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Organized Crime Infiltration of Legitimate Businesses in Europe: A Pilot Project in Five European Countries

Executive summary of
Project ARIEL



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Final Report of Project ARIEL - Assessing the Risk of the Infiltration of Organized Crime in EU MSs Legitimate Economies: a Pilot Project in 5 EU Countries (HOME/2012/ISEC/FP/C1/4000003801)

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Executive summary

Project ARIEL – Assessing the Risk of the Infiltration of Organised Crime in EU MSs Legitimate Economies: a Pilot Project in 5 EU Countries (www.arielproject.eu) – was carried out with the financial support of the European Commission, DG Home Affairs, within the Prevention of and Fight against Crime (ISEC) Programme. It focused on five EU MS: Italy, the Netherlands, Slovenia, Sweden, and United Kingdom.

This research is an exploratory study on the infiltration of organised crime groups (OCGs) in legal businesses. Infiltration occurs in every case in which a natural person belonging to a criminal organisation or acting on its behalf, or an already infiltrated legal person, invests financial and/or human resources to participate in the decision-making process of a legitimate business.

The main output of the research is a list of risk factors of OCG infiltration in legal businesses, i.e. factors that facilitate or promote infiltration. Risk factors are derived from an unprecedented cross-national comparative analysis of the vulnerabilities of territories and business sectors, criminal groups' *modi operandi*, and the characteristics of infiltrated businesses.

Infiltration risk factors provide inputs for the development of a risk assessment model of OCG infiltration. Its development will assist Law Enforcement Agencies (LEAs) in identifying the factors facilitating and/or promoting infiltration and enhancing the prevention and enforcement of criminal infiltration. This will help protect EU MS legitimate economies from the misuse of legal businesses for illicit purposes.

PART I. Mapping organised crime infiltration in legitimate businesses

This study analyses OCG infiltration in legitimate businesses through 2,380 references to OCG infiltration from a variety of open sources (i.e. academic studies, LEA operations and reports, newspaper articles). It examines the distribution of OCG infiltration and its correlation with socio-economic indicators to identify the main characteristics of the territories and business sectors targeted by OCGs.

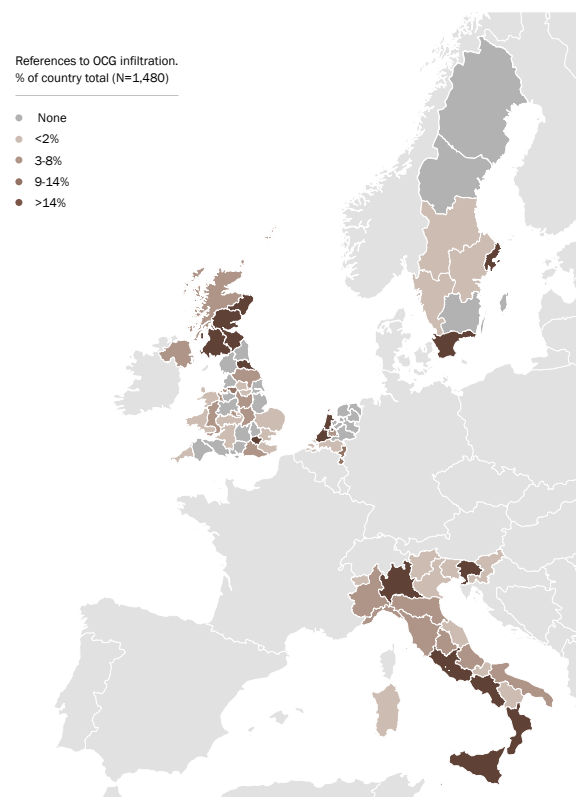
Infiltrated territories

The results show that territories with references to OCG infiltration include (Figure 1):

- Regions with a stable, historical presence of criminal groups (e.g. Southern Italy);
- Border regions (e.g. Western Slovenia) and regions with important ports and airports (e.g. North and South Holland);
- Regions with large urban areas (e.g. Lazio and Lombardy in Italy, the Stockholm and Malmö regions in Sweden, the London area in the UK).

References to OCG infiltration seem to be associated with high levels of shadow economy and corruption, and high levels of infrastructural development. By contrast, low competition levels and low openness to foreign countries do not seem to be associated with references to OCG infiltration in legal businesses.

Figure 1. Number of references to OCG infiltration in open sources by region (NUTS 2). Percentage of the country total¹



Source: Transcrime elaboration on DCI data

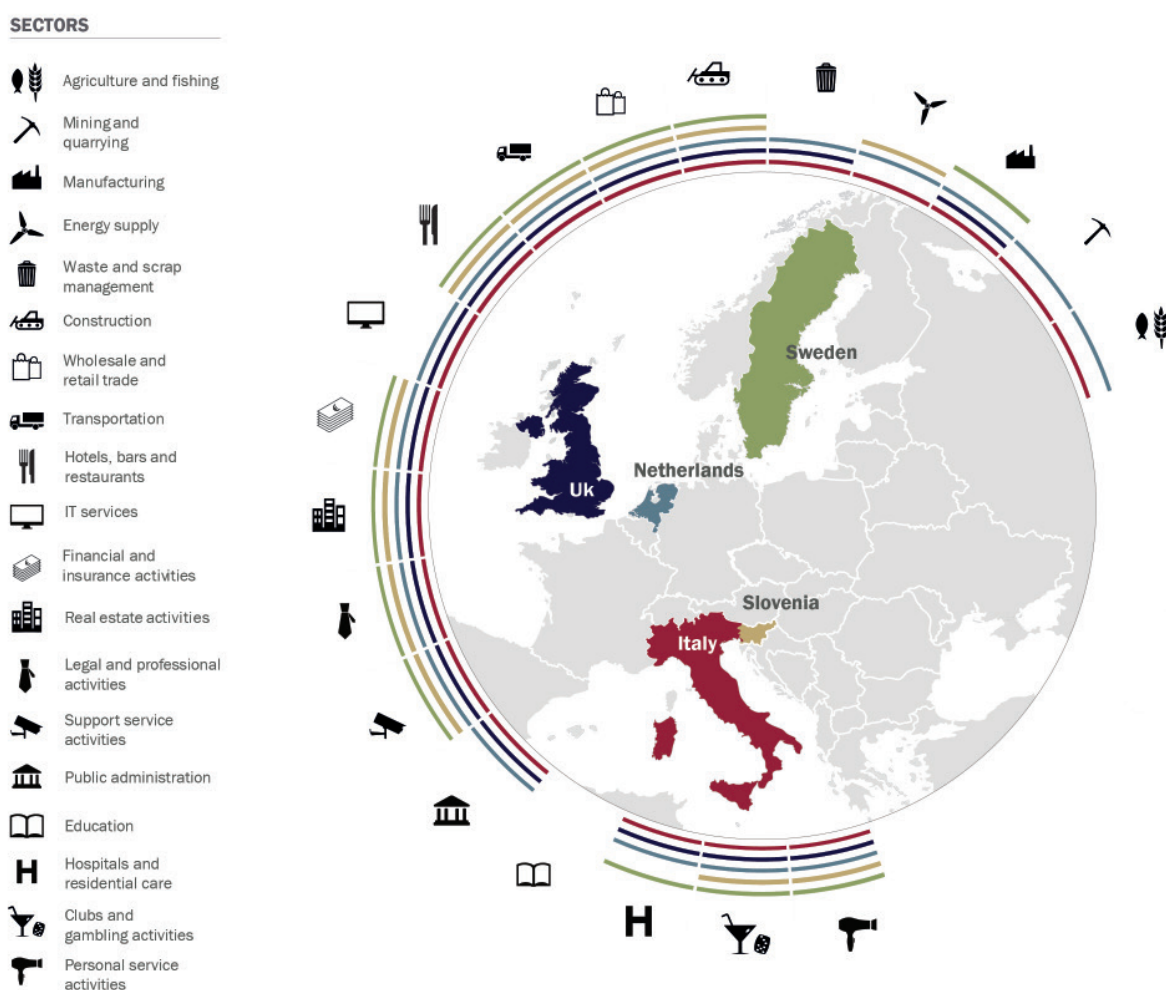
1. Details on the geographic location of the infiltration (NUTS 2) are available for 1,069 references in Italy, 125 references in the Netherlands, 69 references in Slovenia, 49 references in Sweden, and 168 references in the United Kingdom.

Infiltrated business sectors

The results show that business sectors with references to OCG infiltration include (Figure 2):

- Cash-intensive sectors (e.g. bars and restaurants);
- Sectors that are territorially specific (e.g. hotels);
- Labour-intensive sectors characterised by low technology (e.g. construction);
- Sectors functional to illicit activities (e.g. transportation; wholesale and retail trade; financial and insurance activities);
- Sectors characterised by weak or developing regulation (e.g. gambling activities; renewable energy), or inefficient control systems (e.g. construction).

Figure 2. Number of references to OCG infiltration in open sources by country and business sector²



Source: Transcrime elaboration on DCI data

References to OCG infiltration seem to be associated with low levels of openness to foreign investments; low levels of competition and technology; and small

average business entity size. The relationship between references to OCG infiltration and a sector's profitability is weak and negative.

2. Details on the business sector of the infiltration (NACE 0-digit) are available for 1,286 references in Italy, 558 references in the Netherlands, 74 references in Slovenia, 114 references in Sweden, and 248 references in the United Kingdom.

PART II. Assessing the risk of infiltration in legitimate businesses

This study analyses 70 case studies of OCG infiltration and 299 infiltrated businesses. It identifies the main drivers of OCG infiltration of legal businesses, the step-by-step process of infiltration, and the characteristics of infiltrated businesses.

Drivers of OCG infiltration

OCGs infiltrate legitimate businesses to maximise economic and non-economic benefits. In particular, they aim to:

- Launder the profits from criminal activities;
- Obtain considerable earnings and benefit from their profitability;
- Perpetrate frauds (e.g. insurance fraud, VAT and tax fraud, benefit fraud);
- Conceal illicit activities such as drug trafficking and prostitution;
- Achieve other goals such as maximising social consensus and achieving control over a particular sector or territory.

OCGs active in the Netherlands, Sweden, and the United Kingdom mainly infiltrate businesses in order

to perpetrate frauds. Most Slovenian OCGs infiltrate legal businesses to conceal illegal activities, mainly prostitution. In Italy, some OCGs have invested in legal business entities to maximise their social consensus and to control a particular market of the local economy.

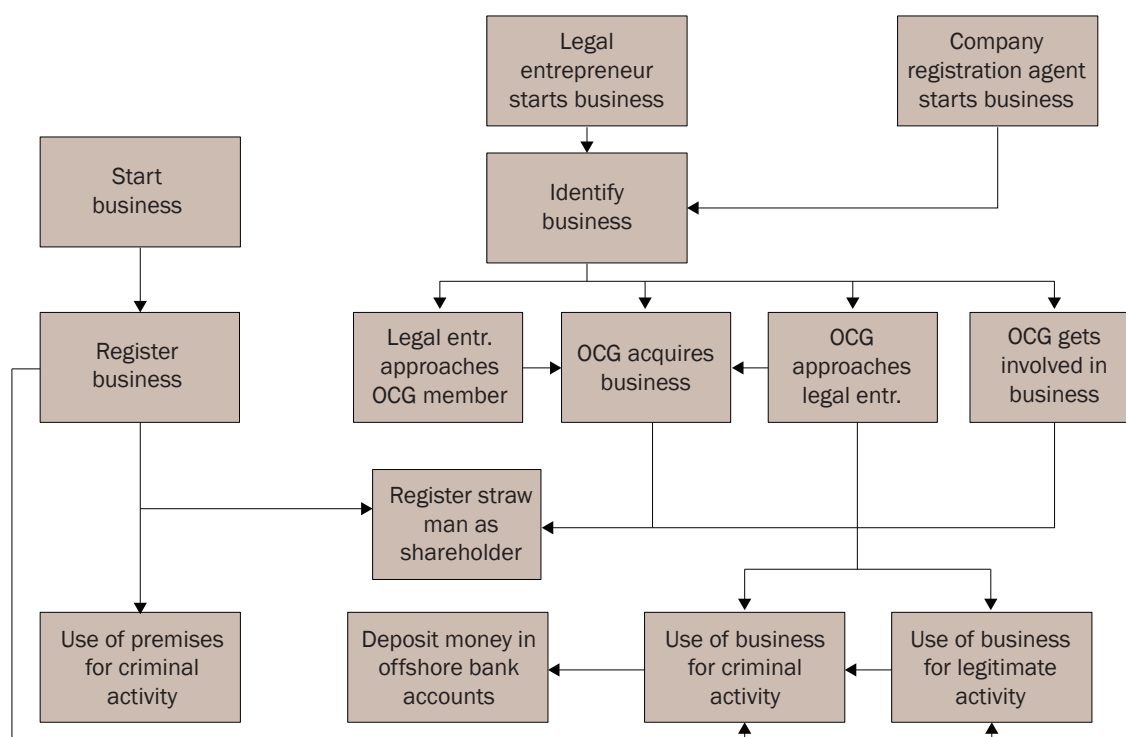
The step-by-step process of infiltration

Infiltrated legal businesses divide between two types: already-existing businesses and new ones. Dutch organised criminals are more prone to infiltrate the former; Slovenian organised criminals favour the start of new businesses. In Italy, Sweden, and the United Kingdom, there is a balance between the two types of infiltrated businesses.

The infiltration process is often straightforward. It involves one member of the criminal group regularly starting a new business or acquiring an already-existing one from a legal entrepreneur. This process can be facilitated by the scant requirements needed to set up a company or the lack of regulation on the process of acquiring a business.

In other cases, the infiltration process requires further steps, e.g. establishment of a partnership with the former shareholder and/or director of the targeted business (Figure 3). The infiltration process occasionally involves OCG members' relatives, professionals, public officials, and politicians who help organised criminals to acquire and manage the legal business.

Figure 3. Crime script of OCG infiltration of legal businesses



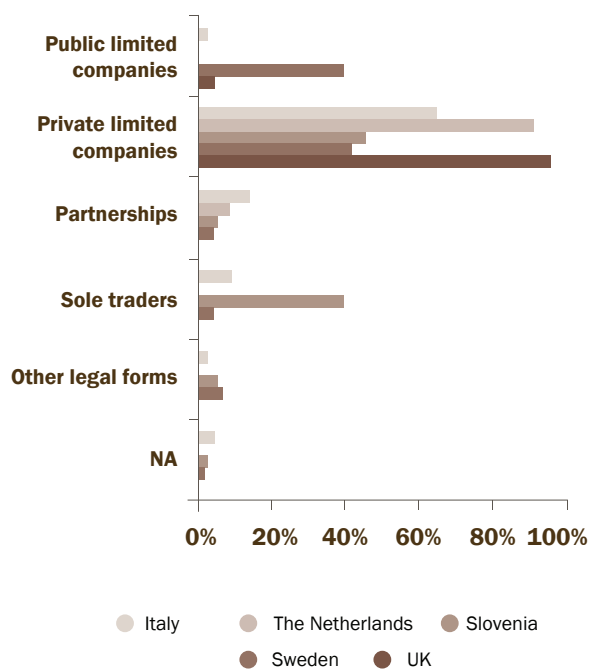
Source: Transcrime elaboration

Control strategies of infiltrated businesses

Control strategies refer to the ownership structure of infiltrated businesses, i.e. how infiltrated businesses are owned and controlled.

Most infiltrated businesses are private limited liability companies (Figure 4). They allow for greater fragmentation of the share capital, thus making it more difficult for law enforcement agencies to identify the beneficial owners of the infiltrated businesses and reducing the potential impact of seizure and confiscation.

Figure 4. Legal forms of infiltrated businesses by country³



Source: Transcrime elaboration on DCS data

Shareholders are divided among the following types:

- OCG members (in more than half of infiltrated businesses);
- Figureheads, i.e. relatives and legal entrepreneurs (especially in Italy), legal (shell) companies (particularly in the Netherlands), and professionals (in a limited number of cases in Italy and Sweden).

Other control strategies include cross-shareholding and large networks of companies; groups of interconnected companies; frequent transformations of registered address, name and shareholders; and the creation of multi-jurisdictional structures.

3. The category 'other legal forms' includes: branches, non-profit organisations, and foreign companies.

Management strategies of infiltrated businesses

Management strategies refer to the financial management of infiltrated businesses, i.e. how infiltrated businesses are financed and if they are able to produce profits.

The analysis of infiltrated businesses' financing sources, use of assets and profitability shows:

- Low levels of financial net debt compared to legal, non-infiltrated companies. This indicates that legal businesses infiltrated by OCGs do not need to resort to banks and other financial institutions for loans to finance their activities;
- High levels of debts to suppliers and other debts. This may indicate the use of fictitious suppliers to conceal the injection of illicit proceeds as trade payables;
- High levels of non-financial current credits (i.e. inventory). High levels of current assets and cash could facilitate organised criminals in liquidating the business in the case of a law enforcement investigation and avoiding the risk of asset confiscation;
 - Low profits compared to non-infiltrated businesses, regardless of the driver of infiltration. Infiltrated businesses often face economic difficulties, either because of their management by the members of the criminal group or because organised criminals target businesses with financial difficulties.

Key inputs for a common risk assessment model

The infiltration process is often difficult to detect. Risk assessment models help monitor the vulnerabilities of the legal economy that may be exploited by criminal organisations, thus anticipating the negative consequences and developing appropriate actions to recognise and prevent them.

Infiltration risk factors are those features of the territory, business sector and legal business that favour infiltration or highlight an already infiltrated business. Four dimensions are identified, each corresponding to specific risk factors: territory, business sector, ownership structure, and economic and financial management (Table 1).

Table 1. Dimensions and risk factors of OCG infiltration

Dimension	Risk factor
Territory	Past evidence of OCG infiltration
	Presence of OCGs
	Large urban areas
	High level of infrastructural equipment
	High level of shadow economy
	High level of corruption
Business sector	Past evidence of OCG infiltration
	Low level of competition
	Low level of openness to foreign investments
	Low level of technology
	Small average company size
	Low barriers to entry
	Weak or developing regulation
Ownership structure of legal business	Limited company
	Characteristics of shareholders (young/old, female shareholders)
	Corporate shareholders
	Complex corporate ownership schemes and cross-shareholding
	Frequent change of company details
	Small company size
Financial management of legal business	Low level of financial debt
	High level of current assets
	Low revenues and profitability

Source: Transcrime elaboration

The risk of infiltration can be identified as a function of the features of the territory, business sector, and ownership structure and financial management of legal businesses. The list of risk factors identified in Project ARIEL – that could be further integrated and updated – is the first step towards the development of a risk assessment model to detect the infiltration of OCGs in European legitimate economies.