Approved by the Decision No1/913A
Dated September 11, 2008
Of the Chairman of the Central Bank of the Republic of Armenia

1. Typology

Scheme for money laundering using alternative remittance systems for the purpose of concealing the true origin of funds

1) Description of the Scheme

As a rule, offices and/or individuals in foreign countries (hereinafter the Organizer), organizations or natural persons holding bank accounts in the Republic of Armenia are engaged in such transactions. The transactions are conducted with the following scheme and series of steps:

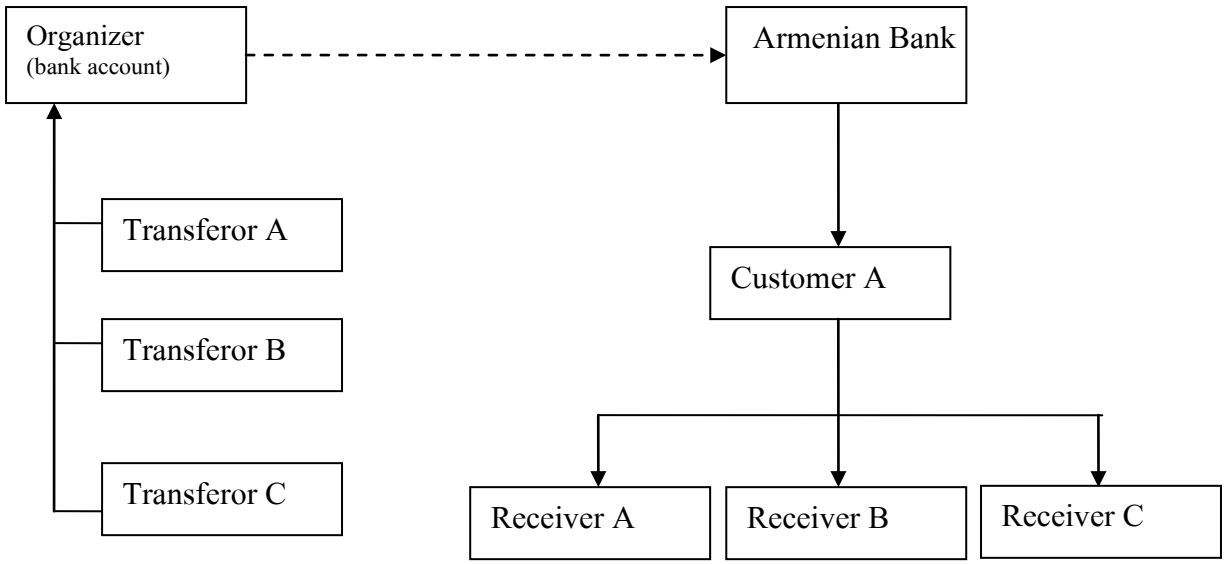
The Organizer accepts amounts of money from citizens and organizations of his/her country of operation which are aggregated into the bank account of the Organizer or persons related to him/her. With the next step, the mentioned funds are transferred with one or more transactions to a bank account of an organization (registered in a off-shore territory) or a natural person with a bank operating in the territory of Armenia. Particularly, when the funds are transferred for an organization, the purpose of the transfer is often indicated as supplying goods, providing services, payments for trading securities/bills of exchange, providing/repaying a loan, and when the transfer is conducted for a natural person, financial aid and other reasons are indicated as a purpose for the transaction.

Afterwards, as rule within one or a more days the received amounts are cash withdrawn from the bank account of the mentioned person by beneficiary legal or natural persons or the amounts are distributed into the bank accounts of legal or natural persons serviced within the same bank and afterwards are cash withdrawn by them.

The conducted examinations suggest that in relation to the aforementioned funds:

- It is impossible to verify the legality of the origin due to lack of relevant information, and
- Legal or natural persons receiving the amounts are not often the final beneficiaries for the funds which are in turn distributed to the final beneficiaries (according to the list received from the Organizer).

2) The mentioned type of operations are schematically illustrated bellow



a. The Organizer accepts amounts of money from Transferors A, B, C,

µ. The collected funds are placed on the bank account of the Organizer or a person related to him/her,

b. Upon the payment order of the account holder the funds are transferred in full or in part to the bank account of an organization (registered in an off-shore territory) or a natural person with a bank operating in the territory of Armenia,

c. The transferred funds are:

- cash withdrawn from the bank account of the mentioned person, or
- distributed to the bank accounts of legal or natural persons serviced within the same bank and afterwards are cash withdrawn by them (the final beneficiary of the transferred funds is either Customer A or the latter is an intermediary for distributing the funds among final beneficiaries Receiver A, Receiver B and others).

3) Conclusion

The operations conducted according to the illustrated scheme and series of steps may be a aimed at concealing the origin, movement or true ownership (final beneficiaries) of proceeds.

In terms of examining transactions with elements of the illustrated scheme, special attention shall be drawn to **transactions when customers of financial institutions shall receive funds in average and large amounts.**

2. Typology

Scheme for circulation and legalization of proceeds derived from tax evasion and illicit entrepreneurial activities using money transfers by natural persons.

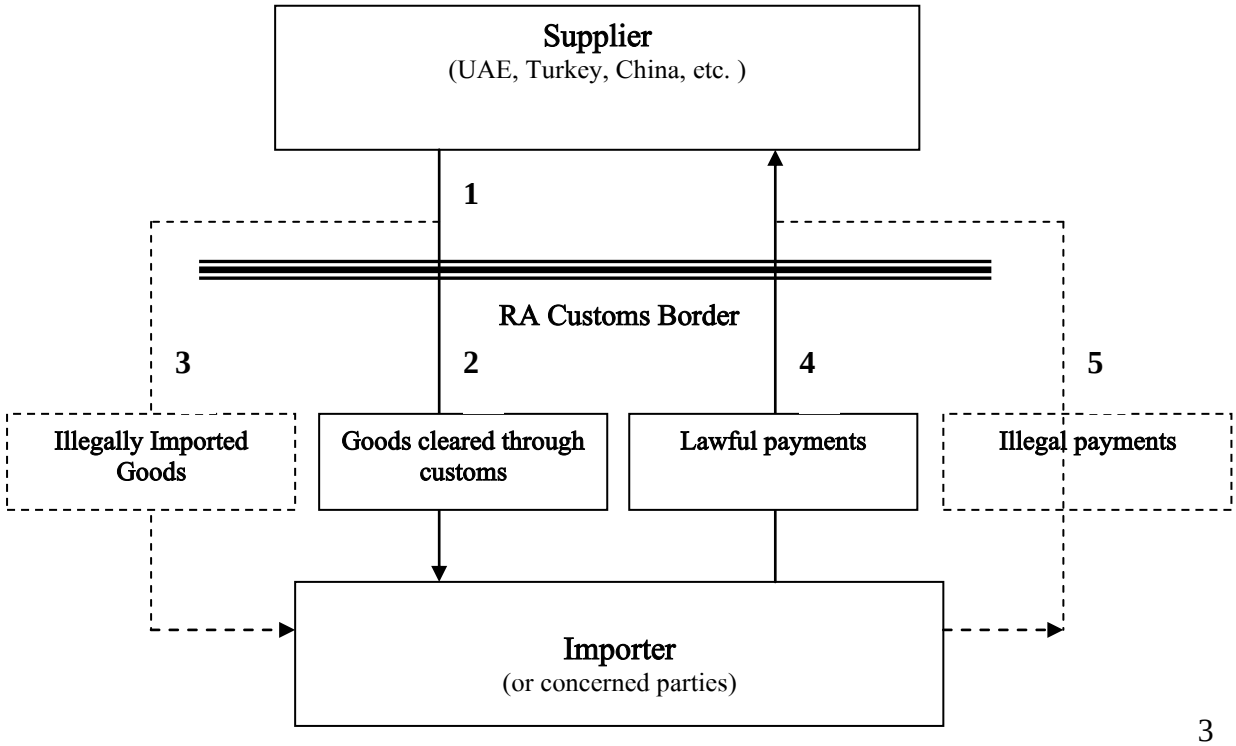
1) Description of the Scheme

The transactions carried out with this scheme generally include the following direction of flow of funds: transfer of funds from a natural person to a non-resident legal person. This direction of flow of funds is primarily connected with import transactions. Particularly, an organization engaged in importing goods to the Republic of Armenia declares and clears the good through customs in reduced volumes, which also means that the undeclared proportion of the goods is sold in shadow (not disclosed in accounting and other documents of the organization). For the purpose of exercising a payment for the goods the organization transfers (through a concerned party, on behalf of a natural person or with his/her bank account) the proceeds derived from the trade of undeclared goods to the organization, that the goods were imported from. As a documentary ground for the large amount transfers standard contracts for loans, securities trade are presented or "repaying debt", "clearing liabilities" are directly indicated as purposes for transfers or invoices of legal persons are presented.

The same scheme is also evidenced when a natural person is engaged in importing goods. The customs clearance of the imported goods is conducted through "specialized" organizations ("one-day life", "paper selling" companies) founded for this purpose and the payment meeting the import is carried out by bank accounts serviced in banks of the Republic of Armenia (or via fast transfer systems, without opening a bank account).

The above illustrated transactions are considered as financing of shadow circulation related to importing entrepreneurial activities and are aimed at evading direct or indirect taxes subject for payment by business entities.

2) The mentioned type of operations are schematically illustrated bellow



a. The Importer purchases and transports goods to Armenia from the Supplier,

b. Part of the imported goods is lawfully declared and cleared through customs,

c. The remaining part of the imported goods is imported in illegal ways and is not declared/customs cleared,

d. The proceeds derived from trade of lawfully declared and customs cleared goods are officially transferred from the bank account of the Importer to the Supplier presenting documents verifying the lawfulness of the payment,

e. The proceeds derived from trade of goods not declared/customs cleared are transferred by concerned parties to the Importer with or without opening an account (in some cases via fast transfer systems) while presenting standard contracts of loans, securities trade as a documentary ground for the payment or directly indicating "repaying debt", "clearing liabilities", etc. as purposes for the transfers or presenting invoices of legal persons.

3) Conclusion

The operations conducted according to the illustrated scheme and series of steps may be aimed at concealing the origin, movement or true ownership (final beneficiaries) of proceeds, as well as evading tax liabilities, concealing real volumes of economic activities.

In terms of examining transactions with elements of the illustrated scheme, special attention shall be drawn to **transfers conducted through financial institutions, where the initiators of the transfers are natural persons and beneficiaries – legal persons, while paying attention to the residency status of the beneficiary organization (as it may give a hint whether the payment is made meeting the imported goods) and verifying the relation of the initiator natural person to any business sphere.**

3. Typology

Scheme for money laundering using foreign currency exchange operations for the purpose of concealing the true origin of funds and the direction of actual movements thereof

The operational mechanism of this kind of scheme is the following: with several trading transactions of two and/or more foreign currencies the financial institution:

- obtains income through transactions with one of its customers, and
- experiences losses due to transactions with another entity, thus providing for the transfer of proceeds derived from the losses of the first party to the second one. As a result of the transactions a flow of funds from one entity to another one takes place while concealing the true origin of the funds and the actual direction of movement.

1) Description of the Scheme

a. Financial institution obtains income from foreign currency exchange transactions with its business entity customer

Such potential suspicious transactions of foreign currency exchange are carried out with the following scheme:

1) The institutions sells, for example, 1.000.000 Euros to its Customer A and buys 1.500.000 US dollars (e.g. exchange rate of 1.500)

2) With the next step, the institution carries out an equal-amount Euros reverse transaction with Customer A buying 1.000.000 Euros and repaying 1.450.000 US dollars instead (e.g. exchange rate of 1.450):

As a result, the financial institutions pays Customer A a smaller amount of US dollars than received (with an amount due to the margin of buy and sell exchange rates) for repurchasing the Euros sold and obtains a certain amount of income (in this case 50.000 US dollars). Thus, Customer A "sacrifices" a certain amount of money for the financial institution at the cost of losses.

b. Financial institution experiences losses due to foreign currency exchange transactions with its business entity customer

The actions specified under the previous Point are repeated herewith, but this time with an opposite result. Particularly:

1) The institutions sells, for example, 1.000.000 Euros to its Customer B and buys 1.450.000 US dollars (e.g. exchange rate of 1.450),

2) With the next step the institution carries out an equal-amount Euros reverse transaction with Customer B buying 1.000.000 Euros and repaying 1.500.000 US dollars instead (e.g. exchange rate of 1.500).

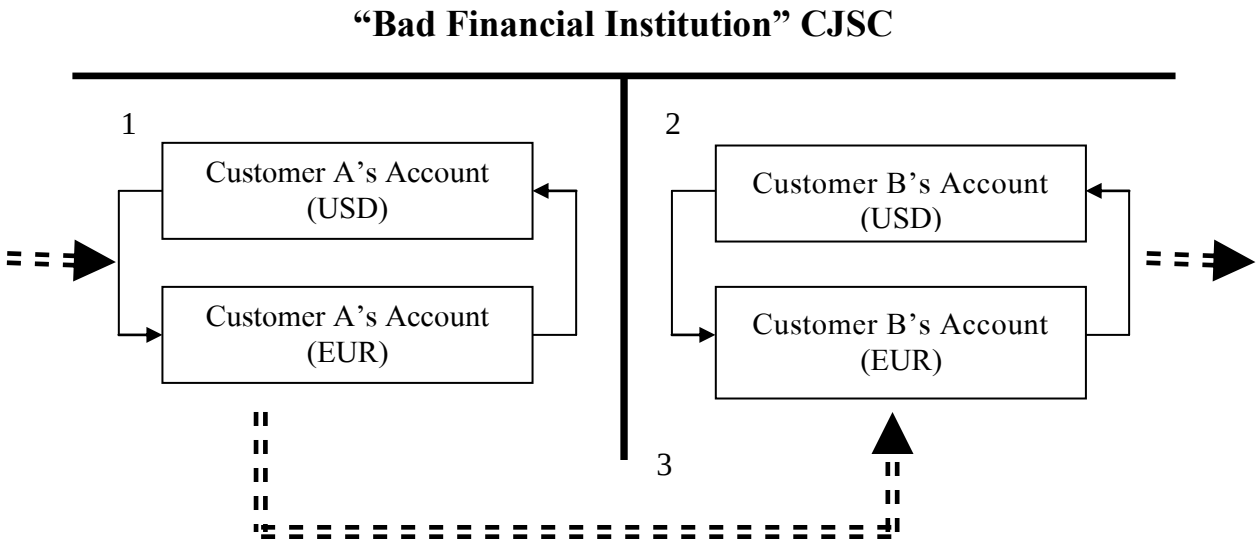
As a result, the financial institution pays Customer B a greater amount of US dollars than received (with an amount due to the margin of buy and sell exchange rates) for repurchasing the Euros sold and experiences certain amount of losses (in this case 50.000 US dollars). Thus, the financial institution "sacrifices" a certain amount of money for Customer B at the cost of losses.

As a result of the aforementioned transactions the proceeds derived from losses of Customer A are placed on the account of Customer B, concealing the true origin of the funds and the actual direction of movement, where, as a rule, the financial institution receives a "bonus" instead in the form of tariffs charged for foreign exchange transactions and/or income derived from the differences in exchange rates for buying/selling currencies.

Particularly, as a condition verifying the lawfulness of the conducted transactions, the financial institution can present/explain the aforementioned transactions to a possible third party with the following correspondence – "a1-b2" and "a2-b1" (according to the numbers of the abovementioned Points). That is, the institution can insist that the US dollars purchased in step "a1" from Customer A with an exchange rate of 1.500 were later on sold to Customer B in step "b2" with the same exchange rate and the Euros purchased in step "a2" from Customer A with an exchange rate of 1.450 were later on sold to Customer B in step "b1" with the same exchange rate, while in both cases having obtained income in the form of tariffs charged for foreign currency exchange transactions in this case.

The operations illustrated in both Point "a" and Point "b" can be conducted through a chain of exchanges in not only two, but three, four or more currencies, where the underlying logic and the aim of the transactions will not change. It is worth to also mention, that there is no standard or "best" timeframe for transactions to follow each other for the purpose of considering any combination of foreign exchange transactions as a "chain": the term can be somewhere in between one or more days, or a longer interval in certain cases. When reviewing similar transactions, the examination of the overall income (or the loss) of the relationship between the bank and the customer shall be important, including also the similarity of the conditions established for this category of customers (or material dissimilarities thereof).

2) The mentioned type of operations are schematically illustrated bellow



a. In the result of the two equal-amount foreign exchange reverse transactions carried out with Customer A, "Bad Financial Institution" CJSC obtains net income (e.g. sells Euros

and buys US dollars with an exchange rate of 1.500 and afterwards buys Euros and sells US dollars with an exchange rate of 1.450),

b. In the result of the two equal-amount foreign exchange reverse transactions carried out with Customer B, "Bad Financial Institution" CJSC experiences net losses (e.g. sells Euros and buys US dollars with an exchange rate of 1.450 and afterwards buys Euros and sells US dollars with an exchange rate of 1.500),

·. In the result, "Bad financial institution" CJSC provides for the transfer of funds derived from losses of Customer A to Customer B.

3) Conclusion

The operations conducted according to the illustrated scheme and series of steps may be aimed at concealing the origin, movement or true ownership (final beneficiaries) of proceeds.

In terms of examining transactions with elements of the illustrated scheme, special attention shall be drawn to **foreign exchange transactions carried out by financial institutions.**

4. Typology

Scheme for money laundering using transactions of trading bills of exchange/securities for the purpose of concealing the true origin of funds and directions of actual movements thereof

Transfer of funds is provided between customers of the bank with the types of transactions under consideration concealing (modifying) the true origin of funds acting as means of payments and the actual movement or the true ownership thereof.

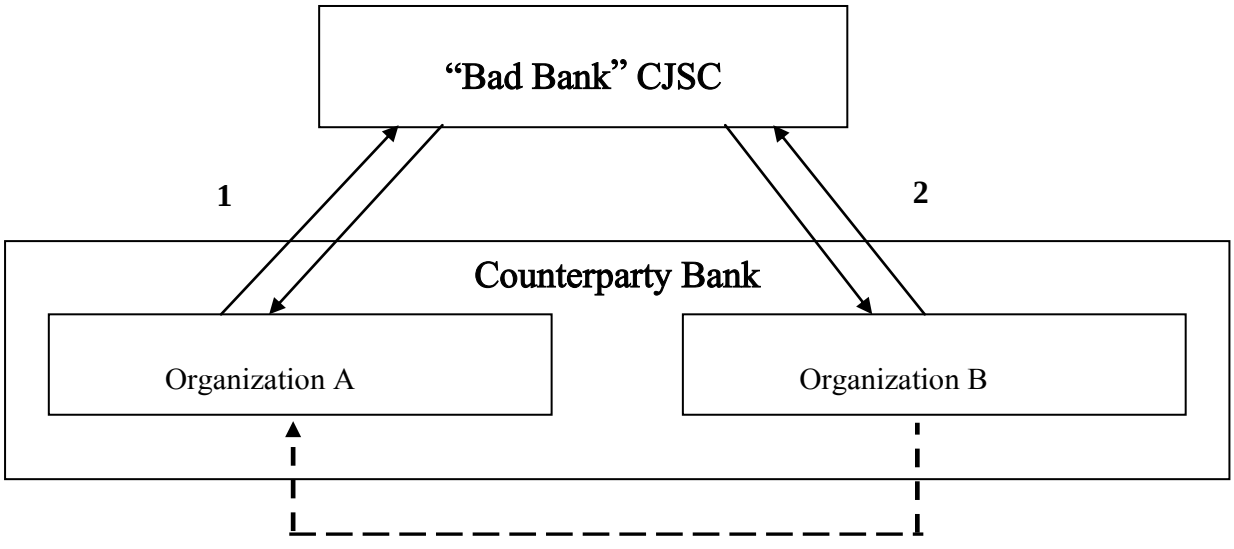
1) Description of the Scheme

The bank acquires bills of exchange/securities from an organization (e.g. Organization A), often issued by not prime companies, including also banks and other financial institutions. The acquired bills of exchange/securities are sold by the bank to another organization (e.g. Organization B) on the same day or the following short period. As a result, Organization B pays out and Organization A actually receives funds commensurate to the traded value of the bills of exchange/securities, though the transfer of these funds are reflected as separate transactions with the bank in the reports of each of the counterparties of the transaction, while in the reports of the bank the transactions are reflected as two separate transactions having nothing in common between two different business entities.

The purpose of engagement in such transactions for counterparties A and B is the concealment/modification of the movement of funds used as means of payments and the true ownership thereof. The bank in turn obtains income for providing intermediary services for ensuring the movement of funds in an amount commensurate to the difference in the buying and selling amounts of the securities.

Similar operations can be conducted through providing short-time credit to the buyer for the formation of sufficient funds to be used for purchasing bills of exchange/securities.

2) The mentioned type of operations are schematically illustrated bellow



a. “Bad Bank” CJSC acquires bills of exchange/securities of different companies from a foreign bank customer Organization A,

b. The acquired bills of exchange/securities are sold to another party serviced in the same or another foreign bank – Organization B on the same day or the following short period.

3) Conclusion

The operations conducted according to the illustrated scheme and series of steps may be aimed at concealing the origin, movement or true ownership (final beneficiaries) of proceeds.

In terms of examining transactions with elements of the illustrated scheme, special attention shall be drawn to **bills of exchange/securities trading operations carried out by financial institutions.**

Typology 5

Scheme for money laundering using Close-End Credit Cycle for the purpose of concealing the true origin of funds

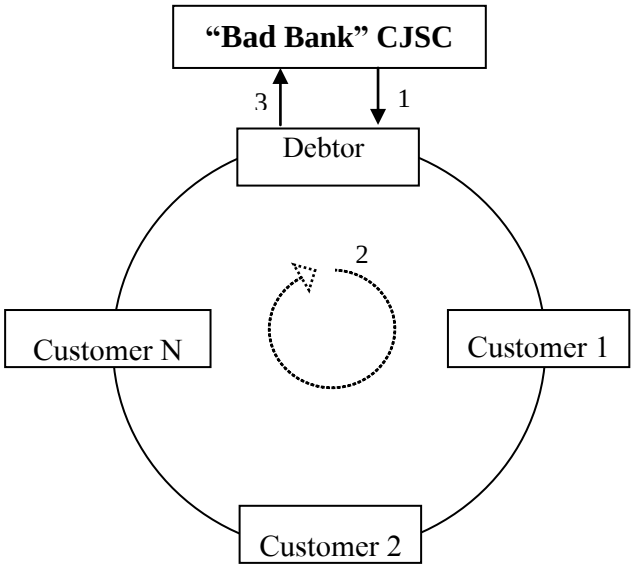
By using this scheme, a bank creates account turnover (credit history) for its clients, which afterwards can be used as justification of legality of the funds circulated by them.

1) Description of the Scheme

Thus, the bank grants a loan (or overdraft, financing of account) to one of its customers. Then, in a short period of time (usually a few days) those funds are sequentially transferred to the accounts of different customers of the bank. Finally, the funds are returned to the account of borrower and channeled to the repayment of the credit.

It is worth to mention that, as a rule, both opening and closing balances of the accounts of "intermediary" customers before and after the transactions are close to nil. Thus, a number of transactions take place allowing the participants to assert (obtain a confirmation from the bank) about certain balances on their accounts as of a certain date, or about the payments for certain contracts or obligations. Such transactions often are utilized in the so called "VAT carousel" schemes.

2) The mentioned type of operations are schematically illustrated bellow



1. The bank grants a loan (or overdraft, financing of account) to one of its customers,
2. In a short period of time (usually a few days) funds are sequentially transferred to the accounts of different customers of the bank;
3. Funds are returned to the account of borrower and channeled to the repayment of the credit and the accrued interest.

3) Conclusion

The operations conducted according to the illustrated scheme and series of steps may be aimed at concealing the origin, movement or true ownership (final beneficiaries) of proceeds.

In terms of examining transactions with elements of the illustrated scheme, special attention shall be drawn to **lending operations carried out by financial institutions, particularly lending to non-resident companies (especially companies registered in off-shore jurisdictions).**

6. Typology

Scheme for money laundering using lending practices at the cost of accepted deposits for the purpose of concealing the true origin of funds

1) Description of the Scheme

The operational mechanism of this scheme is that, the funds with unknown origin and in possession of the customer are injected into the banking system by one or more transactions, where afterwards loans are granted upon pledging these funds as a collateral for the purpose of verifying the lawful origin of funds in question for a third party.

Thus, cash or non-cash (via transfers from abroad) funds are developed on the account of the local bank customer, which are placed in the bank in the form of an account balance or a time deposit. As a document verifying the lawful origin of funds, real estate trade, lending, financial aid and other contracts can be presented. With the next step, having the mentioned account balance or the time deposit pledged as a collateral, loans are granted by the bank, which are managed upon the instructions of the customer, while generally being transferred abroad (in some cases - cash withdrawn).

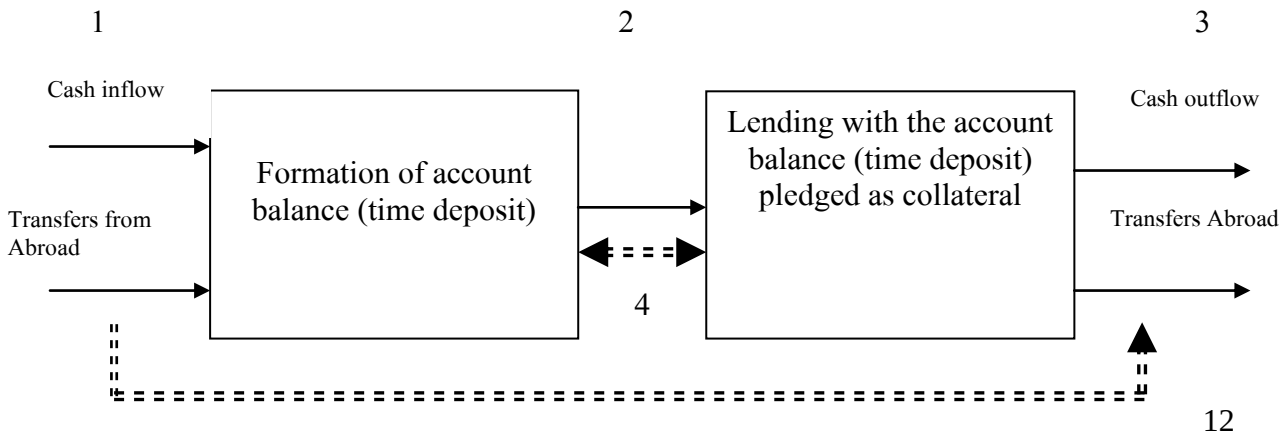
Similar operations can be carried out in the form of interbank operations following the same logic and order, i.e. when a foreign bank forms a loro account balance with the local bank (allocates a time deposit), loans collateralized with the mentioned funds are granted to local customers which are managed by them being generally transferred abroad. Particularly, in accordance with the logic of the mentioned transactions, the fact that the loro account balance (time deposit) is pledged at a local bank is not anyhow reflected in financial or other statements of the foreign bank.

In case of both options specified above the granted loans are repaid after a period of time at the cost of the customer's account balance (time deposit).

As a result of operations conducted with the mentioned schemes:

- The customer of the local bank verifies the lawfulness of the funds in possession for a third party – foreign country supervisory authority, by presenting the funds as loans obtained from the Armenian bank often being awarded privileges for transactions carried out by means of borrowed funds,
- The foreign banks resolves problems related to indirect lending of its customers and/or the refinancing/restructuring of impaired assets formed in the past.

2) The mentioned type of operations are schematically illustrated bellow.



a. Cash or non-cash funds are formed by the customer of the bank (via transfers from abroad) in the form of an account balance or a time deposit,

µ. Loans are granted with the account balance or the time deposit pledged as collateral,

b. The borrowed funds are managed upon the instructions of the customer being generally transferred abroad (in some cases cash withdrawn),

c. The granted loans are repaid after a period of time at the cost of the customer's account balance (time deposit).

3) Conclusion

The operations conducted according to the illustrated scheme and series of steps may be aimed at concealing the origin, movement or true ownership (final beneficiaries) of proceeds.

In terms of examining transactions with elements of the illustrated scheme, special attention shall be drawn to **transactions of financial institutions related to accepting deposits, granting loans, i.e. loans with funds and other high liquid assets being pledged as collateral.**

7. Typology

Money Laundering Scheme through Counterfeit Bank (Credit) Cards

1) Scope of Application

The scheme of transactions presented by this typology may be relevant for banks, which are reporting entities.

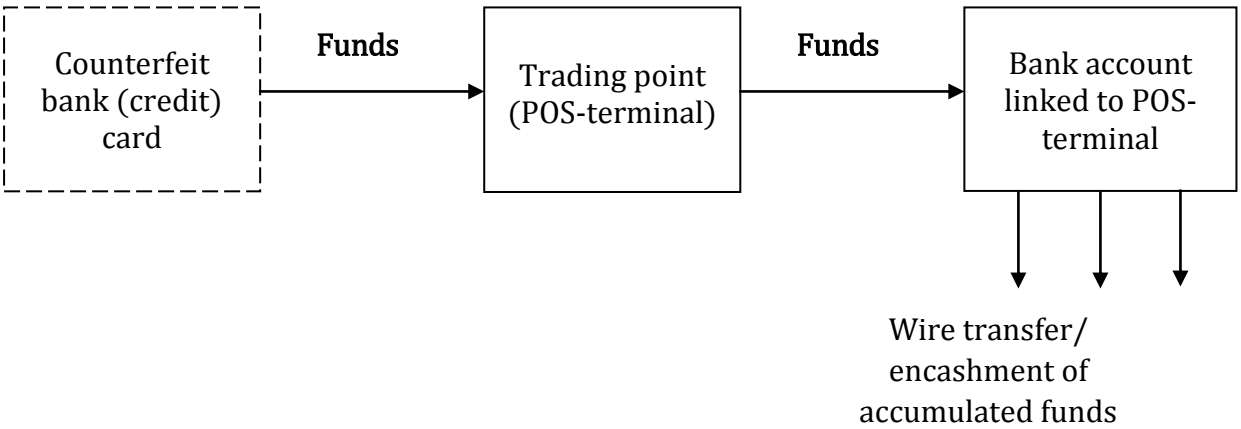
2) Description of Scheme

Transactions described in the typology below are usually carried out by means of counterfeit bank (credit) cards produced through illegal use of banking data of the customers of foreign banks. Such transactions are performed in the following sequence of actions:

a. A POS-terminal is installed at a trading point of a commercial entity/ individual entrepreneur to enable non-cash payment against goods sold (services delivered);
b. One or several customers make payments at the trading point by using counterfeit bank (credit) cards produced through illegal use of banking data of the customers of foreign banks; such payments may be made against factually or allegedly sold goods (delivered services)
c. Funds generated by the transactions are accumulated on the bank account of the commercial entity/ individual entrepreneur linked to the POS-terminal;
d. The accumulated funds are usually further channeled to financing regular activities of the commercial entity/ individual entrepreneur, by means of either wire transfers or encashment.

3) Schematic Illustration of Transactions

Schematic illustration of the transactions is presented below:



4) Conclusions

a. Transactions carried out through the illustrated scheme and sequence of actions are aimed at concealing the origin, movement, or true ownership (final beneficiaries) of illegal proceeds (generated through card fraud).

b. The following characteristics are typical for the transactions with counterfeit bank (credit) cards:
   1) Attempts of transactions are made within a short, unreasonable period of time (usually, several minutes);
   2) Several transactions with the same card are carried out one after another, some of them being attempts of transaction (for finding out the available balance on the card);
   3) Consecutively carried out transactions are either equal or proportionately diminishing in amount;
   4) Transactions are often carried out in "round" sums (e.g. AMD 300.000, AMD 100.000, AMD 50.000 etc);
   5) A number of transactions are carried out through the same POS-terminal, by means of one or several counterfeit cards.

c. The following measures should be taken for preventing the ML/FT risks pertinent to the transactions described in the scheme above:
   1) Pay special attention to numerous consecutive transactions by the same card and at the same trading point;
   2) Depending on the type of activities of the trading point, pay attention also to the amounts of factually carried out or attempted transactions, comparing them with the amounts of transactions usually carried out at the given trading point.

8. Typology

Money Laundering Scheme through Real Estate Transactions

1) Scope of Application

The scheme of transactions presented by this typology[1] may be relevant for the following types of reporting entities:

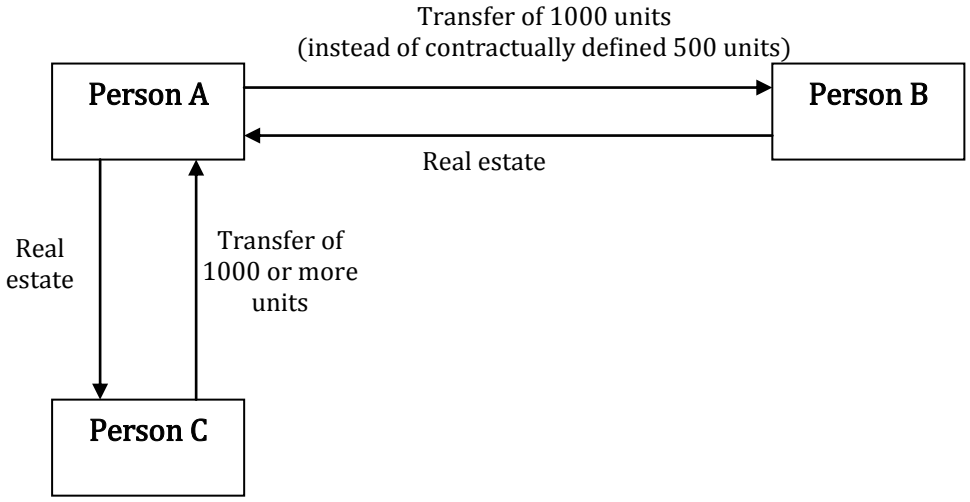
a. Banks, credit organizations, insurance companies;
b. The authorized body responsible for maintaining the integrated state cadastre of real estate;
c. Realtors;
d. Notaries;
e. Independents accountants and auditors; accounting and auditing firms;
f. Independent lawyers and firms providing legal services.

2) Description of Scheme

Transactions described in the typology below are usually performed in the following sequence of actions: Person A, who has illegally gained income totaling, for example, 1.000 units, comes to agreement with Person B selling a real estate and offers him to buy the property for 1.000 units; however, he wants that the price of the deal to be indicated in the contract is 500 units. Later on, Person A sells the real estate to Person C for 1.000 units (or even at a higher price), thus making the illegally gained income look like being generated from the sales of the property. In this case, it is possible that an offshore company acts as the buyer/ seller of the real estate for further concealment of the illegal origin of the funds.

3) Schematic Illustration of Transactions

Schematic illustration of the transactions is presented below:



[1] The typology was developed on basis of typologies published by FATF in 1997-1998 (www.fatf-gafi.org).

4) Conclusions

a. Transactions carried out through the illustrated scheme and sequence of actions are aimed at concealing the origin, movement, or true ownership (final beneficiaries) of illegal proceeds. The following characteristics are typical for such transactions:
   1) Inconsistency of the contractually defined price with the real (market) price of the property;
   2) Relatively short period between the purchase and the sale of the property (e.g. one or several weeks/ one month);
   3) Cash or non-cash transactions carried out by the initial seller of the real estate in amounts significantly exceeding the contractual price;
   4) Unclear/ suspicious sources of income of the intermediate and final payers against the transactions;
   5) Involvement of entities based in high-risk (offshore) territories.

b. The following measures should be taken for preventing the ML/FT risks pertinent to the transactions described in the scheme above:
   1) Enhanced due diligence of the customer;
   2) Additional scrutiny of the documents underlying the transaction;
   3) Check of legitimacy of the transaction;
   4) Efficient exchange of information with authorized state bodies and other organizations.

9. Typology

Money Laundering Scheme through Insurance Transactions

1) Scope of Application

The scheme of transactions presented by this typology[2] may be relevant for the following types of reporting entities:

a. Banks;

b. Insurance companies;

c. Insurance brokers and agents.

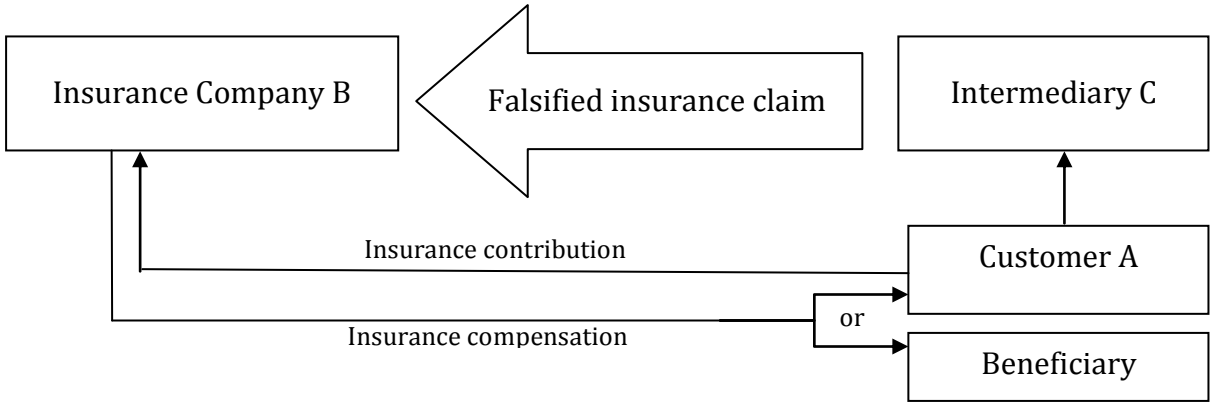
2) Description of Scheme

Insurance products are handy instruments for legalizing illegally gained income, since a significant part of insurance policies are sold by means of insurance brokers and agents, which often are the only ones to directly contact with the customers.

Customers (or, involved intermediaries) can explore money laundering schemes through the use of insurance companies by means of both false insurance claims and of early surrender of contracts within the allowable period. Transactions described in the typology below are usually performed in the following sequence of actions:

a. Customer A concludes an insurance contract with the Insurance Company B at extraordinary terms or under conditions not typical for the business. At that, the contract may define either the insured person or a third party (not related to the insured person) as the beneficiary of the contract. Later on, Customer A independently or in agreement with Intermediary C falsifies the respective documents for the purpose of filing an insurance claim and getting compensation. Thus, Customer A by means of falsification devised independently or jointly with Intermediary C, gains illegal income, which, declared as compensation received from the insurance company, may be freely used as legal income.

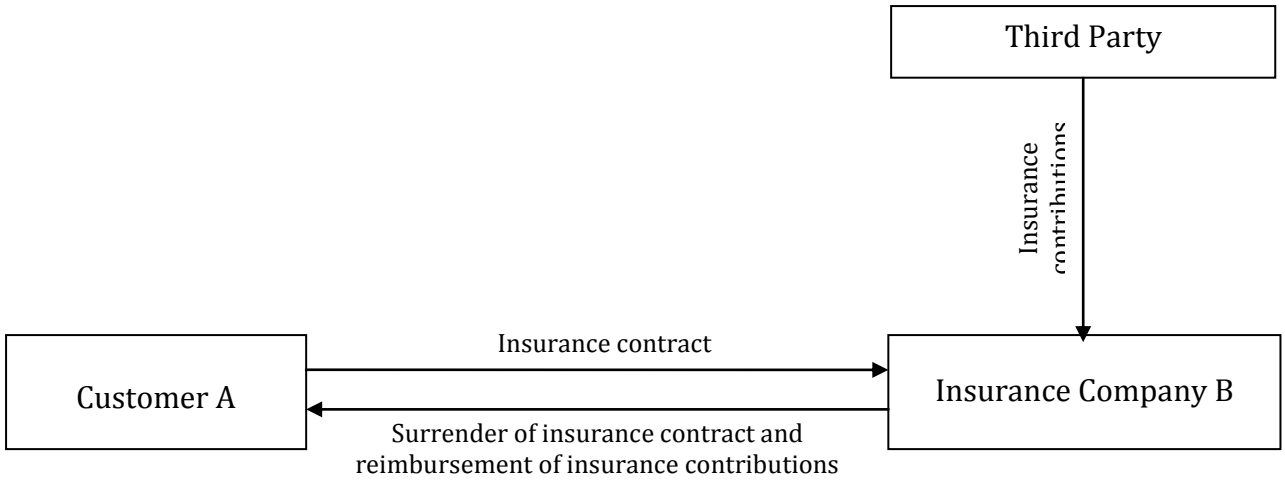
- Schematic illustration of the transactions is presented below:



[2] The typology was developed on basis of typologies published by FATF in 1995-1996 and 2003-2004 (www.fatf-gafi.org).

b. Customer A concludes an insurance contract with the Insurance Company B. At that, the contract may define a third, unrelated Third Party as the payer of insurance contributions. Later on, within the allowable period defined by the contract, Customer A requests early surrender and reimbursement of contributions. This sequence of transactions is aimed at legalizing the income illegally gained by the payer of contributions and transferring it to the insured person through the use of the insurance company.

- Schematic illustration of the transactions is presented below:



3) Conclusion

a. Transactions carried out through the illustrated scheme and sequence of actions are aimed at concealing the origin, movement, or true ownership (final beneficiaries) of illegal proceeds. The following characteristics are typical for such transactions:
   1) Obvious inconsistency of insurance contributions with the business profile and income of the insured person;
   2) Payment of insurance contributions by third (often, unrelated) parties;
   3) Absence or formal interrelation between the insured person and the beneficiary;
   4) Early and suspicious occurrence of the insured event;
   5) Early surrender of the insurance contract and reimbursement of contributions.

b. The following measures should be taken for preventing the ML/FT risks pertinent to the transactions described in the scheme above:
   1) Enhanced due diligence of the customer;
   2) Additional scrutiny of the documents underlying the transaction;
   3) Detailed examination of the circumstances of the insured event; request for submission of additional documents;
   4) Detailed examination of cases of early surrender of the insurance contract; disclosure of real reasons;
   5) Efficient exchange of information with authorized state bodies and other organizations.

Typology No 10

Money Laundering through Commercial Transactions Related to Cross-Border Conveyance of Goods

Chapter 1: Scope of Application

1. The scheme of transactions presented by this typology may be relevant for the following types of reporting entities:
   g. Banks;
   h. Attorneys, independent lawyers and firms providing legal services;
   i. Independents accountants and accounting firms;
   j. Independents auditors and auditing firms.

Chapter 2: General Provisions

2. The purpose of this typology is to uncover motives of economic entities to forge documents on commercial transactions related to the conveyance of goods trough the customs border of the Republic of Armenia (hereinafter: RA), and to identify money laundering schemes deriving from such motives. This, in turn, aims to assist the reporting entities designated by the RA Law on Combating Money Laundering and Terrorism Financing (hereinafter: the Law) in due performance of their obligation to recognize suspicious transactions or business relationships and to file suspicious transaction reports to the Authorized Body.
3. The description of possible money laundering schemes and the examples of their use, as presented by this typology, is not exhaustive; it just outlines a standard framework of typical money laundering risks in commercial transactions, so as to provide a general understanding to reporting entities and to guide their internal compliance function in the prevention of identical and similar risks.
4. Reporting entities should pay special attention to the prevention of money laundering risks related to the cross-border conveyance of goods in fulfillment of their obligation to conduct on-going customer due diligence as defined by Article 16 of the Law. This obligation entails monitoring of the transactions with customers to assure veracity of the information on customers, their business and risk profile and, where necessary, the source of their income. In view of this, in the course of monitoring the customers involved in import or export activities, reporting entities should take into consideration the specific risks pertinent to such transactions, understand the nature of the transactions – by means of requesting from the customers and examining the necessary information or documents, and assess their veracity, conducting enhanced due diligence as appropriate and filing to the Authorized Body reports on suspicious transactions or business relationships as necessary.

Chapter 3: Basic Terms and References

5. This document uses the following terms as defined by the RA Customs Code and by other laws:

1) *Customs territory of the RA* comprises land, water, and air space of the RA. The territory of the RA may comprise customs warehouses and free trade zones not included into the RA customs territory.
2) *Customs value* is the price of the transaction, that is the amount actually paid or subject to payment or to be paid for the purchase of goods and for their transportation to the customs border of the RA. Customs value of goods conveyed through the RA customs border is determined by the declarant, except for the cases stipulated by the RA Customs Code, when it is determined by customs authorities.
3) *Customs payments* are payments defined by law and collected by customs authorities for the conveyance of goods and vehicles through the RA customs border, including:
   a. Customs duties;
   b. Customs fees;
   c. Taxes, duties, and other mandatory payments defined by law and collected by customs authorities.
4) *Customs duties* are mandatory collections to the State Budget pursuant to the procedure and in the amounts stipulated by the RA Customs Code for the conveyance of goods through the customs border of the RA. Customs duties and their rates are determined by the RA Customs Code. Depending on the nature of operations, the following customs duties are applied in the RA:
   a. Export duties – for goods exported out of the customs territory of the RA;
   b. Import duties – for goods imported into the customs territory of the RA;
   c. Seasonal duties – for exporting specific goods out or importing thereof into the customs territory of the RA within certain periods of the year.

   The rate of customs duties may be zero or 10 percent[3] as per the list defined by Article 102 of the RA Customs Code.
5) *Customs fees* are mandatory collections to the State Budget pursuant to the procedure and in the amounts stipulated by the RA Customs Code, used for the promoting customs affairs, providing the material/ technical basis of customs authorities, and social protection of customs officials.

   The rates of customs fees is defined 3.500 drams for customs formalities, 10.000 drams for customs escort (for each 100 kilometers), and 1.000 drams for each document produced.
6) *Taxes, duties, and other mandatory payments* defined by law and collected by customs authorities include value added tax (VAT), excise tax, environmental payments, road payments etc. For the purposes of this typology, consideration is given only to value added tax – an indirect tax paid at all phases of importing

[3] At that, the agreement on Armenia's joining the World Trade Organization in 2003 envisages that the country may establish and apply other rates, as well. The RA Government so far has not made such a decision (which, in essence, would establish a predicate for determining a rate other than zero or 10 percent); however, this does not mean that a higher (up to 15 percent) rate may not be applied in future for protecting domestic producers.

goods into the country, of their production and sales within the country, as well as at all phases of the provision of services.

6. According to Item 4, Article 6 of the RA Law on Value Added Tax, import of goods under the *"import for free turnover"* customs regime is a VAT taxable operation, which implies calculation and collection of taxes by customs authorities on the RA customs border. According to Article 16 of the same law, export of goods under the *"export for free turnover"* customs regime is taxable by a zero percent rate of VAT applied to the taxable turnover of exported goods.
7. Application of VAT on the RA customs border in the case of imports has certain peculiarities and exceptions, as follows:
   1) No VAT is calculated and collected on the border in respect of the goods, for which:
      a. The RA Customs Code determines a zero percent rate of import customs duties and an exemption from excise tax; the list of such goods is defined by a separate law[4];
      b. Supply is exempt of VAT in accordance with Item 28, Article 15 of the RA Law on Value Added Tax (supply of goods under humanitarian or charitable programs by intergovernmental, religious, and non-governmental organizations, including charitable organizations).
   2) Article 6^1 of the RA Law on Value Added Tax defines that in the case of importing certain types of goods (the article also specifies unique identification codes of those goods) payment of VAT is deferred: a) by one year from the date of declaration – for goods below 70 million drams of customs value; b) by two years from the date of declaration – for goods above 70 million drams of customs value; and c) by three years from the date of declaration – for goods above 300 million drams of customs value. The same article establishes that in the case of importing goods other than those specified by the said article and imported under investment projects above 300 million drams by entities and individual entrepreneurs determined by the RA Government decisions, payment of VAT may be deferred by three years.
8. Application of VAT on the RA customs border in the case of exports has certain peculiarities, as follows:
   1) According to Article 16 of the RA Law on Value Added Tax, VAT is not calculated and collected in respect of export transactions; in other words, a zero percent rate of VAT is applied[5].
   2) According to the same article, the amount of VAT credited to tax accounts of VAT taxpayers in respect of purchased goods and received services related to transactions taxable by a zero percent rate of VAT are subject to refund (set-off).

[4] Law on Approving the List of Goods Imported by Organizations and Private Entrepreneurs, Subject to a Zero Percent Rate of Customs Duties and Exempt from Excise Tax, For Which Customs Authorities Do Not Calculate and Collect Value Added Tax" (adopted on June 29, 2001, HO-195).

[5] At that, the RA Customs Code also establishes a zero percent rate of customs duties in respect of exported goods.

9. In respect of transactions, which are not taxable by a zero percent rate of VAT, the first paragraph of Article 25 of the same law defines that if the amount of VAT subject to set-off in the reporting period exceeds the amount of VAT calculated for the taxable turnover of that period, the exceeding portion of VAT is set-off with the amount of VAT payable to the State Budget in the future periods. This does not apply to transactions taxable by a zero percent rate of VAT[6], for which, based on the written application of the taxpayer, the amount of VAT credited to tax accounts and separated in import customs declarations of the suppliers may:
   1) Be set-off with other tax liabilities of the taxpayer; and (or)
   2) In the absence of tax liabilities payable to the State Budget, be refunded or set-off with other tax liabilities of the taxpayer, should the taxpayer have a positive balance of VAT receivable. In such cases, the part of the positive balance of VAT receivable (excluding overpayments and amounts of taxes not subject to set-off) in an amount not exceeding 20 percent of the taxable turnover of zero percent rated VAT taxable transactions may be set-off with other tax liabilities of the taxpayer, and (or) be refunded.
10. Article 22 of the RA Customs Code defines the following **customs regimes** for the conveyance of goods through the RA customs border:
   1) *Import for free turnover;*
   2) Re-import;
   3) Transit shipment;
   4) Import to customs warehouse;
   5) Import to duty free shop;
   6) *Temporary import for processing;*
   7) Temporary import;
   8) Temporary export;
   9) Import to free customs warehouse;
   10) *Temporary export for processing;*
   11) *Export for free turnover;*
   12) Re-export;
   13) Renunciation of the ownership right for the benefit of the State;
   14) Destruction;
   15) Import to free trade zone.

Chapter 4: Description of Potential Money Laundering Schemes

11. In order to recognize operations potentially aimed at money laundering by means of commercial transactions related to conveyance of goods through the RA customs border, it should be considered from the viewpoint of importers and exporters separately.

12. **Identification of Money Laundering Risks in Import Operations**

[6] Except for transactions related to the export of black and color scrap metals.

1) The description of perhaps the most widely-used regime – "import for free turnover" – of conveyance of goods through the RA customs border is the following:

   Let us assume that a RA resident entity imports goods with unit purchasing price of USD 85 and unit cost of transportation to the RA customs border (including insurance, freight etc) of USD 15[7]. For the purposes of this example, it is assumed that a certain rate (10 percent) of import customs duties defined by the RA Customs Code is applicable to the imported goods. For the customs clearance of the goods, apart from the calculation and collection of customs fees, the following computations are made:

   a. Customs value is equal to the sum total of all expenses related to transportation of goods to the RA customs border – in this example equal to USD 100;
   b. Customs duties, as per the list defined by Article 102 of the RA Customs Code, are equal to 10 percent of the customs value – in this example equal to USD 10;
   c. The amount of applicable VAT is equal to 20 percent of the sum total of customs value and customs duties (100+10=110) – in this example equal to USD 22.

2) For maximal exactness, the expenses related to transportation of goods to the importer's warehouses – in this example equal to USD 5 – are also taken into account. Thus, the unit cost of imported goods in this example is equal to USD 115 (100+10+5), and the VAT receivable from the State Budget is equal to USD 22.
3) Let us also assume that the importer intends to make at least a 30 percent profit on the sales of imported goods. This means that unit sales price of the goods should be at least USD 150 ([150-115]/115 = 30%). Hence, the retail unit sales price is set at USD 180, of which 16.67 percent – or USD 30 - is to be credited to the importer's tax accounts as the amount of VAT generated after the import of goods, due to their sales in the RA territory. Taking into account that, in terms of VAT, the importer has already accrued and made a payment of USD 22, the amount to be paid to the State Budget after the sales of the goods is USD 8 per sold unit.
4) In the sequence of actions described in sub-clauses 1 to 3 of this clause, for the purpose of maximizing profit through artificial reduction of the amount of customs duties and taxes payable to the State Budget, economic entities may have motives to **artificially reduce** the customs value of imported goods by means of forging import-related documents. The following circumstances have an influence on the formation of such motives in import operations:

[7] In the Republic of Armenia, accounts are kept in Armenian drams; however, for the sake of simplicity, cost and other calculations in this example are presented in US dollars.

a. The rate of customs duties, which may be equal to zero or 10 percent depending on the type of the goods (as per the list defined by Article 102 of the RA Customs Code);
b. Applicability of VAT, since the imported goods may be taxable or non-taxable in terms of VAT depending on whether they match the exception criteria defined by Item 4, Article 6 of the RA Law on Value Added Tax.

5) For instance, an economic entity importing goods subject to a 10 percent rate of customs duties and (or) taxable by VAT, may involve in abusive practices by artificially reducing customs value of the imported goods (particularly, by presenting forged documents on their purchase price), thus reducing customs payments to be made for those goods.
6) In similar circumstances, importers may have motives for **artificially raising** customs value of the imported goods. For instance, an economic entity importing goods subject to a zero percent rate of customs duties and (or) non-taxable by VAT, may artificially raise customs value of the imported goods, thus reducing sales profit and, consequently, paying less profit tax (in the case of private entrepreneurs – less income tax) to the State Budget.
7) At that, one should take into consideration specific details pertinent to the given situation: for instance, an importer enjoying a tax recess, or operating as a flat taxpayer, or having large accrued tax losses deferrable for 5 years forward, may not demonstrate the conduct of a "standard" profit taxpayer, since it is not concerned with the high profitability of its import operations.
8) Likewise, one should take into account that in addition to the transaction price method defined by Article 87 of the RA Customs Code (when the purchasing price documents presented by importers are taken as basis for determining customs value), customs authorities are authorized to use any of the other five methods defined by Articles 88-93 of the same Code[8]. As a result, the situation may be that, if the transaction value method is not used, a direct influence on profit tax under the given transaction perhaps is not relevant, since according to the RA Law on Profit Tax the original accounting documents are taken into account instead of the customs value determined and applied for customs clearance of the goods.
9) Moreover, forging the customs value in import operations may be conditioned not by or not only by the attempt to artificially reduce customs duties or taxes payable – so as to maximize profit, but also to create documentary substantiation for certain financial flows out of Armenia. For example, an importer wishing to legally move certain funds out of the country may "sacrifice" some money by paying more taxes (duties) due to declaring a higher purchasing price, which will enable making to its foreign counterparts/ suppliers transfers above the real cost of the purchased goods, thereafter making use of the extra-

[8] These methods for determining customs value are: 1) transaction price of identical goods; 2) transaction price of similar goods; 3) unit sales price in the domestic market; 4) computed value; and 5) residual method.

transferred funds by means of certain schemes (the possibility of using this option is higher when the counterparts/ suppliers are registered/ operating in offshore countries or territories).

10) Another wide-spread scheme involves the import of equipment, whose price structure may or may not comprise the cost of installation works and (or) intellectual property or accommodation rights. Since works, services, or intellectual property rights are not separate goods conveyable through the border, there is a possibility that economic entities attempt to change customs value of imported goods by means of these constituents. Typical examples of this are the import – through modern means of communication – of the software necessary for the startup of the imported equipment; acquisition of installation works or consultancy or data processing services at unrealistically high prices or under conditions not typical for the business practice.

13. Identification of Money Laundering Risks in Export Operations

1) The description of perhaps the most widely-used regime – "export for free turnover" – of conveyance of goods through the RA customs border is the following:

   Let us assume that a RA resident entity is involved in the production and export of certain goods. At that, the structure of the unit export price comprises material expenses equal to 60.000 drams, wages and social contributions equal to 15.000 drams, and an expected profit equal to 25.000 drams; that is the unit sales price totals 100.000 drams. According to Article 25 of the RA Law on Value Added Tax, exporters are authorized to claim refund of VAT in respect of material expenses included in the export price, while the amount of such refund can not exceed 20 percent of the export price. In accordance with Article 9 of the same law, the amount of refund is determined at a rate of 16.67 percent, which means that in this example the maximum amount of refund would be around 16.670 drams, whereas the concrete amount to be refunded (which usually is approved through examination by tax authorities) is equal to 60.000 * 20% = 12.000 drams.

2) In the sequence of these actions, for the purpose of maximizing the refund of VAT from the State Budget, economic entities may have motives to **artificially raise** the export price of goods by means of forging export-related documents. The following circumstances have an influence on the formation of such motives in export operations:
   a. The specific type of goods, which may be VAT exempt as per the list defined by Article 15 of the RA Law on Value Added Tax[9];
   b. The specific taxation regime, which the exporter may use;
   c. Presence of a free trade agreement, which might be signed between Armenia and the country of import.

[9] For example, sales of newspapers and magazines, prosthetic/ orthopedic devises, precious and semi-precious stones as specified by the RA Government's list are exempt of VAT.

3) For instance, an economic entity enjoying a profit tax privilege (according to Chapter 6 of the RA Law on Profit Tax) and exporting goods taxable by a 20 percent VAT, may involve in abusive practices by artificially raising customs value of the imported goods (particularly, by presenting forged documents on price formation), thus increasing the claimed VAT refund from the State Budget for the export of those goods. The same logic is applicable in the case of transfer pricing operations.
4) In this case, as well, one should take into consideration specific details pertinent to the given situation: for instance, an exporter enjoying a tax recess, or having large accrued tax losses deferrable for 5 years forward may not demonstrate the conduct of a "standard" profit taxpayer, since it is not concerned with the high profitability of its export operations.
5) Moreover, just like in the case of import operations, forging the export price may be conditioned not by or not only by the attempt to artificially raise that price – so as to maximize the amount of VAT refund, but also to create documentary substantiation for certain financial flows into Armenia. For example, an exporter wishing to legally move certain criminal funds into the country may "sacrifice" some money by paying more taxes (duties) due to declaring a higher export price, which will enable receiving from its foreign counterparts/ suppliers transfers above the real cost of the exported goods, thereafter making use of the extra-received funds by means of certain schemes (the possibility of using this option is higher when the counterparts/ buyers are registered/ operating in offshore countries or territories).
6) A particular case of the schemes described in clauses 1 to 5 above are the **commodity-void transactions** (the so called VAT "carousel" schemes), when economic entities involved in abusive practices attempt to get VAT refund for the export of non-existent goods or services on basis of forged documents[10].
7) Economic entities involved in export operations may also have motives to **artificially reduce** the export price of goods by means of forging export-related documents in cases, when the country of import has a more favorable taxation regime; that is, the exporter is interested in exporting goods and, respectively, importing them into the destination country at a lower price, since the profit generated thereon would be taxed at a lower rate as compared with the taxation in the RA – should the real export price be declared.
8) Hence, both in the case of import and export operations, disclosure of potential money laundering schemes requires that the specific characteristics of the transaction are considered so as to uncover the concrete motives of the importer/ exporter to demonstrate abusive conduct.

[10] In general, money laundering schemes through commodity-void transactions may be used under the veil of both import and export operations; that is, when flows of funds out or into the country are substantiated by agreements on provision of non-existent goods or services.

14. **Peculiarities of Transaction Related to Temporary Import for Processing and Temporary Export for Processing**

1) Motives for forging price-formation documents in import or export-related economic activities may be separately or in combination be present also in operations involving temporary import or export of goods for processing. Here one should take into consideration that: 1) under the "re-export" customs regime, when exporting goods once imported under the "temporary import for processing" regime, and 2) under the "re-import" customs regime, when importing goods once exported under the "temporary export for processing" regime, the following differences are calculated and collected on the RA customs border (in both cases excluding customs fees, which are non-deductible):
   a. In the first case – the positive difference between the customs payments envisaged for the export of processed goods under the "export for free turnover" customs regime and those for the import of to-be-processed goods under the "export for free turnover" customs regime;
   b. In the second case – the difference between the customs payments envisaged for the import of processed goods under the "import for free turnover" customs regime and those for the export of to-be-processed goods under the "import for free turnover" customs regime.
2) The peculiarity of operations specified in sub-clause 1 of this clause is that, for instance, the purpose of price forgery in the import of goods under the "import for free turnover" customs regime may be attained by means of one step (for example, through reducing the amount of calculated and collected customs duties and taxes on the RA customs border by means of presenting forged documents), and the movement of goods/ services and the underlying price-formation documents takes place in one direction (in this example, to Armenia), whereas in the case of temporary import/ export operations attainment of such purpose usually requires more than one step and a series of actions with constituents, which individually do not necessarily comprise irregular or illegal activities. Nevertheless, the totality such actions has a final objective of legalizing proceeds of a predicate offence, that is laundering money.

   For example, a company involved in imports of semi-processed goods, their further processing in Armenia (adding value), and exporting the final product may be interested in **artificially raising** the value of imported semi-processed goods and declaring the real cost of exported final product, thus minimizing the value added in the territory of the RA and, therefore, the taxes accruable and payable in the country. In this case, the motives for artificially raising the value of imports is not the same as those in the case of importing goods under the "import for free turnover" customs regime or of exporting goods under the "export for free turnover" customs regime, since the economic entity involved in abusive practices attains the ultimate purpose of its illegal actions at the moment

of exporting the final product – by means of minimizing the value added in the RA.

Chapter 5: Conclusions

15. In order to arrive at a conclusion on the existence of potential money laundering schemes, reporting entities should pay attention to the circumstances, which are essential in terms of uncovering such schemes, such as:
    1) Integrity of contents of the documents substantiating economical or logical relevance of the transaction (i.e. contracts, agreements etc); their conformity with the business practice of the given type of activity;
    2) Trustworthiness of other transaction-related documents (invoices, documents verifying conveyance through borders, transportation expenses etc);
    3) Conformity of the basic characteristics (price, deadlines, supply terms etc) of the transaction with the market terms and reasonable conduct;
    4) Conformity of the transactions with the customer's business profile, its declared and factually realized business objectives;
    5) Conformity of the amounts, directions, and frequency of financial flaws and other characteristics of the customer's transactions with the circumstances and facts set forth in the documents substantiating economical or logical relevance of the transactions;
    6) Involvement of offshore and other high-risk companies in the customer's transactions.

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