G8 SUMMIT: Cleaning house — G8 initiatives in illicit finance

Jun 17 2013 Denisse V. Rudich

With much of the world mired in recession, tackling illicit finance — including money laundering, tax evasion, bribery and corruption — has become a priority for G8 governments. This year's G8 Summit host, British Prime Minister David Cameron, has included several initiatives on the Lough Erne Summit's agenda to tackle illicit finance and promote open economies, open societies and open governments around the world. Broadly based on the "Track it, Stop It, Get It" model developed by the UN Economic Commission for Africa, these include:

1. "track" illicit finance through increased financial transparency and sharing of tax information;
2. "stop it" by stepping up regulation and supervision of existing anti-money laundering (AML) regimes and improving access to information on beneficial ownership; and
3. "get it" through better international cooperation in the area of asset tracing and recovery.

The G8 is focusing on high-growth countries, with a particular emphasis on Africa.

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This article will look at why illicit finance is on the G8 agenda, the G8's role in this policy space, what the G8 hopes to achieve at Lough Erne and what this means for money laundering and financial crime officers in the banking industry.

Why is illicit finance on the G8's radar?

When assessing the size, effects and flows of illicit finance, it quickly becomes clear why this is high on the G8's agenda. Although difficult to pin down, global estimates indicate that illicit finance amounts to more than $1 trillion annually. Money laundering and illicit finance are recognized as the lifeblood of organised crime networks, which engage in drug, weapon and human trafficking. These networks cause serious economic and social harm by getting drugs on the streets, inciting gang warfare and providing small arms to already unstable geographies.

Additionally, as these funds are difficult to track, illicit finance also accounts for billions of dollars in lost tax revenue for governments, which is dearly needed in the face of austerity. Of note, it is estimated that approximately 60 percent of illicit finance relates to commercial transactions involving tax evasion.

This in turn affects the pool of funds left over to support developing countries. The African Partnership Forum held in April 2013 highlighted that between 2007 and 2009, Africa's share of illicit finance accounted for 6 percent of total flows, estimated at $60 billion annually. When measured against official development assistance (ODA) figures listed at $42 billion, it is clear that this is a hidden source of development funding. Additionally, recent literature suggests that developed countries, such as the G8 economies, act as the main destination of illicit finance flows from sources made up of both developed and developing economies. Given the impact of illicit finance, what is the G8's role in this policy space?

The G8's leadership role

The G8 has traditionally and continues to play a leadership role in the development of the international fight against illicit finance. It does so by shining the spotlight on issues of concern as they emerge — thereby setting the international agenda, garnering consensus amongst its members, and exerting political pressure on non-G8 member states.

Since the G8 established the Financial Action Task Force (FATF", the G8 has successfully re-focused the lens on various illicit finance areas as new trends and threats are identified. For example, the G7/G8 developed the FATF in 1989 to prevent the banking system from being used to launder drug money as members collectively recognised in the Economic Statement that "the drug problem" had reached "devastating proportions". The FATF issued its first set of international standards, the FATF 40 Recommendations (FATF40), against money laundering in 1990 at the request of the G7/G8.

In 1996, the FATF amended its international standards so countries would expand the criminalisation of money laundering beyond the proceeds of drug trafficking to the proceeds of other serious offences. Following 9/11, the G8 broadened the FATF's mandate to develop counter-terrorist financing and proliferation financing measures, and in 2003, politically exposed persons (PEPs) and corruption was recognized as a key area of concern. Just last February, as tax crimes gained more prominence amongst G8 members, the revised FATF40 were issued listing tax crimes as one of the offences which should be considered as a predicate offence for money laundering.

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The G8 has effectively used the FATF's blacklisting tool to exert political pressure on non-G8 countries to move forward in the development of domestic AML regimes. By blacklisting countries with AML deficiencies, which can delay and decrease the availability of international finance to businesses located in those countries, the G8 and the FATF have provided a strong incentive to non-G8 governments to develop local legislation formally implementing the FATF40. For 2013, the FATF has pushed effectiveness to the top of its agenda.

The Lough Erne agenda

As part of the Tax and Transparency agenda, Prime Minister David Cameron has indicated that the G8 will work to ensure that anti-money laundering and counter-terrorist financing regimes are more effective in both G8 and high growth countries. Prime Minister Cameron has stated that he will use the G8 Presidency to "galvanise international action" on tax evasion and it is likely that the G8 will explore how asset recovery and asset tracing initiatives can be used recover tax revenues and other income that belongs to developing countries. The G8 will also commit to improving financial transparency and transparency of beneficial ownership.

The UK has indicated that it will work to ensure that more free-of-charge data is available online and accessible to ordinary citizens. The UK will also look to work with the G8 to fight corruption by setting higher international transparency standards, global reporting requirements, and expanding membership of the Extractive Industries Transparency Initiative (EITI). The G8 will also look to strengthen capacity of extractive industries, which are highly susceptible to corruption, by working in partnership with businesses, civil society and developing countries to support existing initiatives such as the Kimberley Process, the African Mining Vision and the African Mineral Development Centre.

What does this mean for MLROs and financial crime officers?

For MLROs and financial crime officers, this means that they need to keep their eye on the ball and, as part of their upstream risk programmes, monitor how G8 initiatives unfold as they are built into regional and local laws and regulations. With regards to effectiveness of AML/CTF regimes, it is likely that by placing this topic on the G8 agenda, regulators will have a stronger incentive to increase enforcement action, issue higher fines and adopt more intrusive regulatory measures to affect credible deterrence.

In the area of beneficial ownership and financial transparency, depending on how the G8 decides to tackle these topics, this will likely decrease the difficulties faced by banks in identifying and verifying the identities of ultimate beneficial owners. However, as information becomes more accessible to the public, there will be a higher expectation for banks to have a greater level of understanding of their customers' business, how and where they structure their financial affairs, and could be called upon to evidence and provide this information to support global tax information sharing efforts. If tax treaties such as the Foreign Account Tax Compliance Act (FATCA) become the norm, this will place a huge burden on financial institutions to build into their due diligence programmes and data capture systems the ability to capture other types of identifiers, similar to U.S. Indicia, to allow governments to report where foreign businesses, residents and nationals are operating in their borders.

In the area of extractive industries, MLROs and financial crime officers will need to understand how these initiatives will affect their country, industry, and bribery and corruption risk assessments and take this into consideration when they updating policies and procedures or conducting new customer risk assessments. In 2011, a KPMG survey saw an average rise of 40 percent in AML compliance spending annually. The bottom line is that the cost of compliance will continue to rise, especially as governments look to the private sector to support capacity building in high growth countries through their correspondent banking and associated person relationships. It is therefore essential that the private sector engages with the government to develop incentives and innovative ways of sharing the cost and decreasing waste through duplication of effort.

The focus placed on cleaning house at this year's summit presents a great opportunity for G8 leaders to continue enhancing efforts to fight illicit crime and for business to partner with governments to develop new ways of working together to fight financial crime and illicit finance. Is it essential that the G8 work together to set the ball rolling on innovative global initiatives that promote transparency, good governance, accountability which will go a long way to cut off criminals from accessing the international financial system. But as David Cameron indicated, G8 countries have to look inward and clean house before they can fully look outwards and must work in partnership with the private sector to do so.

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