that in the following pages it will be analysed companies, both criminal and non-criminal, of these three regions, it helps to know how and why organized crime is located in these regions.

First of all, it is known that organized crime plays a large part of its activities in Northern Italy, mainly because it is richer than the South. Since 1994 the Anti-Mafia Commission attested the existence of "*una vastissima ramificazione di forme varie di criminalità organizzata di tipo mafioso, praticamente in tutte le regioni d'Italia"*[106]. It is interesting to notice that, as reported by Enzo Fantò[107], criminals penetrate into northern Italy economy not with force or imposition, but by offering them money coming from illegal activities.

Looking at *PON Progetto Sicurezza 2007-2013 – Gli investimenti delle Mafie*[108], it perceives that these regions, especially Liguria and Piemonte have a high IPM (Indice Presenza Mafiosa)[109], that confirms a marked presence of organized crime[110]. This index was calculated taking in consideration: murders with mafia origin; numbers of reported person for criminal association; municipalities and governments loose for mafia infiltration; assets confiscated from organized crime; DIA reports.

Watching Italian provinces' lists with the highest IPM, Imperia is at 16th position, Genova 17th and Torino at 20th, instead Milano is at 26th position: this data is very significant because it shows that these cities are subject to greater risk than the richest city in the north Italy, Milano.

In detail, for each region can be said that:

- Emilia Romagna, despite the economic crisis, remains one of the Italian regions with the highest income; thanks to a homogeneous development in various production sectors such as industry, agriculture or the services sector. Moreover, it plays an important role at national level, as it is the connection between the north and south-central Italy. For all these reasons this region has always

[106] Commissione parlamentare d'inchiesta sul fenomeno della mafia e sulle altre associazioni criminali similari, Relation on: "*insediamenti e infiltrazioni di soggetti ed organizzazioni di tipo mafioso in aree non tradizionali".* Roma, December 1993.

[107] Enzo Fantò, *L'impresa a partecipazione mafiosa- Economia legale e economia criminale*, page 192.

[108] This report was made by Transcrime and Università Cattolica del Sacro Cuore.

[109] This index was created by Transcrime.

[110] In the IPM's rank Liguria is at 6th position, Piemonte at 7th and Emilia-Romagna at 12th position.

attracted organized crime: in fact the last Sos-Impresa report indicates that: *"La crisi economica in un'area caratterizzata da un'imprenditorialità diffusa ha creato quel terreno fertile nel quale l'usura si è insinuata quale credito sussidiario a quello bancario [...]. Nel triangolo Modena-Reggio Emilia-Parma, si segnala la presenza consolidata di gruppi camorristici del casertano attivi anche nelle pratiche Camorristiche e della 'ndrangheta che gestisce da anni il comparto delle bische clandestine e del gioco d'azzardo".*

- Liguria baits criminal both because it is a border area, and because it is the headquarters of major ports like Savona, Genova, La Spezia. With regard of the first point, Liguria allows access to Costa Azzurra where, from the '70, mafia clans have woven articulated logistic networks for business and the management of important businesses, exploiting the friendly relations with the Marseilles crime. Considering the second point, Liguria with its harbours allows connection with Italian and foreign regions, so criminals can both move their goods both their dirty money. Moreover, Liguria is famous for its casino, like San Remo Casino: as it was said in previous Chapters, casino is a very easy way to launder dirty money.
- In Piemonte there is the first municipality that was dissolved for mafia crimes, Bardonecchia. This happened because lot mafia criminals lived in Piemonte and have established their criminal activities, including money laundering. Considering that Piemonte is one of the richest regions of Italy, it is not difficult to find companies that want to invest dirty money.

As reported in Second Chapter, also the FIU's report showed critical issues in these three regions.

3.2 Steps of the research

As it has been said above, this research is the result of other thesis, which, after analysing the recycling operations conducted by law enforcement agency, identified a list of people embroiled in money laundering. Later, thanks to Telemaco, it had looked to see if these people were members or shareholders of companies. The starting assumption is that these people use companies to launder money or to conceal illegal activities.

First, in order to carry out these analyses, beginning from criminal database of Emilia-Romagna, Liguria and Piemonte, it is found all the balance sheet that has financial assets other than zero. For clarity, it is useful to remember what Financial Assets items are:

*"**1) partecipazioni in:***

- ***a) imprese controllate;***
- ***b) imprese collegate;***
- ***c) imprese controllanti;***
- ***d) altre imprese***

2) crediti:

- *a) verso imprese collegate*
- *b) verso imprese controllate;*
- *c) verso controllanti;*
- *d) verso altri;*

3) altri titoli

4) azioni proprie, con indicazione anche del valore nominale complessivo"

For this research will be considered only the values of point 1). After obtaining the list of criminal companies with financial assets other than zero, the following step is to download from the database Telemaco the additional notes of these balance sheets. In this way it is possible to see which companies owned equity participation, rather receivable, securities and own shares: this is the database with all criminal companies balance sheets and their eventual equity participation. The list was then inserted into the database Stata. Note that for each firm could be more than one year observation, because for criminal database is taking in consideration all the years in which criminals were fulfilling a position of manager or shareholder.

In order to make a proper analysis a sample was selected from the database that contains all the non-criminal enterprises of the three regions and, for companies with financial assets other than zero it is downloading their additional notes, doing as it is described above. This sample was selected considering companies that have similar feature to those criminal, such as: size, Ateco codes and province where is located the headquarter.

The final database has all criminal and control balance sheet items, including other information that will be analysed, such as:

- Total number of participation, this is Total Participation variable;
- County in which the subsidiaries are located;
- Share of participation, this is Quota Mean variable;
- Business name of the subsidiaries.

Unfortunately, many additional notes refer only to the euro amount of the equity investment and not the interest held in percentage; this is the reason why the sample of the Quota Mean model is smaller than the sample of Total Participation model.

The analyses have a sample of 336 companies, of which:

- 169 are criminal companies;
- 167 are control companies.

The total number of firms' year observation is 1708, of which 991 belong to control companies and 717 belong to criminal companies.

3.3 The research Hypothesis

The involvement of legitimate businesses in all phases of the laundering process, combined with a global and high speed funds movement, has provided the means for criminal activity to continue to grow at an exponential rate. For this reason financial institution, auditors and the other recipients of Decree 231/2007 must take a new look at how they evaluate their commercial customers from a money laundering risk perspective, in order to more effectively identify and mitigate risk. One way to find criminal activity is to detect anomalies between the accounting items. In particular, this thesis will analyse the Total Participation item, comparing the sample of criminal companies with the sample of non-criminal companies.

At this point it is useful to formulate some hypothesis about the relationship between Total Participation variable and Criminal variable: specifically, Total Participation is total number of minority interest for each company and Criminal variable is a dichotomous variable and takes value zero in the case of non-criminal company and takes value one in case of criminal company. The questions are: do criminal companies

have more holdings in respect to non-criminals? Is this relationship influenced by other variables? Are there any differences between the regions taken in consideration? Do criminal companies detect more equity participation in foreign company than those non-criminals? Do criminal companies have on average a higher share of equity participation in respect to those non-criminal? Finally, why criminals decide to hold shares on other companies, rather than investing money in other things, such as in illegal activities?

The analysis that will be made in the next few pages will try to answer this question, isolating the variables, in order to study their impact on Total number of participation and Criminal variable. The starting points are the information obtained on what has been argued in previous Chapters: specifically, in the First Chapter it is listed some ways to use companies for laundering money; it can be assumed that the use of the equity investments can be combined with another of the techniques that have been described in First Chapter. This assumption is based on the fact that criminals are not only interested in increasing the synergies, but also they want to derive benefits for their illegal activities. Transcrime's document[111] shows that the company's economic growth is not the aim for the criminals, but criminals are interest to diversify investments, and this is also achieved by investing profits in new companies. The diversification of the investment portfolio, together with the use of nominees, also reduces the risk of confiscation and seizure. Moreover, the choice of investing money in equity participation may rely on the fact that equity participation, rather than the other assets, allow to better hide and clean the resources of criminal organizations and can be used as a screen to make false invoices to conceal and transfer income deriving from illegal activities. Specifically, in this case criminals can use the so called "*imprese cartiere*": this kind if company is created only for producing paper, like invoices for services never made. The purpose of *imprese cartiere* is to conceal illegal activities and to launder money. Another reason that encourage criminals to detect equity investment could be the possibility to detect shares in foreign companies, particularly in low-tax countries or countries where company law is favourable and allows to hide the identity of the owner's share; in this way criminals can also take advantage of international trade-based money laundering method. Ping He showed that international trade-based operations is a typical money laundering technique, because *"using the international trade system, the criminal organisation would then be able to transfer illegal funds back*

[111] Transcrime, *PON Progetto Sicurezza 2007-2013 – Gli investimenti delle Mafie*, page 91.

into the country using the trade transaction to justify payments through the financial system"[112]. There are many reasons behind this choice: for example, international trade-based operation allows to better conceal the proceeds of crime, thanks to the huge quantity and value of the commodity; secondly, it allows to benefit from freight, insurance and foreign currency exchange links; finally, and most important, this kind of trade permits to take advantage of the gaps existing in different countries' laws and on their information exchange.[113]

The Second Chapter has shown what are the duties of the institutions who actively collaborate with the authorities and it has described what is the Customer Due Diligence, which is also based on observations of abnormal value. Obviously, each case must be considered for its characteristics; the acquisition of equity investments could allow criminals to transfer money from one company without suspecting banks or professionals, especially if the subsidiary is abroad.

3.3.1 Equity investment and criminal variable

The first and most simple analysis considers only the two variables Total Participation and Criminal variable.

	Tot. Part
Mean	0,220
Std. Dev.	0,642
obs	991

Table 3 Mean and Standard errors Control

	Tot. Part
Mean	0,901
Std. Dev.	4,942
obs	717

Table 4 Mean and Standard errors Criminal

Table 3 and 4 show that, on average, criminal companies have 0.9 participations, instead control companies have less participation, 0.22. These tables also show that standard deviation for criminal companies is high; this means that there is a greater dispersion. In fact, while the maximum number of participation for non-criminal enterprises is 5, for criminal enterprises it is 58. In order to not twist the results of the

[112] Ping He (2010), *A typological study on money laundering*, Journal of Money Laundering Control, Vol. 13 Iss 1, page 23.
[113] Ping He (2010), *A typological study on money laundering*, Journal of Money Laundering Control, Vol. 13 Iss 1, page 23.

data analysis, it is decided to winsorize for 1% this variable: in this way it is possible to remove outliers, the extreme values which differ significantly from the mean.
Now, we have new data:

	Tot. Part_w
Mean	0,220
Std. Dev.	0,642
obs	991

Table 5 Mean and Standard errors for Control

	Tot. Part_w
Mean	0,425
Std. Dev.	1,142
obs	717

Table 6 Mean and Standard errors Criminal

The tables show again that criminal companies have, on average, more equity participation than non-criminal companies.
At this moment, it is possible to do other investigation, in order to analyse more in detail the existing relationship between these two variables.
Table 7 shows the correlation between winsorized Total Participation and Criminal variable.

	Tot. Part_w
Criminal	0,1137*** 0,000
obs	1708
***p<0.01, **p<0.05, *p<0.1	

Table 7 Correlation between Participation and Criminal variable

The first row is correlation coefficient**,** which shows the strength and direction of the association between these two variables. As the sign of the correlation coefficient is positive, it can conclude that there is a positive correlation between the variables. This means that higher value of winsorized Total Participation is related to higher value of Criminal variable, which is when there is a criminal firm. The second row represents the level of statistical significance (i.e., the ***p***-value), which is 0.0000, which means that there is a statistically significant relationship between the two variables.
Even if this information is interesting, it must remember that correlation does not include the concept of cause and effect, but only to the relationship between variables.

Finally, in this first part it is introduced the t test, that compares the means of two groups, in this case being criminal or control firm.
In this case the null hypothesis is that the two means are equal; if this hypothesis is true, it means that any differences between the two values are due to chance.

Criminal	obs	Mean	Std. Err.
0	991	0,220	0,020
1	717	0,425	0,043
	1708		
t	=	-4,725	
Pr(|T| > |t|)	=	0.0000	

Table 8 t test

The Mean column shows that criminal firms have higher total number of participation compared to non-criminal firms. Moreover, the table shows that the group means are significantly different as the p-value in the Pr(|T| > |t|) row is 0.000: we can reject the null hypothesis, with a 5% significance level.
Table 8 highlight that criminal companies have more participation than non-criminal: this result is in line with our expectations. The outcome, although interesting, needs to be further analysed, because in reality almost never an event depends solely on the performance of a certain factor. It is more useful to formulate a model that considers the possible influences; this analysis will be made later, with multivariate analysis.

3.3.2 Regions and Ateco codes

In this paragraph it is introduced other variables that will be used later: Ateco codes companies, indicating the sector in which operate companies, and the distribution of firms in the regions which are taking into consideration. As mentioned above, in order to have a uniform sample, for the control group it is selected companies that have headquarters and code Ateco similar to criminal companies.

- Regions: since that this paper takes into account firms of tree regions, it has been created the following tables, illustrating the distribution in each region of criminal and non-criminal companies, with mean and standard deviation.

Emilia-R	Tot. Part_w	
	Control	Criminal
Mean	0,281	0,324
Std. Dev.	0,650	1,010
obs	256	182

Table 9 Total Participation in Emilia-Romagna

Liguria	Tot. Part_w	
	Control	Criminal
Mean	0,134	0,234
Std. Dev.	0,450	0.771
obs	187	189

Table 10 Total Participation in Liguria

Piemonte	Tot. Part_w	
	Control	Criminal
Mean	0,221	0,584
Std. Dev.	0,690	1,338
obs	548	346

Table 11 Total Participation in Piemonte

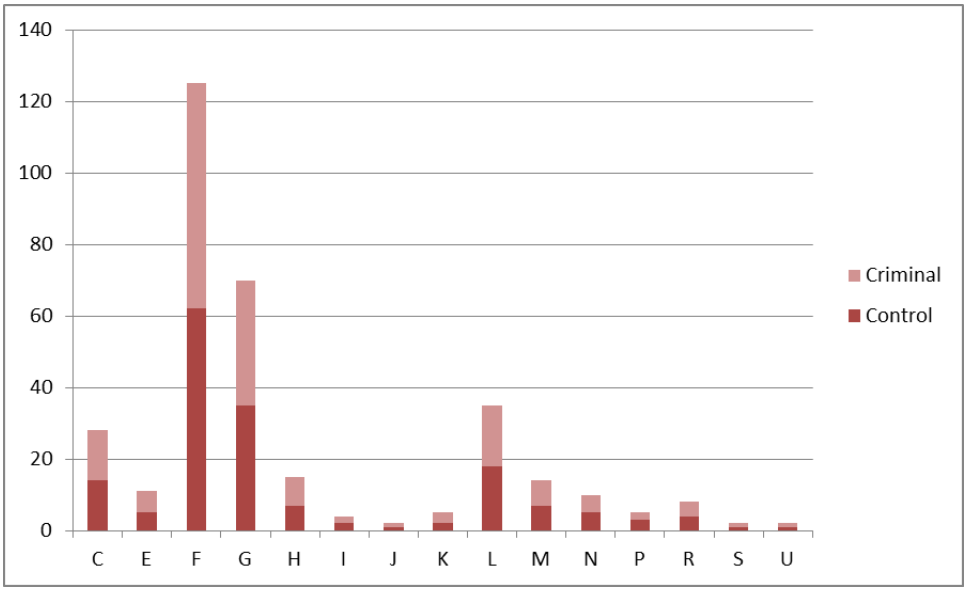
All Tables show that winsorized Total Participation is higher in case of criminal companies.

In the following pages it will be analysed if being in one region in respect to another can change the relationship between equity participation and criminal factor.

- Ateco codes: Graph 2 illustrate the distribution of all sample's companies for Ateco codes, divided by criminal and control firms.

  Graph 2 shows that more than 120, precisely 125 firms, belong to F codes, that is construction sector; this confirms what has been said in the First Chapter, that is, that the building sector is one of the most used to launder money and it is one of the most interesting sector to study the phenomenon of money laundering. In general, criminals prefer to invest in areas where the business risk is moderate and competition is limited: these features are found in the construction industry and in the retail business. Another sector that has always been used by launders

is the real estate; in fact, the Table 11 shows that in our sample there are 17 companies that belong to this branch.



Graph 2 Distribution of Ateco codes

		Control	Criminal
C	MANUFACTURING ACTIVITIES	14	14
E	WATER SUPPLY; DRAINAGE SYSTEM, WASTE MANAGEMENT	5	6
F	CONSTRUCTION	62	63
G	WHOLESALE AND RETAIL TRADE; REPAIR OF MOTOR VEHICLES	35	35
H	TRANSPORT AND WAREHOUSING	7	8
I	RESIDENCE AND FOOD SERVICE ACTIVITIES	2	2
J	INFORMATION AND COMMUNICATION SERVICES	1	1
K	FINANCIAL ACTIVITIES AND INSURANCE	2	3
L	REAL ESTATE ACTIVITIES	18	17
M	PROFESSIONAL, SCIENTIFIC AND TECHNICAL ACTIVITIES	7	7
N	RENTAL, TRAVEL AGENCIES	5	5
P	EDUCATION	3	2
R	ARTA, SPORTS AND ENTERTAINTMENT ACTIVITIES	4	4
S	OTHER SERVICES	1	1
U	EXTRATERRITORIAL BODIES	1	1
	Total	167	169

Table 11 Description of present' Ateco sectors

In future research, the dummy variables of Ateco codes will be included in the regression, as the number of investments and the criminal factor can be

influenced by business sector: in fact, as we have already said, there are economic areas in which there are several criminal companies in respect to other areas.

3.4 Description of the variables

In this section it is analysed, through the use of Table 12, all the variable that will be further taken into consideration. The purpose of this Chapter is to check whether there exist a relationship between Total Participation and Criminal variables; then it will go over, and through regression will occur if it is possible to predict scores on one variable from the scores on a second variable. In previous pages it is shown that, looking only at these two variable, there is a significant relationship, that is, criminal companies have higher Total Participation value.

However, as mentioned above, the t test shows whether the dependent variable, in this case Total Participation, depends on the trend of the other, that is if the company is criminal or not. For a more correct analysis it is necessary to use the multivariate regression, because in this way it is possible to consider other variables that may influence both the dependent variable as the independent variable, in order to obtain a 'clean' report: these control variables would have otherwise affected the result if not considered in the model.

Now, for each variable that will be used, it is indicate its number of observation, mean, standard deviation and the 25^{th} , 50^{th} and 75^{th} percentiles.

	Obs.	Mean	SD	p25	p50	p75
Criminal	1708	0,420	0,494	0	0	1
Tot.Part._w	1708	0,306	0,892	0	0	0
Ln.Attivo_w	1708	13,105	1,776	12,104	13,308	14,304
Roe_w	1707	0,052	1,055	-0,049	0,043	0,234
Leverage_w	1707	16,994	54,800	1,621	4,552	13,570
Quota_media	341	0,217	0,332	0	0	0,5

Table 12 Description of variable used for multivariate regression

Since it is decided to winsorize Total Participation, to be fair it is also winsorized the other variables. Specifically, in addition to the two variables that are already used, the Table shows:

- The logarithm of Total assets: using the logarithm is taken into account company size. In fact it would be wrong to use the Total assets item, because this value depends greatly on the size of the firm and has a highly skewed distribution; using the logarithm is obtained a symmetrical distribution;
- ROE (Return on Equity), given by net income over equity, is a measure of profitability that calculates how many euros of profit a company generates with each euros of shareholders' equity. This indicator can be used to evaluate how management is able to manage its own resources to increase corporate profits. ROE is not only determined by the choices made in the context of operational management, but also by the decisions on the financial and asset management. The ROE is useful for comparing the profitability of a company to that of other firms in the same industry.
- Another factor that can influence the presence or absence of equity investments is the leverage, given by Total Liabilities over Equity. It shows how a company is able to finance its investments, especially if finances them with equity capital or borrowed capital; it plays a fundamental influence on profitability.
- Finally, it will be considered the mean share of participation, in the next pages it will be made a regression in order to see if criminal companies have, on average, an higher share of participation in respect to non-criminal companies

3.4.1 Correlation matrix

In this paragraph it is explained the correlation between the variables mentioned above, with the purpose to know the strength and direction that exists between two variables.
Table 13 shows the correlation coefficient and the number of observation for each correlation. Moreover, it is highlighted with asterisk, the significance level: it is placed three asterisk next to the correlation score if the result is statistically significant and the p-value is lower than 0,01; there are two asterisk if the p-value if between 0,01 and 0,05 and one if the p-value is lower than 0,10.

	Criminal	Tot.Part._w	Ln.Attivo_w	Roe_w	Leverage_w	Emilia-Romagna	Liguria	Piemonte	Quota_media
Criminal	1								
obs	1708								
Tot.Part._w	0,1137***	1							
obs	1708	1708							
Ln.Attivo_w	0,0611**	0,2398***	1						
obs	1708	1708	1708						
Roe_w	0,0611**	-0,035	0,0572**	1					
obs	1707	1707	1707	1707					
Leverage_w	0,024	-0,014	0,1790***	-0.3967***	1				
obs	1707	1707	1707	1707	1707				
Emilia-Romagna	-0,005	-0,005	0,0444*	-0,025	0,0923***	1			
obs	1708	1708	1708	1707	1707	1708			
Liguria	0,0892***	-0,0731***	-0,0952***	0,002	-0,019	-0,3120***	1		
obs	1708	1708	1708	1707	1707	1708	1708		
Piemonte	-0,0696***	0,0647***	0,0401*	0,020	-0,0651***	-0,6154***	-0,5568***	1	
obs	1708	1708	1708	1707	1707	1708	1708	1708	
Quota_media	0,194***	0,682***	0,150***	0,122**	-0,044	0,191***	0,094*	0,121**	1
obs	341	341	341	341	341	341	341	341	341

***p<0.01, **p<0.05, *p<0.1

Table 13 Correlation matrix

Looking at correlation coefficients of Criminal column, it is possible to see that this variable has, as already be mentioned, a positive correlation with winsorized Total Participation variable. Moreover, it has a positive correlation with the logarithm of winsorized Total assets, means that criminal companies are related to higher value of logarithm of winsorized Total assets. The same works for winsorized ROE; criminal companies are associated to greater Total Participation values.

With regard to winsorized Total Participation, this value has, as expected, a positive correlation with the logarithm of winsorized Total assets. This because Assets representing the complex of investments and economic resources of the company: among these resources there are equity investments, which are investments intended to remain permanently in the company.

Both the variables Total Participation and Criminal factor has positive and significant correlation with Liguria and Piemonte variables, but not with Emilia-Romagna variable.

Finally, there is positive and significant correlation between Quota mean and Total Participation; the same is with Criminal factor.

3.5 Multivariate regression

This is the most interesting part of this Chapter, and it is the culmination of this research.

In the previous pages it has seen that Criminal variable influences winsorized Total Participation variable: first, through the correlation it is seen that in the presence of criminal companies there is a higher value of investments; the result was also confirmed by the t test. However, as it has already been explained, these analyses are not sufficient to confirm that a variables influence the other: it is necessary to conduct a multivariate analysis, which takes into account factors that can influence these two variables. This type of regression makes it possible to know if the total of equity investments change in criminal companies in respect to non-criminal, holding constant other variables; this analysis is necessary because it is uncorrected do a simple regression using as sample companies from different industries and of different sizes.

VARIABLE	(1) Tot.Part_w	(2) Tot.Part_w	(3) Tot.Part_w	(4) Tot.Part_w
Criminal	0,186** (0,091)	0,169* (0,088)	0,174** (0,088)	0,179** (0, 087)
Ln.Attivo_w		0,078*** (0, 026)	0,079*** (0,026)	0,086*** (0,028)
Roe_w			-0,034* (0,020)	-0,058** (0,025)
Leverage_w				-0,001* (0,0001)
Constant	4,814*** (0,091)	3,516*** (0,483)	-0,903*** (0,30)	-0,965*** (0,311)
Dummy_ateco	yes	yes	yes	yes
Observations	1708	1708	1707	1707
R-squared	0,287	0,305	0,307	0,310
***p<0.01, **p<0.05, *p<0.1				

Table 14 Multivariate regression

Table 14, on first column, shows that winsorized Total Participation is positively correlated with Criminal factor; moreover, the coefficient for Criminal is significantly different from zero because its p-value is lower than 0,05, as it is indicated by the two asterisks. This is the simplest model, because it tells how much the dependent variable is expected to increase when the independent variable increases by one, regardless of the company activity's sector.

The second model includes a very important variable, the logarithm of Total assets, which, as has been said before, is used to erase the effect "size" of the company. This model is more accurate than the first, as this affects the very variable number of participation held by the company, as it was also shown in Table 13. This result show that company size influence Total Participation variable, that is, larger companies have more equity participation.

The last two columns considers a sample of 1707 observation instead 1708 because one observation has Equity equal to zero. The third and the fourth models include winsorized ROE and winsorized Leverage, because it is assumed that the decision to hold shares also depends on the return on capital and the degree of indebtedness. Both this regression coefficient have a negative signs. The leverage coefficient shows that, as it was predictable, higher is the degree of debt, lower is the total number of

participation. The sign of ROE is a consequence of this data, because ROE depends on Leverage: the more the Leverage is high, the more the ROE increases, and vice versa.
The final result of this set of regressions is very interesting: even if the coefficient logarithm of Total assets is always positive and significant, with p-value near zero, also Criminal factor has positive and significant correlation. This means that, regardless of company size, sector, ROE and leverage, criminal companies have higher Total Participation value.

3.6 Multivariate regression by Regions

In this paragraph it will be made a multivariate regression between independent variables considering the three regions: in this way it will be possible to see if this variables change results that were previously obtained.
Beside Criminal and Emilia variable, it is taken into account the variable Cri*Emilia, that has value equal to one if the company is criminal and it is located in Emilia; it has value equal to zero otherwise.

VARIABLE	(1) Tot.Part_w	(2) Tot.Part_w	(3) Tot.Part_w	(4) Tot.Part_w
Criminal	0,243** (0,112)	0,228** (0,106)	0,232** (0,107)	0,240** (0,107)
Emilia	0,154 (0,107)	0,147 (0,108)	0,145 (0,109)	0,158 (0,109)
Cri*Emilia	-0,228 (0,186)	-0,232 (0.187)	-0,233 (0,187)	-0,243 (0,187)
Ln.Attivo_w		0,078*** (0, 026)	0,079*** (0,026)	0,086*** (0,028)
Roe_w			-0,034* (0,019)	-0,059** (0,025)
Leverage_w				-0,001** (0,0005)
Constant	4.757*** (0,112)	3.459*** (0491)	-0,986*** (0,289)	-1,072*** (0,308)
Dummy_ateco	yes	yes	yes	yes
Observations	1708	1708	1707	1707
R-squared	0, 290	0,309	0, 310	0,314
***p<0.01, **p<0.05, *p<0.1				

Table 15 Multivariate regression- Emilia Romagna

Table 15 shows that, in all the models, Criminal factor is positively related to Total Participation, and p-value is always lower than 0,05, means that criminal variable explains a significant proportion of the variance of Total Participation. This was confirmed also by Table 13, in which the correlation between Total Participation and Emilia variable was not significant. As regard to Emilia and Cri*Emilia variables, their p-value is higher than 0,10 and it is possible to ignore these variables. This means that variables Emilia and Cri*Emilia does not need to explain this model.

VARIABLE	(1) Tot.Part_w	(2) Tot.Part_w	(3) Tot.Part_w	(4) Tot.Part_w
Criminal	0,216** (0,112)	0,197* (0,107)	0,203* (0,108)	0,206* (0, 108)
Liguria	0,051 (0,128)	0,074 (0,126)	0,078 (0,026)	0,070 (0,126)
Cri*Liguria	-0,128 (0,176)	-0,123 (0,174)	-0,130 (0,175)	-0,119 (0,174)
Ln.Attivo_w		0,078*** (0, 026)	0,079*** (0,026)	0,086*** (0,028)
Roe_w			-0,035* (0,020)	-0,058** (0,025)
Leverage_w				-0,001* (0,0005)
Constant	4.784*** (0,111)	3.49*** (0,494)	-0,926*** (0,31)	-0,985*** (0,320)
Dummy_ateco	yes	yes	yes	yes
Observations	1708	1708	1707	1707
R-squared	0,288	0,306	0,308	0,311
***p<0.01, **p<0.05, *p<0.1				

Table 16 Multivariate regression- Liguria

With regard to the model related to Liguria region, it is possible to conclude the same thing: Criminal factor is positively correlated and is significant, with p-value lower than 0,10; on the other side, Liguria and Cri*Liguria does not explain variable in Total Participation, even if Table 13 shown positive and significance correlation between Total Participation and Liguria variables.

Finally, Table 17 shows that neither region variables nor criminal variable explain the model; they useless in predicting Total Participation variable.

The results of this paragraph reveal that Regions variable are not statistically significant for our model; this means that the positive and significant correlation found on Table 13 between Region and Criminal variables depends on other variables.

VARIABLE	(1) Tot.Part_w	(2) Tot.Part_w	(3) Tot.Part_w	(4) Tot.Part_w
Criminal	0,047 (0,101)	0,031 (0,102)	0,032 (0,103)	0,038 (0, 103)
Piemonte	-0,153 (0,101)	-0,161 (0,101)	-0,162 (0,101)	-0,167* (0,101)
Cri*Piemonte	-0,265 (0,183)	-0,263 (0,179)	-0,268 (0,177)	0,267 (0,178)
Ln.Attivo_w		0,078*** (0, 026)	0,079*** (0,026)	0,086*** (0,028)
Roe_w			-0,036* (0,196)	-0,056** (0,025)
Leverage_w				-0,001* (0,0001)
Constant	4.841*** (0,153)	3.550*** (0,505)	-0,851*** (0,277)	-0,922*** (0,291)
Dummy_ateco	yes	yes	yes	yes
Observations	1708	1708	1707	1707
R-squared	0,292	0,311	0,313	0,316
***p<0.01, **p<0.05, *p<0.1				

Table 17 Multivariate regression - Piemonte

3.7 Quota Analysis

The last part of this research focuses on quota analysis: in this way it is made a model, in order to explain the relationship between Mean of total Participation variable from Criminal variable, taken the others variable constant. The aim of this part is to understand if criminal enterprises tend to have a greater share of participation in respect to non-criminal firms.

The variable Mean of total participation is calculated by averaging the investments held every year.

VARIABLE	(1) Quota_media	(2) Quota_media	(3) Quota_media	(4) Quota_media
Criminal	0,137** (0, 066)	0,127* (0,068)	0,128* (0,067)	0,131** (0, 108)
Ln.Attivo_w		0,156 (0, 023)	0,019 (0,021)	0,021 (0,020)
Roe_w			-0,031* (0,017)	-0,048** (0,021)
Leverage_w				-0,001** (0,0004)
Constant	-0,102 (0,066)	0,178 (0,334)	-0,138 (0,316)	-0,114 (0,302)
Dummy_ateco	yes	yes	yes	yes
Observations	341	341	341	341
***p<0.01, **p<0.05, *p<0.1				

Table 18 Quota analysis

Table 18 shows that Criminal factor is positively correlated with Quota mean, independently from the other variables: in case of criminal company, quota mean is 0,13 higher than in the case of non-criminal company.

Surprisingly, p-value shows that company size does not affect the average share owned by each company; this variable is influenced not only by the criminal factor, but by ROE and Leverage. In particular, our sample shows that with an increase of ROE there is a decrease of quota mean: this suggests that companies with a high ROE prefer to hold low participation. As stated above, ROE depends also on company's leverage and this is the reason why the two coefficient have the same sign. The sign of leverage shows that companies with a high debt ratios tend to have lower average share of participation.

3.8 Overview of the analysis

Finally, the last part of this Chapter has the aim to summarize the results of this research, taking in consideration the hypothesis.

With regard to the relation between criminal companies and Total Participation item, the result of the t test, the correlation matrix and especially the multivariate regression

showed the hypothesis that criminal enterprises hold more equity participation than non-criminals was confirmed. As stated above, the reason behind this choice could rely on several factors: in this case it was assumed that the criminals acquire participation to create a group and be able to transfer from company to company money and goods; moreover, if a company has subsidiary, it is more easily to make false invoices, in order to move dirty money. Finally, this method satisfies the need to transfer income, so the company that is in good situation has a lower tax base, while the company which is in difficulty will have an highest total assets.

The goal is the concealment of the criminal origin of the proceeds, because if a company has equity participation in other company can frequently transfer and split dirty money; the money launders create an apparent legal origin of the money by fabricating transactions, such as invoices and other agreement with the use of false documents. This opinion is also supported by *PON Progetto Sicurezza 2007-2013 – Gli investimenti delle Mafie*[114], which argues that an abnormal level of non-financial and non-tax receivables can hide a criminal company. In order to hide their activities, criminals use outputs to other companies, including their subsidiaries, increasing the value of 'trade receivables' and 'receivables from associated or subsidiary companies'.

These results also show that, for the purposes of this analysis, the variables that identify the region where the business is located are not significant, so it is possible to say that in order to evaluate the relationship between criminal enterprises and equity investments it doesn't matter if they are located in Emilia-Romagna, Liguria or Piemonte.

With regard to quota analysis, the results showed that in these three regions criminal enterprises have an higher average level of participation, this probably because criminals want to hold the majority and, in this way, set their rules.

Finally, it would be very interesting to examine if criminals companies hold more investments abroad than non-criminals; in fact today, thanks to globalization, it is very easy to hold investments in foreign companies. It must pay specific attention to this circumstance, especially if the subsidiary is located in low-tax countries or in those states where it is not necessary to identify the holder of the company's shares. Furthermore, the holding of shares on foreign companies allows the creation of 'corporate boxes' that confuse control activities. Unfortunately in the sample that was taken into consideration because only 5 companies own shares abroad, too small number to perform valued analyses.

[114] Page 180.

Conclusion

The ultimate goal of this thesis is to identify the signals in the companies' management that can be used in risk assessment models or for criminal infiltration prevention; in particular, this elaborate concerns the equity investments item.
The itinerary that has been discussed in this Paper was designed to see if criminal companies use, among the methods to clean dirty money, equity investment in other companies. Since that there is not a lot of literature on this topic, it was conducted an empirical analysis on a sample of companies from three regions: Emilia-Romagna, Liguria and Piemonte.

Summarizing the previous Chapters:

- The First Chapter has shown that laundering techniques using criminal connected companies are many and always changing, in order to avoid regulatory control. The entrance of dirty money in the economy affects the proper function of markets and distorts competition between individuals and firms. In particular, it is seen that criminals tend to participate in the limited companies or in companies that are in financial difficulties. Moreover, there are other reasons that lead to launder dirty money in companies, such as creating new profit, having control of the territory and the increasing of social consensus; these reasons influence the choices of whether to settle the company and what kind of economic sector choose.

  Finally, it is important to remember that criminals are using companies to launder money cash because in this way it is easier to separate money from its illicit origin.
- The Second Chapter has shown what is the active cooperation and it has described what are the tasks that institution, like banks, must conduct against their client. Decree 231/2007, as it was seen above, lists entities' obligation, which are: customer due diligence obligation; abstention' obligation from completing the transaction; registration obligation; mandatory reporting of suspicious transactions. This was also underlined by the Fourth Directive, that wants the money laundering risk assessment is carried out at the appropriate level and with the necessary flexibility. This element is linked to a fundamental

principle, the risk-based approach, which is the most adequate method to deal with new threats, because it allows to graduate controls. In fact, as it has been said many times, the risk of money laundering is not always the same because it is constantly changing. Another important element, which is connected with the First Chapter, is the need to identify the beneficial owners: this is essential to identify people who may conceal their identity within a company. This is possible due to customer due diligence, which consists on carrying out checks with the aim to identify customers.

Conclusively, the Fourth Directive stressed on the focus to create greater harmonization of anti-money laundering measures, in order to make them more homogeneous in the countries.

- The last Chapter focused on analysis of a companies' sample, both criminal and non-criminal: the aim was to see if criminal companies tend to have more equity participation in respect to non-criminal.

  In order to have a complete analysis, it was made the t test, the correlation matrix and the multivariate regression. The results showed that, taking into account only the Criminal variables and Total Participations, there is a positive and significant relationship, that is, criminal enterprises have an higher Total Participation value compared to non-criminals. At a later time, the multivariate analysis showed that there is a relationship between these two variables, and this relationship does not depend on factors such as business sector, ROE, size and leverage of the companies.

  At the end of this first analysis, it is stated that criminal companies have higher value of Total Participation in respect to those non-criminal and this difference is significant.

  In order to explain the reasons behind these results it is useful confront what has been previously said. First of all, it has been explained what are the five reasons that bring criminals to invest in the legal economy; these reasons may also explain why the criminal companies have more equity participation than non-criminals, because with equity participation is more easily to achieve these goals.

  - The main reason that encourages criminals to invest in companies is the possibility to conceal their criminal activities: through subsidiaries, they can

mask illicit flows, by means of false invoices, which produce commercial receivables. Criminals can also create 'corporate boxes' to make difficult the traceability of goods and to hide the beneficial owner. This danger occurs especially when the subsidiaries are foreign companies.

In particular, the use of "*imprese cartiere*" allows to better hide criminal activities: in the case that subsidiary is an *impresa cartiere* it is conceivable that its value of production have a strong variability from year to year, because its purpose is to launder money, not make business.

- There are economic reasons that may be of interest to criminals, such as the creation of synergies to reduce costs, even if profit maximization is not necessarily the primary target for criminals.
- There are social reasons: for example, if the criminal's objective is the maximization of social consensus, the choice of the sector in which to invest depends on the ease with which the criminal organization is able to offer jobs work; in this case criminals want to take participation in companies that require a lot of manpower.
- Finally, there are strategic reasons, because by acquiring controlling stakes in new territories increase the area in which criminals carry out illegal activities. In this way they also get the support of new people, thus, increase their power of corruption. Moreover structures and subsidiaries resources can also be used in the fulfilment of illegal activities, for example the offices of a company can become headquarters for criminal organization meetings.

Since that criminals have different reasons to invest dirty money in legal activities, the decision to invest in a sector rather than another depends on the purpose they want to achieve.

As crime and money laundering methods evolve, the perceptions of the characteristics of business change as well. Financial institution, in particular, should expand their CDD and obtain a clear understanding of the nature of the customer's business and activities. These analysis could be translated into risk indicators to be used in developing the common risk assessment model.

The results obtained in this thesis are very interesting, even if it was taken into account only three regions; as mentioned above, the existing relationship between criminal

companies and equity participation is useful for the improvement of money laundering's risk assessment and the creation of a better fight against organized crime.

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