CENTER FOR THE STUDY OF DEMOCRACY

GLOBAL INITIATIVE AGAINST TRANSNATIONAL ORGANIZED CRIME

CASH IS KING

IMPACT OF THE UKRAINE WAR ON ILLICIT FINANCIAL FLOWS IN SOUTH EASTERN EUROPE

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This research report is the output of work conducted by the Global Initiative Against Transnational Organized Crime (GI-TOC)'s Observatory of Illicit Economies in South Eastern Europe, in collaboration with the Center for the Study of Democracy (CSD).

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UK Government

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Cover photograph: A woman walks past a currency exchange office in central Belgrade, Serbia. © *Reuters/Ivan Milutinovic*

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CONTENTS

EXECUTIVE SUMMARY

Illicit cross-border financial flows – estimated at US$1–1.6 trillion a year globally[1] – are harming economic development on a national and global level.[2] This is particularly true when such flows originate in heavily étatist economies, with no effective division or independence of the private from the public or state-owned sector. Autocracies have long utilized obfuscated corporate ownership structures and illicit financial flows (IFFs) for nefarious purposes such as bribery, corruption and improper lobbying to secure anything from technologies and know-how to economic and political influence on countries of interest. Russia has established a pattern of malign economic impact in Europe through its cultivation of 'an opaque network of patronage across the region that it uses to influence and direct decision-making' in key markets and institutions.[3] IFFs in the Balkan region, in particular, are manifold, multi-directional and, proportionally, large as a percentage of GDP.[4] While global illicit outflows are 3–5% of world GDP, IFFs in the Balkans are estimated at about 6% of the region's GDP.[5] The common denominator of the Western Balkan countries is their vulnerabilities kindled by institutional weakness and state capture. IFFs promote rent-seeking and criminal behaviour, reduce governments' capacity to support development and inclusive growth, undermine the rule of law and jeopardize the business environment. Illicit flows drain public resources, reduce the scope and quality of public services and, thus, undermine confidence in state institutions.[6]

The Kremlin has repeatedly taken advantage of its integration into the Western financial system to exploit governance gaps through the corrosive effect of illicit finance.[7] The brutal invasion of Ukraine shed a harsh light on the sobering dangers of kleptocracy and the risks to which Europe – and the world – has exposed itself by taking a lax approach to dirty money. Russia's war in Ukraine could exacerbate these circumstances and accelerate further IFFs in the Balkan region – a crucial entry point and essential route for a plethora of illegal activities, such as drug trafficking, human smuggling, illicit trade and contraband.[8] Due to imposed travel bans, Serbia is one of the few remaining routes for Russians to establish themselves in the region. Since the start of the invasion of Ukraine, Russian nationals have registered more than 5 000 companies in Serbia, over 1 000 being limited liability companies and nearly 4 000 entrepreneurial businesses.[9] The establishment of so many companies in the country offers fertile ground for money laundering.[10] As observed in the Serbian national risk

A billboard in Belgrade for Gazprom PJSC, featuring the Russian and Serbian national flags, reads 'Together'. Since the start of the Ukraine invasion, Russian nationals have registered more than 5 000 companies in Serbia, with consequent risks for money laundering. *© Oliver Bunic/Bloomberg via Getty Images*

assessment by the Administration for the Prevention of Money Laundering, limited liability companies and entrepreneurs pose a particularly high degree of threat with respect to money laundering. Through such means wealthy Russians could seek investment opportunities and use existing connections to launder money in real estate and other sectors traditionally vulnerable to IFFs in the region.

The primary goal of this report is to assess the major enablers and vulnerabilities of illicit finance in the eight Balkan countries (Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Kosovo, Montenegro, North Macedonia and Serbia) after Russia's invasion of Ukraine. More concretely, the study aims to analyze the primary IFFs sources and channels in the region, and identify any emerging trends concerning modus operandi, routes, business models, use of information and communications technology. In addition, the study intends to inspect the pressing challenges to border control, police and anti-money laundering authorities to effectively prevent, investigate and counter organized crime involved in cash smuggling and money laundering. Finally, the report aims to suggest feasible recommendations for improvement.

The analysis presented is based on information collected through mixed methods research consisting of qualitative and quantitative desk research and in-depth interviews with key professionals from different organizations and professional affiliations in the eight countries. A total of 15 semi-structured interviews were conducted with experts from regional organizations, customs agencies, national anti-money laundering authorities, national revenue agencies, national customs agencies and NGOs, as well as with journalists and academics. A guiding questionnaire with key questions and topics was shared with the field researchers to facilitate the work and to ensure consistency in the information collection process.

WHAT ARE IFFS?

Understanding and estimating illicit finance is an enormous task, as there is no universally accepted definition or single indicator that can comprehensively capture the phenomenon.[11] The term IFFs, coined in the 1990s, has only recently gained attention among decision-makers and within international organizations.[12] An illicit financial flow is money – illegally earned, used or moved – that crosses an international border. According to a broader definition, IFFs are funds that, through legal loopholes and other artificial arrangements, circumvent the spirit of the law. IFFs emerge from 'financial activities and practices that are illegal or abusive' and elusive in nature with a cross-border impact.[13] These include tax abuse; exploiting bilateral/multilateral tax, trade and investment agreements; abusive transfer pricing; odious debt; trade misinvoicing; crime; and corruption. A financial flow can be classified as illicit if either its origin (source), the method used for moving it (channel) or its eventual use is illegal. The channels of IFFs are the methods by which illicit flows move across borders, including different forms of money laundering, trade misinvoicing, cash transfers and capital account channels. It is important to note that a single flow of money might go through different channels. Common sources of IFFs are:

- Corrupt proceeds (funds acquired through abuse of state power);
- Criminal proceeds (illegal markets money, individual tax evasion or tax fraud); and
- Commercial proceeds (multinational tax or tariff evasion).

The Bar–Boljare highway, linking Montenegro to Serbia, is being constructed by the China Road and Bridge Corporation. Infrastructure investments in the Balkans – mostly a consequence of China's Belt and Road Initiative – are a catalyst for financial flows. *© Savo Prelevic/AFP via Getty Images*

Each source tends to favour specific channels over others.[14] For instance, no grand corruption cases seem to involve trade-based money laundering. Numerous studies determine illicit finance as being hidden by definition.[15] However, this is not necessarily so: capital, generated through illegal activities, may be transferred through legitimate channels and held in a transparent manner. IFFs often end up commingled with or laundered into the legitimate economy, or held in offshore jurisdictions and tax havens.

Stemming IFFs requires international collaboration and a whole-of-government approach to discern the overall problem, the extent and origin of flows, their routes and destinations, and regional and country-specific circumstances. Moreover, proactive public–private partnership is crucial to enable in-depth investigations – so as to follow the money. However, much-needed progress has been stalled due to the lack of a standardized methodological framework for measuring IFFs and the fact that most methods evaluating these flows lead to biased estimates as they measure, in part, the same source or channel and regularly favour types of flows that can be more easily constructed.

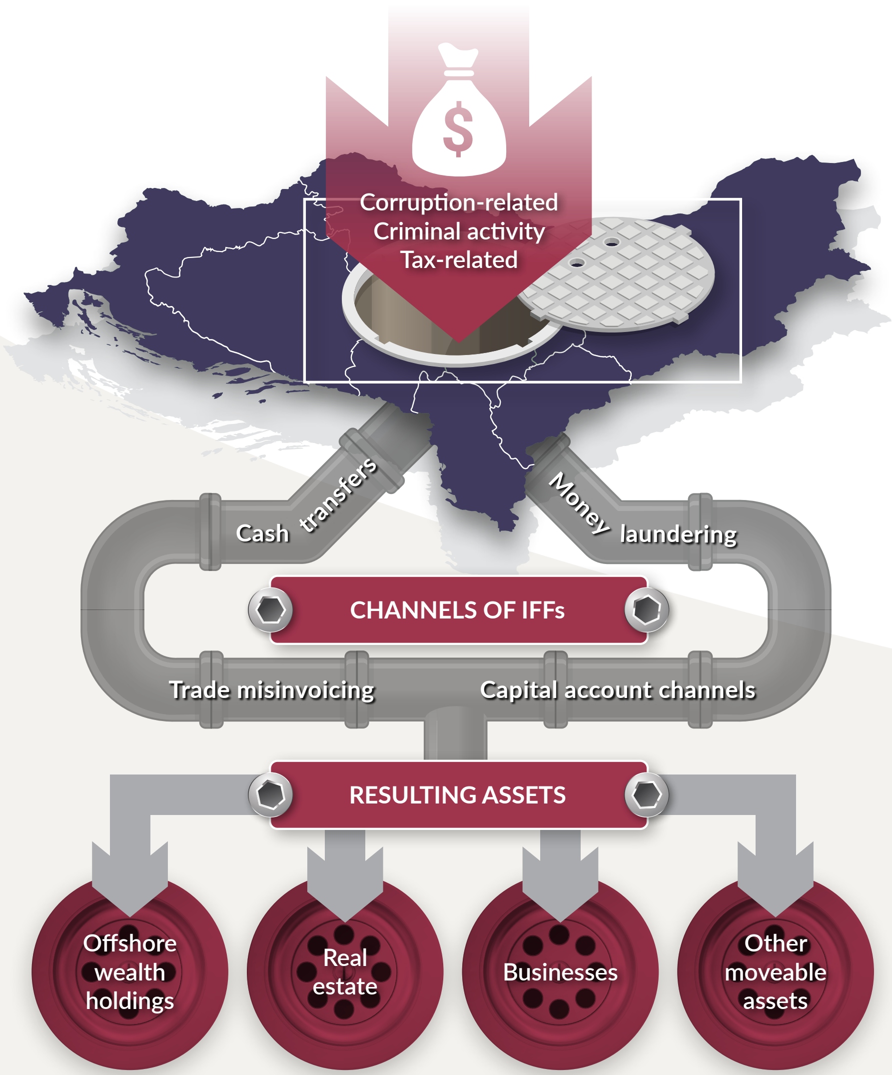


FIGURE 1 Conceptualizing illicit financial flows in the Balkans.

Country	Illicit outflows (% of GDP)	Illicit inflows (% of GDP)	Most vulnerable to	Trading partners most responsible for vulnerability
Albania	2.16%	0.84%	Inward FDI	The Netherlands, Italy, Switzerland
Bosnia and Herzegovina	8.30%	0.91%	Inward FDI	Austria, Croatia, Russia
Bulgaria	3.55%	4.81%	Inward FDI	The Netherlands, Austria, Germany
Croatia	2.63%	4.70%	Outward FDI	The Netherlands, Slovenia, Marshall Islands
Kosovo	7.83%	4.34%	Outward FDI	Germany, Switzerland, Cyprus
Montenegro	4.10%	3.95%	Inward FDI	Russia, Italy, UAE
North Macedonia	5.72%	1.62%	Inward FDI	South Africa, Austria, UK
Serbia	3.46%	0.98%	Inward FDI	The Netherlands, Austria, Cyprus

FIGURE 2 Vulnerabilities of Western Balkan countries to illicit financial flows, including foreign direct investment (FDI).

SOURCE: Center for the Study of Democracy

Illicit capital moves in and out of the Western Balkans in every direction and on a staggering scale, enabled by an ecosystem of state capture, organized crime and a rampant shadow economy. The Center for the Study of Democracy has estimated through trade mispricing that IFFs in the Balkans constitute around 6% of the region's GDP (approximately 8% in Bosnia and Herzegovina, and 7% in Kosovo). This, proportionally, far exceeds the global estimates of illicit outflows. The facts speak for the magnitude of the problem: in 2022, out of 18 United Nations Development Programme projects related to Sustainable Development Goal target 16.4, which deals with IFFs, half were in the Western Balkans (five in Bosnia and Herzegovina and one in Serbia, Kosovo, Montenegro and North Macedonia, respectively) with a budget of nearly US$4 million. And yet, illicit finance in the Western Balkans is severely understudied. The absence of consensus on what constitutes IFFs in the research and policy community, and the dispute of naming them, is a problem magnified in Slavic languages.[16]

FIGURE 3 Illicit financial inflows (top) and outflows (bottom) in the Balkans.

SOURCE: Center for the Study of Democracy calculations based on gross excluding reversals and hot money narrow trade-misinvoicing methods, 2000–2020

Country	Informal economy (% of GDP) in 2022	Corruption Perceptions Index, 2022 Score/Rank
Albania	31.9%	↑ 36/101
Bosnia and Herzegovina	33.0%	↓ 34/110
Bulgaria	27.7%	↑ 43/72
Croatia	29.5%	↑ 50/57
Kosovo		↑ 41/84
Montenegro		↓ 45/65
North Macedonia	33.4%	↑ 40/85
Serbia	31.3%	↓ 36/101

FIGURE 4 Vulnerabilities of Western Balkan countries to illicit financial flows.

SOURCE: Quarterly Informal Economy Survey, December 2022

The strategic geographic position of the Western Balkans, between Asia and Western Europe, enables criminal networks to cross the indistinct divide between legal and illegal markets. The Western Balkan region has traditionally served as a gateway route for drug trafficking, human smuggling and illicit trade. Moreover, recent substantial infrastructure investments – mostly a consequence of China's Belt and Road Initiative – are a powerful catalyst for capital and commercial flows. The porous borders, the interdependent nature of the Western Balkan economies and the large informal sector – exceeding 25% in all countries covered – provide a permissive playing field for the movement of illicit funds. Most of all, the overall governance features of the Balkan countries, plagued by chronic corruption and clientelism, weak rule of law, corrupted and disabled criminal justice institutions, and undue political interference, are the primary driver of IFFs. The issue of illicit finance is particularly prevalent in Bosnia and Herzegovina due to the division of responsibilities between entities, state level and cantons, where responsibilities are intertwined and institutions are exceptionally fragile, and insufficiently staffed and financed to counteract the problem.

IN THE SHADOW OF THE WAR

Beyond the suffering and humanitarian crisis resulting from Russia's war of aggression in Ukraine, the global economy has felt the most significant supply shock since the early 1970s, along with the effects of slower growth and faster inflation.[17] The economies of the Western Balkans face an exceptionally turbulent external environment, placing households, firms and governments under acute stress. The impacts flow through three main channels:

- Higher prices for commodities (e.g. food and energy) push up inflation, in turn eroding the value of incomes and weighing on demand.
- Neighbouring countries, in particular, grapple with disrupted trade, supply chains and remittances, as well as a historic surge in refugee flows.
- Reduced business confidence and higher investor uncertainty drive asset prices down, tightening financing conditions and, potentially, spurring capital outflows and delaying foreign direct investment (FDI). This is especially true for Bulgaria and Romania in the context of the militarization of the Black Sea.

Inflationary pressures burden lower income economies the most, where food commodities (such as grain and corn) and energy account for a larger proportion of consumption. Food inflation, for example, reached as much as 25% in Bosnia and Herzegovina, Montenegro and North Macedonia in 2023.[18] Similarly, rent prices in Serbia have skyrocketed due to the large influx of Russian and Ukrainian citizens, leading to many locals being pressured into either paying excessive rents or having to vacate their apartments. This practice, dubbed by many renters as 'war profiteering' has led to landlords requesting as much as twice the regular rent.[19]

Country	2020	2021	2022
Albania	1.62	2.04	6.24
Bosnia and Herzegovina	-1.05	1.99	10.50
Bulgaria	1.22	2.84	12.40
Croatia	0	2.70	10.70
Kosovo	0.22	3.31	12.00
Montenegro	-0.24	2.40	12.76
North Macedonia	1.20	3.23	10.61
Serbia	1.58	4.09	11.46

FIGURE 5 Changes in average consumer prices (in per cent), 2020–2022.

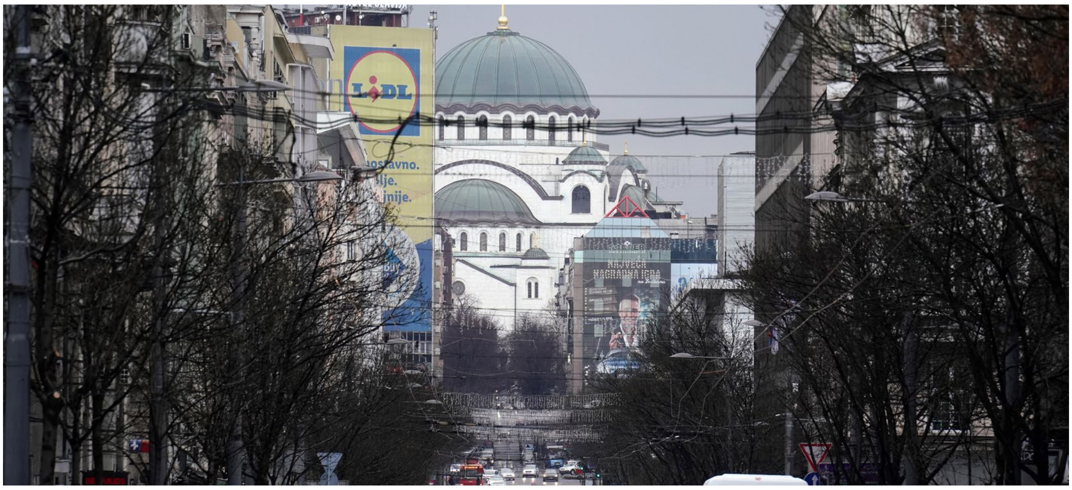
SOURCE: World Economic Outlook database, October 2022

The underground battle: Evading sanctions

Russia's war of aggression in Ukraine has inspired an unprecedented display of solidarity, resolve and resilience from the global democratic community, which has imposed sweeping economic sanctions on the Russian war machine. The 'sanctions revolution' resulted in an unparalleled set of measures targeting key sectors of the Russian economy and political elites. Shortly after the invasion, the G7 countries froze an estimated US$315 billion in reserves held in the Central Bank of the Russian Federation (CBR) jurisdictions.[20] One year after the invasion, the Russian Elites, Proxies and Oligarchs (REPO) Task Force, comprising representatives from the EU, UK, US, Canada, Australia and Japan, successfully blocked or froze more than US$58 billion worth of sanctioned Russians' assets.[21] Nevertheless, some sanctioned Russian elites and their financial networks have found ways to circumvent the restrictions and, in some instances, maintained access to funds. Furthermore, in certain cases, blacklisted individuals and entities may be able to generate additional revenue or procure export-controlled and sanctioned items.[22]

For instance, shortly after the Russian invasion, in April 2022, Ukrainian authorities discovered a shipment of metal from Russia worth 93 million Ukrainian hryvnia (UAH) (around US$2.7 million) in the port of Odesa. Russia tried to bypass the sanctions and secretly transport the shipment through Ukraine to its final destination.[23] Thus, rather than seek new sanctions, the EU wants to crack down on bypassing those already imposed, identifying the UAE, Turkey, Armenia, Georgia, Kazakhstan, Kyrgyzstan and the Balkans as potential circumvention routes.[24] In February 2023, the EU launched an ad hoc group to identify solutions that would enable the use of frozen Russian assets to support Ukraine. The European Commission has also mandated that member states report any CBR assets held by their financial institutions. However, there has been no confiscation of Russian state-owned assets as of June 2023.

The Western Balkans remains one of the most vulnerable soft targets for the Kremlin's ongoing hybrid war against the EU and the democratic West. The combination of state and media capture, simmering ethnic divisions between and within countries, the slow pace of EU accession and the legacy of Russian cognitive bias make the region a gateway for sanctions evasion. For instance, since it is only a potential EU-membership candidate, Bosnia and Herzegovina is not required to align with the EU's Common Foreign and Security Policy (CSFP). The country has not followed the EU's sanctions against Russia since 2014. Furthermore, Bosnia and Herzegovina's alignment with the EU's restrictive measures has significantly declined since 2021.[25] And although Bosnia and Herzegovina has officially supported EU



Serbia, traditionally one of Russia's closest allies in Europe, is trying to put some distance between itself and Moscow as the war in Ukraine strains ties between the two countries. Yet Belgrade is one of the few remaining routes for Russians to travel abroad. *© Oliver Bunic/Bloomberg via Getty Images*

measures in retaliation against Moscow since the full-scale invasion of Ukraine, it has been unable to formulate a coherent foreign policy position and lacks a systematic approach to the implementation of sanctions. Similarly, Serbia, whose record on agreement with the CSFP has been inconsistent, has not aligned with the EU's restrictive measures against Russia since 2014.[26] Even though Serbia has condemned the invasion of Ukraine at the United Nations and other international forums, it has not formally introduced sanctions against Moscow.

Notably, one of the few remaining routes for Russians to travel abroad is via Belgrade. Almost 220 000 Russian citizens have entered Serbia since the start of the conflict – although it is hard to estimate how many have stayed in the country. Serbia and other Western Balkan countries could offer safe haven for capital and assets, given that Russians already feel comfortable doing business there. In recent years, several thousand foreigners have taken advantage of the so-called 'golden' passport schemes that offer citizenship in return for investment in real estate, business or government funds. Numerous investigations reveal that citizens from Russia and Saudi Arabia, including individuals under sanctions and associated with money laundering, fraud and embezzlement, were able to acquire de facto European citizenship.[27]

And, even though North Macedonia and Montenegro have faced harsh criticism from the EU, they continue to offer 'citizenship for investment'. Despite the numerous European Commission warnings and recommendations that Montenegro effectively phase out the investor citizenship scheme as soon as possible, because it poses risks of money laundering and corruption, the Montenegrin government recently hit new records in granting honorary citizenships.[28] Between 31 August and 8 November 2022, the government granted 296 new citizenships (287 were based on the Economic Citizenship Programme; for five, the state interest was not specified in the decisions). The largest number of recipients came from Russia (110), followed by China (67) and the US (24). Elsewhere in the region, in March 2023, and under EU pressure, Albania temporarily shelved its controversial cash-for-passports scheme.[29] However, the Albanian government declared it would not give up on another thorny economic programme – 'fiscal amnesty', under which any Albanian or foreign citizen can deposit up to €2 million in non-declared money into the national banking system, enjoying legal immunity and a tax of only 5–10%. The EU and the International Monetary Fund both denounced an earlier version of this law, which was the subject of tense discussions with the EU and various diplomatic missions in Tirana. International stakeholders' main concern is that the scheme provides criminals with a platform to launder the proceeds of crime, such as drug and human trafficking.

EU member states, such as Bulgaria, must directly apply EU regulations on sanctions, meaning that tax authorities should initiate freezing procedures even when no national regulation stipulates that this be the case (the Bulgarian legal system only provides a procedure to seize assets but not to freeze them). However, Bulgaria has not imposed any sanctions against Russian citizens or companies featured on the EU sanctions list since they were first imposed after the annexation of Crimea in 2014.[30] According to the latest data, nearly 300 000 Russians own over 500 000 properties in Bulgaria and, while the national tax agency acknowledges that it should apply the EU regulations on sanctions, this promise remains on paper. As a matter of fact, Bulgaria received a derogation from the European Commission, allowing it to keep importing crude oil and petroleum products from Russia by sea until the end of 2024.

Typologies of Russian sanctions evasion

The most common ways to bypass the sanctions include:

- **Use of family members and close associates.** The act of transferring assets to family members or close associates, either before or shortly after the designation, may indicate an attempt to evade sanctions on the part of the sanctioned individual and the party that facilitates the transfer.[31] REPO Task Force members pointed out various instances in which Russian oligarchs transferred the beneficial ownership of legal entities and arrangements to their children to ensure continued control and access to wealth after the imposition of sanctions.[32]
- **Use of real estate and business assets to hold value, benefit from wealth.** Historically, Russian oligarchs have commonly invested in properties around the world.[33] Although not the biggest investors in the Western Balkans, Russian and Ukrainian oligarchs have previously deposited their assets in Serbia and Montenegro. Since the invasion of Ukraine in 2022, there has been a surge in the use of real estate as a vehicle to preserve Russian wealth. The Adriatic coast is a playground for the ultra-rich, with, for example, the superyacht of former Chelsea football club owner Roman Abramovich docked at a marina in Montenegro.[34] Sanctioned Russian individuals and entities may launder or attempt to launder and obfuscate illicit proceeds through the purchase of real estate, often hiding behind intermediaries or straw purchases and/or opaque corporate structures. A red flag is the purchase of real property below or above its market value, as well as the use of offshore buyers with potential links to Russia.
- **Use of enablers to leverage expertise and avoid involvement.** Russian individuals and entities who have been sanctioned may look to avoid direct involvement in sanctions evasion by utilizing certain professionals – commonly referred to as enablers – including those who regularly interact with the international financial system. They may leverage their ability to open bank accounts, initiate bank transactions, transfer funds and create corporate structures to support sanctioned individuals both directly and indirectly.
- **Use of complex ownership structures to avoid identification.**
- **Use of third-party jurisdictions and false trade information to facilitate sensitive goods shipments to Russia.**

An unlawful Chinese bank in Italy has allegedly laundered at least €15 billion for drug traffickers, Russian oligarchs and Chinese citizens.[35] The illegal financial institution, referred to as 'China Underground Bank' by the Italian investigators, delivered 'special services' to its clients and routed cash flows through shell companies located in Bulgaria, Hungary and Slovenia, before sending them to banks in China.[36] The bank's clients ranged from tax-evading Chinese workers and members of China's ultra-rich to mafia-linked drug traffickers, north-eastern Italian entrepreneurs and Russian oligarchs hit by sanctions.

Smugglers' paradise

The war in Ukraine has caused the largest disturbance in European security since the end of the Cold War and the most significant disruption of the world order since 1945. In such turbulent times, those engaged in illicit activities are often the first ones to take advantage of the conflict and struggle. There is ample evidence that a massive amount of weaponry is pouring into Ukraine, including from the Western Balkans.[37] Evidence suggests that automatic rifles and mortars made in Serbia are being used on the battlefield. There is a viable risk that some of the weapons flooding into Ukraine eventually end up back in the hands of criminal groups or paramilitaries in the Balkans, or are sold illegally on the black market. Bosnia and Herzegovina, especially the Brcko District – a triangle where the borders of Croatia, Serbia, and Bosnia and Herzegovina meet – stands out as the key transit country for weapons smuggling in Europe.

In 2022, EU and Schengen-associated countries faced unprecedented challenges at their external borders: the people-smuggling networks capitalized on the dire refugee crisis that consumed much of the border authorities' focus and resources, and the influx of undocumented migrants from the Middle East through the Balkan route increased substantially. The irregular border crossings on the Western Balkan route were 136% more than in 2021 – the highest number of crossings reported on this route since 2015.[38]

Cash is still king

The widespread use of cash and the sizeable informal Western Balkan economies facilitate the entry of illicit cash into the licit economies of the region. The cash economy eases IFFs in various ways in different formal sectors and industries. In stark contrast to sensationalized financial transactions portrayed in Hollywood involving cryptocurrencies and convoluted schemes, the reality is much more straightforward. Numerous experts have sounded the alarm that smuggling cash is still the most important channel to move illicit money across borders, whether in concealed car compartments or hidden among legitimate products in transport trucks or in shipping containers. Laundering of smaller amounts of money is often done through cash-intensive businesses, such as restaurants, bars, beauty salons, petrol stations, private parking lots and taxi companies. Throughout the region, illegal funds are mixed with actual gains from running these operations, making the flows indistinguishable from one another and, thereby, conveniently enabling them to enter the banking system.

Yet there is a lack of transparency and clarity when it comes to understanding the volumes of cash entering and leaving the region. A few cases from Bulgaria's Kapitan Andreevo checkpoint, at the border with Turkey, reveal the possible extent of the problem. In March 2023, customs officers at the Kapitan Andreevo checkpoint found undeclared currency worth approximately €1 million (2 204 065 Bulgarian lev – BGN) in three vehicles attempting to cross the border.[39] In another case, on 2 March 2023, during the inspection of a bus travelling from Ukraine to Turkey, a polyethylene bag filled with stacks of US dollars was discovered in a cavity in one of the stairs on the bus.[40] The next day, bundles of Ukrainian banknotes worth approximately €0.5 million at the time (UAH32 461 000) were found in a passenger minibus travelling from Turkey to Moldova through Bulgaria.[41] Before this, on 28 February 2023, a Turkish-registered lorry, travelling to Turkey from the Netherlands via Bulgaria, had been seized with nearly €700 000 in smuggled currency found hidden in the vehicle.[42] In another incident, at the end of January 2023, customs inspectors at the Danube Bridge–Rousse border check-point found over €0.5 million (UAH20 million) in a bus driven by a Turkish citizen. And in late 2022, two Ukrainians were detained at the Lesovo border checkpoint, also located on the border between Bulgaria and Turkey, trying to smuggle gold worth over €0.5 million.[43] The list of cash smuggling cases from the previous year is extensive, but what is more interesting is the trends behind these activities.

Bulgaria's Kapitan Andreevo checkpoint, on the border with Turkey, has been the site of several cash smuggling attempts so far in 2023. *© Nikolay Doychinov/AFP via Getty Images*

It is evident that immediately after the Russo-Ukraine war broke out in 2022, Ukrainian citizens fleeing across borders took cash with them. The problem, rather, was that, in many instances, they were caught transporting large amounts of undeclared cash. A notable case involved the wife of a former Ukrainian MP, who was caught at a border crossing for refugees carrying US$28 million and €1.3 million as she tried to enter Hungary.[44] In another incident, an ex-general of the Security Service of Ukraine, accused of being a Russian collaborator, was detained at the border between Serbia and North Macedonia with €600 000 in cash, a large sum in US dollars, and emeralds and diamonds of an undisclosed value.[45] As of October 2022, this former top official – who had allegedly helped Russian forces seize the Chernobyl nuclear power plant in February – along with his companion, were in the pre-trial detention centre of Niš, charged with money laundering.

Multiple unofficial sources have confirmed the existence and intensified use of covert channels for illegal money transfers into Albania.[46] The primary reason for this modus operandi is the criminal origin of the money, which is predominantly derived from the trafficking, distribution and sale of hard drugs from Latin America and cannabis grown in Albania. A sharp increase has been seen in these illicit activities since 2016. Methods of transfer involve vehicles, often adapted as 'safes', which are used instead of electronic transfers, due to the high cost of transactions through recognized agencies, such as Western Union and MoneyGram. It also allows individuals to evade taxes in their country of origin and take advantage of Albania's high levels of 'informality', weak tax administration and attractive investment opportunities, especially in construction. Anecdotal evidence from informal discussions with former high-ranking officials of the Albanian state police and the anti-money laundering department illustrate that second-hand cars are often purchased cheaply in the UK and equipped with secret safes installed to conceal money. These transporters then travel through Europe to Albania to distribute the funds to recipients, primarily family members of the senders but also criminal partners of Albanian emigrants abroad. After distributing the money, the cars are often dumped into two large lakes in the north-eastern part of the country. This process is then repeated. Notably, the recent public and political debate on fiscal, asset and criminal amnesty seems to have contributed to a rise in the volume of money being transferred through this channel in the last few years.

2021				2022			
Type	Number of cases	Value/quantity	Perpetrators by nationality	Type	Number of cases	Value/quantity	Perpetrators by nationality
Currency	49	12 820 643.29 BGN (€6 538 830.61)	Bulgarian (7), Romanian (2), Moldovan (1), Turkish (32), Polish (3), Chinese (1), Hungarian (1), Iranian (1), Syrian (1)	**Currency**	83	30 723 560.13 BGN (€15 673 993.46)	Bulgarian (9), Georgian (2), Romanian (8), Moldovan (2), Serbian (1), Turkish (56), Ukrainian (4), Uzbek (1)
Gold and gold products	66	82 245.28 grams	Bosnian (1), Bulgarian (21), North Macedonian (2), Russian (1), British (1), Romanian (18), Turkish (21), Unknown (1)	**Gold and gold products**	62	101 400.80 grams	Belgian (3), Bulgarian (7), German (2), French (1), Moldovan (5), Romanian (18), Turkish (21), Ukrainian (2), Serbian (2), Kazakh (1)

FIGURE 6 Cash and valuables seized or confiscated by Bulgarian customs, 2021 and 2022.

Fuel fraud

In Bulgaria, excise and tax fuel frauds appear to have decreased sharply in the last six or seven years. It is believed that this is due to an explicit amendment to the law requiring petrol product traders to provide bank guarantees when purchasing from licenced excise or customs stores. This requirement was adopted in 2016 so as to eliminate the missing-trader schemes taking place with respect to petrol products.[47] However, the increase in excise revenue in 2022 compared to 2021 was a mere 0.2–0.3%, despite the post-COVID-19 pandemic spur in consumption and the effects of escalated inflation. Current fraud schemes involve manipulating the centralized excise system using, for example, the following modus operandi: a warehouse operator issues a legitimate Electronic Excise Declaration (EED) for a specific fuel quantity (tanker truck). However, the operator releases fuel from the warehouse for three or four trucks, which are then transported with the same EED to different end destinations (petrol stations). This fraudulent manoeuvre enables the excise store owner to resell unregistered fuel through the manipulation of legitimate documents. The drivers maintain constant communication with the warehouse owner in the event of any issues arising during transportation If an inspection is encountered, the operator can immediately issue another EED in the centralized electronic register.

There are various other traditional fraudulent practices that can also be observed, such as selling fuel from ships on the Danube River to fishers. In addition, amid the crisis with Ukraine and Viktor Orbán's move to reduce fuel prices, numerous schemes have been organized to purchase fuel in Hungary and sell it in Serbia. There are also customary fraud schemes employing customs tariffs, for instance, declaring less than actual quantities or declaring an oil product with lower customs duties.

In conclusion, despite the steep increase in fuel prices in 2022, no fraud cases were detected of fuel officially exported to Ukraine that was diverted to the Bulgarian market and resold without excise tax or VAT.

VAT fraud

In the case of Bulgaria, thus far, no significant instances of fraud have arisen in connection with the newly implemented VAT exemptions for specific items, such as zero VAT on bread and flour, reduced VAT on printed books and periodicals, as well as on restaurant and fitness services. That said, some of the most common schemes are the so-called 'VAT frauds on triangular operations'. In these instances, goods are shipped directly by the supplier (party A) to the end-client (party C) but invoiced to an intermediary (party B), who then re-invoices for the supply to party C. According to the EU single market legal framework, triangular operations allow for zero VAT invoices for parties A and B. Examples of intermediaries (party B) include companies incorporated in Bulgaria (often owned by foreign citizens). Party B issues zero VAT invoices to parties A and C. Thus, the Bulgarian budget does not incur any losses. However, party C is often non-existent, with goods never leaving the country where party A resides. But party A uses invoices and CMR documents[48] that party B, in Bulgaria, has issued to claim VAT refunds in their own country. Recently, such triangular operations have been undertaken involving luxury vehicles, which, by virtue of their high value, generate significant VAT losses in other EU member states. In December 2022, the European Public Prosecutor's Office (EPPO) uncovered what is believed to be the biggest VAT carousel fraud ever investigated in the EU, responsible for an estimated loss to EU taxpayers of €2.2 billion.[49] Criminal activities were spread throughout the 22 EPPO-participating members, including Bulgaria and Croatia, as well as third countries such as Albania and Serbia.[50] In February 2023, the EPPO exposed another case of massive VAT carousel fraud with estimated losses of €40 million. A complex investigation uncovered a network of companies established in Bulgaria, Poland, Slovakia and the Netherlands, selling computer equipment and electronics to shell companies in Italy, with these companies administered by figureheads so as to avoid paying VAT.[51] According to evidence, the commodities were sold at very competitive prices to Italian and other companies in the EU, thus generating massive tax savings and enormous VAT credits in Italy.

Another VAT fraud scheme is committed by online traders, who exploit the fact that customers cannot verify whether the trader, the supplier who issues the invoice and delivers the goods and the beneficial owner of the receiving bank account, are the same. Taking advantage of this situation, fraudulent online traders, effectively missing traders, issue invoices and accumulate VAT but never transfer it to the appropriate budget.

In general, trade misinvoicing remains the most prominent channel through which IFFs flow in and out of the Western Balkans. This involves creating fake legal transactions when no real business is taking place. Contracts are made fictitiously, and there is a flow of money involved, but no exchange of goods or services. This kind of activity is often used to launder money. For instance, someone can issue an invoice for a service that was never provided, and that invoice could be the basis for a money transfer. This method is primarily used in the second stage of money laundering, referred to as layering.[52]

STEMMING THE TIDE OF IFFS

Europe needs a strategic decoupling of its economy from Russia's. Priority should be given to breaking energy dependence and dismantling Russian oligarchic networks across the continent. In the more vulnerable economies of the Balkan countries, Russia's weaponization of trade must be opposed by pursuing a policy of strategic investment by the EU and the US. Two concurrent policies would produce a tangible result: exposing and targeting the loci of political corruption, and increasing the level of anti-money laundering enforcement against Russian financial flows in the Balkans.

- The first step is to assess the nature and scope of the threat, by identifying the government institutions and decision-making processes that have been affected by institutionalized political corruption (state capture). The EU should establish an evidence-gathering mechanism capable of verifying the existence of capture practices across various economic sectors and regulatory institutions. The initial application of such a mechanism to selected countries in Europe has revealed numerous and varied sources of risk and levels of governance vulnerabilities.[53] Its further regular use across Europe and in South Eastern Europe should involve a broad coalition of civic actors. It is essential to continue the efforts to prevent and fight corruption and organized crime by increasing the track record of final convictions in high-level corruption cases (i.e. by further confiscating criminal assets), and by strengthening the record of investigations, prosecutions and convictions for organized crime and money laundering. The countries in the region need to adopt/enact anti-corruption strategies underpinned by credible and realistic action plans and effective coordination mechanisms. Some of the Western Balkan countries – particularly Bosnia and Herzegovina – also need to implement efficient legislation on conflict of interests, public procurement and whistleblowers' protection, as well as ensuring the methodological functioning and systematic coordination of anti-corruption bodies. Furthermore, the Joint Action Plan on Counter-Terrorism for the Western Balkans should be implemented more rigorously.
- There is a critical need to increase the quantity and quality of data available on the nature and magnitude of IFFs so as to comprehend their key drivers, channels and trends, and initiate a stronger policy response. As a transnational problem, the push to curb IFFs requires coherence within and between national and international normative frameworks and coordinated action within the scope of EU enlargement and the Berlin Process.
- The second step of an effective response to Russian capture is concerted transatlantic action against illicit money and rogue assets in the Balkans through the effective enforcement of the unprecedented sanctions against Russia following the invasion of Ukraine. There is an urgent need

Serbian President Aleksandar Vučić (left) attends a meeting with Emmanuel Macron and Olaf Scholz aside the European Political Community Summit in Moldova, June 2023. Curbing illicit financial flows in the Balkans requires coordinated action with the EU.
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for screening and halting Russian strategic investments in the Balkans linked to Russian state-owned companies and oligarchic networks close to the Kremlin. The sanctioning countries must clarify legal authorities for the seizure of Russian sovereign assets: domestic authorities must identify, freeze, confiscate and manage tainted assets.

- To prevent Russian companies from evading sanctions, the EU should prioritize halting Russian IFFs, including by accelerating the integration of the Balkans into the rollout of the newly designed Anti-Money Laundering Authority (AMLA). The AMLA and its Balkan counterparts should coordinate their actions closely with US FinCEN and the financial intelligence institutions in each EU member state. Under the current status quo, the authorities of the member states serve as the EU's anti-money laundering supervisors, and there is often more than one supervisory authority in each country.
- Stricter measures should be taken to halt indirect Russian investments through EU companies, especially in the green energy sector.
- Not all of the funds that run through IFFs originate from a predicate crime. Capital that has been generated legally, quasi-legally or informally may be transferred through illegitimate channels and held in offshore jurisdictions. Thus, the Balkan countries must allow money laundering to be investigated as a separate crime. Authorities have also been slow to act in areas that have long been vulnerable to illicit finance, such as beneficial ownership transparency, which directly relates to preventing, detecting, prosecuting and sanctioning financial crimes. Enforcement of transparency requirements for beneficial ownership is vital, as is the stricter security vetting of investments by third parties in the Balkans and European companies or operations.
- More attention should be given to the crypto sphere, which comprises a prominent new channel to move money illicitly in and out of the Balkan countries, especially due to the lower-than-average levels of compliance with international standards on risks from virtual assets.
- As a matter of urgency, the Balkan countries must prioritize updating their investment and national security strategies to incorporate a robust FDI screening mechanism as an essential defence against foreign malign influence and an additional safeguard for boosting quality foreign investment. Governments should integrate the private and civil society sectors in the development of this mechanism and ensure adequate transparency of the process.

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