



Italy: Seeing the threat behind the corruption

In the context of anti-money laundering (AML), the Italian scenario is influenced by a series of typically Italian characteristics which distinguishes the country apart from other advanced European economies. Italy is a member of the EU and part of G8 and can appear to outsiders to be a country that is full of contradictions where decisions often appear difficult to decode.

A strong element in Italy is the existence of 'family capitalism' — small- and middle-sized family-owned companies which are subject to rapid transformations. As the real drivers of the Italian economy, they are deeply rooted locally and share close relations with foreign relatives in Latin America, Eastern Europe and the Mediterranean.

High levels of corruption also play a large factor in the Italian scenario. Corruption also is coupled with the presence of sophisticated organized crime groups that emerged as a cause and effect of an enormous gap between the poor regions of the south and the prosperous northern and central Italy. The economic disparity has continued to exist regardless of decades of public funding in the south to reduce these inequalities.

A subculture of illegality

Italy is well-known for its extremely high fiscal evasion rate, and its proportion of cash payments is one of the highest in Europe. The widespread diffusion of corruption, which originates from an existing interrelation between political and business milieus, has never been countervailed — but rather further promoted — by the Italian governments, which succeeded one after another following the Second World War. The interests and the balance of powers of the financial and the business worlds have often not just been mediated but actually managed by politicians. Finance and business are susceptible to sudden changes and even reflect the whims of political interests. The borders between licit and illicit have become "more flexible" than in other West-European countries. Progressively, corruption has pervaded all levels of Italian society with particular concentration in the South — a situation favored by the presence of criminal organizations and the above mentioned existence of the socio-economic gap among the south, the center and northern Italy.

The Clean Hands inquiry

The investigation of corruption escalated in the early 1990s. The famous

national inquiry known as Clean Hands, that was launched to investigate a series of major scandals, revealed the existence of a corruption system, based on agreements which ensured a constant flow of bribes to political parties from companies providing services to the public administration. The inquiry led to confessions and convictions of major representatives of the Italian entrepreneurial and political world, and resulted in the largest political crisis since the Second World War. In the investigation's wake, two major Italian political parties — the Italian Socialist Party (PSI) and the Christian Democratic Party (DC) — collapsed after it emerged that large sectors of business and politics survived through illicit activities. The corruption involved not just politicians and entrepreneurs, but magistrates and high-ranking military officers.

Corruption today

The Clean Hands inquiry weakened corruption, which became less visible, but it did not defeat the corruptive system. To the contrary, according to Achille Serra, former High Commissioner against corruption in Italy, the corruption system was damaged by the judicial inquiries of the 1990s. However soon after, Italy adopted an "evolution of the species" approach and more efficient, sophisticated and less visible corruption techniques were invented — de facto the corruption level increased.

Over the last fifteen years, the Italian government has ratified a series of international conventions against corruption but failed to adopt special legislation and the necessary reforms to contain illegality in an efficient way.

The corruption perception index published by Transparency International in June 2008 evaluated the abuse of public office for private gain. Italy's ranking this year worsened by fourteen positions compared to 2007's index, reaching 55, after countries such as South Korea and Costa Rica. Out of the first fifteen members of the EU (before the enlargement of the EU to nine eastern European countries, which started in 2004) Italy is positioned in second to last place in Europe.

The response of the Italian government to this situation seems contrary to Transparency International's indicators on 25 June 2008, through a decree, the Italian government abolished the agency named High Commissioner against Corruption, which had become fully operative in September 2007.

In the confinements of corruption via fiscal evasion, the statistics of public and private businesses show impressive numbers. In January 2007 it was estimated that fiscal evasion equaled approximately 19% of the GDP.

Corruption and fiscal evasion are strictly related. These two elements, combined with a high level of cash payment provide a fertile environment for money laundering.

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Organized crime

The most significant and worrying element characterizing money laundering in Italy is the pervasive presence of organized crime groups. Unlike any other developed European country, the local economies of some of the southern regions and in particular those of Campania, Calabria and Sicily are nearly entirely controlled by criminal organizations such as the mafia, the "ndrangheta" and the "camorra." They tend to rely on the alliance of corrupt local politicians, who want to keep their positions and are interested in maintaining the support of criminal organizations, which are largely funded by an unlawful use of the public money.

In these regions, the control of the organized crime economy is the biggest risk factor. This affects not just the south, but the central and northern Italy, as a good

part of the financial resources accumulated through illegal activities in the South are transferred to the rich regions where they are recycled and reinvested into the legal economy.

Anti-Money Laundering

The Italian legislative AML framework is the result of a twenty-year engagement of the Italian authorities in the fight against organized crime. Italy perceived the danger of the criminal aggression to the legal economy much sooner than other European countries, and as early as 1982, adopted legislative interventions, such as the criminal offense of Association of Mafia Type, which was defined also by the scope to control entrepreneurial activities in which funds originating from illicit activities were reinvested.

During the 1990s, AML legislation became increasingly sophisticated and far reaching to the point that Italy sometimes anticipated the principal indications of international organizations.

In 1991, one month before the adoption of the 1st European AML directive, Italy passed an AML law under which banks were obliged to identify their customer and record any transaction exceeding ITL 20 million (equaling today's 10,000 Euros), increased to 12,500 in 2002, which is lower than the thresholds set in the first and the second European AML directives (15,000 Euros). In addition, investment firms and management companies were also subject to the AML regime (thus anticipating the 2nd AML directive).

In 1993, the Bank of Italy issued a Decalogo, a document containing operational instructions aimed at identifying suspicious operations, in order to strengthen the control over the use of intermediaries for money laundering purposes. The document was updated in 2001, in consideration of the development of new money laundering techniques in the areas most at risk of money laundering.

In 1997, Italy assigned the primary responsibility for matters related to anti-money laundering to the AML Department of the Italian Foreign Exchange Office (Ufficio Italiano Cambi – UIC) which acted in conjunction with the Financial Police and the Bureau of Anti-Mafia (DIA). In 2000, in line with the European directives, a national FIU was created within the UIC.

The Italian legislative framework was then progressively updated to mirror international standards and the European AML directives. In 2002 Italy implemented the December 2001 Second European AML directive, which extended the risk of recycling from financial institutions to professional and commercial operators.

In 2005, Financial Action Task Force's (FATF's) inspectors determined that Italy's AML framework is extensive and mature, and that the country highly complied with most of FATF's forty plus nine recommendation. The law enforcement efforts against money laundering led to convictions in almost 600 cases every year, one of the highest rates of successful prosecutions in Europe and more than and over 130

million euro worth of criminal proceeds were confiscated in 2004.

However, the FATF also assessed that it was necessary to clarify and reorder relevant laws, to implement a more detailed risk-based Customer Due Diligence (CDD) requirements and other new provisions of the revised FATF standard and of the Second European Directive on Money Laundering in particular with reference to non financial businesses and professions.

In addition, Italy was asked to consolidate the AML legal framework in one single text to reduce its complexity and increase its efficiency.

The Third European Directive

On 21 November 2007, Italy implemented the Third European AML directive (2005/60 EC) regarding the prevention of the use of the financial system for the purpose of money laundering and terrorist financing which EU member states were required to implement by December 2007.

The new AML law brought several changes to the Italian legislative AML framework of which the most significant are the following:

- The UIC ceased to exist on January 1, 2008 and its functions were transferred on the Bank of Italy where a new Financial Information Unit (FIU) was constituted.
- The modification of the existing law, which improved the coordination between the authorities and the AML law.
- The national legislative framework on the fight against terrorism made the obligation to signal suspicion operations more explicit.
- The introductions of so called "risk-based approach" to assess levels of money laundering and financing of terrorism.
- Obligations were extended in the customer identification and CDD and the obligation to identify the beneficial owners was introduced.
- Obligations to apply enhanced due diligence to Politically Exposed Persons (national PEPs excluded) were introduced.
- The adoption of a broader definition of money laundering than the one of the Italian criminal code (articles 648 and 684).
- To combat high cash transactions rates, the maximum sum for cash payment has been set at 5.000 Euro. However, on 25 June 2008 the new Italian government increased the threshold to 12.500 euro (law nr. 112).
- Stricter rules regarding money transfers

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were introduced: it has been limited to 2.000 euro without documentation and to 5.000 Euro if documentation to attest the operation is presented.

What are the effects of the implementation of the European AML directives?

The Italian AML framework was improved significantly thanks to the implementation of the Second and Third European AML directives. However, some experts stressed that a closer coordination with other specific legislations would be required and that adjustments would be needed on the enforcement side.

The obligation to adopt a risk-based approach and to abstain from conducting certain operations autonomously and not just upon request of the authorities should discourage fiscal offenses and, in particular, fiscal evasion which is a significant problem in Italy.

The extension of control and suspicious transactions reporting (STRs) obligations to professionals and other financial and non financial intermediaries should further speed up this process.

The data shows an increasing trend in the number of STRs filed. In 2007 the UIC received 12.503 STRs, 21% more than in 2006, the majority of which appeared to be related to fiscal evasion, followed by frauds, "layering" operations of organized crime groups as well as illegal waste dismantling. Nevertheless, the number of STRs is relatively still low.

Although the situation seems to be promising and financial institutions increasingly give attention to AML, there persists a noticeable gap in the number of STRs, both across the categories of those reporting and the geographic areas. In particular, it has emerged that the numbers of STRs filed by non-financial operators and professionals is extremely low (only 1.4%). This shows a difficulty by these subjects to adopt the new legislation.

The impression is that professionals such as notaries, lawyers and accountants continue to feel close to the interests of their clients and are not always willing to strictly adhere to the norms of compliance with AML regulations.

The inspections of money services businesses by Italian authorities have nearly doubled in 2007 compared to 2006. An operation conducted by the Italian authorities known as "Easy money" uncovered more than 400 unauthorized money services businesses, as well as traces of persons listed on UN blacklists.

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The transformation of the UIC into a FIU under the umbrella of the Bank of Italy should increase the efficiency of the national FIU, which can rely on the large structure and network of the Bank of Italy. The bank is present in all Italian provinces and exercise control over a high number of financial agencies.

What are the difficulties of compliance with the European AML directives?

Unlike the Anglo-Saxon countries, the praxis of customer verification and knowledge has not been adopted by the Italian financial and business worlds.

Historically, Italian financial institutions have always made use of in-house techniques to verify their customers. This verification, however, has been limited to evaluating the risks of financial insolvencies. Customer verification activities were conducted by the "Centrale dei Rischi" of the Bank of Italy in the form of monitoring the customers' financial situation on a national level. It also was handled by a series of service providers, controlled by banks, that evaluated the possibilities of insolvency through a "black list" of "bad" creditors.

While these techniques were efficient to identify and monitor potential risks of financial insolvencies, they are less appropriate for adequate compliance with the strict Know Your Customer requirements of the current AML legislation. To comply with the current AML legislation, these hindrances must be overcome:

- Lack of customary conducting CDD activities both on national and international level by the Italian bankers and financiers.
- Wrong and/or exaggerated perception of confidentiality level between customer and managers of financial institutions who fear to invade the privacy of their

clients and to lose the fiduciary relationship with them.

- Collusion between banks and clients at limits of legality in regions of the South of Italy and in some provinces of Central and Northern Italy. (Even more this collusion is spread between professionals and their clients, which explains the low number of STRs, as mentioned earlier).
- Lack of transparency in the public administration, especially in Southern Italy; many public bodies do not collaborate sufficiently in the supply of information required for tackling problems related to corruption and money laundering, either for lack of efficiency or, in some cases, for reasons of collusion with the "grey zone" of the local entrepreneurial world.
- In some cases, the strict legal framework in relation to privacy does not enable independent parties to obtain a sufficient level of knowledge on individuals most at risk (politically exposed persons and others). For example, criminal records and information on civil or criminal litigation is not public (unless it has been published by the press).

Italy, with a history of corruption and fraud, has made strides to combat money laundering and other forms of corruption; however, it still has a long way to go. Recently an immunity bill has been introduced in the Italian legislation to protect those holding the highest positions of public office from prosecution, a controversial proposal, considering that the Prime Minister was facing trial on corruption, which was suspended in October 2008 as a result of the immunity bill. 

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