

Policy Coherence in Combating Illicit Financial Flows:

PCSD Thematic Module

DRAFT

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1. Introduction

Illicit financial flows and measures to combat them are a complex and multi-dimensional area of international and national economic, development, security and rule of law policy. Illicit financial flows affect (and are affected by) many wider policy objectives, and involve many disparate actors across a variety of governmental and non-governmental policy disciplines. There is therefore a high risk that policies regarding illicit financial flows will be incoherent or badly-coordinated, and that their effectiveness will suffer as a result. Because of its multidisciplinary nature, complex international normative framework and deterministic relationship to equity, growth, sustainable development, security, governance and the rule of law; lack of coherence in the implementation of IFF policy is likely to result in lack of sustainability, unintended consequences, and competing priorities – for example with missed opportunities to be more effective, or unintended negative consequences for other objectives. Because of this risk, illicit financial flows have been identified as a priority area for *Policy Coherence for Sustainable Development*.

This paper is intended to help policymakers across governments, as well as competent authorities, regional networks and in industry, to understand the complex web of policies involved in combating illicit financial flows, and in particular to highlight the issues of coherence that arise and how they can be addressed. It aims to build a coordinated and coherent approach to implementing risk mitigating policies to prevent and deter illicit financial flows encompassing all the relevant government departments and agencies. It aims to set out the connections between policy issues, to enable governments to take a more coherent approach and exploit synergies where they exist. It is not supposed to be a detailed guide to implementing policies in each area: great deal of guidance is already available from the relevant standard setting bodies and advisory groups, including the conventions and standards themselves; guidance and best practises produced by the FATF and by some national authorities, and technical assistance from some international bodies.

There is no need for this module to duplicate the standards or to offer guidance on how to implement the specific measures they contain. Instead, it looks at the big picture - how to put together the whole spectrum of policies to deal with IFFs; including where there are coherence issues to address which arise from the international framework; and the interactions between the policy measures used to combat IFFs, and other policies - both at a national level and across borders. The goal of the module is to give a road-map of all those policy interactions, so that countries can plan for, avoid, and resolve the most significant tradeoffs or policy-conflicts, and can apply these measures in a coherent and effective way.

Some aspects of policy on illicit financial flows are highly technical, but this paper is written for a non-specialist audience, so that it may be used across disciplines. It therefore uses terms in their non-technical sense. Detailed technical analysis and guidance is available from the relevant bodies on most of the specific issues covered in this report. The focus of this report is on policy coherence issues - specifically the interactions of IFFs and measures to combat them with other policy objectives. It does not discuss in detail the main measures used to combat IFFs. More information on these is available from the standard-setting bodies noted below.

This module builds on work from across the OECD - in particular the 2014 report on illicit financial flows from developing countries - and on the work of the different directorates in the OECD which look at illicit financial flows - including the CTP, DCD, FATF, ABC, GOV. It has also benefited from input by the UN Office on Drugs and Crime, the World Bank, and national Focal Points for Policy Coherence.

Outline

The module starts setting out a *definition of illicit financial flows* and why they pose a policy coherence challenge. We take a fairly wide scope: all funds with an illegal origin, destination, or transferred by illegal means. It is common to talk about illicit financial flows as comprising several distinct types of activity - money laundering and terrorist financing, bribery and corruption, tax evasion, and asset recovery and repatriation. . This section also places illicit financial flows in the context of the proposed post-2015 Sustainable Development Goals, which include some goals directly concerned with illicit financial flows, others which deal with closely related policies; and a wider set which relate to the sources and drivers of illicit finance.

- Section 2 looks at the complicated *international normative framework* for dealing with IFFs. This framework is a huge advantage - because illicit financial flows are international in nature, the existence of global rules is essential to combat them, and to prevent states becoming safe-havens for criminals. It also means there are well-understood templates for policy measures, institutions, laws, and practises to fight illicit financial flows, and that developing countries can access technical assistance and sometimes financing to help build that capacity. So the international framework helps a lot with the design and implementation of policy. However, from a coherence perspective, the international framework also brings some difficulties. There can be policy conflicts between the international rules on illicit financial flows and national laws or objectives on another subject - such as company creation and registration. The module then goes through coherence issues in a methodical way:
- Section 3 sets out the “environmental” factors, which can create an *enabling or disabling environment* for illicit financial flows -which include accidents of geography as well as institutional and financial factors.
- Section 4 examines the *policy and institutional context* for measures to combat illicit financial flows - the areas of policy in which anti-IFF measures are embedded, and the institutions or agencies which implement them.
- Section 5 considers *tradeoffs, conflicts, and spillovers* between different policy objectives, and how governments can ensure balanced outcomes. These are specific problems which have arisen when countries seek to combat illicit financial flows, and they include situations where there may be a conflict of laws (such as data protection); where there are negative impacts on other important policy objectives (such as on financial inclusion or the availability of remittance channels); and cases where there is a difficult balance to be struck by policymakers, for example whether more intensive measures to combat IFFs are worth their cost in terms of burdens on business or in terms of diplomatic relations. These are the issues which a coherent approach will need to resolve.
- The final substantive section considers *how to promote coherence* in combating IFFs, e.g. through formal institutional mechanisms such as inter-agency bodies for coordination and discussion of policies within governments or for liaison with the non-government partners. Many problems of coherence in this field occur because the different actors fail to understand each other - e.g. because the different policy communities involved in combating IFFs speak different languages and care about fundamentally different objectives. So as well as organisational mechanisms, this section also looks at how “soft” mechanisms can cultivate organisational cultures and working practices which make inter-agency cooperation and coherent policymaking easier to achieve.
- The last part of the module is a *self-assessment tool* for countries. This is in the form of a structured set of questions that policymakers can use to understand and assess their own situation, and to identify ways they could build a more integrated whole-of-government approach to IFFs.

What are illicit financial flows?

For the purposes of this guidance, illicit financial flows (IFFs) means all cross-border financial transfers which contravene national or international laws. This is a wide category which encompasses several different types of financial transfers, made for different of reasons. It can include:

- Funds with criminal origin, such as the proceeds of crime;
- Funds with a criminal destination, such as bribery, terrorist financing or conflict financing;
- Funds associated with tax evasion;
- Transfers to, by, or for, entities subject to financial sanctions; and
- Transfers which seek to evade anti-money laundering /counter-terrorist financing measures or other legal requirements (such as transparency or capital controls).

This report also discusses “illicit finance”, which refers to funds with a criminal origin or destination, but outside the context of an international transfer (e.g. the domestic proceeds of crime). It can be useful to distinguish the reasons why funds themselves are illicit (e.g. their association with corruption and other proceeds-generating crimes); the methods used to move or launder them, which can include techniques which are legal (e.g. the use of shell companies or companies in secrecy jurisdictions) or illegal (e.g. false invoices); and the laws, mechanisms and policies used by governments to combat them.

A coherent approach to illicit financial flows needs to encompass illicit funds, illicit financial techniques, the deficiencies in the legislative, enforcement and policy framework which allow them to take place, and the measures which can be applied to fight them. This module considers policy coherence regarding the main types of illicit financial flows and the legal and policy instruments used to combat them, including the measures to counter money laundering; terrorist financing; and corruption; and recover stolen assets.

This module aims to help countries design and implement legislation and policies to counter illicit financial flows in a coherent way that reflects inter-sectoral linkages and minimises the unintended consequences to effectiveness. To do this it maps the interactions of illicit financial flows and measures to combat them with each other and with wider policy objectives; identifies the most significant synergies and spillovers; and gives advice on how to facilitate a joined-up, whole-of-government approach to dealing with them.

Why are Illicit Financial Flows a Policy Coherence challenge?

The amount of money lost to developing countries through illicit financial flows is huge - many times the size of ODA - so even a modest improvement in how effectively we combat IFFs will make a significant contribution to sustainable development. This is made very clear in the chart below:

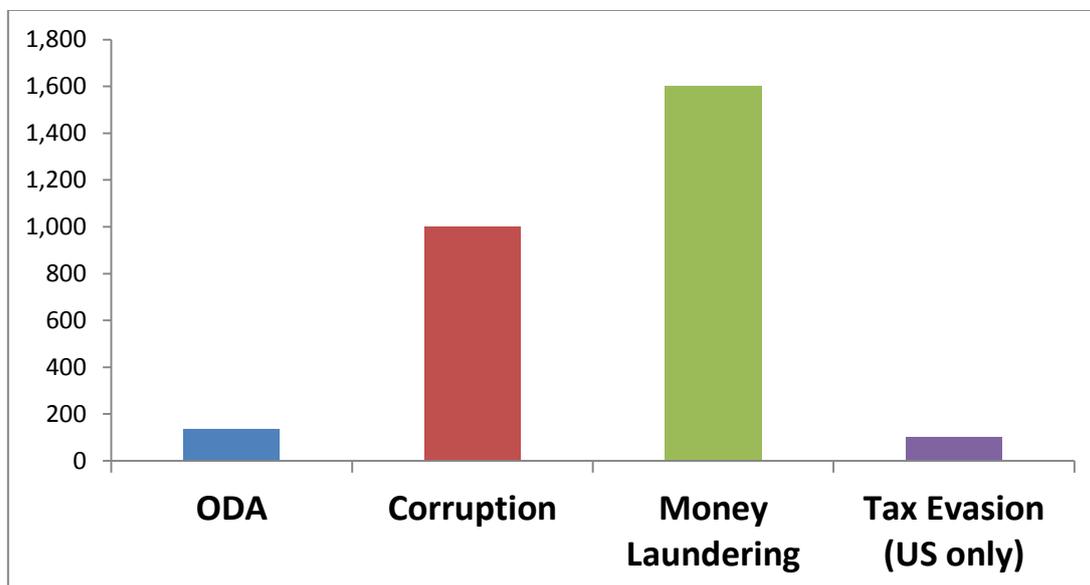


Figure 1: Scale of Illicit Financial Flows and Official Development Assistance

Total ODA provided by DAC members in 2013 was USD 134.4 billion. The estimates cited in this report place global losses from corruption at USD 1,000 billion; and from money laundering (which includes some of the proceeds of corruption) at USD 1,600 billion. Losses from tax evasion in the United States alone - are estimated at USD 100 billion annually, which would imply over USD 500 billion in criminal tax evasion each year globally.

A further demonstration of why illicit financial flows need to be considered in the context of development finance comes from Nigeria. During the rule of Sani Abacha, Nigeria received around USD 1.1 billion in ODA. In the same four-year period, Abacha and his immediate family stole USD 6 billion from the Nigerian state. Illicit financial flows dwarf aid flows.

Illicit financial flows are an area where incoherent and conflicting policies are common, so there is scope for a PCD approach to deliver real improvements. The key reason for this is the complexity of IFFs and of measures to combat them. These involve a number of different and often technical areas of policy, and require a large number of different actors and agencies from inside and outside government to work together effectively.

Illicit financial flows and development

Illicit financial flows can be a fundamental determinant of growth, development, governance, security and rule of law outcomes and, as such, should be considered a significant disabler of sustainable development. They are strongly correlated with other determinants of governments' efforts to effectively use and mobilise their own revenues and resources for sustainable development:

- **Crime¹** – *Proceeds-generating crime*, and particularly *organised crime*, displaces productive economic activity, discourages investment, and draws people into a criminal lifestyle. Organised crime also goes hand-in-hand with corruption and wider governance failures such as a weak or ineffective law enforcement or justice sector, that undermine the rule of law.
- **Corruption²** – Corruption is a key source of illicit financial flows. It is a global problem – but particularly damaging in some developing countries, with pervasive effects. Corruption undermines the effectiveness and legitimacy of governments, compromising their ability to support sustainable development. It broadens income inequality, and reinforces countries vulnerability to crime and terrorism. Corruption also distorts competition and diverts resources away from productive investment - including by discouraging legitimate investment in corrupt countries.
- **Terrorism** – terrorist groups destabilise countries, displace people, and destroy livelihoods. They depend on financing to recruit and support fighters, to purchase equipment, and to create safe havens where they can operate. Terrorist financing is a core component of IFFs.
- **Conflict** - Illicit financial flows also support non-state armed groups in several parts of the world, undermining United Nations' led peacekeeping missions.
- **Weak domestic resource mobilisation** – Tax evasion is a key form of illicit finance, and weakens tax receipts in both developing countries and advanced economies. In some cases, tax evasion also drives authorities to rely principally on forms of taxation such as tariffs, which are harder to avoid but more distorting or damaging to economic development.
- **Poor governance and weak institutions** – Illicit financial flows can be both a cause and a symptom of underlying governance problems. Crime (including terrorism, corruption, and tax evasion) can occur in all countries, but flourish under weak institutions, lack of transparency, and poor accountability..
- **Uncontrolled exploitation of natural resources** – Illicit financial flows enable the exploitation of natural resources – e.g. through illegal and unsustainable mineral extraction, forestry, fishing, or trade in wildlife.
- **Inequality and exploitative elites** - Illicit financial flows include mechanisms which allow wealthy individuals or exploitative elites to engage in tax evasion, use political power for personal gain, conceal their ownership of assets, and pass their wealth to new generations, and thereby frustrate efforts to redistribute wealth and reduce governments' capacity to mobilise resources for inclusive growth. They therefore have a role in sustaining inequality and rent-seeking behaviour, which are key obstacles to achieving the sustainable development goals.

The impact of illicit flows on the ability of countries to use their own revenues and resources for financing sustainable development is enormous:

¹ The term “crime” encompasses a wide range of criminal offences including proceeds-generating crimes such as drug smuggling and organised crime, and economic crimes such as money laundering, tax evasion and corruption. The latter are considered components of IFFs in their own right. The FATF Recommendations list 21 types of crime which should be predicate offences for money laundering.

² For the purposes of this report, the term “corruption” is used in a wide sense, including domestic and foreign bribery, active and passive bribery, misfeasance in public office, and the proceeds of all these activities.

- Losses from corruption are estimated to be more than 1 trillion dollars per year; with corruption adding up to 25% to the cost of government contracts in developing countries³.
- Estimates of global losses from tax evasion vary widely, but all are large. The US Senate estimates revenue losses from tax evasion by U.S.-based firms and individuals at around 100 billion dollars a year, while a World Bank study estimates losses through tax evasion at 8-12% of GDP in Malawi, and 9% of GDP in Namibia⁴.
- The estimated amount of money laundered globally in 2009 was \$1.6 trillion, or 2.7 per cent of global GDP⁵.

These figures are significantly larger than ODA, which in 2013 totalled \$134.4bn from DAC members. Combating illicit financial flows could potentially contribute more resources to support sustainable development than a doubling of global ODA, and would also bring improved governance and stability, and help to reduce crime and violence.

Illicit financial flows are not only a problem for developing countries. All of the factors above also affect OECD member countries to some extent, with increasing focus recently on the role of tax evasion in undermining tax revenues. Countering illicit financial flows is a particularly important tool in the fight against terrorism, and against serious transnational organised crimes such as human trafficking or drug trafficking.

BOX - Tax Inspectors without Borders initiative

The TIWB initiative was launched in a pilot phase in mid-2013, aiming to build capacity to tackle complex tax audits in developing country tax administrations. TIWB facilitates the deployments of experienced tax auditors to work alongside local tax audit teams on a demand-led basis, to transfer tax audit knowledge and skills through a real-time, practical approach. This leads to improvements in the quality and consistency of audits and the transfer of knowledge to recipient administrations (tax administrations seeking assistance), as well as the potential for more revenues, greater certainty for taxpayers and encouraging a culture of compliance through more effective enforcement. A TIWB Toolkit is now available to guide all parties through the expert deployment process.

³ World Bank, Myths and Realities of Governance and Corruption, Daniel Kaufman (2005). Analysis is set out on page 96 of [this chapter](#). Cost of contracts is from the Partnering Against Corruption Initiative.

⁴ http://siteresources.worldbank.org/EXTFINANCIALSECTOR/Resources/Ill_gotten_money_and_economy.pdf

⁵ UNODC estimate, from http://www.unodc.org/unodc/en/frontpage/2011/October/illicit-money_-how-much-is-out-there.html

Illicit Financial Flows in the Post-2015 Sustainable Development Goals

Reflecting their significance as a potential disabler of development efforts, the framework of Sustainable Development Goals includes IFFs as an element of Target 16.4: “by 2030 significantly reduce illicit financial and arms flows, strengthen recovery and return of stolen assets, and combat all forms of organised crime”. For the purposes of this paper, it is important to highlight how the target on illicit financial flows is interrelated to other goals and targets within the SDG framework. IFFs appear directly in only one target, related to Goal 16 (on peace and justice), but they are connected with many other targets which are central to the sustainable development agenda. The following table sets out the main interactions with the other policy objectives in the SDGs:

SDG Targets related to Illicit Financial Flows (16.4)		
SDG	Summary of Target	Relevance to IFFs
Enablers and Disablers		
Factors which make an essential contribution to combating illicit financial flows, e.g. as a precondition for certain measures, or as structural factors which could undermine the effectiveness of anti-IFF measures.		
10.5	Regulation of Financial markets	Some measures to counter IFFs rely on requiring preventive measures by financial institutions, supported by supervision.
16.3	Rule of Law	An essential precondition for anti-IFF measures
16.5	<i>Reduce corruption</i>	Corruption of key institutions can undermine anti-IFF measures
16.6	Sound institutions	An essential precondition for anti-IFF measures
16.9	Identity documentation	Required for many anti-IFF preventive measures
16.10	<i>Public access to information</i>	Transparency to relevant government authorities can discourage crime and enhance anti-IFF measures
16.a	Institutions to combat crime	An essential precondition for anti-IFF measures
Potential Trade-offs and Policy Conflicts		
Areas where there is a risk that excessively strict, or poorly targeted anti-IFF measures could undermine implementation of other SDG targets.		
8.3	<i>SME development</i>	Longer company registration process, with additional information requirements.
8.10	Access to financial services	Financial inclusion issues – e.g. with poor people who lack good identity documentation
10.c	Cheaper remittances	De-risking means money remitters lack access to financial system... potential to drive remitters underground (with cost to recipients). Also cost of compliance may make remittances more expensive...
16.10	<i>Public access to information</i>	Data protection rules, business secrecy, and censorship may conflict with measures to counter IFFs.
Key Sources of Illicit Funds		
SDG targets which relate to significant sources of IFFs. Laundering of illicit flows is an essential enabler for many of these activities, so restricting illicit flows is an effective way to combat the underlying activity.		
2.3	Agricultural productivity/incomes	Drug production is a major source of illicit funds. Measures promoting agricultural productivity and rural incomes can reduce pressure on farmers to grow narcotics.
16.5	<i>Reduce corruption</i>	Corruption is a major source of illicit funds.
17.1	Strengthen domestic resource mobilisation	Tax evasion is a major source of illicit funds, which weakens the capacity of countries to fund their own development through domestic resource mobilisation.
3.a	Tobacco control	Illicit trade in tobacco products generates illicit funds
5.2	Violence against women	Human trafficking generates illicit funds
10.5	Regulation of Financial markets	Poorly-supervised financial institutions are important facilitators of tax evasion and other sources of illicit funds
10.7	Safe migration	Smuggling migrants generates illicit funds
12.7	Public Procurement	Public procurement, public works and construction, are at high risk of corruption, and major sources of funds
12, 14, 15	Sustainable use of oceans and terrestrial ecosystems	Exploitation of natural resources is a driver of corruption and source of illicit funds. This includes forestry and fisheries, as well as extractive industries.

2. Global Framework to combat illicit financial flows

Overview of the international framework

Illicit financial flows are international – criminals exploit differences between national legal systems and weak international cooperation in order to hide funds from authorities. Therefore, a broad set of international conventions, standards, and bodies has been developed in order to combat illicit financial flows. These include UN conventions which establish standards that all countries are expected to meet in order to avoid providing a safe haven for various kinds of illicit financial flows. They also include treaties or organisations with narrower membership, but which set out more intensive or detailed measures to be applied by their member countries, and conduct peer reviews to ensure adequate compliance.

The international framework includes several different layers:

- Universal Legal Obligations, set through the UN Framework, including the Vienna Convention; the Palermo Convention; the Merida Convention; the Terrorist Financing Convention; and various UN Security Council Resolutions;
- International standards, developed in the OECD, including (on tax matters) - the OECD Model Tax Convention; the Convention on Mutual Administrative Assistance in Tax Matters; and the Global Forum on Transparency and Exchange of Information for Tax Purposes. These also include the OECD Anti-Bribery Convention and the Financial Action Task Force recommendations.
- Voluntary and Regional Codes, Standards, Initiatives and Bodies which apply to illicit financial flows.

At UN level, the key instruments which establish legal obligations are:

- *United Nations Convention against Illicit Traffic in Narcotic Drugs and Psychotropic Substances 1988* (Vienna Convention). This includes provisions on money laundering and international cooperation.
- *United Nations Convention against Transnational Organized Crime 2000* (Palermo Convention) . This requires countries to criminalise money laundering, and includes frameworks for extradition, mutual legal assistance and law enforcement cooperation.
- *International Convention for the Suppression of the Financing of Terrorism 1999* – requires states to criminalise the financing of terrorism, and adopt powers to freeze and seize funds intended to be used for terrorist activities.
- *United Nations Convention against Corruption 2003* (Merida Convention) – requires measures to prevent and criminalise corruption, provide international cooperation and asset recovery on corruption cases.
- In addition a number of *UN Security Council Resolutions* have introduced measures to counter illicit financial flows, in particular by establishing targeted financial sanctions regimes applied to Al Qaida and other terrorist groups⁶.

The OECD sets (or hosts) the main international standards and standard-setting bodies which are responsible for setting international soft law:

- *OECD Model Tax Convention* - The OECD published its first draft *Double Taxation Convention on Income and Capital* in 1963, building on work which had begun in the League of Nations in the 1920s. Today more than 3 000 bilateral tax treaties are based on the OECD

⁶ In particular UN Security Council Resolution 1267 (1999) and its successor resolutions.

Model, which addresses key issues arising in the international tax system including to promote the elimination of double taxation and to prevent fiscal evasion.

- *Multilateral Convention on Mutual Administrative Assistance in Tax Matters* - The multilateral Convention was developed by the OECD and Council of Europe in 1988 as a legal instrument for countries to undertake cross-border cooperation to counter tax evasion and avoidance in areas including exchange of tax information (on request, automatic and spontaneous) as well as assistance in tax collection and simultaneous tax examinations. The multilateral Convention was updated in 2010 with an amending Protocol to reflect the latest standards, including in the area of tax information exchange, and to allow the Convention to be signed by all States (not only OECD or Council of Europe members). Today (March 2015) there are 85 jurisdictions participating in the Convention, and that number is growing rapidly.
- *OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions* (the OECD Anti Bribery Convention / ABC) – Countries which join the OECD ABC⁷ agree to establish a criminal offence of bribing a foreign public official in their national laws, and to implement effective policies to prevent, detect, investigate and sanction foreign bribery committed by individuals and/or companies. .
- *Global Forum on Transparency and Exchange of Information for Tax Purposes* – The Global Forum is the multilateral framework through which the international standards on tax transparency and exchange of information are monitored and reviewed.
- *The Financial Action Task Force* – The Financial Action Task Force (FATF) is an independent inter-governmental body that develops and promotes policies to protect the global financial system against money laundering, terrorist financing and the financing of proliferation of weapons of mass destruction. The FATF Recommendations⁸ are recognised as the global anti-money laundering (AML) and counter-terrorist financing (CFT) standard.

In addition to the conventions and standards above, there are a range of initiatives and dialogues which aim to improve the capacity of governments and the functioning of the international systems for combating illicit financial flows, many of them led by the OECD. These include:

- *Regional Anti-Corruption Initiatives*⁹, reaching out to non-OECD countries on bribery and corruption issues.
- *CleanGovBiz* – This initiative supports governments, business and civil society to build integrity and fight corruption. It draws together existing anti-corruption tools in its

⁷ The Parties to the OECD ABC are currently: the 34 OECD member countries and seven non-member countries - Argentina, Brazil, Bulgaria, Colombia, Latvia, Russia, and South Africa.

The Working Group on Bribery monitors the enforcement of the Convention and related instruments including:

- the 2009 *OECD Recommendation for Further Combating Bribery of Foreign Public Officials in International Business Transactions and other related instruments*;
- the 2009 *Recommendation on Tax Measures for Further Combating Bribery of Foreign Public Officials in International Business Transactions*;
- the *OECD Recommendation on Bribery and Officially Supported Export Credits*;
- the 1996 *Recommendation on Anti-Corruption Proposals for Bilateral Aid Procurement*; and
- the *OECD Guidelines for Multinational Enterprises*

⁸ International Standards on Combating Money Laundering and the Financing of Terrorism and Proliferation; the FATF Recommendations, FATF 2012.

⁹ These include:

- the Joint ADB/OECD Anti-Corruption Initiative for Asia and the Pacific,
- the joint AfDB/OECD Initiative to Support Business Integrity and Anti-Bribery Efforts in Africa;
- The Anti-Corruption Network for Eastern Europe and Central Asia (in partnership with the Basel Institute on Governance; the Asset Recovery Center, the UNODC and the GRECO); and
- the [Latin America](#) Anti-Corruption Programme (jointly led with the Organisation of American States (OAS) and the Inter-American Development Bank.

CleanGovBiz Toolkit, reinforces their implementation, improves co-ordination among relevant players and monitors progress towards integrity..

- *The OECD Recommendation on Public Procurement* (and corresponding Toolkit) include guidelines for enhancing integrity and transparency in public procurement, which is vulnerable to corruption (including mis-invoicing) and/or bribery (whether from domestic or foreign sources).
- *The OECD Principles on Transparency and Integrity in Lobbying*, as well as the *OECD Recommendations for Managing Conflict of Interest* and *Improving Ethical Conduct in the Public Service* all address the risk factors for potential policy capture and undue influence resulting from political contributions/donations, conflict-of-interest situations including those arising from previous employments (“revolving doors”) which can hinder government’s ability to effectively combat IFFs.
- *OECD Guidelines for Multinational Enterprises* encourage the positive contribution MNEs can make to economic and social progress, including chapters on human rights, combating bribery and taxation.
- *OECD Due Diligence Guidance for Responsible Supply Chains of Minerals from Conflict-Affected and High-Risk Areas*, which provides detailed recommendations to help companies respect human rights and avoid contributing to conflict through their mineral purchasing decisions and practices. The Due Diligence Guidance is for use by any company potentially sourcing minerals or metals from conflict-affected and high-risk areas. It is one of the only international frameworks available to help companies meet their due diligence reporting requirements.
- *Oslo Dialogue on Tax and Crime* - Promoting a whole of government approach to fighting tax crime and other financial crimes, this initiative was launched in 2011 and has included the establishment in 2014 of the *OECD International Academy for Tax Crime Investigation* near Rome, Italy.
- *The Trust and Business (TNB) Project* is a multidisciplinary and multi-stakeholder initiative that aims to bridge the gap between business standards and their implementation, in order to promote business integrity.¹⁰
- *Stolen Asset Recovery Initiative (StAR)* - is a partnership between the World Bank Group and the United Nations Office on Drugs and Crime (UNODC) that works with developing countries and financial centres to prevent the laundering of the proceeds of corruption and to facilitate more systematic and timely return of stolen assets. The StAR Initiative has jointly published with the OECD Working Group on Bribery an analysis on the *Identification and Quantification of the Proceeds of Bribery*.¹¹
- *Tax and Development* - The OECD’s Task Force on Tax and Development was created in 2010 and has an advisory role to the OECD’s Committee on Fiscal Affairs and the Development Assistance Committee. Participants are officials from OECD and developing countries, business, NGOs and other international organisations. Key elements of the Tax and Development Programme’s work agenda include: promoting the link between State building, Taxation and Aid; supporting developing countries build capacity on transfer pricing and other international tax issues as well as natural resource taxation; and supporting low-income countries improve transparency and governance of tax incentive regimes.
- *Extractive Industries Transparency Initiative (EITI)* – a global standard to promote openness and accountable management of natural resources, through full disclosure of taxes and other payments made by oil, gas, and mining companies.

¹⁰ Information available here: www.oecd.org/corruption/trust-business.htm

¹¹ Analysis available here: [The OECD-StAR analysis on the Identification and Quantification of the Proceeds of Bribery](#)

- *Egmont Group of Financial Intelligence Units* - which promotes good practice among FIUs, and facilitates international exchange of information on IFFs;
- *International Corruption Hunters Alliance (ICHA)* – Hosted by the World Bank Group, ICHA brings together heads and senior officials of corruption investigating bodies and prosecuting authorities, anti-corruption experts, academics, and representatives of international organizations from over 130 countries.
- *G20* - which has taken a leadership role on several aspects of IFF policy, including through the *G20 Principles on Beneficial Ownership*.

Some of the conventions and mechanisms above include assessment of compliance and effective implementation by countries. For some this is based on self-assessment by the countries themselves, supplemented by more detailed peer review processes in some cases. Other bodies have mandatory peer review processes for all members of the relevant body – particularly for the UNCAC, the OECD Anti-Bribery Convention, the Global Forum on Transparency and Exchange of Information for Tax Purposes, and the FATF.

The OECD, the UN, the IFIs, and other bodies are also active in producing guidance and analysis to support implementation of the standards and of other measures to counter IFFs. This includes best practices and technical guidance in the implementation of specific requirements, guidance on tools or methods to improve effectiveness in certain policy areas, and studies analysing specific problems which arise in relation to the standards (some of which are noted below).

Is the international system to address IFFs coherent?

The international normative framework for combating illicit financial flows is based on the independent conventions, standards, and initiatives above, but has developed organically. Each standard was developed to address a specific and distinct element of IFF, and they were not planned as an integrated system. This means there may be some gaps and overlaps between the various elements. How can the international community maximise policy coherence within the framework as a whole to improve SDG outcomes

On the specific requirements of the conventions, standards, and initiatives, there is a high degree of consistency. In general, the UN Conventions set out essential and universal requirements, while the other, later standards incorporate the requirements of the Conventions, but also include more detailed requirements for specific related areas. One example is international cooperation: Most of the UN Conventions, and several standards, include requirements for mutual legal assistance between countries regarding their specific focus. The level and type of cooperation, as well as the specific measures required, has increased over time, as countries' capacity and experience have grown, meaning that the more recent conventions and standards incorporate and extend the requirements of previous conventions.

Each of the conventions, standards, and initiatives has been developed with regard to the existing framework, with a view to avoiding conflicting requirements and priorities, unintended consequences, reducing the costs of duplicate requirements, and integrating the framework more effectively. Recent examples include:

- The FATF's decision in their 2012 revision of the FATF standards to require countries to make tax crimes a predicate offence for money laundering (thereby bringing them within the scope of the FATF's requirements on international cooperation and asset confiscation);
- The Global Forum on Transparency's decision in 2014 to adopt in its Terms of Reference for reviews on compliance with the international standard for exchange of information on request, the FATF concept of beneficial ownership.
- The UNCAC uses the definition of the offence of bribing a foreign public official (Article 16), which was first introduced under the OECD Anti-Bribery Convention (Article 1).

- The OECD Anti-Bribery Convention provides a mechanism whereby when more than one country Party to the Convention has jurisdiction over an alleged offence of foreign bribery, the countries involved must consult with a view to determine the country which is the best placed to prosecute the offence (Article 4.3).

The coherence of the global framework is also helped by the increasing focus on three core bodies on IFFs: the OECD Working Group on Bribery; the Global Forum on Transparency; and the FATF. These bodies have come to take a leading role in preventing and mitigating the risk of IFFs. Their role, driven by the scope and content of their requirements (some of which incorporate requirements from the UN conventions), and by their in-depth peer-review processes, which exert pressure on countries to make serious efforts to implement their standards. Nevertheless, some coherence challenges remain on specific issues, as set out below.

The membership of the different global frameworks varies, as they have developed separately, over several decades. Each of the conventions, standards, and initiatives has different governance and membership arrangements, with UN and OECD bodies, as well as stand-alone treaty-based organisations, task-forces, and initiatives. Many standards are open to all countries and have wide membership: over 180 countries are members of the FATF and its network of FATF-style regional bodies; the Global Forum now has 126 members on an equal footing; and the OECD Anti-Bribery convention has 41 state parties (and additional countries which participate through regional initiatives).

The differences in membership lead to some duplication of requirements between standards, since none of the standards can rely on all their members already being party to another standard (and so already implementing a given obligation). Nevertheless, the standard-setters do avoid duplication where possible, such as by recognising the conclusions of each other's peer-review evaluations on issues which are common to two standards.

The separate governance arrangements for each body may present a challenge: there is no central coordination body or mechanism mandated to set a global strategy on illicit financial flows. This is mitigated in part by informal groups: the G20 countries make up a common core membership of all the bodies noted above, and since the 2008 financial crisis, the G20 has taken on a more decisive role in relation to related policies. Recently it has taken on a greater leadership role with regard to IFFs, through action to improve transparency of beneficial ownership, and other specific measures to combat illicit financial flows, giving a high-level political steer on the further development of the relevant standards.

Overall, there do not seem to be major points of conflict within the international standards, and there seems to be effective coordination between the different bodies involved on cross-cutting issues such as beneficial ownership. Seeking greater coherence between the international standards could be disruptive and difficult to achieve, because of the mandate and membership issues. It would also risk losing the focus and nuances which makes each of the standards effective.

Tensions between national and international systems

The scope and detail of the system of global standards relevant to IFFs places significant constraints on the scope countries have to make independent policy decisions. Countries can in principle choose not to become party to the conventions, standards, and initiatives. However the costs of doing so could be high: non-participation could lead to a lack of reciprocal international cooperation (and potentially to blacklisting); loss of access to international financial markets or IFI facilities; and even sanctions or countermeasures¹².

Countries which do participate in the global framework to combat illicit financial flows have significant constraints on their discretion: each standard or convention requires countries to implement a set of policies which constitute the minimum requirements of the standard. Some

¹² e.g. through the FATF's International Cooperation Review Group (ICRG) process.

standard-setting bodies evaluate compliance, implementation and effectiveness, through peer review processes to check whether the standards are adequately applied.

A certain level of capacity is needed both to comply with standards and to evaluate implementation – this can be cumbersome and expensive, especially for low capacity countries.

The mandatory requirements set by international standards are demanding, as highlighted in the 2014 OECD study *Illicit Financial Flows from Developing Countries: Measuring the OECD Response*. This reviewed the results of peer reviews assessing OECD countries implementation of key standards and initiatives: the FATF 40 Recommendations; the Anti-Bribery Convention; the Global Forum on Transparency; the UN Convention Against Corruption, and the Stolen Asset Recovery Initiative. The results presented a mixed picture of global compliance:

- *Combating Money Laundering*: the report highlighted significant variations in country performance, and significant gaps to be filled. The three areas where countries have faced the biggest difficulties in complying with the 2003 FATF standards were: (i) implementation of customer due diligence procedures; (ii) compliance with beneficial ownership requirements; and (iii) effective regulation, supervision, and sanctions.
- *Tax evasion*: the report noted that OECD countries are generally compliant on standards for the effective exchange of tax information, but that developing countries need to continue to expand their network of agreements, and strengthen their institutions. It noted that a whole-of-government approach to fighting tax crimes and illicit financial flows could strengthen their ability to detect and pursue such crimes.
- *International Bribery*: Progress in implementing the OECD Anti-Bribery Convention has been mixed among OECD member countries. On the positive side, 221 individuals and 90 companies had been sanctioned in criminal proceedings by the end of 2012, good practices had been identified in several OECD countries. On the other hand, more than half of OECD countries still had no prosecutions, and common concerns remain, such as loopholes in the legal framework, poor awareness, and lack of resources.
- *Freezing, recovering, and repatriating stolen assets*: Progress has been modest in this area. In 2006-9, USD 276 million in stolen assets were returned to developing countries, and USD147 million between 2010 and June 2012. However, the overwhelming majority of these came from just four OECD countries. The report found that OECD countries could do more: to signal that asset recovery is a political priority, to dedicate more resources to it; and to adopt legal best practices.

The performance of OECD countries is a clear indication that implementing international standards against IFFs is demanding, and significant further steps remain to be taken in most OECD countries.

Many of the policies that countries are required to implement are already determined by the relevant standards: countries face strong peer pressure to implement the core requirements of the global framework, and on some central policy choices (e.g. whether to criminalise the financing of terrorism or to require financial institutions to report suspicious transactions), the standards do not leave countries any discretion. In those areas, policy coherence has to be considered at the level of the international standards, not of national implementation.

The international community has made progress over the last decade in improving the way in which it assesses implementation, by looking at this in terms of risk and effectiveness. Both of these approaches take a more meaningful view of implementation - placing more weight on how a country has practically addressed the IFF risks which it faces, and less emphasis on measures which may not be relevant, or on formal requirements which are not observed in practice. This has also built some much-needed flexibility into the assessments to account for different levels of resource and capacity. The risk-based approach adopted by the FATF, in which countries are required to assess their risks and to apply proportionate measures to mitigate them – including enhanced or simplified measures and exemptions from the requirements - is an example of this approach.

There is also a wide policy space between the mandatory, universal global standards and their implementation in the unique context of a each country. No global standard can specify in detail how every country should implement each requirement, and individual countries must adapt the requirements into a form that is compatible with their legal and administrative systems and policy objectives. This means there is also a pressing need to consider policy coherence at national level – and also to consider coherence in the context of *implementation* as well as of policy.

3. Enablers and disablers of illicit financial flows

Many factors influence the risks that a country faces from illicit financial flows. The threats and vulnerabilities existing in a particular country (whether of a domestic, regional or international origin) affect the scale and the type of IFFs they may see; the capacity to effectively prevent and mitigate them; and the effectiveness of policies and institutions. This section sets out the most significant general factors which determine risk and exposure to IFFs, and contribute to creating an enabling or disabling environment for them.

(a) Crime

Illicit financial flows largely result from proceeds-generating criminal activity. Drug trafficking by organised criminal gangs is one of the most important sources of criminal proceeds globally, and a critically important source of illicit financial flows. Large scale smuggling takes place in legal but highly-taxed goods such as tobacco, and in goods such as gold or other mineral resources which are themselves legal but obtained illicitly. Proceeds-generating crimes also include crimes of corruption and tax evasion, which are important elements of IFFs in their own right. These activities are undertaken primarily for the purpose of financial gain. Money laundering is an essential part of the ability to move and use criminal proceeds without detection. Because of this, combating illicit financial flows directly (e.g. through preventing money laundering and confiscating and recovering the proceeds of crime) can have a significant deterrent effect on the proceeds-generating criminal activity. Combating illicit financial flows is an effective and efficient way to prevent and detect crime, and can be more effective than combating the underlying crimes themselves.. Thanks to the financial tools and investigative techniques available, as well as the enhancement of the normative framework with the UNTOC, preventing and mitigating the risk of illicit financial flows has become particularly useful in combatting transnational organised crime.

This means that in terms of the outcomes of government actions, there is a very close relationship between measures to combat illicit financial flows, and measures to fight other proceeds-generating criminal activity. IFFs and proceeds-generating crimes could therefore be expected to rise and fall together, and reduction on one side will imply a reduction on the other - although the extent to which they are correlated is unknown.

The type and level of criminal activity will have a strong influence on the type and level of illicit financial flows – for example flows generated through drug trafficking use different routes and methods to those related to tax evasion. Countries with high levels of crime, corruption, or tax evasion will experience significant outflows (and potentially also inflows) of illicit finance. Countries with low levels of crime, corruption and tax evasion will not see the same level of illicit finance generated locally, but may nevertheless experience high flows of illicit finance from other countries.

Measures against IFFs already embody a form of policy coherence approach: financial tools used because they are a highly effective way of detecting and deterring crime, and because using financial measures alongside conventional law enforcement focused on the proceeds-generating crime is significantly more efficient than targeting only the proceeds-generating crime.

(b) Good governance, rule of law, and strong institutions

Strong, capable, and well-respected government institutions create a hostile environment for illicit financial flows. well-respected and legitimate institutions foster a culture which discourages some illegal activities, preventing illicit financial flows from arising: e.g. a transparent tax system and sound public expenditure management can discourage tax evasion; while a culture of integrity and accountability within government is essential to prevent and manage potential conflict-of-interest situations and can act as a strong deterrent to corruption. And when illicit financial flows do occur,

effective government institutions - particularly strong and independent law enforcement, judicial and tax authorities, and comprehensive and enforceable laws are more effective in combating illicit financial flows - are critical to detecting and responding to them.

The relationship between good governance and illicit financial flows works in both directions: IFFs and the underlying activity can undermine the legitimacy and capacity of government institutions, e.g. by reducing the resources available to fund them, or by corrupting officials.

Good governance is not limited to government institutions: civil society and independent media are also key contributors, and essential to holding elected leaders and government institutions to account. They are essential to demanding greater transparency, and in many countries have built and sustained pressure to deal with IFFs and the related criminal activity.

(c) Financial sector

The size and nature of a country's financial sector can be a key factor affecting its exposure to illicit financial flows. Countries with small and recently-established financial sectors, or which have only recently begun to apply preventive measures to counter IFFs, will have less weaker implementation of safeguards against IFFs. Larger and longer-established financial sectors will be better able to apply preventive measures, and to develop a pool of expertise in combating IFFs. This reflects both the effectiveness of the regulation of the financial sector (whether measures to combat IFFs are well-implemented and rigorously supervised), and the nature of the financial sector itself - including the capacity and experience of the private sector partners.

International and offshore financial centres face particular risks, since their size, reputation, and connectedness - the factors that make them attractive for legitimate business - also make them attractive destinations for illicit financial flows. The large volume of transactions and non-face-to-face business done in financial centres makes them even more attractive to criminals, and they face risks of IFFs even if they are well-regulated and located in low-crime countries. The highly mobile nature of illicit financial flows also means that countries which provide important enablers for illicit finance – such as secrecy for banking or company ownership – will be exploited opportunistically by criminals (possibly to the exclusion of legitimate business).

(d) International environment

Risk for IFFs is also determined by geographical position and trade or cultural links. Countries may have porous borders with neighbours with high rates of proceeds-generating crime, corruption, or tax evasion; or they may be intermediate steps in routes for smuggling drugs or other illicit items. There are particular risks for countries whose neighbours are in conflict or contain lawless spaces used by terrorist groups or non-state armed groups, since they are likely to be used as convenient channels for funds, arms, and persons. Countries are also at risk of contributing to grand corruption when companies created or based there are operating in other countries, regions, or sectors that are particularly prone to corruption, even if these countries and regions are not their geographical neighbours.

(e) Secrecy, Opacity, and Transparency

Secrecy facilitates crime, corruption, tax evasion, and money laundering, while transparency is an essential tool in fighting them. The degree of transparency which a country requires for the ownership of bank accounts, and legal persons and arrangements (such as companies, and trusts) is a key determinant of the extent to which a country is exposed to and can combat illicit financial flows. Enhancing transparency is a central element of global efforts to counter illicit financial flows, and remains a focus for strengthening implementation. The most important aspects are:

- *Bank secrecy* - Bank secrecy provisions are contrary to several international standards, and its prevalence globally has declined recently in response. Nevertheless, it remains an impediment to the effective investigation and prosecution of economic crimes, and to international cooperation, in a number of jurisdictions.
- *Beneficial ownership of legal persons and arrangements* - The use of complex ownership structures of opaque legal persons or arrangements is now the most commonly used means of hiding ownership and control of assets. Transparency on the beneficial ownership and control of all legal persons and legal arrangements is required by the 2012 FATF Recommendations and in 2014, the Global Forum committed to adopt the FATF concept of beneficial ownership in its terms of reference for Exchange of Information on request. However, as highlighted in the *Illicit financial flows from developing countries*¹³ report, this remains an area where compliance is weak. Establishment of beneficial ownership is so fundamental to the prevention of IFFs, ML and TF that a few jurisdictions have announced plans to go further than the international standards in this area, e.g. by establishing public registries of companies' beneficial ownership information.
- *Transparency regarding payments and contracts*, is used to further discourage corruption, particularly in high-risk areas such as extractive industries and public procurement. The importance of transparency in payments and contracts is reflected in the emphasis it is given in the UNCAC. The EITI is a successful example of how commitments to transparency can help improve governance in vulnerable countries.
- *Transparency of supply chains*, in addition to payments and contracts, is used to prevent natural resources (such as diamonds) being used to support armed groups in several parts of the world, or to encourage sustainable exploitation of such resources.
- “*Secrecy jurisdictions*” – Despite international efforts, there remain a few “secrecy jurisdictions” from which it is either legally or practically impossible to obtain certain information. Exerting pressure on those weak-link jurisdictions is an important focus for international groups noted above. The FATF regards this as so important that they have considered applying risk-based enhanced measures to positively verify the ownership of legal persons and arrangements registered in jurisdictions which do not apply adequate transparency measures, or by refusing to do business with them if this is not possible.
- *Defence and State Security Secrecy* - Many countries have laws to prevent the disclosure of state secrets and protect national security. In some cases these mean defence procurement is exempt from the scrutiny and controls applied to other forms of government spending. These measures are vulnerable to misuse as they prevent effective scrutiny of corrupt contracts and payments.
- *Information flows between authorities* - Many countries apply restrictions which prevent the use of tax information by law enforcement authorities and vice versa, which can hinder investigations and require duplication of efforts. Similarly, some countries restrict tax authorities' access to suspicious transaction reports filed to counter money laundering. Changing these restrictions in appropriate circumstances and under appropriate conditions may increase effectiveness of agencies engaged with tackling illicit financial flows. Those advantages would need to be assessed with a view to the commensurate risks.
- *Data Protection* – there are concerns that data protection measures may be misused as a means to revive bank secrecy, or that they may pose new barriers to the effective exchange of information between authorities and countries – for example, some data protection regulations permit data to be shared only with authorities which apply at least the same level of data protection. It is critical to ensure the protection of personal data, and authorities should ensure

¹³ *Illicit financial flows from developing countries* (OECD, 2014), available from: www.oecd.org/publications/measuring-oecd-responses-to-illicit-financial-flows-from-developing-countries-9789264203501-en.htm.

that those rules are not inappropriately applied to prevent the exchange of relevant information in appropriate cases.

(f) Composition of the Economy

The composition and structure of a country's economy can significantly influence the risks of illicit financial flows. There are several different factors which can be relevant:

- The sector composition of the economy is a major factor. Extractive industries can incentivise to rent-seeking behaviour and are more prone to generate IFFs¹⁴;
- State-owned enterprises can be vulnerable to pressure or exploitation by politicians and other public officials, generating IFFs through corruption or through illegal contracts¹⁵;
- Inequality or lack of opportunity can undermine the moral authority of national laws and government institutions, and can encourage people to turn to illicit activity to support themselves.

¹⁴ as indicated by Andersen et. al. in the paper "Petro Rents, Political Institutions, and Hidden Wealth: Evidence from Offshore Bank Accounts" http://www.nielsjohannesen.net/wp-content/uploads/2014/08/Oil_submission.pdf

¹⁵ Note the CODE report - State-owned enterprises: Good governance as a facilitator for development (OECD, 2015), available from: www.oecd.org/pcd/State-owned%20enterprises_CfD_Ebook.pdf

4. Policy and Institutional Context

Effective policies to counter illicit financial flows need to be embedded within wider national frameworks of policies and institutions, and are dependent on the good functioning of those frameworks. In most cases, measures to combat illicit financial flows will be spread across a large number of disparate policy areas, and make up only a small part of each one. This means combating IFFs is unlikely to be the central objective of policymakers in each area, and measures will only be taken forward if they are compatible with the main policy objectives being sought.

This section sets out the most significant interactions between measures to fight IFFs and wider areas of domestic policy: the justice system; financial supervision; the tax system; public administration; and company & trust law. In particular it sets out possible areas of friction or inconsistency between measures focused on IFFs and more general objectives. A whole-of-government approach to tackling IFFs will require a dialogue with legislators and policymakers on these five areas, in addition to operational cooperation by the specialised agencies set out above.

Institutional arrangements and cultures can be a further obstacle to coherent implementation of measures to combat illicit financial flows, so this section also surveys the different institutions and agencies which are involved in implementing policy in these areas.

Five Key Policy Inter-linkages

1. *Criminal Justice*

Many of the measures used to counter illicit financial flows are within the criminal justice system. This includes establishing criminal offences of money laundering, tax evasion, bribery (including foreign bribery), and related activities; as well as legal provisions for corporate criminal liability, access to financial information, and for the freezing, confiscation, and, where relevant, repatriation of criminal proceeds. Implementing these laws also relies on core elements of the criminal justice system, including law enforcement and prosecution authorities; and the judiciary.

Coherence issues arise regarding the consistent treatment of illicit financing offences and other criminal offences. For example, consistency issues often arise regarding international cooperation, where conventions and treaties establish norms for mutual legal assistance and extradition regarding specific offences, which may not be consistent with those for other offences not included in the conventions. Several standards use the notion of *functional equivalence* to ensure differences in context and legal tradition do not obstruct cooperation against IFFs.

Offences relating to illicit financial flows are complex and time consuming to investigate and prosecute. They can therefore place significant demands on investigators, prosecutors, and judges, in terms of time, resources and technical qualifications.

2. *Regulation and supervision of financial institutions and professions*

As well as preventive measures to counter illicit finance, financial institutions are also subject to prudential supervision, and supervision of their conduct of business, consumer protection, and data protection. These different supervisory regimes have distinct purposes, different approaches to supervision, and in many cases different agencies are responsible for supervising compliance with regulations relevant to IFFs and for other forms of financial supervision. A consistent approach to these various regulatory regimes and their supervision is desirable to enable a coherent compliance culture in financial institutions (for example with a consistent approach to risk, so that managers do not face a zero-failure regime on one issue, and a risk-based approach on another), and to avoid overburdening the financial sector and their supervisors. It can also enable synergies between different

forms of supervision, e.g. where there are red-flag indicators of IFF activity which are visible to a prudential supervisor, but not normally reviewed by AML/CFT or conduct or business supervisors.

At a global level, coherence of financial sector standards is promoted through links between the standard-setters for illicit financial flows noted above, and the financial sector standard-setters, notably the Financial Stability Board (FSB), the Basel Committee on Banking Supervision (BCBS); the (IOSCO); and the International Association of Insurance Supervisors (IAIS). However, there is considerable flexibility about how countries supervise the standards.

At national level, coherence issues are relevant to how supervision is organised: some countries use a single financial sector supervisor responsible for all forms of supervision; some have separated prudential supervision from other forms of supervision, and others have a network of separate supervisors for each sector, including banking, insurance, securities sectors, and regulated businesses and professions.

Differences of approach between supervisors and other oversight bodies can give rise to confusion and send conflicting messages to financial firms. In some cases a confused supervisory architecture can lead to multiple interventions or sanctions for the same activity. The same problems arise for multinational financial institutions which are supervised in several countries: while international standards provide for a coordinated approach by a college of supervisors, and assign clear responsibilities within international financial groups, differences of supervisory philosophy can mean a firm faces very different levels of regulatory risk in different countries. This is discussed further in the next section on international spillovers.

3. Tax System

Tax evasion is defined by each country's tax law. Therefore, while in most countries tax evasion is a crime, the behaviours which fall within the definition of "tax evasion" can differ. An absence of measures to support tax transparency can create opportunities for tax evasion and tax fraud. Tax policy and illicit finance present multiple trade-offs at national level:

- Some types of tax are harder to evade than others, e.g. physical assets such as land or imports are harder to conceal or relocate in another jurisdiction than intangible or financial assets such as shares or bank deposits. Countries facing high risks of evasion may come to rely more on harder-to-evade forms of taxation. However, hard-to-avoid taxes are not always the most economically efficient or non-distorting, and over-reliance on such forms of taxation can potentially weaken economic activity and growth. The use of import and export duties as the principal source of tax revenue can mean the tax burden falls disproportionately on trade, with negative consequences for inward investment and for growth.
- When tax evasion is detected, countries can face a choice between maximising the revenues recovered, or punishing the criminal offence. Tax evasion is a criminal offence and a predicate offence for money laundering. In many countries tax evasion is investigated and prosecuted by the tax authority rather than by law enforcement, and tax authorities may take a different approach to law enforcement when determining whether to proceed with a prosecution. In many cases, their policy is to prioritise recovery of revenues through an agreement with the offender rather than proceed with a prosecution – particularly in complex cases. This is a difficult trade-off: policymakers must balance the efficient use of prosecutorial resources and the need to maximise revenues, against the deterrent effect of prosecutions and the risk that the public may perceive the treatment of offenders as inconsistent or unfair.

4. Government and Public administration

Measures to improve public administration, combat corruption, and counter illicit finance are interdependent and mutually supporting. Combating IFFs supports good governance by reducing the opportunities for corrupt officials or contractors to safely misappropriate public funds. Reducing

corruption in the public administration increases the authorities' capacity to effectively combat illicit finance, by preventing circumvention of justice and making more resources available for prevention.

There is also negative feedback, corresponding to the positive picture above: large-scale illicit financial flows have a corrosive effect on the integrity of public officials, and can undermine good governance and sound administration. In turn, corrupt and ineffective governments are a key enabler of illicit financial flows.

Direct measures to prevent corruption and policy capture, to combat foreign bribery, and to promote sound and transparent public procurement and financial management practices, can have a significant effect by removing opportunities for corruption and increasing the risk of getting caught. These include measures to:

- ensure law and policy making is up-to-date and responds to the public's best interests (not purely corporate ones) and are not unduly influenced by lobbying efforts¹⁶;
- promote integrity in the public sector, including the prevention and management of potential conflict-of-interest situations such as revolving doors¹⁷;
- implement fair and competitive public procurement practices¹⁸;
- increase the transparency of government information (including on such key issues as political contributions, public procurement contracts, public finances, etc.)¹⁹;
- repeal unnecessary or out-of-date laws and regulations²⁰; and
- Hold elected leaders and government to account by monitoring compliance with ethics and integrity measures through strong internal controls and external audit.

5. *Company and trust law*

The misuse of legal persons and arrangements such as companies and trusts is an important tool used by criminals to launder money, conceal their identities, and disguise the true ownership of assets. Rules governing the establishment of companies or corporate governance can have a significant effect on illicit finance. Ensuring transparency about beneficial ownership (the ultimate ownership and control of companies), e.g. through the obligation to maintain up to date information on the verified beneficial ownership of all legal persons and arrangements, could make a major contribution to combatting illicit financial flows. Measures to ensure changes of ownership and control are recorded could also make a significant contribution.

However, there are trade-offs: the ease with which a company can be formed can be an important determinant of growth in the private sector, and is an important indicator of the ease of doing business in a country²¹. Each of the transparency measures above imposes some additional cost and delay when establishing or administering a company, and therefore worsens the perceived ease of doing business. Countries face a trade-off between being (and seen to be) business-friendly, and preventing the exploitation of legal persons and arrangements established by or operating in their jurisdiction for purposes relating to illicit financial flows.

¹⁶ (see OECD principles on lobbying and OECD regulatory governance recommendation)

¹⁷ (see OECD Recommendation on Managing Conflict of Interest in the public Service and corresponding toolkit)

¹⁸ (see new OECD Public Procurement Recommendation)

¹⁹ See OECD Budgetary Governance Recommendation, Best Practices in Budget Transparency as well as previous instruments mentioned (on lobbying, CoI, public procurement, regulatory governance) which also include transparency components).

²⁰ <http://www.oecd.org/governance/regulatory-policy/2012-recommendation.htm>

²¹ This is one of the indicators that makes up the World Bank's "Doing business" index, which measures the burden of business regulations on companies. [NOTE – are there also OECD indices for ease of doing business, that we could refer to here?]

Corporate criminal liability can have a significant impact on the behaviour of companies regarding IFFs. This was demonstrated in the response to the Anti-Bribery Convention (ABC). In the 41 countries which are Parties to the OECD ABC, companies as well as individuals face liability for the payment of bribes to foreign public officials: bribery is no longer only an offence for the official who receives a bribe but also for the person or company who promises or gives the bribe. Since the entry into force of the OECD ABC, governments and business representatives have worked closely with companies to put into place internal controls, ethical and compliance programs and measures to prevent and detect the perpetration of bribery offences. Strong, and consistently-applied sanctions, including imprisonment of individuals, are a strong deterrent. Consistency should also be applied in the information available to the public and the financial sector or professions, which in some countries are encouraged to self-disclose such offences to limit their liability.

Actors: Key Agencies and Institutions

Combating IFFs is about effective implementation as well as sound and coherent policy-making. This is a complex area, in which specialised functions have been (or should be) created within existing government structures and agencies. This means there are many different departments, institutions, and other actors involved in making and implementing policy in this area, with different skills. The organisation and structure of this framework can be very different from one country to another, depending on their legal traditions and administrative systems. Understanding (and connecting) the different actors involved in combating IFFs is a prerequisite for a coherent approach. The scale of the challenge is illustrated below:

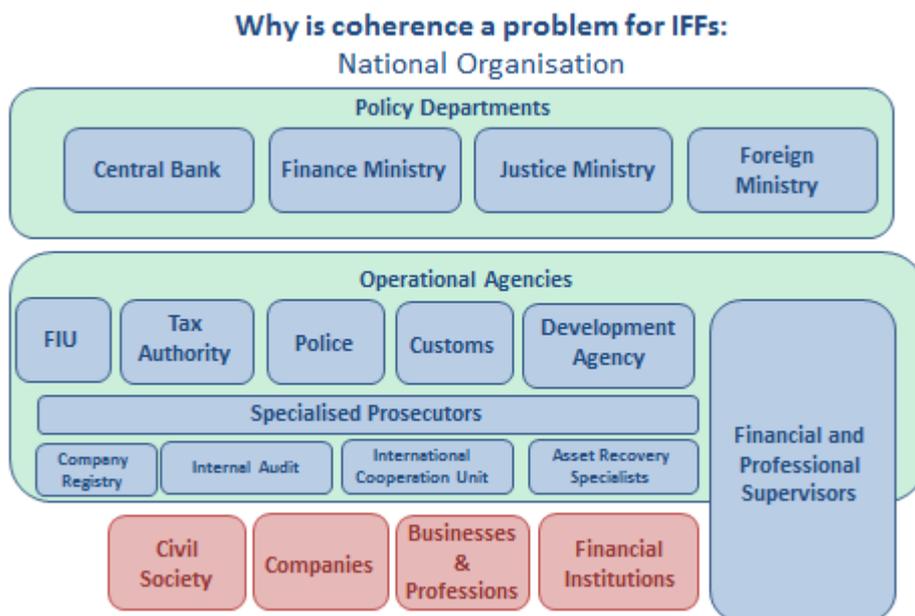


figure 2 : Key actors involved in Combating Illicit Financial Flows.

To combat illicit financial flows effectively, governments have to bring together different agencies, with different skills and expertise, different cultures, and different priorities. They also need the active engagement and participation of a wide range of entities outside government. In Fig.2:

- the top level is the key policymaking departments in central government. IFFs do not sit within the normal remit of a single ministry, but cut across several departments.
- The middle level includes the operational agencies which implement the laws, regulations, and policies to counter IFFs - both preventive and punitive. This includes parts of the criminal justice system; financial and professional supervisors; and a range of specialised agencies.

- The lower level shows the sectors outside government which have a role in applying measures to prevent and detect illicit financial flows, of which there are many. For example “businesses and professions” in this case applies to accountants, auditors, lawyers, notaries, dealers in gemstones and antiquities, real estate agents, company formation agents, financial advisors, and several others.

The main government actors involved in combating IFFs are:

- *Central Government Policymakers* – policy on IFFs is generally set by one or more central government departments (typically the ministry of Finance, Interior, or Justice), which may also have a role in coordinating implementation by other agencies.
- *Tax Authorities* – are responsible for enforcing tax laws, and also often have the power to issue relevant tax regulations or guidance for taxpayers. In many cases the tax authority is also responsible for investigating and prosecuting tax evasion and other tax crimes, and in some cases, money laundering.
- *Financial Intelligence Units* – are central bodies for receiving and analysing reports of suspicious activity from the financial sector and professions, and disseminating the results to the relevant authorities. The FIU function may be established as an independent unit within a law enforcement agency, central bank, or department of government, and many FIUs also have a supervisory role - so this may overlap with other types of actors.
- *Law Enforcement, Customs, Prosecutors, and the justice sector* – Criminal activity related to illicit finance is in most cases handled by existing law enforcement agencies that are responsible for investigating and prosecuting offences of money laundering, corruption, and tax evasion, along with all other criminal offences. This often involves multiple authorities with different geographic or thematic mandates.
- *Specialised Investigation / Prosecution units* – Some functions, such as financial investigation, investigation of bribery or corruption, fraud, or financial crimes, asset tracing and confiscation, or prosecution for tax offences, are highly specialised, and many countries establish dedicated expert units to perform these tasks. These may be a specialised unit within another agency, or a stand-alone unit independent of existing institutions and agencies. Several countries have established dedicated anti-corruption units which fall within this category.
- *Supervisors* – Supervisors oversee compliance by the financial sector, firms, and relevant professions with preventive measures to combat IFFs, including the control of products or services which can enable IFFs. Supervisors form a diverse group, including both government agencies (often within the Central Bank), operationally independent authorities, and self-regulatory organisations. Some supervisors enforce rules made by a separate rule-making body, while others also have rule-making authority in their own right.
- *Development agencies*; through programmes to ensure and monitor the integrity of aid spending, and through capacity building on combating IFFs and recovering assets. Development itself can be a long term preventive measure by increasing overall capacity, growth and governance and decreasing vulnerabilities created by unemployment, poverty and lack of resources. The international community, in their elaboration of SDG 16 drew a hard link between development and the rule of law, and illicit financial flows.
- *Ministries of Finance* play several essential roles: as the institution responsible for setting budgets and monitoring expenditure, the finance ministry is crucial to the resourcing and prioritisation of measures to combat IFFs, and to prevent corruption. As the institution responsible for setting tax policy and fiscal forecasting, it is able to influence the degree and type of tax evasion, and to quantify the impact on revenue. And as the institution responsible for laws and regulations applying to the financial sector, it is able to decide the extent of preventive measures applied. In developing countries, the finance ministry may also be the

main interlocutor with the international community, and would be involved in decisions about the prioritisation of measures against IFFs in national development plans or IFI programmes. In resource-poor countries this is an extremely important function and can determine the development of the preventive framework.

- Many governments also include other bodies which can make a significant contribution to fighting IFFs, such as:
 - *Trade promotion and export credit agencies*, which can play an important role in preventing and detecting corruption and foreign bribery;
 - *Internal and external audit bodies*; which monitor compliance with relevant laws and regulations; monitor effectiveness; and ensure sound financial management;
 - *Centralised purchasing and procurement agencies*; which can harmonise good practices and reduce the scope for corruption; and
 - *Bodies for promoting professional standards and integrity* - e.g. by managing potential conflict-of-interest situations arising from previous employment, avoiding decisions being compromised by a “revolving door” between public and private sectors.

Measures to combat IFFs also involve a range of actors outside government. Most countries require financial institutions and some professions to apply preventive measures to prevent IFFs (e.g. by reporting suspicious transactions to the FIU). The sectors required to apply such measures are also key actors in combating IFFs.

- *Financial sector* – As “gatekeepers” to the financial system, banks and other financial institutions are required to implement a wide range of preventive measures to combat IFFs, and are an essential source of information for the investigative agencies above. This includes not only formal financial institutions, but also “informal” providers of financial services such as money remitters or hawalas.
- *Regulated professions* – lawyers, accountants, real estate agents, auditors, trust and company service providers, and some other businesses or professions are also required to apply preventive measures to prevent economic crimes, and thereby combat IFFs.
- *Companies* - companies face growing incentives to put into place ethical and compliance programs, including internal controls, to prevent and detect corruption and foreign bribery. This is true of companies in countries party to the Anti-Bribery Convention or likely to fall under the jurisdiction of these countries, and particularly where such programmes may be a defence or a mitigating factor to the criminal liability of companies.

5. Trade-offs, Conflicts, and Spillovers

The description of the policy and institutional context for IFFs and measures to counter them above shows how these issues are related to a wide range of other areas of policy, domestic and international.

This section looks more specifically at the areas where policy tensions can arise as a result of those interactions. These tensions include direct policy conflicts between objectives relating to IFFs and other policy objectives; and unforeseen conflicts which arise from the way policies are implemented - in particular from the way in which the financial sector and regulated professionals respond to policies. It also sets out some of the trade-offs or choices which countries can face when seeking to integrate the fight against IFFs into these areas and a balanced and coherent set of national policies, and highlights the considerations on both sides of them.

The overarching trade-off regarding illicit financial flows concerns **risk, cost, and proportionality**: are anti-IFF policies, given the costs they involve, a proportionate and justified response to the risks posed by IFFs? Policy making involves considering options on the basis of risks, costs and benefits. Under the international normative framework of rules and standards, countries have a great deal of flexibility about how intensively they apply measures to combat illicit financing – including the strength of preventive measures in the financial sector, and the staffing, powers, and resources of the agencies responsible for preventing, detecting and punishing financial crimes. Decisions on the priority given to fighting illicit financial flows, or on whether to apply additional measures, should be based on an understanding of the risks - which vary considerably from country to country. This fundamental element of policy making and implementation has been recognised for many years and in 2012 this concept was included as the first recommendation of the new FATF standard.

IFFs can be a cause for concern even in jurisdictions which have low domestic levels of proceeds-generating crimes, corruption, and tax evasion – and therefore face low domestic risks of illicit financial flows, because international risks - e.g. inflows of the proceeds of foreign crimes, or foreign bribery by companies located in the country, are also relevant when deciding how strongly to prioritise actions against illicit finance. A country which relaxed its controls on the basis that its domestic risks are low could potentially become a haven for illicit finance originating in other countries - even if its risk assessment is correct.

The rest of this section looks at the most significant policy interactions, in four general areas.

Economic Issues

Trafficking in illicit goods and smuggling

The conditions which make trafficking or smuggling of drugs and other illicit goods profitable are the result of policy choices which determine differences in the availability or price of goods on either side of a border: either where products are prohibited, or where products are legal but there are large differences in their price between countries (e.g. because of the level of tax or duty applied). As well as the physical movement of goods, smuggling can also give rise to flows of illicit funds; corruption of border officials; and the establishment of organised crime groups.

Spillovers can arise whenever policies on both sides of a border are not aligned: a country which significantly increases the tax or duty on a specific product will unwittingly economically incentivise the inbound smuggling of that product. The significance of these risks varies according to the type of goods and the ease of crossing borders: easily transported goods; small countries; good transport links; and light border controls mean greater risks. Bulky goods, and larger, more remote, or stricter countries will see less risk of smuggling. Countries should be aware of the risks of incentivising IFFs when considering changes to controlled substances or specific goods taxes or duties.

Export promotion

Some companies may consider that they are placed at a competitive disadvantage by anti-foreign bribery measures – for example when competing for contracts in a corrupt country and/or sector, against foreign competitors which are not subject to the same anti-bribery requirements. A clear way to manage this trade-off is to further level the playing field through ensuring peer pressure for a steadier enforcement of the Anti-Bribery Convention (ABC) by all Parties to the Convention and through continuing to expand the membership of the Convention. Increased peer pressure and broadened accession to the Convention have already had a strong impact. Recent studies have shown that after the onset of Phase 3 in 2010, when the risk of punishment under the OECD ABC increased firms from signatory countries reduced their actual bribery relative to their non-signatory competitors.²² Investors from countries that implemented the OECD Anti-Bribery Convention also reduced their investments in corrupt countries.²³

Voluntary Tax Compliance (VTC) Programmes

These programmes enable taxpayers to normalise their situation, regarding income and assets which were previously unreported for tax purposes (e.g. funds transferred or held overseas for tax evasion purposes). VTC programmes take a variety of forms, but typically involve an amnesty for tax evasion on the condition that funds are returned to the country and the tax paid. They are particularly used by countries facing economic crises, and more recently have been used to allow taxpayers to regularise their affairs now that bank secrecy vis-a-vis tax authorities is coming to an end.

VTC programmes offer the opportunity to maximise the benefits of improvements in transparency and exchange of information for tax purposes, to increase short-term tax revenues and improve medium-term tax compliance. To succeed, they need to tread a fine line between encouraging non-compliant taxpayers to improve their compliance (a balancing act in itself) and retaining the support and compliance of the vast majority of taxpayers who are already compliant. To do this, these programmes need to form part of wider voluntary compliance and enforcement strategies. They also need to be consistent with relevant rules in the non-tax area such as anti-money laundering rules, to ensure they are not misused. The FATF has set out principles²⁴ (which could guide the improvement of policy coherence) governing how VTC programmes should manage this risk.

Financial markets and financial stability

In some cases, the volume of illicit financial flows into or out of a country can be very large, and can have a noticeable impact on the legitimate economy, including specific sectors, or the economy as a whole. Some examples include:

- *Demand-driven price inflation:* In some countries, residential property has come to be seen as a safe place to store illicit assets from other countries. The volume of illicit finance can be sufficient to significantly affect prices. One recent example is from Kenya, where property prices in Nairobi increased significantly between 2000 and 2010, out of line with Kenya's wider economy. Much of this increase was ascribed to purchases by Somali pirates.
- *Loss of trade-related revenue:* Trade mis-pricing is a common money laundering technique: in order to move value without the need for financial transfers, imports are deliberately under-priced (or smuggled as contraband), and sold at a large profit in the destination country. In

²² Jensen, N.M., E.J. Malesky. 2013. Does the OECD Convention affect bribery? Investment liberalization and corruption in Vietnam. Washington University, St. Louis.

²³ Cuervo-Cazurra, A. 2008. The Effectiveness of Laws against Bribery Abroad. *Journal of International Business Studies* 39(4) 634-651.

²⁴ http://www.fatf-gafi.org/media/fatf/documents/reports/BPP_VTC.pdf

Colombia, where this technique is used to launder the proceeds of drug trafficking, it happens on a large enough scale that heavily discounted contraband goods have depressed prices and driven-out legitimate, full-priced imports.

- *Exchange rate volatility*: Illicit financial flows from some developing countries can be large enough to place long-term downward pressure on exchange rates, affecting the economy as a whole. Illicit financial flows are also highly volatile in response to a range of “push” and “pull” factors, with potentially destabilising exchange rate effects on both origin and destination countries.
- *Destabilising systemically important financial institutions*: Illicit financial flows can be used to perpetuate large-scale fraudulent schemes, potentially tainting a significant portion of deposits or capital. In low income countries, with low levels of formal sector intermediation, the discovery of IFF activity, or its interruption, could significantly affect the position of individual financial institution, undermine the confidence of counterparties, or even threaten trust in the banking system and its regulation.
- *Volatility and unpredictability*: Illicit financial flows are “hot money” - prone to shift suddenly from one jurisdiction to another in response to changes in the risk of detection or confiscation. Such changes can be large enough to affect the wider economy. Furthermore, even when illicit financial flows are stable, they form an un-measured and un-modelled part of the economy, which can render economic forecasts less reliable, and reduce the effectiveness of economic policies.

The trade-offs and linkages in this area are complex: in some cases, the application of more effective financial controls may displace illicit activity into a different sector. In other cases there may be hidden costs (in terms of macroeconomically destabilising flows) resulting from openness to illicit finance inflows. Countries should be alert for these effects, particularly following major changes to their regimes for countering IFFs.

Capital Controls

Capital controls are sometimes used to support an exchange rate regime or prevent capital flight during a crisis. These controls typically limit the amount of money which citizens and companies can exchange or transfer abroad. In some cases, widespread efforts to evade capital controls have led to thriving black markets. They have also led to the development of underground financial channels which, in addition to enabling the circumventing of controls during the control period, were perpetuated to facilitate crime, tax evasion, and money laundering long after the foreign exchange crisis was over.

Social Issues

Financial Inclusion

Financial inclusion is a significant enabler for development, and some have pressed for it to be considered as a human right and adopted as a high-level goal in the SDG framework. Given the importance of financial inclusion to development, policy to prevent IFFs must be coherent with policies to improve financial inclusion.. The tensions are well known and quite complex, for example, preventive measures to counter money laundering require financial institutions to verify the identity of their customers. But many people in developing countries lack identity documentation, and risk being excluded from access to financial services by customer identification rules. Also, financial inclusion must take advantage of technologies which are difficult to regulate from an IFF policy perspective. This is not only an issue for developing countries: financial inclusion is also a challenge in OECD member countries, several of which have initiatives to ensure basic financial services are available to all citizens.

In order to manage the tensions between financial inclusion and anti-IFF measures, the FATF has developed guidance on financial inclusion²⁵, which sets out how countries can pursue the objective of financial inclusion without compromising measures to combat crime – for example by relaxing identification requirements or using alternative means of identification in low-risk situations, or by using thresholds and ongoing monitoring to mitigate the risks of reduced customer due diligence. This guidance should be mainstreamed into development planning in low income countries to improve policy coherence at the national level.

The informal financial sector

For a large portion of the world's population, the informal sector is the only form of financial intermediation available. Informal operators typically provide money remittances, but may offer a wider range of services, particularly in countries such as Afghanistan, where the formal financial sector accounts for only a small fraction of financial intermediation. Left unregulated, the informal sector can be exploited as a channel for illicit financial flows, or can exploit its customers, who are not protected by authorities. Some countries have responded by prohibiting informal providers altogether, sometimes with the unintended consequence of denying people access to even basic financial services, or of driving activity even further underground. Other countries have sought to license, regulate and supervise these organisations, so as to reduce their vulnerability, but recognising their importance to their customers. Regulating informal providers of financial services is a difficult task. In policy terms, governments must recognise that applying the same rules to informal providers as to mainstream financial institutions would effectively shut them down altogether. However, applying less burdensome rules can raise concerns about fairness and equal treatment of formal and informal sectors. At a practical level, regulating informal providers requires capacity, resources and geographical reach. It also requires a tremendous amount of cross border cooperation, which does not really exist. This is a very important issue for many countries and likely contains many trade-offs and conflicts which are not yet known.

NGOs and CSOs

Non-Government and Civil Society Organisations are subject to some preventive measures, because of their vulnerability to misuse for IFFs. The security community is especially concerned with the misuse of NGOs to front the financing of terrorism. However, there are concerns that these measures can be applied excessively by governments seeking to suppress the NPO sector and the civil society voice it provides. The challenge for countries is to take proportionate measures to ensure NPOs are not misused to finance terrorism, without limiting NPOs access to the financial system or their ability to operate effectively, including their work in fragile or high-risk states. NPOs are also particularly affected by de-risking by financial institutions, as set out above, based on their perceived vulnerability to misuse.

Migrant Remittances

Remittances from migrants are a key source of finance for many developing countries, and are particularly related to the need for financial inclusion and the impact of de-risking, both of which can necessitate policy trade offs. Lack of financial inclusion and de-risking both limit the ability of migrants to send money home, either individually, or by restricting the available channels, with potentially serious consequences for persons, communities, and countries which are reliant on remittances.

Many countries have taken steps to ensure remittance flows can continue uninterrupted. Several countries, including India, have programmes to provide identity documentation to all persons. Others

²⁵ Available from: www.fatf-gafi.org/topics/financialinclusion/

have implemented financial inclusion measures such as the use of non-standard forms of identification (e.g. confirmation by village elders) for customers without documents. And many countries are using non-traditional ways to access financial services, such as through mobile phones, to reach customers in remote areas. There is also a role for governments in countries hosting migrant workers, particularly development ministries, in ensuring sound regulation of money transmitters, promoting fair fees, and using their influence with banks to ensure the continued availability of remittance channels.

Financial Sector Issues

De-risking

De-risking is a relatively recent phenomenon of financial institutions ceasing to do business with certain high-risk categories of customers – particularly operators of money and value transfer services (MVTs) and non-profit organisations (NPOs). It is intimately linked to the issues noted above. This affects both new customers, who are unable to open accounts, and existing customers whose accounts have been closed. Financial institutions' explanation for this approach is that these customers present an unacceptably high level of risk, which would require additional (and costly) measures to manage, and therefore that retaining them as customers is not commercially viable.

In policy terms, the effects of this behaviour by banks are felt most severely by MVTs providers and NPOs. MVTs are critical channels for remittance flows sent by migrants to their home countries – which are a major source of finance for many developing countries. Ensuring reliable and inexpensive channels for remittances is an important element of the SDGs (target 10.c). MVTs providers rely on access to the formal financial system for settlement purposes, and are generally unable to operate without it. Preventing new MVTs operators from accessing the financial system creates barriers to market entry and competition, and threatens to raise remittance costs. Denying access to existing providers effectively closes remittance channels, with severe effects on the cost and availability of remittance services. De-risking may also increase the overall risks of illicit financing, by encouraging the use of informal and unregulated channels once formal channels are closed. It is therefore a significant concern for governments.

Debate is still ongoing about the nature of de-risking, the responsibility for it, and the best response. Much discussion has focused on the business climate following the 2008 financial crisis (in which banks are under pressure to reduce their costs and to drop their less profitable customers), and on pressure from regulators. De-risking is not only a response to the risks of criminal misuse of the financial system, but also to the risks of regulatory action, e.g. guarding against the reputational risks of the resulting fines and publicity. The sectors concerned are seen as exposing banks to unacceptably high risks of regulatory action, which cannot be managed in a cost-effective way. This means there are several ways countries can influence policy coherence for de-risking behaviour by banks:

- Dialogue between regulators, supervisors, and the financial sector can clarify the expectations of supervisors regarding risk management of MVTs and other supposedly higher-risk types of customer, and provide reassurance about the regulatory risk financial institutions will be undertaking.
- Reinforced supervision of the sectors concerned can also provide reassurances. De-risking is in part a reflection of the banking sector's lack of confidence in the separate regulatory and supervisory regimes applied to MVTs and NPOs, which are not seen as adequate to mitigate the risks in those sectors. Stronger and more visible supervision of the NPO and MVTs sectors can help restore confidence in the systems and controls they apply, and hence reduce banks fears about their risk exposure.

De-risking involves transnational risks, and could benefit from a policy coherence approach. Further action will be needed to address this issue at global level – as discussed below in the context of international spillovers.

Burden on the private sector

Preventive measures by financial institutions and other regulated entities to combat illicit financial flows can be costly and time consuming. They impose a significant burden on the sectors concerned: in some banks up to 10% of staff work on compliance issues. They also impose costs in terms of the systems and processes needed, and the time taken. Dialogue between government and the private sector is important, to ensure that government decisions on preventive measures are based on a full understanding of their costs and impact on the conduct of business.

Supervision of multinational financial institutions

Supervision of multinational financial institutions raises particular challenges. Financial institutions face global supervision by their home supervisor (the supervisor of the jurisdiction where they are headquartered), and also face local supervision in other countries where they have branches or subsidiaries – with a different regulatory environment in each country. Many financial institutions seek to harmonise their internal procedures globally, and to make decisions about illicit financial flow risk management at a global level. This means that actions by regulators and supervisors in one country may have an effect globally – e.g. by adding to the procedures required, or affecting the institution’s perceptions of the regulatory risks. In some cases these spillovers are benevolent (i.e. banks will apply strict internal controls even in countries with weak regulations). In others they may be destructive (e.g. de-risking by banks in one country, in response to supervisory actions in another).

Data Protection

Conflicts can arise with data protection requirements, for example FATF Recommendations require financial institutions to retain customer and account information for a *minimum* of five years (to ensure an adequate trail for investigators), while data protection rules set a *maximum* data retention period of five years (to prevent the misuse of old information). Firms subject to both requirements can find themselves facing a choice of which legal requirement to implement. Conflicts can also arise between requirements to circulate some customer information within an international financial group, and prohibitions on sending customer information to a country without adequate data protection. Policy coherence work is ongoing in this area. This has been based on a recognition that data protection and measures to counter illicit finance have a shared objective to protect people from crime, which is not advanced by incoherent policies.

In some countries there is effective coordination between the regulatory authorities responsible for data protection and for illicit financial flows, and clear direction has been given to the private sector entities which are affected by both requirements.

International Issues

Diplomatic Relations

Requests for mutual legal assistance are often issued through ministries of foreign affairs, and diplomatic relations are always part of facilitating international normative agreements. Measures to counter illicit finance can also have diplomatic costs – particularly where the policies of other countries or the personal interests of their leaders and officials are affected, as is often the case for investigations of bribery and corruption. Diplomatic pressure may be exerted to have investigations discontinued, accompanied by threats to ongoing or future contracts, joint projects, and possibly military or intelligence cooperation if investigations are allowed to proceed. The OECD ABC explicitly prohibits countries from taking such considerations into account in the decision to investigate and prosecute foreign bribery (e.g. Article V of the Anti-Bribery Convention).

Constitutional or operational independence of investigators and prosecutors from the Executive is a key element to prevent this type of influence, since the politicians and officials who are exposed to this pressure do not have the power to end or prevent the opening of investigations.

International Cooperation arrangements

In an international setting; differences between countries' criminal laws and procedures and in the rules governing international cooperation can give rise to safe havens for criminals or for illicit financial activity. Criminals may choose to launder their money in a country which has a weak criminal offence or light penalties for money laundering, or in a country which does not extradite its own citizens. Similarly, companies may use subsidiaries or intermediaries in countries where there is no foreign bribery offence or corporate criminal liability, or which does not respond effectively to foreign requests for ownership information.

Measures to combat illicit financial flows internationally depend on a framework of international cooperation measures, affecting all aspects of cooperation. These include:

- Mutual Legal Assistance and extradition (e.g. in the terms set by the multilateral conventions noted above, or under bilateral treaties);
- Law enforcement cooperation (e.g. through Interpol or Europol, or through bilateral arrangements);
- Supervisory cooperation (e.g. through the frameworks for cooperation set out by BCBS, IOSCO, or IAIS);
- FIU cooperation (e.g. through the Egmont group);
- Cooperation on asset tracing and recovery (e.g. through the StAR initiative or GAFILAT) and
- Tax information exchange, under the international standards for the exchange of tax information on request (EOIR) and the automatic exchange of financial account information (AEOI).

Countries' membership and participation in these mechanisms for cooperation and information exchange is critical to their ability to provide or receive international cooperation against illicit financial flows, but is not enough on its own. Practical capacity to use these mechanisms is also essential. Countries also need:

- Secure communication channels through which sensitive information can be passed, and the ability to safeguard information after it is received.
- Working relationships with authorities in other countries: even within a multilateral cooperation framework, practical cooperation depends on having an adequate understanding of other countries' arrangements; mutual trust; and an active and reciprocal relationship. Countries with regular contact or dedicated liaison officers in embassies are much better able to seek or provide cooperation than those seeking assistance irregularly or for the first time.
- The ability to adequately and appropriately use information received, which can be labour-intensive or technically demanding – particularly in the case of automatic exchange of tax information, which requires capacity to process large volumes of data.

Development Assistance

Development assistance programmes can make an important contribution to combating illicit financial flows. In general terms, improved governance and capacity in developing countries can strengthen the effectiveness of the regime to combat IFFs. Measures to combat tax evasion or corruption strengthen the capacity to mobilise and use domestic resources. Such assistance need not be limited to activity in developing countries themselves: measures to support developing countries' capacity to

engage in international cooperation such as the StAR initiative can also be effective, as can the establishment of dedicated law enforcement capacity to pursue stolen assets on behalf of developing countries.

Global Forum on Transparency - Africa Initiative

The Global Forum on Transparency and Exchange of Information for Tax Purposes, in conjunction with CREDAF, ATAF and the World Bank Group launched the *Africa Initiative* at its plenary meeting in October 2014. This initiative is supported by development partners. It is designed to unlock the potential for tax transparency and exchange of information in Africa and ensure that the continent can seize the opportunities presented by exchange of information. Over the course of 2015-17, the Africa Initiative will engage with current African members of the Global Forum to provide support and guidance to ensure effective exchange of information can happen. There will also be a programme of high-level events to ensure that the benefits of exchange of information are being communicated. The Africa Initiative is steered by a Taskforce made up of a small group of “first mover” countries from Africa and participating international organisations.

6. Improving Policy Coherence on IFFs

Combating illicit financial flows is a complex area, and involves a large number of different actors, many of which have similar or overlapping mandates and responsibilities. It also potentially presents many areas where compromises are needed between the goal of combating IFFs and other domestic or international policy objectives. Sustainable development and effective implementation of policies to counter IFFs both depend on a concrete understanding of the entire policy picture. This means there is a need for countries to take an integrated and high-level approach to ensure policy coherence, which is fully mainstreamed into national development planning. Operationally, countries will need to be able to resolve conflicts between agencies and disciplines, and promote cooperation and coordination in the implementation of policy.

Building and implementing coherent policies on a subject which involves so many different elements of government policy, and so many different actors is challenging. Governments need to clearly articulate IFF priorities in the context of planning for the whole of government. That is not an easy exercise but one which is increasingly called for by the international normative framework, for example by calling on countries to first understand their risk environment, and then plan appropriate measures to mitigate the risks they face. All government agencies compete for policy space, therefore a deliberate and considered articulation of measures to be taken in developing the framework for preventing IFIs is crucial.

It is a good practise to involve all competent authorities - including operational agencies - in the development of policy, to avoid requirements which are impractical or competing. Feedback to policymakers from implementing authorities and from other stakeholders inside and outside government is also essential, to identify and respond to unexpected or unintended consequences as they arise, and to enable improved or better-focused policies to develop over time.

This section sets out approaches which can help promote policy coherence specifically on IFF issues - as a supplement to the general good practices on institutional measures to promote coherence, which are set out in the *Framework for Policy Coherence*. It also sets out some good practices for operational cooperation and coordination in the context of the complex institutional framework for combating IFFs.

The OECD has produced practical advice on implementing a whole-government approach and ensuring policy coherence, in the main sections of the *Policy Coherence for Sustainable Development Toolkit*, as well as in the *2010 Council Recommendation on Good Institutional Practises in Promoting Policy Coherence for Development*; and the 1996 *Public Management Occasional Paper, Building Policy Coherence: Tools and Tensions*. The general lessons, mechanisms, and good practises which these papers suggest apply to policy making to reduce illicit financial flows.

Wider OECD work is also highly relevant to promoting policy coherence; in particular on the role of the Centres of Government in meeting governance challenges and managing cross-cutting policy issues²⁶.

Some of the specific coherence challenges in reducing illicit financial flows are listed below, as well as means of addressing them which have been adopted by some countries.

Understanding the Risks and the Illicit Finance Environment

The nature of the challenge posed by illicit financial flows varies a great deal between countries – according to their nature of their economy and financial sector; their administrative structure; and their international connections - as well as their level of capacity, resources, crime, and security.

²⁶ See <http://www.oecd.org/gov/cog.htm>

Policy coherence always begins with understanding the country's risk environment for IFFs, in order to effectively prioritise the most relevant areas, and allocate resources appropriately.

National risk assessments of money laundering and terrorist financing are already required by the FATF standards, with countries required to identify, assess, and understand the ML/TF risks they face²⁷. Many countries also conduct risk assessments focused on domestic crime or on abuses of the fiscal system. Given the interactions between different types of illicit financing, these different risk assessments may be able to inform each other, and there may be value in combining their conclusions in order to give a comprehensive picture of illicit financial flows. However, these may still leave significant gaps: for example if they are focused on domestic misconduct and not on illicit financial flows from other countries. At present there is no accepted methodology for assessing the risks of IFFs as a whole - although there are approaches which assess specific components of IFFs. Developing such a methodology could be a significant support to countries seeking a full understanding of the IFF environment, so as to work out which of the policy links are most significant and should be prioritised.

A sound understanding of the risk environment supports analysis of the impact of proposed policies - including possible unintended consequences of policy measures (e.g. de-risking by banks, or the impact on informal artisanal miners reported to associated with section 1502 of the US Dodd-Frank Act).

Inter-agency coherence mechanisms

Combating illicit financial flows involves a large number of different government authorities and agencies, as set out above. It needs the active involvement of several central government ministries with different priorities (finance, foreign affairs, interior, justice, and possibly others), as well as the centre of government. It also needs effective participation and advice from a large number of regulatory and operational agencies. Preventive measures are also implemented by financial institutions and professionals. This can make policy decisions complicated. To handle these issues, and reflect the frequent need for coordination on IFFs, some countries have established standing arrangements at two levels:

- *At policy level*, differences in priorities between ministers and departments arise routinely in the sphere of illicit finance, which means the ad-hoc processes, based on cabinet or its subcommittees, which are described in the general good practises on policy coherence; may be inadequate or inefficient in the case of IFFs. Instead, it may be more coherent to have standing arrangements for the governance of illicit financial flows that include multiple ministries. For example, some countries have a single government department and minister responsible for illicit financial flows – but with a responsibility to consult the other departments involved on all decisions. Other countries have no single lead on the issue, but several different ministers are jointly responsible for illicit financial flows (or specific types of illicit financial flow). Regardless of the institutional model used to coordinate policy, the important elements seem to be: a policy framework built on informing, consulting, building a shared understanding of tradeoffs, and gaining inputs from relevant ministries involved; mechanisms for information exchange and dialogue across sectors; gathering/centralising evidence from across ministries/institutions; mechanisms for anticipating/flagging conflicts or implementation challenges and a forum for discussing how to overcome these.
- *At the level of implementation*: there is a need for operational and expert agencies, including development agencies, to input to policy and priorities; to assist the government in evaluating whether operational coordination (discussed below) is working effectively; and to provide assistance and cooperate on high-level activities such as risk assessment. Several countries have established standing inter-agency groups or committees for these purposes, which

²⁷ National money laundering and terrorist financing risk assessment (FATF, 2013), available from: www.fatf-gafi.org/publications/methodsandtrends/documents/nationalmoneylaunderingandterroristfinancingriskassessment.html

include the relevant ministries, operational agencies, and other government stakeholders as members, with a central secretariat to support coordination efforts. These types of efforts are particularly important in low income countries which have a high risk.

- *Inter-Regional coordination* can also be important. Some countries have highly decentralised systems, in which some or all of the agencies above are managed and responsible at regional level. Such systems can be very effective, but can face additional coordination challenges when seeking to respond to national or trans-regional activity.
- The OECD's *Oslo Dialogue on Tax and Crime* has focused on facilitating more effective inter-agency cooperation on tax and crime issues, and has produced several pieces of guidance enabling cooperation. These include: *Effective inter-agency cooperation in fighting tax crimes and other financial crimes*²⁸; and *International Cooperation against Tax Crimes and other Financial Crimes: A catalogue of the Main Instruments*²⁹.

Working across disciplines

Dealing with illicit financial flows requires bringing together experts and officials who not only have different expertise and objectives, but also different backgrounds and working cultures; different legal authorities and administrative procedures, and different professional languages. For example, law enforcement officers, financial supervisors, tax inspectors, and civil servants have very different backgrounds and knowledge and likely work in different organisational cultures. A coherent and inter-agency approach to IFFs requires the people involved to communicate and cooperate effectively despite such differences of approach. Poor communication can undermine policy development and implementation, as can the inability of all of those involved to understand other disciplinary perspectives.

There are several ways of dealing with these challenges. Standing bodies like those described above can help, because they foster regular contact between the different agencies and officials involved. A central secretariat, where it exists, is well placed to act as a “translator” in cases where agencies are not used to working with each other directly. Countries can also foster better bilateral links between operational agencies by encouraging joint working on cases, or fostering exchanges of staff (e.g. through short-term secondments in both directions).

To help overcome the lack of inter-agency understanding in this area, the OECD's Oslo Dialogue on Tax and Crime has also produced guidance for tax authorities on other key agencies involved in combating IFFs; including the 2015 report on *Improving Co-operation between Tax and Anti-Money Laundering Authorities*³⁰; and the *Bribery and corruption awareness handbook for tax examiners and tax auditors*³¹. The Oslo Dialogue has also led to the establishment in 2014 of the *OECD International Academy on Tax Crime Investigation*. This is a mechanism which helps train officials from various backgrounds (finance ministries, judiciary, tax authorities etc) in financial investigation techniques, and provides a community to share expertise, as well as developing a longer-term network of officials from different countries to more effectively combat tax crimes and other financial crimes (e.g. corruption, money laundering, smuggling). Other organisations involved in development policy

²⁸ *Effective Inter-Agency Co-Operation in Fighting Tax Crimes and Other Financial Crimes* (OECD, 2013), available from: www.oecd.org/ctp/crime/effectiveinter-agencyco-operationinfightingtaxcrimesandotherfinancialcrimes.htm

²⁹ *International Cooperation against Tax Crimes and other Financial Crimes: A catalogue of the Main Instruments* (OECD, 2012), available from: www.oecd.org/ctp/crime/internationalco-operationagainsttaxcrimesandotherfinancialcrimesacatalogueofthemaininstruments.htm

³⁰ *Improving Co-operation between Tax and Anti-Money Laundering Authorities: Access by tax administrations to information held by financial intelligence units for criminal and civil purposes* (OECD, 2015), available from: www.oecd.org/tax/crime/improving-cooperation-between-tax-and-anti-money-laundering-authorities.htm

³¹ *Bribery and corruption awareness handbook for tax examiners and tax auditors* (OECD, 2013), available from: www.oecd.org/tax/bribery-corruption-awareness-handbook.htm

have mandates to work across disciplines. The United Nations, for example, is promoting ‘delivering as one’, and working across disciplines in country teams. Some low income countries can request that policy recommendations come from multi-stakeholder groups or task forces.

Dialogue beyond government:

Private sector entities are front-line partners of governments in combating illicit financial flows. Many of the measures used against IFFs are implemented by financial institutions and other regulated sectors; they bear much of the cost of the counter-IFF regime, and they are often the first to identify changing risks and trends. A strong and continuous dialogue with the affected sectors can make a very important contribution to the coherence and focus of the overall policy framework. At operational level, the private sector’s perspective can enrich and expand government’s understanding of the risks and of the international environment. And at a policy level, dialogue can make sure that governments consider the costs and impact of new measures, and are open to alternative ways to achieve the same objectives.

Many countries have standing mechanisms for outreach, consultation, and feedback with the private sector. These typically include practitioners or compliance heads from major financial institutions, as well as representative bodies for all regulated sectors, and act as a channel for regular communication about the implementation of preventive measures, and the evolution of risks.

International Engagement

Measures to combat illicit financial flows can be complex and technical. They must also be responsive to an international and ever-changing threat. It is not effective or coherent for each country to pursue these measures in isolation. Countries are more effective when they share information about the changing risk environment; when they pool their resources to identify and disseminate best practices in the implementation of policy measures; and when they exert concerted pressure on jurisdictions which do not play by the rules. Active participation in the international groups and bodies concerned with illicit financial flows can support effectiveness and coherence at home, and open-up cooperative options for managing conflicts and spillovers internationally.

Policy coherence in low-income countries

Policy coordination is particularly challenging In low income countries, post-conflict countries, or fragile states, which may have to deal with a number of additional obstacles:

- *Lack of capacity and resources* - The resource constraints which affect all countries are magnified in states with limited funds and limited capacity in central government. This makes planning and prioritisation more important, as countries cannot realistically implement all the measures they would ideally require.
- *Coordination with international organisations and donors* - there may be a number of international organisations and bilateral partners providing recommendations and assistance, as well as national authorities. National plans and priorities can be distorted by the objectives and conditions set by external partners, which can weaken national ownership and lead to incoherent policies.
- *Missing institutions* - the agencies and institutions which combat illicit financial flows may not exist at all; and existing agencies may be unable to take on IFF responsibilities in addition to their core business. Establishing agencies from scratch is far more demanding - of resources and the attention of Government - than expanding the responsibilities of an existing agency. This can raise difficult questions of prioritisation and timing.

- *Incomplete legal frameworks* - Combating IFFs requires a large amount of detailed legislation on a range of topics. Model laws are available from the UN and several other organisations, but these nevertheless have to be adopted by national legislatures, and embedded in the existing framework of national laws and regulations. In many countries, the legal framework itself is confused, including laws from several sources and even different legal traditions; with duplicative and redundant laws; and potentially with provisions which could undermine measures to counter IFFs. In some cases legislative reform and consolidation is a precondition for an effective framework to combat IFFs.
- *Security and rule of law* - Lack of security and limited ability to enforce laws can undermine most or all of the measures to combat illicit financial flows noted in this paper. But at the same time, security threats (such as insurgent movements) need finance - from IFFs - to support their activities. Countries facing significant security threats may be unable to implement comprehensive measures to combat IFFs, but could face a worsening security situation if they do not address the specific financial flows which support militant groups.

All these challenges require countries to place a greater emphasis on understanding the risks and taking a coherent approach to dealing with them. Fragile countries face a different set of IFF risks to stable and developed countries, and many of the measures required by the international normative framework are irrelevant or low priority (e.g. a country without a financial system does not need rules on correspondent banking). But these countries do not have the capacity or resources to implement the whole anti-IFF framework initially, and must make hard choices about which measures to prioritise, and how to sequence the measures they do take forward.

A failure to coordinate policies from the beginning of framework development or crisis management can be extremely costly, e.g. as urgent measures implemented in haste may undermine more important long-term steps. In some cases, this may mean most measures to combat IFFs are delayed, while more basic or urgent actions are taken.

[NOTE - this could be expanded to discuss the role/challenges for donors]

Practical coordination

Even when policies are coherent, the complex network of agencies and authorities can make it difficult to implement those policies in a coordinated and effective manner. Practical coordination is therefore an essential supplement to policy coherence.

All the measures to combat illicit finance involve more than one actor – often where different agencies have overlapping responsibilities, or where they are acting as separate links in a chain of measures - for example a case may begin with a financial institution submitting a suspicious transaction report, then include investigation by a variety of agencies (as in the example in the introduction), with each step taken by a different unit or several cooperating units. No actor or agency will be familiar with the breadth of policy governing illicit financial flows – this can result in an ineffective approach or even gaps in the legislative, institutional or policy framework. Effective implementation depends on the agencies working together coherently.

In many countries there are multiple investigating and law enforcement authorities with different and sometimes overlapping mandates. In order to effectively combat illicit financial flows, countries need to have clear rules or systems for ensuring different authorities' activities do not undermine or interfere with each other, and where possible to coordinate and cooperate in their activities.

In cases where different agencies have overlapping mandates (e.g. national and local law enforcement agencies), countries may need a *deconfliction* mechanism to ensure they do not accidentally interfere with or obstruct each other. In some jurisdictions this includes clear rules about which agency takes priority in cases of conflict, or a clearing-house database to track individual cases. There are a range of mechanisms which can do this – including for example a hierarchy of precedence; information sharing through a database of investigations; or active coordination mechanisms.

Going beyond deconfliction, to build effective *operational cooperation* – e.g. through exchanges of relevant information, expertise, and capacity between agencies - can realise synergies and significantly improve the effectiveness of efforts to combat IFFs. This is most often achieved through bilateral links between the agencies concerned – although this depends on an appropriate legal framework, good communications and a collaborative culture.

The need for deconfliction, cooperation, and coordination applies to supervision as well as to enforcement. Some countries have multiple financial supervisors, with different geographic or sectoral responsibilities: a single universal financial institution which is active in multiple regions may be overseen by a large number of supervisors.

Many countries have a national coordination body for specific policy issues related to IFFs, such as money laundering, including all the relevant agencies, which can act to ensure operational coordination arrangements are functioning well, and act as a forum for policy coordination.

7. Self-assessment toolkit:

This section sets out tools countries can use internally to test the coherence of their national policy framework for countering illicit financial flows, and to identify areas for improvement. This is a subject-focused supplement to the more general *integrated checklist of issues to be addressed* for PCSD.

These questions do not seek to measure compliance with the international standards: the normative standards for measures to combat illicit financial flows are well-defined and have detailed and rigorous peer-review mechanisms in place already, such as the peer review processes by the OECD Working Group on Bribery; by the Global Forum on Transparency and Exchange of Information for Tax Purposes; the UNCAC; and the Financial Action Task Force. This toolkit focuses on the policy coherence aspects of IFFs (although this does leave some overlap with international standards). The self-assessment toolkit looks at four themes:

- Risk and Strategy
- Institutional Arrangements;
- Managing Trade-offs and Policy Conflicts; and
- Effective Implementation.

For each theme, there are a series of questions to consider, based on national systems and practices; on the views of a range of practitioners. These do not set out a one-size-fits-all model, but are flexible and neutral between differing ways to achieve the desired functional outcome, reflecting national priorities and administrative systems. The questions are intended as a guide to help officials structure their discussion about their approach to illicit financial flows, and how it could be made more coherent or more effective.

MAIN ELEMENTS	ISSUES ADDRESSED
1. RISK AND STRATEGY	
<p><i>(a) Risk</i></p> <ul style="list-style-type: none"> • Does the government have a good understanding of the types and levels of illicit financial flows in the country? Is there a formal national risk assessment? This includes understanding: <ul style="list-style-type: none"> - the main domestic sources of illicit finance; - the main foreign sources and destinations for illicit finance; - the channels used for inflows and outflows; and - the domestic sectors affected by illicit finance (and their impact on the economy as a whole) • Are there indicators of the scale and impact of illicit financial flows in the country (e.g. estimates of tax gaps or the black economy)? • What is the perceived or assessed level of priority given to IFFs. Is it commensurate to the risk? • Are the main domestic sources of illicit finance and the main foreign sources of illicit finance a specific priority area of government? 	<ul style="list-style-type: none"> - Establish the evidence-base for further analysis; - Quantify the risk and impact of IFFs and their distribution (to support a targeted and proportionate response to controls and tradeoffs in key sectors); - Identify knowledge-gaps
<p><i>(b) Enabling Environment</i></p> <ul style="list-style-type: none"> • How do non-policy drivers contribute to making a friendly or a hostile environment for illicit financial flows? <ul style="list-style-type: none"> - How much domestic proceeds-generating crime is there? - Are there strong government institutions? Do they have an accountability framework and a culture of integrity? 	<ul style="list-style-type: none"> - Identify the most relevant enablers and disablers;

<ul style="list-style-type: none"> - What level of resources and capacity is available for preventive measures, supervision, risk mitigation and justice sector implementation? Is there a comprehensive body of legislation? - How large is the financial sector? Does it act as an international financial centre? Are there close international connections with countries that have high levels of IFFs (including borders, trade, or cultural links)? - Are there secrecy and transparency provisions that can help or hinder IFFs (including in banking, ownership of legal persons, and other transparency requirements)? 	
<p><i>(c) Compliance with International Norms</i></p> <ul style="list-style-type: none"> • Which of the international standards and bodies on IFFs is the country a party to? • What is the country's assessed level of compliance with each of those international standards? What is their assessed level of effectiveness? • Are there action plans to improve the level of compliance and implementation? 	<ul style="list-style-type: none"> - Identify whether the basic building-blocks for countering IFFs are in place; - Identify priority reforms, and outside sources of advice and assistance.
<p><i>(d) Strategy</i></p> <ul style="list-style-type: none"> • Do measures to combat IFFs appear in the government's national strategy? • Are resources commensurate to risk made available through the budget (or off budget through donors and donor requests)? • Are IFFs considered as a single issue, or separately (e.g. as corruption, money laundering, tax evasion etc)? <ul style="list-style-type: none"> - If considered separately, how do the strategies for different types of IFFs take account of each other? - If there is a single IFF strategy, how does it relate to wider contextual strategies (e.g. for taxation, law enforcement)? - Are there plans for risk mitigation, crisis management and asset recovery? 	<ul style="list-style-type: none"> - Level of commitment and priorities in combating IFFs; - Clear government objectives; - Role of the centre of government in countering IFFs.
<p>2. Institutional Arrangements</p>	
<p><i>(a) Government Actors</i></p> <ul style="list-style-type: none"> • Who has overall responsibility for IFFs within government? <ul style="list-style-type: none"> - Is there a responsible minister at Cabinet level? - Is there a clear accountability framework (e.g. to a committee of the legislature)? • Which government actors are involved in deciding strategy on IFFs? • Which government actors are involved in implementing measures to combat IFFs? <ul style="list-style-type: none"> - Do relevant agencies have clear objectives regarding IFFs? - Do investigators, prosecutors, FIUs, supervisors, and other relevant agencies have sufficient operational independence? 	<ul style="list-style-type: none"> - Identify the main actors within government and how responsibilities are assigned
<p><i>(b) Non-Government Actors</i></p> <ul style="list-style-type: none"> • Which sectors and actors outside government are required to implement measures to combat IFFs? • Which other actors are affected by IFFs and measures to combat them? • Are there any consultative bodies where policymakers can discuss IFFs and policies to combat them with non-government actors? 	<ul style="list-style-type: none"> - Identify the main non-government stakeholders - including regulated sectors and others. - Check if key stakeholders have a voice in the policy process
<p><i>(c) Coordination Mechanisms</i></p> <ul style="list-style-type: none"> • How is the centre of government involved in policy on IFFs? • Is there an inter-agency coordination mechanism? Does it include: 	<ul style="list-style-type: none"> - Identify whether there are coordination mechanisms, and whether they perform all the relevant functions.

<ul style="list-style-type: none"> - A central secretariat ? - multi-agency involvement in assessing the risks of IFFs? - inter-agency decision-making on policies to combat IFFs? - Oversight and coordination of the operational agencies responsible for implementation of policies to combat IFFs? • Are there agreements or memoranda in place to allow information sharing between different operational authorities? • Are there other (formal and informal) mechanisms to improve awareness and understanding, or to encourage cooperation, between the different agencies involved in combating IFFs? 	
3. Managing trade-offs and policy conflicts	
<p><i>(a) Policy Inter-linkages</i></p> <ul style="list-style-type: none"> • How well are counter-IFF measures implemented within the criminal justice system? Is there adequate capacity to investigate and prosecute for offences related to IFFs and their predicate crimes? • How are counter-IFF obligations on the financial sector and other regulated businesses supervised? <ul style="list-style-type: none"> - Which supervisors have responsibility for counter-IFF measures? Do they take a consistent approach? - How is supervision of counter-IFF measures linked with other types of supervision? Are the approach taken and sanctions applied consistent? - Is the private sector aware of its obligations? Does the private sector have an opinion on the effect of the IFF regulatory framework on business. • How does the tax authority reflect the risks of tax evasion in the design of tax policies? Does the risk of evasion influence the type of taxes or distribution of the tax burden? • What measures are used to promote integrity and prevent corruption in government and public administration? • What controls and transparency measures are applied to the formation of legal persons and arrangements? <ul style="list-style-type: none"> - Can companies be prosecuted for criminal offences (including for foreign bribery offences)? 	<ul style="list-style-type: none"> - Review the interaction of counter-IFF policies with the most relevant other areas of policy. - Identify any linkages which are not adequately understood or reflected in policies.
<p><i>(b) International Spillovers</i></p> <ul style="list-style-type: none"> • Is there significant smuggling of goods across the country's borders (in either direction)? Is smuggling taken into account when considering prohibitions or duties? • Can the government provide a full range of international cooperation (set out in the UN conventions and other standards)? <ul style="list-style-type: none"> - Can authorities cooperate effectively (in both directions) with the main foreign sources and destinations of IFFs? - Are adequate resources allocated to cooperation with key countries? - Do the authorities take part in the exchange of tax information? - Do other countries exert diplomatic or political pressure to influence actions against IFFs (e.g. investigations)? • Does the development assistance agency support measures to counter IFFs (in developing countries and domestically)? • How much influence do national supervisors have over financial institutions' measures against IFFs? Are they more influenced by foreign (group) supervisors? 	<ul style="list-style-type: none"> - Review the main international factors affecting IFFs - Identify potential for international action to reinforce domestic measures (and vice versa)

<p>(c) <i>Trade-offs and Conflicts</i></p> <ul style="list-style-type: none"> • What proportion of the population uses the formal financial sector? What proportion rely on the informal sector for access to financial services? Does the government have policies to promote financial inclusion? Are these taken into account in IFF policies? • Do remittance providers and NPOs have adequate access to banking services? <ul style="list-style-type: none"> - Is there adequate supervision of NPO and MVTS sectors to be adequate? - Is there a policy dialogue about access, involving banks, NPOs, and remittance providers? - Does the government have policies to promote the availability of remittance channels? • How do data protection laws interact with anti-IFF measures or transparency requirements? Is there consultation between data protection authorities and anti-IFF authorities? • Is there a formal voluntary tax compliance programme? If so, what controls are applied to prevent it being misused? • Do the preventive measures required of financial institutions and other private sector firms reflect their role and risk? <ul style="list-style-type: none"> - Are additional measures applied in those sectors which are most exposed to IFFs? - Are low-risk sectors allowed to apply streamlined measures? - Do the measures applied reflect both domestic and foreign risks? 	<ul style="list-style-type: none"> - Monitor and manage the risks of specific policy conflicts arising.
<p>4. Effective Implementation</p>	
<ul style="list-style-type: none"> • Do policy-makers receive and make use of: <ul style="list-style-type: none"> - Data and statistics on the implementation and effect of measures to combat IFFs? - Indicators of changes or trends in the sources, methods, and risks of IFFs? - Feedback from operational agencies on the implementation of policies to counter IFFs? - Feedback from non-government actors on the impact of preventive measures and controls? • Are there periodic reporting or accountability mechanisms on the impact of measures to combat IFFs (e.g. annual reports to parliament)? • Is there sufficient capacity to assess new evidence or developments and to amend or reform policies in response? 	<ul style="list-style-type: none"> - Review the data collection, monitoring, and reporting arrangements - Identify accountability processes which can maintain responsive and up-to-date policies.