



Report on Wilton Park Conference WP869

CURBING MONEY LAUNDERING: INTERNATIONAL CHALLENGES

Monday 10 – Wednesday 12 September 2007

1. Money laundering is a global phenomenon requiring a co-ordinated and co-operative response at global and local levels. International success in combating it depends on the effective implementation to common standards of anti-money laundering controls in jurisdictions around the world.

2. The hiding and use of the proceeds of crime dates back as far as there have been laws to break. The labelling of this activity as money laundering and the growth of an elaborate global system to counter it is a more recent development, going back perhaps no more than 30 years. The initial focus of the international community was on the proceeds of drugs trafficking, but towards the end of the 20th century more attention was paid to capital flight and 'kleptocracy'. Following the events of 11 September 2001 terrorist finance became a major issue around the world.

3. The establishment of the Financial Action Task Force (FATF), with its role of setting international standards, and the involvement of the International Monetary Fund (IMF) and the World Bank (WB) has added impetus and credibility to the fight against money laundering. In particular, the FATF system of mutual evaluation and the listing of non-cooperative countries and territories led to a rapid (in international relations terms) acceptance of the relevant conventions and standards. In turn, these international norms drove national policies. It remains an unanswered question as to how effective this activity has been. Indeed the question may be unanswerable as there has been a dearth of systematic examination of the goals of the system, and some fear that compliance with the standards has become an end in itself, which is no measure of success at all. It can also be argued that no-one

effectively owns or provides strategic leadership on this theme internationally – certainly this is not the role of the FATF.

4. Much is made of a 'risk based' approach to anti-money laundering, which suggests some flexibility in approach, although there is no common definition of the 'risk based' approach. The FATF has produced guidance for financial supervisors and firms, but to some the 'risk based' approach appears at odds with a system of standards and a methodology based on criteria. In addition, there will always be a fear of making judgements in an audit culture, be that at a financial institution level (although many major firms have well developed risk identification and mitigation processes) or at national level implementation of FATF standards. More work is needed on emerging threats, such as the use of the internet and other electronic means to transmit money or gamble illegally, at the international level. This may be a role the FATF could usefully take on, building on its work on typologies. Joining the anti-money laundering international community, as represented by the FATF and FATF Style Regional Bodies (FSRBs), more closely with other international structures dealing with bribery and corruption, such as the United Nations (UN) and the Organisation for Economic Co-operation and Development (OECD), would aid greater harmonisation. Policy goals should be set from a point of view of comprehensive threat assessments, rather than compliance with international standards and fear of critical assessments.

5. It is broadly accepted that the fight against money laundering has several primary and secondary goals. Firstly, it should reduce the underlying predicate crime, with its attendant social harm, which in itself leads to difficulty measuring the relative harms of different types of crime. There appears to be at best a weak basis for saying that there has been much success in reducing crime (by whatever measure). The multitude of other factors involved makes it difficult to assess the influence anti-money laundering systems have had.

6. It should also protect the integrity of the financial system as a whole. The effect that money laundering can have on financial stability is one of the major reasons the IMF is involved in this field. If trust in the financial markets is eroded systematic impacts can result and money laundering can contribute to financial

instability, and other political crises, although it is not normally significant enough to cause them.

7. It has been argued that the obligations imposed by the international standards on the financial sector, such as identifying customers, monitoring account activity and reporting suspicious transactions, brought those institutions into the law enforcement field. The counter argument is that these obligations require them to do no more than be good corporate citizens, protecting the environment in which they work. The more recent extension of these obligations to accountants, lawyers and other so-called gatekeepers, with the further implications for client privilege, has done nothing to quell the concerns of those who fear this is an erosion of privacy with little demonstrable gain.

8. Some commentators argue that even to think of public and private sectors in this context is not useful. The globalisation of the economy and the ease of movement of money or value around the world may even mean the concept of nation states tackling money laundering is not a helpful construct. A real challenge is to engage sufficiently all the stakeholders on a global level. It may not be useful even to speak of a 'fight against money laundering', as this implies there is a chance of winning – it is more realistic to accept that as long as there is crime there will be laundering of the proceeds. The objective should be to define the goals of the systems introduced worldwide and to have some agreed way of measuring success.

9. However, public and private sectors *do* exist and that there are historic barriers to sharing information across the divide. Reporting requirements and the investigative tools provided to law enforcement and other authorities allow information to flow primarily from the commercial to the public sectors. The flow of information the other way is still much more restricted and denies the private institutions the raw data they need to fulfil more successfully their legal obligations. Financial institutions, in particular, have devoted significant resources to systems designed to fulfil their obligations. Closer co-operation with law enforcement can bring improved results in the quality of reporting.

10. Although corrupt or criminally negligent institutions should rightly fear enforcement action against them, those institutions (probably the significant majority) seeking to do the right thing should be encouraged and incentivised, rather than relying on fear or prosecution for their continued support. In Australia, for example, there was a period of 15 months following the introduction of new requirements during which no civil penalties would be brought against reporting entities who could demonstrate they were making reasonable steps towards compliance.

11. There are secondary goals of the global anti-money laundering systems, such as reaching the ill-gotten gains of criminals beyond the reach of conventional law enforcement. Confiscating ill-gotten assets is seen as ensuring justice has been done, provides newsworthy coverage and raises public awareness, or at least perception, of success in the struggle against organised crime. The increasingly comprehensive controls on the use of the financial system, such as identification and monitoring, are also believed by some to increase the costs of doing criminal business, making it harder to move, control and use the proceeds of crime. Hitting the criminal where it hurts, in the pocket, is intended to reduce the attractiveness of crime as a career, although again there is little substantial evidence that this influences the criminal mind.

12. Given the international nature of much money laundering related to serious and organised crime, the sharing of these seized assets is a multi-national issue. Asset sharing of any assets seized should be the culmination of successful co-operative investigations, but often there are either legal or cultural barriers to sharing between jurisdictions. This in turn may dis-incentivise co-operation on the initial investigation. Ways to overcome these difficulties may include multi-national, global operational asset recovery groups; the CARIN¹ (Camden Asset Recovery Interagency Network) network of experts in Europe may represent a start and focus on the development of international standards and techniques in this field.

13. Anti-money laundering systems also have a role to play in the investigation of crime – records kept of transactions and identities can be useful in network analysis. This may particularly be the case in terrorist finance investigations, where the

¹ CARIN is an informal network of contacts in all aspects of tackling the process of crime. It was launched in 1004. Europol holds the permanent secretariat of CARIN

preventative or predictive effect may be quite limited, as the amounts involved in transactions can be small, although the post-incident utility of accurate records can be extremely high.

14. A question frequently asked by politicians, policy makers and the public is how much money is being laundered. On the face of it, this is an entirely reasonable and straightforward question, but the academic research has shown it to be almost unknowable. There is no agreed, credible methodology to measure the scale of the problem. Both those researchers using macro measurements of the scale of the underground economy and using that as a proxy for the demand for money laundering services, and those using a micro approach of measuring offences and estimating the proceeds, come up with figures that are so huge and at such variance as to have questionable value. Nevertheless the scale of laundered assets is clearly very large and demands a response.

15. Interestingly, the reduction of money laundering, per se, should perhaps not be regarded as an important goal of the system. However, it can be seen as a very important factor for individual jurisdictions or sectors (or, indeed, individual firms). Taking a global view, if the amount of proceeds to be laundered remains the same or increases, all that reduction achieves is displacing the problem, possibly to jurisdictions or sectors less able to deal with or monitor it. Of course, this may increase the inconvenience factor for the criminal fraternity. However, without a comprehensive and agreed evaluation of the success *and* burdens of the system on business, the general law-abiding public and Governments, it is difficult for policy makers to be sure their efforts are achieving anything or, even worse, not having a negative overall effect. This remains one of the largest challenges for the international anti-money laundering community.

16. Contributing to this confusion are the subtle differences in the definitions of money laundering in use around the world. Are all crimes considered predicate offences, or just a list of those regarded as serious? Is self-laundering covered or just the acts of a third party? Is there a requirement to have an intent as opposed to simple negligence? Are value thresholds in money laundering offences included?

17. There is considerable debate about extending international standards, originally designed for established economies and well developed financial systems, into developing markets. Small, poor countries appear to be unattractive places to launder money, particularly for international organised crime, so is it either reasonable or productive to expect them to adopt the same standards? In some cases, such as the global attention on money transmission services post-9/11, there can be significant negative impact (for example poor immigrants rely on the availability of cheap and reliable money transmission to support families at home). There is also an argument that tight control in major markets can marginalise and isolate other economies and impact on their development and financial stability. Perhaps one size of international policy does not fit all?

18. On the other hand, representatives of both emerging (or smaller) economies and of international institutions such as the FATF, IMF and WB argue that global standards should be exactly that – worldwide standards. They should be implemented and assessed consistently, with due regard for local legal and institutional constraints. A major step forward was the adoption of a common methodology for the mutual evaluations carried out by these bodies and the increase in transparency of the process, such as the publication of the reports of these evaluations.

19. Low income countries are often struggling with other major issues, for example HIV/AIDS epidemics, famine or conflict. Their economies may be cash based, they will have limited and under-developed financial markets and laws or regulation, and if they have a Financial Intelligence Unit (FIU) at all, it is likely to be under-resourced and have limited functionality. As a result, their anti-money laundering system will be assessed as having limited compliance or effectiveness by the FATF methodology. It would not be uncommon for there to be a low perceived terrorist threat, so the implementation of the FATF 9 Special Recommendations will be a low priority. This begs the question if it is meaningful to carry out full scale assessments of such countries at this stage of their economic development?

20. A useful approach for the international community to consider would be an assessment based around development leading towards full assessment, with

feedback and ratings identifying core recommendations and resource requirements. This could also sensibly inform technical assistance (TA) programmes, which should take account of local circumstances and not seek to impose a standard model. The World Bank seeks to contribute to anti-money laundering reform through TA, with the highest level of reform being in the area of legislation, which works as a foundation for advancement on other reforms. TA programmes should deliver effectiveness rather than mere compliance and should ensure that policies are proportionate to risk through risk assessments, which should also inform resource allocation. As with assessments, which should also provide implementation roadmaps, TA should be coordinated and carried in collaboration by the World Bank, IMF, FATF, FSRBs and other international actors.

21. Middle income countries face different problems, although there are common themes. Such countries may not be regional or 'offshore' financial centres, but they can have significant criminal problems, such as the narcotics trade. This may give rise to corruption issues. Major cases of corruption, when tackled, can lead to significant reform and a move to proper 'Know Your Customer' processes, rather than a 'know your friend' situation. Where there have been limited anti-money laundering systems previously, strategies can be designed to educate consumers perhaps through innovative use of the mass media, such as TV commercials used in Colombia, to introduce preventative measures and controls through law and regulation, and to increase the detection, investigation and prosecution of money laundering offences. As always, these measures should be based on effectiveness, not just compliance with standards.

22. Countries with fast developing economies face their own unique problems. In order to exploit properly the possibilities opening up to them in the global economy, a good FATF-style assessment is an absolute necessity and membership of FATF itself is seen as a very desirable goal. In a short period of time such countries may have to sign and ratify the relevant UN conventions, introduce new legal instruments, possibly in a very different legal framework to established, Western economies, which can cause some problems during assessment.

23. It is even more important in these circumstances that FATF standards take account of history, culture, legal structures and economic environment and concentrate on the effectiveness of the anti-money laundering system, which may face huge challenges in rapidly developing economies with significant inward investment opportunities and requirements. Although the anti-money laundering authorities and FIUs in these countries may be very young, both organisationally and in actual age of their staff, they can have large impacts and deal with major cases. For example International partners must be prepared to share information, develop a relationship of trust and work effectively with these jurisdictions.

24. In the face of all these varied and complicated issues, the international institutions and one FATF must rise to the current challenges and those unforeseen ones. The FATF has established itself as the international standard setter, through developing the 40+9 Recommendations² to address developing threats. Many countries around the world need assistance in implementing the Recommendations, not just those with low capacity or developing economies. There is a need to move away from the idea that non or partial compliance on particular Recommendations is akin to failure rather than highlighting key areas for development. The FATF in its role as assessor, in conjunction with the IMF, WB and FSRBs, will continue to assist all countries that embrace the standards to reach full compliance. The FATF's capacity to analyse money laundering methods and trends has developed and should continue to do so. It will also seek to develop its engagement with the private sector, where much anti-money laundering experience and expertise lies.

25. Increased co-operation and working relationships between FATF and other international partners is vital and should increase. FRSBs have been extremely successful in expanding the anti-money laundering network to more than 180 countries. There has been useful sharing of experience between the FSRBs and FATF, for example in participation in development of a common assessment methodology and provision of assessors. However, they face many practical challenges across regions, such as competing political, financial and legislative priorities, scarce resources, and the loss of experienced public sector staff. It is also

² see www.fatf-gafi.org

important to recognise that the complexity of the assessment methodology creates its own problems, for example uncertainty as to how effectiveness is to be addressed.

26. Equally international financial institutions have their own roles to play relating to development and poverty. The work of the WB and the IMF, in the context of financial stability, should be co-ordinated with FATF/FSRB programme. It can appear sometimes that their roles are over-lapping, although they would argue that the behind the scenes co-ordination of activity mitigates this risk. Simple measures, such as a common internet portal to bring together all the anti-money laundering resources available, could help build trust and transparency, but the underlying and un-resolved issue of strategic leadership and ownership may remain.

27. One clear area of concern is that few countries have embarked upon a national assessment of money laundering risks. This should be a priority for technical assistance and training, which should reflect a growing risk assessment and surveillance role for FATF itself, drawing on work from around the world. This role takes FATF beyond the original concept of a task force with a limited life and mandate to establish international standards. It goes to the heart of the effectiveness issue and brings into question the FATF's rotating presidency structure (which may cause strategic leadership issues), its mandate (recent work on counter proliferation finance may appear to be outside its terms of reference), its accountability to Ministers, and its membership.

28. These issues must continue to be vigorously debated by the international anti-money laundering community, with openness and transparency. Much progress has been made over the past 30 years, but much also remains to be done.

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