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ECONOMIC SECURITY AND PREVENTION OF MONEY LAUNDERING IN COMMERCIAL BANKS OF LATVIA

ABSTRACT: After the analysis, the authors of the study suggest their interpretation of “economic security”. They also view Latvian banks as one of the most important elements of state financial and economic security. The article focuses on the fight against money laundering. The article shows the use of Latvian normative acts on the prevention of criminal schemes for money laundering. The authors propose mechanisms for effective blocking of suspicious accounts in commercial banks in Latvia and suggest methods for their implementation in practice. As a result of these methods, criminal communities will not be able to bypass the blocking of accounts in commercial banks established by the law enforcement agencies. The arrested funds will be able to replenish the budget of the Republic of Latvia.

KEYWORDS: economic security, banks, legalization of funds, commercial banks, Latvia

BEZPIECZEŃSTWO EKONOMICZNE I PRZECIWDZIAŁANIE PRANIU PIENIĘDZY W BANKACH KOMERCYJNYCH ŁOTWY

ABSTRAKT: Po przeprowadzeniu analizy autorzy artykułu proponują własną interpretację pojęcia „bezpieczeństwo ekonomiczne”. Uważają również banki łotewskie za jeden z najważniejszych elementów bezpieczeństwa finansowego i gospodarczego państwa. Artykuł koncentruje się na walce z praniem pieniędzy. Przedstawia zastosowanie łotewskich aktów normatywnych dotyczących zapobiegania przestępczym procedurom prania pieniędzy. Autorzy proponują mechanizmy skutecznego blokowania podejrzanych rachunków w bankach komercyjnych na Łotwie oraz sposoby ich praktycznej realizacji. W wyniku ich zastosowania środowiska przestępcze nie będą w stanie ominąć blokad rachunków w bankach komercyjnych nałożonych przez organy ścigania. Zatrzymane fundusze będą mogły uzupełnić budżet Republiki Łotewskiej.

SŁOWA KLUCZOWE: bezpieczeństwo ekonomiczne, banki, legalizacja funduszy, banki komercyjne, Łotwa

INTRODUCTION

In modern economic conditions, commercial banks must find mechanisms for sustainable development and flexible response to external influences. The most important condition for the sustainable development of banks is to ensure their economic security.

In the economic literature, in connection with the transition of states to the digital economy, the term “economic security” is used both at the state level and at the level of an enterprise, organization¹.

The definition of “economic security” has been studied by many scientists of various industries. Academic V.K. Senchagov defines it as “... the state of the economy and institutions of power, under which guaranteed protection of national interests, the social orientation of politics, and sufficient defense potential even under unfavorable conditions for the development of internal and external processes are ensured”². From the point of view of banking security, this is ensuring the sustainable development of the bank and the fullest use of its economic potential in an aggressive environment.

Issues and problems of ensuring economic security are presented in the scientific works of V.A. Fatuev and M.A. Bakaev, where “economic security” is interpreted as a set of internal and external conditions conducive to the effective dynamic growth of the national economy, its ability to meet the needs of society, the state, an individual, to ensure competitiveness in foreign markets, protecting against various kinds of threats and losses”³. I.N. Storozhuk gives the following definition – “economic security is a state of the economy and institutions of power, which ensures guaranteed protection of national interests, socially oriented development of the country as a whole, sufficient defense potential even under the most unfavorable conditions for the development of internal and external processes”⁴. A.S. Illarionov argues that economic security combines economic, political, and legal conditions that ensures the sustainable production of the maximum amount of economic resources per capita in the most efficient way in the long term⁵. G.Yu. Khachatryan believes that “the basis for ensuring the economic security of a modern commercial bank is its financial stability, which is a consequence of the action of a system of institutional, managerial, organizational, technical and information measures aimed at ensuring a reproductively stable mode of operation of the bank, protecting

¹ А.В. Тарадаева, А.А. Сюмкина, Теоретические аспекты экономической безопасности коммерческого банка, Научно-исследовательский журнал "Вектор экономики" № 4 (10) - Финансы и кредит, 2017, с.232-241. Журнал вектор экономики. (kdc-tori.ru)

² И.В. Караваева, Социальные аспекты новой стратегии экономической безопасности России, сб. *Стратегия экономической безопасности России: новые ориентиры развития: Сборник научных трудов I научно-практической конференции «Сенчаговские чтения» ученых, специалистов, преподавателей вузов, аспирантов (г. Институт экономики РАН, 14 марта 2017 г.)*, ред. И. В. Караваева, А.Г. Коломиец, И.А. Колпаков Москва 2017, с. 37-56.

³ В.А. Фатуев, М.А. Бакаева, *Управление активами коммерческого банка*, „Известия Тульского государственного университета. Экономические и юридические науки” Issue 2-1/2010, с. 63-79.

⁴ И.Н. Сторозжук, *Финансовая стабильность в системе обеспечения экономической безопасности коммерческого банка*, Автореферат диссертации, Ростов-на-Дону 2010.

⁵ А.Н. Илларионов, *Критерии экономической безопасности*, „Вопросы экономики” № 10/1998, с.56-67

its rights and interests, increasing the statutory capital, increasing the liquidity of assets, the safety of financial and material assets, as well as to ensure the repayment of loans”⁶.

One of the definitions of economic security often used in the scientific literature is the possibility of effectively achieving its main goal – making a profit through the most rational performance of functions in conditions of external and internal threats⁷.

At the same time, it should be emphasized that economic security includes maintaining financial stability, solvency, planning future cash flows of an economic entity, and employment security.

The economic security of an organization is based on how effectively the services of this organization manage to prevent threats and eliminate damage from negative impacts on various aspects of economic security. The sources of such negative impacts may be the deliberate or unconscious actions of people, organizations, including public authorities, international organizations or competing enterprises, as well as a combination of objective circumstances, such as the state of the financial situation in the markets of a given enterprise, scientific discoveries and technological developments, force majeure and so on.

When assessing the economic security of an organization, it is important to take into account the risks of a specific entrepreneurial activity within which the organization operates.

FINDINGS AND DISCUSSION

Experts identify the following types of economic security:

- financial and economic (it is necessary to combine financial security, the criterion of which is financial stability, and economic, the parameters of which reveal the influence of non-financial indicators on financial results)
- investment;
- informational;
- price;
- currency;
- personal.

The authors of this article will focus on the financial and economic security of Latvian banks. Therefore, the financial and economic component is a set of processes of the bank's functioning, the control result of which is the financial and economic indicators⁸.

As in all EU countries, banking activities in Latvia are controlled by the Bank of Latvia: Article 26: The Council of the Bank of Latvia shall make decisions on behalf of the Bank of

⁶ Г.Ю. Хачатурян, *Институциональные основы обеспечения экономической безопасности банковской системы Российской Федерации в современных условиях*, Автореферат диссертации, Москва 2010.

⁷ М.А. Азарская, В.Л. Поздеев, *Принципы экономической безопасности коммерческих банков*, „Вестник Московского университета МВД России” № 6 / 2016, с. 149-152.

⁸ А.О. Панина, *Формирование волатильности на рынках развивающихся стран в условиях глобальных потрясений и стабильной экономики*, „Вестник Евразийской науки” 10(2)/2018, с. 1-9.

Latvia that are necessary to ensure the implementation of the tasks of the Bank of Latvia, including the tasks of the European System of Central Banks⁹.

There are 14 banks in Latvia, some data on the activities of banks are shown in Table 1.

Table 1. General data on banks in Latvia as of June 30, 2020, compiled by the authors

| Bank's name | BANK ASSETS, thousands EUR | Liquidity coverage ratio ¹⁰ | Return on assets (ROA) |
|-------------------------------------|----------------------------|--|------------------------|
| Swedbank | 7,051,986.6 | 318.0% | 9.9% |
| Citadele banka | 4,316,333.2 | 386.8% | -19.7% |
| SEB banka | 4,040,681.1 | 190.4% | 7.1% |
| Luminor Bank branch in Latvia | 3,517,605.3 | - | - |
| BlueOrange Bank | 619,305.2 | 152.1% | 1.7% |
| Rigensis Bank | 425,085.3 | 408.0% | 10.5% |
| Latvian branch of OP Corporate Bank | 404,068.0 | - | - |
| Regional Investment Bank | 281,226.6 | 240.0% | 4.1% |
| Signet Bank | 231,291.7 | 181.0% | 10.6% |
| Baltic International Bank | 215,414.2 | 145.0% | 0.3% |
| LPB Bank | 201,161.6 | 191.7% | 16.6% |
| Industra Bank | 193,850.3 | 574.6% | -61.0% |
| PrivatBank | 192,327.3 | 1188.0% | -19.7% |
| Expobank | 64,231.6 | 776.4% | -3.7% |
| Total Banks sectors | 23,312,982.2 | - | - |

Source: Association of Latvian Commercial Banks.

Therefore, as can be seen from the data presented in Table 1, in terms of the volume of bank assets in the first place in the list of Latvian banks, Swedbank has an amount of assets - 7,051,986.6 thousand euros, in the second place is Citadele banka and the third place belongs to SEB banka with assets of 4,040,681.1 thousand euros and 4,040,681.1 thousand euros, respectively.

However, Signet Bank has the highest return on assets – 10.6% and Rigensis Bank – 10.1%. Swedbank showed a return on assets of 9.9%, Citadele banka – a decrease in profitability by 19.7% and SEB banka showed ROA of 7.1% in the corresponding period.

⁹ Law "On the Bank of Latvia", 19.05.1992 In <https://www.bank.lv/en/about-us/8436-law-on-the-bank-of-latvia> (10.11.2019).

¹⁰ Statutory minimum requirement 100%.

Latvia, like all other civilized countries of the world, is fighting against the prevention of money laundering, ensuring the economic security of both banks and the country as a whole. The country has adopted legislative amendments to the Law on Latvian Credit Institutions¹¹, for money laundering, for example, Article 63. of this law states: Undisclosed information at the disposal of a credit institution is provided to a state institution, civil servant, or other institution and official in the manner prescribed by this Law in the following cases and in the following volume:

2. 2 to the State Revenue Service – an application by the subject of the Law on the Prevention of Money Laundering, Financing and Spread of Terrorism, which is under the supervision and control of the State Revenue Service, or the bank account of his client for a certain period on the basis of a request received by the State Revenue Service. The head of the structural unit responsible for the supervision and control of the subjects of the Law on the Prevention of Money Laundering and the Financing of Terrorism and the Proliferation of Weapons of Mass Destruction, or his deputy, if necessary to perform the supervisory functions provided for by the Law on the Prevention of Money Laundering and the Financing of Terrorism and the Proliferation of Weapons of Mass Destruction.

Over the past 20 years, significant success has been achieved in this direction. In Latvia, no payment over EUR 10,000 can be made without submitting documents confirming the transaction to credit institutions. However, when implementing such a strict economic security policy, one important question arises: how is it still possible to carry out illegal value added tax (VAT) refund schemes and other illegal transactions through commercial banks?

It should be noted that such schemes are very complicated and rather risky to execute, and the most key factor in their implementation is the risk of freezing funds in the bank. Therefore, participants in a dubious “business” need to look for accomplices among bank employees through whom it is possible to carry out such operations.

The procedure for the seizure of suspicious accounts in Latvia is as follows: law enforcement agencies, having identified suspicious transactions, send a letter to the bank where the suspicious account is opened, demanding the seizure of the funds in this account. In the vast majority of cases, they receive the arrest of a completely empty account. Although, even a moment before the imposition of such an arrest, there were substantial funds on the account. The question arises: is this an accident or a pattern? The overwhelming number of arrested accounts with zero balance. The conclusion is obvious: among the people who carry out such operations, there are employees of a commercial bank. They are responsible for accepting “dubious” funds and promptly debiting them from the client's account in the event of a request for arrest. Banks always take their economic security seriously. Therefore, what is the problem?

To determine who can help in the implementation of these schemes, it is necessary to understand the structure of the functioning of any commercial bank. You should also understand

¹¹ *Kredītiestāžu likums* In <https://likumi.lv/ta/id/37426-kreditiestazu-likums> (11.12.2020).

the exact algorithm of actions, according to which law enforcement agencies send documentation for the arrest of funds in the bank.

The bank is managed by the Bank's Board, which consists of members of the Board, each of whom, in turn, is responsible for the subdivisions entrusted to him.

Generally, cash and settlement services are run by the Vice President (Board Member) in charge of the business. All cashiers and operationals obey him through the heads of departments.

In turn, the operational management is subordinated to the first vice president (deputy chairman of the board). This management is the first to see the receipt of funds on the customer accounts. It can also slow down the transfer of funds to the client's accounts and send them promptly. The same department is engaged in registering the arrests received and directly seizing the accounts.

One of the important functions of the third member of the Bank's Board in Latvia is compliance. Compliance is an internal control over the compliance of a company's activities with legislation. Its main goal is to eliminate the risk of losing profits. These include fines, damages or non-performance of contracts. At the same time, compliance risks can lead to a deterioration in reputation, limited business opportunities, or a shrinking customer base. This has a direct impact on the stability of the bank and its economic security.

From the above, it is obvious that it is inappropriate for persons committing illegal actions to negotiate with three highly paid bank managers who are responsible for its work. It seems that the costs of bribery are high, the risk of rejection is high and, as a result, the transaction will not be completed. Therefore, implementers of such schemes need to look for access to performers in key divisions of the bank. These employees have relatively low salaries and may be willing to engage in such dubious deals. Management about such actions of their employees may not know anything. Although, according to the authors, in such a situation it is not essential who exactly participates in the implementation of the criminal scheme. It is important to accept another fact: there are problems with economic security in banks. And criminal communities take advantage of this. How, with such support from banks, can law enforcement agencies effectively implement mechanisms for the seizure of funds obtained illegally? And thus make this "business" highly risky, and therefore ineffective.

The procedure for seizing an account in the banking system of Latvia follows this scheme:

1. Law enforcement agencies send a request to the bank to arrest the client's account.
2. The bank registers the receipt of the document on the same day. This is a legal requirement.
3. The seizure goes to the blocking of the account in the operational management. The management officer who is to seize checks whether the client has funds. If there is a balance on the account, then he calls the client manager and offers to promptly make a payment to his client. After debiting funds from the client's account, the employee seizes the empty client's account. Therefore, the requirement of the law is formally fulfilled.

If other funds are transferred to the client's account at this time, the bank employees try to stop them. This must be done as the money goes to an already blocked account. Those will be

irretrievably lost and it will be necessary to answer for this to the “client”. In this case, an employee of the operational management comes to the rescue. He may not credit the money to the client's account and return it to the sender (after receiving a written request from the sender and the recipient of funds). Thus, the account blocked by law enforcement agencies will remain empty.

Why the police, prosecutor's office, and other economic security management structures of Latvia have not been able to solve this problem for thirty years? According to the authors, this can only be achieved by changing the requirements for credit institutions to process customer payments. Customer payments must be processed no earlier than the next day after the funds are credited by the bank to the customer's accounts and not earlier than the next day after the customer has sent the payment order to the bank. Control should be carried out by a special banking program, i.e., all payments must be registered in it. In this case, the documents for the arrest of accounts must be brought to the bank itself and receive a note from the bank on the date of receipt of the arrest. Thus, bank employees will not be able to write off funds from the client's account on that day, and they will remain blocked. This, according to the authors, will make such illegal transactions unprofitable and they will cease to exist.

Of course, all banks in the world are competing to increase the speed of payments. And skeptics will object to the authors of this article that their proposal will throw the entire banking system of Latvia back for years.

However, the authors believe that, on a legal basis, it is possible to split the amounts that can pass in one day. For example, amounts up to five thousand euros can be executed on the same day, while payments of a large amount must be executed only the next day. Thus, 90% of payments will be made on the same day and large payments - the very next day.

It should be noted that in many countries of the EU and the world (France, Italy, Switzerland, etc.), making payments the next day is a normal banking practice.

This mechanism will help the law enforcement bodies of Latvia to solve the serious problem of blocking funds obtained by criminal means, while the bank's customers will not be affected. The whole Latvian society will benefit from this legislative change, and only organized crime will lose.

CONCLUSION

Based on the results of the study, the authors came to the following conclusion:

With the strengthening of the development of the digital economy in the world, the relevance of issues of economic security of both companies and the state will increase. The review of Latvian banks as of June 1, 2020 showed that in terms of the volume of bank assets, Swedbank is in the first place in the list of Latvian banks, with the total assets of EUR 7,051,986.6 thousand, followed by Citadele banka and the third place belongs to SEB banka with assets of 4,040,681.1 thousand euros and 4,040,681.1 thousand euros, respectively. However, Signet Bank has the highest return on assets – 10.6% and Rigensis Bank – 10.1%.

Swedbank showed a return on assets of 9.9%, Citadele banka showed a decrease in profitability by 19.7% and SEB banka showed ROA of 7.1% as of 01.06.2020. One of the indicators of a bank's stability is liquidity. According to this indicator, the leaders are: PrivatBank, this indicator amounted to 1088%, Expobank 776% and Industra Bank 574%.

To eliminate money laundering processes in the Latvian banking system, according to the authors, the procedure for payments from bank customers' accounts should be changed: payments up to 5,000 euros should be paid on the day of receipt, and over 5,000 euros – the next day.

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